

CRESTON CITY WATER WORKS

INDEPENDENT AUDITOR'S REPORT
FINANCIAL STATEMENTS AND
SUPPLEMENTAL INFORMATION

ADDITIONAL REQUIRED AUDITOR'S REPORTS

Year Ended June 30, 2004

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CRESTON CITY WATER WORKS

OFFICIALS

<u>Name</u>	<u>Title</u>	<u>Term Expiration</u>
Dennis C. Bailey	Chairman Trustee	December, 2004 December, 2006
Lee McNichols	Vice-Chairman Trustee	December, 2004 December, 2004
Ken Sharp	Treasurer Trustee	December, 2004 December, 2006
Ray Fogle	Secretary Trustee	December, 2004 December, 2004
William Stuart	Trustee	December, 2008
Steve Green	Assistant Secretary Manager	December, 2004 March 31, 2006
Cheryl Eblen	Office Manager	Indefinite

INDEPENDENT AUDITOR'S REPORT

To the Board of Trustees of the
Creston City Water Works

We have audited the accompanying financial statements of the business type activities of the Creston City Water Works, as of and for the year ended June 30, 2004. These financial statements are the responsibility of Water Works officials. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with U.S. 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. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

We did not observe the taking of physical inventories at June 30, 2004, and we were unable to satisfy ourselves as to the inventory quantities by means of other auditing procedures.

Property and equipment, contributed capital and retained earnings records are not complete; therefore, we were unable to perform sufficient auditing procedures to satisfy ourselves as to the balances in those accounts.

As explained in Note 1 of the Notes to Financial Statements, that portion of the fund equity represented by contributed capital and retained earnings is accounted for in total rather than being separated into its component parts. Further, property and equipment are accounted for using estimated values and no allowance for accumulated depreciation has been provided. These practices, the effects of which are not readily determinable because of the inadequacy of existing accounting records, are not in conformity with U.S. generally accepted accounting principles.

Because the items mentioned above enter materially into the determination of financial position, the scope of our work was not sufficient to enable us to express, and we do not express, an opinion on the balance sheet referred to in the first paragraph.

As described in Note 1, these financial statements referred to in the following paragraph 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.

In our opinion, the financial statements referred to above present fairly, in all material respects, the cash basis financial position of the business type activities of the Creston City Water Works as of June 30, 2004, and the changes in cash basis financial position for the year then ended in conformity with the basis of accounting described in Note 1.

As described in Note 11, during the year ended June 30, 2004, the Water Works 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, we have also issued a report dated July 29, 2004, on our consideration of Creston City Water Works’ internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grants. That report is 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 our audit.

Management’s Discussion and Analysis and budgetary comparison information on pages 4 through 8 and 21 through 22 are not required parts of the basic financial statements, but are supplementary information required by the Governmental Accounting Standards Board. We applied limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. We did not audit the information and express no opinion on it.

Our audit was performed for the purpose of forming opinions on the financial statements that comprise the Creston City Water Works’ basic financial statements. We 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 unqualified opinions on those financial statements. Other supplementary information included in Schedules 1 through 3, is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in our audit of the basic financial statements and, in our opinion, except for that portion marked “unaudited” on which we express no opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

Drapen, Smidgrass, Mikkelsen + Co., P.C.

July 29, 2004

MANAGEMENT'S DISCUSSION AND ANALYSIS

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

Financial Highlights

The City of Creston Water Works total water revenues increased by \$16,930 from the previous fiscal year. The rural water sales increased by \$30,136 from the previous fiscal year.

The general water sales from the City of Creston Water Works decreased by \$17,717. This reduction in water sales is mainly due to the loss of sales to the Creston Water Works when the PTI Protein (Bean) plant shut down production in the fall of 2003.

Using this Annual Report

The annual report consists of a series of financial statements as well as other requirements as follows.

Management's Discussion and Analysis introduces the basic financial statements and provides an analytical overview of the City of Creston Water Works' financial activities.

The City of Creston Water Works' financial statements consists of a statement of activities and changes in cash balances. The statement provides information about the activities of the Creston Water Works as a whole and presents an overall view of the Water Works' finances.

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

Required Supplementary Information provides detailed information about the annual budget.

Basis of Accounting

The City of Creston Water Works maintains its financial records on the basis of cash receipts and disbursements and the financial statements of the Water Works are prepared on that basis. The cash basis of accounting does not give effect to accounts receivable, accounts payable and accrued items. The accounts of the Water Works are organized on the basis of funds, each of which is considered to be a separate accounting entity. The operations of each fund are accounted for by providing a separate set of self-balancing accounts which comprise its assets, liabilities, reserves, fund balance, receipts and disbursements. Accordingly, the financial statements do not represent 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 that limitations resulting from the use of cash basis accounting.

Reporting the City of Creston Water Works as a Whole

The statement of activities and changes in cash balance presents information showing how the City of Creston Water Works' cash balances changed during the most recent fiscal year.

The City of Creston Water Works' activities are displayed in the statement of activities and changes in cash balance.

The business type activities of the City of Creston Water Works include the collection of user fees for sewer, garbage, service connection and cable television service. The primary activity is the Municipal Water Utility.

Fund Financial Statements

The fund financial statements begin on page 9 and provide detailed information about individual significant funds. Some funds are established by State law and bond covenants. The City of Creston Water Works can establish other funds to help it control and manage money for particular purposes.

The City of Creston Water Works has Three Sources of Funds

Sewer and garbage receipts, which are billed, collected and paid to the City of Creston on a monthly basis. The primary source of revenue is from the City of Creston Water Works – water sales.

Government Wide Financial Analysis

As noted earlier, the City of Creston Water Works reports the activities of the funds using the cash basis of accounting, which is a comprehensive basis of accounting other than U.S. generally accepted accounting principles (GAAP). The City of Creston Water Works does not report capital assets or depreciation on those assets as would be required by GAAP.

Business Type Activities – Water Works

The City of Creston Water Works total receipts/disbursements – cash balance, increased by less than one percent or \$1,565.

The City of Creston Water Works has not had a rate increase since January 1986.

The cost of all Water Works' activities this year was \$3,514,964, as compared to \$3,306,545 the last fiscal year. This includes the sewer and garbage collection payments made to the City of Creston as shown below on the "Business Type Activities".

Business Type Activities

	<u>2004</u>	<u>2003</u>
Receipts:		
Program receipts		
Charges for services and sales:		
Water utility (all sources)	\$2,073,628	\$2,094,169
Sewer rental revenue	988,983	970,365
Garbage revenue	453,918	380,950
Total revenue	<u>\$3,516,529</u>	<u>\$3,445,484</u>
Disbursements:		
All water utility expenditures	\$2,101,147	\$1,969,163
Sewer rental expenditure	976,491	967,659
Garbage expenditure	437,326	369,723
Total disbursements	<u>\$3,514,964</u>	<u>\$3,306,545</u>
Increase (decrease) in cash balance	\$ 1,565	\$ 138,939
Cash balance beginning of fiscal year	<u>3,545,479</u>	<u>3,406,540</u>
Cash balance end of fiscal year	<u>\$3,547,044</u>	<u>\$3,545,479</u>

The total business type activity receipts for the fiscal year were \$3,516,529, which includes sewer and garbage collections that are in turn paid to the City of Creston, as compared to \$3,445,484 collected the last fiscal year.

The Water Works Individual Major Funds

The City of Creston Water Works uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. The focus of the Water Works funds is to provide information on near-term inflows, outflows, and cash balances of spendable resources. The following are the major reasons for changes in cash balances from the prior year for the City of Creston Water Works major funds.

City of Creston Water Works – General Fund

The General Fund is the chief operating fund of the City of Creston Water Works. At the end of the current fiscal year, the cash balance in the General Fund was \$3,547,044, an increase in \$1,565.

The Employee Benefits Fund is included in the General Fund for revenues received and expenditures paid to the support of employee benefits for health insurance, FICA, IPERS, and unemployment benefits. The types of revenues received are the water rate revenues.

The Debt Service Fund is utilized to account for the payment of interest and principal on the City of Creston Water Works general obligation and long-term debt. The City of Creston Water Works, from its General Fund, pays monthly payments for the two general obligation bonds in the amount of \$7,975. The total annual payments are \$95,698.

Budgetary Highlights

In accordance with the Code of Iowa, the City of Creston Water Works annually adopts a budget following the required public notice and hearings for all funds. Although the budget document presents functional disbursements by fund, the legal level of contract is at the aggregated function level, not at the fund or fund type level. The budget may be amended during the year utilizing similar statutorily prescribed procedures, ie; a required public notice followed by a public hearing. The City of Creston Water Works did not amend its operating budget at year end. The budget was approved and passed unanimously by the City of Creston Water Works Board of Trustees.

Debt Administration

At year end, the City of Creston Water Works had approximately \$1,026,821 in bonds as compared to \$1,078,980 the last fiscal year.

Economic Factors and Next Year's Budget and Rates

The City of Creston Water Works Board of Trustees consider many factors when setting the 2005 fiscal year budget. The Water Works Board of Trustees is involved in four major projects as follows:

Project #1
Sludge Lagoon Project
12-Mile Water Treatment Plant

Project #2
Water System Improvements
Division I – Elevated Water Storage Tank
Division II – Water Piping Improvements
Estimated Cost \$1,544,000

Project # 3
Water Treatment Plant Rehabilitation
Improvements for Regulatory Compliance and Capacity Improvements
Estimated Cost \$3.2 Million

Project #4
Water Tower Painting
500,000 Gallon Tank
Estimated Cost \$200,000

These projects are in review. Applications are being prepared for grant fund assistance, low interest loans, etc.

The City of Creston Water Works Board of Trustees has reviewed the needs of all the projects budgeted in for the 2004-2005 fiscal year. Portions of these projects will continue on through fiscal year 2007.

In addition to the projects stated above, other items of importance to the Water Works Board of Trustees are return on investments and the cost of employee benefits.

These factors all contributed when adopting the fiscal year 2005 budget. The budget includes all business type activities, including sewer, garbage and water expenditures. Steps implemented by the Water Works Board of Trustees, while taking into account increased costs of employee benefits, low returns on investments and the need to keep services at an acceptable level were also a factor in the year 2005 fiscal year budget.

Contacting the City of Creston Water Works Financial Management

This financial report is designed to provide our rate-payers and creditors with a general overview of the City of Creston Water Works' finances and to show the City of Creston Water Works accountability for the money it receives. If you have questions about this report or need additional information, contact Steve A. Green, General Manager, City of Creston Water Works, 116 West Adams Street, P.O. Box 405, Creston, IA 50801.

CRESTON CITY WATER WORKS
BALANCE SHEET
June 30, 2004

Exhibit A

ASSETS

Cash and time deposits (Note 2)		\$ 3,294,792
Consumer accounts receivable, net of allowance for doubtful accounts of \$1,132		86,161
Accrued interest receivable		3,815
Unbilled usage		127,179
Prepaid insurance		28,490
Inventory (Note 1)		66,929
Restricted assets:		
Cash and time deposits (Note 2)		252,253
Property and equipment (Note 1 and 3)		16,412,622
Intangible, deferred debt expense, at amortized cost		3,191
		<u>3,191</u>
Total assets		<u>\$ 20,275,432</u>

LIABILITIES AND FUND EQUITY

LIABILITIES

Accounts payable and accrued expenses		\$ 150,878
Due to city - garbage and sewer collections		185,374
Consumer deposits		213,196
Bonds payable and other debt (Note 4)		1,026,822
		<u>1,026,822</u>
Total liabilities		\$ 1,576,270

FUND EQUITY (Note 1)

Contributed capital and retained earnings		
Reserves:		
Bond Sinking Fund	\$ 156,555	
Bond Reserve Funds	95,698	\$ 252,253
Unreserved:		
Undesignated		18,446,909
Total fund equity		<u>18,699,162</u>
Total liabilities and fund equity		<u>\$ 20,275,432</u>

The Notes to Financial Statements are an integral part of this statement.

CRESTON CITY WATER WORKS
STATEMENT OF ACTIVITIES AND NET ASSETS - CASH BASIS
As of and For the Year Ended June 30, 2004

	Program Receipts				Net (Disbursements), Receipts and Changes In Cash Basis Net Assets
	Charges for Services	Operating Grants, Contributions, and Restricted Interest	Capital Grants, Contributions, and Restricted Interest		Business Type Activities
Disbursements					
Functions/Programs:					
Business type activities:					
Water	\$ 3,514,964	\$ 3,319,585	\$ -	\$ -	\$ (195,379)
Total business type activities	<u>\$ 3,514,964</u>	<u>\$ 3,319,585</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ (195,379)</u>
General receipts:					
Interest on investments					\$ 87,026
Miscellaneous					<u>109,918</u>
Total general receipts					<u>\$ 196,944</u>
Change in cash basis net assets					\$ 1,565
Cash basis net assets, beginning of year					<u>3,545,479</u>
Cash basis net assets, end of year					<u><u>\$ 3,547,044</u></u>

The Notes to Financial Statements are an integral part of this statement.

CRESTON CITY WATER WORKS
STATEMENT OF CASH RECEIPTS, DISBURSEMENTS AND
CHANGES IN CASH BALANCES
As of and For the Year Ended June 30, 2004

	Exhibit C
	<u>Enterprise Funds</u>
Operating receipts:	
Charge for service	<u>\$ 3,319,585</u>
Total operating receipts	<u>\$ 3,319,585</u>
Operating disbursements:	
Business type activities	<u>\$ 3,419,266</u>
Total operating disbursements	<u>\$ 3,419,266</u>
Excess (deficiency) of operating receipts over (under) operating disbursements	<u>\$ (99,681)</u>
Non-operating receipts (disbursements):	
Interest on investment	\$ 87,026
Miscellaneous	109,918
Debt service	<u>(95,698)</u>
Total non-operating receipts (disbursements)	<u>\$ 101,246</u>
Excess (deficiency) of receipts over (under) disbursements	\$ 1,565
Operating transfers out	<u>-</u>
Net change in cash balances	\$ 1,565
Cash balances, beginning of year	<u>3,545,479</u>
Cash balances, end of year	<u><u>\$ 3,547,044</u></u>
Cash basis fund balances:	
Reserved for debt service	\$ 156,555
Reserved for bond reserve funds	95,698
Reserved for customer deposits	213,221
Unreserved	<u>3,081,570</u>
Total cash basis fund balances	<u><u>\$ 3,547,044</u></u>

The Notes to Financial Statements are an integral part of this statement.

CRESTON CITY WATER WORKS
NOTES TO FINANCIAL STATEMENTS
June 30, 2004

Note 1. Significant Accounting Policies

The Creston City Water Works is a governmental subdivision of the State of Iowa located in Union County. It was incorporated in the mid 1930's. The Water Works Board of Trustees is appointed by the Mayor of Creston and approved by the Creston City Council. The Water Works provides water services to Creston area residents and surrounding counties.

Reporting Entity:

The financial statements include all funds of the Creston City Water Works. The Water Works 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 Water Works are such that exclusion would cause the Water Works' 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 Water Works 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 Water Works.

The Creston City Water Works is a component unit of the City of Creston.

Basis of Presentation:

Government-wide Financial Statements – The Statement of Activities and Net Assets reports information on all of the nonfiduciary activities of the Water Works. 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 Water Works' 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.

CRESTON CITY WATER WORKS
NOTES TO FINANCIAL STATEMENTS
June 30, 2004

Note 1. Significant Accounting Policies (continued):

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 proprietary funds. Major individual enterprise funds are reported as separate columns in the fund financial statements.

The Water Works reports the following major proprietary funds:

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

Basis of Accounting:

The Water Works maintains its financial records on the basis of cash receipts and disbursements and the financial statements of the Water Works 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.

Budgets and Budgetary Accounting:

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

CRESTON CITY WATER WORKS
NOTES TO FINANCIAL STATEMENTS
June 30, 2004

Note 1. Significant Accounting Policies (continued)

Balance Sheet:

The balance sheet was prepared by making memorandum adjusting entries converting the cash basis accounting records to the accrual basis as is consistent with U.S. generally accepted accounting principles for governmental units.

Cash and Time Deposits:

The Water Works pools cash resources of most funds in a combined bank account to facilitate the management of cash. The Water Works makes disbursements and investments from the combined cash balance. Time deposits are stated at cost which approximates market. All interest is credited to the operating fund.

Inventory:

Inventory is valued at cost plus 10 percent, which is not in accordance with U.S. generally accepted accounting principles.

Restricted Assets:

The Water Works, based on certain bond covenants, is required to establish and maintain prescribed amounts of resources (consisting of cash and investments) that can be used only to service outstanding debt.

Property and Equipment:

At June 30, 1978, management estimated the value of property and equipment and additions and deletions have been accounted for annually since that date. Depreciation is not being computed on property and equipment.

Complete property and equipment cost records are not available, making it impossible to determine the effect of the use of the estimated value and lack of depreciation on the presentation of financial position. Accounting for property and equipment on the basis of estimated values and not computing depreciation is not in accordance with U.S. generally accepted accounting principles.

CRESTON CITY WATER WORKS
NOTES TO FINANCIAL STATEMENTS
June 30, 2004

Note 1. Significant Accounting Policies (continued)

Fund Equity:

The reserved contributed capital and retained earnings represent the net assets that have been legally identified for specific purposes. The unreserved contributed capital and retained earnings represent the net assets available for future operations.

The accounting records are not adequate to separately identify and account for contributed capital and retained earnings. As a result, these separate elements of the fund equity are grouped for financial statement presentation which is not in accordance with U.S. generally accepted accounting principles.

Note 2. Deposits and Investments

The Water Works' deposits at June 30, 2004, were entirely covered by Federal depository insurance, collateralized with securities or letters of credit held by the Water Works or the Water Works' agent in the Water Works' name or by a multiple financial institution collateral pool in accordance with Chapter 12C of the Code of Iowa. This chapter provides for additional assessments against the members of the pool to insure there will be no loss of public funds.

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

The Water Works' investments are categorized to give an indication of the level of risk assumed by the Water Works at year-end. The Water Works' investment at June 30, 2004, consisted of Certificates of Deposits and are not subject to risk categorization.

CRESTON CITY WATER WORKS
NOTES TO FINANCIAL STATEMENTS
June 30, 2004

Note 3. Property and Equipment

Detail of property and equipment at estimated values at June 30, 2004, by category is as follows:

	Balance <u>July 1, 2003</u>	Additions or <u>Deletions</u>	Balance <u>June 30, 2004</u>
Land and buildings Twelve Mile Watershed Project - Land	\$ 883,523	\$ 108,179	\$ 991,702
Twelve Mile Watershed Project – Treatment Plant, Dam, Intake Structure, and Other Property	2,076,852	---	2,076,852
Distribution system	10,050,868	51,309	10,102,177
Equipment and vehicles	2,824,790	120,075	2,944,865
	<u>289,711</u>	<u>7,315</u>	<u>297,026</u>
	<u>\$ 16,125,744</u>	<u>\$286,878</u>	<u>\$ 16,412,622</u>

Note 4. Bonds Payable and Other Debt

A summary of the Water Works' June 30, 2004, revenue bonds is as follows:

Year Ending <u>June 30,</u>	<u>Revenue Bonds</u>	
	<u>Principal</u>	<u>Interest</u>
2005	\$ 57,440	\$ 38,258
2006	56,666	39,032
2007	59,052	36,647
2008	61,538	34,161
2009	64,129	31,570
2010	66,828	28,870
2011	69,642	26,056
2012	72,575	23,123
2013	75,632	20,066
2014	78,817	16,881
2015	82,137	13,561
2016	85,595	10,101
2017	89,203	6,495
2018	91,828	2,737
2019	<u>15,739</u>	<u>198</u>
TOTALS	<u>\$1,026,821</u>	<u>\$ 327,756</u>

CRESTON CITY WATER WORKS
NOTES TO FINANCIAL STATEMENTS
June 30, 2004

Note 4. Bonds Payable and Other Debt (continued)

Interest expense for the year ended June 30, 2004, was \$43,540.

Revenue Bonds:

The interest rates on the revenue bonds range from 4.012% to 4.371%.

The resolutions providing for the issuance of the revenue bonds include the following provisions:

- a. That the bonds will be redeemed from the future net earnings of the Water Works and that the bondholders hold a lien against future earnings of the funds.
- b. That before any bonds ranking on parity are issued an opinion must be obtained that the net revenues for the preceding fiscal year were equal to 1.25 times the maximum that will be required in any fiscal year prior to the largest maturity of any of the outstanding and proposed bonds.
- c. That sufficient monthly cash transfers shall be made to a separate sinking fund restricted for the purpose of making bond interest and principal payments when due.
- d. That a monthly cash transfer of 25% of the amount deposited in the sinking fund shall be made to a separate reserve fund until an amount has been accumulated equal to the maximum amount due in any subsequent year for principal and interest.

As of June 30, 2004, transfers have been made in amounts adequate on a cumulative basis, to meet the foregoing requirements, and the Water Works complied with the provisions.

The Water Works is required to set aside in a sinking fund the amounts needed to meet the principal and interest payments annually for all the revenue bonds. The next five years sinking fund requirements are as follows:

CRESTON CITY WATER WORKS
 NOTES TO FINANCIAL STATEMENTS
 June 30, 2004

Note 4. Bonds Payable and Other Debt (continued)

Year Ending June 30,	
2005	\$ 95,698
2006	95,698
2007	95,698
2008	95,698
2009	95,698

Note 5. Pension and Retirement Benefits

The Water Works 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 Water Works is required to contribute 5.75% of annual covered payroll. Contribution requirements are established by State statute. The Water Works' contribution to IPERS for the year ended June 30, 2004, 2003, and 2002 were \$33,664, \$31,872 and \$30,185 respectively, equal to the required contribution for the year.

Note 6. Related Parties

The City of Creston has title to all the land and buildings used by the Creston City Water Works. The Mayor appoints and the City Council confirms the appointments to the Water Works Board of Trustees.

The Water Works determines fees charged to users and also charges the City for usage. The Water Works collects sewage and garbage fees for the City of Creston. Funds collected are remitted to the City monthly. The Water Works remitted \$964,798 for sewer rental and \$437,326 for garbage collections to the City for the year ended June 30, 2004. The Water Works received from the City \$9,088 for utilities.

CRESTON CITY WATER WORKS
 NOTES TO FINANCIAL STATEMENTS
 June 30, 2004

Note 6. Related Parties (continued)

The Creston City Water Works and City of Creston are covered under the same property insurance policy. Each year the City pays the total premium and the Water Works reimburses the City for its share of the cost.

As of June 30, 2004, the Water Works owes the following to the City of Creston:

Sewer rental	\$ 125,845
Garbage collections	<u>59,529</u>
	<u>\$ 185,374</u>

The City and the Water Works have an agreement for the Water Works to pay the City rent of \$500 per month to cover expenses of office space, utilities, and supplies provided by the City. The Water Works paid the City \$6,000 during the year ended June 30, 2004.

During the year ended June 30, 2004, the City provided employees of both the City and Water Works with payments of co-insurance and deductibles for health insurance. The Water Works remitted to the City \$216,526 for health insurance premiums for the year ended June 30, 2004. The City's plan is self-funded and pays claims from its employee benefits special revenue fund up to maximum limits and carries stop loss insurance for claims in excess of limits.

The Water Works had business transactions totaling \$592 between the Water Works and Water Works officials during the year ended June 30, 2004.

Note 7. Compensated Absences

Water Works' employees accumulate a limited amount of earned but unused leave hours for subsequent use or for payment upon termination, retirement or death. These accumulations are not recognized as disbursements by the Water Works until used or paid. The Water Works approximate liability for earned leave termination payments payable to employees at June 30, 2004, is as follows:

<u>Type of Benefit</u>	<u>Amount</u>
Compensated absences	\$ 47,097

This liability has been computed based on rates of pay as of June 30, 2004.

CRESTON CITY WATER WORKS
NOTES TO FINANCIAL STATEMENTS
June 30, 2004

Note 8. Risk Management

The Creston City Water Works 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. Settled claims from these risks have not exceeded commercial insurance coverage in any of the past three fiscal years.

Note 9. Major Customer

A material part of the Water Works' business is dependent upon Southern Iowa Rural Water Association (SIRWA), the loss of which could have a materially adverse effect on the Water Works. During the year ended June 30, 2004, SIRWA accounted for approximately 80% of the water sales. The Water Works has a contract to provide water to SIRWA through April, 2032.

Note 10. Litigation

The Water Works is subject to pending litigation concerning the construction of a new water tower. A request for a temporary injunction to prevent the construction of the water tower has been filed until the matter can be tried. At trial the plaintiffs are requesting a permanent injunction, together with damages for nuisance, loss of value to their property, punitive damages, and damages for emotional distress. The Water Works is vigorously defending the suit. It is difficult to assess the nature and extent of possible damages in this matter.

Note 11. Accounting Change and Restatements

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 Water Works' 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.

REQUIRED SUPPLEMENTARY INFORMATION

CRESTON CITY WATER WORKS
 BUDGETARY COMPARISON SCHEDULE OF RECEIPTS, DISBURSEMENTS
 AND CHANGES IN BALANCES - ACTUAL TO BUDGET (CASH BASIS)
 REQUIRED SUPPLEMENTARY INFORMATION
 Year Ended June 30, 2004

	<u>Actual</u>	<u>Less Garbage and Sewer not Budgeted for</u>	<u>Creston City Water Works Net Actual</u>
RECEIPTS:			
Property tax	\$ -	\$ -	\$ -
Tax increment financing collections	-	-	-
Other city tax	-	-	-
Licenses and permits	-	-	-
Use of money and property	87,026	-	87,026
Intergovernmental	-	-	-
Charges for services	3,319,585	1,402,124	1,917,461
Special assessments	-	-	-
Miscellaneous	109,918	-	109,918
	<u>\$ 3,516,529</u>	<u>\$ 1,402,124</u>	<u>\$ 2,114,405</u>
Total receipts			
DISBURSEMENTS:			
Public safety	\$ -	\$ -	\$ -
Public works	-	-	-
Health and social services	-	-	-
Culture and recreation	-	-	-
Community and economic development	-	-	-
General government	-	-	-
Debt service	-	-	-
Capital projects	-	-	-
Business type activities	3,514,964	1,402,124	2,112,840
	<u>\$ 3,514,964</u>	<u>\$ 1,402,124</u>	<u>\$ 2,112,840</u>
Total disbursements			
EXCESS OF RECEIPTS OVER DISBURSEMENTS	\$ 1,565	\$ -	\$ 1,565
OTHER FINANCING SOURCES, NET	<u>-</u>	<u>-</u>	<u>-</u>
EXCESS OF RECEIPTS AND OTHER FINANCING SOURCES OVER DISBURSEMENTS AND OTHER FINANCING USES	\$ 1,565	\$ -	\$ 1,565
BALANCE BEGINNING OF YEAR	<u>3,545,479</u>	<u>-</u>	<u>3,545,479</u>
BALANCE END OF YEAR	<u><u>\$ 3,547,044</u></u>	<u><u>\$ -</u></u>	<u><u>\$ 3,547,044</u></u>

The Notes to Financial Statements are an integral part of this statement.

Published Budget	Less City of Creston Budget	Creston City Water Works Budget	Water Works Variance Favorable (Unfavorable)
\$ 2,276,970	\$ 2,276,970	\$ -	\$ -
172,300	172,300	-	-
209,638	209,638	-	-
56,726	56,726	-	-
51,870	51,870	-	87,026
1,114,185	1,114,185	-	-
6,304,567	1,828,217	4,476,350	(2,558,889)
-	-	-	-
270,899	270,899	-	109,918
<u>\$ 10,457,155</u>	<u>\$ 5,980,805</u>	<u>\$ 4,476,350</u>	<u>\$ (2,361,945)</u>
\$ 1,433,716	\$ 1,433,716	\$ -	\$ -
1,185,335	1,185,335	-	-
-	-	-	-
433,509	433,509	-	-
35,065	35,065	-	-
1,023,379	1,023,379	-	-
1,165,227	1,165,227	-	-
195,500	195,500	-	-
5,166,597	690,247	4,476,350	2,363,510
<u>\$ 10,638,328</u>	<u>\$ 6,161,978</u>	<u>\$ 4,476,350</u>	<u>\$ 2,363,510</u>
\$ (181,173)	\$ (181,173)	\$ -	\$ 1,565
53,846	53,846	-	-
\$ (127,327)	\$ (127,327)	\$ -	<u>\$ 1,565</u>
5,039,576	5,039,576	-	
<u>\$ 4,912,249</u>	<u>\$ 4,912,249</u>	<u>\$ -</u>	

CRESTON CITY WATER WORKS
NOTES TO REQUIRED SUPPLEMENTARY INFORMATION – BUDGETARY REPORTING
June 30, 2004

In accordance with the Code of Iowa, the Board of Trustees annually adopts a budget on the cash basis following required public notice and hearing. The annual budget may be amended during the year utilizing similar statutorily prescribed procedures.

The Water Works' budget is submitted with the City of Creston's budget. 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 include 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. The Water Works budget is included in the business type activities function.

OTHER SUPPLEMENTARY INFORMATION

CRESTON CITY WATER WORKS
 SCHEDULE OF INDEBTEDNESS
 Year Ended June 30, 2004

	<u>Date Of Issue</u>	<u>Interest Rate</u>	Schedule 1 <u>Amount Originally Issued</u>
<u>OBLIGATION</u>			
Revenue Bonds:	03-21-79	4.012	\$ 1,198,000
	07-01-80	4.371	600,000

The Notes to Financial Statements are an integral part of this statement.

<u>Balance Beginning Of Year</u>	<u>Issued During Year</u>	<u>Redeemed During Year</u>	<u>Balance End Of Year</u>	<u>Interest Paid</u>	<u>Coupons Due and Unpaid</u>
\$ 707,028	\$ -	\$ 35,032	\$ 671,996	\$ 27,660	\$ -
<u>371,952</u>	<u>-</u>	<u>17,126</u>	<u>354,826</u>	<u>15,880</u>	<u>-</u>
<u><u>\$ 1,078,980</u></u>	<u><u>\$ -</u></u>	<u><u>\$ 52,158</u></u>	<u><u>\$ 1,026,822</u></u>	<u><u>\$ 43,540</u></u>	<u><u>\$ -</u></u>

CRESTON CITY WATER WORKS
BOND AND OTHER DEBT MATURITIES
June 30, 2004

Schedule 2

Year Ending June 30,	REVENUE BONDS				
	Issued March 31, 1979		Issued July 1, 1980		Total
	Interest Rates	Amount	Interest Rates	Amount	
2005	4.012%	\$ 38,420	4.371%	\$ 19,020	\$ 57,440
2006	4.012%	37,966	4.371%	18,700	56,666
2007	4.012%	39,518	4.371%	19,534	59,052
2008	4.012%	41,133	4.371%	20,405	61,538
2009	4.012%	42,814	4.371%	21,315	64,129
2010	4.012%	44,563	4.371%	22,265	66,828
2011	4.012%	46,384	4.371%	23,258	69,642
2012	4.012%	48,280	4.371%	24,295	72,575
2013	4.012%	50,253	4.371%	25,379	75,632
2014	4.012%	52,306	4.371%	26,511	78,817
2015	4.012%	54,444	4.371%	27,693	82,137
2016	4.012%	56,667	4.371%	28,928	85,595
2017	4.012%	58,985	4.371%	30,218	89,203
2018	4.012%	60,262	4.371%	31,566	91,828
2019	4.012%	-	4.371%	15,739	15,739
		<u>\$ 671,995</u>		<u>\$ 354,826</u>	<u>\$ 1,026,821</u>

See accompanying independent auditor's report.

CRESTON CITY WATER WORKS
 UNAUDITED SCHEDULE OF OPERATING STATISTICS
 Year Ended June 30, 2004

Schedule 3

	Year Ended June 30,		
	2004	2003	2002
Number of customers	3,397	3,401	3,403
Number of gallons billed	1,241,367,130	1,239,501,515	1,025,881,514
Number of gallons pumped	1,275,063,000	1,268,421,000	1,069,005,000
% of gallons billed to total pumped	97%	98%	96%

Water rates in effect at June 30, 2004

Cubic Feet Used Per Month	Rate Per 100 Cubic Feet of Usage
0 - 2,000	\$ 2.42*
2,001 - 8,000	1.86
8,001 - 32,000	1.49
32,001 and over	1.19

*Minimum charge per month is \$6.78

The Water Works and the City of Creston are covered under one insurance policy. The Water Works reimburses the City annually for its portion of the insurance premium. At June 30, 2004, the following coverages were in effect:

Fire and extended coverage:	
Buildings and contents	\$ 3,737,996
Liability:	
Umbrella excess policy	2,000,000
Linebacker liability	1,000,000
Workmen's compensation	Statutory
Comprehensive automobile policy	1,000,000
Employee Benefit Liability:	
Per occurrence	1,000,000
Aggregate	2,000,000
Employees blanket bond	100,000
Bond on Water Works manager	350,000

The foregoing operating statistics and insurance information are presented on the basis of unaudited records maintained in the Water Works office. The amounts and accuracy of the operating statistics were not investigated by the auditors.

See accompanying independent auditor's report.

INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE AND
ON INTERNAL CONTROL OVER FINANCIAL REPORTING

To the Board of Trustees of the
Creston City Water Works

We have audited the financial statements of Creston City Water Works as of and for the year ended June 30, 2004, and have issued our report thereon dated July 29, 2004. Our report expressed an unqualified opinion on the financial statements which were prepared in conformity with an other comprehensive basis of accounting. We conducted our audit in accordance with U.S. 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 Controller General of the United States.

Compliance

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

Comments involving statutory and other legal matters about the Water Works' operations for the year ended June 30, 2004, are based exclusively on knowledge obtained from procedures performed during our audit of the financial statements of the Water Works. Since our 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 year statutory comments have been resolved except for item number 7.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered Creston City Water Works' internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. However, we noted certain matters involving the internal control over financial reporting and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect Creston City Water Works' ability to record, process, summarize and report financial data consistent with the assertions of management 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. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the 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, we believe none of the reportable conditions described above is a material weakness.

This report is intended for the information of the Creston City Water Works and other parties to whom the Creston City Water Works may report and is not intended to be and should not be used by anyone other than these specified parties. However, this report is a matter of public record and its distribution is not limited.

We would like to acknowledge the many courtesies and assistance extended to us by personnel of the Creston City Water Works during the course of our audit. Should you have any questions concerning any of the above matters, we shall be pleased to discuss them with you at your convenience.

Drapen, Smidgrass, Mickelson + Co., P.C.

July 29, 2004

CRESTON CITY WATER WORKS
SCHEDULE OF FINDINGS
Year Ended June 30, 2004

Reportable Conditions:

Segregation of duties: A limited number of people have primary responsibility for most of the accounting and financial duties. As a result, some of the aspects of accounting internal controls which rely on adequate segregation of duties, for all reasonable purposes, are missing in the Creston City Water Works.

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

Response: We have reviewed this recommendation and we will review our procedures to obtain the maximum control possible.

Auditor's Conclusion: Response accepted.

Other Findings Related to Required Statutory Reporting:

- (1) Depository Banks - A resolution naming official depositories has been adopted by the board of trustees. The maximum deposit amounts stated in the resolution were not exceeded during the year ended June 30, 2004.
- (2) Certified Budget - Water Works' expenditures during the year ended June 30, 2004, did not exceed amounts budgeted.
- (3) Questionable Disbursements - We noted no disbursements that may not meet the requirements of public purpose as defined in an Attorney General's opinion dated April 25, 1979.
- (4) Travel Expense - No expenditures of Water Works' money for travel expenses of spouses of Water Works' officials or employees were noted.
- (5) Business Transactions – No business transactions between the Water Works and Water Works' officials or employees were noted.
- (6) Bond Coverage - Surety bond coverage of Water Works' 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.

- (7) Board Minutes - No transactions were found that we believe should have been approved in the Board minutes but were not.

The Water Works published all annual gross salaries as required by an Attorney General's opinion dated April 12, 1979.

- (a) Although the Board minutes were published, they were not published within fifteen days as required by Chapter 372.13(6) of the Code of Iowa.

Auditor's Recommendation - We recommend the Water Works comply with Chapter 372.13(6) of the Code of Iowa.

Water Works' Response - The Creston City Water Works Board of Trustees meets once a month on the second Tuesday of the month. The minutes from the previous meeting need to be approved by the Board before publication. This requires 30-35 days before publication can be met. The City of Creston Water Works will request modification to the Code of Iowa so publication requirements can be met.

Auditor's Conclusion - Response accepted.

- (8) Revenue Bonds - The Water Works has complied with the provisions of the revenue bond indentures.
- (9) Deposits and Investments - The Water Works has adopted a written investment policy as required by Chapter 12B.10B of the Code of Iowa.

No instances of non-compliance with the deposit and investment provisions of Chapter 12B and 12C of the Code of Iowa and the Water Works' investment policy were noted.