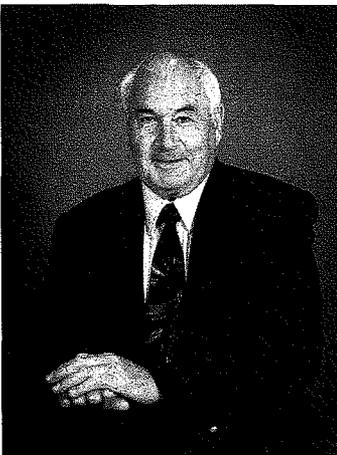


04 - 0251

“The best way to predict the future is to create it.”

Highlights of this report:

- Earning the Right to be Heard; Executive Director Letter— Page 2
- Hazard Mitigation Planning Underway — Page 3
- New HRDC Partnership with Beltrami HRA — Page 4
- Red Lake Reservation Develops Pavement Management System — Page 5
- Knowledge Clusters Used for Competitive Advantage — Page 6
- HRDC Initiates JOBZ Proposal — Page 7

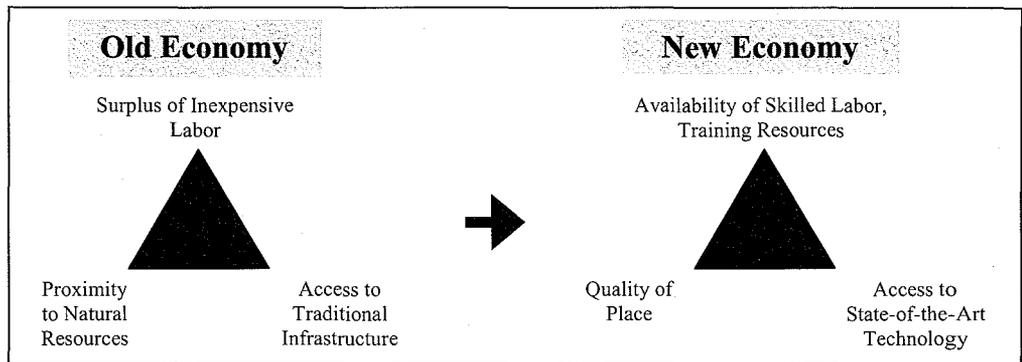


Quentin Fairbanks, HRDC Chairman

HRDC 2003 Annual Report

Compete or Retreat — HRDC Challenges Region to Act on its Future

In the words of Yogi Berra, “the future ain’t what it used to be.” In fact, things are changing so rapidly, it is hard just to keep up with the present. Despite that, the HRDC has spent much of the past year challenging the Region, its communities and businesses, to not only think about the future, but act on it.



Recent demographic and economic shifts have changed the whole nature of how communities and businesses compete in the future. Gone are the days when economic development was all about cheap labor, traditional infrastructure and abundant natural resources. Economic development now is much more complex, and it includes not only those things, but quality of life, knowledge and skills, technology and other new economic factors.

Two of the key trends that are changing the nature of economic development in the Headwaters Region are:

- *Demographic Change.* While the Region’s population is growing (rather rapidly in some areas), the number of persons in some age groups is declining. The Region will see a dramatic decline in student age population, which will have a tremendous impact on communities. Even

(See Compete or Retreat continued on page 7)

Chairman’s Letter

Conversations these days are preoccupied with recession, deflation, budget cuts, and layoffs. Everyone is concerned, but I’m pleased to say that the Headwaters Regional Development Commission is poised to do something about it. The critical services offered by the staff have never been so needed. Their expertise and commitment provide the most efficient delivery of services that continue to strengthen the long-term social, economic, and environmental health of our area of the state.

Our staff is leading the Region’s participation in the Job Opportunity Building Zones (JOBZ) program and in numerous housing initiatives. With careful planning, these efforts will lift skill levels and provide economic opportunities that will attract and retain workers and businesses in the Region.

The Commission is to be commended on its past and present leadership role. Without the leadership that the Commission provides, along with cooperation from the staff, none of the HRDC’s successes would be possible.

Building Organizational and Community Capacity

Broad Community Initiatives Added to the Mix



HRDC activities in this area are in evolution, reflecting our changing understanding of what it will take to realize success for our Region. While our traditional organizational development efforts continue, we are increasingly directing our energies at the broader community. The premise underlying all of these efforts is straightforward: the HRDC can only be successful if other organizations and the Region are successful, and that capacity building is often a key to that success.

During the past year the HRDC has helped the following organizations with strategic planning efforts: *The Bemidji Area Joint Economic Development Commission (JEDC)*, *Northwoods Interfaith Volunteer Caregivers (NICE)*, *the newly-formed Beltrami County*

Lakes and Rivers Association (CLARA), and *the Park Rapids Economic Development Authority (EDA)*. Some of these efforts have been completed, while others are still in progress.

The HRDC also launched several ambitious efforts in communities throughout the Region to help those communities think about the future, and to find ways to make progress on important initiatives. The lead article in this report (see front page) provides detail on this effort.

From The Executive Director

Cliff Tweedale

"Earning the right to be heard" is a phrase I really like, one that applies to organizations as well as individuals. It implies that credibility is borne out of commitment and hard work. The HRDC works hard to earn that right every year, as we listen carefully to our customers, and then help them address their most important priorities.

In this report you will find a sample of the dozens of projects and activities the HRDC has undertaken this past year, activities that have touched every corner of the Headwaters Region. Houses built, loans made, development and planning projects completed -- all of these activities and more, have been completed by the HRDC in partnership with its customers over the last 12 months. Our customers should be proud of their achievements.

As we continually earn the right to be heard, this is the message we want to share: there is more to a successful community than a string of successful projects. Becoming a successful community requires a clear understanding of the existing social and economic environment, a broad definition of community that blurs jurisdictional lines, the development of a

leadership structure that involves all sectors of the community, and broad agreement on a vision for the future. Without all of these components, communities cannot sustain the commitment needed for success. The lead article illustrates our focus on successful communities.

The HRDC will continue its commitment to the Region's bread and butter issues -- neighborhood and housing improvement, natural resource management, transportation improvements, business financing and economic development planning -- but we also have a sustaining commitment to successful community development in its broadest sense.

Our ambition is no less than this: to help our communities prosper by deriving competitive advantage from broad-based, effective leadership structures and a clear vision for the future. We will then celebrate successful communities as well as successful projects.

"As we continually earn the right to be heard, this is the message we want to share... Becoming a successful community requires a clear understanding of the existing social and economic environment, a broad definition of community that blurs jurisdictional lines, the development of a leadership structure that involves all sectors of the community, and broad agreement on a vision for the future."

Managing Our Resources

Counties Plan for Hazard Mitigation Activities

Working under a pair of grants from the Minnesota Department of Public Safety, the HRDC is helping the Region's Emergency Management Directors develop an all-hazard mitigation plan for each county. A task force, made up of local law enforcement, fire department, emergency medical services, SWCD, county and city public works, planning and zoning, and GIS personnel is providing technical guidance for each plan.

An All-Hazard Mitigation Plan opens the door for federal assistance on local projects that are designed to reduce the impacts of future disasters. Project ideas could include improving drainage infrastructure, securing hazardous wastes, or providing Fire Wise training. As this report goes to press, a socio-economic profile and hazard history

have been developed for each county. From this profile, an initial assessment of potential magnitude and frequency of each of 22 human, natural and technological disasters will be made. When complete, the plan will have identified three or four key hazards in each county and ways to reduce the risk of damages or injury.

After the local task force has identified the key hazards and completed an analysis of each, the public will be invited to review and comment on the draft information. Using these comments, the task force will develop strategies for mitigating each of the key hazards. Final approval will be granted by the County and State Department of Public Safety.

Clearwater County Local Water Plan Addresses Priority Issues

HRDC and Clearwater SWCD staff worked with a task force of local residents and water resource professionals over the past year to identify strategies that will improve water quality in Clearwater County. County-wide strategies seek to fine tune the County's response to development impacts and deal with the spread of invasive weeds. Other strategies deal with issues specific to individual watersheds. The plan is currently undergoing a mandatory review process before official adoption.



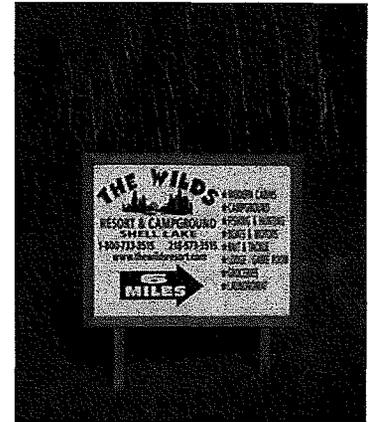
Lake of the Woods County Modifies State Wetland Rules with Local Plan

"One size does not fit all" is the theme behind county wetland planning efforts. While state regulations provide a foundation for local wetland management, they are not tailored to address unique local circumstances and local values. Lake of the Woods County has recently completed its own wetland planning effort to address this shortcoming.

The resulting plan and ordinance, now under review by the state, treats different wetland

types differently, based on local judgments about wetland importance. It also provides a much broader range of options when mitigation is required.

The HRDC, in partnership with the Lake of the Woods SWCD, provided staff support in this year long effort.



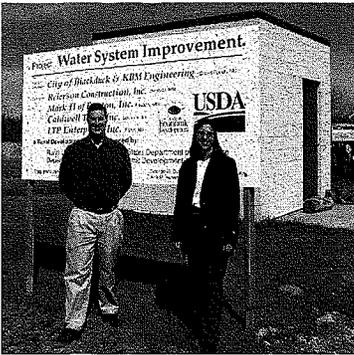
A County-sponsored committee determined, with HRDC assistance, that smaller, attractive signs can be just as effective as larger signs in many Hubbard County locations. Their review helped to form a new county-wide sign ordinance that was recently adopted by the County Board.

Other Activities

- Assisted Hubbard County in the creation of a county-wide sign ordinance.
- Provided technical assistance for flood recovery across the region.
- Began working with Lake of the Woods County to develop a ditch management program.
- Started a strategic planning process for a new coalition of Lake and River Associations in Beltrami County.

Improving Infrastructure and Communities

Small Cities Development Program Supports Community Development Efforts



Pat Armon, Minnesota Department of Employment and Economic Development, and Marcia Larson, Blackduck City Administrator, in front of the Blackduck Water System Improvement site.

"The Northwest Minnesota Foundation shares with the HRDC a belief that affordable housing is a critical component of our quality of place. The NMF has supported many of the HRDC's housing activities because the organization has been very effective in helping communities meet their housing challenges."

— John S. Ostrom, President, Northwest Minnesota Foundation

One of the objectives of the HRDC's community development activities is to assist local customers package resources needed to satisfy local housing and infrastructure needs. One of those resources is the Small Cities Development Program administered by the Minnesota Department of Employment and Economic Development. This past year HRDC staff helped the City of Bemidji administer a neighborhood improvement project which included housing rehabilitation and gap financing needed to make new single-family housing affordable to moderate income buyers. HRDC staff also helped the City of Blackduck administer SCDP funds awarded as

part of a new water storage, treatment and collection system. Finally, staff assisted the City of Shevlin secure SCDP funds as part of a multi-community sanitary sewer collection and treatment project. HRDC staff teamed with the Clearwater Economic Development Organization (CEDO) in the preparation of the competitive application. CEDO will administer the grant funds on behalf of Shevlin and its partners.

These projects received more than \$1.3 million in SCDP funds, and leveraged more than \$4.25 million in other resources, all directed toward helping these communities meet their most pressing community development needs.

Partnership with Beltrami County HRA Formalized

The HRDC has worked closely with the Beltrami County HRA in the promotion of affordable housing for a number of years. Beginning January 1, 2003, the HRDC began providing formalized staff support for all facets of the HRA's operations. Two major HRA initiatives include administration of the Beltrami County Down Payment Assistance

Program and investigation of potential reuse of the old Bemidji High School complex.

This relationship is supported financially by Beltrami County, and also the Northwest Minnesota Foundation which would like to see similar increases in the capacity to deliver affordable housing throughout the Region.

Affordable Mortgage Financing Obtained for the Region

One of the key challenges that must be faced to help families attain home ownership is affordable long-term financing. Toward that end, the HRDC has helped local governments and interested financial institutions obtain low interest rate financing available on an application basis from the Minnesota Housing Finance Agency. Beltrami, Clearwater, Hubbard, and Lake of the Woods Counties, and the City of Mahanomen received a total

allocation of more than \$1.3 million in the Agency's 2003 Minnesota City Participation Program. In addition, a Bemidji area lender consortium obtained \$720,000 in Community Activity Set Aside Program mortgage funds in support of newly constructed affordable homes. This \$2 million will enable approximately 20 moderate income families to achieve their dream of home ownership.

HHDC Uses New Construction Models to Build Homes in the Region

The Headwaters Housing Development Corporation (HHDC) began its construction activities in 1999 by working with school construction programs in Mahanomen and Bemidji. Since that time, these programs have built 20 houses for low and moderate income households.

Over time the HHDC has developed additional projects using different models of construction and working with a variety of builders, including contractors and Building

Trades Unions. As a result, an additional eight houses have been built — six new construction and two homes that were donated to the HHDC and completely rehabilitated.

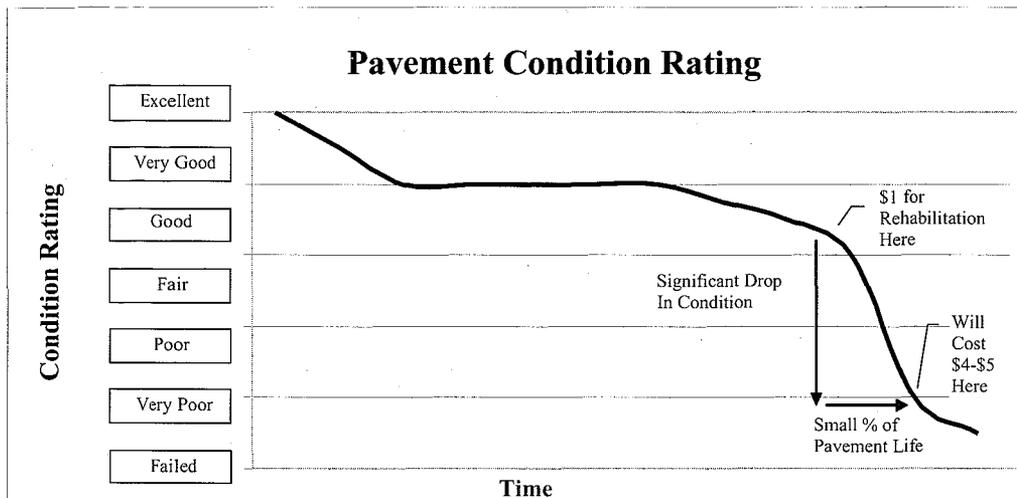
A new construction program has also been created in Red Lake in conjunction with the Northwest Technical College—Red Lake. One house will be built by the college during the 2003-2004 school year. The HHDC is also working to develop new projects in communities where it presently is not building.

Improving Infrastructure and Communities

HRDC Assists Red Lake Reservation in Creating a Pavement Management System

The HRDC is assisting the Red Lake Reservation Transportation Department develop a Pavement Management System. Using sophisticated software, the Transportation Department will be able to assess the current condition of its roads and

then predict when various sections of pavement will deteriorate to the point that they need to be repaired or replaced. The accompanying graph illustrates how improved systems can result in significant cost savings for the Red Lake Reservation.



Key Transportation Activities Completed

• Chippewa National Forest

Staff worked with several agencies to conduct a long term study of the supply and demand for aggregate resources in and near the Chippewa National Forest. Forest managers hope the study will provide some direction on future forest policy regarding gravel sales. This study will conclude in the summer of 2003.

• Canadian National Rail Corridor Safety

A study designed to improve the safety of roadway crossings along the Canadian National Rail corridor in Lake of the Woods and Roseau Counties started with on-site inspections of each crossing. Recommended safety improvements are being reviewed with local residents and will result in a long-term improvement plan by December 2003.

• Walker Transportation Action Model

Several key transportation linkages between our Region and the Twin Cities run through the Walker area. HRDC staff worked with

community residents to define future improvements to the area's transportation network that will help preserve traffic flow and community character.



Members of the Walker Task Force celebrate the completion of the Walker TAM.

Other HRDC Community

Improvement Activities

- Completed permanent addressing for the City of Gonvick and the Red Lake Reservation.
- Provided annexation information for the City of Baudette.
- Helped resolve Laporte sewer and water project financial issues.
- Completed a household survey and provided housing assistance for Gonvick.
- Provided assistance to Bagley housing leadership group.
- Helped with revision to the Bemidji Shoreland Management Ordinance.
- Provided leadership in the area of housing through the Northwest Minnesota Housing Coalition.
- Co-sponsored Census Data Center/Census 2000 workshop.
- Conducted Mahnomon County flood survey analysis.
- Addressed Helga Township subdivision issues.
- Helped Baudette explore demolition financing options.
- Helped plan Indian Housing Conference.
- Coordinated Lake Country Scenic Byway resource enhancement efforts.
- Conducted workshop to train local groups about the federal Transportation Enhancement grant application process.
- Helped the Area Transportation Partnership develop a policy guide document.
- Worked with MN/DOT to conduct Access Management Workshop for our region.

Improving the Economy

HRDC Looks to Use Knowledge Clusters to Help Region Compete

Historically, the economy in the Headwaters Region has been focused on its natural resources. Now, the economy in the Region, just like the nation's economy, is becoming increasingly knowledge-based. In the new, emerging economy, people and knowledge are determining the winners and losers.

Understanding this, the HRDC recently entered into a partnership with the Northwest Technical College, Northwest Minnesota Foundation, and the Minnesota Department of Employment and Economic Development to identify and capitalize on competitive

advantages in the Region based on its people, their skills, and unique knowledge. Once the Region has identified the clusters of knowledge and skills that set it apart from other areas, the partners will begin to develop strategies that seek to build upon the innovation and competitiveness of the Region and its existing industries, and then market the Region to prospective workers and businesses.

The project will continue into 2004, with strategies being implemented over an extended period.

HRDC Responds to Business Flood Victims

In the summer of 2002, much of the Headwaters Region experienced unprecedented flooding, particularly in Mahnommen, Clearwater, and Lake of the Woods Counties. Roads and bridges were damaged, homes destroyed, and public infrastructure overwhelmed.

The HRDC responded quickly to the needs of its customers. One of the key areas of focus for the HRDC was the Region's flood-affected businesses. Many experienced direct and indirect impact, including physical damage, loss of income and rising accounts receivable.

In response, the HRDC created a Disaster Revolving Loan Fund (DRLF). Funding for the DRLF came from the Minnesota Department of Employment and Economic Development (DEED) and the HRDC. All total, \$950,000 was raised to make flexible, low-interest loans to the Region's flood-affected businesses.

The Royal Dutchman Resort/Motel, near Baudette, was purchased by Doug and Marilyn Rainforth two weeks prior to the flood. During the flood, the Royal Dutchman lost a significant amount of river frontage and the resort's septic system was compromised. The future for the resort looked dismal, at best, and it appeared as though the Rainforths would lose their investment in the business. The DRLF allowed the HRDC to provide funding to the Royal Dutchman to help them purchase property that would allow space for a new septic system and create new opportunities for the business. "The financing not only allows us to continue our business for many years, but has greatly increased the value of our business. Many thanks to Susan Hoosier and the Headwaters organization for their support!" said Doug and Marilyn Rainforth.

Many thanks go to DEED for their support for our Region!

Summary of Revolving Loan Activity 2002/2003

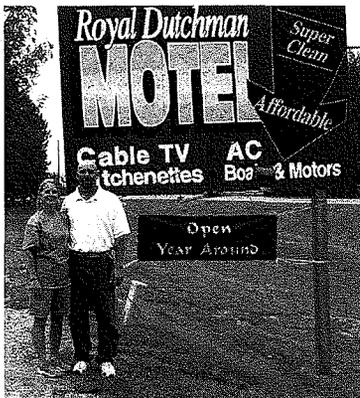
The HRDC has been making loans to businesses in the Region for 23 years. The HRDC's finance arm is the Headwaters Regional Finance Corporation. Active loans are spread throughout the Region and are represented in each county as follows:

Beltrami County	
Northern Beltrami	8%
Southern Beltrami	32%
Hubbard County	12%
Clearwater County	13%
Lake of the Woods County	14%
Mahnommen County	21%

Over the past 12 months, the HRFC has financed the following projects:

- *Clearwater Co.: DMRK Ventures, Inc. — \$198,092 — purchase of an existing business.*
- *Beltrami Co.: BAK, LTD/Robert Kiewatt — \$77,678 — purchase of an existing business.*
- *Mahnommen Co.: Waubun Steel — \$75,000; and Mahnommen Country Club — \$22,500; flood relief.*
- *Lake of the Woods Co.: Rosalie's Restaurant, — \$70,000; Border View Lodge — \$100,000; and Royal Dutchman Resort — \$80,000; flood relief.*

Additionally, funds have been committed, but not disbursed, for projects totaling \$855,000. Of the committed funds, \$605,000 are flood-related.



"The financing not only allows us to continue our business for many years, but has greatly increased the value of our business. Many thanks to Susan Hoosier and the Headwaters organization for their support!"
 — Doug and Marilyn Rainforth
 Royal Dutchman Resort



Flooding in 2003 caused significant damage in the Headwaters Region.

Improving the Economy

HRDC to Lead Regional JOBZ Initiative

During the past legislative session the Legislature passed the Job Opportunities Building Zones (JOBZ) program, which will create ten tax free zones in Minnesota. The zones are designed to generate private investment and job creation in the state's most distressed areas. Businesses and income generated within the zones will be exempt from virtually all state and local taxes.

The HRDC is leading the development of an application for JOBZ designation in the Headwaters Region. An application will be submitted in the fall, with designation by the Commissioner of the Department of Employment and Economic Development in December 2003. Tax free designation will take effect in 2004.

(Compete or Retreat continued from page 1)

more dramatic will be the continued labor force shortage, which is projected to peak in 2015.

- *The New Economy.* A new economy is emerging that puts a premium on knowledge and skills, access to advanced technology and a region's quality of life. Today, more than ever before, people and businesses can locate anywhere they choose, creating both threats and opportunities for rural areas.

If the rules of the game are changing, how we compete needs to change as well. In light of that, the HRDC has been challenging the Region to understand the changes, be candid about its current situation, and effectively position itself to compete in the future.

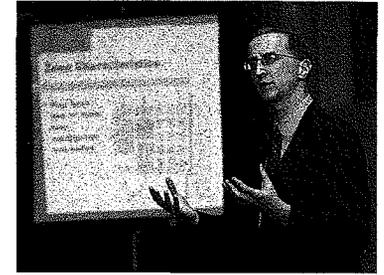
How? With funding from the Northwest Minnesota Foundation, the HRDC has hosted a number of community meetings throughout the Region, where the trends and their implications were discussed. In follow-up activities, the HRDC is helping many of these

same communities respond to the challenge by facilitating strategic positioning efforts.

Leadership Quick Takes

One of the more innovative ways the HRDC is both informing and challenging the Region is through an effort called "Leadership Quick Takes." Leadership Quick Takes utilize e-mail and the internet to provide in-depth analysis of the trends and changes, identification of successful efforts in other areas, and opportunities for further discussion.

Every three weeks, 600 of the Region's leaders receive an e-mail from the HRDC identifying a key element of future economic and community success. If the recipient is interested, they can link to the HRDC's website, where the topic is discussed further, and there is opportunity to comment or question HRDC staff. If you have an interest in receiving the Leadership Quick Takes e-mails, send an e-mail to hrdc@hrdc.org.



Matt Kramer, Commissioner of the Minnesota Department of Employment and Economic Development (DEED) discusses the State's newest rural development initiative, JOBZ.

(Photo courtesy of the Bemidji Pioneer)

Operational Budget

Revenues	2003	2004	Expenditures	2003	2004
	Actual	Budget		Actual	Budget
Tax Levy	204,528	\$ 205,631	Personnel/Staffing Capacity	\$ 604,485	\$ 615,221
Long Term Contracts	96,702	100,000	Operating Expenditures	161,935	103,577
Shorter Term Contracts	375,968	253,387	Investment Expenditures	21,376	29,500
Beltrami HRA Services	11,177	17,500	Fund Balance Reserve	<u>89,562</u>	<u>20,000</u>
HHDC	94,369	77,000			
HRFC	69,584	70,000	Total Expenditures	\$ 877,358	\$ 768,298
Other Sources	25,030	3,000			
Other Contracts	<u>0</u>	<u>41,780</u>			
Total Revenues	\$ 877,358	\$ 768,298			

The 2003 figures shown above are unaudited figures. The latest audit, covering Fiscal Year 2002 finances, was performed by Miller, McDonald, Erickson and Moller, Ltd., Certified Public Accountants, and dated October 25, 2002. An unqualified report was issued.

HRDC 2003 Annual Report

Headwaters Regional Development
Commission
403 Fourth Street NW
P.O. Box 906
Bemidji, MN 56619-0906
Phone: 218-444-HRDC (4732)
Fax: 218-444-4722
Email: hrdc@hrdc.org
Website: www.hrdc.org

HRDC Staff

Cliff Tweedale
Executive Director

Tim Flathers
Community Development
Director

Joe Czapiewski
Physical Planner

David Hengel
Economic Development Director

Susan Hoosier
Business Loan Specialist

Anne Sand
Housing Specialist

Tony Mayer
Technical Planner

Joan Randt
Office Manager

Mary Thompson
Financial Officer

Leslie Bartels
Secretary/Receptionist

Nancy Brown
Intern

HRDC Members

Lawrence Anderson — Beltrami Small Cities
Steve Beltz — Clearwater Cities
James (Butch) Boe — Clearwater Townships
Kim Bredeson — Lake of the Woods Co.
Mark Edevold — Labor
Quentin Fairbanks, Chair — Red Lake Reservation
Roger Hannigan — Beltrami Townships
Vicki Haugen — Beltrami Co.
Cal Johannsen — Hubbard Co.
Ron Johnson — City of Bemidji
Don Krueger — Agriculture
Lorna LaGue — White Earth Reservation
Jean Nelson — Mahnomen Townships

John A. Nelson — Clearwater Co.
Charles Pazdernik — Mahnomen Co.
Joyce Powell — Hubbard Cities
LeRoy Riewer — Business
Rick Rone, Vice Chair — Lake of the Woods Cities
Tom Ryan — Mahnomen Cities
Frank Schaap, Secretary — School Districts
Greg Smith — Forestry
Duane Splittstoesser — Hubbard Townships
George Swentik — Lake of the Woods Co.
Emmet Weidenborner — School Districts
Victoria White, Treasurer — Leech Lake Reservation

Transportation Advisory Committee

Craig Collison
Floyd Frank, Chair
Brian Freeberg
Bruce Hasbargen
Jim Heltzer

Dave Heyer
Mike Kamnikar
Sean McKnight
Brad Monson
Jean Nelson

John Nelson
Curt Oakes
David Olsonawski
Dan Sauve

David Siedschlag
George Swentik
Betty Thomsen
Jim Worester

Headwaters Housing Development Corporation

Tom Ryan
LeRoy Riewer
Rick Rone

Ray Melander
Doug St. Onge

Headwaters Regional Finance Corporation

Rick Rone
Frank Schaap
Terry Matson
Victoria White
Royce Peterson

Quentin Fairbanks
John Masog
Peter Haddeland
Cliff Tweedale



**PRSR STD
US POSTAGE PAID
BEMIDJI MN
PERMIT NO. 13**

403 Fourth Street NW
P.O. Box 906
Bemidji, MN 56619-0906