STATE OF MINNESOTA
Office of the State Auditor

Rebecca Otto
State Auditor

LINCOLN, LYON, & MURRAY
HUMAN SERVICES
MARSHALL, MINNESOTA

FOR THE YEAR ENDED DECEMBER 31, 2007

Description of the Office of the State Auditor

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

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

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

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

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

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

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

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

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

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LINCOLN, LYON, & MURRAY HUMAN SERVICES MARSHALL, MINNESOTA

For the Year Ended December 31, 2007

Audit Practice Division
Office of the State Auditor
State of Minnesota

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LINCOLN, LYON, & MURRAY HUMAN SERVICES
MARSHALL, MINNESOTA

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Introductory Section

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LINCOLN, LYON, & MURRAY HUMAN SERVICES
MARSHALL, MINNESOTA

ORGANIZATION
2007

Board	County	Appointment Expires
Chair		
Robert Fenske	Lyon	December 31, 2007
Vice Chair		
Steve Ritter	Lyon	December 31, 2007
Secretary		
Ann Svendsen	Lincoln	July 5, 2008
Members		
Joan Jagt	Lincoln	December 31, 2007
Deane Sagmoe	Lincoln	December 31, 2007
Carmen Marben	Lyon	July 5, 2008
Gail Byers	Murray	July 5, 2008
Gerald Magnus	Murray	December 31, 2007
Kevin Vickerman	Murray	December 31, 2007
Lincoln, Lyon, & Murray Human Services		
Attorney		
William J. Toulouse		Indefinite
Director		
Christopher Sorensen		Indefinite
Director of Business Management		
Nancy Walker		Indefinite

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Financial Section

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REBECCA OTTO
STATE AUDITOR

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INDEPENDENT AUDITOR'S REPORT

Board Members
Lincoln, Lyon, & Murray Human Services

We have audited the financial statements of the governmental activities, the major fund, and the remaining fund information of Lincoln, Lyon, & Murray Human Services as of and for the year ended December 31, 2007, which collectively comprise the Human Services' basic financial statements as listed in the table of contents. These financial statements are the responsibility of the Human Services' management. Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the basic financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the basic 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 basic financial statements referred to above present fairly, in all material respects, the financial position of the governmental activities, the major fund, and the remaining fund information of Lincoln, Lyon, & Murray Human Services as of December 31, 2007, and the changes in financial position thereof and the General Fund budgetary comparison for the year then ended in conformity with accounting principles generally accepted in the United States of America.

The Management's Discussion and Analysis is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted primarily of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was made for the purpose of forming opinions on the basic financial statements of Lincoln, Lyon, & Murray Human Services. The statement and schedule listed as supplementary information and as a supporting schedule in the table of contents are presented for the purpose of additional analysis and are not a required part of the basic financial statements of the Human Services. The supplemental and supporting information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly presented in all material respects in relation to the basic financial statements taken as a whole.

In accordance with *Government Auditing Standards*, we have also issued our report dated June 26, 2008, on our consideration of Lincoln, Lyon, & Murray Human Services' internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

/s/Rebecca Otto	*/s/Greg Hierlinger*
REBECCA OTTO STATE AUDITOR	GREG HIERLINGER, CPA DEPUTY STATE AUDITOR

June 26, 2008

MANAGEMENT'S DISCUSSION AND ANALYSIS

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LINCOLN, LYON, & MURRAY HUMAN SERVICES
MARSHALL, MINNESOTA

MANAGEMENT'S DISCUSSION AND ANALYSIS
DECEMBER 31, 2007
(Unaudited)

Lincoln, Lyon, & Murray Human Services' Management's Discussion and Analysis (MD&A) provides an overview of the Human Services' financial activities for the fiscal year ended December 31, 2007. Since this information is designed to focus on the current year's activities, resulting changes, and currently known facts, it should be read in conjunction with the Human Services' financial statements (beginning with Exhibit 1).

FINANCIAL REPORTING ENTITY

Lincoln, Lyon, & Murray Human Services was formed pursuant to Minn. Stat. § 393.01, subd. 7, (joint powers agreement) by Lincoln, Lyon, and Murray Counties. The Human Services began official operation on July 1, 1974, and performs Board and welfare functions. Local financing is provided by the three member counties on the basis of each county's welfare expenditures in 1973. Percentages are:

Lincoln County	-	20.90 percent
Lyon County	-	54.77 percent
Murray County	-	24.33 percent

FINANCIAL HIGHLIGHTS

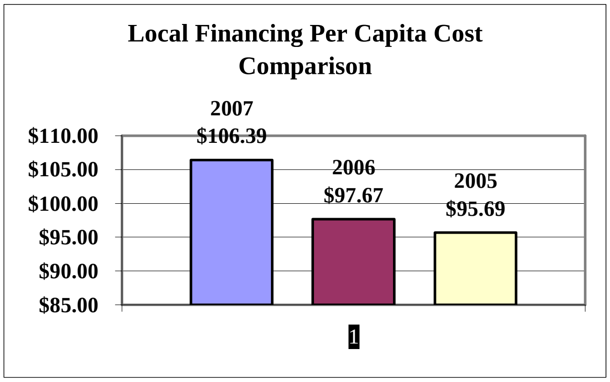
Governmental activities' total net assets are $3,476,003, of which $80,519 is invested in capital assets (Exhibit 1). Governmental activities' total net assets increased by $101,046. Lincoln, Lyon, and Murray Human Services' net assets increased primarily due to additional revenue derived from Medical Assistance Transportation claiming, Medical Assistance recoveries, refiling claims due to insufficient service units, and look-backs of Targeted Case Management Units.

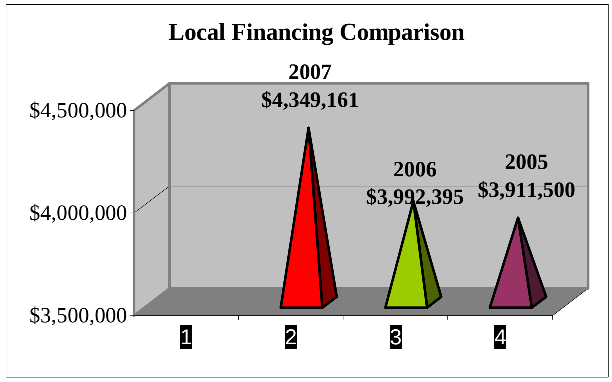
Local financing for the Human Services in 2007 was $4,349,161, which comprised 43.2 percent of the total intergovernmental revenue. Comparing 2007 with 2006 and 2005, the following tables show local financing costs and per capita cost increased beginning with 2005 through 2007.

Schedule of Local Financing Revenue (Schedule 1)

	2007	2006	2005
Payments from participating counties	$ 4,349,161	$ 3,992,395	$ 3,911,500

Population of all three counties is 40,878.





From 2005 to 2006, intergovernmental revenue decreased by $220,026, and from 2006 to 2007, intergovernmental revenue increased by $1,063,243. This significant increase was primarily in the area of county contributions, state reimbursement for services, and state grants. However, since 2005, investment earnings increased from 2005 to 2006 but decreased from 2006 to 2007, as relative to interest rates and the economy. From 2005 to 2006, investment earnings increased by $23,393; from 2006 to 2007, it decreased by $33,467.

OVERVIEW OF THE FINANCIAL STATEMENTS

This MD&A is intended to serve as an introduction to the basic financial statements. Lincoln, Lyon, & Murray Human Services' basic financial statements consist of two statements that combine government-wide financial statements and fund financial statements, a budgetary comparison statement, a statement of changes in assets and liabilities for the agency fund, and notes to the financial statements. The MD&A (this section) is required to accompany the basic financial statements and, therefore, is included as required supplementary information.

The first column of each of the first two statements presents governmental fund data. These columns focus on how money flows in and out and the balances left at year-end available for spending. They are reported using an accounting method called modified accrual accounting. This method measures cash and all other financial assets that can be readily converted to cash. These columns provide a detailed short-term view of the Human Services' general government operations and the basic services it provides. Governmental fund information helps determine whether there are more or fewer financial resources that can be spent in the near future to finance the Human Services' programs. We reconcile the relationship (or differences) between governmental funds and governmental activities (reported in the third column) in the center column of each statement.

The third column in each statement presents the governmental activities' statement of net assets and the statement of activities, which provide information about the activities of the Human Services as a whole and present a longer-term view of the Human Services' finances. These columns include all assets and liabilities using the accrual basis of accounting, which is similar to the accounting used by most private-sector companies. All of the current year's revenues and expenses are taken into account regardless of when cash is received or paid. Over time, increases or decreases in the Human Services' net assets are one indicator of whether its financial health is improving or deteriorating.

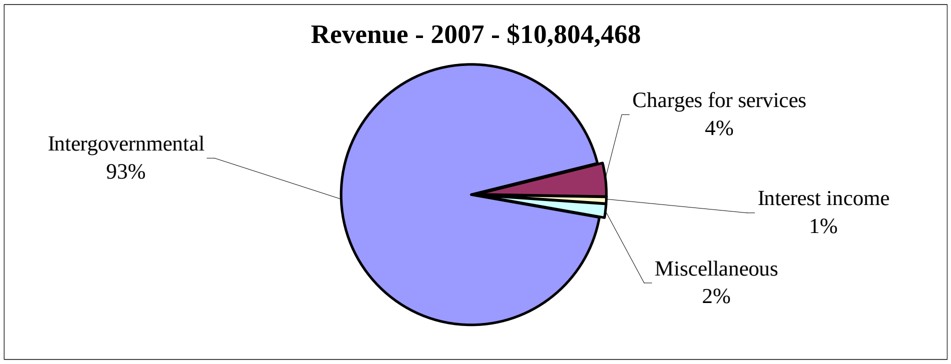
Governmental Activities

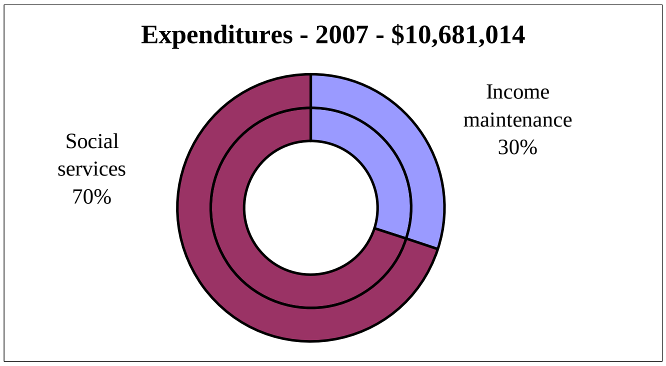
Comparative statements of net assets and activities illustrate the changes from 2006 to 2007:

	2007	2006	Percent (%) Change
Assets			
Current assets	$ 4,913,435	$ 4,357,909	12.7
Capital assets, net of depreciation	80,519	111,634	(27.9)
Total Assets	$ 4,993,954	$ 4,469,543	11.7
Liabilities			
Current liabilities	$ 1,062,574	$ 630,502	68.5
Long-term liabilities	455,377	464,084	(1.9)
Total Liabilities	$ 1,517,951	$ 1,094,586	38.7
Net Assets			
Invested in capital assets	$ 80,519	$ 111,634	(27.9)
Unrestricted	3,395,484	3,263,323	4.0
Total Net Assets	$ 3,476,003	$ 3,374,957	3.0
Revenues			
Intergovernmental	$ 10,073,472	$ 9,010,229	11.8
Charges for services	475,748	428,212	11.1
Investment earnings	84,448	117,915	(28.4)
Miscellaneous	170,800	192,099	(11.1)
Total Revenues	$ 10,804,468	$ 9,748,455	10.8
Expenses	10,703,422	11,293,783	(5.2)
Change in Net Assets	$ 101,046	$ (1,545,328)	106.5
Net Assets - January 1	3,374,957	4,920,285	(31.4)
Net Assets - December 31	$ 3,476,003	$ 3,374,957	3.0

Governmental Fund

Revenues for the Human Services' General Fund increased 10.8 percent ($1,056,013) from the prior year, while total expenditures decreased by 4.47 percent ($500,166) from the prior year. This results in a 3.31 percent increase in fund balance in the year ended December 31, 2007.





As shown in the Statement of Activities on Exhibit 2, the amount that was received through intergovernmental revenue was 93 percent of the total revenue received. See below for breakout of intergovernmental revenue.

General Fund - 2007

Revenues	Amount
Intergovernmental	$ 10,073,472
Charges for services	475,748
Interest on investments	84,448
Miscellaneous	170,800
Total Revenues	$ 10,804,468

General Fund Budgetary Highlights

Over the course of the year, the original to final budget totals stayed the same. Actual revenue exceeded budgeted revenue by $1,123,574. Areas that contributed to this were over $350,000 in reimbursement for Medical Assistance Transportation, resubmission of previously reduced and rejected claims, and higher than expected revenue for Child Welfare Targeted Case Management. Another related factor was due to the way that MMIS revenue was receipted in previous years; however, this has been updated in the 2008 budget. CW-TCM revenue was not budgeted for 2007 because of the unknown status of claiming as a result of the 2006 Federal Budget Reconciliation Act. This act passed Congress on February 1, 2006, and provided for many changes affecting the Human Services in the area of federal revenues. In 2007, the Centers for Medicaid and Medicare Services (CMS) notified Minnesota that the interim-final rule regarding Targeted Case Management and specifically Child Welfare Targeted Case Management would no longer be an eligible service to be billed to Medical Assistance. This interim-final rule triggered action from the Minnesota Department of Human Services that is two-fold: (1) counties were to discontinue claiming for CW-TCM as of February 29, 2008; and (2) a provision passed in the 2007 Minnesota State Legislature would divide approximately $23 million in set-aside funding for counties based upon prior year earning and be distributed accordingly. Lincoln, Lyon, & Murray Human Services received approximately $185,000 this year (2008) in set-aside funding as a result. The State of Minnesota-approved remedy mitigated some of the funding reductions for CW-TCM but will still leave the LLMHS with approximately $50,000 less in funding for 2008 as compared with 2007. This one-time measure is not enough to offset projected costs in child welfare services and could be a factor in increased agency costs in 2009 and beyond.

Actual expenditures exceeded budgeted by $885,892. The areas of Medical Assistance Transportation costs, costs related to children's services, and general overhead costs in both income maintenance and social services were all contributing factors.

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets

The Human Services' investment in capital assets for its governmental activities for the year ended December 31, 2007, is $80,519 (net of accumulated depreciation). This investment in capital assets includes office furniture and equipment and automotive equipment. There was a decrease in the Human Services' investment in capital assets for the current fiscal year of 27.87 percent. Overall, the Human Services has been holding onto capital assets longer and replacing at a slower rate due to decreased funding and revenues.

Capital asset activity for the year ended December 31, 2007, was as follows:

	Beginning Balance	Increase	Decrease	Ending Balance
Capital assets depreciated				
Office furniture and equipment	$ 227,911	$ 19,509	$ 25,390	$ 222,030
Automotive equipment	220,854	-	-	220,854
Total capital assets depreciated	$ 448,765	$ 19,509	$ 25,390	$ 442,884
Less: accumulated depreciation for				
Office furniture and equipment	$ 176,122	$ 31,607	$ 25,390	$ 182,339
Automotive equipment	161,009	19,017	-	180,026
Total accumulated depreciation	$ 337,131	$ 50,624	$ 25,390	$ 362,365
Total Capital Assets Depreciated, Net	$ 111,634	$ (31,115)	$ -	$ 80,519

Depreciation expense was charged to income maintenance and social services programs for the year ended December 31, 2007.

Information on the Human Services' capital assets can be found in the notes to the financial statements.

Long-Term Liabilities

The Human Services' long-term liabilities consist of compensated absences at December 31, 2007, as follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Compensated absences	$ 464,084	$ -	$ 8,707	$ 455,377	$ 40,346

ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES

Lincoln, Lyon, & Murray Human Services planned to use approximately $114,000 in fund balance for the 2007 budget year but ended the year by adding to the fund balance by approximately $123,000. For 2008, Lincoln, Lyon, & Murray Human Services passed a balanced budget. Local government financing (county levy) for Lincoln, Lyon, & Murray Human Services increased by five percent for 2008.

As of this report, the State of Minnesota and federal legislative bodies are considering budgets that will affect human services on a local level. We expect little growth in revenue in the next couple of years with additional financial and programmatic costs to local human services as a result of the current economic conditions. The trending of budgetary reductions for local county human services agencies has become a normative feature over the last seven years. We anticipate that, given the current funding priorities, most of the emphasis for service development will be focused upon maintaining the "safety net" of services for our most vulnerable community members.

CONTACTING THE HUMAN SERVICES' FINANCIAL MANAGEMENT

This financial report is designed to provide a general overview of Lincoln, Lyon, & Murray Human Services' financial statements. Additional questions or further explanation of this report can be obtained by contacting Christopher J. Sorensen, Director of Lincoln, Lyon, & Murray Human Services, 607 West Main Street, Marshall, Minnesota 56258.

BASIC FINANCIAL STATEMENTS

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LINCOLN, LYON, & MURRAY HUMAN SERVICES
MARSHALL, MINNESOTA

EXHIBIT 1

GENERAL FUND BALANCE SHEET AND
GOVERNMENTAL ACTIVITIES - STATEMENT OF NET ASSETS
WITH ADJUSTMENTS TO CONVERT MODIFIED TO FULL ACCRUAL
DECEMBER 31, 2007

	General Fund	Reconciliation	Governmental Activities
Assets			
Current assets			
Cash and pooled investments	$ 4,079,423	$ -	$ 4,079,423
Petty cash and change funds	540	-	540
Accounts receivable	18,788	-	18,788
Accrued interest receivable	6,128	-	6,128
Due from other governments	808,556	-	808,556
Capital assets			
Depreciable - net	-	80,519	80,519
Total Assets	**$ 4,913,435**	**$ 80,519**	**$ 4,993,954**
Liabilities			
Current liabilities			
Accounts payable	$ 271,510	$ -	$ 271,510
Salaries payable	303,662	-	303,662
Due to other governments	487,402	-	487,402
Long-term liabilities			
Due within one year	-	40,346	40,346
Due in more than one year	-	415,031	415,031
Total Liabilities	**$ 1,062,574**	**$ 455,377**	**$ 1,517,951**
Fund Balance/Net Assets			
Fund Balance			
Reserved for unspent grant monies	$ 39,496		
Unreserved, undesignated	3,811,365		
Total Fund Balance	**$ 3,850,861**	**$ (3,850,861)**	
Total Liabilities and Fund Balance	**$ 4,913,435**		
Net Assets			
Invested in capital assets		$ 80,519	$ 80,519
Unrestricted		3,395,484	3,395,484
Total Net Assets		**$ 3,476,003**	**$ 3,476,003**

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

LINCOLN, LYON, & MURRAY HUMAN SERVICES
MARSHALL, MINNESOTA

EXHIBIT 1
(Continued)

**GENERAL FUND BALANCE SHEET AND
GOVERNMENTAL ACTIVITIES - STATEMENT OF NET ASSETS
WITH ADJUSTMENTS TO CONVERT MODIFIED TO FULL ACCRUAL
DECEMBER 31, 2007**

Reconciliation of the General Fund Balance to Net Assets		
Fund Balance - General Fund	$	3,850,861
Capital assets are reported on the Statement of Net Assets but not on the Fund Balance Sheet.		80,519
Long-term liabilities are reported on the Statement of Net Assets but not on the Fund Balance Sheet.		(455,377)
Net Assets - Governmental Activities	**$**	**3,476,003**

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

LINCOLN, LYON, & MURRAY HUMAN SERVICES
MARSHALL, MINNESOTA

EXHIBIT 2

GENERAL FUND STATEMENT 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, 2007

	General Fund	Reconciliation	Governmental Activities
Revenues			
Intergovernmental	$ 10,073,472	$ -	$ 10,073,472
Charges for services	475,748	-	475,748
Investment earnings	84,448	-	84,448
Miscellaneous	170,800	-	170,800
Total Revenues	**$ 10,804,468**	**$ -**	**$ 10,804,468**
Expenditures/Expenses			
Current			
Human services			
Income maintenance	$ 3,194,608	$ 8,963	$ 3,203,571
Social services	7,486,406	13,445	7,499,851
Total Expenditures/Expenses	**$ 10,681,014**	**$ 22,408**	**$ 10,703,422**
Net Change in Fund Balance/Net Assets	**$ 123,454**	**$ (22,408)**	**$ 101,046**
Fund Balance/Net Assets - January 1	**3,727,407**	**(352,450)**	**3,374,957**
Fund Balance/Net Assets - December 31	**$ 3,850,861**	**$ (374,858)**	**$ 3,476,003**

Reconciliation of the Statement of General Fund Revenues, Expenditures, and Changes in Fund Balance to the Statement of Activities - Governmental Activities

Net Change in Fund Balance		**$ 123,454**
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.		
Capital outlay expenditures	$ 19,509	
Current year depreciation expense	(50,624)	(31,115)
Some expenses reported in the Statement of Activities do not require the use of current financial resources and, therefore, are not reported as expenditures in governmental funds.		
(Increase) decrease in compensated absences payable		8,707
Change in Net Assets of Governmental Activities		**$ 101,046**

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

LINCOLN, LYON, & MURRAY HUMAN SERVICES
MARSHALL, MINNESOTA

EXHIBIT 3

STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCE
BUDGETARY COMPARISON
FOR THE YEAR ENDED DECEMBER 31, 2007

	Budgeted Amounts		Actual	Variance with
	Original	**Final**	**Amounts**	**Final Budget**
Revenues				
Intergovernmental	$ 8,944,927	$ 8,944,927	$ 10,073,472	$ 1,128,545
Charges for services	378,967	378,967	475,748	96,781
Interest on investments	120,000	120,000	84,448	(35,552)
Miscellaneous	237,000	237,000	170,800	(66,200)
Total Revenues	**$ 9,680,894**	**$ 9,680,894**	**$ 10,804,468**	**$ 1,123,574**
Expenditures				
Current				
Human services				
Income maintenance	$ 2,855,544	$ 2,855,544	$ 3,194,608	$ (339,064)
Social services	6,939,578	6,939,578	7,486,406	(546,828)
Total Expenditures	**$ 9,795,122**	**$ 9,795,122**	**$ 10,681,014**	**$ (885,892)**
Net Change in Fund Balance	**$ (114,228)**	**$ (114,228)**	**$ 123,454**	**$ 237,682**
Fund Balance - January 1	**3,727,407**	**3,727,407**	**3,727,407**	**-**
Fund Balance - December 31	**$ 3,613,179**	**$ 3,613,179**	**$ 3,850,861**	**$ 237,682**

FIDUCIARY FUND

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LINCOLN, LYON, & MURRAY HUMAN SERVICES
MARSHALL, MINNESOTA

EXHIBIT 4

STATEMENT OF FIDUCIARY NET ASSETS
AGENCY FUND
DECEMBER 31, 2007

Assets	
Cash and pooled investments	**$ 22,980**
Liabilities	
Due to other governments	**$ 22,980**

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

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1. Summary of Significant Accounting Policies

Lincoln, Lyon, & Murray Human Services' financial statements are prepared in accordance with generally accepted accounting principles (GAAP) as of and for the year ended December 31, 2007. The Governmental Accounting Standards Board (GASB) is responsible for establishing GAAP for state and local governments through its pronouncements (statements and interpretations). Governments are also required to follow the pronouncements of the Financial Accounting Standards Board issued through November 30, 1989, (when applicable) that do not conflict with or contradict GASB pronouncements. The more significant accounting policies established in GAAP and used by the Human Services are discussed below.

A. Financial Reporting Entity

Lincoln, Lyon, & Murray Human Services was formed pursuant to Minn. Stat. § 393.01, subd. 7, by Lincoln, Lyon, and Murray Counties. The Human Services began official operation on July 1, 1974, and performs welfare functions formerly performed by the individual counties. Local financing is provided by the three member counties on the basis of each county's welfare expenditures in 1973. Percentages are:

Lincoln County	20.90%
Lyon County	54.77
Murray County	24.33

Lincoln, Lyon, & Murray Human Services is governed by two County Commissioners from each of the participating counties, who are chosen by their respective County Boards, and one lay person from each participating county. In 1999, the Human Services changed its name from the Region VIII North Welfare Board.

Lincoln, Lyon, & Murray Human Services is an independent joint venture and is not included in any of the member counties' reporting entities.

Joint Ventures

Lincoln, Lyon, & Murray Human Services participates in a joint venture which is described in Note 6.B.

1. Summary of Significant Accounting Policies (Continued)

B. Basic Financial Statements

Basic financial statements include information on the Human Services' non-fiduciary activities and information on the General Fund of the Human Services. These separate presentations are reported in different columns on Exhibits 1 and 2. Each of the exhibits starts with a column of information based on activities of the General Fund and reconciles it to a column that reports the "governmental activities" of the Human Services as a whole.

The governmental activities columns are reported on the full accrual, economic resources basis, which recognizes all long-term assets and receivables as well as long-term debt and obligations. The Human Services' net assets are reported in two parts: invested in capital assets and unrestricted net assets. The Statement of Activities demonstrates the degree to which the expenses of the Human Services are offset by revenues.

The Balance Sheet and Statement of Revenues, Expenditures, and Changes in Fund Balance for the General Fund are presented on the modified accrual basis and report current financial resources.

Additionally, the Human Services reports a fiduciary fund type, which is excluded from the governmental activities. The Agency Fund is custodial in nature and does not present result of operations or have a measurement focus. This fund accounts for assets that the Human Services holds for the Collaborative in an agent capacity.

C. Measurement Focus and Basis of Accounting

The governmental activities and fiduciary fund 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. Lincoln, Lyon, & Murray Human Services considers all revenues as available if collected within

1. <u>Summary of Significant Accounting Policies</u>

C. <u>Measurement Focus and Basis of Accounting</u> (Continued)

60 days after the end of the current period. Charges for services and interest are considered susceptible to accrual. Expenditures are recorded when the related fund liability is incurred, except for principal and interest on general long-term debt, compensated absences, and claims and judgments, which are recognized as expenditures to the extent that they have matured. Proceeds of long-term debt and acquisitions under capital leases are reported as other financing sources.

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

D. <u>Assets, Liabilities, and Net Assets or Equity</u>

1. <u>Deposits and Investments</u>

Deposits and investments are reported at their fair value at December 31, 2007, based on market prices.

Under the direction of the Investment Committee and the Board, most cash transactions are administered by the Lyon County Auditor/Treasurer.

Lincoln, Lyon, & Murray Human Services invests in an external investment pool, the Minnesota Association of Governments Investing for Counties (MAGIC) Fund, which is created under a joint powers agreement pursuant to Minn. Stat. § 471.59. The MAGIC Fund is not registered with the Securities and Exchange Commission (SEC), but does operate in a manner consistent with Rule 2a-7 prescribed by the SEC pursuant to the Investment Company Act of 1940 (17 C.F.R. § 270.2a-7). Therefore, the fair value of Lincoln, Lyon, & Murray Human Services' position in the pool is the same as the value of the pool shares.

2. <u>Receivables</u>

The financial statements for the Human Services contain no allowance for uncollectible accounts. Uncollectible amounts due for receivables are recognized as bad debts at the time information becomes available that indicates the uncollectibility of the particular receivable. These amounts are not considered to be material in relation to the financial position or operations of the fund.

1. Summary of Significant Accounting Policies

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

3. Capital Assets

Capital assets, which include office furniture and equipment and automotive equipment, are reported in the governmental activities column in the Statement of Net Assets. Capital assets are defined as assets with an initial, individual cost of more than $1,500 and an estimated useful life in excess of two years. Such assets are recorded at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at estimated fair 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.

Office furniture and equipment and automotive equipment are depreciated using the straight-line method over the following estimated useful lives:

Assets	Years
Office furniture and equipment	3 to 10
Automotive equipment	6

4. Compensated Absences

The liability for compensated absences reported in financial statements consists of unpaid, accumulated annual and sick leave balances. The liability has been calculated using the vesting method, in which leave amounts for both employees who currently are eligible to receive termination payments and other employees who are expected to become eligible in the future to receive such payments upon termination are included. Compensated absences are accrued when incurred in the fund financial statements. A liability for these amounts is reported in the governmental funds only if they have matured, for example, as a result of employee resignations and retirements.

1. Summary of Significant Accounting Policies

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

      5. Deferred Revenue

         Governmental funds and the government-wide statements defer revenue recognition in connection with 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.

      6. Long-Term Liabilities

         Long-term liabilities are not reported in the fund. The General Fund reports only liabilities expected to be financed with available, spendable financial resources. The Statement of Net Assets reports long-term liabilities of the governmental activities.

      7. Fund Equity

         The fund financial statements report reservations of fund balance for amounts not available for appropriation or legally restricted by outside parties for use for a specific purpose. Designations of fund balance represent tentative management plans subject to change. The Human Services reported no designations for the year ended December 31, 2007.

      8. Use of Estimates

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

2. Stewardship, Compliance, and Accountability

Excess of Expenditures Over Budget

The General Fund had expenditures in excess of budget for the year ended December 31, 2007.

Fund	Expenditures	Budget	Excess
General	$ 10,681,014	$ 9,795,122	$ 885,892

3. Detailed Notes

A. Assets

1. Deposits and Investments

Deposits

Minn. Stat. §§ 118A.02 and 118A.04 authorize Lincoln, Lyon, & Murray Human Services to designate a depository for public funds and to invest in certificates of deposit. Minn. Stat. § 118A.03 requires that all Human Services' 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 bonds; issues of U.S. government agencies; general obligations rated "A" or better, revenue obligations rated "AA" or better; irrevocable standby letters of credit issued by the Federal Home Loan Bank; and certificates of deposit. Minnesota statutes require that securities pledged as collateral be held in safekeeping in a restricted account at the Federal Reserve Bank or in an account at a trust department of a commercial bank or other financial institution not owned or controlled by the financial institution furnishing the collateral.

3. Detailed Notes

A. Assets

1. Deposits and Investments

Deposits (Continued)

Custodial Credit Risk

Custodial credit risk is the risk that in the event of a financial institution failure, the Human Services' deposits may not be returned to it. The Human Services does not have a policy for custodial credit risk. As of December 31, 2007, $176,392 of the Human Services' deposits was exposed to custodial credit risk.

Investments

Minn. Stat. §§ 118A.04 and 118A.05 generally authorize the following types of investments as available to Lincoln, Lyon, & Murray Human Services:

(1) securities which are direct obligations or are guaranteed or insured issues of the United States, its agencies, its instrumentalities, or organizations created by an act of Congress, except mortgage-backed securities defined as "high risk" by Minn. Stat. § 118A.04, subd. 6;

(2) mutual funds through shares of registered investment companies provided the mutual fund receives certain ratings depending on its investments;

(3) general obligations of the State of Minnesota and its municipalities, and in certain state agency and local obligations of Minnesota and other states provided such obligations have certain specified bond ratings by a national bond rating service;

(4) bankers' acceptances of United States banks;

(5) commercial paper issued by United States corporations or their Canadian subsidiaries rated in the highest quality category by two nationally recognized rating agencies and maturing in 270 days or less; and

3. Detailed Notes

A. Assets

1. Deposits and Investments

Investments (Continued)

(6) with certain restrictions, in repurchase agreements, securities lending agreements, joint powers investment trusts, and guaranteed investment contracts.

Interest Rate Risk

Interest rate risk is the risk that changes in the market interest rates will adversely affect the fair value of an investment. The Human Services minimizes its exposure to interest rate risk by investing in both short-term and long-term investments and by timing cash flows from maturities so that a portion of the portfolio is maturing or coming close to maturity evenly over time as necessary to provide the cash flow and liquidity needed for operations.

Credit Risk

Generally, credit risk is the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment. This is measured by the assignment of a rating by a nationally recognized statistical rating organization. It is the Human Services' policy to invest only in securities that meet the ratings requirements set by state statute.

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 in the possession of an outside party. As of December 31, 2007, the Human Services' investments were not exposed to custodial credit risk.

3. Detailed Notes

A. Assets

1. Deposits and Investments

Investments (Continued)

Concentration of Credit Risk

The concentration of credit risk is the risk of loss that may be caused by the Human Services' investment in a single issuer. The Human Services does not have a policy that addresses this risk but currently invests only in certificates of deposit and the MAGIC Fund external investment pool.

At December 31, 2007, the Human Services had the following deposits and investments.

Petty cash and change funds	$ 540
Cash in bank	2,949,134
MAGIC Fund	1,153,269
Total Cash and Investments	$ 4,102,943

As reported in the financial statements:

Governmental activities	
Cash and pooled investments	$ 4,079,423
Petty cash and change funds	540
Agency Fund	
Cash and pooled investments	22,980
Total	$ 4,102,943

2. Receivables

The Human Services did not have any receivables scheduled to be collected beyond one year as of December 31, 2007.

3. Detailed Notes

A. Assets (Continued)

3. Capital Assets

Capital asset activity for the year ended December 31, 2007, was as follows:

	Beginning Balance	Increase	Decrease	Ending Balance
Capital assets depreciated				
Office furniture and equipment	$ 227,911	$ 19,509	$ 25,390	$ 222,030
Automotive equipment	220,854	-	-	220,854
Total capital assets depreciated	$ 448,765	$ 19,509	$ 25,390	$ 442,884
Less: accumulated depreciation for				
Office furniture and equipment	$ 176,122	$ 31,607	$ 25,390	$ 182,339
Automotive equipment	161,009	19,017	-	180,026
Total accumulated depreciation	$ 337,131	$ 50,624	$ 25,390	$ 362,365
Total Capital Assets Depreciated, Net	$ 111,634	$ (31,115)	$ -	$ 80,519

Depreciation expense was charged to income maintenance and social services programs for the year ended December 31, 2007.

B. Liabilities

1. Retired Employee Health Insurance Benefits

The Human Services pays the health and dental insurance for qualified employees who retire between the ages of 55 and 65, have worked for the Human Services for at least 15 years, and are receiving a disability benefit or Public Employees Retirement Association of Minnesota (PERA) annuity, or who have met age and service requirements necessary to receive a PERA annuity. These employees are entitled to receive four percent per year of service toward the employee’s health and dental insurance premium. The coverage shall discontinue at age 65 and/or when they become Medicare eligible, or until they obtain work in which insurance benefits are available to them as an individual at no cost.

3. Detailed Notes

B. Liabilities

1. Retired Employee Health Insurance Benefits (Continued)

The Human Services' contributions for the year ended December 31, 2007, were for ten employees, for a total of $63,400. The Human Services records the expenditures for retired employees' health and dental insurance benefits in the year paid and does not accrue a liability for future benefits.

2. Changes in Long-Term Liabilities

Long-term liability activity for the year ended December 31, 2007, was as follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Compensated absences	$ 464,084	$ -	$ 8,707	$ 455,377	$ 40,346

4. Pension Plans

A. Plan Description

All full-time and certain part-time employees of Lincoln, Lyon, & Murray Human Services are covered by defined benefit plans administered by PERA. PERA administers the Public Employees Retirement Fund, which is a cost-sharing, multiple-employer retirement plan. The plan is established and administered in accordance with Minn. Stat. chs. 353 and 356.

Public Employees Retirement Fund members belong to either the Coordinated Plan or the Basic Plan. Coordinated Plan members are covered by Social Security, and Basic Plan members are not. All new members must participate in the Coordinated Plan.

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 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.

4. Pension Plans

A. Plan Description (Continued)

Two methods are used to compute benefits for Coordinated and Basic Plan members. The retiring member receives the higher of a step-rate benefit accrual formula (Method 1) or a level accrual formula (Method 2). Under Method 1, the annuity accrual rate for a Basic Plan member is 2.2 percent of average salary for each of the first ten years of service and 2.7 percent for each year thereafter. For a Coordinated Plan member, the annuity accrual rate is 1.2 percent of average salary for each of the first ten years of service and 1.7 percent for each successive year. Using Method 2, the annuity accrual rate is 2.7 percent of average salary for Basic Plan members and 1.7 percent for Coordinated Plan members for each year of service.

For Public Employees Retirement Fund members whose annuity is calculated using Method 1, a full annuity is available when age plus years of service equal 90. A reduced retirement annuity is also available to eligible members seeking early retirement.

The benefit provisions stated in the previous paragraphs of this section are current provisions and apply to active plan participants. Vested, terminated employees who are entitled to benefits but are not yet receiving them are bound by the provisions in effect at the time they last terminated public service.

PERA issues a publicly available financial report that includes financial statements and required supplementary information for the Public Employees Retirement Fund. That report may be obtained on the internet at www.mnpera.org; by writing to PERA at 60 Empire Drive, Suite 200, Saint Paul, Minnesota 55103-2088; or by calling 651-296-7460 or 1-800-652-9026.

B. Funding Policy

Pension benefits are funded from member and employer contributions and income from the investment of fund assets. Minn. Stat. ch. 353 sets the rates for employer and employee contributions. These statutes are established and amended by the State Legislature. The Human Services makes annual contributions to the pension plans equal to the amount required by state statutes. Public Employees Retirement Fund

4. Pension Plans

B. Funding Policy (Continued)

Basic Plan members and Coordinated Plan members are required to contribute 9.10 and 5.75 percent, respectively, of their annual covered salary in 2007. Contribution rates in the Coordinated Plan increased in 2008 to 6.00 percent. The Human Services is required to contribute the following percentages of annual covered payroll in 2007 and 2008:

	2007	2008
Public Employees Retirement Fund		
Basic Plan members	11.78%	11.78%
Coordinated Plan members	6.25	6.50

The Human Services' contributions for the years ending December 31, 2007, 2006, and 2005, for the Public Employees Retirement Fund were:

2007	2006	2005
$ 222,354	$ 218,324	$ 197,630

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

5. Risk Management

Lincoln, Lyon, & Murray Human Services is exposed to various risks of loss related to torts; theft of, damage to, or destruction of assets; errors or omissions; injuries to employees; or natural disasters. The Human Services has entered into a joint powers agreement with Minnesota counties to form the Minnesota Counties Insurance Trust (MCIT). For all other risk, the Human Services carries commercial insurance. There were no significant reductions in insurance from the prior year. The amount of settlements did not exceed insurance coverage for each of the past three fiscal years.

The Workers' Compensation Division of MCIT is self-sustaining based on the contributions charged, so that total contributions plus compounded earnings on these contributions will equal the amount needed to satisfy claims liabilities and other expenses.

5. Risk Management (Continued)

MCIT participates in the Workers' Compensation Reinsurance Association with coverage at $400,000 per claim in 2007 and $410,000 per claim in 2008. Should the MCIT Workers' Compensation Division liabilities exceed assets, MCIT may assess the Human Services in a method and amount to be determined by MCIT.

The Property and Casualty Division of MCIT is self-sustaining, and the Human Services pays an annual premium to cover current and future losses. MCIT carries reinsurance for its property lines to protect against catastrophic losses. Should the MCIT Property and Casualty Division liabilities exceed assets, MCIT may assess the Human Services in a method and amount to be determined by MCIT.

6. Summary of Significant Contingencies and Other Items

A. Contingent Liabilities

Amounts received or receivable from grant agencies are subject to audit and adjustment by grantor agencies, principally the federal government. Any disallowed claims, including amounts already collected, may constitute a liability of the applicable funds. The amount, if any, of the expenditures that may be disallowed by the grantor cannot be determined at this time, although Lincoln, Lyon, & Murray Human Services expects such amounts, if any, to be immaterial.

Lincoln, Lyon, & Murray Human Services is a defendant in various lawsuits. Although the outcome of these lawsuits is not presently determinable, in the opinion of the Human Services' attorney, the resolution of these matters will not have a material adverse effect on the financial condition of the government.

B. Joint Venture

Southwestern Minnesota Adult Mental Health Consortium Board

In November 1997, Lincoln, Lyon, & Murray Human Services entered into a joint powers agreement with several counties creating and operating the Southwestern Minnesota Adult Mental Health Consortium Board under the authority of Minn. Stat. § 471.59. The Consortium Board is headquartered in Windom, Minnesota, where Cottonwood County acts as fiscal host.

6. Summary of Significant Contingencies and Other Items

B. Joint Venture

Southwestern Minnesota Adult Mental Health Consortium Board (Continued)

The Consortium Board shall take actions and enter into such agreements as may be necessary to plan and develop within the Consortium Board's geographic jurisdiction a system of care that will serve the needs of adults with serious and persistent mental illness. The governing board is composed of one board member from each of the participating counties. Financing is provided by state proceeds or appropriations for the development of the system of care.

The following is a summary of the Consortium Board's annual financial report for the year ended December 31, 2005 (the latest information available):

Total assets	$ 1,148,132
Total liabilities	497,546
Total net assets	650,586
Total revenues	1,960,287
Total expenditures	1,671,076
Net change in net assets	289,211

The Consortium Board reported no long-term obligations at December 31, 2005.

A complete financial report of the Southwestern Minnesota Adult Mental Health Consortium Board can be obtained at Cottonwood County Family Services Agency, Windom, Minnesota 56101.

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SUPPLEMENTARY INFORMATION

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LINCOLN, LYON, & MURRAY HUMAN SERVICES
MARSHALL, MINNESOTA

Statement 1

STATEMENT OF CHANGES IN ASSETS AND LIABILITIES
AGENCY FUND
FOR THE YEAR ENDED DECEMBER 31, 2007

	Balance January 1	Additions	Deductions	Balance December 31
COLLABORATIVE				
Assets				
Cash and pooled investments	$ 58,677	$ 66,715	$ 102,412	$ 22,980
Liabilities				
Due to other governments	$ 58,677	$ 66,715	$ 102,412	$ 22,980

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SUPPORTING SCHEDULE

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LINCOLN, LYON, & MURRAY HUMAN SERVICES
MARSHALL, MINNESOTA

Schedule 1

SCHEDULE OF INTERGOVERNMENTAL REVENUE
FOR THE YEAR ENDED DECEMBER 31, 2007

Shared Revenue		
Payments from participating counties	**$**	**4,349,161**
Reimbursement for Services		
State		
Minnesota Department of Human Services	**$**	**2,773,327**
Payments		
Local		
McKnight	**$**	**11,624**
Grants		
State		
Minnesota Department of Human Services	**$**	**2,208,189**
Federal		
Department of		
Agriculture	$	8,900
Health and Human Services		722,271
Total Federal	**$**	**731,171**
Total State and Federal Grants	**$**	**2,939,360**
Total Intergovernmental Revenue	**$**	**10,073,472**

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Management and Compliance Section

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Schedule 2

SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED DECEMBER 31, 2007

I. SUMMARY OF AUDITOR'S RESULTS

A. Our report expresses an unqualified opinion on the basic financial statements of Lincoln, Lyon, & Murray Human Services.

B. Significant deficiencies in internal control were disclosed by the audit of financial statements of Lincoln, Lyon, & Murray Human Services and are reported in the "Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards*." We consider some of the significant deficiencies to be material weaknesses.

C. No instances of noncompliance material to the financial statements of Lincoln, Lyon, & Murray Human Services were disclosed during the audit.

D. No matters involving internal control over compliance relating to the audit of the major federal award programs were reported in the "Report on Compliance with Requirements Applicable to Each Major Program and Internal Control Over Compliance in Accordance with OMB Circular A-133."

E. The Auditor's Report on Compliance for the major federal award programs for Lincoln, Lyon, & Murray Human Services expresses an unqualified opinion.

F. No findings were disclosed that are required to be reported in accordance with Section 510(a) of OMB Circular A-133.

G. The major programs are:

Foster Care - Title IV-E	CFDA #93.658
Social Services Block Grant Title XX	CFDA #93.667

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

I. Lincoln, Lyon, & Murray Human Services was determined not to be a low-risk auditee.

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

INTERNAL CONTROL

PREVIOUSLY REPORTED ITEMS NOT RESOLVED

06-1 Internal Accounting Controls - Segregation of Duties

Due to the limited number of office personnel within Lincoln, Lyon, & Murray Human Services, proper segregation of the accounting functions necessary to ensure adequate internal accounting control is not always possible. Although this is not unusual in entities of this size, management should constantly be aware of this condition and realize that the concentration of duties and responsibilities in a limited number of individuals is not desirable from an internal control point of view.

Lincoln, Lyon, & Murray Human Services does not segregate the duties of cash receipting and disbursing from one accounting technician. Also, the same person has the ability to make journal entries and maintain the general ledger.

One basic objective of internal control is to provide for segregation of incompatible duties. In other words, responsibilities should be separated among employees so that a single employee is not able to authorize a transaction, record the transaction in accounts, and be responsible for custody of the asset resulting from the transaction.

We recommend that the Human Services' management segregate duties within the accounting functions as much as possible by limiting access to accounting programs commensurate to the employees' duties and job responsibilities. If it is not possible to segregate duties, management should be aware of the lack of segregation of duties and implement oversight procedures to ensure the integrity and reliability of the financial information in the accounting system.

Client's Response:

LLMHS will further review duties within the department, primarily in regards to the technician who is receipting, disbursing, making journal entries, and maintaining the general ledger. We will further make changes that segregate duties or provide management oversight of the process.

06-4 Preparation of Financial Statements

The Human Services is required to prepare financial statements in accordance with generally accepted accounting principles (GAAP). The preparation of the financial statements is the responsibility of the Human Services' management. Financial statement preparation in accordance with GAAP requires internal controls over recording, processing, and summarizing accounting data (maintaining internal books and records) and preparing and reporting appropriate government-wide and fund financial statements, including the related notes to the financial statements.

As is the case with many small and medium-sized entities, the Human Services has relied on its independent external auditors to assist in the preparation of the basic financial statements, including notes to the financial statements, as part of its external financial reporting process. Accordingly, the Human Services' ability to prepare financial statements in accordance with GAAP is based, at least in part, on its reliance on its external auditors, who cannot by definition be considered part of the government's internal control. This condition was caused by the Human Services' decision that it is more cost-effective to have its auditors prepare its annual basic financial statements than to incur the time and expense of obtaining the necessary training and expertise required to prepare the financial statements internally. As a result of this condition, the Human Services lacks internal controls over the preparation of financial statements in accordance with GAAP.

The Human Services' accounting system has been upgraded to accommodate the modified accrual and full accrual bases of accounting in separate general ledger systems to allow for the preparation of the annual financial statements in accordance with generally accepted accounting principles for governments. During our audit, we noted several deficiencies that prevented the accounting system from providing accurate modified and full accrual financial statements. These deficiencies resulted in additional audit time because significant audit adjustments were required to correct the financial statements prepared by the Human Services.

Although Lincoln, Lyon, & Murray Human Services has identified and has been training individuals to obtain the expertise to improve its preparation of financial statements, we recommend the Human Services continue to obtain the training and expertise to internally prepare its annual financial statements in accordance with GAAP, including preparing and reporting appropriate government-wide and fund financial statements, including the related notes to the financial statements. Also, this process should be monitored by a knowledgeable person to ensure that the accounts are correctly summarized for financial statement purposes. As part of the financial statement preparation, summary schedules and worksheets should be prepared by the Human Services' staff to document the various accrual adjusting journal entries and to demonstrate how the accounts in the financial records are classified or summarized for the annual financial statements. When the financial statements are completed by the accounting system, the Human Services' staff should review the statements to ensure that reported amounts can be traced back to the prepared supporting schedules and worksheets.

Client's Response:

LLMHS will obtain further training in order to improve its preparation of financial statements and related documents. Our goal is to eventually prepare financial statements including related notes. Staff will be trained on the use of accrual codes and how to properly mark receivables and payables. Additional review will be done of the chart of accounts and mapping. LLMHS will also investigate the implementation of a capital assets program on IFS.

06-6 Accounting Policies and Procedures Manual

The Human Services does not have a current and comprehensive accounting policies and procedures manual. All governments should document their accounting policies and procedures. Although other methods might suffice, this documentation is traditionally in the form of an accounting policies and procedures manual. This manual should document the accounting policies and procedures which make up the Human Services' internal control system.

An accounting policies and procedures manual will enhance employees' understanding of their role and function in the internal control system, establish responsibilities, provide guidance for employees, improve efficiency and consistency of transaction processing, and improve compliance with established policies. It can also help to prevent deterioration of key elements in the Human Services' internal control system and can help to avoid circumvention of the Human Services' policies.

We recommend the Human Services establish an accounting policies and procedures manual. The accounting policies and procedures manual should be prepared by appropriate levels of management and be approved by the Human Services' Board to emphasize its importance and authority. The documentation should describe procedures as they are intended to be performed, indicate which employees are to perform which procedures, and explain the design and purpose of control-related procedures to increase employee understanding and support for controls.

Client's Response:

LLMHS will establish an accounting and policy and procedure manual that provides documentation of procedures, employees roles and responsibilities, and provide the purpose of control-related procedures to increase employee understanding and support of controls. Once prepared, the County Board will review and approve.

06-8 Computer Risk Management

The Human Services has internal controls in place for its computer systems. However, the Human Services has not developed a formal plan to identify and manage risks associated with its computer systems or tested its disaster recovery plan.

Risk management begins with a risk assessment of the computer systems to identify those risks that could negatively influence computer operations. Internal controls should be implemented to reduce the identified risks. Those controls should be documented in a well-maintained policies and procedures manual, which should be communicated to the Human Services' staff. Staff adherence to these policies and procedures should be monitored. Because computer systems are ever-changing, the Human Services should include in its plan periodic reassessment of risk to ensure existing internal controls are still effective.

We recommend the Human Services' Board develop a plan to ensure that internal controls are in place to reduce the risk associated with the Human Services' computer systems. These controls are necessary to maintain proper controls over financial reporting. We also recommend the Human Services update and test its disaster recovery plan.

Client's Response:

LLMHS has the most current virus protections and thorough backup procedures and protection. The system is backed every night, with off sight storage of backup tapes. We are confident that the backup is reliable as we have utilized them occasionally during the last year to restore files. LLMHS will develop a disaster recovery plan which will include written documentation and testing.

06-11 Audit Adjustments

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. One control deficiency that typically is considered significant is identification by the auditor of a material misstatement in the financial statements not initially identified by the entity's internal controls. During our audit, we proposed numerous adjustments that resulted in significant changes to the Human Services' financial statements. The adjustments resulted from: management not sufficiently reviewing preliminary financial data relating to accruals; controls over calculating the proper amount of receivables and payables did not detect errors, which resulted in the client understating receivables by $308,017 and understating payables by $325,105; errors made in recording transactions and with mapping of various account codes; and accounting staff not keeping current on accounting and financial reporting requirements. The inability to detect a material misstatement in the financial statements increases the likelihood that the financial statements could be not fairly presented.

We recommend that the Human Services review internal controls currently in place, then design and implement procedures to improve internal control over financial reporting to detect misstatements in the financial statements. The updated controls should include review of the balances and supporting documentation by a qualified individual to identify potential misstatements.

Client's Response:

As related to 06-4, LLMHS will work to reduce adjustments proposed by the auditors. LLMHS will obtain needed training to prepare the financial statements and related notes. LLMHS has corrected the 2007 MA recovery issues as of April 23, 2008. In addition, MA recoveries are current through April 30, 2008. As stated earlier, LLMHS will be training staff and will move toward using accrual codes rather than report codes. As part of the process, supervision will review all transactions during the first 60 days of the year and will sign off on the Transaction Listing by Accrual Code Report prior to the audit. Additional review of mapping will also be done. Hopefully, by improving in the area LLMHS can return to being categorized as "low risk" after two consecutive years.

ITEMS ARISING THIS YEAR

07-1 Controls Over Medical Assistance Recoveries

The Human Services does not review or monitor the status of medical assistance (MA) recoveries or the subsequent payment to the Minnesota Department of Human Services (DHS) for the state and federal share of such collections.

At the time of our audit, it was noted the Human Services had received a large amount of MA recovery collections during 2007 but that there were few payments to the DHS for the state and federal shares of collections. A liability had not been recorded by the Human Services for the amount of funds on hand that were owed to the DHS.

In April 2008, the Human Services reported collections of MA recoveries for January through December 2007. The Human Services' staff determined the entity's liability at the end of December 2007 was $325,967.

We recommend that the Human Services implement internal controls to ensure collections of MA recoveries are reported to the DHS on a timely basis. We also recommend the process for collecting, reporting, and remitting MA recoveries be monitored by appropriate levels of the Human Services' staff and that MA recoveries are reconciled for financial reporting at the end of the year.

Client's Response:

As stated in 06-11, LLMHS has already corrected the issue with MA recoveries. Additional review of the MA invoice has already been implemented and so it is verified that recoveries have been processed. Invoices have been received from DHS, and payments will be made to DHS within 90 days.

07-2 Payroll

No controls exist to verify the correct pay rates were in the payroll system for all employees, that pay rates were updated for authorized reasons, or that any payroll information changes were reviewed by other Human Services' personnel. These conditions represent a serious weakness to the Human Services' internal controls. Without improved controls, employees could be receiving incorrect pay or employees could be added or deleted from the system without being noticed.

We recommend that the Human Services' management implement oversight procedures to ensure any changes made to an employee's payroll information are correct, are made for authorized purposes, and are reviewed by someone other than the person making the change.

Client's Response:

LLMHS will add additional controls in the processing payroll so that there is segregation of duties and that more than one staff person reviews payroll changes and processing.

PREVIOUSLY REPORTED ITEMS RESOLVED

Budgeting Procedures (06-2)

Approval of the revenues and expenditures budget was not documented in the Board minutes. As a result, the detail of estimated revenue sources for the fund and the budgeted expenditures by fund, function, and department were not always clearly documented.

Resolution

The Human Services' Board adopted and recorded in its minutes the budget by major revenue source and estimated expenditures by function and department for its operational fund.

Antifraud Programs and Controls (06-3)

Responses of management and staff regarding the risks of fraud and how Lincoln, Lyon, & Murray Human Services addresses those risks indicated deficiencies in antifraud programs and controls.

Resolution

The Human Services improved internal communication regarding fraud and the importance of ethical behavior.

Access to the Computer Systems - Passwords (06-5)

Control over computer passwords needed to be strengthened. The Human Services used a minimum password length of only five characters and set no limitations on passwords such as requiring a number, not allowing adjacent characters, or not allowing multiple repeated strokes of the same key. Weak control over access to the computer systems increases the risk of access to the system by unauthorized individuals.

Resolution

Management strengthened access controls to the information system by requiring employee passwords be changed on a regular basis and using strong password systems which include longer and more randomized characters.

Capital Assets Policies and Procedures (06-7)

A capital assets policy should be adopted which defines the Human Services' accounting policies over capital assets, such as capitalization thresholds, useful lives, and depreciation methods.

The Human Services was carrying a significant amount of fully depreciated assets. Typically, a capital asset still in use should not be considered fully depreciated. For significant assets, the estimated useful lives assigned to capital assets should be reconsidered. At the time of redetermination, the estimated useful life of an asset includes both the years the asset has been in service and the estimated number of years of service remaining.

Resolution

While the Human Services did not develop a new comprehensive capital assets policy, an approved capital assets policy was found to be part of the Human Services' Governmental Accounting Standards Board (GASB) Statement 34 policies as revised in 2006, and a procedure was created to reassess the useful lives of capital assets before the assets are fully depreciated.

Adding New Vendors to the Accounting System (06-9)

The Human Services did not have any procedures for determining if new vendors have been added to the accounts payable system or if the new vendors added were legitimate vendors.

Resolution

The ability to set up new vendors on the accounts payable system is limited to those individuals with a logical need for this function. In addition, periodically, the Director of Business Management reviews the new vendors added to the system and documents her review by signing off on a printed report from the accounting system.

Accounting System Journal Entries (06-10)

The ability to make journal entries on the accounting system is a powerful function because it allows employees to make changes to the system. The journal entries made to the accounting system were not reviewed or approved by anyone.

Resolution

A procedure was established to require review approval of journal entries by the Director of Business Management.

Quarterly Fiscal Reports (06-12)

When testing a sample of two fiscal reports for the third quarter of 2006, we noted that the amounts reported did not agree with the general ledger for either submission. The Human Services under-reported various expenditures on the Social Services Expenditure and Grant Reconciliation (SEAGR) report for a net difference of $29,836. Thirty of the 65 accounts reported on the SEAGR did not tie to what was found in the corresponding BRASS [Budgeting, Reporting, and Accounting for Social Services] codes in the general ledger. The Income Maintenance Expenditures Report for the third quarter also had differences.

Resolution

The amounts submitted on fiscal reports to the DHS were complete and accurate for the quarter tested for 2007.

III. FINDINGS AND QUESTIONED COSTS FOR FEDERAL AWARD PROGRAMS

None.

IV. OTHER FINDINGS AND RECOMMENDATIONS

A. <u>MINNESOTA LEGAL COMPLIANCE</u>

<u>PREVIOUSLY REPORTED ITEM NOT RESOLVED</u>

06-13 <u>Notice Required to Collect Collateral Upon Default by Bank</u>

The depository pledge agreements between the Human Services and Wells Fargo and Bank of the West state that the Human Services is required to give notice of a failure, insolvency, or breach to the bank and wait at least three business days after the notice before the Human Services can collect the collateral from the custodian so the bank has time to cure the default.

Minn. Stat. § 118A.03, subd. 4, states, "The written assignment shall recite that, upon default, the financial institution shall release to the government entity on demand, free of exchange or any other charges, the collateral pledged."

We recommend that the Human Services' fiscal agent (Lyon County) review this security agreement to ensure that it is consistent with the default language of Minn. Stat. § 118A.03, subd. 4, and that the required language is included.

Client's Response:

Per the fiscal agent (Lyon County), this should be on file shortly.

ITEM ARISING THIS YEAR

07-3 Collateral Pledged to Secure Deposits

Federal deposit insurance coverage (FDIC) and collateral pledged at December 31, 2007, was insufficient for the amount on deposit at Bremer Bank by $485,092.

Minn. Stat. § 118A.03, subd. 3, provides that, to the extent funds deposited are in excess of available federal deposit insurance, "The total amount of the collateral computed at its market value 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."

We recommend that the Human Services' fiscal agent monitor the deposits in designated depositories to ensure that the Human Services' funds are fully protected as required by Minn. Stat. § 118A.03 at all times.

Client's Response:

Fiscal agent will monitor Bremer's collateral pledge sheet more closely.

PREVIOUSLY REPORTED ITEMS RESOLVED

Collateral Substitution - Depository Pledge Agreement (06-14)

The depository pledge agreement between the Human Services and Bank of the West allowed the bank to substitute eligible securities for any of the pledged collateral by providing the custodian with a substitution notice signed by an authorized representative of the bank before the bank gave any notice to the governmental entity and received approval.

Resolution

The depository pledge agreement was updated to indicate the depositor would receive written notice and have to confirm collateral substitution or withdrawal. Lincoln, Lyon, & Murray Human Services is in compliance with Minn. Stat. § 118A.03, subd. 5.

Pledged Collateral Rating (06-15)

Information was not on file with the Human Services' fiscal agent relating to the rating of some of the local government obligations pledged to the Human Services by Bremer Bank.

Resolution

The fiscal agent had the ratings of all local government obligations pledged on file, so the Human Services is in compliance with Minn. Stat. § 118A.03, subd. 2.

Depository Pledge Agreement (06-16)

The Human Services did not have a depository pledge agreement for collateral pledged by Bremer Bank.

Resolution

A depository pledge agreement is on file with the fiscal agent. The Human Services is in compliance with Minn. Stat. § 118A.03.

Travel Claims/Disbursements (06-17)

While reviewing travel claims, we noted that one hotel was paid twice for the same stay, and an unitemized credit card receipt was used to support a hotel reimbursement.

Resolution

Any reimbursements requested without proper receipts must be approved before the claim is paid. The Human Services complies with the provisions of Minn. Stat. § 471.38.

B. <u>MANAGEMENT PRACTICES</u>

<u>ITEM ARISING THIS YEAR</u>

07-4 <u>Outdated Policies</u>

The Human Services has approved accounting policies that address investments and GASB Statement 34 compliance-related issues. Those policies are outdated and need revision. Outdated policies that assign responsibility to untrained personnel may not prove to be nearly as effective as intended in times of actual need.

The investment policy was last updated in 1999. The Human Services' fiscal agent was not aware the policy even existed, and the policy does not address disclosures required by GASB Statement 40.

The GASB Statement 34 compliance-related policies were last revised in February 2006. These policies address, in part, capital assets, the budget, and the determination of the current share of the compensated absences liability. The capital assets policy does not address: policies and procedures to identify capital asset additions and deletions, the redetermination of useful lives, or the performance of a periodic physical inventory. The budget policy does not address: budgeted revenues, the adoption and recording of the budget in the Human Services' Board minutes by major revenue source and estimated expenditures by function and department, or the procedures for monitoring the budget. The policy to determine the current share of compensated absences states a five-year trend analysis will be used to determine the amount of liability due in one year. The Human Services used a three-year trend analysis for reporting the liability for year-end 2007.

We recommend the Human Services update accounting policies on an annual basis or as needed and sufficiently train its staff so policies and procedures in place are followed.

Client's Response:

We will update the GASB #34 policies and annually will review them to ensure they address current practice. The fiscal agent and the Director of Business Management have met and reviewed proposed changes in the Investment Policy. The Investment Policy is scheduled to be reviewed and approved at May 2008 Board. In addition, staff will be trained on related policies and procedures.

C. OTHER ITEM FOR CONSIDERATION

Other Postemployment Benefits (OPEB)

GASB issued Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions,* which governs employer accounting and financial reporting for OPEB. This standard, similar to what GASB Statement 27 did for government employee pension benefits and plans, provides the accounting and reporting standards for the various other postemployment benefits many local governments offer to their employees. OPEB can include many different benefits offered to retirees such as health, dental, life, and long-term care insurance coverage.

If retirees are included in an insurance plan and pay a rate similar to that paid for younger active employees, this implicit subsidy is considered OPEB. In fact, local governments may be required to continue medical insurance coverage pursuant to Minn. Stat. § 471.61, subd. 2b. This benefit is common when accumulated sick leave is used to pay for retiree medical insurance. Under the new GASB statement, accounting for OPEB is now similar to the accounting used by governments for pension plans.

This year the legislature enacted a new law, Minn. Stat. § 471.6175, intended to help local governments address their OPEB liability in at least three important ways:

- it allows governments to create both irrevocable and revocable OPEB trusts;
- it authorizes the use of a different list of permissible investments for both irrevocable and revocable OPEB trusts; and
- it also permits governments to invest OPEB trust assets with the State Board of Investment, (SBI) bank trust departments, and certain insurance companies.

Some of the issues that the Human Services' Board will need to address in order to comply with the statement are:

- determine if employees are provided OPEB;
- if OPEB are being provided, the Human Services Board will have to determine whether it will advance fund the benefits or pay for them on a pay-as-you-go basis;
- if OPEB are being provided, and the Human Services Board determines that the establishment of a trust is desirable in order to fund the OPEB, the Human Services Board will have to comply with the new legislation enacted authorizing the creation of an OPEB trust and establishing an applicable investment standard;
- if an OPEB trust will be established, the Human Services will have to decide whether to establish an irrevocable or a revocable trust, and report that trust appropriately in the financial statements; and
- in order to determine annual costs and liabilities that need to be recognized, the Human Services Board will have to decide whether to hire an actuary.

GASB Statement 45 would be applicable to Lincoln, Lyon, & Murray Human Services for the year ended December 31, 2008.

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REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*

Board Members
Lincoln, Lyon, & Murray Human Services

We have audited the financial statements of the governmental activities, the major fund, and the remaining fund information of Lincoln, Lyon, & Murray Human Services as of and for the year ended December 31, 2007, and have issued our report thereon dated June 26, 2008. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards,* issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered Lincoln, Lyon, & Murray Human Services' 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 Human Services' internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Human Services' internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph of this section and would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed below, we identified certain deficiencies in internal control over financial reporting that we consider to be significant deficiencies.

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 on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the Human Services' ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the Human Services' financial statements that is more than inconsequential will not be prevented or detected by the Human Services' internal control. We considered the deficiencies described in the accompanying Schedule of Findings and Questioned Costs as items 06-1, 06-4, 06-6, 06-8, 06-11, 07-1, and 07-2 to be significant deficiencies in internal control over financial reporting.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by Lincoln, Lyon, & Murray Human Services' internal control.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, of the significant deficiencies described above, we consider items 06-4, 06-11, and 07-1 to be material weaknesses.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Lincoln, Lyon, & Murray Human Services' 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 and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards.*

Minnesota Legal Compliance

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 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 Local Government* contains six categories of compliance to be tested: contracting and bidding, deposits and investments, conflicts of interest, public indebtedness, claims and disbursements, and miscellaneous provisions. Our study included all of the listed categories.

The results of our tests indicate that, for the items tested, the Human Services complied with the material terms and conditions of applicable legal provisions, except as described in the Schedule of Findings and Questioned Costs as items 06-13 and 07-3.

Also included in the Schedule of Findings and Questioned Costs is a management practices comment and an other item for consideration. We believe these recommendations and information to be of benefit to the Human Services, and they are reported for that purpose.

Lincoln, Lyon, & Murray Human Services' written responses to the significant deficiencies, material weaknesses, legal compliance, and management practice findings identified in our audit have been included in the Schedule of Findings and Questioned Costs. We did not audit the Human Services' responses and, accordingly, we express no opinion on them.

This report is intended solely for the information and use of the Human Services' Board, management, others within the Human Services, and federal awarding agencies and pass-through entities and is not intended to be, and should not be, used by anyone other than those specified parties.

/s/Rebecca Otto	*/s/Greg Hierlinger*
REBECCA OTTO STATE AUDITOR	GREG HIERLINGER, CPA DEPUTY STATE AUDITOR

June 26, 2008

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REPORT ON COMPLIANCE WITH REQUIREMENTS APPLICABLE TO EACH MAJOR PROGRAM AND INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133

Board Members
Lincoln, Lyon, & Murray Human Services

Compliance

We have audited the compliance of Lincoln, Lyon, & Murray Human Services with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) *Circular A-133 Compliance Supplement* that are applicable to each of its major federal programs for the year ended December 31, 2007. Lincoln, Lyon, & Murray Human Services' major federal programs are identified in the Summary of Auditor's Results section of the accompanying Schedule of Findings and Questioned Costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs is the responsibility of the Human Services' management. Our responsibility is to express an opinion on the Human Services' compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards,* issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations.* Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about Lincoln, Lyon, & Murray Human Services' compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on the Human Services' compliance with those requirements.

In our opinion, Lincoln, Lyon, & Murray Human Services complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended December 31, 2007.

Internal Control Over Compliance

The management of Lincoln, Lyon, & Murray Human Services is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered the Human Services' 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, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the Human Services' internal control over compliance.

A control deficiency in internal control over compliance 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 noncompliance with a type of compliance requirement of a federal program on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the Human Services' ability to administer a federal program such that there is more than a remote likelihood that noncompliance with a type of compliance requirement of a federal program that is more than inconsequential will not be prevented or detected by the Human Services' internal control.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that material noncompliance with a type of compliance requirement of a federal program will not be prevented or detected by the Human Services' internal control.

Our consideration of the internal control over compliance was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses, as defined above.

Schedule of Expenditures of Federal Awards

We have audited the financial statements of the governmental activities, the major fund, and the remaining fund information of Lincoln, Lyon, & Murray Human Services as of and for the year ended December 31, 2007, which collectively comprise the Human Services' basic financial statements, and have issued our report thereon dated June 26, 2008. Our audit was performed for the purpose of forming opinions on the financial statements that collectively comprise the

Human Services' basic financial statements. The accompanying Schedule of Expenditures of Federal Awards is presented for purposes of additional analysis as required by OMB Circular A-133 and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

This report is intended solely for the information and use of the Human Services' Board, management, others within the Human Services, and federal awarding agencies and pass-through entities and is not intended to be, and should not be, used by anyone other than those specified parties.

/s/Rebecca Otto	*/s/Greg Hierlinger*
REBECCA OTTO STATE AUDITOR	GREG HIERLINGER, CPA DEPUTY STATE AUDITOR

June 26, 2008

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LINCOLN, LYON, & MURRAY HUMAN SERVICES
MARSHALL, MINNESOTA

Schedule 3

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED DECEMBER 31, 2007

Federal Grantor Pass-Through Agency Grant Program Title	Federal CFDA Number	Expenditures
U.S. Department of Agriculture		
Passed Through Minnesota Department of Human Services		
State Administrative Matching Grants for Food Stamp Program	10.561	**$ 8,900**
U.S. Department of Health and Human Services		
Passed Through Minnesota Department of Human Services		
Promoting Safe and Stable Families	93.556	$ 64,687
Temporary Assistance for Needy Families (TANF)	93.558	164,668
Child Care and Development Block Grant	93.575	10,312
Child Care Mandatory Matching Funds	93.596	12,732
Child Welfare Services - State Grants	93.645	37,845
Foster Care - Title IV-E	93.658	109,643
Social Services Block Grant - Title XX	93.667	284,146
Chafee Foster Care Independence Program	93.674	32,652
Block Grants for Community Mental Health Services	93.958	5,586
Total U.S. Department of Health and Human Services		**$ 722,271**
Total Federal Awards		**$ 731,171**

The notes to the Schedule of Expenditures of Federal Awards are an integral part of this schedule.

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LINCOLN, LYON, & MURRAY HUMAN SERVICES
MARSHALL, MINNESOTA

NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED DECEMBER 31, 2007

1. Reporting Entity

   The Schedule of Expenditures of Federal Awards presents the activities of federal award programs expended by Lincoln, Lyon, & Murray Human Services. The Human Services' reporting entity is defined in Note 1 to the financial statements.

2. Basis of Presentation

   The accounting records for grant programs are maintained on the modified accrual basis of accounting. Under the modified accrual basis, revenues are recorded when susceptible to accrual--when both measurable and available. Available means collectible within the current period or soon enough thereafter to be used to pay liabilities of the current period. Lincoln, Lyon, & Murray Human Services considers all revenues to be available if they are collected within 60 days of the current period. Expenditures are recorded when the liability is incurred.

   The information in the schedule is presented in accordance with the requirements of Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations.*

3. Passed Through to Subrecipients

   During 2007, Lincoln, Lyon, & Murray Human Services did not pass any federal money to subrecipients.

4. Pass-Through Grant Numbers

   Pass-through grant numbers were not assigned by the pass-through agencies.