

LENOX MUNICIPAL UTILITIES

FINANCIAL STATEMENTS

DECEMBER 31, 2004

LENOX MUNICIPAL UTILITIES
LENOX, IOWA
DECEMBER 31, 2004

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LENOX MUNICIPAL UTILITIES
OFFICIALS
DECEMBER 31, 2004

<u>NAME OF OFFICIAL</u>	<u>TITLE</u>	<u>TERM EXPIRES</u>
Dennis Bunch	Trustee - Chairman	May 1, 2008
Norbert Bradley	Trustee	May 1, 2006
Winston Tyler	Trustee	May 1, 2010
David D. Ferris	Superintendent	

DEAN M. BROICH, P.C.
CERTIFIED PUBLIC ACCOUNTANT

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Omaha, Nebraska 68144
(402) 829-0121

INDEPENDENT AUDITOR'S REPORT

To the Board of Trustees
Lenox Municipal Utilities
Lenox, Iowa

To the Board of Trustees:

I have audited the accompanying financial statements of the Lenox Municipal Utilities, Lenox, Iowa, a component unit of the City of Lenox, as of and for the years ended December 31, 2004 and 2003, as listed in the table of contents. These financial statements are the responsibility of the Lenox Municipal Utilities' management. My responsibility is to express an opinion on these financial statements based on my audit.

I conducted my audit in accordance with auditing standards generally accepted in 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 of America. Those standards 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 management, as well as evaluating the overall financial statement presentation. I believe that my audit provides a reasonable basis for my opinion.

Lenox Municipal Utilities, Lenox, Iowa has not presented management's discussion and analysis, that accounting principles generally accepted in the United States of America has determined is necessary to supplement, although not required to be part of, the financial statements.

As discussed in footnote 1, the financial statements present only the Lenox Municipal Utilities and do not purport to, and do not, present fairly the financial position of the City of Lenox, Lenox, Iowa, and the changes in its financial position and cash flows, where applicable, in conformity with accounting principles generally accepted in the United States of America.

In my opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Lenox Municipal Utilities as of December 31, 2004 and 2003, and the results of its operations and the changes in its financial position for the years then ended in conformity with accounting principles generally accepted in the United States of America. Also, the statement of budgeted and actual cash receipts and disbursements presents fairly, in all material respects, the cash transactions and the legally adopted budget for the years ended December 31, 2004 and 2003.

In accordance with *Government Auditing Standards*, I have also issued a report dated January 18, 2005 on my consideration of Lenox Municipal Utility's internal control structure over financial reporting and my tests of its compliance with certain provisions of laws, regulations, 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 the audit report in considering the results of my audit.

A handwritten signature in black ink, appearing to read "Dan M. Broich". The signature is written in a cursive style with a large initial "D".

Certified Public Accountant

Omaha, Nebraska
January 18, 2005

LENOX MUNICIPAL UTILITIES
BALANCE SHEETS
DECEMBER 31, 2004 AND 2003

ASSETS

	2004		Combined Memorandum Only
	Electric	Water	
Current assets:			
Cash	\$ 53,506	\$ 29,147	\$ 82,653
Receivables	89,924	38,347	128,271
Accrued interest receivable	358	94	452
Prepaid expenses	6,151	3,175	9,326
Inventories	64,713		64,713
Total current assets	214,652	70,763	285,415
Property and equipment - net	1,558,590	644,270	2,202,860
Other assets:			
Investments - long-term portion	1,228,735	330,943	1,559,678
Bond sinking fund - restricted	41,098	15,300	56,398
Bond reserve fund - restricted	51,500	30,515	82,015
Deferred compensation - restricted	46,020	25,315	71,335
Total other assets	1,367,353	402,073	1,769,426
Total assets	\$ 3,140,595	\$ 1,117,106	\$ 4,257,701

LIABILITIES AND RETAINED EARNINGS

Current liabilities:			
Accounts payable - trade	\$ 63,007	\$ 14,806	\$ 77,813
Current portion of long-term debt	45,000	7,119	52,119
Accrued interest	2,566	12,483	15,049
Accrued expenses	6,765	3,760	10,525
Customer deposits	9,000		9,000
Total current liabilities	126,338	38,168	164,506
Long-term liabilities:			
Deferred compensation	46,020	25,315	71,335
Note and bonds payable	425,000	388,399	813,399
Total long-term liabilities	471,020	413,714	884,734
Retained earnings - reserved		45,815	45,815
Retained earnings - unreserved	2,543,237	619,409	3,162,646
Total retained earnings	2,543,237	665,224	3,208,461
Total liabilities and retained earnings	\$ 3,140,595	\$ 1,117,106	\$ 4,257,701

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

LENOX MUNICIPAL UTILITIES
BALANCE SHEETS
DECEMBER 31, 2004 AND 2003

ASSETS

	2003		Combined Memorandum Only
	Electric	Water	
Current assets:			
Cash	\$ 52,878	\$ 30,614	\$ 83,492
Receivables	95,619	36,682	132,301
Accrued interest receivable	233	149	382
Prepaid expenses	6,044	2,863	8,907
Inventories	41,750		41,750
Total current assets	<u>196,524</u>	<u>70,308</u>	<u>266,832</u>
Property and equipment - net	<u>956,471</u>	<u>698,570</u>	<u>1,655,041</u>
Other assets:			
Investments - long-term portion	1,458,419	266,665	1,725,084
Bond reserve fund - restricted		30,515	30,515
Bond sinking fund - restricted		51,975	51,975
Deferred compensation - restricted	41,769	22,322	64,091
Total other assets	<u>1,500,188</u>	<u>371,477</u>	<u>1,871,665</u>
Total assets	<u>\$ 2,653,183</u>	<u>\$ 1,140,355</u>	<u>\$ 3,793,538</u>

LIABILITIES AND RETAINED EARNINGS

Current liabilities:			
Accounts payable - trade	\$ 116,425	\$ 11,745	\$ 128,170
Current portion of long-term debt	-	6,711	6,711
Accrued interest	-	12,364	12,364
Accrued expenses	4,866	2,558	7,424
Customer deposits	8,150		8,150
Total current liabilities	<u>129,441</u>	<u>33,378</u>	<u>162,819</u>
Long-term liabilities:			
Deferred compensation	41,769	22,322	64,091
Note payable	-	395,518	395,518
Total long-term liabilities	<u>41,769</u>	<u>417,840</u>	<u>459,609</u>
Retained earnings - reserved	-	82,490	82,490
Retained earnings - unreserved	2,481,973	606,647	3,088,620
Total retained earnings	<u>2,481,973</u>	<u>689,137</u>	<u>3,171,110</u>
Total liabilities and retained earnings	<u>\$ 2,653,183</u>	<u>\$ 1,140,355</u>	<u>\$ 3,793,538</u>

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

LENOX MUNICIPAL UTILITIES
STATEMENTS OF REVENUES, EXPENSES AND
CHANGES IN RETAINED EARNINGS
FOR THE YEARS ENDED DECEMBER 31, 2004 AND 2003

	2004		Combined Memorandum Only
	Electric	Water	
Operating revenues:			
Current use charges	\$ 978,519	\$ 422,350	\$ 1,400,869
Wind turbine generation	47,085	-	47,085
Miscellaneous and rentals	7,842	13,860	21,702
Total operating revenues	<u>1,033,446</u>	<u>436,210</u>	<u>1,469,656</u>
Operating expenses:			
Administrative	114,649	38,312	152,961
Sales and use taxes	35,267	22,137	57,404
Payroll and payroll taxes	167,312	92,038	259,350
Office expense	11,476	2,684	14,160
Repairs and maintenance	6,546	5,531	12,077
Plant expense	501,507	200,994	702,501
Distribution expense	52,953	22,413	75,366
Bad debts	4,262	1,820	6,082
Depreciation	101,827	54,300	156,127
Total operating expenses	<u>995,799</u>	<u>440,229</u>	<u>1,436,028</u>
Operating income (loss)	<u>37,647</u>	<u>(4,019)</u>	<u>33,628</u>
Non-operating revenues/(expenses):			
Interest income	11,106	3,115	14,221
Interest expense	(18,357)	(24,042)	(42,399)
Total non-operating revenues/ (expenses)	<u>(7,251)</u>	<u>(20,927)</u>	<u>(28,178)</u>
Income (loss) before operating transfers	30,396	(24,946)	5,450
Operating transfers from City	<u>30,868</u>	<u>1,033</u>	<u>31,901</u>
Net income (loss)	61,264	(23,913)	37,351
Retained earnings, beginning of year	<u>2,481,973</u>	<u>689,137</u>	<u>3,171,110</u>
Retained earnings, end of year	<u>\$ 2,543,237</u>	<u>\$ 665,224</u>	<u>\$ 3,208,461</u>

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

LENOX MUNICIPAL UTILITIES
STATEMENTS OF REVENUES, EXPENSES AND
CHANGES IN RETAINED EARNINGS
FOR THE YEARS ENDED DECEMBER 31, 2004 AND 2003

	2003		Combined Memorandum Only
	Electric	Water	
Operating revenues:			
Current use charges	\$ 927,501	\$ 415,689	\$ 1,343,190
Wind turbine generation	859,859	-	859,859
Miscellaneous and rentals	19,154	11,024	30,178
Total operating revenues	<u>1,806,514</u>	<u>426,713</u>	<u>2,233,227</u>
Operating expenses:			
Administrative	103,398	33,128	136,526
Sales and use taxes	28,148	17,120	45,268
Payroll and payroll taxes	160,215	85,621	245,836
Office expense	13,104	2,808	15,912
Repairs and maintenance	8,082	4,246	12,328
Plant expense	493,879	216,277	710,156
Wind turbine operations	885,118		885,118
Distribution expense	37,019	8,347	45,366
Bad debts	2,775	923	3,698
Depreciation	59,624	56,067	115,691
Total operating expenses	<u>1,791,362</u>	<u>424,537</u>	<u>2,215,899</u>
Operating income	<u>15,152</u>	<u>2,176</u>	<u>17,328</u>
Non-operating revenues/(expenses):			
Interest income	11,301	2,764	14,065
Interest expense	-	(23,985)	(23,985)
Total non-operating revenues/ (expenses)	<u>11,301</u>	<u>(21,221)</u>	<u>(9,920)</u>
Income (loss) before operating transfers	26,453	(19,045)	7,408
Operating transfers from City	<u>21,984</u>	<u>3,251</u>	<u>25,235</u>
Net income (loss)	48,437	(15,794)	32,643
Retained earnings, beginning of year	<u>2,433,536</u>	<u>704,931</u>	<u>3,138,467</u>
Retained earnings, end of year	<u>\$ 2,481,973</u>	<u>\$ 689,137</u>	<u>\$ 3,171,110</u>

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

LENOX MUNICIPAL UTILITIES
STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2004 AND 2003

	2004		Combined Memorandum Only
	Electric	Water	
Cash flows from operating activities:			
Cash received from customers	\$ 1,031,299	\$ 420,685	\$ 1,451,984
Cash payments to suppliers	(798,625)	(289,576)	(1,088,201)
Cash payments employees, payroll taxes and benefits	(169,211)	(92,340)	(261,551)
Other revenues	7,842	13,860	21,702
Net cash provided by operating activities	<u>71,305</u>	<u>52,629</u>	<u>123,934</u>
Cash flows from noncapital financing activities:			
Operating transfers from City	<u>30,868</u>	<u>1,033</u>	<u>31,901</u>
Net cash provided from noncapital financing activities	<u>30,868</u>	<u>1,033</u>	<u>31,901</u>
Cash flows from capital and related financing activities:			
Proceeds from revenue bonds	515,000		515,000
Payment on principal	(45,000)	(6,711)	(51,711)
Interest paid	(15,791)	(24,042)	(39,833)
Purchase of fixed assets	<u>(703,946)</u>	<u>-</u>	<u>(703,946)</u>
Net cash used for capital and related financing activities	<u>(249,737)</u>	<u>(30,753)</u>	<u>(280,490)</u>
Cash flows from investing activities:			
Purchase of investments	(132,373)	(27,491)	(159,864)
Proceeds from investments	269,459	-	269,459
Interest on investments	<u>11,106</u>	<u>3,115</u>	<u>14,221</u>
Net cash provided (used) by investment activities	<u>148,192</u>	<u>(24,376)</u>	<u>123,816</u>
Net increase (decrease) in cash	628	(1,467)	(839)
Cash - beginning of year	<u>52,878</u>	<u>30,614</u>	<u>83,492</u>
Cash - end of year	<u>\$ 53,506</u>	<u>\$ 29,147</u>	<u>\$ 82,653</u>

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

LENOX MUNICIPAL UTILITIES
STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2004 AND 2003

	2003		Combined Memorandum Only
	Electric	Water	
Cash flows from operating activities:			
Cash received from customers	\$ 1,772,285	\$ 410,287	\$ 2,182,572
Cash payments to suppliers	(1,491,569)	(292,113)	(1,783,682)
Cash payments employees, payroll taxes and benefits	(161,702)	(86,293)	(247,995)
Other revenues	19,154	11,024	30,178
Net cash provided by operating activities	<u>138,168</u>	<u>42,905</u>	<u>181,073</u>
Cash flows from noncapital financing activities:			
Operating transfers from City	<u>21,984</u>	<u>3,251</u>	<u>25,235</u>
Net cash provided from noncapital financing activities	<u>21,984</u>	<u>3,251</u>	<u>25,235</u>
Cash flows from capital and related financing activities:			
Payment on principal	-	(6,401)	(6,401)
Interest paid	-	(23,985)	(23,985)
Purchase of fixed assets	<u>(147,153)</u>	<u>-</u>	<u>(147,153)</u>
Net cash used for capital and related financing activities	<u>(147,153)</u>	<u>(30,386)</u>	<u>(177,539)</u>
Cash flows from investing activities:			
Purchase of investments	(50,447)	(37,042)	(87,489)
Proceeds from investments	13,735	25,000	38,735
Interest on investments	<u>11,301</u>	<u>2,764</u>	<u>14,065</u>
Net cash used by investment activities	<u>(25,411)</u>	<u>(9,278)</u>	<u>(34,689)</u>
Net increase (decrease) in cash	(12,412)	6,492	(5,920)
Cash - beginning of year	<u>65,290</u>	<u>24,122</u>	<u>89,412</u>
Cash - end of year	<u>\$ 52,878</u>	<u>\$ 30,614</u>	<u>\$ 83,492</u>

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

LENOX MUNICIPAL UTILITIES
STATEMENTS OF CASH FLOWS-CONTINUED
FOR THE YEARS ENDED DECEMBER 31, 2004 AND 2003

SCHEDULE OF NET CASH FROM OPERATING ACTIVITIES

	2004		Combined Memorandum Only
	Electric	Water	
Operating income (loss)	\$ 37,647	\$ (4,019)	\$ 33,628
Adjustments to reconcile operating income to net cash provided by operations:			
Depreciation	101,827	54,300	156,127
Changes in assets and liabilities:			
Receivables	5,695	(1,665)	4,030
Accrued interest receivable	(125)	55	(70)
Prepaid expenses	(107)	(312)	(419)
Inventories	(22,963)		(22,963)
Sinking fund	-	(112)	(112)
Accounts payable	(53,418)	3,061	(50,357)
Accrued interest	-	119	119
Accrued expenses	1,899	1,202	3,101
Customer deposits	850	-	850
Net cash provided by operating activities	<u>\$ 71,305</u>	<u>\$ 52,629</u>	<u>\$ 123,934</u>

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

LENOX MUNICIPAL UTILITIES
STATEMENTS OF CASH FLOWS-CONTINUED
FOR THE YEARS ENDED DECEMBER 31, 2004 AND 2003

SCHEDULE OF NET CASH FROM OPERATING ACTIVITIES

	2003		Combined Memorandum Only
	Electric	Water	
Operating income	\$ 15,152	\$ 2,176	\$ 17,328
Adjustments to reconcile operating income to net cash provided by operations:			
Depreciation	59,624	56,067	115,691
Changes in assets and liabilities:			
Receivables	(15,075)	(5,402)	(20,477)
Accrued interest receivable	90	43	133
Prepaid expenses	(797)	(160)	(957)
Inventories	5,352	-	5,352
Accounts payable	72,335	(10,360)	61,975
Accrued interest		(130)	(130)
Accrued expenses	1,487	671	2,158
Customer deposits	-	-	-
Net cash provided by operating activities	<u>\$ 138,168</u>	<u>\$ 42,905</u>	<u>\$ 181,073</u>

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

LENOX MUNICIPAL UTILITIES
STATEMENTS OF BUDGETED AND ACTUAL CASH RECEIPTS AND DISBURSEMENTS
FOR THE YEARS ENDED DECEMBER 31, 2004 AND 2003

ELECTRIC FUND

	2004 Budgeted	2004 Actual	2003 Actual
Revenues	\$ 907,211	\$ 1,033,446	\$ 946,655
Expenses	<u>971,104</u>	<u>1,095,496</u>	<u>1,791,362</u>
Excess revenues over expenses from operations	(63,893)	(62,050)	(844,707)
Other revenues	<u>86,070</u>	<u>41,974</u>	<u>893,144</u>
Excess revenues over expenses	<u>\$ 22,177</u>	<u>\$ (20,076)</u>	<u>\$ 48,437</u>

WATER FUND

Revenues	\$ 382,927	\$ 436,210	\$ 426,713
Expenses	<u>409,896</u>	<u>464,271</u>	<u>448,522</u>
Excess revenues over/(under) expenses from operations	(26,969)	(28,061)	(21,809)
Other revenues	<u>36,330</u>	<u>4,148</u>	<u>6,015</u>
Excess revenues over/(under) expenses	<u>\$ 9,361</u>	<u>\$ (23,913)</u>	<u>\$ (15,794)</u>

COMBINED - (MEMORANDUM ONLY)

Revenues	\$ 1,290,138	\$ 1,469,656	\$ 1,373,368
Expenses	<u>1,381,000</u>	<u>1,559,767</u>	<u>2,239,884</u>
Excess revenues over/(under) expenses from operations	(90,862)	(90,111)	(866,516)
Other revenues	<u>122,400</u>	<u>46,122</u>	<u>899,159</u>
Excess revenues over expenses	<u>\$ 31,538</u>	<u>\$ (43,989)</u>	<u>\$ 32,643</u>

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

LENOX MUNICIPAL UTILITIES
STATEMENTS OF BUDGETED AND ACTUAL CASH RECEIPTS AND DISBURSEMENTS
FOR THE YEARS ENDED DECEMBER 31, 2004 AND 2003

ELECTRIC FUND

	2003 Budgeted	2003 Actual	2002 Actual
Revenues	\$ 931,833	\$ 946,655	\$ 947,944
Expenses	<u>1,875,249</u>	<u>1,791,362</u>	<u>942,036</u>
Excess revenues over expenses from operations	(943,416)	(844,707)	5,908
Other revenues	<u>932,316</u>	<u>893,144</u>	<u>42,442</u>
Excess revenues over expenses	<u>\$ (11,100)</u>	<u>\$ 48,437</u>	<u>\$ 48,350</u>

WATER FUND

Revenues	\$ 415,877	\$ 426,713	\$ 386,746
Expenses	<u>417,402</u>	<u>448,522</u>	<u>426,864</u>
Excess revenues over/(under) expenses from operations	(1,525)	(21,809)	(40,118)
Other revenues	<u>6,908</u>	<u>6,015</u>	<u>6,234</u>
Excess revenues over/(under) expenses	<u>\$ 5,383</u>	<u>\$ (15,794)</u>	<u>\$ (33,884)</u>

COMBINED - (MEMORANDUM ONLY)

Revenues	\$ 1,347,710	\$ 1,373,368	\$ 1,334,690
Expenses	<u>2,292,651</u>	<u>2,239,884</u>	<u>1,368,900</u>
Excess revenues over/(under) expenses from operations	(944,941)	(866,516)	(34,210)
Other revenues	<u>939,224</u>	<u>899,159</u>	<u>48,676</u>
Excess revenues over expenses	<u>\$ (5,717)</u>	<u>\$ 32,643</u>	<u>\$ 14,466</u>

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

LENOX MUNICIPAL UTILITIES
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2004

1. Summary of Significant Accounting Policies

Basis of Accounting:

Lenox Municipal Electric and Water Utilities operate under a Trustee-Supervisor form of government and provide electricity and water to the City of Lenox and the surrounding community. The Utilities operate as enterprise funds which utilize the accrual basis of accounting. The accrual basis of accounting recognizes revenues when earned and expenses when incurred.

Allowance for Doubtful Accounts:

Management charges off uncollectible accounts to operations when it is determined that they are uncollectible. At December 31, 2004 and 2003, accounts receivable were considered to be fully collectible and therefore, these financial statements do not contain an allowance for doubtful accounts.

The Reporting Entity:

The Utilities, for financial statement purposes, include all of the funds and account groups relevant to the operation of the Electric and Water facilities. The Utilities also provide billing and collection services for the City of Lenox, however these amounts have been eliminated for financial statement purposes. These financial statements do not reflect any activity or transactions of the City of Lenox and do not present consolidated information.

Fund Accounting:

The electric and water funds operate similar to business enterprises. The intent of the governing body is that the cost, including depreciation, of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges.

Cash and Cash Equivalents:

For the purpose of the presentation of the statement of cash flows, the Electric and Water Funds do not treat investments (restricted or unrestricted) as cash or cash equivalents.

Use of Estimates:

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

Reclassifications:

Certain amounts or presentations in the December 31, 2003 statements have been reclassified to conform to the December 31, 2004 presentation. Net income (loss) remained unchanged as a result of any reclassifications.

LENOX MUNICIPAL UTILITIES
NOTES TO FINANCIAL STATEMENTS - CONTINUED
DECEMBER 31, 2004

Budgets and Budgetary Accounting

In accordance with the Code of Iowa, the Utilities annually adopt a budget on the cash basis following required public notice. Accordingly, the budget to actual comparisons are presented on a non-GAAP budgetary basis in the accompanying financial statements. The adjustments necessary to reconcile the differences between the two methods of accounting are summarized as follows:

	2004		
	Electric	Water	Combined Memorandum Only
Net income (loss) - budgetary basis	\$ 88,258	\$ (21,565)	\$ 66,693
Increase (decrease) in:			
Receivables	(5,695)	1,665	(4,030)
Accrued interest receivable	125	(55)	70
Prepaid expenses	107	312	419
Inventories	22,963		22,963
Sinking fund	(92,598)	112	(92,486)
 (Increase)/decrease in:			
Accounts payable	53,418	(3,061)	50,357
Accrued interest payable	(2,566)	(119)	(2,685)
Accrued expenses	(1,898)	(1,202)	(3,100)
Other current liabilities	(850)	-	(850)
 Net income (loss) - accrual (GAAP basis)	\$ 61,264	\$ (23,913)	\$ 37,351
	2003		
	Electric	Water	Combined Memorandum Only
Net income (loss) - budgetary basis	\$ 120,707	\$ (61,731)	\$ 58,976
Increase (decrease) in:			
Receivables	15,075	5,402	20,477
Accrued interest receivable	(90)	(43)	(133)
Prepaid expenses	797	160	957
Inventories	(5,352)	-	(5,352)
Sinking fund		30,600	30,600
 (Increase)/decrease in:			
Accounts payable	(72,335)	10,360	(61,975)
Accrued interest payable		130	130
Accrued expenses	(1,487)	(672)	(2,159)
Other current liabilities	(8,878)	-	(8,878)
 Net income (loss) - accrual (GAAP basis)	\$ 48,437	\$ (15,794)	\$ 32,643

LENOX MUNICIPAL UTILITIES
NOTES TO FINANCIAL STATEMENTS - CONTINUED
DECEMBER 31, 2004

3. Deposits and Investments

The Utilities are authorized to invest in interest bearing savings accounts, interest bearing money market accounts, interest bearing checking accounts, obligations of the United States government or its agencies and instrumentalities, certificates of deposit and other evidence of deposit at federally insured Iowa depository institutions approved and secured pursuant to Chapter 453; Iowa Public Agency Investment Trust and certain other investments with prior approval by the board of trustees.

The Utilities deposits and investments are categorized to give an indication of the level of risk assumed by the Utilities at December 31, 2004 and 2003.

Category A

Includes accounts and deposits which are fully insured. Carrying values and market values of Category A funds amounted to \$140,000 and \$140,000 in 2004 and 2003, respectively.

Non-Categorized

The Utilities had deposits and investments with Iowa Public Agency Investment Trust with carrying and market values of \$1,640,744 and \$1,751,066 in 2004 and 2003, respectively.

4. Inventories

Inventories consist mainly of electrical materials and supplies and are valued at lower of cost or market value (first-in, first-out).

5. Property and equipment

Depreciation is provided using the straight-line method over the estimated economic useful lives of the respective assets.

<u>Property and Equipment</u>	<u>2004</u>		<u>Combined Memorandum Only</u>
	<u>Electric</u>	<u>Water</u>	
Land	\$ -	\$ 32,000	\$ 32,000
Buildings and plants	1,853,585	909,042	2,762,627
Distribution system	775,086	658,046	1,433,132
Sub-station	425,994	-	425,994
Transmission line	98,652	-	98,652
Automotive equipment		<u>58,936</u>	<u>58,936</u>
Total	<u>3,153,317</u>	<u>1,658,024</u>	<u>4,811,341</u>
Less: accumulated depreciation	<u>1,594,727</u>	<u>1,013,754</u>	<u>2,608,481</u>
Property and equipment - net	<u>\$ 1,558,590</u>	<u>\$ 644,270</u>	<u>\$ 2,202,860</u>

LENOX MUNICIPAL UTILITIES
NOTES TO FINANCIAL STATEMENTS - CONTINUED
DECEMBER 31, 2004

5. Property and equipment - (Continued)

<u>Property and Equipment</u>	2003		Combined Memorandum
	Electric	Water	Only
Land	\$ -	\$ 32,000	\$ 32,000
Buildings and plants	1,266,712	909,042	2,175,754
Distribution system	679,142	658,046	1,337,188
Sub-station	425,994	-	425,994
Transmission line	77,523	-	77,523
Automotive equipment	-	58,936	58,936
Total	2,449,371	1,658,024	4,107,395
Less: accumulated depreciation	1,492,900	959,454	2,452,354
Property and equipment - net	\$ 956,471	\$ 698,570	\$ 1,655,041

6. Pension and Retirement Benefits

Lenox Municipal Utilities 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 covered salary and Lenox Municipal Utilities is required to contribute 5.75% of annual covered payroll, respectively. Contribution requirements are established by State statute. Lenox Municipal Utilities contribution to IPERS for the years ended December 31, 2004 and 2003 were \$23,419 and \$22,066, respectively, equal to the required contributions for each year.

7. Deferred Compensation

Lenox Municipal Utilities offer all full-time employees the option of participating in the ICMA Retirement Corporation's Deferred Compensation Plan. Under the plan, an employee may elect to have up to a maximum of 25% of compensation or \$13,000 a year, whichever is smaller, withheld and invested with ICMA. The salary of the employee that is deferred is not taxable for federal income tax purposes to the employee until retirement, but is taxable for social security and state income taxes and is included in determining IPERS contributions (see Note 6). The employer retains ownership of the fund until paid or made available to participants, subject only to the claims of the government's general creditors. A written contract exists with each plan participant and the Utilities responsibility is limited to the payment of the deferred compensation to the plan. For the years ended December 31, 2004 and 2003, five employees participated in the plan and contributions amounted to \$4,335 and \$4,750 respectively. The unfunded balance at December 31, 2004 and 2003 amounted to \$195 and \$190, respectively.

LENOX MUNICIPAL UTILITIES
NOTES TO FINANCIAL STATEMENTS - CONTINUED
DECEMBER 31, 2004

8. Electric Revenue Notes

In 2003, Lenox Municipal Utilities was the sub-recipient of a Community Development Block Grant issued to the City of Lenox, Iowa by the Iowa Department of Economic Development. The City of Lenox received CDGB funds in the amount of \$400,000. The City of Lenox entered into a construction and operation agreement and designated the Lenox Municipal Utilities a sub-recipient of the Grant money to construct and operate a Wind Turbine for the benefit of the Lenox community. In conjunction with the construction of the wind turbine, Lenox Municipal Utilities was required to provide all funds in excess of the \$400,000 grant. Electric Revenue Notes were issued in the amount of \$515,000, to replace construction reserves for extension lines which were used in the construction of the wind turbine. The Electric Revenue Notes dated May 1, 2003 were issued in \$5,000 denominations or multiples thereof, and mature on May 1 of each year. Interest on the notes are payable semi-annually on May 1 and November 1 of each year the notes are outstanding. Interest paid in 2004 and 2003 on the Electric Revenue Notes amounted to \$15,791 and \$ -0-, respectively.

Principal payments on the Electric Revenue Notes are due as follows:

	<u>Principal</u>	<u>Interest</u>
2005	\$ 45,000	\$ 14,936
2006	45,000	13,935
2007	50,000	12,708
2008	50,000	11,258
2009	50,000	9,670
2010 - 2014	<u>230,000</u>	<u>18,730</u>
	<u>\$ 470,000</u>	<u>\$ 81,237</u>

The operating agreement provides that City shall repay Lenox Municipal Utilities for the contributions made by Lenox Municipal Utilities to purchase the wind turbine. The City also agreed to reimburse the Utility for and amount of dollars which will be adequate for the operation, maintenance, insurance, and long term equipment repair and replacement cost of the wind turbine generator. The operating agreement is in effect for a period of 20 years from the effective date of the agreement. The agreement provides that at the time of termination of the agreement, the City of Lenox will assign all accompanying responsibilities for the wind turbine generator to Lenox Municipal Utilities.

Note payments, reserves, sinking funds and related reserves are payable solely from the Net Revenues of the Electric System. The notes are callable May 1, 2010.

Funds are restricted in conjunction with the issuance of Electric Revenue Notes to assist with the construction and operation of a Wind Turbine. The Electric Reserve Fund is funded by the Gross Revenues of the Electric System and shall be used to maintain and operate the Electric System, and after payment of the operating expenses shall, to the extent herein provided, be used to pay the principal and interest on the Electric Revenue Notes and to create and maintain the Electric Revenue Sinking Fund. At December 31, 2004 and 2003, funds accumulated amounted to \$51,500 and \$ -0- , respectively.

Electric Revenue Sinking Fund payments are required on a monthly basis to be used solely for payment of principal and interest on the Electric Revenue Notes. Note sinking payments are to be funded at no less than one-twelfth of the installment maturing each May 1. At December 31, 2004 and 2003, Electric Revenue Sinking Funds amounted to \$41,098 and \$ - 0 - , respectively.

LENOX MUNICIPAL UTILITIES
NOTES TO FINANCIAL STATEMENTS - CONTINUED
DECEMBER 31, 2004

9. Long-term Debt – Water Fund

Lenox Municipal Utilities incurred debt in 1990 in conjunction with an undivided interest in a water line jointly constructed by Southern Iowa Rural Water Association (SIRWA). Parties to the contract were Taylor County, City of Lenox, the Municipal Waterworks Board (Lenox) and SIRWA. Terms of the contract are for 40 years and allows Lenox and Taylor County the perpetual right to use the water transmission line and to purchase established maximum capacities of water. There are no minimum purchase requirements. Lenox Municipal Utilities incurred debt from Rural Economic and Community Development in the original amount of \$453,000. The note matures July 1, 2029 and is payable annually on July 1 in installments of \$30,515, including principal and interest. The note bears interest at the rate of 6 percent.

Maturities of long-term debt are as follows:

	<u>Principal</u>	<u>Interest</u>
2005	\$ 7,119	\$ 23,396
2006	7,540	22,975
2007	7,993	22,522
2008	8,472	22,043
2009	8,980	21,535
2010 - 2014	53,661	98,914
2015 - 2019	71,810	80,765
2020 - 2024	96,098	56,477
2025 - 2029	<u>133,845</u>	<u>18,730</u>
	<u>\$ 395,518</u>	<u>\$ 367,357</u>

Funds are restricted in conjunction with the issuance of Rural Economic and Community Development debt. The bond reserve fund was funded at the rate of \$255 per month until the sum of \$30,515 had been accumulated. At December 31, 2004 and 2003, funds accumulated amounted to \$30,515. The reserve fund is to be transferred to the sinking fund whenever necessary to prevent or remedy a default in the payment of the principal and interest to Rural Economic and Community Development .

Bond sinking fund payments are required on a monthly basis to be used solely for payment of principal and interest on the Rural Economic and Community Development note. Bond sinking payments are to be funded at no less than one-twelfth of the installment maturing each July 1. At December 31, 2004 and 2003, sinking funds amounted to \$15,300 and \$51,975, respectively.

10. Risk Management

The Utility 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.

LENOX MUNICIPAL UTILITIES
NOTES TO FINANCIAL STATEMENTS - CONTINUED
DECEMBER 31, 2004

11. Off Balance Sheet and Concentration of Credit Risk

The Utilities receivables are due from customers for electric and water charges for the City of Lenox, Iowa and the surrounding community. None of the receivables are collateralized. To date, these concentrations of credit risk have not had an adverse effect on the results of operations of the Utilities.

DEAN M. BROICH, P.C.
CERTIFIED PUBLIC ACCOUNTANT

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**REPORT ON COMPLIANCE AND ON INTERNAL CONTROL OVER FINANCIAL
REPORTING BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED
IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS**

To the Board of Trustees
Lenox Municipal Utilities
Lenox, Iowa

I have audited the financial statements of the Lenox Municipal Utilities, Lenox, Iowa as of and for the year ended December 31, 2004, and have issued my report thereon dated January 18, 2005. I conducted my audit in accordance with auditing standards generally accepted in 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 of America.

Compliance

As part of obtaining reasonable assurance about whether Lenox Municipal Utilities' financial statements are free of material misstatement, I 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 my audit and, accordingly, I do not express such an opinion. The results of my tests disclosed instances of noncompliance that are required to be reported under *Government Auditing Standards* which are described in the accompanying schedule of findings and questioned costs. I also noted certain immaterial instances of noncompliance, which were communicated to and discussed with the management of Lenox Municipal Utilities.

Comments involving statutory and other legal matters about Lenox Municipal Utilities' operations for the year ended December 31, 2004 are based exclusively on knowledge obtained from procedures performed during my audit of the financial statements of Lenox Municipal Utilities. 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 year statutory comments, if any, have been satisfactorily resolved.

Internal Control Over Financial Reporting

In planning and performing my audit, I considered Lenox Municipal Utilities' 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 judgement, could adversely affect the Utilities ability to record, process, summarize and report financial data

Internal Control Over Financial Reporting – (Continued)

consistent with the assertions of management in the financial statements. Current and prior year reportable conditions are as follows:

- A. Segregation of duties - Cash receipts, billings, and postings to customer's accounts are incompatible duties which are often performed by the same people. Segregation of duties is an important aspect in any system of internal controls to prevent individuals from performing incompatible duties.

Recommendation - While segregation of duties is difficult with a limited number of personnel, management should review its operating procedures at regular intervals to obtain the maximum internal control possible.

Response - Based on monthly reviews of internally prepared financial statements and overall supervision by the superintendent and the Board, there appear to be sufficient controls. Part-time employees assist in the accounting and billing cycles at various intervals.

Conclusion - Response accepted.

- B. Facsimile signature stamps - Facsimile signature stamps are used to facilitate payment of vouchers. Without proper controls or retention of the stamps internal control is not effective. Unauthorized use of the stamps on disbursements or other documents could occur.

Recommendation - Eliminate the stamps or provide adequate controls against their unauthorized use.

Response - The stamps are retained by office personnel, locked in the Utilities safe, and are only used by the respective board member for check signing purposes. All other documents are signed manually. Also, all vouchers paid are approved at monthly meetings and reconciliations are performed monthly.

Conclusion - Response accepted.

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 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, I believe the above items are material weaknesses. Prior year reportable conditions have been resolved except for the segregation of duties and the use of facsimile signature stamps.

This report is intended solely for the information and use of the audit committee, management and trustees within the organization, the Lenox City Council, federal awarding agencies, and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

To the Board of Trustees
Lenox Municipal Utilities

Internal Control Over Financial Reporting – (Continued)

The following comments about the Lenox Municipal Utilities' operations for the year ended December 31, 2004, are based exclusively on knowledge obtained from procedures performed during my audit of the financial statements of the Utility. 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.

1. Official depositories - Deposits were maintained in accounts which had been adopted by resolution as official depositories and were within the deposit limits in the Utilities policies.
2. Certified Budget – Budgeted revenues for the year ended December 31, 2004 did not exceed actual disbursements as required under Chapter 384.20 of the Code of Iowa.
3. Questionable disbursements - I noted no disbursements that did not meet the requirements of public purpose as defined in an Attorney General's opinion dated April 25, 1979.
4. Travel expenses - No disbursements of the Utilities money for travel expenses of spouses of utility officials or employees were noted.
5. Business transactions - All business transactions noted between the Utility and Utility officials appeared to be in the normal course of business and appeared to be at arm's length.
6. Bond coverages - Surety bond coverage of the Utilities officials and employees is in accordance with statutory provisions. The amount of the coverage is reviewed annually to insure that the coverage is adequate for the current operations.
7. Board minutes – Certain instances were noted where there was no mention of the posting of the board meeting notice within the required time prior to the occurrence of the meeting. The matter was discussed with Utility personnel and corrected.
8. Deposits and investments - I noted no instance of noncompliance with the deposit and investment provisions of the Code of Iowa and the Utilities' investment policies and deposit limits.

I would like to acknowledge the courtesies extended to me and the assistance provided me by Lenox Municipal Utility employees.

Should you have any questions or concerns regarding the above matters, please contact me.



Certified Public Accountant

Omaha, Nebraska
January 18, 2005

DEAN M. BROICH, P.C.
CERTIFIED PUBLIC ACCOUNTANT

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**REPORT ON COMPLIANCE WITH REQUIREMENTS APPLICABLE
TO EACH MAJOR PROGRAM AND INTERNAL CONTROL OVER
COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133**

To the Board of Trustees
Lenox Municipal Utilities
Lenox, Iowa

I have audited the compliance of Lenox Municipal Utilities, Lenox, 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 each of its major federal programs, if any, for the year ended December 31, 2004. Lenox Municipal Utilities' major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to each of its major federal programs is the responsibility of Lenox Municipal Utilities' management. My responsibility is to express an opinion on Lenox Municipal Utilities compliance based on my audit.

I conducted my audit in accordance with auditing standards generally accepted in 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 of America; OMB Circular A-133, *Audits of States, Local Government, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that I plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about Lenox Municipal Utilities' 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 Lenox Municipal Utilities' compliance with those requirements.

In my opinion, Lenox Municipal Utilities, Lenox, Iowa, complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended December 31, 2004.

Internal Control Over Compliance

The management of Lenox Municipal Utilities, Lenox, Iowa, is responsible for establishing and maintaining effective internal control over compliance with requirements of law, regulations, contracts and grants, applicable to federal programs. In planning and performing my audit, I considered Lenox Municipal Utilities' 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 the internal control over compliance in accordance with OMB Circular A-133.

Internal Control Over Compliance – continued

My consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be a material weakness. 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. With the exceptions of the lack of segregation of duties and the use of facsimile stamps, I noted no matters involving the internal control over compliance and its operation that I consider to be material weaknesses.

This report is intended solely for the information and use of the audit committee, management, employees and trustees within the organization, the Lenox City Council, federal awarding agencies, pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.



Certified Public Accountant

Omaha, Nebraska
January 18, 2005