

CITY OF WINDOM - TELECOMMUNICATIONS FUND

FINANCIAL STATEMENTS
TOGETHER WITH
INDEPENDENT AUDITORS' REPORT

DECEMBER 31, 2005

CITY OF WINDOM - TELECOMMUNICATIONS FUND

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INDEPENDENT AUDITORS' REPORT

City Council
Windom, Minnesota

We have audited the accompanying statement of net assets of the City of Windom - Telecommunications Fund (an enterprise fund of the City of Windom) as of December 31, 2005 and 2004, and the related statements of revenues, expenses and changes in net assets and cash flows for the years then ended. These financial statements are the responsibility of the Fund's management. 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. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As discussed in Note 1, the financial statements present only the City of Windom - Telecommunications Fund and are not intended to present fairly the financial position of the City of Windom, Minnesota, and the results of operations and cash flows of its proprietary fund types and nonexpendable trust funds in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the City of Windom - Telecommunications Fund as of December 31, 2005 and 2004, and the results of its operations and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

The management's discussion and analysis on pages 3 through 5 is not a required part of the basic financial statements but is supplementary information required by U.S. generally accepted accounting principles. We have applied certain limited procedures, which consisted principally of inquires of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

Olsen Thielen & Co., Ltd.

St. Paul, Minnesota
February 2, 2006

CITY OF WINDOM - TELECOMMUNICATIONS FUND

MANAGEMENT'S DISCUSSION AND ANALYSIS

As management of the City of Windom - Telecommunications Fund, we offer readers of the City of Windom - Telecommunications Fund's financial statements this narrative overview and analysis of the financial activities of the City of Windom - Telecommunications Fund for the years ended December 31, 2005 and 2004. All amounts, unless otherwise indicated, are expressed in whole dollars.

Financial Highlights

- * The liabilities of the City of Windom - Telecommunications Fund exceeded its assets at the close of the most recent fiscal year by \$1,673,112 which is a result of the costs incurred in the implementation phase of providing telecommunications services.
- * The City of Windom - Telecommunications Fund's total net assets decreased by \$1,254,517 in 2005 and \$650,422 in 2004. The majority of this decrease is attributable to operating losses and costs relating to the implementation of providing telecommunications services which began in 2005.
- * The Fund's total debt increased by \$1,000,000 in 2005 and \$9,470,000 in 2004 as a result of issuing an operating line of credit during 2005 and Revenue Bonds during 2004 for construction of its communications facilities.

Overview of the Financial Statements

This discussion and analysis is intended to serve as an introduction to the City of Windom - Telecommunications Fund's basic financial statements. The City of Windom - Telecommunications Fund's basic financial statements are comprised of three components: (1) Statement of Net Assets, (2) Statement of Revenues, Expenses and Changes in Net Assets, and (3) Statement of Cash Flows.

The Statement of Net Assets presents information on all of the City of Windom - Telecommunications Fund's assets and liabilities, with the difference between the two reported as net assets. Over time, increases and decreases in net assets may serve as a useful indicator of whether the financial position of the Fund is improving or deteriorating.

The Statement of Revenues, Expenses, and Changes in Net Assets shows the revenue sources, expenses, classification of expenses and reflects the net change in net assets for the years.

The Statement of Cash Flows demonstrates the sources and uses of funds received and expended and reconciles beginning and ending cash balances.

The basic financial statements can be found on pages 6-9 of this report.

Notes to the financial statements provide additional information that is essential to a full understanding of the data provided in the basic financial statements. The notes to the financial statements can be found on pages 10-16 of this report.

CITY OF WINDOM - TELECOMMUNICATIONS FUND
MANAGEMENT'S DISCUSSION AND ANALYSIS (Continued)

Financial Analysis

As noted earlier, net assets may serve over time as a useful indicator of a fund's financial position. In the case of the City of Windom - Telecommunications Fund, liabilities exceed assets by \$1,673,112 in 2005 and \$418,595 in 2004. This is a result of costs incurring during the implementation phase of providing communications services.

A summary of the statement of net assets is as follows.

	<u>2005</u>	<u>2004</u>
Current and Other Assets	\$ 748,079	\$ 4,708,785
Capital Assets	8,856,338	6,276,199
Total Assets	<u>9,604,417</u>	<u>10,984,984</u>
Long-Term Liabilities	9,470,000	9,470,000
Other Liabilities	1,807,529	1,933,579
Total Liabilities	<u>11,277,529</u>	<u>11,403,579</u>
Total Assets Less Total Liabilities	<u>\$ (1,673,112)</u>	<u>\$ (418,595)</u>

Net assets are categorized as follows:

	<u>2005</u>	<u>2004</u>
Invested in Capital Assets, Net of Related Debt	\$ -	\$ 75,698
Restricted	241,332	987,864
Unrestricted	<u>(1,914,444)</u>	<u>(1,482,157)</u>
Total Net Assets	<u>\$ (1,673,112)</u>	<u>\$ (418,595)</u>

Operating revenues and expenses decreased net assets by \$1,289,995 in 2005 and \$650,422 in 2004. Elements of these decreases are as follows:

	<u>2005</u>	<u>2004</u>
Operating Revenues	\$ 745,302	\$ 508,435
Operating Expenses	<u>(1,724,358)</u>	<u>(1,158,857)</u>
Operating Loss	(979,056)	(650,422)
Interest Expense, Net of Amount Capitalized	<u>(313,886)</u>	<u>-</u>
Change in Net Assets	<u>\$ (1,292,942)</u>	<u>\$ (650,422)</u>

At the end of 2005 and 2004, the City of Windom - Telecommunications Fund had unrestricted cash deficits of \$403,241 and \$357,033 in pooled cash with the City of Windom. In 2005, the debt service fund was funded by cash advances from other Funds of the City.

Capital Assets and Debt Administration

Capital Assets:

The Fund's investment in capital assets as of December 31, 2005 and 2004 amounts to \$8,856,338 and \$6,276,199 (net of depreciation). This investment in capital assets includes land, buildings, tower, buried cable facilities and circuit equipment, central office equipment, CATV headend equipment, vehicles and telecommunications plant under construction. The total increase in capital assets (net of depreciation) was \$2,580,139 and \$6,021,697 during 2005 and 2004.

CITY OF WINDOM - TELECOMMUNICATIONS FUND
MANAGEMENT'S DISCUSSION AND ANALYSIS (Continued)

Capital Assets and Debt Administration (Continued)

Major capital asset events during the current fiscal year included the following:

- * Additions to equipment and Plant Under Construction of \$2,910,623.
- * Depreciation expenses for the year was \$330,484.
- * Retirements of obsolete and abandoned assets totaled \$680,839 in 2005.

	<u>2005</u>	<u>2004</u>
Physical Facilities:		
Building and Tower	\$ 677,736	\$ 659,614
Buried Cable Facilities and Circuit Equipment	4,058,891	622,557
Central Office Equipment	1,151,332	-
Circuit Equipment	2,603,696	-
General Purpose Computer	85,872	65,015
Boxes and Converters	21,007	-
Head End Equipment	464,822	151,152
Furniture and Fixtures	10,529	30,249
Motor Vehicles	57,586	67,803
Tools and Equipment	80,716	41,963
Internet Equipment	117,755	-
Plant Under Construction	-	5,461,806
Total Physical Facilities	<u>9,329,942</u>	<u>7,100,159</u>
Less: Accumulated Depreciation	<u>(473,604)</u>	<u>(823,960)</u>
Total Capital Assets	<u>\$ 8,856,338</u>	<u>\$ 6,276,199</u>

Outstanding Line of Credit:

At the end of 2005, the City of Windom - Telecommunications Fund had a line of credit outstanding of \$1,000,000 that is due on August 16, 2006. The line of credit increased \$1,000,000 during 2005.

Additional information on the Fund's line of credit can be found in Note 4 on Page 14 of this report.

Outstanding Long-Term Debt:

At the end of 2005 and 2004, the City of Windom - Telecommunications Fund had debt outstanding of \$9,470,000. Total debt did not increase during 2005 and increased \$9,470,000 in 2004.

Additional information on the Fund's long-term debt can be found in Note 5 on Pages 14-15 of this report.

Economic Factors and Next Year's Budget

The 2006 budget indicates gross revenues of approximately \$1,267,000, expenses of approximately \$1,734,500, and net loss from operations of approximately \$467,500. No major capital projects are planned.

CITY OF WINDOM - TELECOMMUNICATIONS FUND
MANAGEMENT'S DISCUSSION AND ANALYSIS (Continued)

Economic Factors and Next Year's Budget (Continued)

Additional funding will be needed to finance future operations. The Fund is considering extending the line of credit and using cash from other funds.

The Fund began providing telecommunications and internet services in late 2005 and is in the process of building its customer base. With additional customers and reduced expenditures for CLEC start-up costs, the Fund expects improvement in operating cash flow and a move toward more profitable operations.

Request for Information

This financial report is designed to provide a general overview of the City of Windom - Telecommunications Fund's finances for all those with an interest in the Fund's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the City of Windom - Telecommunications Fund, 444 9th St, PO Box 38, Windom, MN 56101-0038.

CITY OF WINDOM - TELECOMMUNICATIONS FUND

**STATEMENT OF NET ASSETS
DECEMBER 31, 2005 AND 2004**

ASSETS		
	<u>2005</u>	<u>2004</u>
CURRENT ASSETS:		
Restricted Cash - Construction	\$ -	\$ 3,269,499
Due from Customers	-	45,871
Other Accounts Receivable	7,325	-
Materials and Supplies	<u>226,726</u>	<u>32,905</u>
Total Current Assets	<u>234,051</u>	<u>3,348,275</u>
OTHER ASSETS		
Restricted Cash - Bond Reserve	-	650,000
Restricted Cash - Debt Service Reserve	241,332	337,864
Bond Issuance Costs, Net of Accumulated Amortization of \$4,662 and \$1,369	61,191	64,484
Bond Discount Costs, Net of Accumulated Amortization of \$13,416 and \$3,946	175,984	185,454
Deferred Charges	<u>35,521</u>	<u>122,708</u>
Total Other Assets	<u>514,028</u>	<u>1,360,510</u>
PROPERTY, PLANT AND EQUIPMENT:		
Plant in Service	9,329,942	1,638,353
Plant Under Construction	-	5,461,806
Total	9,329,942	7,100,159
Less Accumulated Depreciation	<u>473,604</u>	<u>823,960</u>
Net Property, Plant and Equipment	<u>8,856,338</u>	<u>6,276,199</u>
TOTAL ASSETS	<u>\$ 9,604,417</u>	<u>\$ 10,984,984</u>

The accompanying notes are an integral part of the financial statements.

LIABILITIES AND NET ASSETS

	<u>2005</u>	<u>2004</u>
CURRENT LIABILITIES:		
General Cash Overdraft	\$ 403,241	\$ 357,033
Accounts Payable - Trade	33,125	32,301
Accounts Payable - Construction	-	1,151,098
Line of Credit	1,000,000	-
Interest Payable	265,706	337,864
Deferred Revenue	92,093	41,578
Customer Deposits	13,364	13,705
Total Current Liabilities	<u>1,807,529</u>	<u>1,933,579</u>
 LONG-TERM DEBT	 <u>9,470,000</u>	 <u>9,470,000</u>
 NET ASSETS:		
Invested in Capital Assets, Net of Related Debt	-	75,698
Restricted:		
Bond Reserve	-	650,000
Debt Service Reserve	241,332	337,864
Unrestricted	<u>(1,914,444)</u>	<u>(1,482,157)</u>
Total Net Assets	<u>(1,673,112)</u>	<u>(418,595)</u>
 TOTAL LIABILITIES AND NET ASSETS	 <u>\$ 9,604,417</u>	 <u>\$ 10,984,984</u>

CITY OF WINDOM - TELECOMMUNICATIONS FUND

STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS
YEARS ENDED DECEMBER 31, 2005 AND 2004

	2005	2004
OPERATING REVENUES:		
Local Network	\$ 23,542	\$ -
Long Distance	4,720	-
Internet	121,436	-
CATV	553,609	494,934
Other Revenue	41,995	13,501
Total Operating Revenues	745,302	508,435
OPERATING EXPENSES:		
Plant Maintenance	263,940	12,111
Depreciation	330,484	126,458
Amortization	12,763	5,315
Internet Expense	7,992	-
Signal Purchases	308,011	307,592
Salaries and Benefits	334,406	183,444
General and Administrative	466,762	523,937
Total Operating Expenses	1,724,358	1,158,857
OPERATING LOSS	(979,056)	(650,422)
INTEREST EXPENSE	(313,886)	-
CHANGE IN NET ASSETS	(1,292,942)	(650,422)
TRANSFER OF UHF FUND EQUITY	38,425	-
NET ASSETS - Beginning of the Year	(418,595)	231,827
NET ASSETS - End of the Year	\$ (1,673,112)	\$ (418,595)

The accompanying notes are an integral part of the financial statements.

CITY OF WINDOM - TELECOMMUNICATIONS FUND

**STATEMENT OF CASH FLOWS
YEARS ENDED DECEMBER 31, 2005 AND 2004**

	<u>2005</u>	<u>2004</u>
CASH FLOWS FROM OPERATING ACTIVITIES:		
Cash Received from Customers	\$ 841,688	\$ 508,217
Cash Payments to Suppliers for Goods and Services	(1,185,774)	(850,227)
Cash Payments to Employees for Services	(194,513)	(167,218)
Net Cash Used In Operating Activities	<u>(538,599)</u>	<u>(509,228)</u>
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES:		
Proceeds from Line of Credit	1,000,000	-
Increase in General Cash Overdraft	77,308	337,999
Decrease in Customer Deposits	(341)	(614)
Net Cash Provided By Noncapital Financing Activities	<u>1,076,967</u>	<u>337,385</u>
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES:		
Additions to Property, Plant and Equipment	(4,061,721)	(4,659,193)
Proceeds from Bond Issuance, Net	-	9,214,747
Interest Paid, Net of Amounts Capitalized	(386,044)	-
Increase in Materials and Supplies	(193,821)	(3,640)
Decrease (Increase) in Restricted Cash	4,016,031	(4,257,363)
Decrease (Increase) in Deferred Charges	87,187	(122,708)
Net Cash Provided By (Used In) Capital and Related Financing Activities	<u>(538,368)</u>	<u>171,843</u>
NET CHANGE IN CASH	-	-
CASH at Beginning of Year	-	-
CASH at End of Year	<u>\$ -</u>	<u>\$ -</u>
RECONCILIATION OF OPERATING LOSS TO NET CASH USED IN OPERATING ACTIVITIES:		
Operating Loss	\$ (979,056)	\$ (650,422)
Adjustments to Reconcile Operating Loss to Net Cash Used In Operating Activities:		
Depreciation and Amortization	343,247	131,773
Changes in Assets and Liabilities:		
Due from Customers	45,871	(217)
Accounts Payable-Trade	824	9,638
Deferred Revenue	50,515	-
Net Cash Used In Operating Activities	<u>\$ (538,599)</u>	<u>\$ (509,228)</u>
NONCASH TRANSACTIONS:		
Transfer in of Equity in UHF Fund	<u>\$ 38,425</u>	<u>\$ -</u>

The accompanying notes are an integral part of the financial statements.

CITY OF WINDOM - TELECOMMUNICATIONS FUND

NOTES TO FINANCIAL STATEMENTS

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Reporting Entity

The City of Windom - Telecommunications Fund is an enterprise fund of the City of Windom, Minnesota. The principal line of business is providing a cable television franchise for the City. In 2005, the Fund began providing local and long-distance telecommunications service and internet service. The principal market for these services are local residential and business customers residing in the City of Windom. The Fund is governed by the Windom City Council.

Measurement Focus, Basis of Accounting, and Financial Statement Presentation

The Fund operates as an enterprise fund of the City of Windom. Enterprise funds are used to account for operations (1) that are financed and operated in a manner similar to a private business enterprise 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, or (2) where the governing body has decided that periodic determination of revenues earned, expenses incurred, and/or net income is appropriate for capital maintenance, public policy, management accountability, or other purposes. The financial statements in this report are prepared on the accrual basis of accounting.

The financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America. The Fund applies all Governmental Accounting Standards Board (GASB) pronouncements as well as the Financial Accounting Standards Board (FASB) pronouncements issued on or before November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements.

The Fund distinguishes operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and delivering goods in connection with the Fund's principal ongoing operation. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

Accounting Estimates

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

Receivables

Receivables are stated at the amounts the Fund expects to collect from outstanding balances. The Fund monitors outstanding balances and periodically writes off balances that are determined to be uncollectible. The Company has determined that losses on balances outstanding at year end will not be significant.

Materials and Supplies

Materials and supplies are recorded at average cost.

CITY OF WINDOM - TELECOMMUNICATIONS FUND

NOTES TO FINANCIAL STATEMENTS

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Property and Depreciation

Property and equipment are recorded at original cost. Additions, improvements or major renewals are capitalized. If the assets are sold, retired or otherwise disposed of in the ordinary course of business, the cost plus removal costs less salvage, is charged to accumulated depreciation. Any gains or losses on non-telecommunications property and equipment retirements are reflected currently in operations.

The Fund includes in its telecommunications plant account an average cost of debt used for the construction of the plant. Interest expense capitalized in 2005 and 2004, net of interest income of \$11,565 and \$52,630, respectively, earned on funds borrowed for specific construction projects, was \$278,031 and \$261,833, respectively.

Depreciation is computed using the straight-line method based on estimated service or remaining useful lives of the various classes of depreciable assets. Composite depreciation rates are 8.8% and 10.7% for 2005 and 2004.

Bond Costs

The cost of debt issuance and the bond discount have been capitalized and are being amortized over 20 years.

Revenue Recognition

Revenues are recognized when earned and are based on monthly service charges to customers.

Income Taxes

The City of Windom - Telecommunications Fund is an enterprise fund of the City of Windom and as such is exempt from income taxes; therefore, the financial statements do not include a provision for income taxes.

Net Assets

Net Assets are classified into three components, defined as follows:

Invested in capital assets, net of related debt – This component of net assets consists of capital assets, including restricted capital assets, net of accumulated depreciation and reduced by the outstanding balances of any bond, mortgages, notes, or other borrowings that are attributable to the acquisition, construction, or improvement of those assets. If there are significant unspent related debt proceeds at year end, the portion of the debt attributable to the unspent proceeds are not included in the calculation of invested in capital assets, net of related debt. Rather, that portion of the debt is included in the same net asset component as the unspent proceeds.

Restricted net assets – This component of net assets consists of constraints placed on net assets use through external restrictions imposed by creditors (such as through debt covenants), grantors, contributors, or laws or regulations of other governments, or restrictions imposed by law through constitutional provisions or enabling legislation.

Unrestricted net assets – This component of net assets consists on net assets that do not meet the definition of "restricted net assets" or "invested in capital assets, net of related debt."

Reclassifications

Certain amounts in the 2004 financial statements have been reclassified to conform with the 2005 presentation. These reclassifications had no effect on net assets or the change in net assets.

CITY OF WINDOM - TELECOMMUNICATIONS FUND

NOTES TO FINANCIAL STATEMENTS

NOTE 2 - CASH AND INVESTMENTS

Minnesota statutes authorize the Fund to invest in the following:

1. In governmental bonds, notes, bills, mortgages, and other securities, which are direct obligations or are guaranteed or insured issues of the United States, its agencies, its instrumentalities, or organizations created by an act of congress.
2. In shares of an investment company (mutual funds) registered under the Federal Investment Company Act of 1940, whose shares are registered under the Federal Securities Act of 1933, whose only investments are in securities described above, whose fund was rated in one of the two highest risk rating categories by at least one nationally recognized statistical rating organization, and that only invests in financial instruments with a final maturity no longer than 13 months.
3. In any security which is a general obligation of the State of Minnesota, any of its municipalities with taxing powers, or a general obligation of the Minnesota Housing Finance Agency which are rated "A" or better by a national bond rating service.
4. In bankers acceptances of United States Banks eligible for purchase by the Federal Reserve System.
5. In commercial paper issued by United States corporations or their Canadian subsidiaries that is rated in the highest quality by at least two nationally recognized rating agencies and matures in 270 days or less.
6. In time deposits fully insured by the Federal Deposit Insurance Corporation.
7. Mortgage-backed securities that are direct obligations or guaranteed or insured issues of the United States, its agencies, its instrumentalities, or organizations created by an act of Congress. These securities shall not be "High Risk" as defined in Minnesota Statutes.

The Fund's cash is categorized as follows:

Investments	Maturities	2005	2004
Savings Account	Daily	\$ 241,332	\$ 4,257,363

Interest Rate Risk:

The Fund does not have a formal investment policy that limits investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates.

Credit Risks:

The Fund has no formal policy regarding credit risk or limits the amount that can be invested in any one issuer.

Concentration of Credit Risk:

The Fund has no formal policy which limits the amount that can be invested in any one issuer. At December 31, 2005, the Fund did not have any significant concentration of credit risk.

CITY OF WINDOM - TELECOMMUNICATIONS FUND

NOTES TO FINANCIAL STATEMENTS

NOTE 2 - CASH AND INVESTMENTS (Continued)

The City of Windom follows the practice of aggregating the cash assets of various funds to maximize cash management efficiency and returns. Cash restricted for construction, the bond reserve, and debt service are not included in the aggregated cash assets of various funds. As of December 31, 2005 and 2004, the Fund has general cash overdrafts of pooled city funds of \$400,294 and \$357,033.

At December 31, 2005 and 2004, all of the City of Windom - Telecommunications Fund's cash deposits were covered by federal depository insurance or by pledged collateral held by the bank's agent in the City's name in amounts equal to at least 110% of the amount in excess of the federal depository insurance, as required by Minnesota statute.

Restricted Investments are those designated by loan covenants for specific purposes. At December 31, 2005 and 2004, investments consisted of the following:

	<u>2005</u>	<u>2004</u>
Restricted Investment Securities:		
Debt Service Reserve - Funds Designated by Bond Covenants	\$ 241,332	\$ 337,864
Bond Reserve - Funds Designated by Bond Covenants for the Payment of Interest and Principal	-	650,000
Construction Reserve - Funds Designated from Bond Proceeds to be Used to Fund Construction	-	<u>3,269,499</u>
Total Restricted Investment Securities	<u>\$ 241,332</u>	<u>\$ 4,257,363</u>

The restricted cash investments are designated by the 2004 revenue bond issuance which requires that a bond reserve fund and a debt service fund be established, and that the remaining proceeds of the bond issuance be set up in a separate construction account to be disbursed for approved construction costs. In 2005, the Construction Reserve was used to complete construction projects, and the balance in the Bonds Reserve was used for interest payments as designated in the bond agreement.

NOTE 3 - PROPERTY AND EQUIPMENT

Activities for property and equipment that are capitalized by the Fund are as follows:

		<u>2005</u>			
	<u>Years of Estimated Life</u>	<u>Beginning Balance</u>	<u>Additions</u>	<u>Retirements/ Adjustments</u>	<u>Ending Balance</u>
Vehicles	5	\$ 67,803	\$ 30,259	\$ (40,476)	\$ 57,586
Tools and Equipment	7-12	41,963	39,216	(463)	80,716
Furniture and Fixtures	7	30,249		(19,720)	10,529
General Purpose Computer	3	65,015	20,857		85,872
Boxes and Converters	8	-	21,007		21,007
Tower	8	31,056			31,056
Building	25-40	628,558	15,745	2,377	646,680
Central Office Equipment	10	-	1,151,332		1,151,332
Circuit Equipment	10	-	2,603,696		2,603,696
Head End Equipment	5-10	151,152	313,670		464,822
Buried Fiber Cable	20	-	4,058,891		4,058,891
Distribution Equipment	25	622,557		(622,557)	-
Internet Equipment	5	-	117,755		117,755
Plant Under Construction	-	<u>5,461,806</u>	<u>(5,461,806)</u>		<u>-</u>
Total Telecommunications Plant		<u>\$ 7,100,159</u>	<u>\$ 2,910,622</u>	<u>\$ (680,839)</u>	<u>\$ 9,329,942</u>

CITY OF WINDOM - TELECOMMUNICATIONS FUND

NOTES TO FINANCIAL STATEMENTS

NOTE 3 - PROPERTY AND EQUIPMENT (Continued)

	Years of Estimated Life	2004			Ending Balance
		Beginning Balance	Additions	Retirements/ Adjustments	
Vehicles	5	\$ 81,578	\$	\$ (13,775)	\$ 67,803
Tools and Equipment	7-12	34,508	7,455		41,963
Furniture and Fixtures	7	26,149	4,100		30,249
General Purpose Computer	3	—	65,015		65,015
Tower	8	—	31,056		31,056
Building	25-40	50,777	577,781		628,558
Head End Equipment	5-10	151,152			151,152
Distribution Equipment	25	621,615	942		622,557
Plant Under Construction	—	—	5,461,806		5,461,806
Total Telecommunications Plant		<u>\$ 965,779</u>	<u>\$ 6,148,155</u>	<u>\$ (13,775)</u>	<u>\$ 7,100,159</u>

NOTE 4 - LINE OF CREDIT

As of December 31, 2005, the Fund has an operating line of credit from the Bank Midwest, Minnesota Iowa, N.A. The Fund can borrow up to \$1,000,000 at an interest rate of 6.5%. The line of credit is due on August 16, 2006. The balance outstanding on this line of credit at December 31, 2005 was \$1,000,000.

NOTE 5 - LONG-TERM DEBT

Long-term debt as of December 31, 2005 and 2004 are as follows:

Description of Issue	Interest Rate	Issue Date	Final Maturity	Original Issue	Principal
Communications System Revenue Bonds, Series 2004	4.50% - 6.25%	June 1, 2004	August 2024	\$ 9,470,000	<u>\$ 9,470,000</u>

The summary of long-term debt activity for the years ended December 31, 2005 and 2004 is as follows:

	2005			
	Beginning Balance	Additions	Retirements	Ending Balance
Communications System Revenue Bonds, Series 2005	<u>\$ 9,470,000</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ 9,470,000</u>
	2004			
	Beginning Balance	Additions	Retirements	Ending Balance
Communications System Revenue Bonds, Series 2004	<u>\$ —</u>	<u>\$ 9,470,000</u>	<u>\$ —</u>	<u>\$ 9,470,000</u>

CITY OF WINDOM - TELECOMMUNICATIONS FUND

NOTES TO FINANCIAL STATEMENTS

NOTE 5 - LONG-TERM DEBT (Continued)

The Communications System Revenue Bonds were issued by the City of Windom, Minnesota in 2004. The proceeds were used to provide financing for the cost of constructing telecommunications facilities in the City of Windom. The Bonds are payable solely from the gross revenues of the Telecommunications Fund and are not a general obligation of the City of Windom, Minnesota. Interest is payable on February 1 and July 1 of each year beginning in 2005. The Bonds begin to mature in August 1, 2009 and are secured by the revenues of the Telecommunications Fund.

The Communications System Revenues Bonds require the City of Windom - Telecommunications Fund to credit proceeds from the sale of the Bonds in the amount of \$650,000 to the Bond Reserve Account which is to be used only when the funds in the Debt Service Account are insufficient to pay principal and interest on the Bonds. The Bond Reserve Account was used in 2005 to pay the interest payments on the bond and was not funded as of December 31, 2005.

Immediately prior to each interest payment date, the Fund shall transfer to the Debt Service Account amounts of net revenues for payment of all interest and principal then due on the Bonds. The Debt Service Account will be used only for payment of principal and interest on the Bonds.

The annual amounts due for principal and future interest are as follows:

	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
Year Ended December 31:			
2006	\$ -	\$ 579,196	\$ 579,196
2007	-	579,196	579,196
2008	-	579,196	579,196
2009	50,000	579,196	629,196
2010	100,000	576,946	676,946
2011 - 2015	1,365,000	2,748,592	4,113,592
2016 - 2020	2,640,000	2,189,688	4,829,688
2021 - 2024	<u>5,315,000</u>	<u>1,066,876</u>	<u>6,381,876</u>
	<u>\$ 9,470,000</u>	<u>\$ 8,898,886</u>	<u>\$ 18,368,886</u>

NOTE 6 - EMPLOYEE PENSION AND BENEFITS

All full-time and certain part-time employees of the City of Windom - Telecommunications Fund are covered by a defined benefit pension plan administered by the Public Employees Retirement Association of Minnesota (PERA). This is a cost sharing multiple employer retirement plan which provides retirement, disability and death benefits established by State statute. Minnesota statutes also set rates for employer and employee contributions which were 5.10% for employees and 5.53% for employers under the coordinated plan.

The payroll for employees covered by PERA plans for the years ended December 31, 2005 and 2004, was \$286,480 and \$113,548. Employee contributions for 2005 and 2004 were \$14,599 and \$5,791, and the Fund's contributions were \$15,830 and \$6,278 for 2005 and 2004. Additional information about PERA is available in its June 30, 2005 Comprehensive Annual Financial Report.

CITY OF WINDOM - TELECOMMUNICATIONS FUND

NOTES TO FINANCIAL STATEMENTS

NOTE 7 - RELATED PARTY TRANSACTIONS

In 2005 and 2004, the City of Windom provided services including labor and overheads for City personnel working for the Telecommunications Fund in the amount of \$373,788 and \$186,402. The City of Windom – Electric Fund does the billing for the Telecommunications Fund's customers and remits the billed revenue to the Fund monthly.

NOTE 8 - RISK MANAGEMENT

The Fund is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. During the year ended December 31, 2005, the Fund managed its risks as follows:

Public Entity Risk Pool:

The Fund is a member of the League of Minnesota Cities Insurance Trust (LMCIT), a public entity risk pool currently operating as a common risk management and insurance program for Minnesota local government entities. The agreement for formation of the LMCIT provides that the pool will be self-sustaining through member premiums and will reinsure through commercial companies for claims in excess of reserved amounts for each insured event. Settled claims resulting from these risks have not exceeded commercial insurance coverage in any of the past three fiscal years.

The pooling agreement allows for the pool to make additional assessments to make the pool self-sustaining. The Fund has determined that it is not possible to estimate the amount of such additional assessments; however, they are not expected to be material to the financial statements taken as a whole. The Fund pays an annual premium to the pool to provide coverage of risks related to property, automobiles, theft, general liability, worker's compensation, employee liability and employee benefits and errors and omissions.

NOTE 9 - LIQUIDITY AND CAPITAL RESOURCES

In 2004, the Fund began construction on a network to provide telephone, internet and CATV service to its customers in the City of Windom. During 2005 and 2004, the Fund used net bond proceeds of \$9,214,747 for the construction of its communications facilities. In addition, the Fund has utilized a line of credit of \$1,000,000 from a local bank and pooled cash advances from other funds of the City to finance its operating activities to date. Additional funding will be needed to finance future operations until the Fund reaches positive cash flow from its operations. The current line of credit of \$1,000,000 is payable in full in August 2006. Presently, the Fund does not have the resources to pay off the line of credit when it is due. The Fund is considering extending the line of credit and utilizing additional cash advances from other funds to finance its operating losses for the next year.

The Fund began providing telecommunications and internet services in late 2005 and is in the process of building its customer base. With additional customers and reduced expenditures for CLEC start-up costs, the Fund expects improvement in operating cash flow and a move toward more profitable operations.