

STATE OF MINNESOTA

Office of the State Auditor



Rebecca Otto
State Auditor

DULUTH AIRPORT AUTHORITY
(A COMPONENT UNIT OF THE
CITY OF DULUTH, MINNESOTA)

FOR THE YEARS ENDED DECEMBER 31, 2014 AND 2013

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 150 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 700 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.

Office of the State Auditor
525 Park Street, Suite 500
Saint Paul, Minnesota 55103
(651) 296-2551
state.auditor@osa.state.mn.us
www.auditor.state.mn.us

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**DULUTH AIRPORT AUTHORITY
(A COMPONENT UNIT OF THE
CITY OF DULUTH, MINNESOTA)**

For the Years Ended December 31, 2014 and 2013



**Audit Practice Division
Office of the State Auditor
State of Minnesota**

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**DULUTH AIRPORT AUTHORITY
DULUTH, MINNESOTA**

TABLE OF CONTENTS

	<u>Exhibit</u>	<u>Page</u>
Introductory Section		
Organization		1
Financial Section		
Independent Auditor's Report		2
Management's Discussion and Analysis		5
Basic Financial Statements		
Comparative Statement of Net Position	1	13
Comparative Statement of Revenues, Expenses, and Changes in Net Position	2	15
Comparative Statement of Cash Flows	3	16
Notes to the Financial Statements		18
Required Supplementary Information		
Schedule of Funding Progress - Other Postemployment Benefits	A-1	37
Notes to the Schedule of Funding Progress - Other Postemployment Benefits		38
Supplementary Information		
Comparative Statement of Operating Revenues	B-1	39
Schedule of Expenditures of Federal Awards	C-1	40
Notes to the Schedule of Expenditures of Federal Awards		41
Schedule of Passenger Facility Charges Collected and Expended	C-2	42
Management and Compliance Section		
Schedule of Findings and Questioned Costs		43
Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with <i>Government</i> <i>Auditing Standards</i>		46
Report on Compliance for Each Major Federal Program and for the Passenger Facility Charge Program and Report on Internal Control Over Compliance		49

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**DULUTH AIRPORT AUTHORITY
DULUTH, MINNESOTA**

ORGANIZATION
DECEMBER 31, 2014

	<u>Term Ending</u>
Directors	
Kenneth Butler	July 1, 2015
Michael Lundstrom	July 1, 2015
Patrick Mullen	July 1, 2015
Heather Rand	July 1, 2016
Sue Ross	July 1, 2017
Richard Stewart	July 1, 2017
Kenneth Stromquist	July 1, 2016
Executive Director	
Thomas Werner	
Officers	
President	
Michael Lundstrom	
Vice President	
Kenneth Stromquist	
Secretary	
Patrick Mullen	

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REBECCA OTTO
STATE AUDITOR

STATE OF MINNESOTA OFFICE OF THE STATE AUDITOR

SUITE 500
525 PARK STREET
SAINT PAUL, MN 55103-2139

(651) 296-2551 (Voice)
(651) 296-4755 (Fax)
state.auditor@state.mn.us (E-mail)
1-800-627-3529 (Relay Service)

INDEPENDENT AUDITOR'S REPORT

Mayor and City Council
City of Duluth

Board of Directors
Duluth Airport Authority
Duluth, Minnesota

Report on the Financial Statements

We have audited the accompanying financial statements of the Duluth Airport Authority, a component unit of the City of Duluth, Minnesota, as of and for the years ended December 31, 2014 and 2013, and the related notes to the financial statements, which collectively comprise the Authority's basic financial statements, as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial

statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Authority's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Authority's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Duluth Airport Authority as of December 31, 2014 and 2013, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis and Required Supplementary Information as listed in the table of contents be presented to supplement the basic financial statements. Such information, although not part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Supplementary Information

Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise the Duluth Airport Authority's basic financial statements. The supplementary information, listed in the table of contents, is presented for purposes of additional analysis and is not a required part of the basic financial statements.

The supplementary information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and

reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated, in all material respects, in relation to the basic financial statements as a whole.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated May 28, 2015, on our consideration of the Duluth Airport Authority's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on 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* in considering the Duluth Airport Authority's internal control over financial reporting and compliance.

Report on Schedule of Expenditures of Federal Awards Required by OMB Circular A-133

Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise the basic financial statements. The accompanying Schedule of Expenditures of Federal Awards (SEFA) 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 is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. The information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the SEFA is fairly stated in all material respects in relation to the basic financial statements as a whole.

/s/Rebecca Otto

REBECCA OTTO
STATE AUDITOR

May 28, 2015

/s/Greg Hierlinger

GREG HIERLINGER, CPA
DEPUTY STATE AUDITOR

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MANAGEMENT'S DISCUSSION AND ANALYSIS

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**DULUTH AIRPORT AUTHORITY
DULUTH, MINNESOTA**

**MANAGEMENT'S DISCUSSION AND ANALYSIS
DECEMBER 31, 2014
(Unaudited)**

Our discussion and analysis of the Duluth Airport Authority's (Authority) financial performance provides an overview of the Authority's financial activities for the fiscal year ended December 31, 2014. Please read it in conjunction with the financial statements.

FINANCIAL HIGHLIGHTS

- Operating expenses (before depreciation and amortization) increased \$138 thousand, or 3.4 percent, compared to fiscal year 2013, due to increased payroll and employee taxes and benefits as well as other adjustments.
- Operating revenues increased \$829.6 thousand, or 19.7 percent, primarily due to the rate increases on space as well as restaurant concessions and parking lot receipts.
- Nonoperating federal and state grant revenues decreased \$2,697 thousand, or 30.1 percent, from 2013; the decreases are due to the completion of the new terminal project. Total net position decreased \$1,201 thousand, or 1.1 percent, compared to fiscal year 2013.
- Total number of passengers including charters decreased by 3.2 thousand, or 1.0 percent, for a total of 313.8 thousand in 2014. The decrease was due to suspension of Allegiant flights to Mesa and Orlando.
- Total traffic count as recorded by the Federal Aviation Administration tower increased by 5.7 thousand, or 10.7 percent, to 59,461.
- Landing fee revenues for 2014 increased by \$41.5 thousand, or 16.2 percent.
- Passenger facility charge revenue decreased by \$14 thousand in 2014, or 2.3 percent, compared to 2013, which is attributed to the passenger count decrease from 2013.
- Customer facility charges collected in 2014 increased by \$12.7 thousand, or 5.1 percent, from 2013.

- Total parking lot sales increased by \$374 thousand, or 41.7 percent, for 2014.
- Total car rental concession sales decreased by \$9.8 thousand, or 2.2 percent, for 2014.
- The 2013/2014 State Maintenance and Operations Agreement, which became effective October 27, 2011, provided for \$168.6 thousand of state aid with amendments to increase to \$185.4 thousand for Duluth International and \$22.3 thousand for Sky Harbor.
- The Transportation Security Administration's agreement with the Authority, effective October 1, 2012, through September 30, 2015, reimbursed the Authority 16.5 hours per day for contracted law enforcement personnel, or approximately \$8 thousand per month.

OVERVIEW OF ANNUAL FINANCIAL REPORT

The Management's Discussion and Analysis (MD&A) serves as an introduction to the Duluth Airport Authority's financial statements. The MD&A represents management's examination and analysis of the Authority's financial condition and well-being. Summary financial statement data, key financial and operational indicators used in the Authority's strategic plan, budget, and other management tools were used for this analysis.

The financial statements report information about the Authority using full accrual accounting methods as utilized by similar business activities in the private sector.

The financial statements include a statement of net position; a statement of revenues, expenses, and changes in net position; a statement of cash flows; and notes to the financial statements. The statement of net position presents the financial position of the Authority on a full accrual historical cost basis. While the statement of net position provides information about the nature and amount of resources and obligations at year-end, the statement of revenues, expenses, and changes in net position presents the results of the business activities over the course of the fiscal year and information as to how the net position changed during the year. All changes in net position are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of the related cash flows. This statement also provides certain information about the Authority's recovery of its costs.

The statement of cash flows presents changes in cash and cash equivalents resulting from operational, financing, and investing activities. This statement presents cash receipts and cash disbursement information without consideration of the earnings event, when an obligation arises, or depreciation of capital assets.

The notes to the financial statements provide required disclosures and other information that are essential to a full understanding of material data provided in the statements. The notes present information about the Authority's accounting policies, significant account balances and activities, material risks, obligations, commitments, contingencies, and subsequent events, if any. The financial statements were prepared by the Authority's staff from the detailed books and records of the Authority. The financial statements were audited and adjusted during the independent external audit process.

SUMMARY OF ORGANIZATION AND BUSINESS

The Legislative Act of 1969, Chapter 577, as approved on May 22, 1969, authorized the organization of the Authority. The purpose of this act was to promote the public welfare and to serve the public interest, convenience and necessity, promote air navigation and transportation, national, state and local; and to these ends, to develop full potentials of aviation in the City of Duluth as an aviation center; and to provide for the most economical and effective use of aeronautical facilities and services in the City of Duluth; and to this end, the Authority shall cooperate with and assist the federal government and the Director of Aeronautics of this state, and shall seek to coordinate its aeronautic activities with these bodies. This Legislative Act established a Board of seven Directors appointed by the Mayor and conferred upon this Board the power and duty to administer, promote, control, direct, and manage and operate all airports owned. On October 9, 1985, the Bylaws were adopted (amended October 16, 1986, and September 16, 1997). These Bylaws established regular monthly meetings, a term for officers, and the appointment of an Executive Director.

The Duluth Airport Authority's vision is to be the region's center of aviation, supporting economic development by growing travel, cargo, and business services for our customers and communities. Our mission is, "We are committed to providing our customers with superior services in a safe, secure, professional environment."

The Duluth International Airport consists of two runways, which provide take-off and landing facilities for all types of commercial and general aviation aircraft, as well as military aircraft. The main runway 9-27 is 10,152 feet long by 150 feet wide and can handle the world's largest aircraft. The cross runway 3-21 is 5,699 feet long by 150 feet wide. The Duluth International Airport is located on 3,294 acres of land and encompasses approximately one-half of the old Duluth Air Force Base. The Authority also operates Sky Harbor Airport, which is both a sea plane base and a general aviation airport. The landside runway is 3,050 long by 75 feet wide. In the bay, there is also a 10,000-foot by 2,000-foot water runway.

Operating revenue for the Authority comes from a variety of sources including: car rental concessions, parking, space and land rentals, Fixed Base Operator (FBO) concessions, Transportation Security Agency reimbursement for law enforcement, maintenance and operations grant funds from the State of Minnesota, and landing fees. The Authority is self-sufficient and is not subsidized by the City of Duluth for operations or capital improvement costs.

FINANCIAL ANALYSIS

The following comparative condensed financial statements and other selected information serve as the key financial data and indicators for management, monitoring, and planning.

Condensed Statement of Net Position (000s)

	FY 2014	FY 2013	FY 2012
Current and other assets	\$ 10,102	\$ 13,853	\$ 16,311
Capital assets	115,673	110,891	64,904
Construction in progress	316	3,112	50,053
Total Assets	<u>\$ 126,091</u>	<u>\$ 127,856</u>	<u>\$ 131,268</u>
Current liabilities	\$ 5,328	\$ 5,248	\$ 10,843
Long-term liabilities	10,702	11,346	8,363
Total Liabilities	<u>\$ 16,030</u>	<u>\$ 16,594</u>	<u>\$ 19,206</u>
Net Position			
Net investment in capital assets	\$ 105,002	\$ 109,554	\$ 105,677
Unrestricted	5,059	1,708	6,385
Total Net Position	<u><u>\$ 110,061</u></u>	<u><u>\$ 111,262</u></u>	<u><u>\$ 112,062</u></u>

As the table illustrates, net position decreased by \$1,201 thousand to \$110 million in 2014. The decrease in net position was primarily due to significant changes to capital assets, other current assets, and construction in progress, with an overall decrease of \$1.8 million, as well as a decrease of \$564 thousand in liabilities.

Condensed Statement of Revenues, Expenses, and Changes in Net Position (000s)

	FY 2014		FY 2013	FY 2012
	Budget	Actual	Actual	Actual
Total operating revenues	\$ 4,251	\$ 5,043	\$ 4,213	\$ 4,076
Total operating expenses	(12,515)	(12,703)	(12,256)	(8,911)
Income (Loss)	\$ (8,264)	\$ (7,660)	\$ (8,043)	\$ (4,835)
Nonoperating revenues	620	673	659	659
Other revenues	6,491	6,308	9,927	29,280
Nonoperating expenses	(814)	(522)	(3,343)	(1,581)
Change in Net Position	<u><u>\$ (1,967)</u></u>	<u><u>\$ (1,201)</u></u>	<u><u>\$ (800)</u></u>	<u><u>\$ 23,523</u></u>

REVENUES

Operating revenues increased by \$829.6 thousand, or 19.7 percent, in 2014 relative to 2013. The operating revenue increase is due primarily to the rate and charges changes, which increased parking revenue by over \$374 thousand. An audit of the rental car agencies also provided for over \$100 thousand in additional revenues.

EXPENSES

Duluth Airport Authority's operating expenses increased by \$447.2 thousand to \$12,703 thousand in 2014, up from \$12,256 thousand in 2013. Depreciation changed significantly due to the addition of the parking structure as well as other adjustments. This change in depreciation accounted for \$289 thousand of the total increase. Personal services expenses increased by \$138 thousand, or 8.2 percent, while utilities expenses went down \$15.7 thousand and other services and charges went up \$10 thousand, or 0.6 percent compared to 2013.

BUDGETARY HIGHLIGHTS

The Duluth Airport Authority develops an annual operating budget which includes proposed expenses as well as proposed sources of revenue to pay for them. The Authority Board approves the operating budget, and it also receives final approval from the Duluth City Council. The Authority's operating budget is adjusted as needed when noticeable changes in business are known to affect the budget. Management and the Board of Directors are presented detailed monthly financial statements as well as an in-depth quarterly analysis in addition to annual analysis of key indicators and budgetary progress.

The airline industry remains competitive and fluid while adverse to risk. Though fuel prices have become much more attractive, airlines have seized the opportunity to strengthen their balance sheets, not passing the savings on to the passenger. In addition, an industry pilot shortage due to new regulations is making it increasingly difficult to attract new or existing air carriers to add flights to new destinations, as regional air carriers do not have the pilots to fly their existing fleets. This issue is being monitored and considered as the establishment of additional air service to our market is continually being pursued. Positive for Duluth, three daily flights from United Airlines between Duluth and its Chicago O'Hare hub have been successfully in place for more than five years. Finally, Monaco Air continues to have productive and successful operations as the FBO offering quality service with a well-respected reputation. Monaco's services and operations have led to more activity for international, corporate, charter, and general aviation users of the Duluth Airport as well as increased revenues for the Authority.

The Authority continued to make improvements to facilities and infrastructure and respond to new security directives. In 2014, the following projects or additions to projects reached completion and were transferred to capital asset records: (1) New Parking Structure and Wayfinding - \$7,269 thousand; (2) Apron Construction and Taxiway Pavement Maintenance - \$2,040 thousand; (3) Sky Walk - \$1,535 thousand; (4) Multi-Use Tractor, Broom and Plow - \$800 thousand; (5) Terminal Building Construction and Equipment - \$521.5 thousand;

(6) Miscellaneous Tower and Hangar Repairs - \$494 thousand; (7) Parking Lot - \$463 thousand; (8) Sky Harbor Environmental Assessment - \$235 thousand; (8) Miscellaneous Equipment of \$36 thousand, Wildlife Assessment for \$31 thousand, Sky Harbor Airport Layout Plan for \$13 thousand and baggage carousel lighting for \$8 thousand.

Ground breaking began in 2009 for the new \$78 million Passenger Terminal Building and supporting infrastructure. During 2010, Phase I, consisting of site work, new roadways, infrastructure, and new parking lots, was completed. Phase II, involving New Terminal Building foundation, structure, and enclosure, was completed in early 2013. Demolition of the former terminal began on February 1, 2013, with apron completion in the fall of 2013. Federal, state, and local airport dollars have funded the project. The parking structure ground breaking began in early 2014 and was completed in the fall of 2014.

The union contract between the Authority and AFSCME Local 66 was negotiated in 2013, effective 2014 through December 31, 2016.

**Capital Assets
(000s)**

	FY 2014	FY 2013	Dollar Change Increase (Decrease)	Total Percent (%) Change
Land	\$ 3,361	\$ 3,361	\$ -	0.00
Runways	84,213	82,172	2,041	2.48
Buildings	84,585	74,840	9,745	13.02
Equipment	17,130	15,866	1,264	7.97
Construction in progress	316	3,112	(2,796)	89.85
Total capital assets	\$ 189,605	\$ 179,351	\$ 10,254	5.72
Less: accumulated depreciation	(73,616)	(65,349)	(8,267)	12.65
Net Capital Assets	\$ 115,989	\$ 114,002	\$ 1,987	1.74

At the end of 2014, the Authority has invested approximately \$189.6 million in capital assets since its inception.

The Authority recently updated its Airport Capital Improvement Program through 2024, which includes for 2015:

- \$2,800 thousand for renovations of hangar 103 for Lake Superior College’s (LSC) Center for Advanced Aviation;
- \$998 thousand for a new pickup, grader with a plow, and loader with a snow box;

- \$275 thousand for the design of runway 9/27 reconstruction;
- \$740 thousand for Sky Harbor gate and fence replacement as well as runway relocation design and aerial surveys;
- \$675 thousand for security fence updates; and
- \$48 thousand for pavement maintenance.

DEBT ADMINISTRATION

The City of Duluth obtained a \$500,000 loan from the Minnesota Investment Fund to remedy soil conditions on Duluth Airport Authority property in support of new business development. On December 20, 2005, the Authority entered into an agreement with the Duluth Economic Development Authority that provided the Authority make payments due on the loan in the amount of \$400,000. The loan is noninterest-bearing, payable in 180 monthly installments of \$2,222 beginning February 2006. The noncurrent portion of the loan payable is \$135,556.

The Authority entered into a Lease Acquisition Agreement with North Country Aviation (NCA) on November 1, 2005. The agreement required the Authority pay NCA \$497,379 in order to acquire NCA's FBO lease agreement and facilitate its transfer to Monaco Air Duluth. The note is payable by the Authority as Airport Facility Revenue Note, Series 2005A. The note is for a term of 13 years, payable each June 1 and December 1, commencing June 1, 2007. Interest is compounded at 8.85 percent per annum.

A summary of changes in the revenue note balances are:

	Debt (000s)	<u>FY 2014</u>
Balance - January 1		\$ 321
Additions		-
Payments		<u>48</u>
Balance - December 31		<u>\$ 273</u>

The City of Duluth issued General Obligation Airport Improvement Bonds for the Authority with a face value of \$7,650,000 in May 2012. These bonds will be repaid over 15 years. The bond proceeds are being used as the local match on federal and state grants for the "project" including the terminal, access roads, apron, and parking ramp.

The City of Duluth also issued General Obligation Airport Improvement Bonds for the Authority with a face value of \$3,400,000 in December 2013. These bonds will be repaid over 16 years. The bond proceeds are also being used as the local match on federal and state grants for the “project” including the terminal, access roads, apron, and parking ramp.

ECONOMIC AND OTHER FACTORS

When setting the 2014 budget, the Authority took many factors into consideration: the continuing financial and operational turmoil of the commercial aviation sector; the continuing vigilance of security requirements and its effects on commercial air travel and airport passenger handling; weather conditions which dictate utility costs and overtime for snow removal crews, energy, operating supplies, labor, and benefits price increases; and a general review of all rates and services so that revenue will keep pace with expenses. The Authority has taken steps to raise all rental and concession fees to competitive rates and carefully manages its costs for equipment, supplies, and services. The Authority actively seeks new lessees to occupy vacant space as well as economic development opportunities that are a good fit for the aviation sector. Examples of this are the Authority’s development efforts and partnership with the Duluth Economic Development Authority to facilitate usage of the former Northwest Airlines Maintenance Facility by AAR. Another is the support of renovations to hangar 103 where LSC will house their Center for Advanced Aviation to educate future employees of major economic players on the airfield, including Cirrus and AAR. The renovation is expected to be complete in the summer of 2015. The Authority will continue to seek diversifying revenue sources in order to be less reliant on airline revenue sources.

FINANCIAL CONTACT

This financial report is designed to provide our customers and creditors with a general overview of the Authority’s finances and to demonstrate the Authority’s accountability for the money it receives. If you have any questions about this report or need additional financial information, contact the Director of Finance, Duluth Airport Authority, 4701 Grinden Drive, Duluth, Minnesota 55811.

BASIC FINANCIAL STATEMENTS

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**DULUTH AIRPORT AUTHORITY
DULUTH, MINNESOTA**

EXHIBIT 1

**COMPARATIVE STATEMENT OF NET POSITION
DECEMBER 31, 2014 AND 2013**

	2014	2013
Assets		
Current assets		
Cash and cash equivalents	\$ 619,459	\$ 617,031
Accounts receivable	517,548	495,025
Grants receivable	35,341	19,807
Inventory	88,778	83,447
Prepaid items	21,007	193,183
Assets restricted for construction		
Cash and cash equivalents	1,415,956	6,631,795
Accounts receivable	69,167	84,605
Grants receivable	5,795,030	4,245,279
Total current assets	\$ 8,562,286	\$ 12,370,172
Noncurrent assets		
Capital assets		
Nondepreciable	\$ 3,677,137	\$ 6,473,465
Depreciable	185,928,079	172,878,264
Less: accumulated depreciation	(73,616,366)	(65,349,013)
Net capital assets	\$ 115,988,850	\$ 114,002,716
Other assets		
Airport planning costs - net of accumulated amortization of \$656,344 in 2014 and \$470,189 in 2013	\$ 1,373,116	\$ 1,279,881
Lease buyout costs - net of accumulated amortization of \$360,578 in 2014 and \$324,184 in 2013	166,803	203,197
Total other assets	\$ 1,539,919	\$ 1,483,078
Total noncurrent assets	\$ 117,528,769	\$ 115,485,794
Total Assets	\$ 126,091,055	\$ 127,855,966

**DULUTH AIRPORT AUTHORITY
DULUTH, MINNESOTA**

**EXHIBIT 1
(Continued)**

**COMPARATIVE STATEMENT OF NET POSITION
DECEMBER 31, 2014 AND 2013**

	2014	2013
Liabilities		
Current liabilities payable from unrestricted assets		
Accounts payable	\$ 209,949	\$ 324,595
Due to the City of Duluth	1,650,000	3,500,000
Accrued salaries payable	73,952	69,905
Accrued vacation payable	84,398	82,583
Construction contracts payable	110,316	205,755
Unearned revenue	19,781	19,781
Revenue notes payable	51,919	47,612
Loans payable - City of Duluth	685,000	455,000
Loans payable	26,667	26,667
Total current liabilities payable from unrestricted assets	\$ 2,911,982	\$ 4,731,898
Current liabilities payable from restricted assets		
Construction contracts payable	2,415,660	515,895
Total current liabilities	\$ 5,327,642	\$ 5,247,793
Noncurrent liabilities		
Unearned revenue	\$ 279,250	\$ 295,498
Revenue notes payable	221,584	273,503
Loans payable - City of Duluth	9,030,000	9,715,000
Loans payable	135,555	162,222
Net other postemployment benefits liability	1,036,226	899,868
Total noncurrent liabilities	\$ 10,702,615	\$ 11,346,091
Total Liabilities	\$ 16,030,257	\$ 16,593,884
Net Position		
Net investment in capital assets	\$ 105,001,608	\$ 109,553,972
Unrestricted	5,059,190	1,708,110
Total Net Position	\$ 110,060,798	\$ 111,262,082

**DULUTH AIRPORT AUTHORITY
DULUTH, MINNESOTA**

EXHIBIT 2

**COMPARATIVE STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET POSITION
YEARS ENDED DECEMBER 31, 2014 AND 2013**

	2014	2013
Operating Revenues		
Charges for services	\$ 5,042,397	\$ 4,212,773
Operating Expenses		
Personal services	\$ 1,822,244	\$ 1,684,200
Supplies	66,175	60,588
Utilities	674,465	690,249
Other services and charges	1,583,936	1,573,825
Depreciation	8,333,501	8,044,434
Amortization	222,549	202,332
Total Operating Expenses	\$ 12,702,870	\$ 12,255,628
Operating Income (Loss)	\$ (7,660,473)	\$ (8,042,855)
Nonoperating Revenues (Expenses)		
Investment earnings	\$ 50,823	\$ 38,533
Passenger facility charge	606,863	620,914
Gain (loss) on disposal of capital assets	15,692	(3,000,917)
Net loan issuance expense	-	(63,544)
Interest expense	(521,844)	(279,012)
Total Nonoperating Revenues (Expenses)	\$ 151,534	\$ (2,684,026)
Net Income (Loss) Before Capital Contributions	\$ (7,508,939)	\$ (10,726,881)
Capital Contributions		
Capital grants		
Federal	\$ 2,992,082	\$ 6,156,814
State	3,258,764	2,791,234
Contributed capital		
Contributed capital - Transportation Security Administration (TSA)	56,809	275,491
Contributed capital - other	-	703,600
Total Capital Contributions	\$ 6,307,655	\$ 9,927,139
Change in Net Position	\$ (1,201,284)	\$ (799,742)
Net Position - January 1	111,262,082	112,061,824
Net Position - December 31	\$ 110,060,798	\$ 111,262,082

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

**DULUTH AIRPORT AUTHORITY
DULUTH, MINNESOTA**

EXHIBIT 3

**COMPARATIVE STATEMENT OF CASH FLOWS
YEARS ENDED DECEMBER 31, 2014 AND 2013**

	2014	2013
Cash Flows from Operating Activities		
Cash received from customers	\$ 4,738,548	\$ 3,896,630
Cash paid to suppliers	(2,272,377)	(2,374,760)
Cash paid to employees	(1,680,024)	(1,542,449)
Other cash receipts	270,792	305,292
	\$ 1,056,939	\$ 284,713
Cash Flows from Noncapital Financing Activities		
Principal paid on revenue note	\$ (47,612)	\$ (43,662)
Interest paid on revenue note	(27,388)	(31,338)
	\$ (75,000)	\$ (75,000)
Cash Flows from Capital and Related Financing Activities		
Proceeds from draw on line of credit	\$ 50,000	\$ 3,985,000
Repayment of line of credit	(1,900,000)	(4,485,000)
Principal paid on loans	(481,667)	(471,666)
Loan proceeds	-	3,400,000
Loan issuance and interest costs	(521,844)	(311,218)
Capital grants - federal	1,284,138	9,331,319
Capital grants - state	3,249,041	4,460,902
Capital contributions - TSA	225,205	874,590
Passenger facility charge	622,301	617,272
Proceeds from sale of capital assets	52,100	-
Acquisition or construction of capital assets	(8,825,447)	(15,415,721)
	\$ (6,246,173)	\$ 1,985,478
Cash Flows from Investing Activities		
Interest on investments	\$ 50,823	\$ 38,533
	\$ (5,213,411)	\$ 2,233,724
Net Increase (Decrease) in Cash and Cash Equivalents		
	\$ (5,213,411)	\$ 2,233,724
Cash and Cash Equivalents - January 1	7,248,826	5,015,102
Cash and Cash Equivalents - December 31	\$ 2,035,415	\$ 7,248,826

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

**DULUTH AIRPORT AUTHORITY
DULUTH, MINNESOTA**

**EXHIBIT 3
(Continued)**

**COMPARATIVE STATEMENT OF CASH FLOWS
YEARS ENDED DECEMBER 31, 2014 AND 2013**

	2014	2013
Reconciliation of Operating Income (Loss) to Net Cash Provided by (Used in) Operating Activities		
Operating income (loss)	\$ (7,660,473)	\$ (8,042,855)
Adjustments to reconcile operating income (loss) to net cash provided by (used in) operating activities		
Depreciation	8,333,501	8,044,434
Amortization	222,549	202,332
Changes in assets and liabilities		
(Increase) decrease in receivables	(38,057)	(10,951)
(Increase) decrease in inventory	(5,331)	(9,518)
(Increase) decrease in prepaid items	172,176	(151,212)
Increase (decrease) in payables	27,574	252,383
Increase (decrease) in unearned revenue	5,000	100
	\$ 1,056,939	\$ 284,713
Net Cash Provided by (Used in) Operating Activities		
	\$ 1,056,939	\$ 284,713
Noncash Investing, Capital, and Financing Activities		
Carrying value of capital assets disposed of	\$ 36,408	\$ 3,000,916
Capital assets acquired by construction contracts payable	1,804,326	-

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**DULUTH AIRPORT AUTHORITY
DULUTH, MINNESOTA**

NOTES TO THE FINANCIAL STATEMENTS
AS OF AND FOR THE YEARS ENDED DECEMBER 31, 2014 AND 2013

1. Summary of Significant Accounting Policies

The accounting policies of the Duluth Airport Authority conform with generally accepted accounting principles. The more significant accounting policies established in GAAP and used by the Authority are discussed below.

A. Financial Reporting Entity

The Duluth Airport Authority was created by the Legislature of the State of Minnesota in 1969 to operate and maintain the aeronautic facilities and services in the City of Duluth. The Authority is a component unit of the City of Duluth according to criteria established by the Governmental Accounting Standards Board (GASB) for determining the financial reporting entity. Specific criteria include: the management of the Authority is vested in seven Directors appointed by the Mayor of Duluth and approved by the City Council, and the City Council approves the budget of the Authority.

B. Basis of Presentation

The accounts of the Duluth Airport Authority are presented as an enterprise fund. Enterprise funds are used to account for operations financed and operated in a manner similar to private business enterprises--where the intent of the governing body is that the costs (expenses, including depreciation) of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges.

Enterprise funds distinguish operating revenues from nonoperating items. Operating revenues generally result from providing and delivering services in connection with a principal ongoing activity. The principal operating revenues of the Authority are charges to customers for the use and lease of airport facilities. All revenues not meeting this definition are reported as nonoperating revenues.

DULUTH AIRPORT AUTHORITY
DULUTH, MINNESOTA

1. Summary of Significant Accounting Policies (Continued)

C. Basis of Accounting

The Authority uses the accrual basis of accounting. Revenues are recognized when they are earned, and expenses are recognized when they are incurred.

D. Budget

The Authority adopts an annual budget, which is approved by the Duluth City Council. The budget is prepared on the accrual basis of accounting.

E. Cash and Cash Equivalents

Cash and cash equivalents consist of cash and investments held by the Duluth City Treasurer. Investments are stated at fair value. For purposes of the statement of cash flows, all highly liquid investments (including restricted assets) with a maturity of three months or less when purchased are considered to be cash equivalents.

F. Accounts Receivable

Amounts due from individuals and organizations are recorded as receivables at year-end. These include amounts owed pursuant to lease agreements.

G. Inventory

Inventories of materials and supplies are priced at the lower of cost or market on a first-in, first-out basis.

H. Restricted Assets

Monies restricted for the payment of construction contracts and passenger facility charge revenues are accounted for as restricted assets. When both restricted and unrestricted resources are available for use, it is the Authority's policy to use restricted resources first and then unrestricted resources as needed.

**DULUTH AIRPORT AUTHORITY
DULUTH, MINNESOTA**

1. Summary of Significant Accounting Policies (Continued)

I. Capital Assets

Purchased or constructed capital assets are stated at cost. Donated capital assets are stated at their estimated fair value at the time of the donation. The Authority's policy is to capitalize assets with a useful life of one year or more and a minimum cost of \$5,000.

J. Depreciation

Depreciation of capital assets is determined using the straight-line method. The estimated useful lives of the assets are:

<u>Classification</u>	<u>Years</u>
Runways	15
Buildings and structures	20 to 30
Equipment	5 to 10

K. Other Assets

Airport planning costs and lease buyout costs are being amortized by the straight-line method over 10 to 20 years.

L. Unearned Revenue

Amounts received as advance payments for construction, rentals, and commissions are reported as unearned revenue until they are earned.

M. Passenger Facility Charges

The Duluth Airport Authority has been authorized by the Federal Aviation Administration to collect passenger facility charges to finance capital improvements at Duluth International Airport and Duluth Sky Harbor Airport.

**DULUTH AIRPORT AUTHORITY
DULUTH, MINNESOTA**

1. Summary of Significant Accounting Policies (Continued)

N. Use of Estimates

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

2. Detailed Notes

A. Deposits and Investments

The Authority and the City Council of Duluth are authorized by Minn. Stat. §§ 118A.02 and 118A.04 to designate a depository of public funds and to invest in certificates of deposit. Minnesota statutes require that all Authority deposits be covered by insurance, surety bond, or collateral.

The Authority may invest in the types of securities authorized by Minn. Stat. §§ 118A.04 and 118A.05.

Additional disclosures, as required by GASB Statement No. 3, *Deposits with Financial Institutions, Investments (Including Repurchase Agreements), and Reverse Repurchase Agreements*; and GASB Statement No. 40, *Deposit and Investment Risk Disclosures*, are disclosed on an entity-wide basis in the City of Duluth's Comprehensive Annual Financial Report. The Duluth Airport Authority is a component unit of the City of Duluth.

The following is a summary of the Authority's cash:

	December 31	
	2014	2013
City's pooled cash and investments	\$ 2,033,688	\$ 7,245,346
Authority's checking accounts	1,608	3,361
Petty cash funds	119	119
Total	<u>\$ 2,035,415</u>	<u>\$ 7,248,826</u>

**DULUTH AIRPORT AUTHORITY
DULUTH, MINNESOTA**

2. Detailed Notes

A. Deposits and Investments (Continued)

	December 31	
	2014	2013
Detail as shown on Comparative Balance Sheet		
Current assets		
Cash and cash equivalents	\$ 619,459	\$ 617,031
Assets restricted for construction		
Cash and cash equivalents	1,415,956	6,631,795
Total Cash and Cash Equivalents	\$ 2,035,415	\$ 7,248,826

B. Capital Assets

A summary of changes in capital assets at December 31, 2014 and 2013, follows:

	Balance January 1, 2014	Increase	Decrease	Transfers/ Reclassifications	Balance December 31, 2014
Capital assets not depreciated					
Land	\$ 3,361,434	\$ -	\$ -	\$ -	\$ 3,361,434
Construction in progress	3,112,031	10,600,754	-	(13,397,082)	315,703
Total capital assets not depreciated	\$ 6,473,465	\$ 10,600,754	\$ -	\$ (13,397,082)	\$ 3,677,137
Capital assets depreciated					
Buildings and structures	\$ 74,839,887	\$ 13,656	\$ 15,206	\$ 9,747,143	\$ 84,585,480
Runways	82,172,485	-	-	2,040,028	84,212,513
Equipment	15,865,892	36,230	102,556	1,330,520	17,130,086
Total capital assets depreciated	\$ 172,878,264	\$ 49,886	\$ 117,762	\$ 13,117,691	\$ 185,928,079
Less: accumulated depreciation for					
Buildings and structures	\$ 8,666,257	\$ 2,550,347	\$ -	\$ -	\$ 11,216,604
Runways	50,530,760	4,113,912	-	-	54,644,672
Equipment	6,151,996	1,669,242	66,148	-	7,755,090
Total accumulated depreciation	\$ 65,349,013	\$ 8,333,501	\$ 66,148	\$ -	\$ 73,616,366
Total capital assets depreciated, net	\$ 107,529,251	\$ (8,283,615)	\$ 51,614	\$ 13,117,691	\$ 112,311,713
Capital Assets, Net	\$ 114,002,716	\$ 2,317,139	\$ 51,614	\$ (279,391)	\$ 115,988,850

**DULUTH AIRPORT AUTHORITY
DULUTH, MINNESOTA**

2. Detailed Notes

B. Capital Assets (Continued)

	Balance January 1, 2013	Increase	Decrease	Transfers/ Reclassifications	Balance December 31, 2013
Capital assets not depreciated					
Land	\$ 3,361,434	\$ -	\$ -	\$ -	\$ 3,361,434
Construction in progress	50,052,647	10,164,892	6,000	(57,099,508)	3,112,031
Total capital assets not depreciated	\$ 53,414,081	\$ 10,164,892	\$ 6,000	\$ (57,099,508)	\$ 6,473,465
Capital assets depreciated					
Buildings and structures	\$ 35,113,702	\$ 720,180	\$ 8,591,214	\$ 47,597,219	\$ 74,839,887
Runways	80,172,803	-	1,590	2,001,272	82,172,485
Equipment	10,097,064	-	945,052	6,713,880	15,865,892
Total capital assets depreciated	\$ 125,383,569	\$ 720,180	\$ 9,537,856	\$ 56,312,371	\$ 172,878,264
Less: accumulated depreciation for					
Buildings and structures	\$ 11,852,490	\$ 2,452,150	\$ 5,638,383	\$ -	\$ 8,666,257
Runways	46,563,455	3,968,895	1,590	-	50,530,760
Equipment	5,425,574	1,623,389	896,967	-	6,151,996
Total accumulated depreciation	\$ 63,841,519	\$ 8,044,434	\$ 6,536,940	\$ -	\$ 65,349,013
Total capital assets depreciated, net	\$ 61,542,050	\$ (7,324,254)	\$ 3,000,916	\$ 56,312,371	\$ 107,529,251
Capital Assets, Net	\$ 114,956,131	\$ 2,840,638	\$ 3,006,916	\$ (787,137)	\$ 114,002,716

Transfers and reclassifications for 2014 and 2013 do not net out to zero because there was construction in progress transferred to "Other Assets - Airport Planning Costs" which is not included on this summary (\$279,391 in 2014 and \$787,137 in 2013).

**DULUTH AIRPORT AUTHORITY
DULUTH, MINNESOTA**

2. Detailed Notes

B. Capital Assets (Continued)

As of December 31, 2014, the Authority had the following commitments with respect to unfinished construction projects:

<u>Projects</u>	<u>Remaining Construction Commitment</u>
AIP 09	\$ 542,249
AIP 54	428,101
Parking Ramp	<u>381,605</u>
Total	<u>\$ 1,351,955</u>

As of December 31, 2013, the Authority had the following commitments with respect to unfinished construction projects:

<u>Projects</u>	<u>Remaining Construction Commitment</u>
AIP 53	\$ 198,582
AIP 54	458,113
Parking Ramp	<u>8,468,985</u>
Total	<u>\$ 9,125,680</u>

**DULUTH AIRPORT AUTHORITY
DULUTH, MINNESOTA**

2. Detailed Notes (Continued)

C. Vacation and Sick Leave

Full-time employees are granted from 12 to 28 days of vacation time per year depending on their years of service. Maximum amounts of vacation time that can be accumulated range from 18 to 42 days. Unpaid vacation time earned at year-end is recognized as a liability in the financial statements. Sick leave is accrued by employees at the rate of 4 hours per pay period and may be accumulated to a maximum of 120 days, 60 days, or 30 days, depending on the employee's start date. Sick leave is recorded as an expense when paid. Employees are not compensated for unused sick leave. Any liability for earned, unused sick leave is not recognized in the financial statements.

D. Leases

The Authority leases space and other facilities under various rates and terms. All such leases are considered to be operating leases.

Minimum future rents receivable on noncancelable leases are:

2015	\$	133,468
2016		134,928
2017		134,928
2018		133,928
2019		116,045
After 2019		<u>1,254,199</u>
Total	\$	<u>1,907,496</u>

Contingent rental income from operating leases for 2014 and 2013 was \$244,335 and \$253,686, respectively.

**DULUTH AIRPORT AUTHORITY
DULUTH, MINNESOTA**

2. Detailed Notes (Continued)

E. Budgets

The Duluth Airport Authority adopts a budget to be approved by the Duluth City Council. A summary of the operating budget for the fiscal years ended December 31, 2014 and 2013, is:

	2014		Variance Favorable (Unfavorable)
	Budget	Actual	
Operating Revenues			
Charges for services	\$ 4,251,357	\$ 5,042,397	\$ 791,040
Operating Expenses			
Personal services	\$ 2,038,030	\$ 1,822,244	\$ 215,786
Supplies	229,300	66,175	163,125
Utilities	626,950	674,465	(47,515)
Other services and charges	1,371,449	1,583,936	(212,487)
Depreciation	8,044,434	8,333,501	(289,067)
Amortization	205,366	222,549	(17,183)
Total Operating Expenses	\$ 12,515,529	\$ 12,702,870	\$ (187,341)
Net Operating Income (Loss)	\$ (8,264,172)	\$ (7,660,473)	\$ 603,699
Nonoperating Revenues (Expenses)			
Investment earnings	\$ 25,000	\$ 50,823	\$ 25,823
Passenger facility charge	595,000	606,863	11,863
Gain (loss) on disposal of capital assets	-	15,692	15,692
Interest expense	(813,693)	(521,844)	291,849
Total Nonoperating Revenues (Expenses)	\$ (193,693)	\$ 151,534	\$ 345,227
Net Income (Loss) Before Capital Contributions	\$ (8,457,865)	\$ (7,508,939)	\$ 948,926
Capital Contributions			
Capital grants - federal	\$ 2,650,168	\$ 2,992,082	\$ 341,914
Capital grants - state	3,841,036	3,258,764	(582,272)
Contributed capital - TSA	-	56,809	56,809
Total Capital Contributions	\$ 6,491,204	\$ 6,307,655	\$ (183,549)
Change in Net Position	\$ (1,966,661)	\$ (1,201,284)	\$ 765,377

**DULUTH AIRPORT AUTHORITY
DULUTH, MINNESOTA**

2. Detailed Notes

E. Budgets (Continued)

	2013		Variance Favorable (Unfavorable)
	Budget	Actual	
Operating Revenues			
Charges for services	\$ 3,985,400	\$ 4,212,773	\$ 227,373
Operating Expenses			
Personal services	\$ 1,660,328	\$ 1,684,200	\$ (23,872)
Supplies	300,000	60,588	239,412
Utilities	500,000	690,249	(190,249)
Other services and charges	1,136,900	1,573,825	(436,925)
Depreciation	5,595,951	8,044,434	(2,448,483)
Amortization	133,233	202,332	(69,099)
Total Operating Expenses	\$ 9,326,412	\$ 12,255,628	\$ (2,929,216)
Net Operating Income (Loss)	\$ (5,341,012)	\$ (8,042,855)	\$ (2,701,843)
Nonoperating Revenues (Expenses)			
Investment earnings	\$ 15,000	\$ 38,533	\$ 23,533
Passenger facility charge	600,000	620,914	20,914
Gain (loss) on disposal of capital assets	-	(3,000,917)	(3,000,917)
Net loan issuance expense	-	(63,544)	(63,544)
Interest expense	(734,000)	(279,012)	454,988
Total Nonoperating Revenues (Expenses)	\$ (119,000)	\$ (2,684,026)	\$ (2,565,026)
Net Income (Loss) Before Capital Contributions	\$ (5,460,012)	\$ (10,726,881)	\$ (5,266,869)
Capital Contributions			
Capital grants - federal	\$ 3,084,600	\$ 6,156,814	\$ 3,072,214
Capital grants - state	43,400	2,791,234	2,747,834
Contributed capital - TSA	-	275,491	275,491
Contributed capital - Federal Prison Bureau	-	703,600	703,600
Total Capital Contributions	\$ 3,128,000	\$ 9,927,139	\$ 6,799,139
Change in Net Position	\$ (2,332,012)	\$ (799,742)	\$ 1,532,270

**DULUTH AIRPORT AUTHORITY
DULUTH, MINNESOTA**

2. Detailed Notes (Continued)

F. Long-Term Debt

On November 1, 2005, the Authority issued an Airport Facility Revenue Note, Series 2005A, to finance the lease buyout of the Authority's Fixed Base Operator. The principal of the note is \$497,379, payable in semi-annual payments on June 1 and December 1 each year, commencing June 1, 2007, until final maturity on June 1, 2019, with an annual interest rate of 8.85 percent.

The City of Duluth obtained a loan from the Minnesota Investment Fund (MIF). Proceeds from the loan have been used to remedy soil conditions on Duluth Airport Authority property. The Duluth Airport Authority has agreed to make payments when due on the loan in the total amount of \$400,000. Payments are due in 180 monthly installments of \$2,222 from February 2006 to January 2021. There is no interest charged on this loan.

In May 2012, the City of Duluth issued General Obligation Airport Improvement Bonds, Series 2012B, on behalf of the Duluth Airport Authority. The bonds have a face value of \$7,650,000 and will be repaid over a period of 15 years. Proceeds of the bonds will be used to provide the local match of federal and state grants in relation to a new terminal facility and for funding involved with a new parking ramp, access road, and aprons. The Duluth Airport Authority entered into a loan agreement with the City of Duluth and makes loan payments to the City in sufficient amounts for the City to make the required payments on the bonds.

In December 2013, the City of Duluth issued General Obligation Airport Improvement Bonds, Series 2013B, on behalf of the Duluth Airport Authority. The bonds have a face value of \$3,400,000 and will be repaid over a period of 16 years. Proceeds of the bonds will be used to provide funding in completion of the parking ramp facilities. The Duluth Airport Authority entered into a loan agreement with the City of Duluth and makes loan payments to the City in sufficient amounts for the City to make the required payments on the bonds.

**DULUTH AIRPORT AUTHORITY
DULUTH, MINNESOTA**

2. Detailed Notes

F. Long-Term Debt (Continued)

The annual requirements to service the debt follow:

Year Ended December 31	Revenue Note		MIF Loan
	Principal	Interest	Principal
2015	\$ 51,919	\$ 23,081	\$ 26,667
2016	56,615	18,385	26,667
2017	61,737	13,263	26,667
2018	67,321	7,679	26,667
2019	35,911	1,589	26,667
2020 to 2024	-	-	28,887
Total	<u>\$ 273,503</u>	<u>\$ 63,997</u>	<u>\$ 162,222</u>

Year Ended December 31	City of Duluth Loan 2012B		City of Duluth Loan 2013B	
	Principal	Interest	Principal	Interest
2015	\$ 465,000	\$ 160,281	\$ 220,000	\$ 118,981
2016	470,000	150,981	225,000	115,571
2017	485,000	141,581	225,000	111,071
2018	490,000	131,881	230,000	105,446
2019	500,000	122,081	240,000	98,776
2020 to 2024	2,705,000	421,319	1,325,000	362,866
2025 to 2027	1,200,000	58,088	935,000	81,757
Total	<u>\$ 6,315,000</u>	<u>\$ 1,186,212</u>	<u>\$ 3,400,000</u>	<u>\$ 994,468</u>

A summary of the changes in the long-term debt follows:

	2014	2013
Balance - January 1	\$ 10,680,004	\$ 7,795,333
Additions	-	3,400,000
Payments	(529,279)	(515,329)
Balance - December 31	<u>\$ 10,150,725</u>	<u>\$ 10,680,004</u>
Due Within One Year	<u>\$ 763,586</u>	<u>\$ 529,279</u>

**DULUTH AIRPORT AUTHORITY
DULUTH, MINNESOTA**

2. Detailed Notes (Continued)

G. Line of Credit

The City of Duluth has extended the Duluth Airport Authority a line of credit of up to \$4,000,000 to assist in the management of cash flows in connection with the Authority's new airport terminal construction project, parking ramp construction, and other projects. Interest at a rate of 2.5 percent is charged on drawn funds.

At December 31, 2013, there was \$3,500,000 outstanding. During 2014, draws on the line of credit were taken by the Authority totaling \$50,000, and repayments of \$1,900,000 were made on the draws. The remaining balance outstanding of \$1,650,000 is reported as Due to the City of Duluth on the Comparative Statement of Net Position at December 31, 2014.

3. Risk Management

The Authority is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; employee health and dental; and natural disasters. The Authority participates in the City of Duluth Joint Powers Enterprise Trust to provide its employees health and dental benefits. The Authority purchases commercial insurance for all other risks of loss. There were no significant reductions in insurance coverage from the previous year. There were no settlements in excess of insurance for any of the past three fiscal years.

Employee health and dental benefits are provided through the City of Duluth Joint Powers Enterprise Trust at premium rates established by the Trust for all plan participants.

4. Major Customers

Major customers are defined under accounting standards as a single customer from which the enterprise derives 10 percent or more of its revenue. There were no customers in 2014 that qualified under this definition as major customers.

**DULUTH AIRPORT AUTHORITY
DULUTH, MINNESOTA**

4. Major Customers (Continued)

Major customers of services provided by the Duluth Airport Authority in 2013 were:

	Operating Revenues	Percentage of Total Operating Revenues
DELTA Airlines	\$ 471,834	11.2%

5. Pension Plans--Defined Benefit Plans

A. Plan Description

All full-time and certain part-time employees of the Duluth Airport Authority are covered by defined benefit plans administered by the Public Employees Retirement Association of Minnesota (PERA). PERA administers the General 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.

General 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 and benefits vest after five years of credited service. No Authority members belong to the Basic 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. Defined retirement benefits are based on a member's highest average salary for any five successive years of allowable service, age, and years of credit at termination of service.

Two methods are used to compute benefits for Coordinated 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 is 1.2 percent of average salary for each of the first ten years of service and 1.7 percent for each remaining year. Using Method 2, the annuity accrual rate is 1.7 percent for Coordinated Plan members for each year of service.

**DULUTH AIRPORT AUTHORITY
DULUTH, MINNESOTA**

5. Pension Plan--Defined Benefit Plans

A. Plan Description (Continued)

For General Employees Retirement Fund members hired prior to July 1, 1989, whose annuity is calculated using Method 1, a full annuity is available when age plus years of service equal 90. Normal retirement age is 65 or 66 (depending on date hired) for General Employees Retirement Fund members. 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 General 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. Rates for employer and employee contributions are set by Minn. Stat. ch. 353. These statutes are established and amended by the State Legislature. The Duluth Airport Authority makes annual contributions to the pension plans equal to the amount required by state statutes. General Employees Retirement Fund Coordinated Plan members were required to contribute 6.25 percent of their annual covered salary in 2014.

In 2014, the Duluth Airport Authority was required to contribute the following percentages of annual covered payroll:

General Employees Retirement Fund Coordinated Plan members	7.25%
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**DULUTH AIRPORT AUTHORITY
DULUTH, MINNESOTA**

5. Pension Plan--Defined Benefit Plans

B. Funding Policy (Continued)

The Authority's contributions for the years ending December 31, 2014, 2013, and 2012, for the General Employees Retirement Fund were:

<u>2014</u>	<u>2013</u>	<u>2012</u>
\$ 79,655	\$ 76,081	\$ 71,779

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

6. Other Postemployment Benefits (OPEB)

A. Plan Description and Funding Policy

The Authority provides postemployment health care benefits and term life insurance coverage in accordance with union contract or Authority policy. Union contract postemployment benefits extend to Authority employees retiring on or after January 1, 1983, who receive retirement benefits from PERA. In addition, the Authority has extended the same postemployment benefits to Authority employees retired prior to January 1, 1983. Thirteen retirees meet these eligibility requirements.

B. Annual OPEB Cost and Net OPEB Obligation

The Authority participates in the City of Duluth Joint Powers Enterprise Trust and pays the required premiums to provide health care benefits and term life insurance for eligible retirees and claimed dependents. Health care premiums are paid by the Authority to the same extent as active employees for the life of the retiree or the surviving spouse. Life insurance premiums are also paid by the Authority for the life of the retiree. Premiums paid for eligible retirees and claimed dependents for health care insurance in 2014 totaled \$59,672. In 2013, the amount paid was \$64,181.

**DULUTH AIRPORT AUTHORITY
DULUTH, MINNESOTA**

6. Other Postemployment Benefits (OPEB)

B. Annual OPEB Cost and Net OPEB Obligation (Continued)

The Authority participates in the City of Duluth Joint Powers Enterprise Trust and pays the required premiums to provide health care benefits and term life insurance for eligible retirees and claimed dependents. Health care premiums are paid by the Authority to the same extent as active employees for the life of the retiree or the surviving spouse. Life insurance premiums are also paid by the Authority for the life of the retiree. Premiums paid for eligible retirees and claimed dependents for health care insurance in 2014 totaled \$59,672. In 2013, the amount paid was \$64,181.

The Authority's annual OPEB cost is calculated based on the annual required contribution (ARC) of the employer, an amount actuarially determined in accordance with the parameters of GASB Statement 45. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and amortize any unfunded actuarial accrued liabilities (or funding excess) over a period not to exceed 30 years. The following table shows the components of the Authority's annual OPEB cost for 2014, the amount actually contributed to the plan, and changes in the Authority's net OPEB obligation:

ARC	\$ 208,028
Interest on net OPEB obligation	51,292
Adjustment to ARC	<u>(63,290)</u>
Annual OPEB cost	\$ 196,030
Contributions during the year	<u>(59,672)</u>
Increase in net OPEB obligation	\$ 136,358
Net OPEB - Beginning of Year	<u>899,868</u>
Net OPEB - End of Year	<u><u>\$ 1,036,226</u></u>

**DULUTH AIRPORT AUTHORITY
DULUTH, MINNESOTA**

6. Other Postemployment Benefits (OPEB)

B. Annual OPEB Cost and Net OPEB Obligation (Continued)

The Authority's annual OPEB cost, the percentage of annual OPEB cost contributed to the plan, and the net OPEB obligation for 2014 and the two preceding years were as follows:

	Fiscal Year Ended December 31		
	2012	2013	2014
Percentage of Annual OPEB Cost Contributed	49.11%	32.45%	30.44%
Annual OPEB cost	\$ 198,641	\$ 197,813	\$ 196,030
Employer contributions	97,544	64,181	59,672
Net Increase in Net OPEB Obligation	<u>\$ 101,097</u>	<u>\$ 133,632</u>	<u>\$ 136,358</u>

C. Funded Status and Funding Progress

The actuarial accrued liability for benefits at January 1, 2013, as of the most recent actuarial valuation date, is \$1,891,190. The Authority currently has no assets that have been irrevocably deposited in a trust for future health benefits; thus, the entire amount is unfunded. The covered payroll (annual payroll of active employees covered by the plan) is \$1,010,000. The ratio of the unfunded actuarially accrued liabilities to covered payroll is 187.25 percent.

Actuarial valuations involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and health care cost trends. Amounts determined regarding the funded status of the plan and the annual required contributions of the employer are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future. The Schedule of Funding Progress - Other Postemployment Benefits, presented as required supplementary information following the notes to the financial statements, presents multi-year trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liabilities for benefits.

**DULUTH AIRPORT AUTHORITY
DULUTH, MINNESOTA**

6. Other Postemployment Benefits (OPEB) (Continued)

D. Actuarial Methods and Assumptions

Projections of benefits for financial reporting purposes are based on the substantive plan (as understood by the employer and plan members) and include the types of benefits provided at the time of each valuation. The actuarial methods and assumptions used include techniques that are designed to reduce the effect of short-term volatility in actuarial accrued liabilities, consistent with the long-term perspective of the calculations.

In the January 1, 2013, actuarial valuation (latest available), the projected unit credit actuarial cost method was used. The actuarial assumptions included a 5.7 percent discount rate, which is based on the estimated long-term investment yield on the general assets of the Authority. The annual health care cost trend rate is 10.0 percent initially, reduced incrementally to an ultimate rate of 5.0 percent after 10 years. The unfunded actuarial accrued liability is being amortized as a level dollar amount over 30 years.

7. Future Change in Accounting Standards

GASB Statement No. 68, *Accounting and Financial Reporting for Pensions*, as amended by GASB Statement No. 71, *Pension Transition for Contributions Made Subsequent to the Measurement Date*, replaces Statement No. 27, *Accounting for Pensions by State and Local Governmental Employers*, and Statement No. 50, *Pension Disclosures*, as they relate to employer governments that provide pensions through pension plans administered as trusts or similar arrangement that meet certain criteria. GASB Statement 68 requires governments providing defined benefit pension plans to recognize their long-term obligation for pension benefits as a liability for the first time, and to more comprehensively and comparably measure the annual costs of pension benefits. This statement will be effective for the Authority's fiscal year 2015. The Authority has not yet determined the financial statement impact of adopting this new standard.

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REQUIRED SUPPLEMENTARY INFORMATION

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**DULUTH AIRPORT AUTHORITY
DULUTH, MINNESOTA**

EXHIBIT A-1

**SCHEDULE OF FUNDING PROGRESS - OTHER POSTEMPLOYMENT BENEFITS
DECEMBER 31, 2014**

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) (b)	Unfunded Actuarial Accrued Liability (UAAL) (b - a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ((b - a)/c)
January 1, 2013	\$ -	\$ 1,891,190	\$ 1,891,190	0.00%	\$ 1,010,000	187.25%
June 1, 2011	-	1,911,042	1,911,042	0.00	858,000	222.73
June 1, 2009	-	2,085,377	2,085,377	0.00	1,073,859	194.19

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**DULUTH AIRPORT AUTHORITY
DULUTH, MINNESOTA**

**NOTES TO THE SCHEDULE OF FUNDING
PROGRESS - OTHER POSTEMPLOYMENT BENEFITS
DECEMBER 31, 2014**

The Duluth Airport Authority implemented Governmental Accounting Standards Board Statement 45 for the fiscal year ended December 31, 2007.

Actuarial valuations were performed in 2007, 2009, 2011, and 2013. No valuations were performed in 2008, 2010, 2012, or 2014; therefore, funding progress information for 2008, 2010, 2012, and 2014 are not included on this schedule. Standards require reporting the three most recent actuarial valuations.

The Authority currently has no assets that have been irrevocably deposited in a trust for future health benefits. Therefore, the actuarial value of assets is zero.

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SUPPLEMENTARY INFORMATION

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**DULUTH AIRPORT AUTHORITY
DULUTH, MINNESOTA**

EXHIBIT B-1

**COMPARATIVE STATEMENT OF OPERATING REVENUES
YEARS ENDED DECEMBER 31, 2014 AND 2013**

	2014	2013
Operating Revenues		
Charges for services		
Tower building		
Space rental and services	\$ 212,966	\$ 209,316
Terminal building		
Space rental	\$ 689,991	\$ 675,957
Utility sales	21,193	10,487
Car rental commissions	448,505	458,385
Other commissions	5,133	5,097
Percentage of lessees' sales	1,325	778
Other income	500,651	281,903
Total terminal building	\$ 1,666,798	\$ 1,432,607
Parking lot		
Parking lot commissions	\$ 1,271,300	\$ 896,907
Land, field, and runways		
Transportation Security Administration charges	\$ 95,792	\$ 103,778
State aid for maintenance and operation	185,426	168,569
Rental income	338,901	314,957
Customer facility charge	262,984	250,264
Fuel flowage fees	102,340	106,050
Landing fees	297,358	255,870
Percentage of lessees' sales	59,563	61,451
Utility sales	19,580	11,883
Total land, field, and runways	\$ 1,361,944	\$ 1,272,822
Hangar		
Space rental	\$ 299,805	\$ 208,694
Utility sales	80,912	48,409
Total hangar	\$ 380,717	\$ 257,103
Sky Harbor		
State aid for maintenance and operation	\$ 22,313	\$ 20,285
Rental income	35,463	34,228
Fuel sales	81,705	79,634
Percentage of lessees' sales	3,416	3,110
Other income	5,775	6,761
Total Sky Harbor	\$ 148,672	\$ 144,018
Total Operating Revenues	\$ 5,042,397	\$ 4,212,773

**DULUTH AIRPORT AUTHORITY
DULUTH, MINNESOTA**

EXHIBIT C-1

**SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED DECEMBER 31, 2014**

Federal Grantor Pass-Through Agency Grant Program Title	Federal CFDA Number	Pass-Through Grant Number	Expenditures
Department of Defense - National Guard Bureau			
Direct			
National Guard Military Operations and Maintenance (O&M) Projects	12.401	None	\$ 14,412
Federal Aviation Administration			
Passed Through Minnesota Department of Transportation - Aeronautics			
Airport Improvement Program	20.106	Various	<u>2,977,670</u>
Total Expenditures of Federal Awards			<u>\$ 2,992,082</u>

**DULUTH AIRPORT AUTHORITY
DULUTH, MINNESOTA**

**NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED DECEMBER 31, 2014**

1. Reporting Entity

The Schedule of Expenditures of Federal Awards presents the activities of federal award programs expended by the Duluth Airport Authority. The Authority's reporting entity is defined in Note 1 to the financial statements.

2. Basis of Presentation

The accompanying Schedule of Expenditures of Federal Awards includes the federal grant activity of the Duluth Airport Authority under programs of the federal government for the year ended December 31, 2014. The information in this schedule is presented in accordance with the requirements of Office of Management and Budget (OMB) Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Because the schedule presents only a selected portion of the operations of the Duluth Airport Authority, it is not intended to and does not present the financial position, changes in net position, or cash flows of the Duluth Airport Authority.

3. Summary of Significant Accounting Policies

Expenditures reported on the schedule are reported on the accrual basis of accounting. Such expenditures are recognized following the cost principles contained in OMB Circular A-87, *Cost Principles for State, Local and Indian Tribal Governments*, wherein certain types of expenditures are not allowable or are limited as to reimbursement. Pass-through entity identifying numbers are presented where available.

4. Subrecipients

Of the expenditures presented in the schedule, the Duluth Airport Authority did not provide federal awards to any subrecipients.

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**DULUTH AIRPORT AUTHORITY
DULUTH, MINNESOTA**

EXHIBIT C-2

**SCHEDULE OF PASSENGER FACILITY CHARGES COLLECTED AND EXPENDED
FOR THE YEAR AND EACH QUARTER WITHIN THE YEAR ENDED DECEMBER 31, 2014**

	<u>Application Seven*</u>	<u>Application Eight**</u>	<u>Application Nine**</u>	<u>Application Ten**</u>	<u>Application Eleven**</u>
Passenger Facility Charge Collections***					
Prior to January 1, 2014	\$ 2,446,424	\$ 514,305	\$ 201,822	\$ 1,785,583	\$ 119,747
Collections in 2014					
First quarter	\$ -	\$ -	\$ -	\$ 141,304	\$ -
Second quarter	-	-	-	201,759	-
Third quarter	-	-	-	104,284	-
Fourth quarter	-	-	-	150,640	-
Total collections in 2014	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 597,987</u>	<u>\$ -</u>
Total Collected Through December 31, 2014	\$ 2,446,424	\$ 514,305	\$ 201,822	\$ 2,383,570	\$ 119,747
Approved expenses through December 31, 2014	<u>(2,113,428)</u>	<u>(514,305)</u>	<u>(201,822)</u>	<u>(2,133,729)</u>	<u>(702,584)</u>
Unexpended Balance - December 31, 2014	<u><u>\$ 332,996</u></u>	<u><u>\$ -</u></u>	<u><u>\$ -</u></u>	<u><u>\$ 249,841</u></u>	<u><u>\$ (582,837)</u></u>

*Federal Aviation Administration Record of Decision passenger facility charge effective date for Application Seven is April 1, 2005.

**Federal Aviation Administration's Acknowledgment of Intent of passenger facility charge effective date for Application Eight is September 30, 2008; Application Nine is October 1, 2010; Application Ten is January 20, 2011; and Application Eleven is January 16, 2013.

***Cash basis of accounting - reported when received rather than when earned in accordance with passenger facility charge reporting guidelines.

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**DULUTH AIRPORT AUTHORITY
DULUTH, MINNESOTA**

**SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED DECEMBER 31, 2014**

I. SUMMARY OF AUDITOR'S RESULTS

Financial Statements

Type of auditor's report issued: **Unmodified**

Internal control over financial reporting:

- Material weaknesses identified? **No**
- Significant deficiencies identified? **Yes**

Noncompliance material to the financial statements noted? **No**

Federal Awards

Internal control over major programs:

- Material weaknesses identified? **No**
- Significant deficiencies identified? **No**

Type of auditor's report issued on compliance for major programs: **Unmodified**

Any audit findings disclosed that are required to be reported in accordance with Section 510(a) of OMB Circular A-133? **No**

The major program is:

Airport Improvement Program

CFDA #20.106

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

Duluth Airport Authority qualified as a low-risk auditee? **Yes**

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

INTERNAL CONTROL

PREVIOUSLY REPORTED ITEM NOT RESOLVED

Finding 2006-001

Segregation of Duties

Criteria: A good system of internal control provides for an adequate segregation of duties so that no one individual handles a transaction from its inception to completion.

Condition: Due to the limited number of office personnel within the Authority, segregation of the accounting functions necessary to ensure adequate internal accounting control is not possible.

Context: This is not unusual in operations the size of the Duluth Airport Authority; however, the Authority's 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 accounting point of view.

Effect: Inadequate segregation of duties could adversely affect the Authority's ability to detect misstatements in amounts that would be material in relation to the financial statements in a timely period by employees in the normal course of performing their assigned functions.

Cause: The size of the Duluth Airport Authority and its staffing limits the internal control that management can design and implement into the organization.

Recommendation: We recommend that the Authority's management be aware of the lack of segregation of duties of the accounting functions and, where possible, implement oversight procedures to ensure that the internal control policies and procedures are being implemented by staff to the extent possible.

Client's Response:

We are aware of the limited number of personnel. The Authority management has implemented oversight procedures and will continue to monitor the staff to help assure controls and procedures are being followed.

III. FINDINGS AND QUESTIONED COSTS FOR FEDERAL AWARD PROGRAMS

None.

IV. FINDINGS - PASSENGER FACILITY CHARGE (PFC) REGULATIONS

None.

V. OTHER FINDINGS AND RECOMMENDATIONS

OTHER ITEM FOR CONSIDERATION

GASB Statement No. 68, *Accounting and Financial Reporting for Pensions*

The Governmental Accounting Standards Board (GASB) is the independent organization that establishes standards of accounting and financial reporting for state and local governments. Effective for your calendar year 2015 financial statements, the GASB changed those standards as they apply to employers that provide pension benefits.

GASB Statement 68 significantly changes pension accounting and financial reporting for governmental employers that prepare financial statements on the accrual basis by separating pension accounting methodology from pension funding methodology. Statement 68 requires employers to include a portion of the Public Employees Retirement Association (PERA) total employers' unfunded liability, called the "net pension liability" on the face of the Authority's Statement of Net Position. The Authority's financial position will be immediately impacted by its unfunded share of the pension liability.

Statement 68 changes the amount employers report as pension expense and defers some allocations of expenses to future years—deferred outflows or inflows of resources. It requires pension costs to be calculated by an actuary; whereas, in the past pension costs were equal to the amount of employer contributions sent to PERA during the year. Additional footnote disclosures and required supplementary information schedules are also required by Statement 68.

The net pension liability that will be reported in the Authority's financial statements is an accounting estimate of the proportionate share of PERA's unfunded liability at a specific point in time. That number will change from year to year and is based on assumptions about the probability of the occurrence of events far into the future. Those assumptions include how long people will live, how long they will continue to work, projected salary increases, and how well pension trust investments will do. PERA has been proactive in taking steps toward implementation and will be providing most of the information needed by employers to report the net pension liability and deferred outflows/inflows of resources.

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REBECCA OTTO
STATE AUDITOR

STATE OF MINNESOTA OFFICE OF THE STATE AUDITOR

SUITE 500
525 PARK STREET
SAINT PAUL, MN 55103-2139

(651) 296-2551 (Voice)
(651) 296-4755 (Fax)
state.auditor@state.mn.us (E-mail)
1-800-627-3529 (Relay Service)

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*

Independent Auditor's Report

Mayor and City Council
City of Duluth

Board of Directors
Duluth Airport Authority
Duluth, Minnesota

We have audited, 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, the financial statements of the Duluth Airport Authority, a component unit of the City of Duluth, Minnesota, as of and for the year ended December 31, 2014, and the related notes to the financial statements, which collectively comprise the Authority's basic financial statements, and have issued our report thereon dated May 28, 2015.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Duluth Airport Authority's internal control over financial reporting to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Authority's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Authority's internal control over financial reporting.

A deficiency in internal control over financial reporting exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A material weakness is a deficiency, or combination of deficiencies, in internal control over financial

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

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be material weaknesses or significant deficiencies and, therefore, material weaknesses or significant deficiencies may exist that were not identified. Given these limitations, during our audit, we did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified. We did identify a deficiency in internal control over financial reporting, described in the accompanying Schedule of Findings and Questioned Costs as item 2006-001, that we consider to be a significant deficiency.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Duluth Airport Authority's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Minnesota Legal Compliance

The *Minnesota Legal Compliance Audit Guide for Political Subdivisions*, promulgated by the State Auditor pursuant to Minn. Stat. § 6.65, contains six categories of compliance to be tested in connection with the audit of the Authority's financial statements: contracting and bidding, deposits and investments, conflicts of interest, public indebtedness, claims and disbursements, and miscellaneous provisions. Our audit considered all of the listed categories, except that we did not test for compliance with the provisions of deposits and investments because that was tested in conjunction with our audit of the City of Duluth, Minnesota, who holds the Authority's cash and investments.

In connection with our audit, nothing came to our attention that caused us to believe that the Duluth Airport Authority failed to comply with the provisions of the *Minnesota Legal Compliance Audit Guide for Political Subdivisions*. However, our audit was not directed primarily toward obtaining knowledge of such noncompliance. Accordingly, had we performed additional procedures, other matters may have come to our attention regarding the Authority's noncompliance with the above referenced provisions.

Other Matters

Also included in the Schedule of Findings and Questioned Costs is an other item for consideration. We believe this information to be of benefit to the Authority, and we are reporting it for that purpose.

Duluth Airport Authority's Response to Findings

The Duluth Airport Authority's response to the internal control finding identified in our audit has been included in the Schedule of Findings and Questioned Costs. The Authority's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

Purpose of This Report

The purpose of this report is solely to describe the scope of our testing of internal control over financial reporting, compliance, and the provisions of the *Minnesota Legal Compliance Audit Guide for Political Subdivisions* and the results of that testing, and not to provide an opinion on the effectiveness of the Authority's internal control over financial reporting or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Authority's internal control over financial reporting and compliance. Accordingly, this communication is not suitable for any other purpose.

/s/Rebecca Otto

REBECCA OTTO
STATE AUDITOR

/s/Greg Hierlinger

GREG HIERLINGER, CPA
DEPUTY STATE AUDITOR

May 28, 2015

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REBECCA OTTO
STATE AUDITOR

STATE OF MINNESOTA OFFICE OF THE STATE AUDITOR

SUITE 500
525 PARK STREET
SAINT PAUL, MN 55103-2139

(651) 296-2551 (Voice)
(651) 296-4755 (Fax)
state.auditor@state.mn.us (E-mail)
1-800-627-3529 (Relay Service)

REPORT ON COMPLIANCE FOR EACH MAJOR FEDERAL PROGRAM AND FOR THE PASSENGER FACILITY CHARGE PROGRAM AND REPORT ON INTERNAL CONTROL OVER COMPLIANCE

Independent Auditor's Report

Mayor and City Council
City of Duluth

Board of Directors
Duluth Airport Authority
Duluth, Minnesota

Report on Compliance for Each Major Federal Program and for the Passenger Facility Charge Program

We have audited the compliance of the Duluth Airport Authority, a component unit of the City of Duluth, Minnesota, with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) *Circular A-133 Compliance Supplement* that could have a direct and material effect on the Authority's major federal program for the year ended December 31, 2014. The Duluth Airport Authority's major federal program is identified in the Summary of Auditor's Results section of the accompanying Schedule of Findings and Questioned Costs.

We have also audited the Duluth Airport Authority's compliance with requirements applicable to its passenger facility charge (PFC) funds collected and expended for the year ended December 31, 2014.

Management's Responsibility

Management is responsible for compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its federal programs and to its PFC program.

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for the Duluth Airport Authority's major federal program and PFC program based on our audit of the types of compliance requirements referred to above. 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 or PFC program occurred. An audit includes examining, on a test basis, evidence about the Duluth Airport Authority's 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 on compliance for its major federal program and its PFC program. However, our audit does not provide a legal determination of the Authority's compliance with those requirements.

Opinion on Each Major Federal Program and the Passenger Facility Charge Program

In our opinion, the Duluth Airport Authority complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on its major federal program or its PFC program for the year ended December 31, 2014.

Report on Internal Control Over Compliance

Management of the Duluth Airport Authority is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered the Authority's internal control over compliance with the types of requirements that could have a direct and material effect on its major federal program or on its PFC program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for the major federal program and the PFC program and to test and report on internal control over compliance in accordance with OMB Circular A-133, and the *Passenger Facility Charge Audit Guide for Public Agencies*, 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 Authority's internal control over compliance.

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program or the PFC program on a timely basis. A material weakness in internal control over compliance is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program or the PFC program

will not be prevented, or detected and corrected, on a timely basis. A significant deficiency in internal control over compliance is a deficiency, or combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program or the PFC program that is less severe than a material weakness in internal control over compliance, yet important enough to merit the attention of those charged with governance.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Purpose of This Report

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of OMB Circular A-133 and Passenger Facility Charge requirements. Accordingly, this report is not suitable for any other purpose.

/s/Rebecca Otto

/s/Greg Hierlinger

REBECCA OTTO
STATE AUDITOR

GREG HIERLINGER, CPA
DEPUTY STATE AUDITOR

May 28, 2015