

**MIDDLE FORK CROW RIVER
WATERSHED DISTRICT
ANNUAL FINANCIAL REPORT**

December 31, 2011

WESTBERG EISCHENS, PLLP
Certified Public Accountants
Willmar, Minnesota 56201

TABLE OF CONTENTS

	<u>PAGE</u>
BOARD OF MANAGERS	1
INDEPENDENT AUDITOR'S REPORT	2
REQUIRED SUPPLEMENTARY INFORMATION	
Management's Discussion and Analysis	3-9
BASIC FINANCIAL STATEMENTS	
Government-Wide Financial Statements	
General Fund Balance Sheet and Governmental Activities – Statement of Net Assets.....	10-11
General Fund Statement of Revenues, Expenditures, and Changes in Fund Balance and Governmental Activities – Statement of Activities	12-13
Notes to Financial Statements	14-20
Required Supplementary Information	
General Fund Budgetary Comparison Schedule	21
Notes to the Required Supplementary Information.....	22
SCHEDULE OF FINDINGS AND RECOMMENDATIONS	23-26
REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND MINNESOTA LEGAL COMPLIANCE	27-28

**MIDDLE FORK CROW RIVER
WATERSHED DISTRICT
BOARD OF MANAGERS
December 31, 2011**

	<u>Position of the Manager</u>	<u>Term Expires</u>
Robert Hodapp	President and Chair	4/26/12
Bruce Wing	Vice-President	4/26/13
Ruth Schaefer	Secretary	4/26/13
Gordon Behm	Treasurer	4/26/14
Joseph Flanders	Co-Treasurer	4/26/12

INDEPENDENT AUDITOR'S REPORT

Board of Managers
Middle Fork Crow River
Watershed District

We have audited the accompanying financial statements of the governmental activities of Middle Fork Crow River Watershed District as of December 31, 2011, and for the year then ended, as listed in the table of contents. These financial statements are the responsibility of the District's management. Our responsibility is to express an opinion 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. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the governmental activities of Middle Fork Crow River Watershed District as of December 31, 2011, and the respective changes in financial position for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and budgetary comparison information on pages 3 through 9 and page 20 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 the 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.

Westberg Eisenberg PLLP

WESTBERG EISENBERG, PLLP

February 11, 2012

**MIDDLE FORK CROW RIVER
WATERSHED DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS
December 31, 2011**

INTRODUCTION

A petition was filed with the Minnesota Board of Water and Soil Resources on November 16, 2004 to establish the Middle Fork Crow River Watershed District (District). The District was established on April 27, 2005 under Minnesota Status § 103D.205.

The District is a local unit of government that works to solve and prevent water related problems. The District will conduct water quality surveys of lakes and streams within the district, conduct education and volunteer programs, implement best management practices, and manage other projects related to fulfilling the purpose of the district.

This section of Middle Fork Crow River Watershed District's annual financial report presents Management's Discussion and Analysis of the District's financial performance during the year ended December 31, 2011. Please read it in conjunction with the District's financial statements, which immediately follow this section. The Management's Discussion and Analysis (MD&A) is an element of Required Supplementary Information specified in the Governmental Accounting Standard Board's (GASB) Statement No. 34 – *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments* issued in June 1999.

OVERVIEW OF THE FINANCIAL STATEMENTS

The financial section of the annual report consists of three parts. They are:

- Independent Auditor's Report,
- Required supplementary information which includes the Management's Discussion and Analysis (this section) and general fund budgetary comparison schedule, and
- Basic financial statements.

The basic financial statements include two kinds of statements that present different views of the District:

- The **Districtwide financial statements**, including the statement of net assets and statement of activities, provide **short-term** and **long-term** information about the District's **overall** financial status.
- The **fund financial statements** focus on individual parts of the District, reporting the District's operation in **more detail** than the Districtwide statements. The District maintains a single government fund.

**MIDDLE FORK CROW RIVER
WATERSHED DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS
December 31, 2011**

OVERVIEW OF THE FINANCIAL STATEMENTS (Continued)

Figure A-1, summarizes the major features of the District's financial statements, including portions of the District's activities covered and the types of information they contain. The remainder of this overview section of Management's Discussion and Analysis highlights the structure and contents of each of the statements.

Figure A-1 Major Features of the Districtwide and Fund Financial Statements		
	Districtwide Statements	Governmental Funds
Scope	Entire District	The activities of the District that are not proprietary or fiduciary
Required financial statements	- Statement of net assets - Statement of activities	- Balance sheet - Statement of revenue, expenditures and changes in fund balances
Accounting basis and measurement focus	Accrual accounting and economic resources focus	Modified accrual accounting and current financial focus
Type of asset/liability information	All assets and liabilities, both financial and capital, short-term and long-term	Generally assets expected to be used up and liabilities that come due during the year or soon thereafter; no capital assets or long-term liabilities included
Type of inflow/outflow information	All revenues and expenses during the year, regardless of when cash is received or paid	Revenues for which cash is received during or soon after the end of the year; expenditures when goods or services have been received and the related liability is due and payable

**MIDDLE FORK CROW RIVER
WATERSHED DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS
December 31, 2011**

OVERVIEW OF THE FINANCIAL STATEMENTS (Continued)

Districtwide Statements

The Districtwide statements (statement of net assets and statement of activities) report information about the District as a whole using accounting methods similar to those used by private sector companies. The statement of net assets includes all of the District's assets and liabilities. All of the current year's revenues and expenses are accounted for in the statement of activities regardless of when cash is received or paid.

The two Districtwide statements report the District's net assets and how they have changed. Net assets – the difference between the District's assets and liabilities – are one way to measure the District's financial health or position.

- Over time, increases or decreases in the District's net assets are indicators of whether its financial position is improving or deteriorating, respectively.
- To assess the overall health of the District requires consideration of additional non-financial factors such as community support for District Programs and activities.

In the Districtwide financial statement the District's activities are shown in one category titled "governmental activities".

- **Governmental activities** – The District's basic services are reported here, including District Programs and administration. Tax levies, state aid, and grants finance most of these activities.

Fund Financial Statements

The fund financial statements provide more detailed information about the District's single major **fund**.

The District maintains the following fund:

- **Governmental funds statements** – The District's basic services are included in governmental funds that generally focus on:
 - 1) how cash and other financial assets that can readily be converted to cash flow in and out, and
 - 2) the balances left at year-end that are available for spending. Consequently, the governmental funds statements provide a detailed short-term view that helps to determine whether there are more or less financial resources that can be spent in the near future to finance the District's programs.

**MIDDLE FORK CROW RIVER
WATERSHED DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS
December 31, 2011**

FINANCIAL HIGHLIGHTS

Key financial highlights from the Statement of Net Assets and the Statement of Activities for the 2011 fiscal year include the following:

- Net assets totaled \$400,939 in the seventh year of operations.
- Revenues totaled \$619,273 and were \$2,712 less than expenses of \$621,985.
- The District's \$621,985 of expenses were for administrating the District and the revenues were primarily from taxes from the various counties, which are part of the Watershed's District, grants and state aid.

The following Table I reflects the District's condensed summary of the statement of net assets as of December 31, 2011:

**Table I
Summary of Statement of Net Assets
As of December 31,**

<u>Description</u>	2011	2010	Change
Current assets	\$ 539,705	\$ 627,973	\$ (88,268)
Capital assets, net of accumulated depreciation	23,368	27,004	(3,636)
Other assets	<u>61,064</u>	<u>55,040</u>	<u>6,024</u>
Total assets	<u>\$ 624,137</u>	<u>\$ 710,017</u>	<u>\$ (85,880)</u>
Current liabilities	\$ 73,660	\$ 228,993	\$ (155,333)
Long term liabilities	<u>149,538</u>	<u>77,373</u>	<u>72,165</u>
Total liabilities	<u>223,198</u>	<u>306,366</u>	<u>(83,168)</u>
Net assets:			
Invested in capital assets	23,368	27,004	(3,636)
Unrestricted	<u>377,571</u>	<u>376,647</u>	<u>924</u>
Total net assets	<u>400,939</u>	<u>403,651</u>	<u>(2,712)</u>
Total liabilities and net assets	<u>\$ 624,137</u>	<u>\$ 710,017</u>	<u>\$ (85,880)</u>

Total assets decreased by \$85,880 (12%) in 2011 due to additional spending on BMP projects over prior years. Total liabilities decreased by \$83,168 (27%) mainly due to recognition of deferred revenue from 2010 that was spent in 2011 on BMP projects.

**MIDDLE FORK CROW RIVER
WATERSHED DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS
December 31, 2011**

Statement of Operations

The results of the District's operations are reported in the statement of activities. Table II presents a condensed summary of data from the District's statements of operations.

**Table II
Summary of Change in Net Assets
For the Year Ended December 31,**

Description	2011	2010	Change
REVENUES			
Grants	\$ 347,526	\$ 165,491	\$ 182,035
Tax levy	247,810	246,293	1,517
State aid	15,098	15,455	(357)
Interest income	7,438	7,634	(196)
Local contributions and miscellaneous	1,401	4,260	(2,859)
Total revenues	<u>619,273</u>	<u>439,133</u>	<u>180,140</u>
EXPENDITURES			
Meetings/seminars	13,473	15,664	(2,191)
Contract labor	75,631	100,870	(25,239)
Administrative	13,210	7,626	5,584
Grant expenses	273,372	36,036	237,336
Professional expenses	19,921	23,864	(3,943)
Employee benefits	25,670	16,790	8,880
Dues	3,805	3,648	157
Insurance	4,084	4,181	(97)
Payroll expenses	132,556	129,289	3,267
Payroll tax expense	10,868	10,324	544
Utilities	1,687	1,736	(49)
Monitoring	24,803	13,741	11,062
Leased equipment	-	750	(750)
Office expense	957	4,743	(3,786)
Public education	4,931	6,733	(1,802)
Miscellaneous	1,900	1,745	155
Depreciation	7,317	6,826	491
Rent	7,800	7,800	-
Total expenses	<u>621,985</u>	<u>392,366</u>	<u>229,619</u>
Increase in net assets	(2,712)	46,767	(49,479)
Net Assets - January 1	<u>403,651</u>	<u>356,884</u>	<u>46,767</u>
Net Assets - December 31	<u>\$ 400,939</u>	<u>\$ 403,651</u>	<u>\$ (2,712)</u>

**MIDDLE FORK CROW RIVER
WATERSHED DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS
December 31, 2011**

Capital Assets and Debt Administration

As of December 31, 2011, the District had \$23,368 invested in net capital assets. (See Table III.) This amount represents a net decrease (including additions and deductions) of \$3,636, from last year.

**Table III
Capital Assets at Year-End**

	2011	2010
Machinery and equipment	\$ 49,095	\$ 45,414
Less: accumulated depreciation	(25,727)	(18,410)
Net Capital Assets	\$ 23,368	\$ 27,004

The District's long-term debt as of December 31, 2011, consists of debt used to finance various watershed projects. A breakdown of the debt obligations is shown in Table IV.

**Table IV
Change in Debt Obligations**

Description	Beginning Balance	Additions	Reductions	Ending Balance	Due within one year
MN Clean Water Partnership Project	\$ 82,096	\$ 85,391	\$ 5,923	\$ 161,564	\$ 12,026

General Fund

The General Fund includes the primary operations of the District in providing services to citizens and some capital outlay projects.

The following schedule presents a summary of General Fund revenues:

**Table V
General Fund Revenues**

Function	Year Ended December 31		Change	
	2011	2010	Increase (Decrease)	Percent (%)
Tax levy	\$ 247,810	\$ 246,293	\$ 1,517	0.61%
Special assessments	9,686	8,543	1,143	11.80%
Grants	429,076	173,491	255,585	59.57%
State aid	15,098	15,455	(357)	-2.36%
Interest income	7,438	7,634	(196)	-2.64%
Local contributions and miscellaneous	1,401	4,260	(2,859)	-204.07%
Total General Fund Revenues	\$ 710,509	\$ 455,676	\$ 254,833	35.87%

**MIDDLE FORK CROW RIVER
WATERSHED DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS
December 31, 2011**

General Fund (continued)

Total General Fund revenue increased by \$254,833, or 35.87%, from the previous year. The mix of property tax, state-aid and grants can change significantly from year to year. The driving factor relating to increased revenues was specific to the deferred revenue recognized in the prior year and the additional grant revenues received for 2011 BMP projects.

The following schedule presents a summary of General Fund expenditures:

**Table VI
General Fund Expenditures**

Function	Year Ended December 31		Change	
	2011	2010	Increase (Decrease)	Percent (%)
Conservation of natural resources	\$ 688,203	\$ 393,540	\$ 294,663	42.82%
Total General Fund Expenditures	<u>\$ 688,203</u>	<u>\$ 393,540</u>	<u>\$ 294,663</u>	42.82%

Total General Fund expenditures increased by \$294,663, or 42.82%, from the previous year. The expenditures increased in conjunction with revenue on the projects opened and/or completed during 2011.

Special Revenue Fund

The District's Special Revenue Fund was established to manage the Nest Lake Aquatic Plant Management Project which receives payments from special assessments from Nest Lake land owners.

General Fund Budgetary Highlights

- Actual revenues were \$237,995 more than expected.
- Actual expenditures were \$214,336 over the budgeted amount.
- No revisions were made to the original adopted budget.

Factors Bearing On The Future And Next Year's Budgets And Rates

The District relies on property tax levies, authorized by underlying state statutes, for a significant portion of its revenue. Continuing surges in land development projects will likely cause the District's activities and expenditures to increase during the next two to five years.

Contacting District Management

This financial report is designed to provide the citizens of Kandiyohi, Meeker, Pope, and Stearns County taxpayers, customers, and creditors with a general overview of the District's finances and to demonstrate the District's accountability for the money it receives. Questions concerning this report or requests for additional financial information should be directed to the Executive Director, Middle Fork Crow River Watershed District, PO Box 8, Spicer, MN 56288.

**MIDDLE FORK CROW RIVER WATERSHED DISTRICT
GENERAL FUND AND SPECIAL REVENUE FUND BALANCE SHEETS AND
GOVERNMENTAL ACTIVITIES - STATEMENT OF NET ASSETS
WITH ADJUSTMENTS TO CONVERT MODIFIED TO FULL ACCRUAL
December 31, 2011**

	General Fund	Special Revenue Fund	Adjustments	Governmental Activities
ASSETS				
Cash and cash equivalents	\$ 294,379	\$ -	\$ -	\$ 294,379
Grants receivable	152,016	-	-	152,016
Property tax receivable	3,395	-	-	3,395
Assessments receivable	-	13,778	137,201	150,979
Capital assets				
Depreciable - net	-	-	23,368	23,368
Total Assets	<u>\$ 449,790</u>	<u>\$ 13,778</u>	<u>\$ 160,569</u>	<u>\$ 624,137</u>
LIABILITIES AND NET ASSETS				
Accounts payable	\$ 26,843	\$ -	-	\$ 26,843
Accrued vacation	3,889	-	-	3,889
Payroll liabilities	7,730	-	-	7,730
Deferred revenue	9,394	13,778	-	23,172
Note payable	-	-	161,564	161,564
Total Liabilities	47,856	13,778	161,564	223,198
FUND BALANCE/NET ASSETS				
Fund balance				
Unassigned	401,934	-	(401,934)	
Total Liabilities and Fund Balance	<u>\$ 449,790</u>	<u>\$ 13,778</u>		
Net Assets				
Invested in capital assets			23,368	23,368
Unrestricted			377,571	377,571
Total Net Assets			400,939	400,939
Total Liabilities and Net Assets			<u>\$ 160,569</u>	<u>\$ 624,137</u>

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

**MIDDLE FORK CROW RIVER WATERSHED DISTRICT
RECONCILIATION OF THE GOVERNMENTAL FUNDS
BALANCE SHEETS TO THE STATEMENT OF NET ASSETS
December 31, 2011**

Reconciliation of Governmental Fund Balance to Net Assets	
Fund Balance - Governmental Fund	\$ 401,934
Amounts reported for governmental activities in the statement of net assets are different because:	
Capital assets are reported in the statement of net assets but not in the fund balance sheet.	
Governmental Capital Assets	49,095
Less: Accumulated Depreciation	(25,727)
Long-term liabilities are reported on the statement of net assets but not in the fund balance sheet.	
Note Payable	(161,564)
Other long-term assets are not available to pay for current period expenditures and, therefore, are deferred in the fund balance sheet.	
Assessments Receivable	<u>137,201</u>
Net Assets - Governmental Activities	<u>\$ 400,939</u>

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

MIDDLE FORK CROW RIVER WATERSHED DISTRICT
GENERAL FUND AND SPECIAL REVENUE FUND STATEMENTS OF
REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCE
AND GOVERNMENTAL ACTIVITIES - STATEMENT OF ACTIVITIES
WITH ADJUSTMENTS TO CONVERT MODIFIED TO FULL ACCRUAL
For the Year Ended December 31, 2011

	<u>General Fund</u>	<u>Special Revenue Fund</u>	<u>Adjustments</u>	<u>Governmental Activities</u>
REVENUES, GAINS, AND OTHER SUPPORT				
Tax levy	\$ 247,810	\$ -	\$ -	\$ 247,810
Special assessments	9,686	-	(9,686)	-
Grants	429,076	-	(81,550)	347,526
State aid	15,098	-	-	15,098
Interest income	7,438	-	-	7,438
Local contributions and miscellaneous	<u>1,401</u>	<u>-</u>	<u>-</u>	<u>1,401</u>
TOTAL REVENUES, GAINS, AND OTHER SUPPORT	<u>710,509</u>	<u>-</u>	<u>(91,236)</u>	<u>619,273</u>
EXPENDITURES				
Meetings/Seminars	13,473	-	-	13,473
Contract labor	75,631	9,498	-	85,129
Administrative	13,210	-	-	13,210
BMP implementation expense	343,225	-	(83,631)	259,594
Professional expenses	19,921	4,125	-	24,046
Employee benefits	25,670	-	-	25,670
Dues	3,805	-	-	3,805
Insurance	4,084	-	-	4,084
Payroll expenses	132,556	-	-	132,556
Payroll tax expense	10,868	-	-	10,868
Utilities	1,687	-	-	1,687
Monitoring	24,803	-	-	24,803
Public education	4,931	-	-	4,931
Rent	7,800	-	-	7,800
Office expense	957	155	-	1,112
Miscellaneous	1,900	-	-	1,900
Capital Outlay	3,682	-	(3,682)	-
Depreciation	<u>-</u>	<u>-</u>	<u>7,317</u>	<u>7,317</u>
TOTAL EXPENDITURES	<u>688,203</u>	<u>13,778</u>	<u>(79,996)</u>	<u>621,985</u>
EXCESS (DEFICIENCY) OF REVENUES OVER (UNDER) EXPENDITURES	22,306	(13,778)	(11,240)	(2,712)
OTHER FINANCING SOURCES (USES)				
Transfer from other funds	-	13,778	-	13,778
Transfer to other funds	<u>(13,778)</u>	<u>-</u>	<u>-</u>	<u>(13,778)</u>
	<u>(13,778)</u>	<u>13,778</u>	<u>-</u>	<u>-</u>
NET CHANGE IN FUND BALANCE/NET ASSETS	8,528	-	(11,240)	(2,712)
FUND BALANCE/NET ASSETS, Beginning of year	<u>393,406</u>	<u>-</u>	<u>10,245</u>	<u>403,651</u>
FUND BALANCE/NET ASSETS, End of year	<u>\$ 401,934</u>	<u>\$ -</u>	<u>\$ (995)</u>	<u>\$ 400,939</u>

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

**MIDDLE FORK CROW RIVER WATERSHED DISTRICT
RECONCILIATION OF THE STATEMENT OF GOVERNMENTAL FUND REVENUES,
EXPENDITURES, AND CHANGES IN FUND BALANCE TO THE STATEMENT OF ACTIVITIES
For the Year Ended December 31, 2011**

Change in Fund Balance - General Fund	\$	8,528
<p>Amounts reported for governmental activities in the statement of activities are different because:</p> <p>Governmental funds report capital outlays 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.</p>		
Cost of capital assets purchased		3,682
Depreciation expense		(7,317)
<p>Certain revenues are recognized as soon as it is earned. Under the modified accrual basis of accounting certain revenues cannot be recognized until they are available to liquidate liabilities of the current period.</p>		
Special assessments		(9,686)
Clean Water Partnership grants		<u>2,081</u>
Change in Net Assets - Governmental Activities	\$	<u>(2,712)</u>

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

**MIDDLE FORK CROW RIVER
WATERSHED DISTRICT
NOTES TO FINANCIAL STATEMENTS
December 31, 2011**

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Introduction

The Watershed District was established on April 27, 2005, because the establishment would benefit the public welfare and public interest, and would advance the purpose of Minnesota Statutes Chapter 103D. The Middle Fork Crow River Watershed District includes approximately 271 square miles in Kandiyohi, Meeker, Pope, and Stearns County.

The accounting policies of the District conform to accounting principles generally accepted in the United States of America (GAAP) as applicable to governmental units. The following is a summary of the Authority's more significant accounting policies:

A. Financial Reporting Entity

The District was established in 2005 pursuant to applicable Minnesota laws and statutes. The District consists of five managers with three managers from Kandiyohi County, one manager from Meeker County and one manager from Stearns County. Elections are held annually on the second regular meeting of the fiscal year.

B. Basic Financial Statements

The financial statements combine fund level (General and Special Revenue) financial statements and government-wide financial statements (the government activities column). These statements include the financial activities of the overall District.

The Special Revenue Fund is used to account for the proceeds of the specific revenue sources that are restricted to expenditures for specified purposes or designated to finance particular projects or activities of the District. In 2011, the District agreed to manage the Nest Lake Aquatic Plant Management Project.

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

C. Measurement Focus and Basis of Accounting

The governmental activities columns 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 the related cash flows. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

Governmental fund columns (General Fund) are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as soon as they are both measurable and available. The Board considers all revenues to be available if collected with 60 days after the end of the current period. Charges for services, grants and interest are considered to be 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, if any, are reported as other financing sources. When both restricted and unrestricted resources are available for use, it is the Board's policy to use restricted resources first, and then unrestricted resources as needed.

**MIDDLE FORK CROW RIVER
WATERSHED DISTRICT
NOTES TO FINANCIAL STATEMENTS
December 31, 2011**

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

D. Cash and Cash Equivalents

The District considers all investment instruments purchased with maturity of three months or less to be cash equivalents. At December 31, 2011, there were no cash equivalents.

E. 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 at the date of the financial statements and the reported amounts of revenues and expenditures during the reporting period. Actual results could differ from those estimates.

F. Budgets

The Board has adopted grant budgets for the various grant periods. These budgets may be amended or modified as additional grants are received.

G. Compensated Absences

Under the District's policies, employees are granted paid time off (combined vacation and sick leave) based on their length of services. Unused accumulated vacation time is paid to employees upon termination. Compensated absences are accrued when incurred in the governmental activities column of the financial statements. A liability for this amount is reported in the General Fund.

H. Deferred Revenue

All District funds and the governmental activities 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.

I. Fund Balance

The District adopted the provisions of Governmental Accounting Standards Board Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions* for the year ended December 31, 2011. This standard changed fund balance classifications within the fund level statements.

In the fund financial statements, fund balance is divided into five classifications based primarily on the extent to which the District is bound to observe constraints imposed upon the use of resources reported in governmental funds. These classifications are as follows:

Nonspendable – consists of amounts that cannot be spent because they are either not in spendable form or are legally or contractually required to be maintained intact, such as, inventories and prepaid items.

Restricted – consists of amounts related to externally imposed constraints established by creditors, grantors or contributors; or constraints imposed by state statutory provisions.

Committed – consists of amounts that are constrained for specific purposes that are internally imposed by formal action of the Board of Directors. 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 it employed to previously commit those amounts. These constraints are established by Resolution of the Board of Directors.

Assigned – consists of amounts intended to be used by the District for specific purposes but do not meet the criteria to be classified as restricted or committed. In the General Fund, assigned amounts represent intended uses established by the governing body itself or by an official to which the governing body delegates the authority. Pursuant to District Policy, the Director of Directors is authorized to establish assignments of fund balance.

**MIDDLE FORK CROW RIVER
WATERSHED DISTRICT
NOTES TO FINANCIAL STATEMENTS
December 31, 2011**

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

I. Fund Balance (continued)

Unassigned – is the residual classification for the General Fund.

The District uses restricted amounts to be spent first when both restricted and unrestricted fund balance is available. Additionally, the District would first use committed, then assigned, and lastly unassigned amounts of unrestricted fund balances when expenditures are made.

The Board of Directors has formally adopted a fund balance policy for the General Fund.

NOTE 2 STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY

Disbursements in Excess of Appropriations

The general fund disbursements exceeded the amounts budgeted for the year ended December 31, 2011.

	Disbursements	Appropriations	Excess
General Fund	\$ 688,203	\$ 473,867	\$ 214,336

NOTE 3 DEPOSITS

Deposits

In accordance with Minnesota statutes, the District is authorized to designate a depository for public funds and to invest in certificates of deposit. The Minnesota statutes require that all District deposits be protected by insurance, surety bond, or collateral. The market value of collateral pledged shall be at least ten percent more than the amount on deposit plus accrued interest at the close of the financial institution's banking day, not covered by insurance or bonds.

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

Custodial Credit Risk

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.

Custodial Credit Risk (continued)

Custodial credit risk is the risk that in the event of a financial institution failure, the District's deposits may not be returned to it. It is the District's policy that collateral or bonds will be required for all uninsured amounts on deposit and the additional insurance will be documented to show compliance with state law and a perfected security interest under federal law. At December 31, 2011, the District deposits were entirely covered by federal depository insurance or collateral held by the District or its agent in the District's name.

**MIDDLE FORK CROW RIVER
WATERSHED DISTRICT
NOTES TO FINANCIAL STATEMENTS
December 31, 2011**

NOTE 4 CAPITAL ASSETS

Capital assets are reported in the governmental activities column of the financial statements. Capital assets are defined by the entity as purchases made for items with an individual cost of \$2,500 or more. Such assets are recorded at historical cost or estimated cost if constructed. Donated capital assets are recorded at estimated fair market value at the date of donation.

The cost of normal maintenance and repairs that do not add to the value of the asset or materially extend assets' lives are not capitalized.

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

Capital Asset Category	Useful Life
Computer equipment	5 years
Furniture	7 years
Monitoring equipment	10 years
Educational tools (exhibits)	15 years

Capital asset activity for the year ended December 31, 2011, was as follows:

Governmental Activities	Beginning Balance	Additions	Deletions	Ending Balance
Capital assets depreciated Machinery, furniture, and equipment	\$ 45,413	\$ 3,682	\$ -	\$ 49,095
Less: accumulated depreciation for Machinery, furniture, and equipment	(18,410)	(7,317)	-	(25,727)
Governmental Activities Capital Assets, Net	\$ 27,003	\$ (3,635)	\$ -	\$ 23,368

NOTE 5 NOTE PAYABLE

Note Payable to the State of Minnesota through its Minnesota Pollution Control Agency (MPCA) dated June 19, 2008 for the maximum amount of \$200,000. The MPCA will disburse funds to the District on an incurred cost reimbursement basis, after the MPCA has approved the specific Project Work Plans. The interest rate of 2% will begin to accrue on each disbursement on the day the MPCA delivers the funds to the District. The loan is secured by a general obligation promissory note and the date to begin repaying the note is deferred until the note has been fully disbursed, the Project has been fully completed or the Project Implementation Period has expired, whichever comes first. The note is due in semiannual installments of \$7,228 beginning December 2011 through June 2021, interest at 2%.

The following is a summary of long-term debt transactions for the year ended December 31, 2011

Description	Beginning Balance	Additions	Reductions	Ending Balance	Due within one year
MN Clean Water Partnership Project	\$ 82,096	\$ 48,341	\$ 5,923	\$ 124,514	\$ 12,026

**MIDDLE FORK CROW RIVER
WATERSHED DISTRICT
NOTES TO FINANCIAL STATEMENTS
December 31, 2011**

NOTE 5 NOTE PAYABLE (continued)

Following is the Final Repayment Schedule outlined in the agreement:

Calendar Year	Principal	Interest	Total
2012	\$ 12,026	\$ 2,430	\$ 14,456
2013	12,268	2,189	14,457
2014	12,514	1,942	14,456
2015	12,766	1,691	14,457
2016	13,022	1,434	14,456
2017-2021	61,918	3,137	65,055
Total	<u>\$ 124,514</u>	<u>\$ 12,823</u>	<u>\$ 137,337</u>

Note Payable to the State of Minnesota through its Minnesota Pollution Control Agency (MPCA) dated June 30, 2011 for the maximum amount of \$150,000. The MPCA will disburse funds to the District on an incurred cost reimbursement basis, after the MPCA has approved the specific Project Work Plans. The interest rate of 2% will begin to accrue on each disbursement on the day the MPCA delivers the funds to the District. The loan is secured by a general obligation promissory note and the date to begin repaying the note is deferred until the note has been fully disbursed, the Project has been fully completed or the Project Implementation Period has expired, whichever comes first. At that time the repayment of the note is as stated in the Estimated Repayment Schedule in the agreement.

The following is a summary of long-term debt transactions for the year ended December 31, 2011

Description	Beginning Balance	Additions	Reductions	Ending Balance	Due within one year
MN Clean Water Partnership Project	\$ -	\$ 37,050	\$ -	\$ 37,050	\$ -

Following is the Estimated Repayment Schedule outlined in the agreement:

Calendar Year	Principal	Interest	Total
2014	\$ 14,486	\$ 2,803	\$ 17,289
2015	14,641	2,648	17,289
2016	14,937	2,353	17,290
2017-2021	79,329	7,119	86,448
Thereafter	26,607	561	27,168
Total	<u>\$ 150,000</u>	<u>\$ 15,484</u>	<u>\$ 165,484</u>

NOTE 6 PROPERTY TAXES AND SPECIAL ASSESSMENTS

An ad valorem property tax may be levied against all properties in the District with levy limits prescribed by state statute. Property tax levies must be approved by the District Board and certified by the Kandiyohi, Meeker, Pope and Stearns County Auditors in October of each year for collection in the following year. Taxes are payable to the Counties in two installments by May 15 and October 15.

Special assessment levies may be approved by the District Board for maintenance and construction purposes in accordance with state statutes. These assessments are charged against those properties benefiting from the maintenance and construction. Special assessments must be certified to the County Auditors in a manner similar to property taxes.

**MIDDLE FORK CROW RIVER
WATERSHED DISTRICT
NOTES TO FINANCIAL STATEMENTS
December 31, 2011**

NOTE 6 PROPERTY TAXES AND SPECIAL ASSESSMENTS (continued)

Property taxes and special assessments receivable consist of amounts certified to Kandiyohi, Meeker, Pope and Stearns County but not yet collected. Special assessments receivable are recorded when the full levy amount is submitted to the County, though actual assessment against property owners may occur over several years.

NOTE 7 DEFINED BENEFIT PENSION PLANS – STATEWIDE

A. Plan Description

All employees of the District are covered by defined benefit pension plans administered by the Public Employees Retirement Association of Minnesota (PERA). The PERA administers the Public Employees Retirement Fund (PERF), which is a cost sharing, multiple-employer retirement plan. These plans are established and administered in accordance with Minn. Statutes, Chapters 353 and 356.

PERF 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.

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 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 remaining year. The annuity accrual rate for a Coordinated Plan member is 1.2 percent of average salary for each of the first ten 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 Public Employees Retirement Fund 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 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 normal annuity is a lifetime annuity that ceases upon 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 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 PERF. That report may be obtained by writing to PERA, 60 Empire Drive, Suite 200, St. Paul, Minnesota, 55103-2088 or by calling (651) 296-7460 or 1-800-652-9026.

**MIDDLE FORK CROW RIVER
WATERSHED DISTRICT
NOTES TO FINANCIAL STATEMENTS
December 31, 2011**

NOTE 7 DEFINED BENEFIT PENSION PLANS – STATEWIDE (continued)

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 are required to contribute 9.10% and 6.25%, respectively, of their annual covered salary in 2011. The District is required to contribute the following percentages of annual covered payroll: 11.78% for Basic Plan members and 7.25% for Coordinated Plan members. The District's contributions to the Public Employees Retirement Fund for the year ending December 31, 2011, 2010, and 2009 were \$9,730, \$8,540, and \$7,784, respectively. The District's contributions were equal to the contractually required contributions for each year as set by state statute. The District's contributions were equal to the contractually required contributions for each year as set by state statute.

NOTE 8 LEASE AGREEMENTS

The District's currently renting on a month to month basis starting July 1, 2009. The Authority is required to make monthly lease payments in the amount of \$650. Total lease expense for the year ended December 31, 2011 was \$7,800.

NOTE 9 OTHER POST EMPLOYMENT BENEFITS

The District does not accrue a liability for other post employment benefits because they do not have an employer sponsored health plan.

**MIDDLE FORK CROW RIVER WATERSHED DISTRICT
STATEMENT OF REVENUES, EXPENDITURES,
AND CHANGES IN FUND BALANCE-BUDGETARY AND ACTUAL
FOR THE YEAR ENDED DECEMBER 31, 2011**

	<u>Budgeted Amounts</u>		<u>Actual Amounts</u>	<u>Over (Under) Final Budget</u>
	<u>Original</u>	<u>Final</u>		
REVENUES				
Tax levy	\$ 252,500	\$ 252,500	\$ 247,810	\$ (4,690)
Special assessments	-	-	9,686	9,686
State aid	-	-	15,098	15,098
Grants	214,839	214,839	429,076	214,237
Interest income	4,500	4,500	7,438	2,938
Local contributions and miscellaneous	<u>675</u>	<u>675</u>	<u>1,401</u>	<u>726</u>
 Total Revenues	 <u>472,514</u>	 <u>472,514</u>	 <u>710,509</u>	 <u>237,995</u>
EXPENDITURES				
Meetings/seminars	19,700	19,700	13,473	6,227
Contract labor	42,000	42,000	75,631	(33,631)
Administrative	17,000	17,000	13,210	3,790
BMP implementation expense	160,000	160,000	343,225	(183,225)
Professional expenses	23,000	23,000	19,921	3,079
Employee benefits	25,000	25,000	25,670	(670)
Dues	4,500	4,500	3,805	695
Insurance	5,000	5,000	4,084	916
Payroll expenses	131,167	131,167	132,556	(1,389)
Payroll tax expense	11,000	11,000	10,868	132
Utilities	-	-	1,687	(1,687)
Monitoring	-	-	24,803	(24,803)
Data collection & district projects	15,000	15,000	-	15,000
Office expense	11,500	11,500	2,857	8,643
Public education	9,000	9,000	4,931	4,069
Rent	-	-	7,800	(7,800)
Capital outlay	<u>-</u>	<u>-</u>	<u>3,682</u>	<u>(3,682)</u>
 Total Expenditures	 <u>473,867</u>	 <u>473,867</u>	 <u>688,203</u>	 <u>(214,336)</u>
 Net Change in Fund Balance	 (1,353)	 (1,353)	 22,306	 <u>\$ 23,659</u>
 Fund Balance/Net Assets, Beginning	 <u>179,390</u>	 <u>179,390</u>	 <u>393,406</u>	
 Transfers	 -	 -	 (13,778)	
 Fund Balance/Net Assets, Ending	 <u>\$ 178,037</u>	 <u>\$ 178,037</u>	 <u>\$ 401,934</u>	

The notes to the required supplementary information are an integral part of this statement.

**MIDDLE FORK CROW RIVER
WATERSHED DISTRICT
NOTES TO THE REQUIRED SUPPLEMENTARY INFORMATION
December 31, 2011**

NOTE 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 unless specifically carried over to the next budget year by Board action.

On or before mid-June of each year, the District Manager prepares a draft budget for the upcoming fiscal year. Before August 31, the proposed budget is presented to the District Board for review. The Board holds public hearings and a final budget must be prepared and adopted no later than September 30.

The appropriated budget is prepared by fund and function. The legal level of budgetary control (the level at which expenditures may not legally exceed appropriations) is the function level.

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

NOTE 2 EXCESS OF EXPENDITURES OVER APPROPRIATIONS

The general fund disbursements exceeded the amounts budgeted for the year ended December 31, 2011.

	<u>Disbursements</u>	<u>Appropriations</u>	<u>Excess</u>
General Fund	\$ 688,203	\$ 473,867	\$ 214,336

MIDDLE FORK CROW RIVER WATERSHED DISTRICT
Schedule of Findings and Recommendations
Year Ended December 31, 2011

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

PREVIOUSLY REPORTED ITEMS NOT RESOLVED

Finding 2007-1

Criteria:

Generally, a system of internal control contemplates separation of duties such that no individual has responsibility to execute a transaction, have physical access to the related assets, and have responsibility or authority to record the transaction.

Condition:

Due to the limited size of the Districts business staff, the District has limited segregation of duties.

Questioned Costs:

None

Context:

The District has informed us that the small size of its business office staff precludes proper separation of duties at this time.

Effect:

The District is unable to maintain separation of incompatible duties.

Cause:

Limited number of staff in the business office

Recommendation:

We recommend that the District continue to separate incompatible duties as best it can within the limits of what the District considers to be cost beneficial.

CORRECTIVE ACTION PLAN (CAP)

Finding 2007-1

Explanation of Disagreement with Audit Finding:

There is no disagreement with the audit finding.

Actions Planned in Response to Finding:

The District reviews and makes improvements to its internal controls on an ongoing basis, and attempts to maximize the segregation of duties in all areas within the limits of the staff available.

Officer Responsible for Ensuring CAP:

Not Applicable

Planned Completion Date:

Not Applicable

Plan to Monitor Completion of CAP:

Not Applicable

MIDDLE FORK CROW RIVER WATERSHED DISTRICT
Schedule of Findings and Recommendations (Continued)
Year Ended December 31, 2011

Finding 2007-2

Criteria:

Generally, a system of internal control includes the ability to understand and prepare the District's financial statements and related disclosures in accordance with accounting principles generally accepted in the United States of America (GAAP).

Condition:

Due to the limited size of the District's business staff and related resources available, the District has relied upon the auditor to prepare the financial statements and related disclosures in accordance with accounting principles generally accepted in the United States of America.

Questioned Costs:

None

Context:

The District has informed us that the small size and qualifications of its business office staff precludes the District from preparing its own financial statements.

Effect:

The District is unable to prepare GAAP based financial statements.

Cause:

Limited number and qualifications of staff in the business office

Recommendation:

We recommend that the District continue to review the auditor prepared financial statements with the intention of understanding and acceptance of responsibility for reporting under generally accepted accounting principles.

CORRECTIVE ACTION PLAN (CAP)

Finding 2007-2

Explanation of Disagreement with Audit Finding:

There is no disagreement with the audit finding.

Actions Planned in Response to Finding:

The District reviews draft financial statements with the auditor in an effort to increase management's understanding and to provide input into the required disclosures.

Officer Responsible for Ensuring CAP:

Not Applicable

Planned Completion Date:

Not Applicable

Plan to Monitor Completion of CAP:

Not Applicable

MIDDLE FORK CROW RIVER WATERSHED DISTRICT
Schedule of Findings and Recommendations (Continued)
Year Ended December 31, 2011

Finding 2008-1

Criteria:

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

Condition:

During our audit, we proposed numerous adjustments that resulted in significant changes to the District's financial statements.

Questioned Costs:

None

Context:

The District's limited size, training and qualifications of business office personnel have precluded the District from the ability to properly identify and correct financial misstatements.

Effect:

The District's inability to detect material misstatements in the financial statements increases the likelihood that the financial statements may not be fairly presented.

Cause:

Inadequate internal controls and monitoring of internal controls by qualified District personnel.

Recommendation:

We recommend that the District review internal controls currently in place, then design and implement procedures to improve internal controls over financial reporting to detect misstatements in the financial statements.

CORRECTIVE ACTION PLAN (CAP)

Finding 2008-1

Explanation of Disagreement with Audit Finding:

There is no disagreement with the audit finding.

Actions Planned in Response to Finding:

The District will continue to review internal controls and work to design modifications that will increase internal control and the ability to detect material misstatements.

Officer Responsible for Ensuring CAP:

Not Applicable

Planned Completion Date:

Not Applicable

Plan to Monitor Completion of CAP:

Not Applicable

MIDDLE FORK CROW RIVER WATERSHED DISTRICT
Schedule of Findings and Recommendations (Continued)
Year Ended December 31, 2011

IV. FINDINGS RELATED TO COMPLIANCE

PREVIOUSLY REPORTED ITEM RESOLVED

Finding 2010-1 – At December 31, 2010, the District did not have adequate pledged collateral in accordance with Minnesota Statute 118A.03, subd. 3.

CORRECTIVE ACTION PLAN

Explanation of Disagreement with Audit Findings:

There is no disagreement with the audit finding.

Actions Planned in Response to Finding:

In the future, adequate collateral will be obtained and monitored.

Official Responsible for Ensuring CAP:

The Executive Director.

Planned Completion Date of CAP:

Immediately.

Plan to Monitor Completion of CAP:

The Executive Director will monitor the CAP.

REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND MINNESOTA LEGAL COMPLIANCE

Board of Directors
Middle Fork Crow River Watershed District

We have audited the basic financial statements of the Middle Fork Crow River Watershed District as of and for the year ended December 31, 2011, and have issued our report thereon dated February 11, 2012. We conducted our audit in accordance with auditing standards generally accepted in the United States of America.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Middle Fork Crow River Watershed District's internal control over financial reporting (internal control) as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the District's internal control. Accordingly, we do not express an opinion on the effectiveness of the District's internal control over financial reporting.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be significant deficiencies or material weaknesses and therefore there can be no assurance that all such deficiencies have been identified. However, as discussed below, we identified certain deficiencies in internal control over financial reporting that we consider to be material weaknesses and other deficiencies that we consider to be significant deficiencies.

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 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. We consider the deficiencies described in the accompanying Schedule of Findings and Recommendations as items 2007-2 and 2008-1 to be material weaknesses.

A significant deficiency is a deficiency, or 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. We consider the deficiency described in the accompanying Schedule of Findings and Recommendations as item 2007-1 to be a significant deficiency in internal control over financial reporting.

Minnesota Legal Compliance

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

The *Minnesota Legal Compliance Audit Guide for Political Subdivisions* contains six categories of compliance to be tested: contract and bidding, deposits and investments, conflicts of interest, public indebtedness, claims and disbursements, and miscellaneous provisions. Our study included all categories, except public indebtedness, because the Middle Fork Crow River Watershed District has no long-term debt.

The results of our tests indicate that, for the items tested, the Middle Fork Crow River Watershed District complied with the material terms and conditions of applicable legal provisions.

This report is intended solely for the information and use of the Board of Directors, management, and others within the Middle Fork Crow River Watershed District and is not intended to be, and should not be, used by anyone other than those specified parties.

Westberg Eischens PLLP

WESTBERG EISCHENS, PLLP

February 11, 2012