

CITY OF KALONA, IOWA  
INDEPENDENT AUDITOR'S REPORTS  
MANAGEMENT'S DISCUSSION AND ANALYSIS  
BASIC FINANCIAL STATEMENTS AND SUPPLEMENTARY INFORMATION  
SCHEDULE OF FINDINGS

JUNE 30, 2006

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CITY OF KALONA, IOWA  
CITY OFFICIALS  
June 30, 2006

<u>Name</u>	<u>Title</u>	<u>Term Expires</u>
Jerry Kauffman	Mayor	December, 2007
Ken Herington	Mayor Pro tem	December, 2009
Steve Lafaurie	Council Member	December, 2007
David Bentley	Council Member	December, 2009
Claudine Miller	Council Member	December, 2007
Aaron Kos	Council Member	December, 2009
Doug Morgan	City Administrator	Indefinite
Karen Christner	City Clerk	Appointed

# Gronewold, Bell, Kyhnn & Co. P.C.

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## INDEPENDENT AUDITOR'S REPORT

To the Honorable Mayor and  
Members of the City Council  
City of Kalona, Iowa  
Kalona, Iowa

We have audited the accompanying financial statements of the governmental activities, the business type activities, each major fund and the aggregate remaining fund information of the City of Kalona, Iowa, as of and for the year ended June 30, 2006. These financial statements are the responsibility of city 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 and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States. Those standards and provisions require that 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 officials, as well as evaluating the overall financial statement presentation. We believe our audit provides a reasonable basis for our opinions.

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

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

In our opinion, except for the effect on the financial statements due to the exclusion of the Kalona Library Foundation, Inc., from the reporting entity, the financial statements referred to above present fairly, in all material respects, the respective cash basis financial position of the governmental activities, the business type activities, each major fund and the aggregate remaining fund information of the City of Kalona as of June 30, 2006, and the respective changes in cash basis financial position for the year then ended in conformity with the basis of accounting described in Note 1.

To the Honorable Mayor and  
Members of the City Council  
City of Kalona, Iowa

In accordance with Government Auditing Standards, we have also issued our report dated October 24, 2006 on our consideration of the City of Kalona's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. That report is an integral part of an audit performed in accordance with Government Auditing Standards and should be considered in assessing the results of our audit.

Management's Discussion and Analysis and budgetary comparison information on pages 4 through 4e and 16 through 17 are not required parts of the basic financial statements, but are supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required 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 collectively comprise City of Kalona's basic financial statements. The financial statements for the two years ended June 30, 2005 (none of which are presented herein), were audited by other auditors whose reports expressed qualified opinions on those financial statements. The supplementary information included in Schedules 1 through 4 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, is fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

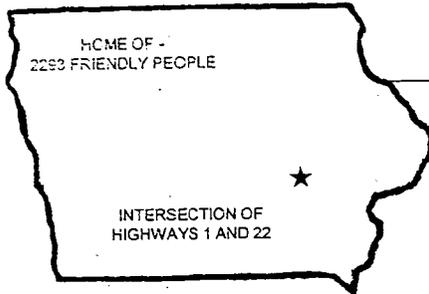
*Gronwald, Bell, Kyhn & Co. P.C.*

Atlantic, Iowa  
October 24, 2006

# CITY OF KALONA

511 C Avenue • P.O. Box 1213  
 KALONA, IOWA 52247-1213  
 City of Kalona AREA CODE 319-656-2310

## Management's Discussion & Analysis



The City of Kalona provides this Management's Discussion and Analysis of its financial statements. This narrative overview and analysis of the financial activities is for the fiscal year ended June 30, 2006. We encourage readers to consider this information in conjunction with the City's financial statements, which follow.

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

### 2006 FINANCIAL HIGHLIGHTS

- Revenues of the City decreased approximately 10% from fiscal year 2005 to 2006 because of reduction to Tax Increment Finance Tax certification and no financing of any projects.
- Disbursements of the City decreased approximately 49% from fiscal year 2005 to 2006 due to completion of Water and Sewer Project and 90% completion of Library Project.
- The City's total cash basis net assets increased approximately 12% or \$325,056 due mainly to decreased expenditures and final payment of Street Project being after July 1, 2006. Of this amount, the assets of the governmental activities increased approximately \$232,000 and the assets of the business type activities increased by approximately \$93,000.

### USING THIS ANNUAL REPORT

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

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

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

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

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

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

## **BASIS OF ACCOUNTING**

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

## **REPORTING THE CITY'S FINANCIAL ACTIVITIES**

### *Government-wide Financial Statement*

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

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

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

### *Fund Financial Statements*

The City has two kinds of funds:

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

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

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

## GOVERNMENT-WIDE FINANCIAL ANALYSIS

Net assets may serve over time as a useful indicator of financial position. The City's cash balance for governmental activities increased from \$2,126,328 to \$2,347,825. The analysis focuses on the changes in cash balances for governmental activities.

### Changes in Cash Basis Net Assets of Governmental Activities

	Year ended June 30,	
	2006	2005
Receipts and transfers:		
Program receipts:		
Charges for services	\$ 63,695	\$ 72,118
Operating Grants	214,910	200,746
General receipts:		
Property tax	589,695	565,156
Debt Service	53,068	763
Local Option Sales Tax	146,363	175,359
TIF revenues	204,193	256,747
Unrestricted interest	32,292	23,170
Miscellaneous	43,399	69,062
Transfer – In	--	39,861
Total receipts and transfers	1,347,615	1,402,982
Disbursements and transfers:		
Public safety	133,259	130,999
Public works	144,316	397,995
Culture and recreation	331,379	291,540
Community and economic development	216,009	254,635
General government	169,350	111,373
Debt service	54,750	--
Capital projects	66,566	1,246,982
Total disbursements and transfers	1,115,629	2,433,524
Increase (decrease) in cash basis net assets	231,986	( 1,030,542)
Cash basis net assets beginning of year (net of prior period adjustment)	2,115,839	3,156,870
Cash basis net assets end of year	\$ 2,347,825	\$ 2,126,328

## Changes in Cash Basis Net Assets of Business Type Activities

	<u>Year Ended June 30,</u>	
	<u>2006</u>	<u>2005</u>
Receipts:		
Program receipts:		
Charges for services		
Water	\$ 337,519	\$ 339,631
Sewer	201,849	190,105
Garbage	44,645	44,214
General receipts:		
Other general receipts	8,213	3,940
Bond proceeds	<u>2,888</u>	<u>166,838</u>
Total receipts	<u>595,114</u>	<u>744,728</u>
Disbursements and transfers:		
Water	161,588	181,905
Sewer	119,015	120,396
Garbage	39,232	40,780
Debt Service	176,959	224,195
Capital Projects	5,250	158,081
Transfers	<u>--</u>	<u>39,861</u>
Total disbursements and transfers	<u>502,044</u>	<u>765,218</u>
Increase (decrease) in cash basis net assets	93,070	( 20,490)
Cash basis net assets beginning of year	<u>654,172</u>	<u>674,662</u>
Cash basis net assets end of year	<u>\$ 747,242</u>	<u>\$ 654,172</u>

### INDIVIDUAL MAJOR GOVERNMENTAL FUND ANALYSIS

As Kalona, Iowa, completed the year, its funds reported a combined fund balance of \$3,095,067, which is an increase of \$325,056. Major reasons for changes in balances from fiscal year 2005 are:

- The General Fund revenues showed a slight increase due to increased tax levy and better interest rates. The fund decreased overall because of increases in expenditures related to several capital improvements and repairs, most notably an electrical project and new storm sewers.
- The Road Use Tax Fund revenue increased slightly and is based on per capita dollars from the state and disbursements decreased dramatically with no major projects completed in fiscal year 2006.
- The Tax Increment Financing Fund revenues decreased by \$52,554 in fiscal year 2006 because of a reduction in total certification.
- The Local Option Sales Tax Fund revenues decreased by \$28,996 from fiscal year 2005. This is based on sales and varies from year to year. Because of the reduction in revenue, less was spent from this fund during the fiscal year 2006 creating an increase in the fund balance.

## INDIVIDUAL MAJOR BUSINESS TYPE FUND ANALYSIS

The Water Utility Fund balance increased by \$72,912 from fiscal year 2005 due to decreased expenditures because of water project completion and reduction of debt.

The Sewer Utility Fund balance increased by \$14,745 from fiscal year 2005 due mainly to prior use of reserve funds in completing sewer project.

## BUDGETARY HIGHLIGHTS

The City amended its budget on May 15, 2006, resulting in an increase of receipts of approximately \$49,302 and disbursements of approximately \$503,121. Receipts increased due to changes in interest rates on reserve funds and charges for services and disbursements were increased for a projected Street Construction Project and purchase of operating equipment.

## DEBT ADMINISTRATION

At June 30, 2006, the City had approximately \$3,163,000 in bonds and other long-term debt, compared to approximately \$3,327,000 last year, as shown below.

### Outstanding Debt at Year-End

	<u>Year Ended June 30,</u>	
	<u>2006</u>	<u>2005</u>
General Obligation Corporate Purpose Bonds		
1997 Water Project	\$ 150,000	\$ 175,000
1995 Sewer Project (State Revolving Fund)	272,000	296,000
2003 Water Project (State Revolving Fund)	986,000	1,027,000
2003 Sewer Project (State Revolving Fund)	465,000	484,000
2004 Library Project	<u>1,290,000</u>	<u>1,345,000</u>
Total	<u>\$ 3,163,000</u>	<u>\$ 3,327,000</u>

Debt decreased as principal was paid down.

## ECONOMIC FACTORS AND NEXT YEAR'S BUDGET

The City of Kalona's elected and appointed officials considered factors such as tax rates and fees that will be charged for various City activities when they adopted the 2007 budget. The 6<sup>th</sup> Street Project has been included in the 2007 budget.

## **CONTACTING THE CITY'S FINANCIAL MANAGEMENT**

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

CITY OF KALONA, IOWA  
STATEMENT OF ACTIVITIES AND NET ASSETS - CASH BASIS  
As of and for the year ended June 30, 2006

	<u>Disbursements</u>	<u>Program Receipts</u>	
		<u>Charges for Service</u>	<u>Operating Grants, Contributions, and Restricted Interest</u>
<b>Functions/Programs:</b>			
<b>Governmental activities:</b>			
Public safety	\$ 133,259	\$ 197	\$ --
Public works	144,316	--	191,982
Culture and recreation	331,379	58,633	22,928
Community and economic development	216,009	3,030	--
General government	169,350	1,835	--
Debt service	54,750	--	--
Capital projects	66,566	--	--
Total government activities	<u>1,115,629</u>	<u>63,695</u>	<u>214,910</u>
<b>Business type activities:</b>			
Water	272,899	337,519	--
Sewer	189,913	201,849	--
Garbage	39,232	44,645	--
Total business type activities	<u>502,044</u>	<u>584,013</u>	<u>--</u>
<b>Total</b>	<u>\$ 1,617,673</u>	<u>\$ 647,708</u>	<u>\$ 214,910</u>
<b>General Receipts:</b>			
Property tax levied for:			
General purposes			
Tax increment financing			
Debt service			
Local option sales tax			
Unrestricted interest on investments			
Bond proceeds			
Miscellaneous			
Total general receipts and transfers			
Change in cash basis net assets, net prior period adjustments			
Cash basis net assets beginning of year, net prior period adjustments			
Cash basis net assets, end of year			

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<u>Program Receipts</u> Capital Grants, Contributions, and Restricted Interest	<u>Net (Disbursements) Receipts and Changes in Cash Basis Net Assets</u>		
	<u>Governmental Activities</u>	<u>Business Type Activities</u>	<u>Total</u>
\$ --	\$( 133,062)	\$ --	\$( 133,062)
--	47,666	--	47,666
--	( 249,818)	--	( 249,818)
--	( 212,979)	--	( 212,979)
--	( 167,515)	--	( 167,515)
--	( 54,750)	--	( 54,750)
--	( 66,566)	--	( 66,566)
--	( 837,024)	--	( 837,024)
--	--	64,620	64,620
--	--	11,936	11,936
--	--	5,413	5,413
--	--	81,969	81,969
<u>\$ --</u>	( 837,024)	81,969	( 755,055)
	589,695	--	589,695
	204,193	--	204,193
	53,068	--	53,068
	146,363	--	146,363
	32,292	8,213	40,505
	--	2,888	2,888
	43,399	--	43,399
	<u>1,069,010</u>	<u>11,101</u>	<u>1,080,111</u>
	231,986	93,070	325,056
	<u>2,115,839</u>	<u>654,172</u>	<u>2,770,011</u>
	<u>\$ 2,347,825</u>	<u>\$ 747,242</u>	<u>\$ 3,095,067</u>

CITY OF KALONA, IOWA  
STATEMENT OF ACTIVITIES AND NET ASSETS - CASH BASIS - Continued

As of and for the year ended June 30, 2006

	<u>Disbursements</u>	<u>Charges for Service</u>	<u>Program Receipts Operating Grants, Contributions, and Restricted Interest</u>
Cash Basis Net Assets			
Restricted:			
Streets			
Urban renewal projects			
Debt service			
Other purpose			
Unrestricted			
Total cash basis net assets			

The accompanying notes are an integral part of these statements.

<u>Program Receipts</u> Capital Grants, Contributions, and Restricted Interest	<u>Net (Disbursements) Receipts and Changes in Cash Basis Net Assets</u>		
	<u>Governmental Activities</u>	<u>Business Type Activities</u>	<u>Total</u>
	\$ 404,851	\$ --	\$ 404,851
	200,672	--	200,672
	138,047	434,236	572,283
	79,688	--	79,688
	<u>1,524,567</u>	<u>313,006</u>	<u>1,837,573</u>
	<u>\$ 2,347,825</u>	<u>\$ 747,242</u>	<u>\$ 3,095,067</u>

CITY OF KALONA, IOWA  
STATEMENT OF CASH RECEIPTS, DISBURSEMENTS  
AND CHANGES IN CASH BALANCES  
GOVERNMENTAL FUNDS

As of and for the year ended June 30, 2006

	General	Special Revenue
		Road Use Tax
<b>Receipts:</b>		
Property tax	\$ 522,135	\$ --
Tax increment financing collections	--	--
Other city tax	14,323	--
Use of money and property	30,767	--
Licenses and permits	4,190	--
Intergovernmental	17,563	191,982
Charges for service	73,917	--
Miscellaneous	16,970	--
Total receipts	679,865	191,982
<b>Disbursements:</b>		
Operating:		
Public safety	133,259	--
Public works	91,787	43,748
Culture and recreation	304,047	--
Community and economic development	--	--
General government	160,790	--
Debt service	--	--
Capital projects	--	--
Total disbursements	689,883	43,748
Excess (deficiency) of receipts over (under) disbursements	( 10,018)	148,234

(continued next page)

<u>Special Revenue</u>		<u>Other Nonmajor Governmental Funds</u>	<u>Total</u>
<u>Urban Renewal Tax Increment</u>	<u>Local Option Sales Tax</u>		
\$ --	\$ --	\$ 120,628	\$ 642,763
204,193	--	--	204,193
--	146,363	3,059	163,745
--	--	1,525	32,292
--	--	--	4,190
--	--	--	209,545
--	--	--	73,917
--	--	--	16,970
<u>204,193</u>	<u>146,363</u>	<u>125,212</u>	<u>1,347,615</u>
--	--	--	133,259
--	--	8,781	144,316
--	--	27,332	331,379
164,741	51,268	--	216,009
--	--	8,560	169,350
--	--	54,750	54,750
--	--	66,566	66,566
<u>164,741</u>	<u>51,268</u>	<u>165,989</u>	<u>1,115,629</u>
39,452	95,095	( 40,777)	231,986

CITY OF KALONA, IOWA  
STATEMENT OF CASH RECEIPTS, DISBURSEMENTS  
AND CHANGES IN CASH BALANCES - Continued  
GOVERNMENTAL FUNDS

As of and for the year ended June 30, 2006

	<u>General</u>	<u>Special Revenue</u>
		<u>Road Use Tax</u>
Balance beginning of year	\$ 1,221,315	\$ 256,617
Prior period adjustment	( 10,489)	--
Adjusted balance beginning of year	<u>1,210,826</u>	<u>256,617</u>
Balance end of year	<u>\$ 1,200,808</u>	<u>\$ 404,851</u>
 Cash Basis Net Assets		
Reserved:		
Debt service	\$ --	\$ --
Unreserved:		
General fund	1,200,808	--
Special revenue funds	--	404,851
Capital projects fund	<u>--</u>	<u>--</u>
Total cash basis net assets	<u>\$ 1,200,808</u>	<u>\$ 404,851</u>

The accompanying notes are an integral part of these statements.

<u>Special Revenue</u>		<u>Other Nonmajor Governmental Funds</u>	<u>Total</u>
<u>Urban Renewal Tax Increment</u>	<u>Local Option Sales Tax</u>		
\$ 161,220	\$ 228,664	\$ 258,512	\$ 2,126,328
--	--	--	( 10,489)
<u>161,220</u>	<u>228,664</u>	<u>258,512</u>	<u>2,115,839</u>
<u>\$ 200,672</u>	<u>\$ 323,759</u>	<u>\$ 217,735</u>	<u>\$ 2,347,825</u>
\$ --	\$ --	\$ 138,047	\$ 138,047
--	--	--	1,200,808
200,672	323,759	64,841	994,123
--	--	14,847	14,847
<u>\$ 200,672</u>	<u>\$ 323,759</u>	<u>\$ 217,735</u>	<u>\$ 2,347,825</u>

CITY OF KALONA, IOWA  
STATEMENT OF CASH RECEIPTS, DISBURSEMENTS  
AND CHANGES IN CASH BALANCES  
PROPRIETARY FUNDS

As of and for the year ended June 30, 2006

	Enterprise Funds			Total
	Water	Sewer	Garbage	
Operating Receipts:				
License and permits	\$ 6,780	\$ 4,250	\$ --	\$ 11,030
Charges for services	<u>322,807</u>	<u>192,214</u>	<u>44,645</u>	<u>559,666</u>
Total operating receipts	329,587	196,464	44,645	570,696
Operating Disbursements:				
Business type activities	<u>166,838</u>	<u>119,015</u>	<u>39,232</u>	<u>325,085</u>
Total operating disbursements	<u>166,838</u>	<u>119,015</u>	<u>39,232</u>	<u>325,085</u>
Excess of receipts over disbursements	162,749	77,449	5,413	245,611
Non-operating receipts (disbursements):				
Interest on investments	5,404	2,809	--	8,213
Miscellaneous	7,932	5,385	--	13,317
State revolving fund loan proceeds	2,888	--	--	2,888
Debt service	<u>( 106,061)</u>	<u>( 70,898)</u>	<u>--</u>	<u>( 176,959)</u>
Total non-operating receipts (disbursements)	<u>( 89,837)</u>	<u>( 62,704)</u>	<u>--</u>	<u>( 152,541)</u>
Excess of receipts over disbursements	72,912	14,745	5,413	93,070
Cash balances beginning of year	<u>188,473</u>	<u>437,785</u>	<u>27,914</u>	<u>654,172</u>
Cash balances end of year	<u>\$ 261,385</u>	<u>\$ 452,530</u>	<u>\$ 33,327</u>	<u>\$ 747,242</u>
Cash Basis Fund Balances				
Reserved for debt service	\$ 59,239	\$ 374,997	\$ --	\$ 434,236
Unreserved	<u>202,146</u>	<u>77,533</u>	<u>33,327</u>	<u>313,006</u>
Total cash basis fund balances	<u>\$ 261,385</u>	<u>\$ 452,530</u>	<u>\$ 33,327</u>	<u>\$ 747,242</u>

The accompanying notes are an integral part of these statements.

CITY OF KALONA, IOWA  
NOTES TO FINANCIAL STATEMENTS  
June 30, 2006

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

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

A. Reporting Entity

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

Excluded Component Unit

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

Related Organization

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

Jointly Governed Organizations

The City also participates in several jointly governed organizations that provide goods or services to the citizenry of the City but do not meet the criteria of a joint venture since there is no ongoing financial interest or responsibility by the participating governments. City officials are members of the following boards and commissions: Washington County Joint E911 Service Board and Washington County Assessor's Board.

B. Basis of Presentation

Government-wide Financial Statements

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

CITY OF KALONA, IOWA  
NOTES TO FINANCIAL STATEMENTS  
June 30, 2006

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

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

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

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

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

Fund Financial Statements

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

The City reports the following major governmental funds:

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

Special Revenue:

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

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

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

CITY OF KALONA, IOWA  
NOTES TO FINANCIAL STATEMENTS  
June 30, 2006

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

The City reports the following major proprietary funds:

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

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

The City also reports the following additional proprietary fund:

The Garbage Fund accounts for the operation and maintenance of the City's garbage service.

C. Measurement Focus and Basis of Accounting

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

Under the terms of grant agreements, the City funds certain activities by a combination of specific cost-reimbursement grants. It is the City's policy to first apply cost-reimbursement grant resources and then general receipts.

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

D. Budgets and Budgetary Accounting

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

NOTE 2 - CASH AND POOLED INVESTMENTS

The City's deposits in banks at June 30, 2006 were entirely covered by federal depository insurance or by the State Sinking Fund in accordance with Chapter 12C of the Code of Iowa. This chapter provides for additional assessments against the depositories to insure there will be no loss of public funds.

CITY OF KALONA, IOWA  
NOTES TO FINANCIAL STATEMENTS  
June 30, 2006

NOTE 2 - CASH AND POOLED INVESTMENTS - Continued

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

Interest rate risk - The City's investment policy limits the investment of operating funds (funds expected to be expended in the current budget year or within 15 months of receipt) in instruments that mature within 397 days. Funds not identified as operating funds may be invested in investments with maturities longer than 397 days but the maturities shall be consistent with the needs and use of the City.

Credit risk - The City had no investments with credit risk.

NOTE 3 - BONDS AND NOTES PAYABLE

Annual debt service requirements to maturity for general obligation and revenue capital loan notes are as follows:

Year Ending June 30,	General Obligation Capital Loan Notes		Revenue Capital Loan Notes		Total	
	Principal	Interest	Principal	Interest	Principal	Interest
2007	\$ 80,000	\$ 54,111	\$ 87,000	\$ 51,690	\$ 167,000	\$ 105,801
2008	80,000	51,953	89,000	49,080	169,000	101,033
2009	80,000	49,605	94,000	46,410	174,000	96,015
2010	85,000	47,068	97,000	43,590	182,000	90,658
2011	85,000	44,213	99,000	40,680	184,000	84,893
2012	85,000	41,213	103,000	37,710	188,000	78,923
2013	65,000	38,050	107,000	34,620	172,000	72,670
2014	65,000	35,937	110,000	31,410	175,000	67,347
2015	65,000	33,695	114,000	28,110	179,000	61,805
2016	70,000	31,355	81,000	24,690	151,000	56,045
2017	70,000	28,730	84,000	22,260	154,000	50,990
2018	75,000	26,035	86,000	19,740	161,000	45,775
2019	80,000	23,072	88,000	17,160	168,000	40,232
2020	85,000	19,833	91,000	14,520	176,000	34,353
2021	85,000	16,305	94,000	11,790	179,000	28,095
2022	90,000	12,693	97,000	8,970	187,000	21,663
2023	95,000	8,777	99,000	6,060	194,000	14,837
2024	100,000	4,550	103,000	3,090	203,000	7,640
	<u>\$1,440,000</u>	<u>\$ 567,195</u>	<u>\$1,723,000</u>	<u>\$ 491,580</u>	<u>\$3,163,000</u>	<u>\$1,058,775</u>

The Code of Iowa requires that principal and interest on general obligation capital loan notes be paid from the Debt Service Fund. However, during the year, \$66,000 of note principal and \$40,061 of interest was paid from the Enterprise Water Fund and \$250 was paid out of the Special Revenue, Local Option Sales Tax Fund.

CITY OF KALONA, IOWA  
NOTES TO FINANCIAL STATEMENTS  
June 30, 2006

NOTE 3 - BONDS AND NOTES PAYABLE - Continued

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

- a. The notes will only be redeemed from the future earnings of the enterprise activity and the note holders hold a lien on the future earnings of the funds.
- b. Sufficient transfers shall be made into a separate and special fund to pay current expenses. The fund shall be known as the Sewer/Water Utility Operation and Maintenance Fund. There shall be deposited in the fund each month an amount sufficient to meet the current expenses of the month plus an amount equal to 1/12 of expenses payable on an annual basis such as insurance.
- c. Moneys shall next be disbursed to a separate and special fund to pay principal of and interest on the Notes and Parity Obligations known as the Sewer/Water Revenue Note Principal and Interest Sinking Fund (the "Sinking Fund"). The required amount to be deposited in the Sinking Fund in any month shall be an amount equal to 1/6 of the installment of interest coming due on the next payment and 1/12 of the installment of principal coming due on the next payment date.

NOTE 4 - PENSION AND RETIREMENT BENEFITS

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

Plan members are required to contribute 3.70% of their annual covered salary and the City is required to contribute 5.75% of annual covered percentages respectively. Contribution requirements are established by state statute. The City's contributions to IPERS for the years ended June 30, 2006, 2005, and 2004 were \$16,844, \$14,185, and \$14,773, respectively, equal to the required contribution for each year.

NOTE 5 - COMPENSATED ABSENCES

City employees accumulate a limited amount of earned but unused vacation and comp time hours for subsequent use or for payment upon termination, retirement or death. These accumulations are not recognized as disbursements by the City until used or paid. The City's liability for earned vacation and comp time leave termination payments payable to employees at June 30, 2006 is \$9,491 for vacation and \$7,417 for comp time, for a total liability of \$16,908. This liability has been computed on rates of pay in effect at June 30, 2006.

CITY OF KALONA, IOWA  
NOTES TO FINANCIAL STATEMENTS  
June 30, 2006

NOTE 6 - WORKERS COMPENSATION

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

NOTE 7 - RISK MANAGEMENT

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

NOTE 8 - SERVICE AGREEMENTS

The City has an agreement with Washington County to provide police protection for its citizens. The City paid \$105,923 for services during the year ended June 30, 2006.

NOTE 9 - CONSTRUCTION CONTRACT

The City entered into a construction contract for their 6<sup>th</sup> Street Project totaling approximately \$282,700. None of this contract was paid in fiscal year 2006 and will be completely funded from local sources during fiscal year 2007.

NOTE 10 - REVENUE BOND

On July 11, 2005, Facility Revenue Bond, Iowa Mennonite School Project, in the amount of \$1,300,000 was issued. This revenue bond is issued for the purpose of financing the cost of constructing, equipping and furnishing a fine arts facility on the Iowa Mennonite School Campus. These bonds will be a special limited obligation of the City and shall not be payable from or charged upon any funds other than Loan Repayments made by the Iowa Mennonite School, a Tax Exempt Organization. The bonds will not constitute a debt of the City within any constitutional or statutory limitation.

NOTE 11 - PRIOR PERIOD ADJUSTMENT

An adjustment has been made to correct an error that occurred in prior years due to the posting of payroll taxes to a liability account within the new computer system instead of an expense account. This was noted as a variance in the prior year audit report. The adjustment for approximately \$10,490 has been made to the General Fund.

\* \* \*

REQUIRED SUPPLEMENTARY INFORMATION

CITY OF KALONA, IOWA  
 BUDGETARY COMPARISON SCHEDULE  
 OF RECEIPTS, DISBURSEMENTS, AND CHANGES IN BALANCES -  
 BUDGET AND ACTUAL (CASH BASIS) - GOVERNMENTAL  
 FUNDS AND PROPRIETRY FUNDS  
 REQUIRED SUPPLEMENTARY INFORMATION

Year ended June 30, 2006

	<u>Governmental Funds Actual</u>	<u>Proprietary Funds Actual</u>	<u>Total</u>
Receipts:			
Property tax	\$ 642,763	\$ --	\$ 642,763
Tax increment financing collections	204,193	--	204,193
Other city tax	163,745	--	163,745
Use of money and property	32,292	8,213	40,505
Licenses and permits	4,190	11,030	15,220
Intergovernmental	209,545	--	209,545
Charges for service	73,917	572,983	646,900
Miscellaneous	16,970	--	16,970
Total receipts	<u>1,347,615</u>	<u>592,226</u>	<u>1,939,841</u>
Disbursements:			
Public safety	133,259	--	133,259
Public works	144,316	--	144,316
Culture and recreation	331,379	--	331,379
Community and economic development	216,009	--	216,009
General government	169,350	--	169,350
Debt service	54,750	--	54,750
Capital projects	66,566	--	66,566
Business type activities	--	502,044	502,044
Total disbursements	<u>1,115,629</u>	<u>502,044</u>	<u>1,617,673</u>
Excess (deficiency) of receipts over (under) disbursements	231,986	90,182	322,168
Other financing sources (uses):			
Bond proceeds			
State revolving fund loan	--	2,888	2,888
Total other financing sources (uses)	<u>--</u>	<u>2,888</u>	<u>2,888</u>
Excess (deficiency) of receipts and other financing sources over (under) disbursements and other financing uses	231,986	93,070	325,056
Balance beginning of year	2,126,328	654,172	2,780,500
Prior period adjustment	<u>( 10,489)</u>	<u>--</u>	<u>( 10,489)</u>
Adjusted balance beginning of year	<u>2,115,839</u>	<u>654,172</u>	<u>2,770,011</u>
Balance end of year	<u>\$ 2,347,825</u>	<u>\$ 747,242</u>	<u>\$ 3,095,067</u>

See accompanying independent auditor's report.

<u>Budgeted Amounts</u>		<u>Final to</u>
<u>Original</u>	<u>Final</u>	<u>Total</u>
		<u>Variance</u>
\$ 637,339	\$ 637,339	\$ 5,424
204,739	204,739	( 546)
169,164	169,164	( 5,419)
6,420	26,883	13,622
3,000	9,760	5,460
196,051	213,615	( 4,070)
589,288	617,376	29,524
32,190	8,617	8,353
<u>1,838,191</u>	<u>1,887,493</u>	<u>52,348</u>
138,011	138,011	4,752
305,367	595,786	451,470
372,002	412,866	81,487
355,383	360,883	144,874
107,238	174,452	5,102
54,750	54,750	--
--	66,566	--
<u>489,482</u>	<u>522,040</u>	<u>19,996</u>
<u>1,822,233</u>	<u>2,325,354</u>	<u>707,681</u>
15,958	( 437,861)	760,029
<u>--</u>	<u>--</u>	<u>2,888</u>
<u>--</u>	<u>--</u>	<u>2,888</u>
15,958	( 437,861)	762,917
4,067,096	2,780,386	114
<u>--</u>	<u>--</u>	<u>( 10,489)</u>
<u>4,067,096</u>	<u>2,780,386</u>	<u>( 10,375)</u>
<u>\$ 4,083,054</u>	<u>\$ 2,342,525</u>	<u>\$ 752,542</u>

CITY OF KALONA, IOWA  
NOTES TO REQUIRED SUPPLEMENTARY INFORMATION -  
BUDGETARY REPORTING

June 30, 2006

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

Formal and legal budgetary control is based upon ten major classes of disbursements known as functions, not by fund or fund type. These ten functions are: public safety, public works, health and social services, culture and recreation, community and economic development, general government, debt service, capital projects, business type activities and non-program. Function disbursements required to be budgeted included disbursements for the General Fund, Special Revenue Funds, Debt Service Fund, Capital Projects Funds and Business Type Funds. Although the budget document presents function disbursements by fund, the legal level of control is at the aggregated function level, not by fund. During the year, the budget amendment increased budgeted disbursements by \$503,121. The budget amendment is reflected in the final budgeted amount.

OTHER SUPPLEMENTARY INFORMATION

CITY OF KALONA, IOWA  
SCHEDULE OF CASH RECEIPTS, DISBURSEMENTS  
AND CHANGES IN CASH BALANCES  
NONMAJOR GOVERNMENTAL FUNDS

As of and for the year ended June 30, 2006

	Special Revenue Employee Benefits	Debt Service
Receipts:		
Property tax	\$ 67,560	\$ 53,068
Other City tax	1,796	1,263
Use of money and property	--	1,525
Total receipts	69,356	55,856
Disbursements:		
Operating:		
Public works	8,781	--
Culture and recreation	27,332	--
General government	8,560	--
Debt service	--	54,750
Capital projects	--	--
Total disbursements	44,673	54,750
Excess (deficiency) of receipts over (under) disbursements	24,683	1,106
Balance beginning of year	40,158	136,941
Balance end of year	\$ 64,841	\$ 138,047
Cash Basis Fund Balances		
Reserved:		
Debt service	\$ --	\$ 138,047
Unreserved:		
Employee benefits	64,841	--
Capital project fund	--	--
Total cash basis fund balances	\$ 64,841	\$ 138,047

See accompanying independent auditor's report.

Schedule 1

<u>Capital Project Library Project</u>	<u>Total</u>
\$ --	\$ 120,628
--	3,059
<u>--</u>	<u>1,525</u>
<u>--</u>	<u>125,212</u>
--	8,781
--	27,332
--	8,560
--	54,750
<u>66,566</u>	<u>66,566</u>
<u>66,566</u>	<u>165,989</u>
( 66,566)	( 40,777)
<u>81,413</u>	<u>258,512</u>
<u>\$ 14,847</u>	<u>\$ 217,735</u>
\$ --	\$ 138,047
--	64,841
<u>14,847</u>	<u>14,847</u>
<u>\$ 14,847</u>	<u>\$ 217,735</u>

CITY OF KALONA, IOWA  
 SCHEDULE OF INDEBTEDNESS  
 Year ended June 30, 2006

<u>Obligation</u>	<u>Date of Issue</u>	<u>Interest Rate</u>	<u>Amount Originally Issued</u>
General Obligation Capital Loan Notes:			
Water	April 1, 1997	4.10% - 5.45%	\$ 350,000
Library	June 1, 2004	1.30% - 4.55%	1,400,000
Total General Obligation Notes			
Capital Loan Notes Payable:			
State revolving funds loans			
Sewer	February 13, 1995	3.00%	489,000
Water	August 26, 2003	3.00%	1,067,000
Sewer	December 12, 2003	3.00%	503,000
Total SRF loans			
Total			

See accompanying independent auditor's report.

<u>Balance Beginning of Year</u>	<u>Redeemed During Year</u>	<u>Balance End of Year</u>	<u>Interest Paid</u>	<u>Interest Due and Unpaid</u>
\$ 175,000	\$ 25,000	\$ 150,000	\$ 9,088	\$ 938
<u>1,345,000</u>	<u>55,000</u>	<u>1,290,000</u>	<u>47,018</u>	<u>2,661</u>
<u>1,520,000</u>	<u>80,000</u>	<u>1,440,000</u>	<u>56,106</u>	<u>3,599</u>
296,000	24,000	272,000	11,159	1,544
1,027,000	41,000	986,000	30,810	3,698
<u>484,000</u>	<u>19,000</u>	<u>465,000</u>	<u>14,520</u>	<u>1,744</u>
<u>1,807,000</u>	<u>84,000</u>	<u>1,723,000</u>	<u>56,489</u>	<u>6,986</u>
<u>\$3,327,000</u>	<u>\$ 164,000</u>	<u>\$3,163,000</u>	<u>\$ 112,595</u>	<u>\$ 10,585</u>

CITY OF KALONA, IOWA  
 BOND AND NOTE MATURITIES  
 June 30, 2006

<u>Year ending June 30,</u>	General Obligation Capital Loan Notes				
	Water Note		Library Note		<u>Total</u>
	Issued April 1, 1997		Issued June 1, 2004		
	Interest Rate	Amount	Interest Rate	Amount	
2007	5.00%	\$ 25,000	1.65%	\$ 55,000	\$ 80,000
2008	5.10	25,000	1.95	55,000	80,000
2009	5.20	25,000	2.25	55,000	80,000
2010	5.30	25,000	2.55	60,000	85,000
2011 - 2024	5.4-5.45	50,000	2.75-4.55	1,065,000	1,115,000
		<u>\$ 150,000</u>		<u>\$1,290,000</u>	<u>\$1,440,000</u>

State Revolving Funds

<u>Year ending June 30,</u>	Sewer Revenue Capital Loan Notes			
	Issued February 13, 1995		Issued December 12, 2003	
	Interest Rate	Amount	Interest Rate	Amount
	2007	3.00%	\$ 25,000	3.00%
2008	3.00	26,000	3.00	20,000
2009	3.00	28,000	3.00	21,000
2010	3.00	29,000	3.00	22,000
2011 - 2024	3.00	164,000	3.00	382,000
		<u>\$ 272,000</u>		<u>\$ 465,000</u>

See accompanying independent auditor's report.

<u>State Revolving Funds</u>		
<u>Water Revenue</u>		
<u>Capital Loan Notes</u>		
<u>Issued</u>		
<u>August 26, 2003</u>		
<u>Interest</u>		
<u>Rate</u>	<u>Amount</u>	<u>Total</u>
3.00%	\$ 42,000	\$ 87,000
3.00	43,000	89,000
3.00	45,000	94,000
3.00	46,000	97,000
3.00	<u>810,000</u>	<u>1,356,000</u>
	<u>\$ 986,000</u>	<u>\$ 1,723,000</u>

CITY OF KALONA, IOWA  
 SCHEDULE OF RECEIPTS BY SOURCE AND  
 DISBURSEMENTS BY FUNCTION -  
 ALL GOVERNMENTAL FUNDS  
 For the Last Three Years

	<u>2006</u>	<u>2005</u>	<u>2004</u>
Receipts:			
Property tax	\$ 642,763	\$ 565,919	\$ 570,135
Tax increment financing collections	204,193	256,747	164,421
Other city tax	163,745	193,729	159,183
Use of money and property	32,292	31,300	20,085
Licenses and permits	4,190	3,633	2,145
Intergovernmental	209,545	203,853	212,966
Charges for service	73,917	67,064	88,222
Miscellaneous	<u>16,970</u>	<u>40,876</u>	<u>6,295</u>
Total	<u>\$ 1,347,615</u>	<u>\$ 1,363,121</u>	<u>\$ 1,223,452</u>
Disbursements:			
Operating:			
Public safety	\$ 133,259	\$ 130,999	\$ 132,944
Public works	144,316	397,995	146,325
Culture and recreation	331,379	291,540	258,118
Community and economic development	216,009	254,635	185,098
General government	169,350	111,373	96,830
Debt service	54,750	--	52,866
Capital projects	<u>66,566</u>	<u>1,246,982</u>	<u>101,705</u>
Total	<u>\$ 1,115,629</u>	<u>\$ 2,433,524</u>	<u>\$ 973,886</u>

See accompanying independent auditor's report.

## COMMENTS AND RECOMMENDATIONS

# Gronewold, Bell, Kyhnn & Co. P.C.

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Independent Auditor's Report on Internal Control over Financial Reporting  
and on Compliance and Other Matters  
Based on an Audit of Financial Statements Performed in Accordance with  
Government Auditing Standards

To the Honorable Mayor and  
Members of the City Council  
City of Kalona  
Kalona, Iowa

We have audited the financial statements of the City of Kalona, Iowa, as of and for the year ended June 30, 2006, and have issued our report thereon dated October 24, 2006. Our report expressed a qualified 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, and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States.

### Internal Control Over Financial Reporting

In planning and performing our audit, we considered the City of Kalona's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinions on the financial statements and not to provide an opinion 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 the City of Kalona's ability to record, process, summarize and report financial data consistent with the assertions of management in the financial statements. Reportable conditions are described in Part II of the accompanying Schedule of Findings.

To the Honorable Mayor and  
Members of the City Council  
City of Kalona

A material weakness is a reportable 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 caused by error or fraud 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, of the reportable conditions described above, we believe item 06-I-A is a material weakness.

#### Compliance and Other Matters

As part of obtaining reasonable assurance about whether the City of Kalona's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, non-compliance 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 non-compliance that are required to be reported under Government Auditing Standards. However, we noted certain immaterial instances of non-compliance or other matters that are described in Part II of the accompanying Schedule of Findings.

Comments involving statutory and other legal matters about the City's operations for the year ended June 30, 2006 are based exclusively on knowledge obtained from procedures performed during our audit of the financial statements of the City. 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.

This report, a public record by law, is intended solely for the information and use of the officials, employees and citizens of the City of Kalona and other parties to whom the City of Kalona may report. This report is not intended to be and should not be used by anyone other than these specified parties.

*Granwald, Bell, Kuhn & P.C.*

Atlantic, Iowa  
October 24, 2006

CITY OF KALONA, IOWA

Schedule of Findings

Year ended June 30, 2006

PART I - REPORTABLE CONDITIONS

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

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

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

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

Payroll – preparation and distribution.

Utilities – collections, depositing and recording.

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

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

Conclusion: Response acknowledged.

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CITY OF KALONA, IOWA

Schedule of Findings

Year ended June 30, 2006

PART II - REQUIRED STATUTORY REPORTING

06-II-A Certified Budget: Disbursements during the year ended June 30, 2006 did not exceed the amounts budgeted.

06-II-B Bond Coverage: Surety bond coverage of City officials and employees is in accordance with statutory provisions. The amount of coverage should be reviewed annually to insure that the coverage is adequate for current operations.

06-II-C Council Minutes: No transactions were found that we believe should have been approved in the Council minutes but were not, except for minutes of the December, 2005 Council meeting were not published as required by Chapter 372.13(6) of the Code of Iowa.

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

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

Conclusion: Response accepted.

06-II-D Questionable Disbursements: Certain disbursements were noted that may not meet the requirements of public purpose as defined in an Attorney General's opinion dated April 25, 1979 since the public benefits to be derived have not been clearly documented. These disbursements are detailed as follows:

<u>Paid to</u>	<u>Purpose</u>	<u>Amount</u>
Niffs Nature Nook	Flower arrangement	\$ 36
Garden of Eden	Flower arrangement	88

According to the opinion, it is possible for such disbursements to meet the test of serving a public purpose under certain circumstances, although such items will certainly be subject to a deserved close scrutiny.

Recommendation: The Council should determine and document the public purpose served by these disbursements before authorizing any further payments. If this practice is continued, the City should establish written policies and procedures, including the requirements for proper documentation.

Response: We will comply with this recommendation.

Conclusion: Response accepted.

CITY OF KALONA, IOWA

Schedule of Findings

Year ended June 30, 2006

PART II - REQUIRED STATUTORY REPORTING - Continued

06-II-E Travel Expense: No disbursements of City money for travel expenses of spouses of City officials or employees were noted.

06-II-F Deposits and Investments: No instances of non-compliance with the deposit and investment provisions of Chapter 12B and 12C of the Code of Iowa. However, it was noted that the City's investment policy is not current and in compliance with the provisions of Chapter 12B.10B of the Code of Iowa. Also, one CD for \$51,000 is not receiving the minimum interest rate per the Rate Setting Committee.

Recommendation: The City should update their investment policy to comply with the provisions of Chapter 12B.10B of the Code of Iowa. Additionally, the City should contact the bank to increase the interest rate for the \$51,000 CD.

Response: We are working towards adopting a current investment policy and contacting the bank.

Conclusion: Response accepted.

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

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

Response: We will include the same in the future.

Conclusion: Response accepted.

06-II-H General Obligation Loan Notes: The Water General Obligation Capital Loan Notes were paid for directly from the Water Fund. The Library General Obligation Capital Loan Note was paid for directly from the Special Revenue, Local Option Sales Tax Fund. Section 384.4 of the Code of Iowa states "Moneys pledged or available to service general obligation bonds, and received from sources other than property taxes, must be deposited in the debt service fund."

Recommendation: The City should transfer water funds designated for payments on notes to debt service and then make note payments out of debt service.

Response: The City will take it under advisement.

Conclusion: The City should consider the implications of paying the note out of the Enterprise Water Fund.

CITY OF KALONA, IOWA

Schedule of Findings

Year ended June 30, 2006

PART II - REQUIRED STATUTORY REPORTING - Continued

06-II-I Library Minutes: Minutes of the August, September, October, and November, 2005 minutes were not approved by signature.

Recommendation: The Library should approve the minutes and evidence approval by signature.

Response: The City has informed the Library of the appropriate procedure.

Conclusion: Response accepted.

06-II-J City Code of Ordinances: The City has not compiled the City ordinances within the past five years.

Recommendation: Chapter 380.8 of the Code of Iowa states in part, "At least once every five years, a City shall compile a code of ordinances containing all City ordinances in effect, except grade ordinances, bond ordinances, zoning ordinances, and ordinances vacating streets and alleys." The City should compile a code of City ordinances as required.

Response: We are currently in the process of compiling a new code of City ordinances.

Conclusion: Response accepted.

06-II-K Cash Balance Variance: The City's books differ from the bank balances by \$187 and the financial report figures differ from the City's books by \$2,180.

Recommendation: The City should investigate this variance and determine why the balances for the City are different.

Response: We are aware of the situation, and we believe something has been recorded incorrectly. Our computer software provider is investigating the problem and through continuous investigation we believe the variances will be resolved.

Conclusion: Response accepted.

06-II-L Business Transactions: In accordance with Chapter 362.5(10) of the Code of Iowa, no transactions between the City and the City officials and City employees were noted that represented conflicts of interest.

CITY OF KALONA, IOWA

Schedule of Findings

Year ended June 30, 2006

PART II - REQUIRED STATUTORY REPORTING - Continued

06-II-M Credit Accounts: The Library has applied for several credit accounts for occasional use by the Library. The Library has not adopted a formal policy to regulate the use of nor established procedures for the proper accounting of credit charges. Additionally, several claims for credit purchases did not include detailed support.

Recommendation: The Library should adopt a formal written policy regulating credit usage. The policy, at a minimum, should address who is authorized to use the credit accounts and for what purpose, as well as the types of supporting documentation (detailed receipts) required to substantiate charges.

Response: The Library Board will adopt a written policy for credit usage for this fiscal year.

Conclusion: Response accepted.

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