

**SAUK RIVER WATERSHED DISTRICT
Stearns County, Minnesota**

***Management Letter
For the Period Ended December 31, 2009***

**SAUK RIVER WATERSHED DISTRICT
Stearns County, Minnesota**

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**REPORT ON MATTERS IDENTIFIED AS A RESULT OF THE
AUDIT OF THE FINANCIAL STATEMENTS**

March 12, 2010

Board of Managers
Sauk River Watershed District
Sauk Centre, Minnesota

In planning and performing our audit of the financial statements of the Sauk River Watershed District, Sauk Centre, Minnesota, as of and for the period ended December 31, 2009, in accordance with U.S. generally accepted auditing standards and *Government Auditing Standards*, we considered the 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.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses and, therefore, there can be no assurance that all deficiencies, significant deficiencies or material weaknesses have been identified. Material weaknesses and significant deficiencies identified, if any, are stated within this letter.

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 District's financial statements will not be prevented or detected and corrected on a timely basis.

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.



The accompanying memorandum includes recommendations for improvement of accounting procedures and internal control measures that came to our attention as a result of our audit of the financial statements of the District for the period ended December 31, 2009. The matters discussed herein were considered by us during our audit and they do not modify the opinion expressed in our Independent Auditor's Report dated March 12, 2010, on such statements.

This communication is intended solely for the information and use of management and the Board of Managers, others within the District and state oversight agencies and is not intended to be and should not be used by anyone other than these specified parties.

Kern, DeWenter, Viere, Ltd.

KERN, DEWENTER, VIERE, LTD.
St. Cloud, Minnesota

SAUK RIVER WATERSHED DISTRICT
Stearns County, Minnesota

MATERIAL WEAKNESSES
December 31, 2009

LACK OF SEGREGATION OF ACCOUNTING DUTIES

During the period ended December 31, 2009, the District had a lack of segregation of accounting duties due to a limited number of office employees. This lack of segregation can be demonstrated in the following areas, which is not intended to be an all inclusive list:

- The Assistant Administrator receipts goods, posts amounts into the finance system, prints and mails the checks and prepares the bank reconciliation. In addition, the Assistant Administrator is an authorized signer on the District's accounts.
- The Assistant Administrator handles the cash receipts, posts amounts into the finance system, prepares the deposits, makes the deposits and prepares the bank reconciliation.
- The Assistant Administrator is responsible for all functions of the payroll process.
- The Assistant Administrator has access to all areas of the accounting system.

Management is aware of this condition and will take certain steps to compensate for the lack of segregation. However, due to the small accounting staff needed to handle all of the accounting duties, the cost of obtaining desirable segregation of accounting duties can often exceed benefits which could be derived. Due to this reason, management has determined a complete segregation of accounting duties is impractical to correct.

We recommend management, along with the Board of Managers, remain aware of this situation and continually monitor the accounting system including changes that occur.

LACK OF ADEQUATE ACCOUNTING SOFTWARE

The District currently uses MYOB[®] as the District's financial accounting system. This system is not intended for governmental accounting and has certain limitations which the District has experienced in the last few years. The most significant of these is the inability to account for multiple funds. As a result, the District is unable to determine the fund balance of any given fund at any given time. This makes it difficult for management and the Board of Managers to accurately determine the financial position of the District throughout the year.

In addition, the current system does not allow the District to enter budgeted amounts into the system. As a result, the system does not provide the necessary reports to accurately monitor budget to actual activity throughout the year.

We recommend the District implement a new accounting software system that is more suited for governmental accounting.

SAUK RIVER WATERSHED DISTRICT
Stearns County, Minnesota

MATERIAL WEAKNESSES
December 31, 2009

PREPARATION OF FINANCIAL STATEMENTS

As a function of the audit process, auditors are required to gain an understanding of the District's internal control, including the financial reporting process.

The District does not have an internal control system designed to provide for the preparation of the financial statements being audited. As auditors, we were requested to draft the financial statements and accompanying Notes to the Financial Statements. This circumstance is not unusual in an organization of your size.

Even though all management decisions related to financial reporting are made by the District's management and approval of the financial statements lies with management, it is the responsibility of management and those charged with governance to make the decision whether to accept the degree of risk associated with this condition because of cost or other considerations.

MATERIAL AUDIT ADJUSTMENTS

During the course of our engagement, we proposed material audit adjustments that would not have been identified as a result of the District's existing internal controls and, therefore, could have resulted in a material misstatement of the District's financial statements.

In order to ensure financial statements were free from material misstatement, audit adjustments were required in the following areas:

- Intergovernmental Revenue and Receivables
- Property Taxes and Special Assessments
- Accounts Payable
- Deferred Revenue
- Long-Term Debt
- Interfund Payables and Receivables

FOLLOW PROPER REIMBURSEMENT PROCEDURES FOR FEDERAL PROGRAMS

During our audit, we noted invoices attached to reimbursement requests did not match the reimbursement request and the same invoice would be included on multiple requests, making it difficult to tell which amounts were actually being submitted for reimbursement. In one instance, the same invoices were submitted twice for reimbursement under two different projects. Proper invoices should be attached to each reimbursement request to ensure monies are being received strictly on a reimbursement basis.

We recommend the District implement procedures to ensure the invoices attached to the pay requests are for actual charges and the invoices and the pay request agree. We further recommend the District ensure only appropriate disbursements are submitted for reimbursements and disbursements are not submitted more than once.

**SAUK RIVER WATERSHED DISTRICT
Stearns County, Minnesota**

**SIGNIFICANT DEFICIENCY
December 31, 2009**

REQUIRE APPROVAL AND BACKUP DOCUMENTATION FOR JOURNAL ENTRIES

During our audit, we tested the internal control over various District financial reporting functions. One such function is the general ledger journal entry process. During our testing, we found the journal entries are not approved on a timely basis and were lacking supporting documentation. Not having these processes in place could jeopardize the integrity of the financial statements.

As the District has a material weakness relating to the lack of segregation of accounting duties, there is the risk that not all significant areas of the District's financial reporting process are protected by adequate internal control. However, the journal entry process is one area we recommend an additional internal control could be implemented without adding significant cost. While implementing this control will not relieve the District of the material weakness, it is another control that reduces the risk that the financial statements are materially misstated. We also recommend the District attach supporting documentation to every journal entry to provide backup and to verify the validity of the entry.

SAUK RIVER WATERSHED DISTRICT
Stearns County, Minnesota

CONTROL DEFICIENCIES
December 31, 2009

RETAIN BACKUP DOCUMENTATION FOR ALL CREDIT CARD TRANSACTIONS

Not all receipts were available to support the transaction activity for the District's credit card statements. Without receipts to verify all charges, administration is unable to monitor credit card purchases for appropriate expenditures.

We recommend the District require adequate documentation be obtained to support the District's credit card purchases to ensure they are proper District expenditures.

RECONCILE WITHHOLDING ACCOUNTS

During our audit, we noted the payroll withholding accounts on the District's financial records are not reconciled. All payroll withholding accounts should be reconciled on a regular basis to ensure proper withholding amounts are posted to the general ledger and paid.

We recommend the Assistant Administrator reconcile the payroll withholding accounts monthly to ensure the proper balances are recorded. The monthly reconciliations should be reviewed for accuracy by the District Administrator. The reconciliations should include signature blocks for the preparer and the reviewer.

ESTABLISH A FORMAL CAPITAL ASSET POLICY

During our audit, we noted the District does not have a formal capital asset policy. The purpose of a capital asset policy is for the governing body to give direction to management with respect to recording and depreciating the District's capital assets.

A formal capital asset policy should include:

- The definition or criteria of a capital asset (tangible in nature, extended useful life, cost greater than capitalization threshold).
- A capitalization threshold (includes new purchases and repairs and betterments).
- Clarification on what amounts account for the initial cost of an asset (purchase price, interest capitalized during construction and other).
- What depreciation method to use (straight-line, accelerated or other).
- The depreciable lives for each class of capital assets.
- Procedures to follow for the disposition of capital assets (sales of assets, identifying obsolete and/or idle assets or other).

We recommend the District consider adopting a formal capital asset policy. A formal capital asset policy consistently applied will provide the District with financial statements that are consistent and comparable for future operating periods.

**SAUK RIVER WATERSHED DISTRICT
Stearns County, Minnesota**

**CONTROL DEFICIENCIES
December 31, 2009**

CONSIDER FORMAL DEPOSIT AND INVESTMENT POLICY

The District currently does not have a formal deposit and investment policy in place. Disclosure of the lack of policies was made in the District's financial statements, as required by Governmental Accounting Standards Board (GASB) Statement No. 40.

We recommend the District consider adopting a formal deposit and investment policy to establish guidelines for investing the District's funds. It is also recommended the policy address the risks outlined in GASB Statement No. 40. Those risks include custodial credit risk for deposits, credit risk, concentration of credit risk, interest rate risk, foreign currency risk and custodial credit risk for investments

IMPROPER CODING

During the audit, we noted improper coding of receipts and expenditures relating to capital outlay, assessments and intergovernmental revenues, including assessment revenues coded to incorrect projects.

We recommend the District review the coding against the chart of accounts prior to entering receipts and expenditures into the accounting system. We further recommend the District ensure that assessment revenue is being recorded in the correct fund.

UPDATE THE DISTRICT'S PERSONNEL POLICY

During our audit, we noted the District's personnel policy is outdated.

We recommend the District update its policy to align with current District philosophy. The policy should address whether or not employees are eligible to receive payment for vacation and sick days accrued during their employment if the employment is terminated. It should also clarify the rate at which an employee earns vacation and sick time.

SAUK RIVER WATERSHED DISTRICT
Stearns County, Minnesota

LEGAL COMPLIANCE FINDINGS
December 31, 2009

FOLLOW STANDARD PROCEDURES RELATED TO UNCLAIMED PROPERTY

Government entities are required to follow standard procedures related to unclaimed property. The District is required to hold unclaimed or uncashed checks or other intangible property for three years. If, after that time period, the District still has the unclaimed property, the District is required to report and deliver it to the State Commissioner of Commerce in accordance with *Minnesota Statutes 345.41 and 345.43*.

During our audit, we noted the District is not following these standard procedures.

We recommend the District certify their outstanding items to the state to be in compliance with *Minnesota Statutes*.

TIMELY SUBMISSION OF PUBLIC INDEBTEDNESS REPORT

Minnesota Statutes 471.70 states the principal accounting officer of the municipality report, on or before February 1 of each year, to the county auditors, the total amount of outstanding obligations and the purpose of which issued, as of December 31 of the preceding year.

During our audit, we noted the District did not submit the Public Indebtedness Report to Pope County, Stearns County and Todd County by the deadline. It was also noted the District had not received the report from the Counties until after February 1.

We recommend the Assistant Administrator ensure the Public Indebtedness Report is submitted on or before February 1 of each year to be in compliance with *Minnesota Statutes*.

CLAIMS AND PAYMENTS – DECLARATIONS

Minnesota Statutes 471.38, Subd. 2 states every person or person's agent claiming payment must sign a declaration to the effect that such account, claim or demand is just and correct and that no part of it has been paid.

During our audit, we noted claims were presented for payment and a signed declaration was not obtained by the District.

We recommend the District receive a declaration for all claims presented for payment.

I declare under the penalties of law that
this account, claim or demand is just and correct
and that no part of it has been paid.

Signature of Claimant

SAUK RIVER WATERSHED DISTRICT
Stearns County, Minnesota

REQUIRED COMMUNICATION
December 31, 2009

We have audited the financial statements of the District for the period ended December 31, 2009, and have issued our report dated March 12, 2010. Professional standards require that we provide you with the following information related to our audit.

**OUR RESPONSIBILITY UNDER U.S. GENERALLY ACCEPTED AUDITING
STANDARDS, *GOVERNMENT AUDITING STANDARDS* AND *OMB CIRCULAR
A-133***

As stated in our engagement letter, our responsibility, as described by professional standards, is to express an opinion about whether the financial statements prepared by management with your oversight are fairly presented, in all material respects, in conformity with U.S. generally accepted accounting principles. Our audit of the financial statements does not relieve you or management of your responsibilities. Our responsibility is to plan and perform our audit to obtain reasonable, but not absolute, assurance that the financial statements are free of material misstatement. As part of our audit, we considered the internal control of the District. Such considerations were solely for the purpose of determining our audit procedures and not to provide any assurance concerning such internal control. We are responsible for communicating significant matters related to the audit that are, in our professional judgment, relevant to your responsibilities in overseeing the financial reporting process. However, we are not required to design procedures specifically to identify such matters.

As part of obtaining reasonable assurance about whether the District's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit.

We also considered internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with U.S. Office of Management and Budget (OMB) *Circular A-133*.

Also, in accordance with OMB *Circular A-133*, we examined, on a test basis, evidence about the District's compliance with the types of compliance requirements described in the OMB *Circular A-133 Compliance Supplement* applicable to its major federal program for the purpose of expressing an opinion on the District's compliance with those requirements. While our audit provides a reasonable basis for our opinion, it does not provide a legal determination on the District's compliance with those requirements.

PLANNED SCOPE AND TIMING OF THE AUDIT

We performed the audit according to the planned scope and timing previously communicated to you.

SAUK RIVER WATERSHED DISTRICT
Stearns County, Minnesota

REQUIRED COMMUNICATION
December 31, 2009

QUALITATIVE ASPECTS OF ACCOUNTING PRACTICES

Management is responsible for the selection and use of appropriate accounting policies. In accordance with the terms of our engagement letter, we will advise management about the appropriateness of accounting policies and their application. The significant accounting policies used by the District are described in Note 1 to the financial statements. No new accounting policies were adopted and the application of existing policies was not changed during 2009. We noted no transactions entered into during the year for which there is a lack of authoritative guidance or consensus. There are no significant transactions that have been recognized in the financial statements in a different period than when the transaction occurred.

Accounting estimates are an integral part of the financial statements prepared by management and are based on management's knowledge and experience about past and current events and assumptions about future events. Certain accounting estimates are particularly sensitive because of their significance to the financial statements and because of the possibility that future events affecting them may differ significantly from those expected. The most sensitive estimate affecting the financial statements was:

Depreciation – The District is currently depreciating its capital assets over their estimated useful lives, as determined by management, using the straight-line method.

We evaluated the key factors and assumptions used to develop the above estimate in determining it is reasonable in relation to the financial statements taken as a whole.

The disclosures in the financial statements are neutral, consistent and clear.

DIFFICULTIES ENCOUNTERED IN PERFORMING THE AUDIT

We encountered no difficulties in dealing with management in performing and completing our audit.

CORRECTED AND UNCORRECTED MISSTATEMENTS

Professional standards require us to accumulate all known and likely misstatements identified during the audit, other than those that are trivial, and communicate them to the appropriate level of management. Management did not identify and we did not notify them of any uncorrected financial statement misstatements. Material misstatements relating to intergovernmental revenue and receivables, property taxes and special assessments, accounts payable, deferred revenue, long-term debt and interfund payables and receivables were detected as a result of audit procedures and were corrected by management.

**SAUK RIVER WATERSHED DISTRICT
Stearns County, Minnesota**

**REQUIRED COMMUNICATION
December 31, 2009**

DISAGREEMENTS WITH MANAGEMENT

For purposes of this letter, professional standards define a disagreement with management as a financial accounting, reporting or auditing matter, whether or not resolved to our satisfaction that could be significant to the financial statements or the auditor's report. We are pleased to report that no such disagreements arose during the course of our audit.

MANAGEMENT REPRESENTATIONS

We requested certain representations from management which were provided to us in the management representation letter.

MANAGEMENT CONSULTATIONS WITH OTHER INDEPENDENT ACCOUNTANTS

In some cases, management may decide to consult with other accountants about auditing and accounting matters, similar to obtaining a "second opinion" on certain situations. If a consultation involves application of an accounting principle to the District's financial statements or a determination of the type of auditor's opinion that may be expressed on those statements, our professional standards require the consulting accountant to check with us to determine that the consultant has all the relevant facts. We are not aware of any consultations by the District's management with other accountants during the course of our audit.

OTHER ISSUES

We generally discuss a variety of matters, including the application of accounting principles and auditing standards, with management each year prior to retention as the District's auditors. However, these discussions occurred in the normal course of our professional relationship and our responses were not a condition to our retention.

OTHER INFORMATION IN DOCUMENTS CONTAINING AUDITED FINANCIAL STATEMENTS

We have not reviewed, and it is our understanding, that no other published documents exist that contain audited financial statement information, for which we are currently auditing. As stated in our engagement letter, if you publish or reproduce the financial statements or make reference to our Firm name in relation to such documents, you agree to provide us with a copy of the final reproduced material for our approval before it is distributed.