

CITY OF KALONA

**INDEPENDENT AUDITOR'S REPORT
BASIC FINANCIAL STATEMENTS AND
SUPPLEMENTARY INFORMATION
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
June 30, 2004**

Juli Ochs, CPA

Table of Contents

		<u>Page</u>
Officials		3
Independent Auditor's Report		5-6
Management's Discussion and Analysis		7-12
Basic Financial Statements:		
	<u>Exhibit</u>	
Government-wide Financial Statement:		
Statement of Activities and Net Assets – Cash Basis	A	13-14
Governmental Fund Financial Statements:		
Statement of Cash Receipts, Disbursements and Changes in Cash Balances	B	15-16
Proprietary Fund Financial Statements:		
Statement of Cash Receipts, Disbursements and Changes in Cash Balances	C	17
Notes to Financial Statements		18-23
Required Supplementary Information:		
Budgetary Comparison Schedule of Receipts, Disbursements and Changes in Balances – Budget and Actual (Cash Basis) – All Governmental Funds and Proprietary Funds		25-26
Notes to Required Supplementary Information – Budgetary Reporting		27
Other Supplementary Information	<u>Schedule</u>	
Statement of Cash Receipts, Disbursements and Changes in Cash Balances – Nonmajor Governmental Funds	1	29
Schedule of Indebtedness	2	30-31
Bond and Note maturities	3	32-33
Schedule of Expenditures of Federal Awards	4	34
Independent Auditor's Report on Compliance and on Internal Control Structure over Financial Reporting		35-36
Independent Auditor's Report on Compliance with Requirements Applicable to Each Major Program and Internal Control over Compliance		39-40
Schedule of Findings and Questioned Costs		41-45

City Of Kalona

Officials
(Before July 2004)

<u>Name</u>	<u>Title</u>	<u>Term Expires</u>
Jean M. Gustafson	Mayor	Dec. 2006
Jerry Kauffman	Mayor Pro tem	Dec. 2006
Steve Lafaurie	Council Member	Dec. 2006
Steve Reif	Council Member	Dec. 2005
Ken Herington	Council Member	Dec. 2005
Steve Schlabaugh	Council Member	Dec. 2005
Doug Morgan	City Administrator	Indefinite
Karen Christner	City Clerk	Indefinite

(After July 2004)

<u>Name</u>	<u>Title</u>	<u>Term Expires</u>
Jerry Kauffman	Mayor	Appointed
Ken Herington	Mayor Pro tem	Dec. 2005
Steve Lafaurie	Council Member	Dec. 2006
Steve Reif	Council Member	Dec. 2005
Claudine Miller	Council Member	Appointed
Steve Schlabaugh	Council Member	Dec. 2005
Doug Morgan	City Administrator	Indefinite
Karen Christner	City Clerk	Indefinite

CITY OF KALONA

Juli Ochs, CPA
1344 240th St.
Victor, Iowa 52347
319-647-2295 (Home)

Independent Auditor's Report

To the Honorable Mayor and
Members of the City Council:

I have audited the accompanying financial statements of the governmental activities, the business type activities, each major fund and the aggregate remaining fund information of the City of Kalona, Iowa, as of and for the year ended June 30, 2004. These financial statements are the responsibility of city officials. My responsibility is to express an opinion on these financial statements based on my audit.

I conducted my audit in accordance with generally accepted auditing standards of the United States of America, Chapter 11 of the Code of Iowa and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States. Those standards and provisions require that I 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 officials, as well as evaluating the overall financial statement presentation. I believe that my audit provides a reasonable basis for my opinion.

As described in note 1, these financial statements were prepared on the basis of cash receipts and disbursements, which is a comprehensive basis of accounting other than United States generally accepted accounting principles.

The financial statements referred to above do not include the financial transactions of the Kalona Library Board Foundation, Inc., a component unit of the City of Kalona pertaining to the Trust Funds which should be included to conform with U.S. generally accepted accounting principles.

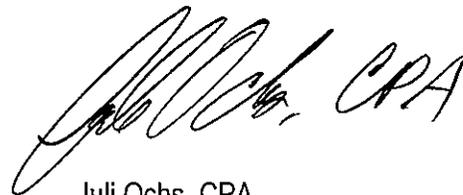
In my opinion, except for the on the financial statements due to the exclusion of the Kalona Library Board Foundation, Inc., from the reporting entity, the financial statements referred to above present fairly, in all material respects, the respective cash basis financial position of the governmental activities, the business type activities, each major fund and the aggregate remaining fund information of the City of Kalona as of June 30, 2004, and the respective changes in cash basis financial position for the year then ended in conformity with the basis of accounting described in Note 1.

As discussed in Note 10, during the year ended June 30, 2004 the City of Kalona adopted Governmental Accounting Standards Board Statement No. 34, Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments; Statement No. 37, Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments: Omnibus; Statement No. 38, Certain Financial Statement Note Disclosures, and Statement No. 41, Budgetary Comparison Schedule – Perspective Differences.

In accordance with Government Auditing Standards, I have also reissued my reports dated April 4, 2006 on my consideration of the City of Kalona's internal control over financial reporting and my tests of its compliance with certain provisions of laws, regulations, and contracts and grants. Those reports are an integral part of an audit performed in accordance with Government Auditing Standards and should be read in conjunction with this report in considering the results of my audit.

Management's Discussion and Analysis and budgetary comparison information on pages 7 through 12 and 25 through 27 are not required parts of the basic financial statements, but are supplementary information required by the Governmental Accounting Standards Board. I applied limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. I did not audit the information and express no opinion on it.

My audit was performed for the purpose of forming an opinion on the aforementioned financial that collectively comprises the City of Kalona's basic financial statements. I previously audited, in accordance with the standards referred to in the second paragraph of this report, the financial statements for the three years ended June 30, 2003 (none of which are presented herein) and expressed qualified opinions on those financial statements. Other supplementary information included in Schedules 1 through 4, including the Schedule of Expenditures of Federal Awards required by U.S. Office of Management and Budget (OMB) Circular A-133, is presented for purposes of additional analysis and is not a required part of the financial statements. Such information has been subjected to the auditing procedures applied in my audit of the aforementioned financial statements and, in my opinion, is fairly stated in all material respects in relation to the aforementioned financial statements taken as a whole.

A handwritten signature in black ink, appearing to read "Juli Ochs, CPA". The signature is fluid and cursive, with the letters "J", "O", and "C" being particularly prominent.

Juli Ochs, CPA

April 4, 2006

City of Kalona

Management's Discussion & Analysis

The City of Kalona provides this Management's Discussion and Analysis of its financial statements. This narrative overview and analysis of the financial activities is for the fiscal year ended June 30, 2004. We encourage readers to consider this information in conjunction with the City's financial statements, which follow.

Because the City is implementing new reporting standards for this fiscal year with significant changes in content and structure, much of the information is not easily comparable to prior years. However, in future years, comparisons will be more meaningful and will go further in explaining the City's financial position and results of operations.

2004 FINANCIAL HIGHLIGHTS

- Revenues of the City increased approximately 6% from fiscal year 2003 to 2004. Bond proceeds were received in 2004 in the amount of \$2,970,000.
- Disbursements of the City increased approximately 40% from fiscal year 2003 to 2004 due to 3 major projects, Water – Sewer – Library Projects.
- The City's total cash basis net assets increased approximately 48% or \$1,840,152 due mainly to funds received to over the 3 projects that were going on during this time. Of this amount, the assets of the governmental activities increased approximately \$1,649,560 and the assets of the business type activities increased by approximately \$190,592.

USING THIS ANNUAL REPORT

The annual report consists of a series of financial statements and other information as follows:

Management's Discussion and Analysis shows basic financial statement and an overview of cash receipts and disbursements. The cash basis of accounting does not take into consideration accounts receivable or accounts payable.

The Government-wide Financial Statement consists of a Statement of Activities and Net Assets. This Statement includes information about the activities of the City as a whole and presents an overall view of the City's finances.

The Fund Financial Statements tell how governmental services were financed in the short term as well as what remains for future spending. Fund financial statements report the City's operations in more detail than the government-wide statement by providing information about the most significant funds.

Notes to financial statements provide additional information essential to a full understanding of the data provided in the basic financial statements.

Required Supplementary Information further explains and supports the financial statements with a comparison of the City's budget for the year.

BASIS OF ACCOUNTING

The City maintains its financial records on the basis of cash receipts and disbursements and the financial statements of the City are prepared on that basis. The cash basis of accounting does not give effect to accounts receivable, accounts payable and accrued items. Accordingly, the financial statements do not present financial position and results of operations of the funds in accordance with U.S. generally accepted accounting principles. Therefore, when reviewing the financial information and discussion within this annual report, the reader should keep in mind the limitations resulting from the use of the cash basis of accounting.

REPORTING THE CITY'S FINANCIAL ACTIVITIES

Government-wide Financial Statement

The Statement of Activities and Net Assets presents the City's net assets. Over time, increases or decreases in the City's net assets may serve as a useful indicator of whether the financial position of the City is improving or declining.

The Statement of Activities and Net Assets is divided into two kinds of activities:

- Governmental Activities include public safety, public works, culture and recreation, general government, debt service, and capital projects. These activities are financed mainly by property taxes and state/federal grants.
- Business Type Activities include the water system, sanitary sewer system, and garbage. Fees charged to the users finance these activities.

Fund Financial Statements

The City has two kinds of funds:

1. Governmental funds account for most of the City's basic services. These focus on how money flows into and out of those funds, and the balances at year-end that are available for spending. The governmental funds include: 1) the General Fund, 2) the Special Revenue Funds, such as Road Use Tax and Urban Renewal Tax Increment, 3) the Debt Service Fund, and 4) the Capital Projects Fund. The governmental fund financial statements provide a detailed, short-term view of the City's general government operations and the basic services it provides. Governmental fund information helps determine whether there are more or fewer financial resources that can be spent in the near future to finance the City's programs.

The required financial statements for governmental funds include a statement of cash receipts, disbursements and changes in cash balances.

2. Proprietary funds account for the City's Enterprise Funds. Enterprise funds are used to report business type activities. The City maintains three Enterprise Funds to provide separate information for the water, sewer and garbage funds, considered to be major funds of the City.

GOVERNMENT-WIDE FINANCIAL ANALYSIS

Net assets may serve over time as a useful indicator of financial position. The City's cash balance for governmental activities increased from \$1,507,304 to \$3,156,864. The analysis focuses on the changes in cash balances for governmental activities

Changes in Cash Basis Net Assets of Governmental Activities

	<u>Year ended June 30,</u>	
	<u>2004</u>	<u>2003</u>
Receipts and transfers:		
Program receipts:		
Charges for services	98,210	91,041
General receipts:		
Property tax	526,053	510,144
Debt Service	53,270	82,160
Local Option Sales Tax	149,992	73,226
Road Use Tax	190,978	186,680
TIF revenues	164,421	116,834
Use of Money and Property	20,085	23,884
Intergovernmental funds	16,340	49,343
Bond proceeds	1,400,000	-
Transfer – In	-	20,468
Short-term debt proceeds	-	-
Other general receipts	4,100	9,378
Total receipts and transfers	\$ 2,623,449	1,163,158
Disbursements and transfers:		
Public safety	132,945	168,156
Public works	146,325	241,998
Culture and recreation	258,119	257,276
Community and economic development	185,098	154,081
General government	96,831	159,330
Debt service	52,866	81,680
Capital projects	101,705	-
Total disbursements and transfers	\$ 973,889	1,062,521
Increase (decrease) in cash basis net assets	1,649,560	100,638
Cash basis net assets beginning of year	1,507,304	1,406,667
Cash basis net assets end of year	\$ 3,156,864	1,507,304

Changes in Cash Basis Net Assets of Business Type Activities

	<u>Year Ended June 30,</u>	
	<u>2004</u>	<u>2003</u>
Receipts:		
Program receipts:		
Charges for services		
Water	329,888	268,581
Sewer	195,147	178,543
Garbage	43,897	43,092
General receipts:		
Other general receipts	3,959	6,037
Bond proceeds	<u>1,382,574</u>	<u>-</u>
Total receipts	1,955,465	496,253
 Disbursements and transfers:		
Water	129,958	126,161
Sewer	91,136	104,844
Garbage	39,779	38,386
Debt Service	123,038	109,783
Capital Projects	1,380,962	139,481
Transfers	<u>-</u>	<u>20,468</u>
Total disbursements and transfers	1,764,873	539,123
 Increase in cash basis net assets	<u>190,592</u>	<u>(42,870)</u>
 Cash basis net assets beginning of year	<u>484,070</u>	<u>526,940</u>
 Cash basis net assets end of year	\$ <u>674,662</u>	<u>484,070</u>

INDIVIDUAL MAJOR GOVERNMENTAL FUND ANALYSIS

As Kalona, Iowa, completed the year, its governmental funds reported a combined fund balance of \$3,831,526, which is an increase of \$1,840,152. Major reasons for changes in balances from fiscal year 2003 are:

- The General Fund continues to receive less money because of budget cuts from the State.
- The Road Use Tax Fund revenue is based on per capita dollars from the state. The rate increased from fiscal year 2003 to fiscal year 2004 therefore revenues increased.
- The Tax Increment Financing Fund revenues increased by \$47,587 in fiscal year 2004. Revenue increase was because of additional increment available to be used to pay towards development agreements formed with the City.
- The Local Option Sales Tax Fund revenues increased by \$76,766 from fiscal year 2003. Revenue increase was due to increased sales activity. Expenditures were approximately the same from fiscal year 2003 to fiscal year 2004.

- The Capital Improvement Fund was the major reason for the increase in the ending fund balance because of revenues received to cover the cost of the impending capital projects the City will be completing in the fiscal year 2005.
- The Debt Service Fund revenues and expenditures were less because of bond debt being paid off.

INDIVIDUAL MAJOR BUSINESS TYPE FUND ANALYSIS

The Water Utility Fund balance increased by \$100,292 from fiscal year 2003 due mainly to increased water rates and usage.

The Sewer Utility Fund balance increased by \$85,899 from fiscal year 2003 due mainly to increased sewer rates and usage.

BUDGETARY HIGHLIGHTS

The City amended its budget on May 17, 2004 resulting in an increase of receipts of approximately \$1,515,699 disbursements of approximately \$1,562,333 related to various projects started in fiscal year 2004.

DEBT ADMINISTRATION

At June 30, 2004, the City had approximately \$3,529,000 in bonds and other long-term debt, compared to approximately \$872,000 last year, as shown below.

Outstanding Debt at Year-End

	<u>Year Ended June 30,</u>	
	<u>2004</u>	<u>2003</u>
General Obligation Corporate Purpose Bonds		
1997 Water Project (refinancing)	40,000	69,625
1997 Pool Project (refinancing)	-	50,373
1997 Water Project	200,000	225,000
1995 Sewer Project (State Revolving Fund)	319,000	590,000
1999 Street Sweeper	-	24,076
2003 Water Project (State Revolving Fund)	1,067,000	-
2003 Sewer Project (State Revolving Fund)	503,000	-
2004 Library Project	<u>1,400,000</u>	<u>-</u>
Total	\$ 3,529,000	710,074

Debt increased as a result of issuing general obligation bonds and state revolving fund financing for a Sewer, Water, and Library Projects.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGET

The City of Kalona's elected and appointed officials considered factors such as tax rates and fees that will be charged for various City activities when they adopted the 2005 budget.

Projects being continued, completed for fiscal year 2005 are:

- Water Tower Project
- Lagoon Repair Project
- Library Project

CONTACTING THE CITY'S FINANCIAL MANAGEMENT

This financial report is designed to provide the citizens, taxpayers, customers, and creditors with a general overview of the City's finances and to show the City's accountability for all money received. If you have questions about this report or need additional information, please contact Douglas W. Morgan, City Administrator, or Karen Christner, City Clerk, at Box 1213, Kalona, Iowa 52247 or call 319-656-2310.

City of Kalona

Statement of Activities and Net Assets - Cash Basis

As of and for the year ending June 30, 2004

	Disbursements	Program Receipts	
		Charges for Service	Operating Grants, Contributions, and Restricted Interest
Functions/Programs:			
Governmental activities:			
Public safety	\$ 132,944	270	-
Public works	146,325	-	190,978
Culture and recreation	258,118	97,617	5,648
Community and economic development	185,098	1,995	-
General government	96,830	6,175	-
Debt service	52,866	-	-
Capital projects	101,705	-	-
Total governmental activities	<u>973,886</u>	<u>106,057</u>	<u>196,626</u>
Business type activities			
Water	1,143,728	329,889	-
Sewer	581,367	195,147	-
Garbage	39,779	43,897	-
Total business type activities	<u>1,764,874</u>	<u>568,933</u>	<u>-</u>
Total	<u>\$ 2,738,760</u>	<u>674,990</u>	<u>196,626</u>

General Receipts:

Property tax levied for:
 General purposes
 Tax increment financing
 Debt service
 Local option sales tax
 Grants and contributions not restricted to a specific purpose
 Unrestricted interest on investments
 Bond proceeds
 Total general receipts and transfers

Change in cash basis net assets

Cash basis net assets beginning of year

Cash Basis Net Assets

Restricted
 Employee Benefits
 Urban renewal projects
 Debt service
 Capital Projects
 Unrestricted
Total cash basis net assets

Capital Grants, Contributions, and Restricted Interest	Net (Disbursements) Receipts and Changes in Cash Basis Net Assets		
	Governmental Activities	Business Type Activities	Total
-	(132,674)	-	(132,674)
-	44,653	-	44,653
-	(154,853)	-	(154,853)
-	(183,103)	-	(183,103)
-	(90,655)	-	(90,655)
-	(52,866)	-	(52,866)
-	(101,705)	-	(101,705)
-	(671,203)	-	(671,203)
-	-	(813,839)	(813,839)
-	-	(386,220)	(386,220)
-	-	4,118	4,118
-	-	(1,195,941)	(1,195,941)
-	(671,203)	(1,195,941)	(1,867,144)
\$	526,056	-	526,056
	164,421	-	164,421
	53,270	-	53,270
	149,992	-	149,992
	16,340	-	16,340
	10,690	3,960	14,650
	1,400,000	1,382,574	2,782,574
	2,320,769	1,386,534	3,707,303
	1,649,566	190,593	1,840,159
	1,507,304	484,069	1,991,373
	3,156,870	674,662	3,831,532
	17,849	-	17,849
	41,555	-	41,555
	139,789	-	139,789
	1,298,295	-	1,298,295
	1,659,382	674,662	2,334,044
\$	3,156,870	674,662	3,831,532

City of Kalona

Statement of Cash Receipts, Disbursements and Changes in Cash Balances

As of and for the year ended June 30, 2004

	General	Special Revenue		
		Road Use Tax	Urban Renewal Tax Increment	Local Option Sales Tax
Receipts:				
Property Tax	\$ 467,813	\$ -	\$ -	\$ -
Tax increment financing collections	-	-	164,421	-
Other City Tax	7,147	-	-	149,992
Use of money and property	19,473	-	-	-
Licenses and permits	2,145	-	-	-
Intergovernmental	21,988	190,978	-	-
Charges for services	88,222	-	-	-
Miscellaneous	6,295	-	-	-
Total Receipts	613,083	190,978	164,421	149,992
Disbursements:				
Operating:				
Public Safety	132,944	-	-	-
Public Works	80,581	54,781	-	-
Health and social services	-	-	-	-
Culture and recreation	234,740	-	-	-
Community and economic development	-	-	154,087	31,011
General government	85,098	-	-	-
Debt service	-	-	-	-
Capital projects	-	-	-	-
Total Disbursements	533,363	54,781	154,087	31,011
Excess (deficiency) of receipts over (under) disbursements	<u>79,720</u>	<u>136,197</u>	<u>10,334</u>	<u>118,981</u>
Other financing sources (uses):				
Bond proceeds:				
General Obligation Bond	-	-	-	-
Total other financing sources (uses)	-	-	-	-
Excess (deficiency) of receipts and other financing sources over (under) disbursements & other financing uses	<u>79,720</u>	<u>136,197</u>	<u>10,334</u>	<u>118,981</u>
Balance beginning of year	1,042,176	230,430	31,221	51,877
Balance end of year	<u>\$ 1,121,896</u>	<u>\$ 366,627</u>	<u>\$ 41,555</u>	<u>\$ 170,858</u>
Cash Basis Fund Balances				
Reserved:				
Debt Service	-	-	-	-
Unreserved:				
General Fund	1,121,896	-	-	-
Special Revenue Funds	-	366,627	41,555	170,858
Capital Project Fund	-	-	-	-
Total cash basis fund balances	<u>1,121,896</u>	<u>366,627</u>	<u>41,555</u>	<u>170,858</u>

Other Nonmajor Governmental Funds	Total
\$ 102,322	\$ 570,135
-	164,421
2,044	159,183
612	20,085
-	2,145
-	212,966
-	88,222
-	6,295
<u>104,978</u>	<u>1,223,452</u>
-	132,944
10,963	146,325
-	-
23,378	258,118
-	185,098
11,732	96,830
52,866	52,866
<u>101,705</u>	<u>101,705</u>
200,644	973,886
<u>(95,666)</u>	<u>249,566</u>
1,400,000	1,400,000
1,400,000	1,400,000
<u>1,304,334</u>	<u>1,649,566</u>
151,600	1,507,304
<u>\$ 1,455,934</u>	<u>\$ 3,156,870</u>
139,789	139,789
-	1,121,896
17,849	596,889
<u>1,298,296</u>	<u>1,298,296</u>
<u>1,455,934</u>	<u>3,156,870</u>

Statement of Cash Receipts, Disbursements and Changes in Cash Balances
Proprietary Funds

As of and for the year ended June 30, 2004

	Enterprise Funds			
	Water	Sewer	Garbage	Total
Receipts:				
License and permits	3,940	4,000	-	7,940
Use of money and property	942	2,735	283	3,960
Charges for services	313,103	191,147	43,897	548,147
Miscellaneous	12,846	-	-	12,846
Total Receipts	330,831	197,882	44,180	572,893
Disbursements:				
Business type activities	1,143,728	581,367	39,779	1,764,874
Total Disbursements	1,143,728	581,367	39,779	1,764,874
Excess (deficiency) of receipts over (under) disbursements	(812,897)	(383,485)	4,401	(1,191,981)
Other financing sources (uses):				
Bond proceeds:				
SRF Loan	913,189	469,385	-	1,382,574
Operating transfers in (out)	-	-	-	-
Total other financing sources (uses)	913,189	469,385	-	1,382,574
Excess (deficiency) of receipts and other financing sources over (under) disbursements & other financing uses	100,292	85,900	4,401	190,593
Balance beginning of year	52,925	376,812	54,332	484,069
Balance end of year	\$ 153,217	\$ 462,712	\$ 58,733	\$ 674,662
Cash Basis Fund Balances				
Unreserved	153,217	462,712	58,733	674,662
Total cash basis fund balances	153,217	462,712	58,733	674,662

City of Kalona

Notes to Financial Statements

June 30, 2004

(1) Summary of Significant Accounting Policies

The City of Kalona is a political subdivision of the State of Iowa located in Washington County. It was first incorporated in 1879 and operates under the Home Rule provisions of the Constitution of Iowa. The City operates under the Mayor-Council form of government with the Mayor and Council Members elected on a non-partisan basis. The City provides numerous services to citizens including public safety, public works, culture, recreation, public improvements and general administrative services.

A. Reporting Entity

For financial reporting purposes, City of Kalona has included all funds, organizations, agencies, boards, commissions and authorities. The City has also considered all potential component units for which it is financially accountable, and other organizations for which the nature and significance of their relationship with the City are such that exclusion would cause the City's financial statements to be misleading or incomplete. The Governmental Accounting Standards Board has set forth criteria to be considered in determining financial accountability. These criteria include appointing a voting majority of an organization's governing body, and (1) the ability of the City to impose its will on that organization or (2) the potential for the organization to provide specific benefits to, or impose specific financial burdens on the City

Excluded Component Unit

The Kalona Library Board Foundation, Inc is a non-profit organization legally separate from the City. The Foundation has been created for the sole purpose of raising funds to support the Kalona Library and has the potential to provide benefits to the City of Kalona Library. The Library Board Foundation is governed by a board not appointed by the Library Board and the Foundation's operating budget is not subject to the approval of the Library Board.

Related Organization

The Friends of the Kalona Library is an organization separate from the City. The Friends has been created for the sole purpose of raising funds to support the Kalona Library but is not financially accountable to the City.

Jointly Governed Organizations

The City also participates in several jointly governed organizations that provide goods or services to the citizenry of the City but do not meet the criteria of a joint venture since there is no ongoing financial interest or responsibility by the participating governments. City officials are members of the following boards and commissions: Washington County Joint E-911 Service Board, and Washington County Assessor's Board.

B. Basis of Presentation

Government-wide Financial Statements – The Statement of Activities and Net Assets reports information on all of the nonfiduciary activities of the City. For the most part, the effect of interfund activity has been removed from this statement. Governmental activities, which are supported by tax and intergovernmental revenues, are reported separately from business type activities, which rely to a significant extent on fees and charges for services.

The Statement of Activities and Net Assets presents the City's nonfiduciary net assets. Net assets are reported in two categories:

Restricted net assets result when constraints placed on net asset use are either externally imposed or imposed by law through constitutional provisions or enabling legislation.

Unrestricted net assets consist of net assets that do not meet the definition of the preceding category. Unrestricted net assets often have constraints on resources imposed by management, which can be removed or modified.

The Statement of Activities and Net Assets demonstrates the degree to which the direct disbursements of a given function are offset by program receipts. Direct disbursements are those clearly identifiable with a specific function. Program receipts include 1) charges to customers or applicants who purchase, use or directly benefit from goods, services or privileges provided by a given function and 2) grants, contributions and interest on investments restricted to meeting the operational or capital requirements of a particular function. Property tax and other items not properly included among program receipts are reported instead as general receipts.

Fund Financial Statements – Separate financial statements are provided for governmental funds and proprietary funds. Major individual governmental funds and major individual enterprise funds are reported as separate columns in the fund financial statements. All remaining governmental funds are aggregated and reported as nonmajor governmental funds.

The City reports the following major governmental funds:

The General Fund is the general operating fund of the City. All general tax receipts and other receipts not allocated by law or contractual agreement to some other fund are accounted for in this fund. From the fund are paid the general operating disbursements, the fixed charges and the capital improvement costs that are not paid from other funds.

Special Revenue:

The Road Use Tax Fund is used to account for road construction and maintenance.

The Urban Renewal Tax Increment Fund is used to account for urban renewal projects financed by tax increment financing.

The Local Option Sales Tax Fund is used to account for projects financed by the Local Option Sales Tax.

The City reports the following major proprietary funds:

The Water Fund accounts for the operation and maintenance of the City's water system.

The Sewer Fund accounts for the operation and maintenance of the City's waste water treatment and sanitary sewer system.

C. Measurement Focus and Basis of Accounting

The City of Kalona maintains its financial records on the basis of cash receipts and disbursements and the financial statements of the City are prepared on that basis. The cash basis of accounting does not give effect to accounts receivable, accounts payable and accrued items. Accordingly, the financial statements do not present financial position and results of operations of the funds in accordance with U.S. generally accepted accounting principles.

Proprietary funds distinguish operating receipts and disbursements from non-operating items. Operating receipts and disbursements generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. All receipts and disbursements not meeting this definition are reported as non-operating receipts and disbursements.

D. Budgets and Budgetary Accounting

The budgetary comparison and related disclosures are reported as Required Supplementary Information.

(2) Cash and Pooled Investments

The City's deposits in banks at June 30, 2004 were entirely covered by federal depository insurance or by the State Sinking Fund in accordance with Chapter 12C of the Code of Iowa. This chapter provides for additional assessments against the depositories to insure there will be no loss of public funds.

The City is authorized by statute to invest public funds in obligations of the United States government, its agencies and instrumentality's; certificates of deposit or other evidences of deposit at federally insured depository institutions approved by the City Council; prime eligible bankers acceptances; certain high rated commercial paper; perfected repurchase agreements; certain registered open-end management investment companies; certain joint investment trusts; and warrants or improvement certificates of a drainage district.

The City's investments are categorized to give an indication of the level of risk assumed by the City at year end. The City's investments are all Category 1, which means the investments are insured or registered or the securities are held by the City or its agent in the City's name.

(3) Bonds and Notes Payable

Annual debt service requirements to maturity for general obligation bonds are as follows:

Year Ending June 30,	General Obligation Bonds		Revenue Bonds		Totals	
	Principal	Interest	Principal	Interest	Principal	Interest
2005	120,000	60,691	82,000	61,582	217,000	122,273
2006	80,000	56,106	84,000	58,768	164,000	114,874
2007	80,000	54,111	87,000	55,878	167,000	109,989
2008	80,000	51,953	89,000	52,884	169,000	104,837
2009	80,000	49,605	94,000	49,814	174,000	99,420
2010	85,000	47,068	97,000	46,562	182,000	93,630
2011	85,000	44,213	99,000	43,206	184,000	87,419
2012	85,000	41,213	103,000	39,774	188,000	80,987
2013	65,000	38,050	107,000	36,206	172,000	74,256
2014	65,000	35,937	110,000	32,488	175,000	68,426
2015	65,000	33,695	114,000	28,664	179,000	62,359
2016	70,000	31,355	81,000	24,690	151,000	56,045
2017	70,000	28,730	84,000	22,260	154,000	50,990
2018	75,000	26,035	86,000	19,740	161,000	45,775
2019	80,000	23,072	88,000	17,160	168,000	40,232
2020	85,000	19,833	91,000	14,520	176,000	34,352
2021	85,000	16,305	94,000	11,790	179,000	28,095
2022	90,000	12,693	97,000	8,970	187,000	21,663
2023	95,000	8,777	99,000	6,060	194,000	14,838
2024	100,000	4,550	103,000	3,090	203,000	7,640
Total	\$1,640,000	\$683,992	\$1,889,000	\$634,106	\$ 3,529,000	\$1,318,098

The Code of Iowa requires that principal and interest on general obligation bonds be paid from the Debt Service Fund. However, during the year, \$54,626 of bond principal was paid from the Enterprise Fund.

The resolutions providing for the issuance of the revenue notes include the following provisions.

- a. The notes will only be redeemed from the future earnings of the enterprise activity and the note holders hold a lien on the future earnings of the funds.
- b. Sufficient transfers shall be made into a separate and special fund to pay current expenses. The fund shall be known as the Sewer/Water Utility Operation and Maintenance Fund. There shall be deposited in the fund each month an amount sufficient to meet the current

expenses of the month plus an amount equal to 1/12th of expenses payable on an annual basis such as insurance. This fund was not established during the fiscal year.

- c. Moneys shall next be disbursed to a separate and special fund to pay principal of and interest on the Notes and Parity Obligations known as the Sewer/Water Revenue Note Principal and Interest Sinking Fund (the "Sinking Fund"). The required amount to be deposited in the Sinking Fund in any month shall be an amount equal to 1/6th of the installment of interest coming due on the next payment and 1/12th of the installment of principal coming due on the next payment date. This fund was not established during the fiscal year.

(4) Pension and Retirement Benefits

The City contributes to the Iowa Public Employees Retirement System (IPERS) which is a cost-sharing multiple-employer defined benefit pension plan administered by the State of Iowa. IPERS provides retirement and death benefits which are established by state statute to plan members and beneficiaries. IPERS issues a publicly available financial report that includes financial statements and required supplementary information. The report may be obtained by writing to IPERS, P.O. Box 9117, Des Moines, Iowa, 50306-9117.

Plan members are required to contribute 3.70% of their annual salary and the City is required to contribute 5.75% of annual covered percentages respectively. Contribution requirements are established by state statute. The City's contribution to IPERS for the years ended June 30, 2002, 2003, and 2004, were \$12,917, \$14,185, and \$14,773 respectively, equal to the required contributions for each year.

(5) Compensated Absences

City employees accumulate a limited amount of earned but unused vacation and comp time hours for subsequent use or for payment upon termination, retirement or death. These accumulations are not recognized as disbursements by the City until used or paid. The City's liability for earned vacation and comp time leave termination payments payable to employees at June 30, 2004 is \$4,417 for vacation and \$5,433 for comp time, for a total liability of \$9,850.

(6) Workers Compensation

The City is a member of the Iowa Municipalities Worker's Compensation Association (IMWCA) which provides worker's compensation coverage to its members. The members own an interest in the assets of the claims payment fund.

(7) Risk Management

The City of Kalona is exposed to various risks of loss related to torts; theft, damage to and destruction of assets; errors and omissions; injuries to employees; and natural disasters. These risks are covered by the purchase of commercial insurance. The City assumes liability for any deductibles and claims in excess of coverage limitations. Settled claims from these risks have not exceeded commercial insurance coverage in any of the past three fiscal years.

(8) Service Agreements

The City has an agreement with Washington County to provide police protection for its citizens. The City paid \$100,847 under this agreement during the year ended June 30, 2004.

(9) Construction Contracts

The City entered into various construction contracts for their water and sewer project totaling approximately \$148,909 and their Library project totaling \$1,102,400. These construction contracts will be funded with local sources in fiscal year 2005 and bond revenues from this fiscal year.

(10) Accounting Change

Governmental Accounting Standards Board Statement No. 34, Basic Financial Statements – and Management’s Discussion and Analysis – for State and Local Governments’ Statement No. 37, Basic Financial Statements – and Management’s Discussion and Analysis – for State and Local Governments: Omnibus; Statement No. 38, Certain Financial Statement Note Disclosures; and Statement No. 41, Budgetary Comparison Schedule – Perspective Differences, were implemented for the year ended June 30, 2004. The statements create new basic financial statements for reporting the City's financial activities. The financial statements now include a government-wide financial statement and fund financial statements which present information for individual major funds rather than by fund type. Nonmajor funds are presented in total in one column.

The government-wide financial statement reports the City's governmental and business type activities.

(11) Subsequent Discovery

The State Revolving Fund loans received by the city were partially federally funded, not entirely state funded as previously reported. The Drinking Water State Revolving Fund was 30.178% federally funded and the Clean Water State Revolving Fund was 83.33% federally funded. This information required the re-issuance of the City of Kalona's financial report as an audit in compliance with A-133 Compliance Supplement.

REQUIRED SUPPLEMENTARY INFORMATION

City of Kalona

Budgetary Comparison Schedule of Receipts, Disbursements, and Changes in Balances-
Budget and Actual (Cash Basis) - Governmental Funds and Proprietary Funds

Required Supplementary Information

	Governmental Funds Actual	Proprietary Funds Actual	Net	Budgeted Original
Receipts:				
Property Tax	\$ 570,135	\$ -	\$ 570,135	\$ 553,074
Tax increment financing collections	164,421	-	164,421	165,455
Other City Tax	159,183	-	159,183	93,545
Use of money and property	20,085	3,960	24,045	-
Licenses and permits	2,145	7,940	10,085	3,000
Intergovernmental	212,966	-	212,966	215,444
Charges for services	88,222	548,147	636,369	539,004
Miscellaneous	6,295	12,846	19,141	7,150
Total Receipts	<u>1,223,452</u>	<u>572,893</u>	<u>1,796,345</u>	<u>1,576,672</u>
Disbursements:				
Public Safety	132,944	-	132,944	130,364
Public Works	146,325	-	146,325	336,284
Culture and recreation	258,118	-	258,118	309,461
Community and economic development	185,098	-	185,098	236,914
General government	96,830	-	96,830	94,161
Debt service	52,866	-	52,866	52,866
Capital projects	101,705	-	101,705	-
Business Type	-	1,764,874	1,764,874	410,688
Total Disbursements	<u>973,886</u>	<u>1,764,874</u>	<u>2,738,760</u>	<u>1,570,738</u>
Excess (deficiency) of receipts over (under) disbursements	249,566	(1,191,981)	(942,415)	5,934
Other financing sources (uses):				
Bond Proceeds				
State Revolving Fund Loan	-	1,382,574	1,382,574	-
General Obligation Bond	1,400,000	-	-	-
Total other financing sources (uses)	1,400,000	1,382,574	2,782,574	-
Excess (deficiency) of receipts and other financing sources over (under) disbursements & other financing uses	<u>1,649,566</u>	<u>190,593</u>	<u>1,840,159</u>	<u>5,934</u>
Balance beginning of year	1,507,304	484,069	1,991,373	1,931,627
Prior period adjustment	-	-	-	-
Adjusted balance beginning of year	1,507,304	484,069	1,991,373	1,931,627
Balance end of year	<u>\$ 3,156,870</u>	<u>\$ 674,662</u>	<u>\$ 3,831,532</u>	<u>\$ 1,937,561</u>

Amounts	Variance
Final	Favorable (Unfavorable)
\$ 553,074	\$ 17,061
165,455	(1,034)
147,556	11,627
-	24,045
3,555	6,530
200,925	12,041
609,280	27,089
19,198	(57)
<u>1,699,043</u>	<u>97,302</u>

135,426	2,482
336,697	190,372
309,461	51,343
375,360	190,262
101,487	4,657
52,866	-
1,400,000	1,298,295
1,992,512	227,638
<u>4,703,809</u>	<u>179,787</u>

(3,004,766)

1,570,000
1,400,000

2,970,000

(34,766)

1,931,627

1,931,627

\$ 1,896,861

City of Kalona

Notes to Required Supplementary Information – Budgetary Reporting

June 30, 2004

In accordance with the Code of Iowa, the City Council annually adopts a budget on the cash basis following required public notice and hearing for all funds except Fiduciary Funds. The annual budget may be amended during the year utilizing similar statutorily prescribed procedures.

Formal and legal budgetary control is based upon ten major classes of disbursements known as functions, not by fund or fund type. These ten functions are: public safety, public works, health and social services, culture and recreation, community and economic development, general government, debt service, capital projects, business type activities and non-program. Function disbursements required to be budgeted included disbursements for the General Fund, Special Revenue Funds, Debt Service Fund, Capital Projects Funds and Proprietary Funds. Although the budget document presents function disbursements by fund, the legal level of control is at the aggregated function level, not by fund. During the year, the budget amendment increased budgeted disbursements by \$3,133,071. The budgeted amendment is reflected in the final budgeted amount.

OTHER SUPPLEMENTARY INFORMATION

Statement of Cash Receipts, Disbursements and Changes in Cash Balances
Nonmajor Governmental Funds

As of and for the year ended June 30, 2004

	Special Revenue	Capital Projects		
	Employee Benefits	Library Project	Debt Service	Total
Receipts:				
Property Tax	\$ 50,323	\$ -	\$ 51,999	\$ 102,322
Other City Tax	773	-	1,271	2,044
Use of Money and Property	-	-	612	612
Total Receipts	<u>51,096</u>	<u>-</u>	<u>53,882</u>	<u>104,978</u>
Disbursements:				
Operating:				
Public Works	10,963	-	-	10,963
Culture and recreation	23,378	-	-	23,378
General government	11,732	-	-	11,732
Debt service	-	-	52,866	52,866
Capital projects	-	101,705	-	101,705
Total Disbursements	<u>46,073</u>	<u>101,705</u>	<u>52,866</u>	<u>200,644</u>
Excess (deficiency) of receipts over (under) disbursements	<u>5,023</u>	<u>(101,705)</u>	<u>1,016</u>	<u>(95,666)</u>
Other financing sources (uses):				
Bond proceeds:				
General Obligation Bond	-	1,400,000	-	1,400,000
Total other financing sources (uses)	-	1,400,000	-	1,400,000
Excess (deficiency) of receipts and other financing sources over (under) disbursements & other financing uses	<u>5,023</u>	<u>1,298,295</u>	<u>1,016</u>	<u>1,304,334</u>
Balance beginning of year	12,827	-	138,773	151,600
Balance end of year	<u>\$ 17,850</u>	<u>\$ 1,298,295</u>	<u>\$ 139,789</u>	<u>\$ 1,455,934</u>
Cash Basis Fund Balances				
Reserved:				
Debt Service	-	-	139,789	139,789
Unreserved:				
Special Revenue Funds	17,850	-	-	17,850
Capital Project Fund	-	1,298,295	-	1,298,295
Total cash basis fund balances	<u>17,850</u>	<u>1,298,295</u>	<u>139,789</u>	<u>1,455,934</u>

City of Kalona

Statement of Indebtedness

Year ended June 30, 2004

	Date of Issue	Interest Rates	Amount Originally Issued	Balance Beginning of Year	Issued During Year
General Obligation Bonds					
Water	April 1, 1997	4.10 - 5.45%	\$ 237,898	\$ 69,625	\$ -
Pool	April 1, 1997	4.10 - 5.45%	242,102	50,373	-
Water	April 1, 1997	4.10 - 5.45%	350,000	225,000	-
Library	June 1, 2004	1.30 - 4.55%	1,400,000	-	1,400,000
Street Sweeper	July 1, 1999	5.00%	55,000	24,076	-
Total General Obligation					<u>1,400,000</u>
Note Payable:					
State Revolving Funds Loans					
Sewer	February 13, 1995	4.54%	590,000	341,000	-
Water	August 26, 2003	3.00%	1,067,000	-	1,067,000
Sewer	December 12, 2003	3.00%	503,000	-	503,000
Total				<u>\$ 872,000</u>	<u>\$ 2,970,000</u>

Redeemed During Year	Balance End of Year	Interest Paid	Interest Due and Unpaid
\$ 29,625	\$ 40,000	\$ 4,545	\$ -
50,373	-	2,493	-
25,000	200,000	12,738	-
-	1,400,000	-	3,978
<u>24,076</u>	<u>-</u>	<u>556</u>	<u>-</u>
<u>129,074</u>	<u>1,640,000</u>	<u>20,332</u>	<u>3,978</u>
22,000	319,000	16,616	-
-	1,067,000	15,591	
-	503,000	6,852	
<u>\$ 151,074</u>	<u>\$ 3,529,000</u>	<u>\$ 59,391</u>	<u>\$ 3,978</u>

City of Kalona

Bond and Note Maturities

As of and for the year ended June 30, 2004

General Obligation Bonds

Year Ending June 30, 2004	Water Bond Issued April 1, 1997		Water Bond Issued April 1, 1997	
	Interest Rate	Amount	Interest Rate	Amount
2005	4.80%	40,000	4.80%	25,000
2006			4.90%	25,000
2007			5.00%	25,000
2008			5.10%	25,000
2009			5.20%	25,000
2010			5.30%	25,000
2011 and beyond			various	50,000
Total		<u>\$ 40,000</u>		<u>\$ 200,000</u>

State Revolving Funds

Year Ending June 30, 2004	Sewer Revenue Notes Issued February 13, 1995		Sewer Revenue Notes Issued December 12, 2003	
	Interest Rate	Amount	Interest Rate	Amount
2005	4.54%	23,000	3.00%	19,000
2006	4.54%	24,000	3.00%	19,000
2007	4.54%	25,000	3.00%	20,000
2008	4.54%	26,000	3.00%	20,000
2009	4.54%	28,000	3.00%	21,000
2010	4.54%	29,000	3.00%	22,000
2011 and beyond	4.54%	164,000	3.00%	382,000
Total		<u>\$ 319,000</u>		<u>\$ 503,000</u>

Library Bond
Issued June 1, 2004

Interest Rate	Amount
1.30%	55,000
1.40%	55,000
1.65%	55,000
1.95%	55,000
2.25%	55,000
2.55%	60,000
various	<u>1,065,000</u>
	<u>\$ 1,400,000</u>

Water Revenue Notes
Issued August 26, 2003

Interest Rate	Amount	Total
3.00%	40,000	202,000
3.00%	41,000	164,000
3.00%	42,000	167,000
3.00%	43,000	169,000
3.00%	45,000	174,000
3.00%	46,000	182,000
3.00%	<u>810,000</u>	<u>2,471,000</u>
	<u>\$ 1,067,000</u>	<u>\$ 3,529,000</u>

Schedule of Expenditures of Federal Awards

Year ended June 30, 2004

Grantor/Program	CFDA Number	Agency Pass-through Number	Program Expendi- tures
Indirect:			
Environmental Protection Agency:			
State of Iowa Department of Natural Resources:			
Drinking Water State Revolving Fund	66.468	542	\$ 280,855
Clean Water State Revolving Fund	66.458	542	<u>375,235</u>
			<u>\$ 656,090</u>

Basis of Presentation - The Schedule of Expenditures of Federal Awards includes the federal grant activity of the City of Kalona and is presented in conformity with an other comprehensive basis of accounting. The information on this schedule is presented in accordance with the requirements of OMB Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations. Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of, the basic financial statements.

Juli Ochs, CPA
1344 240th St.
Victor, Iowa 52347
319-647-2295 (Home)

Independent Auditor's Report on Compliance
and on Internal Control over Financial Reporting

To the Honorable Mayor and
Members of the City Council:

I have audited the financial statements of the City of Kalona, Iowa, as of and for the year ended June 30, 2004, and have re-issued my report thereon dated April 4, 2006. My report expressed a qualified opinion on the financial statements which were prepared in conformity with an other comprehensive basis of accounting. I conducted my audit in accordance with United States generally accepted auditing standards, Chapter 11 of the Code of Iowa, and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States.

During the year ended June 30, 2004 the City of Kalona adopted Governmental Accounting Standards Board Statement No. 34, Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments; Statement No. 37, Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments: Omnibus; Statement No. 38, Certain Financial Statement Note Disclosures, and Statement No. 41, Budgetary Comparison Schedule – Perspective Differences.

Compliance

As part of obtaining reasonable assurance about whether the City of Kalona's financial statements are free of material misstatement, I performed tests of its compliance with certain provisions of laws, regulations, and contracts, non-compliance with which could have a direct and material effect on the determination of financial statements amounts. However, providing an opinion on compliance with those provisions was not an objective of my audit and, accordingly, I do not express such an opinion. The results of my tests disclosed no instances of non-compliance that are required to be reported under Governmental Auditing Standards. Additionally, I noted certain immaterial instances of non-compliance that are described in the accompanying Schedule of Findings.

Comments involving statutory and other legal matters about the Entity's operations for the year ended June 30, 2004 are based exclusively on knowledge obtained from procedures performed during my audit of the general purpose financial statements of the City of Kalona. Since my audit was based on tests and samples, not all transactions that might have had an impact on the comments were necessarily audited. The comments involving statutory and other legal matters are not intended to constitute legal interpretations of those statutes. Prior audit statutory comments have been resolved except for item II-A-04, IV-C-04, IV-D-04, IV-H-04, IV-I-04 and IV-J-04.

Internal Control Over Financial Reporting

In planning and performing my audit, I considered the City of Kalona's internal control over financial reporting in order to determine my auditing procedures for the purpose of expressing my opinion on the financial statements and not to provide assurance on the internal control over financial reporting. However, I noted certain matters involving the internal control over financial reporting and its operation that I consider to be reportable conditions. Reportable conditions involve matters coming to my attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in my judgment, could adversely affect the City of Kalona's ability to record, process, summarize and report financial data consistent with the assertions of city officials in the financial statements. Reportable conditions are described in the accompanying Schedule of Findings.

A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. My consideration of the internal control over financial reporting would not necessarily disclose all matters in internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, of the reportable conditions described above, I believe item 1 is a material weakness. Prior year reportable conditions have been resolved except for item II-A-04. This report, a public record by law, is intended solely for the information and use of the officials, employees and citizens of the City of Kalona and other parties to whom the City of Kalona may report. This report is not intended to be and should not be used by anyone other than these specified parties.

I would like to acknowledge the many courtesies and assistance extended to me by the personnel of the City of Kalona during the course of my audit. Should you have any questions concerning any of the above matters, I would be pleased to discuss them with you at your convenience.



Jill Ochs, CPA, Principal

April 4, 2006

**Independent Auditor's Report on compliance with Requirements
Applicable to Each major Program and Internal Control over Compliance**

City of Kalona

Juli Ochs, CPA
1344 240th St.
Victor, Iowa 52347
319-647-2295 (Home)

Independent Auditor's Report on Compliance with Requirements
Applicable to Each Major Program and Internal Control over Compliance

To the Honorable Mayor and
Members of the City Council:

Compliance

I have audited the compliance of the City of Kalona, Iowa, with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement that are applicable to its major federal program for the year ended June 30, 2004. The City of Kalona's major federal program is identified in Part 1 of the accompanying Schedule of Findings and Questioned Costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to its major federal program is the responsibility of the City of Kalona's responsibility is to express an opinion on the City of Kalona's compliance based on my audit.

I conducted my audit of compliance in accordance with U.S. generally accepted auditing standards, Chapter 11 of the Code of Iowa, 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 provisions require that I plan and perform the audit to obtain reasonable assurance about whether non-compliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the City of Keota's compliance with those requirements and performing such other procedures as I considered necessary in the circumstances. I believe that my audit provides a reasonable basis for my opinion. My audit does not provide a legal determination on the City of Kalona's compliance with those requirements.

In my opinion, the City of Kalona complied, in all material respects, with the requirements referred to above that are applicable to its major federal program for the year ended June 30, 2004.

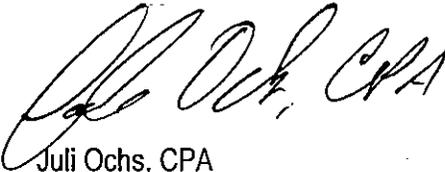
Internal Control Over Compliance

The management of the City of Kalona is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts and grants applicable to federal programs. In planning and performing our audit, I considered the City of Kalona's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine my auditing procedures for the purpose of expressing my opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133.

My consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that noncompliance with applicable requirements of laws, regulations, contracts and grants that would be

material in relation to a major federal program being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. I noted no matters involving the internal control over compliance and its operation that I consider to be material weaknesses.

This report, a public record by law, is intended solely for the information and use of the officials, employees and citizens of the City of Kalona and other parties to whom the City of Kalona my report, including federal awarding agencies and pass-through entities. This report is not intended to be and should not be used by anyone other than these specified parties.

A handwritten signature in black ink, appearing to read "Juli Ochs, CPA". The signature is fluid and cursive, with the letters "J", "O", and "C" being particularly prominent.

April 4, 2006

Juli Ochs, CPA

City of Kalona
Schedule of Findings and Questioned Costs
Year ended June 30, 2004

Part I: Summary of the Independent Auditor's Results:

- (a) A qualified opinion was issued on the financial statements which were prepared on the basis of cash receipts and disbursements, which is a comprehensive basis of accounting other than U.S. generally accepted accounting principles.
- (b) Reportable conditions in internal control over financial reporting were disclosed by the audit of the financial statements, including material weaknesses.
- (c) The audit did not disclose any non-compliance which is material to the financial statements.
- (d) A reportable condition in internal control over the major program was not disclosed by the audit of the financial statements.
- (e) An unqualified opinion was issued on compliance with requirements applicable to the major program.
- (f) The audit did not disclose audit findings which are required to be reported in accordance with Office of Management and Budget Circular A-133, Section .510(a).
- (g) The major program was CFDA Number 66.458 – Clean Water State Revolving Fund.
- (h) The dollar threshold used to distinguish between Type A and Type B programs was \$300,000.
- (i) The City of Kalona did not qualify as a low-risk auditee.

CITY OF KALONA

Schedule of Findings and Questioned Costs

Year ended June 30, 2004

The following comments about the City of Kalona operations for the year ended June 30, 2004, are based exclusively on knowledge obtained from procedures performed during our audit of financial statements of the City.

Part II: Findings Related to the Financial Statements:

INSTANCES OF NON-COMPLIANCE:

No matters were noted.

REPORTABLE CONDITIONS:

II-A-04 Segregation of Duties – One important element in designing an internal control structure that safeguards assets and reasonably ensures the reliability of the accounting records is the concept of segregation of duties. When duties are properly segregated, the activities of one employee act as a check of those of another.

During our review of the city's control procedures, we noted that one person has control over one or more of the following areas:

Accounting system – general journal/general ledger/journal entry function and custody of assets

Receipts – collecting, depositing, journalizing, posting, and reconciling.

Payroll – preparation and distribution.

Utilities – collections, depositing and recording.

Recommendation – We realize that with a limited number of office employees, segregation of duties is difficult. However, the City should review its control procedures to obtain the maximum internal control possible under the circumstances.

Response – Since there are only two employees at city hall, it is difficult to segregate duties. Duties are segregated to the best of our ability.

Conclusion – Response acknowledged. The City could segregate duties to the extent possible with existing personnel and utilize administrative personnel to provide additional control through review of financial transactions and reports.

Part III: Findings and Questioned Costs for Federal Awards:

INSTANCES OF NON-COMPLIANCE:

**CFDA Number 66.468: Drinking Water State Revolving Fund
Federal Award year: 2004
Environmental Protection Agency
Passed through the Iowa Department of Natural Resources**

None noted.

**CFDA Number 66.458: Clean Water State Revolving Fund
Federal Award year: 2004
Environmental Protection Agency
Passed through the Iowa Department of Natural Resources**

None noted.

REPORTABLE CONDITION:

**CFDA Number 66.468: Drinking Water State Revolving Fund
Federal Award year: 2003
Environmental Protection Agency
Passed through the Iowa Department of Natural Resources**

None noted.

**CFDA Number 66.458: Clean Water State Revolving Fund
Federal Award year: 2003
Environmental Protection Agency
Passed through the Iowa Department of Natural Resources**

None noted

Part IV: Other Findings Related to Statutory Reporting:

- IV-A-04 Certified Budget – Disbursements during the year ended June 30, 2004, did not exceed the amounts budgeted.
- IV-B-04 Bond Coverage – Surety bond coverage of City officials and employees is in accordance with statutory provisions. The amount of coverage should be reviewed annually to insure that the coverage is adequate for current operations.
- IV-C-04 Council Minutes – No transactions were found that we believe should have been approved in the Council minutes but were not.

Minutes of the August, and December, 2003 and January and June 2004 Council meetings were not published as required by Chapter 372.13(6) of the Code of Iowa.

Recommendation – The City should publish minutes as required by Chapter 372.13(6) of the Code of Iowa.

Response – Our official publication has requested us email all minutes, notices, etc. for their convenience. The same were emailed for a timely publishing, but if they do not have room they have set them of to the next week, when they have room. I am presuming this is what happened.

Conclusion – Response accepted

IV-D-04 Official Depositories –A resolution naming official depositories has been approved by the City. The maximum deposit amounts stated in the resolution were exceeded during the year ended June 30, 2004 for the holdings at Hills Bank, Kalona.

Recommendation – A new resolution in amounts sufficient to cover anticipated balances at all approved depositories should be adopted by the Council.

Response – We will adjust our depository limits.

Conclusion – Response accepted.

IV-E-04 Payroll Time Cards Approval– During the fiscal year it was determined that many of the time cards from the Library Department were not approved.

Recommendation – Time cards should be reviewed by supervisors or department heads each time period and initialed to indicate their approval.

Response – All timecards are being reviewed by the Librarian or City Administrator and initialed before payment.

Conclusion – This was a prior year comment and it was noted that after the prior year report was issued, the City Administrator was initialing all the timecards except Library.

IV-F-04 Questionable Disbursements –We noted no disbursements that meet the requirements of public purpose as defined in an Attorney General's opinion dated April 25, 1979.

IV-G-04 Travel Expense –No disbursements of City money for travel expenses of spouses of City officials or employees were noted.

IV-H-04 Deposits and Investments – No instances of non-compliance with the deposit and investment provisions of Chapter 12B and 12C of the Code of Iowa. However, it was noted that the City's investment policy is not current and in compliance with the provisions of Chapter 12B.10B of the Code of Iowa.

Recommendation – The City should update their investment policy to comply with the provisions of Chapter 12B.10B of the Code of Iowa.

Response – We are working towards adopting a current investment policy.

Conclusion – Response accepted.

IV-I-04 Cash Drawer – The City does not include the cash drawer in the fund balance. Chapter 384.20 of the Code of Iowa states in part that a City shall keep accounts which show an accurate and detailed statement of all public funds.

Recommendation – The City should include all cash funds in the fund balance to properly account for all funds.

Response – We will include the same in the future.

Conclusion – Response accepted.

IV-J-04 General Obligation Loan Notes – The Water General Obligation Notes were paid for directly from the Water Fund. Section 384.4 of the Code of Iowa states “Moneys pledged or available to service general obligation bonds, and received from sources other than property taxes, must be deposited in the debt service fund.”

Recommendation – The City should transfer water funds designated for payments on bonds to debt service and then make bond payments out of debt service.

Response – The City will take it under advisement.

Conclusion – The city should consider the implications of paying the note out of the Water Fund.

IV-K-04 Cash Balance Variance – The cities books differ from the bank balances by \$10,841.

Recommendation – The City should investigate this variance and determine why the balances for the City reflect less than the bank balance.

Response – We are aware of the situation and are presuming that in the change-over of the software in June 2004, something has been recorded incorrectly and through continuous investigation by the time for next years audit, the variance will be resolved.

Conclusion – This should be investigated thoroughly, response accepted.

IV-L-04 Sewer/Water Revenue Note – The Sewer/Water Revenue Note stipulates that a Sewer/Water Utility Operation and Maintenance, and Sewer/Water Sinking Fund be established. These funds have not been established.

Recommendation – An Operation and Maintenance Fund and Sinking fund should be established to comply with the requirements of the Water/Sewer Revenue Note.

Response – The City has established a separate money market account to act as a combined sinking and operation/maintenance fund.

Conclusion – As this is a good idea, the revenue note requirements should be followed.