

BROWN'S CREEK WATERSHED DISTRICT
STILLWATER, MINNESOTA

ANNUAL FINANCIAL REPORT

FOR THE YEAR ENDED
DECEMBER 31, 2011

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BROWN'S CREEK WATERSHED DISTRICT
 STILLWATER, MINNESOTA
 ANNUAL FINANCIAL REPORT
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INTRODUCTORY SECTION

**BROWN'S CREEK WATERSHED DISTRICT
STILLWATER, MINNESOTA**

**FOR THE YEAR ENDED
DECEMBER 31, 2011**

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BROWN'S CREEK WATERSHED DISTRICT
STILLWATER, MINNESOTA
BOARD OF MANAGERS AND APPOINTED OFFICIALS
FOR THE YEAR ENDED DECEMBER 31, 2011

MANAGERS

<u>Name</u>	<u>Title</u>
Craig Leiser	President
Rick Vanzwol	Vice President
Gail Pundsack	Vice President
Gerald Johnson	Secretary
Connie Taillon	Treasurer

STAFF

Karen Kill	Administrator
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FINANCIAL SECTION

**BROWN'S CREEK WATERSHED DISTRICT
STILLWATER, MINNESOTA**

**FOR THE YEAR ENDED
DECEMBER 31, 2011**

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5201 Eden Avenue
Suite 250
Edina, MN 55436

INDEPENDENT AUDITOR'S REPORT

Honorable Managers of the
Brown's Creek Watershed District
Stillwater, Minnesota

We have audited the accompanying financial statements of the governmental activities and each major fund of the Brown's Creek Watershed District (the District), Stillwater, Minnesota, as of and for the year ended December 31, 2011 which collectively comprise the District's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the District's management. Our responsibility is to express opinions on these financial statements based on our audit. The financial statements of the District as of December 31, 2010 were audited by other auditors whose report dated July 20, 2011, expressed an unqualified opinion on those statements.

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 opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, each major fund, and the aggregate remaining fund information of the District as of December 31, 2011, and the respective changes in financial position and budgetary comparisons for the General and Management Planning funds for the year then ended in conformity with accounting principles generally accepted in the United States of America.

As described in the Note 5 to the basic financial statements, the District adopted the provisions of Governmental Accounting Standards Board (GASB) Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions*, for the year ended December 31, 2011. Adoption of the provision of this statement results in significant changes to the classifications of the components of fund balances.

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Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis starting on page 13 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Government 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.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the District's financial statements as a whole. The introductory section is presented for purposes of additional analysis and is not a required part of the financial statements. The introductory section has not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we express no opinion on it.

June 11, 2012
Minneapolis, Minnesota

Abdo, Eick & Meyers, LLP

ABDO, EICK & MEYERS, LLP
Certified Public Accountants

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Management's Discussion and Analysis

As management of the Brown's Creek Watershed District (the District), Stillwater, Minnesota, we offer readers of the District's financial statements this narrative overview and analysis of the financial activities of the District for the fiscal year ended December 31, 2011. We encourage readers to consider the information presented here in conjunction with the financial statements, which follow this section.

Financial Highlights

- The assets of the District exceeded its liabilities at the close of the most recent fiscal year by \$937,912 (net assets). Of this amount, \$866,074 (unrestricted net assets) may be used to meet the District's ongoing obligations.
- The District's total net assets increased by \$15,670.
- As of the close of the current fiscal year, the District's governmental funds reported combined ending fund balances of \$844,533, an increase of \$18,347 in comparison with the prior year. This increase in fund balance is due to an excess of revenues over expenditures.
- The ending General fund balance is \$285,459, all of which is unassigned.

Overview of the Financial Statements

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

The financial statements also include notes that explain some of the information in the financial statements and provide more detailed data. The statements are followed by a section of combining and individual fund financial statements and schedules that further explains and supports the information in the financial statements. Figure 1 shows how the required parts of this annual report are arranged and relate to one another.

Figure 1
Required Components of the
District's Annual Financial Report

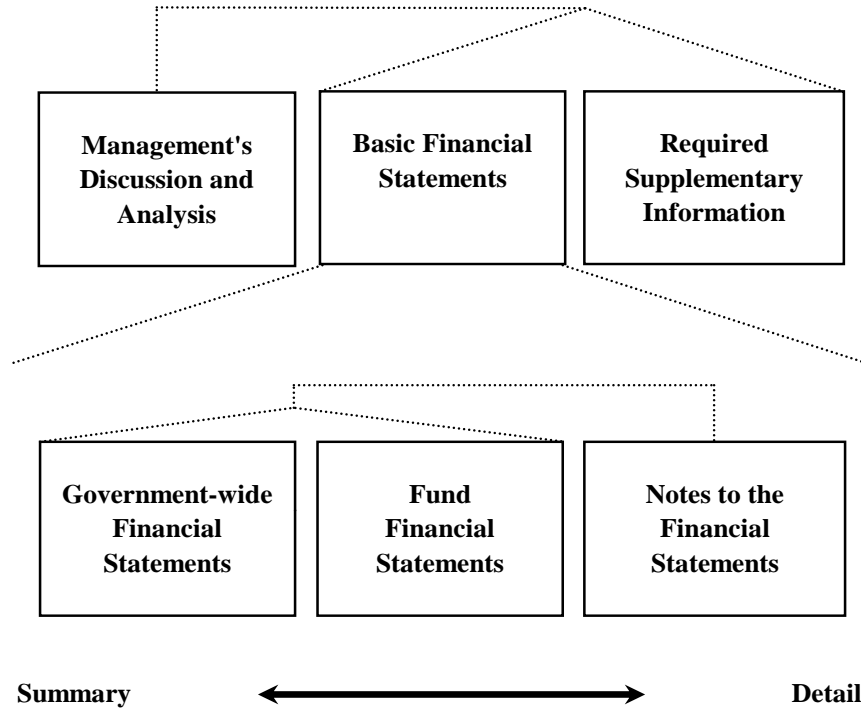


Figure 2 summarizes the major features of the District’s financial statements, including the portion of the District they cover and the types of information they contain. The remainder of this overview section of management’s discussion and analysis explains the structure and contents of each of the statements.

Figure 2
Major features of the Government-wide and Fund Financial Statements

	Fund Financial Statements	
	Government-wide Statements	Governmental Funds
Scope	Entire District	The activities of the District
Required financial statements	<ul style="list-style-type: none"> • Statement of Net Assets • Statement of Activities 	<ul style="list-style-type: none"> • Balance Sheet • Statement of Revenues, Expenditures, and Changes in Fund Balances
Accounting Basis and measurement focus	Accrual accounting and economic resources focus	Modified accrual accounting and current financial resources focus
Type of asset/liability information	All assets and liabilities, both financial and capital, and short-term and long-term	Only assets expected to be used up and liabilities that come due during the year or soon thereafter; no capital assets included
Type of in flow/out flow information	All revenues and expenses during 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 payment is due during the year or soon thereafter

Government-wide financial statements. The government-wide financial statements are designed to provide readers with a broad overview of the District's finances, in a manner similar to a private-sector business.

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

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

The governmental activities of the District include general government and program costs.

The government-wide financial statements start on page 24 of this report.

Fund financial statements. 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. The District, like other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. The District currently maintains two governmental funds.

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

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

The District adopts an annual appropriated budget for its General fund and Management Planning fund. A budgetary comparison statement has been provided for the General fund and Management Planning fund to demonstrate compliance with this budget.

The basic governmental fund financial statements start on page 28 of this report.

Notes to the financial statements. The notes provide 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 start on page 35 of this report.

Government-wide Financial Analysis

As noted earlier, net assets may serve over time as a useful indicator of a government's financial position. In the case of the District, assets exceeded liabilities by \$937,912 at the close of the most recent fiscal year.

The largest portions of the District's net assets are unrestricted and available to meet the ongoing needs of the District. 7.7 percent reflects its investment in capital assets (e.g., land, land improvements, and easements). These assets are not available for future spending.

Brown's Creek Watershed District's Summary of Net Assets

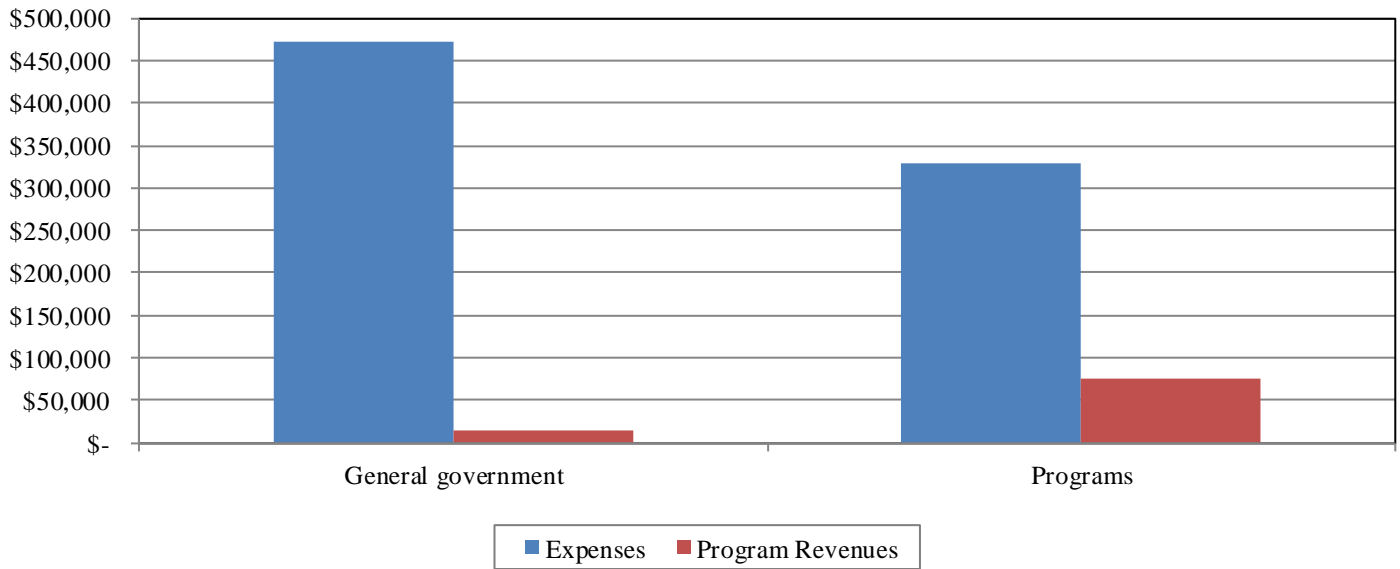
	December 31,		Increase (Decrease)
	2011	2010	
Assets			
Current	\$ 1,149,390	\$ 1,019,986	\$ 129,404
Capital	71,838	62,155	9,683
Total assets	<u>1,221,228</u>	<u>1,082,141</u>	<u>139,087</u>
Liabilities			
Current	<u>283,316</u>	<u>159,899</u>	<u>123,417</u>
Net assets			
Invested in capital assets	71,838	62,155	9,683
Unrestricted	<u>866,074</u>	<u>860,087</u>	<u>5,987</u>
Total net assets	<u>\$ 937,912</u>	<u>\$ 922,242</u>	<u>\$ 15,670</u>

Governmental activities. Governmental activities increased the District’s net assets by \$15,670.

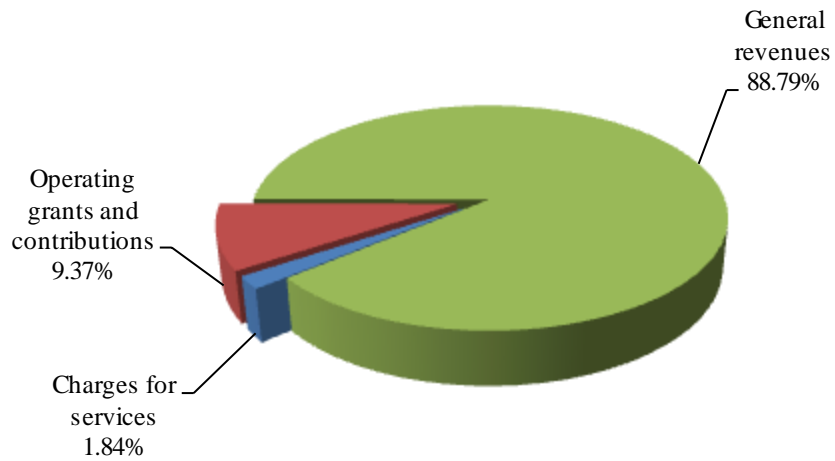
Brown's Creek Watershed District’s Changes in Net Assets

	December 31,		Increase (Decrease)
	2011	2010	
Revenues			
Program			
Charges for services	\$ 15,007	\$ 7,353	\$ 7,654
Operating grants and contributions	76,502	74,617	1,885
General			
Property taxes	719,735	712,330	7,405
Grants and contributions not restricted to specific programs	-	15,555	(15,555)
Unrestricted investment earnings	5,164	3,631	1,533
Total revenues	<u>816,408</u>	<u>813,486</u>	<u>2,922</u>
Expenses			
General government	472,054	424,731	47,323
Projects	328,684	341,206	(12,522)
Total expenses	<u>800,738</u>	<u>765,937</u>	<u>34,801</u>
Change in net assets	15,670	47,549	(31,879)
Net assets, January 1	922,242	820,974	101,268
Prior period adjustment	-	53,719	(53,719)
Net assets, December 31	<u><u>\$ 937,912</u></u>	<u><u>\$ 922,242</u></u>	<u><u>\$ 15,670</u></u>

The following graph depicts various governmental activities and shows the revenue and expenses directly related to those activities.



Revenues by Source - Governmental Activities



Financial Analysis of the Government's Funds

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

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

As of the end of the current fiscal year, the District's governmental funds reported combined ending fund balances of \$844,533, an increase of \$18,347 in comparison with the prior year. Approximately 33.8 percent of this total amount, \$285,459 constitutes *unassigned fund balance*, which is available for spending at the District's discretion. The remainder of fund balance, \$559,074, is committed for the purpose described in the fund balance sheet section.

The General fund is the chief operating fund of the District. At the end of the current year, the fund balance of the General fund was \$285,459. As a measure of the General fund's liquidity, it may be useful to compare total fund balance to total fund expenditures. Total fund balance represents 254.6 percent of 2011 actual expenditures and 197.7 percent of 2012 budgeted fund expenditures. The General fund balance increased by \$14,606 during the current fiscal year.

The fund balance of the Management Planning fund at year end was \$559,074 which is an increase of \$3,741 from the prior year. This was due to revenues exceeding expenditures.

General Fund Budgetary Highlights

The District's General fund budget was amended during the year. The actual results were more favorable than those projected by the 2011 budget. Revenues were over budget by \$3,936, which can be attributed to property taxes and interest on investments. Expenditures were lower than budgeted by \$6,642. The largest variances were provided by salaries and per diems which were under budget by \$2,291 and miscellaneous expenses which were under budget by \$1,223.

Capital Assets

The District's investment in capital assets for its governmental activities as of December 31, 2011 amounts to \$71,838 (net of accumulated depreciation). This investment in capital assets includes land, easements, and land improvements. The District's investment in capital assets for the current fiscal year was 7.7 percent.

Additional information on the District's capital assets can be found in Note 3C on page 42 of this report.

Brown's Creek Watershed District's Capital Assets (net of depreciation)

	December 31,		Increase (Decrease)
	2011	2010	
Land	\$ 62,155	\$ 62,155	\$ -
Land improvements	9,683	-	9,683
Total	<u>\$ 71,838</u>	<u>\$ 62,155</u>	<u>\$ 9,683</u>

Economic Factors and Next Year's Budgets

The Brown's Creek Watershed District goes through a multi-stage process to develop its annual budget.

- Staff reviews the ten-year Watershed Management Plan Implementation Plan and all completed water resource implementation plans for proposed activities.
- Staff contacts all municipalities and agencies to discuss potential cooperative projects and stakeholder priorities.
- Board meets as many times as necessary for a budget workshop, generally at least twice, to assess the previous year's work plan and consider projected projects and programs. For the 2012 budget, the BCWD Board met June 22, 2011 to develop an initial draft 2012 budget. The BCWD Board met jointly with the Citizen Advisory Committee to receive further input on the draft budget on August 22, 2011.
- Board holds a public hearing to receive public comment on the proposed draft levy and budget. For the 2012 budget, the public hearing was held September 12, 2011.
- Board certifies initial levy to the County.
- The budget is presented to the County Commissioners in a public workshop.
- Between September through December, Board reviews projects and programs. The Board determines if the final budget and levy can be reduced at the regular December Board meeting.
- Final levy is certified in December.

For the 2012 budget, the District was notified of the purchase of the Zephyr Rail Road by the MN DNR for conversion to the Brown's Creek State Trail. This presented the District with a unique opportunity to accelerate the implementation of the Brown's Creek TMDL Implementation Plan. Three specific projects for Brown's Creek improvement were identified for 2012, as well as general cooperation with the MN DNR for the trail development to assist with stormwater management for the project. The District will be completing the work on the FY 2011 Clean Water Fund grant to install buffers and stream improvements along Oak Glen Golf Course to reduce Brown's Creek temperatures and improve habitat. The District also was successful in obtaining a FY 2012 Clean Water Fund grant from BWSR to install an iron-enhanced sand filter to improve the water quality of McKusick Lake.

Requests for Information

This financial report is designed to provide a general overview of the District's finances for all those with an interest in the District's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to Karen Kill, Administrator, Brown's Creek Watershed District, 1380 West Frontage Road, Hwy 36, Stillwater, MN 55082.

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GOVERNMENT-WIDE FINANCIAL STATEMENTS

BROWN'S CREEK WATERSHED DISTRICT
STILLWATER, MINNESOTA

FOR THE YEAR ENDED
DECEMBER 31, 2011

BROWN'S CREEK WATERSHED DISTRICT
 STILLWATER, MINNESOTA
 STATEMENT OF NET ASSETS
 DECEMBER 31, 2011

	Governmental Activities
ASSETS	
Cash and temporary investments	\$ 1,102,340
Receivables	
Accounts	4,797
Delinquent taxes	21,541
Due from other governments	20,712
Capital assets	
Land and permanent easements	62,155
Depreciable assets, net of accumulated depreciation	9,683
TOTAL ASSETS	1,221,228
 LIABILITIES	
Accounts payable	29,445
Due to other governments	87,388
Deposits payable	42,150
Unearned revenue	124,333
TOTAL LIABILITIES	283,316
 NET ASSETS	
Invested in capital assets	71,838
Unrestricted	866,074
TOTAL NET ASSETS	\$ 937,912

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

BROWN'S CREEK WATERSHED DISTRICT
 STILLWATER, MINNESOTA
 STATEMENT OF ACTIVITIES
 FOR THE YEAR ENDED DECEMBER 31, 2011

Functions/Programs	Expenses	Program Revenues			Net (Expense) Revenue and Changes in Net Assets
		Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	Governmental Activities
Governmental Activities					
General government	\$ 472,054	\$ 15,007	\$ -	\$ -	\$ (457,047)
Program costs	328,684	-	76,502	-	(252,182)
 Total	\$ 800,738	\$ 15,007	\$ 76,502	\$ -	(709,229)
 General revenues					
Property taxes					719,735
Unrestricted investment earnings					5,164
Total general revenues					724,899
 Change in net assets					15,670
 Net assets, January 1					922,242
 Net assets, December 31					\$ 937,912

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

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FUND FINANCIAL STATEMENTS

**BROWN'S CREEK WATERSHED DISTRICT
STILLWATER, MINNESOTA**

**FOR THE YEAR ENDED
DECEMBER 31, 2011**

BROWN'S CREEK WATERSHED DISTRICT
 STILLWATER, MINNESOTA
 BALANCE SHEET
 GOVERNMENTAL FUNDS
 DECEMBER 31, 2011

	<u>General Fund</u>	<u>Management Planning</u>	<u>Total Governmental Funds</u>
ASSETS			
Cash and temporary investments	\$ 399,892	\$ 702,448	\$ 1,102,340
Receivables			
Accounts	-	4,797	4,797
Delinquent taxes	3,674	17,867	21,541
Due from other governments	<u>2,400</u>	<u>18,312</u>	<u>20,712</u>
 TOTAL ASSETS	 <u><u>\$ 405,966</u></u>	 <u><u>\$ 743,424</u></u>	 <u><u>\$ 1,149,390</u></u>
LIABILITIES AND FUND BALANCES			
LIABILITIES			
Accounts payable	\$ 29,445	\$ -	\$ 29,445
Deposits payable	-	42,150	42,150
Due to other governments	87,388	-	87,388
Deferred revenue	<u>3,674</u>	<u>142,200</u>	<u>145,874</u>
 TOTAL LIABILITIES	 <u>120,507</u>	 <u>184,350</u>	 <u>304,857</u>
FUND BALANCES			
Committed for			
Water resources management plan	-	559,074	559,074
Unassigned	<u>285,459</u>	<u>-</u>	<u>285,459</u>
 TOTAL FUND BALANCES	 <u>285,459</u>	 <u>559,074</u>	 <u>844,533</u>
 TOTAL LIABILITIES AND FUND BALANCES	 <u><u>\$ 405,966</u></u>	 <u><u>\$ 743,424</u></u>	 <u><u>\$ 1,149,390</u></u>

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

BROWN'S CREEK WATERSHED DISTRICT
 STILLWATER, MINNESOTA
 RECONCILIATION OF THE BALANCE SHEET
 TO THE STATEMENT OF NET ASSETS
 GOVERNMENTAL FUNDS
 DECEMBER 31, 2011

Total fund balances - governmental	\$ 844,533
Amounts reported for the governmental activities in the statement of net assets are different because	
Capital assets used in governmental activities are not financial resources and therefore are not reported as assets in governmental funds.	
Cost of capital assets	72,242
Less accumulated depreciation	(404)
Some receivables are not available soon enough to pay for the current period's expenditures, and therefore, are deferred in the funds	
Delinquent taxes	21,541
Total net assets - governmental activities	\$ 937,912

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

BROWN'S CREEK WATERSHED DISTRICT
 STILLWATER, MINNESOTA
 STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES
 GOVERNMENTAL FUNDS
 FOR THE YEAR ENDED DECEMBER 31, 2011

	<u>General Fund</u>	<u>Management Planning</u>	<u>Total Governmental Funds</u>
REVENUES			
Property taxes	\$ 122,036	\$ 593,488	\$ 715,524
Intergovernmental			
Market value homestead credit	2,818	13,753	16,571
Reimbursements/grants	-	76,502	76,502
Interest on investments	1,882	3,282	5,164
Permit and inspection fees	-	15,007	15,007
	<u>126,736</u>	<u>702,032</u>	<u>828,768</u>
TOTAL REVENUES			
EXPENDITURES			
Current			
General government	112,130	359,924	472,054
Program costs	-	338,367	338,367
	<u>112,130</u>	<u>698,291</u>	<u>810,421</u>
TOTAL EXPENDITURES			
NET CHANGE IN FUND BALANCES	14,606	3,741	18,347
FUND BALANCES, JANUARY 1	<u>270,853</u>	<u>555,333</u>	<u>826,186</u>
FUND BALANCES, DECEMBER 31	<u><u>\$ 285,459</u></u>	<u><u>\$ 559,074</u></u>	<u><u>\$ 844,533</u></u>

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

BROWN'S CREEK WATERSHED DISTRICT
 STILLWATER, MINNESOTA
 RECONCILIATION OF THE STATEMENT OF
 REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES
 TO THE STATEMENT OF ACTIVITIES
 GOVERNMENTAL FUNDS
 YEAR ENDED DECEMBER 31, 2011

Total net change in fund balances - governmental funds	\$ 18,347
<p>Amounts reported for governmental activities in the statement of activities are different because</p>	
<p>Capital outlays are reported in governmental funds as expenditures. However in the statement of activities, the cost of those assets is allocated over the estimated useful lives as depreciation expense.</p>	
Capital outlays	10,087
Depreciation expense	(404)
<p>Certain revenues are recognized as soon as they are 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>	
Property taxes	<u>(12,360)</u>
Change in net assets - governmental activities	<u>\$ 15,670</u>

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

BROWN'S CREEK WATERSHED DISTRICT
 STILLWATER, MINNESOTA
 STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES
 BUDGET AND ACTUAL
 GENERAL FUND
 FOR THE YEAR ENDED DECEMBER 31, 2011

	Budgeted Amounts		Actual Amounts	Variance with Final Budget
	Original	Final		
REVENUES				
Property taxes	\$ 119,982	\$ 119,982	\$ 122,036	\$ 2,054
Intergovernmental				
Market value homestead credit	2,818	2,818	2,818	-
Interest on investments	-	-	1,882	1,882
	<u>122,800</u>	<u>122,800</u>	<u>126,736</u>	<u>3,936</u>
TOTAL REVENUES				
EXPENDITURES				
Current				
General government				
Per diems	10,000	9,337	7,046	2,291
Engineering	22,000	22,038	21,455	583
Administrator services	40,600	41,635	40,633	1,002
Legal	15,600	14,115	15,325	(1,210)
Accounting	11,500	12,375	11,735	640
Postage	1,000	1,323	933	390
Printing	750	1,147	1,145	2
Dues and subscriptions	4,000	3,894	3,890	4
Training and seminars	1,000	1,117	1,308	(191)
Insurance and bonds	3,500	3,156	2,275	881
Recording secretary	4,200	4,205	3,518	687
Equipment	-	3,000	2,660	340
Miscellaneous	26,000	1,430	207	1,223
	<u>140,150</u>	<u>118,772</u>	<u>112,130</u>	<u>6,642</u>
TOTAL EXPENDITURES				
NET CHANGE IN FUND BALANCES	(17,350)	4,028	14,606	10,578
FUND BALANCES, JANUARY 1	<u>270,853</u>	<u>270,853</u>	<u>270,853</u>	<u>-</u>
FUND BALANCES, DECEMBER 31	<u>\$ 253,503</u>	<u>\$ 274,881</u>	<u>\$ 285,459</u>	<u>\$ 10,578</u>

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

BROWN'S CREEK WATERSHED DISTRICT
 STILLWATER, MINNESOTA
 STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES
 BUDGET AND ACTUAL
 MANAGEMENT PLANNING FUND
 FOR THE YEAR ENDED DECEMBER 31, 2011

	Budgeted Amounts		Actual Amounts	Variance with Final Budget
	Original	Final		
REVENUES				
Property taxes	\$ 583,447	\$ 583,447	\$ 593,488	\$ 10,041
Intergovernmental				
Market value homestead credit	13,753	13,753	13,753	-
Reimbursements/grants	341,500	214,000	76,502	(137,498)
Interest on investments	-	-	3,282	3,282
Permit fees	-	-	15,007	15,007
Miscellaneous	-	865	-	(865)
	<u>938,700</u>	<u>812,065</u>	<u>702,032</u>	<u>(110,033)</u>
TOTAL REVENUES				
EXPENDITURES				
Current				
General government				
Baseline monitoring and equipment	117,000	112,479	130,884	(18,405)
Legal fees	30,000	39,836	25,441	14,395
Staff engineer	65,600	65,600	64,215	1,385
Permitting	27,500	44,893	39,987	4,906
Administrator services	81,300	81,230	81,267	(37)
East metro water resources educator	16,100	15,900	16,068	(168)
Miscellaneous	14,500	20,034	2,062	17,972
Program costs	926,000	939,775	338,367	601,408
	<u>1,278,000</u>	<u>1,319,747</u>	<u>698,291</u>	<u>621,456</u>
TOTAL EXPENDITURES				
NET CHANGE IN FUND BALANCES	(339,300)	(507,682)	3,741	511,423
FUND BALANCES, JANUARY 1	<u>555,333</u>	<u>555,333</u>	<u>555,333</u>	<u>-</u>
FUND BALANCES, DECEMBER 31	<u>\$ 216,033</u>	<u>\$ 47,651</u>	<u>\$ 559,074</u>	<u>\$ 511,423</u>

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

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BROWN'S CREEK WATERSHED DISTRICT
STILLWATER, MINNESOTA
NOTES TO THE FINANCIAL STATEMENTS
DECEMBER 31, 2011

Note 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. Reporting entity

The District was originally created in 1997 by the Minnesota Board of Water and Soil Resources (the Board) as provided in Minnesota statutes Chapter 103D. The District was established to promote the public welfare and public interest and will advance the purpose of Minnesota statutes, chapters 103B and 103D. The District is operated by a five member Board of Managers.

The District has considered all potential units for which it is financially accountable, and other organizations for which the nature and significance of their relationship with the District are such that exclusion would cause the District's financial statements to be misleading or incomplete. The Governmental Accounting Standards Board (GASB) has set forth criteria to be considered in determining financial accountability. These criteria include appointing a voting majority of an organization's governing body, and (1) the ability of the primary government to impose its will on that organization or (2) the potential for the organization to provide specific benefits to, or impose specific financial burdens on the primary government. The District has no component units that meet the GASB criteria.

B. Government-wide and fund financial statements

The government-wide financial statements (i.e., the statement of net assets and the statement activities) report information on all of the non-fiduciary activities of the District. For the most part, the effect of interfund activity has been removed from these statements.

The statement of activities demonstrates the degree to which the direct expenses of a given function or segment is offset by program revenues. *Direct expenses* are those that are clearly identifiable with a specific function or segment. *Program revenues* include 1) charges to customers or applicants who purchase, use, or directly benefit from goods, services, or privileges provided by a given function or segment and 2) grants and contributions that are restricted to meeting the operational or capital requirements of a particular function or segment. Other items not properly included among program revenues are reported instead as *general revenues*.

Separate financial statements are provided for governmental funds. Major individual governmental funds are reported as separate columns in the fund financial statements.

BROWN'S CREEK WATERSHED DISTRICT
STILLWATER, MINNESOTA
NOTES TO THE FINANCIAL STATEMENTS
DECEMBER 31, 2011

Note 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

C. Measurement focus, basis of accounting and basis of presentation

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

Governmental fund financial statements are reported using the *current financial resources measurement focus* and the *modified accrual basis of accounting*. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be *available* when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the District considers revenues to be available if they are collected within 60 days of the end of the current fiscal period. Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However, expenditures related to compensated absences and claims and judgments, are recorded only when payment is due.

Charges for service, assessments to members, grants and interest associated with the current fiscal period are all considered susceptible to accrual and so have been recognized as revenues of the current fiscal period. All other revenue items are considered to be measurable and available only when cash is received by the organization.

Revenue resulting from exchange transactions, in which each party gives and receives essentially equal value, is recorded on the accrual basis when the exchange takes place. On a modified accrual basis, revenue is recorded in the year in which the resources are measurable and become available.

Non-exchange transactions, in which the District receives value without directly giving equal value in return, include grants, entitlement and donations. Eligibility requirements include timing requirements, which specify the year when the resources are required to be used or the year when use is first permitted, matching requirements, in which the District must provide local resources to be used for a specified purpose, and expenditure requirements, in which the resources are provided to the District on a reimbursement basis. On a modified accrual basis, revenue from non-exchange transactions must also be available before it can be recognized.

Deferred revenue in the fund financial statements and unearned revenue in the government-wide financial statements arises when assets are recognized before revenue recognition criteria have been satisfied. Grants and entitlements received before eligibility requirements are met are also recorded as deferred revenue. On the modified accrual basis, receivables that will not be collected within the available period have also been reported as deferred revenue.

The District reports the following major governmental funds:

The *General fund* is the District's primary operating fund. It accounts for all financial resources not accounted for in a different fund of the District.

The *Management Planning fund* was established pursuant to Minnesota statutes for funding related to the development and implementation of the District's watershed management plan. By law, this plan must contain a capital improvement plan which allows watershed districts to implement projects without petition. The District may impose an ad valorem levy over the entire watershed or subwatershed to fund these projects or allow funds to accumulate to finance these capital improvement projects. The property tax levy is committed to execute the water resources management plan as filed with the Board of Water and Soil Resources.

BROWN'S CREEK WATERSHED DISTRICT
STILLWATER, MINNESOTA
NOTES TO THE FINANCIAL STATEMENTS
DECEMBER 31, 2011

Note 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

Private-sector standards of accounting and financial reporting issued prior to December 1, 1989, generally are followed in the government-wide financial statements to the extent that those standards do not conflict with or contradict guidance of GASB.

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

As a general rule the effect of interfund activity has been eliminated from government-wide financial statements.

Amounts reported as *program revenues* include: (1) charges to customers or member cities for goods, services, or privileges provided; (2) operating grants and contributions; and (3) capital grants and contributions, including special assessments.

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

BROWN'S CREEK WATERSHED DISTRICT
STILLWATER, MINNESOTA
NOTES TO THE FINANCIAL STATEMENTS
DECEMBER 31, 2011

Note 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

D. Assets, liabilities and net assets or fund equity

Deposits and investments

The District's cash and temporary investments are considered to be cash on hand, demand deposits and short term investments with original maturities of three months or less from the date of acquisition.

Cash balances from all funds are pooled and invested, to the extent available, in certificates of deposit and other authorized investments. Earnings from such investments are allocated on the basis of applicable participation by each of the funds.

The District may also invest idle funds as authorized by Minnesota statutes, as follows:

1. Direct obligations or obligations guaranteed by the United States or its agencies.
2. Shares of investment companies registered under the Federal Investment Company Act of 1940 and received the highest credit rating, rated in one of the two highest rating categories by a statistical rating agency, and have a final maturity of thirteen months or less.
3. General obligations of a state or local government with taxing powers rated "A" or better; revenue obligations rated "AA" or better.
4. General obligations of the Minnesota Housing Finance Agency rated "A" or better.
5. Bankers' acceptances of United States banks eligible for purchase by the Federal Reserve System.
6. Commercial paper issued by United States banks corporations or their Canadian subsidiaries, of highest quality category by at least two nationally recognized rating agencies, and maturing in 270 days or less.
7. Repurchase or reverse repurchase 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.
8. Guaranteed investment contracts (GIC's) issued or guaranteed by a United States commercial bank, a domestic branch of a foreign bank, a United States insurance company, or its Canadian subsidiary, whose similar debt obligations were rated in one of the top two rating categories by a nationally recognized rating agency.

BROWN'S CREEK WATERSHED DISTRICT
STILLWATER, MINNESOTA
NOTES TO THE FINANCIAL STATEMENTS
DECEMBER 31, 2011

Note 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

Property tax revenue recognition

The Board of Managers annually adopts a tax levy and certifies it to the County in December (levy/assessment date) of each year for collection in the following year. The County is responsible for billing and collecting all property taxes for itself, the City, the local School District and other taxing authorities. Such taxes become a lien on January 1 and are recorded as receivables by the District at that date. Real property taxes are payable (by property owners) on May 15 and October 5 of each calendar year. Personal property taxes are payable by taxpayers on February 28 and June 30 of each year. These taxes are collected by the County and remitted to the District on or before July 7 and December 2 of the same year. The District has no ability to enforce payments of property taxes by property owners. The County possesses this authority.

Government-wide Financial Statements. The District recognizes property tax revenue in the period for which taxes were levied.

Governmental Fund Financial Statements. The District recognizes property tax revenue when it becomes both measurable and available to finance expenditures of the current period. In practice, current and delinquent taxes and State credits received by the District in July, December, and January are recognized as revenue for the current year. Taxes collected by the County by December 31 (remitted to the District the following January) and taxes and credits not received at year end are classified as delinquent and due from County taxes receivable. The portion of delinquent taxes not collected by the District in January is fully offset by deferred revenue because they are not available to finance current expenditures.

Property taxes on homestead property (as defined by Minnesota statutes) are partially reduced by market value homestead credit. This credit is paid to the District by the State in lieu of taxes levied against the homestead property. The State remits this credit through installments each year. The credit is recognized as revenue by the District at the time of collection.

Accounts receivable

Accounts receivable include amounts billed for services provided before year end.

Capital assets

Capital assets, which include land, land improvements and easements are reported in the applicable governmental activities columns in the government-wide financial statements. Capital assets are defined by the District as assets with an initial, individual cost of more than \$5,000 (amount not rounded) and an estimated useful life in excess of one year. Such assets are recorded at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at estimated fair market value at the date of donation.

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

GASB Statement No. 34 required the District to report and depreciate new infrastructure assets effective with the beginning of the 2004 calendar year. Infrastructure assets include lake improvements, dams and drainage systems. Neither their historical cost nor related depreciation has historically been reported in the financial statements. For governmental entities with total annual revenues of less than \$10 million for the fiscal year ended December 31, 1999 the retroactive reporting of infrastructure is not required under the provisions of GASB Statement No. 34. The District implemented the general provisions of GASB Statement No. 34 in the 2004 calendar year and has elected not to report infrastructure assets acquired in years prior to 2004.

BROWN'S CREEK WATERSHED DISTRICT
STILLWATER, MINNESOTA
NOTES TO THE FINANCIAL STATEMENTS
DECEMBER 31, 2011

Note 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

Fund balance

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 the governmental funds. These classifications are defined as follows:

Nonspendable - Amounts that cannot be spent because they are not in spendable form, such as prepaid items.

Restricted - Amounts related to externally imposed constraints established by creditors, grantors or contributors; or constraints imposed by state statutory provisions.

Committed - Amounts constrained for specific purposes that are internally imposed by formal action (resolution) of the Board, which is the District's highest level of decision-making authority. Committed amounts cannot be used for any other purpose unless the Board modifies or rescinds the commitment by resolution.

Assigned - Amounts constrained for specific purposes that are internally imposed. In governmental funds other than the General fund, assigned fund balance represents all remaining amounts that are not classified as nonspendable and are neither restricted nor committed. In the General fund, assigned amounts represent intended uses established by the Council itself or by an official to which the governing body delegates the authority

Unassigned - The residual classification for the General fund and also negative residual amounts in other funds.

The District considers 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 balance when expenditures are made.

Net assets

Net assets represent the difference between assets and liabilities. Net assets are displayed in three components:

- a. Invested in capital assets - Consists of capital assets, net of accumulated depreciation
- b. Restricted net assets - Consist of net assets restricted when there are limitations imposed on their use through external restrictions imposed by creditors, grantors, laws or regulations of other governments.
- c. Unrestricted net assets - All other net assets that do not meet the definition of "restricted" or "invested in capital assets, net of related debt".

Comparative data/reclassifications

Certain amounts presented in prior year data have been reclassified in order to be consistent with the current year's presentation.

BROWN'S CREEK WATERSHED DISTRICT
STILLWATER, MINNESOTA
NOTES TO THE FINANCIAL STATEMENTS
DECEMBER 31, 2011

Note 2: STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY

Budgetary information

The Board of Managers adopts an annual budget for the General and Management Planning fund of the District on an annual basis. During the budget year, supplemental appropriations and deletions are or may be authorized by the Board. There were amendments to the budget during 2011. The modified accrual basis of accounting is used by the District for budgeting data. All appropriations end with the fiscal year for which they were made.

The District monitors budget performance on the fund basis. All amounts over budget have been approved by the Board through the disbursement process.

The District does not use encumbrance accounting.

Note 3: DETAILED NOTES ON ACCOUNTS

A. Deposits and investments

Deposits

Custodial credit risk for deposits and investments is the risk that in the event of a bank failure, the District's deposits and investments may not be returned or the District will not be able to recover collateral securities in the possession of an outside party.

In accordance with Minnesota statutes and as authorized by the Board, the District maintains deposits at those depository banks, all of which are members of the Federal Reserve System.

Minnesota statutes require that all District deposits be protected by insurance, surety bond or collateral. The market value of collateral pledged must equal 110 percent of the deposits not covered by insurance or bonds.

Authorized collateral in lieu of a corporate surety bond includes:

- United States government Treasury bills, Treasury notes, Treasury bonds;
- Issues of United States government agencies and instrumentalities as quoted by a recognized industry quotation service available to the government entity;
- General obligation securities of any state or local government with taxing powers which is rated "A" or better by a national bond rating service, or revenue obligation securities of any state or local government with taxing powers which is rated "AA" or better by a national bond rating service;
- General obligation securities of a local government with taxing powers may be pledged as collateral against funds deposited by that same local government entity;
- Irrevocable standby letters of credit issued by Federal Home Loan Banks to a municipality accompanied by written evidence that the bank's public debt is rated "AA" or better by Moody's Investors Service, Inc., or Standard & Poor's Corporation; and
- Time deposits that are fully insured by any Federal agency.

BROWN'S CREEK WATERSHED DISTRICT
 STILLWATER, MINNESOTA
 NOTES TO THE FINANCIAL STATEMENTS
 DECEMBER 31, 2011

Note 3: DETAILED NOTES ON ACCOUNTS - CONTINUED

Minnesota statutes require that all collateral shall be placed in safekeeping in a restricted account at a 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. The selection should be approved by the District.

At year end, the District's carrying amount of deposits was \$1,102,340 and the bank balance was \$1,128,375. Of the bank balance, \$835,500 was covered by federal depository insurance. The remaining balance was covered by collateral held in the District's name.

C. Capital assets

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

	Beginning Balance	Increases	Decreases	Ending Balance
Governmental activities				
Capital assets, not being depreciated				
Land	\$ 62,155	\$ -	\$ -	\$ 62,155
Capital assets, being depreciated				
Land improvements	-	10,087	-	10,087
Less accumulated depreciation for				
Land improvements	-	(404)	-	(404)
Total capital assets being depreciated, net	-	9,683	-	9,683
Governmental activities capital assets, net	<u>\$ 62,155</u>	<u>\$ 9,683</u>	<u>\$ -</u>	<u>\$ 71,838</u>

Depreciation expense charged to the project function for 2011 was \$404.

D. Deferred revenue/unearned revenue

Governmental funds report deferred revenue in connection with receivables for revenues that are not considered to be available to liquidate liabilities of the current period. Also, governmental funds defer revenue recognition in connection with resources that have been received, but not yet earned. At the end of the current fiscal year, the various components of deferred revenue/unearned revenue reported were as follows:

	Unavailable	Unearned
General fund		
Delinquent taxes	\$ 3,674	\$ -
Management Planning fund		
Delinquent taxes	17,867	-
Grants	-	124,333
Total	<u>\$ 21,541</u>	<u>\$ 124,333</u>

BROWN'S CREEK WATERSHED DISTRICT
STILLWATER, MINNESOTA
NOTES TO THE FINANCIAL STATEMENTS
DECEMBER 31, 2011

Note 4: OTHER INFORMATION

A. 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; injuries to employees; and natural disasters for which the District carries insurance. The District pays annual premiums for its workers compensation and property and casualty insurance. Settled claims have not exceeded the District's coverage in any of the past three fiscal years.

Liabilities are reported when it is probable that a loss has occurred and the amount of the loss can be reasonably estimated. Liabilities, if any, include an amount for claims that have been incurred but not reported (IBNRs). The District's management is not aware of any incurred but not reported claims.

B. Permit collateral

The District issues permits to applicants who wish to make changes to land that may affect the water drainage or alter the lake shore within the boundaries of the District. The District requires collateral to be deposited to ensure the projects are completed in accordance with the permit application. As of December 31, 2011, the District was holding \$42,150 of collateral deposits.

Note 5: ACCOUNTING CHANGE

GASB Statement 54 "*Fund Balance Reporting and Governmental Fund Type Definitions*" enhances the usefulness of fund balance information by providing clearer fund balance classifications that can be more consistently applied and by clarifying the existing governmental fund type definitions. The District implemented this standard for fiscal year end December 31, 2011. Changes to governmental fund type fund balance reporting is reflected in the financial statements and schedules and related disclosures are included in Note 1.

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OTHER REQUIRED REPORTS

BROWN'S CREEK WATERSHED DISTRICT
STILLWATER, MINNESOTA

FOR THE YEAR ENDED
DECEMBER 31, 2011



5201 Eden Avenue
Suite 250
Edina, MN 55436

REPORT ON MINNESOTA LEGAL COMPLIANCE

Board of Managers
Brown's Creek Watershed District
Stillwater, Minnesota

We have audited the financial statements of the governmental activities and each major fund of the Brown's Creek Watershed District (the District), Stillwater, Minnesota, as of and for the year ended December 31, 2011, and have issued our report thereon dated June 11, 2012.

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

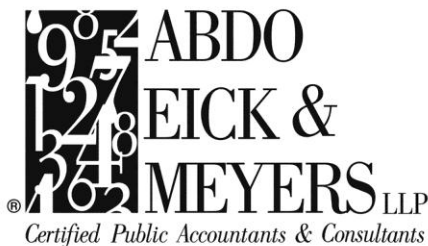
The *Minnesota Legal Compliance Audit Guide for Local Government* covers seven main categories of compliance to be tested: contracting and bidding, deposits and investments, conflicts of interest, public indebtedness, claims and disbursements, tax increment financing, and other miscellaneous provisions. Our study included all of the listed categories except that we did not test for compliance in tax increment financing because the District has not established a tax increment financing district.

The results of our tests indicate that for the items tested, the 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 Managers, management and the Minnesota Office of the State Auditor, and is not intended to be and should not be used by anyone other than these specified parties.

June 11, 2012
Minneapolis, Minnesota


ABDO, EICK & MEYERS, LLP
Certified Public Accountants



5201 Eden Avenue
Suite 250
Edina, MN 55436

REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING
BASED ON AN AUDIT OF FINANCIAL STATEMENTS

Board of Managers
Brown's Creek Watershed District
Stillwater, Minnesota

In planning and performing our audit of the financial statements of the governmental activities and each major fund of the Brown's Creek Watershed District (the District), Stillwater, Minnesota, as of and for the year ended December 31, 2011, in accordance with auditing standards generally accepted in the United States of America, we considered the District's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the District's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the District's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over financial reporting that might be 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 over financial reporting exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A material weakness is a deficiency or combination of deficiencies in internal control, such that there is a reasonable possibility that a material misstatement of the District's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiency presented as finding 2011-2 in the Schedule of Findings and Responses to be a material weakness in internal control over financial reporting.

A significant deficiency is a deficiency, or a combination of deficiencies, in internal control over financial reporting that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider the deficiency presented as finding 2011-1 in the Schedule of Findings and Responses to be a significant deficiency in internal control over financial reporting.

In addition, we noted other matters involving the internal control and its operation that we have reported to management of the District in a separate letter dated June 11, 2012.

The District's responses to the findings identified in our audit are described in the accompanying Schedule of Findings and Responses. We did not audit the District's responses and, accordingly, we express no opinion on them.

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

June 11, 2012
Minneapolis, Minnesota

Abdo, Eick & Meyers, LLP
ABDO, EICK & MEYERS, LLP
Certified Public Accountants

BROWN'S CREEK WATERSHED DISTRICT
STILLWATER, MINNESOTA
SCHEDULE OF FINDINGS AND RESPONSES
FOR THE YEAR ENDED DECEMBER 31, 2011

Finding Description

2011-1 **Preparation of financial statements**

Condition: We were requested to draft the audited financial statements and related footnote disclosures as part of our regular audit services. Ultimately, it is management's responsibility to provide for the preparation of your statements and footnotes, and the responsibility of the auditor to determine the fairness of presentation of those statements. However, based on recent auditing standards, it is our responsibility to inform you that this deficiency could result in a material misstatement to the financial statements that could have been prevented or detected by your management. Essentially, the auditors cannot be part of your internal control process.

Criteria: Internal controls should be in place to provide reasonable assurance over financial reporting.

Cause: From a practical standpoint, we both prepare the statements and determine the fairness of the presentation at the same time in connection with our audit. This is not unusual for us to do with organizations of your size.

Effect: The effectiveness of the internal control system relies on enforcement by management. The effect of deficiencies in internal controls can result in undetected errors in financial reporting.

Recommendation: It is your responsibility to make the ultimate decision to accept this degree of risk associated with this condition because of cost and other considerations. We have instructed management to review a draft of the auditor prepared financials in detail for accuracy; we have answered any questions that management might have, and have encouraged research of any accounting guidance in connection with the adequacy and appropriateness of classification of disclosures in your statements. We are satisfied that the appropriate steps have been taken to provide you with the completed financial statements. While the District is reviewing the financial statements we recommend a disclosure checklist is utilized to ensure all required disclosures are presented and the District should agree its financial software to the numbers reported in the financial statements.

Management response:

For now, the District's management accepts the degree of risk associated with this condition and thoroughly reviews a draft of the financial statements.

BROWN'S CREEK WATERSHED DISTRICT
STILLWATER, MINNESOTA
SCHEDULE OF FINDINGS AND RESPONSES - CONTINUED
FOR THE YEAR ENDED DECEMBER 31, 2011

<u>Finding</u>	<u>Description</u>
2011-2	Material audit adjustment
<i>Condition:</i>	During our audit, an adjustment was needed to record deferred grant revenue.
<i>Criteria:</i>	The financial statements are the responsibility of the District's management; therefore, the District must be able to prevent or detect a material misstatement in the financial statements including footnote disclosures.
<i>Cause:</i>	The year-end trial balance did not reflect all necessary accounting entries.
<i>Effect:</i>	This indicates that it would be likely that a misstatement may occur and not be detected by the District's system of internal control. The audit firm cannot serve as a compensating control over this deficiency.
<i>Recommendation:</i>	We recommend that management review each journal entry, obtain an understanding of why the entry was necessary and modify current procedures to ensure that future corrections are not needed.
<i>Management response:</i>	Management is aware of this issue and will review grant agreements and provide grant expenditure information needed to record any deferred revenue.