

CITY OF SHELL ROCK, IOWA
INDEPENDENT AUDITOR'S REPORTS
BASIC FINANCIAL STATEMENTS AND
SUPPLEMENTARY INFORMATION
SCHEDULE OF FINDINGS

JUNE 30, 2006

- Prepared By -

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CITY OF SHELL ROCK, IOWA

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CITY OF SHELL ROCK, IOWA

OFFICIALS

<u>NAME</u>	<u>TITLE</u>	<u>TERM EXPIRES</u>
(Before January 2006)		
Larry Young	Mayor	January 2006
Carol Gomez	Mayor Pro tem	January 2008
Carol Ann Kruse	Council Member	January 2006
Terry Quigley	Council Member	January 2006
Glen Kliebenstein	Council Member	January 2008
Richard Smith	Council Member	January 2008
(After January 2006)		
Larry Young	Mayor	January 2008
Carol Gomez	Mayor Pro tem	January 2008
Glen Kliebenstein	Council Member	January 2008
Richard Smith	Council Member	January 2008
Lance Brown	Council Member	Resigned
Steve Nieman	Council Member	January 2010
Greg Woodley	Council Member (Appointed)	January 2010
Marilyn Hardee	Clerk/Treasurer	January 2007
Karl Nelson and Bruce Toenjjes	Attorney	January 2007



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INDEPENDENT AUDITOR'S REPORT

To the Honorable Mayor and
Members of the City Council:

I have audited the accompanying financial statements of the governmental activities, the business type activities, each major fund and the aggregate remaining fund information of the City of Shell Rock, Iowa, as of and for the year ended June 30, 2006, which collectively comprise the City's basic financial statements listed in the table of contents. These financial statements are the responsibility of the City of Shell Rock's management. My responsibility is to express opinions on these financial statements based on my audit.

I conducted my 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 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 my audit provides a reasonable basis for my 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. Also, as permitted by the Code of Iowa, the accounting records of the City have not been audited for all prior years. Accordingly, I was unable to satisfy myself as to the distribution of the total fund balance at July 1, 2005.

In my opinion, except for the effects of such adjustments, if any, as might have been determined to be necessary had I been able to verify the distribution by fund of the total fund balance at July 1, 2005, as discussed in the preceding paragraph, 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 Shell Rock 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.

In accordance with Government Auditing Standards, I have also issued my report dated November 8, 2006 on my consideration of the City of Shell Rock's internal control over financial reporting and my tests of its compliance with certain provisions of laws, regulations, contracts and other matters. The purpose of that report is to describe the scope of my testing of internal control over financial reporting and compliance and the results of that testing and not to provide an opinion on internal control over financial reporting or compliance. 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 my audit.

Management's Discussion and Analysis and budgetary comparison information on pages 4 through 8 and 23 through 25 are not required parts of the basic financial statements, but are supplementary information required by the Governmental Accounting Standards Board. I have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. I did not audit the information and express no opinion on it.

My audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the City of Shell Rock's basic financial statements. Other 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 my audit of the basic financial statements and, in my opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

A handwritten signature in cursive script that reads "Larry Pump".

November 8, 2006

MANAGEMENT'S DISCUSSION AND ANALYSIS

The City of Shell Rock 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. I encourage readers to consider this information in conjunction with the City's financial statements, which follow.

2006 FINANCIAL HIGHLIGHTS

Receipts of the City's governmental activities decreased 21.7%, or approximately \$216,000 from fiscal 2005 to fiscal 2006. Capital grants, contributions and restricted assets accounted for approximately \$253,000 of the decrease while operating grants, contributions and restricted assets increased approximately \$40,000.

Disbursements of the City's governmental activities decreased 18.8%, or approximately \$183,000, in fiscal 2006 from fiscal 2005. Public works, culture and recreation, community and economic development, and capital projects disbursements increased (decreased) approximately \$55,000, \$(44,000), \$109,000 and \$(305,000), respectively.

The City's total cash basis net assets decreased less than 1%, or approximately \$13,400, from June 30, 2005 to June 30, 2006. Of this amount, the assets of the governmental activities decreased approximately \$10,600 and the assets of the business type activities decreased by approximately \$2,700.

USING THIS ANNUAL REPORT

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

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

The Government-wide Financial Statement consists of a Statement of Activities and Net Assets. This statement provides 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.

Other Supplementary Information provides detailed information about the nonmajor governmental and proprietary funds.

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

One of the most important questions asked about the City's finances is, "Is the City as a whole better off or worse off as a result of the year's activities?" The Statement of Activities and Net Assets reports information which helps answer this question.

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 deteriorating.

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

Governmental Activities include public safety, public works, health and social services, culture and recreation, community and economic development, general government, debt service and capital projects. Property tax and state and federal grants finance most of these activities.

Business Type Activities include the waterworks, the sanitary sewer system and the solid waste collection. These activities are financed primarily by user charges.

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 Tax Increment Financing, 3) the Debt Service Fund, 4) the Capital Projects Fund and 5) the Permanent 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 statement for governmental funds is 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.

The required financial statement for proprietary funds is a statement of cash receipts, disbursements and changes in cash balances.

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 decreased slightly from a year ago, decreasing from \$1,090,000 to \$1,079,000. The analysis that follows focuses on the changes in cash balances for governmental activities.

Changes in Cash Basis Net Assets of Governmental Activities
(Expressed in Thousands)

	Year ended June 30,	
	2006	2005
Receipts and transfers:		
Program receipts:		
Charges for service	\$ 67	\$ 41
Operating grants, contributions and restricted interest	214	174
Capital grants, contributions and restricted assets	-	253
General receipts:		
Property tax	358	390
Local option sales tax	60	57
Unrestricted investment earnings	11	20
Other general receipts	54	44
Transfers, net	15	16
Total receipts and transfers	\$ 779	\$ 995
Disbursements:		
Public safety	\$ 150	\$ 127
Public works	139	84
Health and social services	4	-
Culture and recreation	134	178
Community and economic development	113	4
General government	134	157
Debt service	116	118
Capital projects	-	305
Total disbursements	\$ 790	\$ 973
Increase (decrease) in cash basis net assets	\$ (11)	\$ 22
Cash basis net assets beginning of year	1,090	1,068
Cash basis net assets end of year	\$1,079	\$1,090

The City's total receipts for governmental activities decreased 21.7%, or approximately \$216,000. The total cost of all programs and services decreased by approximately \$183,000, or 18.8%, with no new programs added this year. The decrease in disbursements was primarily the result of no capital projects this year, however, community and economic development increased approximately \$109,000.

The cost of all governmental activities this year was \$790,000 compared to \$973,000 last year. However, as shown in the Statement of Activities and Net Assets on pages 9-12, the amount taxpayers ultimately financed for these activities was only \$509,000 because some of the cost was paid by those directly benefited from the programs (\$67,000) or by other governments and organizations that subsidized certain programs with grants, contributions, and restricted interest \$(214,000). The City paid for the remaining "public benefit" portion of governmental activities with approximately \$417,000 in tax (some of which could only be used for certain programs) and with other receipts, such as interest and general entitlements.

Changes in Cash Basis Net Assets of Business Type Activities
(Expressed in Thousands)

	Year ended June 30,	
	2006	2005
Receipts:		
Program receipts:		
Charges for service:		
Water	\$ 91	\$ 95
Sewer	83	91
Garbage	109	94
Other	4	-
General receipts:		
Unrestricted interest on investments	2	-
Total receipts	\$ 289	\$ 280
Disbursements and transfers:		
Water	\$ 75	\$ 76
Water debt service	1	-
Sewer	87	53
Garbage	112	91
Other	2	-
Transfers, net	15	16
Total disbursements and transfers	\$ 292	\$ 236
Increase (decrease) in cash basis net assets	\$ (3)	\$ 44
Cash basis net assets beginning of year	295	251
Cash basis net assets end of year	\$ 292	\$ 295

Total business type activities receipts for the fiscal year were \$289,000 compared to \$280,000 last year. This increase was due primarily to an increase in garbage receipts. Total disbursements for the fiscal year increased by 23.7% to a total of \$292,000, while the cash balance decreased approximately \$3,000 from the prior year.

INDIVIDUAL MAJOR GOVERNMENTAL FUND ANALYSIS

As the City of Shell Rock completed the year, its governmental funds reported a combined fund balance of \$1,079,105, a decrease of \$10,642 from last year's total of \$1,089,747. The following are the major reasons for the changes in fund balances of the major funds from the prior year.

The General Fund cash balance decreased \$41,632 from the prior year to \$459,170. This decrease was due mainly to revenues being less than operating disbursements.

The Road Use Tax Fund cash balance increased by \$7,039 to \$164,794 during the fiscal year. This increase was attributable to timing of the completion of certain road projects for the upcoming fiscal year.

The Debt Service Fund cash balance increased by \$2,051 to \$36,203 due primarily to disbursements being less than transfers in.

The Capital Improvements Fund cash balance increased by \$35,975 to \$288,173 in 2006 due to no expenditures during the fiscal year.

INDIVIDUAL MAJOR BUSINESS TYPE FUND ANALYSIS

The Water Fund cash balance increased \$183 to \$135,961, due primarily to balanced revenues and expenditures.

The Sewer Fund cash balance decreased by \$5,130 to \$100,967, due primarily to an increase in operating expenses.

The Garbage Fund cash balance decreased by \$2,761 to \$125, due primarily to an increase in operating expenses.

BUDGETARY HIGHLIGHTS

Over the course of the year, the City amended its budget once on May 22, 2006. This resulted in an increase in operating disbursements related to public safety, public works, culture and recreation, community and economic development and general government of \$205,765. The City had sufficient cash balances to absorb these additional costs.

DEBT ADMINISTRATION

At June 30, 2006, the City had \$685,000 in bonds and other long-term debt, compared to \$775,000 last year, as follows:

Outstanding Debt at Year-End
(Expressed in Thousands)

	June 30,	
	2006	2005
General obligation bonds	<u>\$ 685</u>	<u>\$ 775</u>

The City did not incur any new debt during 2006. Principal and interest payments were made as scheduled. The Constitution of the State of Iowa limits the amount of general obligation debt cities can issue to 5% of the assessed value of all taxable property within the City's corporate limits. The City's outstanding general obligation debt of \$685,000 is significantly below its constitutional debt limit of \$2,344,846.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES

The City of Shell Rock's elected and appointed officials and citizens considered many factors when setting the fiscal year 2007 budget, tax rates, and fees that will be charged for various City activities. One of those factors is the economy.

CONTACTING THE CITY'S FINANCIAL MANAGEMENT

This financial report is designed to provide our citizens, taxpayers, customers, and creditors with a general overview of the City's finances and to show the City's accountability for the money it receives. If you have questions about this report or need additional financial information, contact Marilyn Hardee, City Clerk, City of Shell Rock, Iowa.

CITY OF SHELL ROCK, 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>Contributions and Restricted Interest</u>	<u>Capital Grants, Contributions and Restricted Interest</u>
FUNCTIONS/PROGRAMS:				
Governmental activities:				
Public safety	\$ 150,208	\$ 29,845	\$ 19,480	\$ -
Public works	138,823	17,235	108,676	-
Health and social services	4,355	-	-	-
Culture and recreation	133,704	14,291	6,458	-
Community and economic development	112,826	-	79,303	-
General government	134,547	5,838	-	-
Debt service	<u>116,007</u>	<u>-</u>	<u>-</u>	<u>-</u>
Total governmental activities	<u>\$ 790,470</u>	<u>\$ 67,209</u>	<u>\$ 213,917</u>	<u>\$ -</u>
Business type activities:				
Water	\$ 76,101	\$ 91,353	\$ -	\$ -
Sewer	87,169	82,823	-	-
Garbage	111,710	108,949	-	-
Other	<u>1,775</u>	<u>3,780</u>	<u>-</u>	<u>-</u>
Total business type activities	<u>\$ 276,755</u>	<u>\$ 286,905</u>	<u>\$ -</u>	<u>\$ -</u>
Total	<u>\$1,067,225</u>	<u>\$ 354,114</u>	<u>\$ 213,917</u>	<u>\$ -</u>

(Continued)

**Net (Disbursements) Receipts and
Changes in Cash Basis Net Assets**

Governmental Activities	Business Type Activities	Total
\$ (100,883)	\$ -	\$ (100,883)
(12,912)	-	(12,912)
(4,355)	-	(4,355)
(112,955)	-	(112,955)
(33,523)	-	(33,523)
(128,709)	-	(128,709)
(116,007)	-	(116,007)
\$ (509,344)	\$ -	\$ (509,344)
\$ -	\$ 15,252	\$ 15,252
-	(4,346)	(4,346)
-	(2,761)	(2,761)
-	2,005	2,005
\$ -	\$ 10,150	\$ 10,150
\$ (509,344)	\$ 10,150	\$ (499,194)

CITY OF SHELL ROCK, IOWA
STATEMENT OF ACTIVITIES AND NET ASSETS - CASH BASIS
AS OF AND FOR THE YEAR ENDED JUNE 30, 2006

General Receipts:

Property and other city tax levied for:
 General purposes
 Tax increment financing
 Debt service
Local option sales tax
Unrestricted interest on investments
Miscellaneous
Transfers

Total general receipts and transfers

Change in cash basis net assets

Cash basis net assets beginning of year

Cash basis net assets end of year

Cash Basis Net Assets

Restricted:
 Streets
 Urban renewal purposes
 Debt service
 Other purposes
Unrestricted

Total cash basis net assets

See Notes to Financial Statements.

**Net (Disbursements) Receipts and
Changes in Cash Basis Net Assets**

<u>Governmental Activities</u>	<u>Business Type Activities</u>	<u>Total</u>
\$ 295,021	\$ -	\$ 295,021
6,154	-	6,154
56,652	-	56,652
59,747	-	59,747
11,494	2,536	14,030
54,214	-	54,214
<u>15,420</u>	<u>(15,420)</u>	<u>-</u>
<u>\$ 498,702</u>	<u>\$ (12,884)</u>	<u>\$ 485,818</u>
\$ (10,642)	\$ (2,734)	\$ (13,376)
<u>1,089,747</u>	<u>294,969</u>	<u>1,384,716</u>
<u>\$1,079,105</u>	<u>\$ 292,235</u>	<u>\$ 1,371,340</u>
\$ 164,794	\$ -	\$ 164,794
21,605	-	21,605
36,203	-	36,203
397,333	55,182	452,515
<u>459,170</u>	<u>237,053</u>	<u>696,223</u>
<u>\$1,079,105</u>	<u>\$ 292,235</u>	<u>\$ 1,371,340</u>

CITY OF SHELL ROCK, IOWA
STATEMENT OF CASH RECEIPTS, DISBURSEMENTS AND CHANGES IN CASH BALANCES
GOVERNMENTAL FUNDS
AS OF AND FOR THE YEAR ENDED JUNE 30, 2006

	<u>General</u>	<u>Special Revenue Road Use Tax</u>
RECEIPTS:		
Property tax	\$ 263,830	\$ -
Tax increment financing	-	-
Other city tax	4,615	-
Licenses and permits	4,752	-
Use of money and property	6,919	-
Intergovernmental	105,241	108,676
Charges for service	41,361	-
Special assessments	2,127	-
Miscellaneous	30,009	-
Total receipts	<u>\$ 458,854</u>	<u>\$ 108,676</u>
DISBURSEMENTS:		
Operating:		
Public safety	\$ 150,208	\$ -
Public works	37,186	101,637
Health and social services	4,355	-
Culture and recreation	129,541	-
Community and economic development	90,281	-
General government	134,547	-
Debt service	400	-
Total disbursements	<u>\$ 546,518</u>	<u>\$ 101,637</u>
Excess (deficiency) of receipts over (under) disbursements	<u>\$ (87,664)</u>	<u>\$ 7,039</u>
Other financing sources (uses):		
Operating transfers in	\$ 79,919	\$ -
Operating transfers out	(33,887)	-
Total other financing sources (uses)	<u>\$ 46,032</u>	<u>\$ -</u>
Net change in cash balances	\$ (41,632)	\$ 7,039
Cash balances beginning of year	<u>500,802</u>	<u>157,755</u>
Cash balances end of year	<u>\$ 459,170</u>	<u>\$ 164,794</u>
Cash Basis Fund Balances:		
Reserved:		
Debt service	\$ -	\$ -
Unreserved:		
General fund	459,170	-
Special revenue funds	-	164,794
Capital projects funds	-	-
Permanent fund	-	-
Total cash basis fund balances	<u>\$ 459,170</u>	<u>\$ 164,794</u>

See Notes to Financial Statements.

<u>Debt Service</u>	<u>Permanent Capital Improvements</u>	<u>Other Nonmajor Governmental Funds</u>	<u>Total</u>
\$ 56,652	\$ -	\$ 31,191	\$ 351,673
-	-	6,154	6,154
-	-	59,747	64,362
-	-	-	4,752
150	5,597	1,043	13,709
-	2,282	-	216,199
-	-	-	41,361
-	-	17,235	19,362
-	14,492	2,335	46,836
<u>\$ 56,802</u>	<u>\$ 22,371</u>	<u>\$ 117,705</u>	<u>\$ 764,408</u>
\$ -	\$ -	\$ -	\$ 150,208
-	-	-	138,823
-	-	-	4,355
-	-	4,163	133,704
-	-	22,545	112,826
-	-	-	134,547
115,607	-	-	116,007
<u>\$ 115,607</u>	<u>\$ -</u>	<u>\$ 26,708</u>	<u>\$ 790,470</u>
<u>\$ (58,805)</u>	<u>\$ 22,371</u>	<u>\$ 90,997</u>	<u>\$ (26,062)</u>
\$ 60,856	\$ 50,332	\$ -	\$ 191,107
-	(36,728)	(105,072)	(175,687)
<u>\$ 60,856</u>	<u>\$ 13,604</u>	<u>\$ (105,072)</u>	<u>\$ 15,420</u>
\$ 2,051	\$ 35,975	\$ (14,075)	\$ (10,642)
34,152	252,198	144,840	1,089,747
<u>\$ 36,203</u>	<u>\$ 288,173</u>	<u>\$ 130,765</u>	<u>\$ 1,079,105</u>
\$ 36,203	\$ -	\$ -	\$ 36,203
-	-	-	459,170
-	-	117,259	282,053
-	-	13,506	13,506
-	288,173	-	288,173
<u>\$ 36,203</u>	<u>\$ 288,173</u>	<u>\$ 130,765</u>	<u>\$ 1,079,105</u>

CITY OF SHELL ROCK, IOWA
STATEMENT OF CASH RECEIPTS, DISBURSEMENTS AND
CHANGES IN CASH BALANCES
PROPRIETARY FUNDS
AS OF AND FOR THE YEAR ENDED JUNE 30, 2006

	<u>Enterprise Funds</u>		
	<u>Water</u>	<u>Sewer</u>	<u>Garbage</u>
Operating receipts:			
Charges for service	\$ 91,353	\$ 82,823	\$ 108,949
Operating disbursements:			
Business type activities	<u>75,281</u>	<u>87,169</u>	<u>111,710</u>
Excess (deficiency) of operating receipts over (under) operating disbursements	<u>\$ 16,072</u>	<u>\$ (4,346)</u>	<u>\$ (2,761)</u>
Non-operating receipts (disbursements):			
Interest on investments	\$ 1,551	\$ 416	\$ -
Debt service	<u>(820)</u>	<u>-</u>	<u>-</u>
Total non-operating receipts (disbursements)	<u>\$ 731</u>	<u>\$ 416</u>	<u>\$ -</u>
Excess (deficiency) of receipts over (under) disbursements	<u>\$ 16,803</u>	<u>\$ (3,930)</u>	<u>\$ (2,761)</u>
Other financing sources (uses):			
Operating transfers in	\$ -	\$ -	\$ -
Operating transfers out	<u>(16,620)</u>	<u>(1,200)</u>	<u>-</u>
Total other financing sources (uses)	<u>\$ (16,620)</u>	<u>\$ (1,200)</u>	<u>\$ -</u>
Net change in cash balances	\$ 183	\$ (5,130)	\$ (2,761)
Cash balances beginning of year	<u>135,778</u>	<u>106,097</u>	<u>2,886</u>
Cash balances end of year	<u>\$ 135,961</u>	<u>\$ 100,967</u>	<u>\$ 125</u>
Cash Basis Fund Balances			
Reserved for other	\$ -	\$ -	\$ -
Unreserved	<u>135,961</u>	<u>100,967</u>	<u>125</u>
Total cash basis fund balances	<u>\$ 135,961</u>	<u>\$ 100,967</u>	<u>\$ 125</u>

See Notes to Financial Statements.

<u>Nonmajor Enterprise Funds</u>	<u>Total</u>
\$ 3,780	\$ 286,905
<u>1,775</u>	<u>275,935</u>
\$ 2,005	\$ 10,970
\$ 569	\$ 2,536
<u>-</u>	<u>(820)</u>
\$ 569	\$ 1,716
\$ 2,574	\$ 12,686
\$ 2,400	\$ 2,400
<u>-</u>	<u>(17,820)</u>
\$ 2,400	\$ (15,420)
\$ 4,974	\$ (2,734)
<u>50,208</u>	<u>294,969</u>
<u>\$ 55,182</u>	<u>\$ 292,235</u>
\$ 55,182	\$ 55,182
<u>-</u>	<u>237,053</u>
<u>\$ 55,182</u>	<u>\$ 292,235</u>

CITY OF SHELL ROCK, IOWA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2006

(1) Summary of Significant Accounting Policies

The City of Shell Rock is a political subdivision of the State of Iowa located in Butler County. It was first incorporated in 1873 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, health and social services, culture and recreation, community and economic development, and general government services. The City also provides water, sewer, and solid waste utilities for its citizens.

A. Reporting Entity

For financial reporting purposes, the City of Shell Rock 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. The City has no component units which meet the Governmental Accounting Standards Board Criteria.

Jointly Governed Organizations - The City 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 Butler County Assessor's Conference Board and Butler County Emergency Management Commission.

B. Basis of Presentation

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

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

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

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

CITY OF SHELL ROCK, IOWA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2006

(1) Summary of Significant Accounting Policies - continued

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

Fund Financial Statements - Separate financial statements are provided for 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 and proprietary funds are aggregated and reported as nonmajor governmental and proprietary funds.

The City reports the following major governmental funds:

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

Special Revenue:

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

The Debt Service Fund is utilized to account for the payment of interest and principal on the City's general long-term debt.

The Capital Improvements Fund is used to account for moneys set aside for various City capital improvements.

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 Garbage Fund is used to account for the operation of the City's solid waste collection.

CITY OF SHELL ROCK, IOWA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2006

(1) Summary of Significant Accounting Policies - continued

C. Measurement Focus and Basis of Accounting

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

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

D. Budgets and Budgetary Accounting

The budgetary comparison and related disclosures are reported as Required Supplementary Information. During the year ended June 30, 2006, disbursements exceeded the amount budgeted in the community and economic development function.

(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.

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.

The City's investments at June 30, 2006 are as follows:

	<u>Carrying Amount</u>	<u>Fair Value</u>
U.S. Savings Bond	<u>\$ 50</u>	<u>\$ 50</u>

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.

CITY OF SHELL ROCK, IOWA
 NOTES TO FINANCIAL STATEMENTS
 JUNE 30, 2006

(3) **Bonds Payable**

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

Year Ending June 30,	General Obligation Bonds	
	Principal	Interest
2007	\$ 75,000	\$ 23,538
2008	80,000	21,588
2009	80,000	19,268
2010	85,000	16,788
2011	85,000	13,940
2012	90,000	10,880
2013	95,000	7,505
2014	95,000	3,800
Total	<u>\$685,000</u>	<u>\$117,307</u>

The Code of Iowa requires principal and interest on general obligation bonds be paid from the Debt Service Fund. However, during the year, \$820 of general obligation bond principal and interest was paid from the Enterprise, Water Fund.

The resolutions providing for the issuance of the general obligation bonds include the following provision:

At the option of the City, bonds maturing after June 1, 2009 may be called for redemption and paid before maturity on said date or any date thereafter, from any funds regardless of source, in whole or from time to time in part, in any order of maturity and within an annual maturity by lot. The terms of redemption shall be par plus accrued interest to date of call.

(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 statement and required supplementary information. The report may be obtained by writing to IPERS, P.O. Box 9117, Des Moines, Iowa, 50306-9117.

Most regular plan members are required to contribute 3.70% of their annual covered salary and the City is required to contribute 5.75% of covered salary. Certain employees in special risk occupations and the City contribute an actuarially determined contribution rate. Contribution requirements are established by state statute. The City's contribution to IPERS for the year ended June 30, 2006, was \$12,854, which was equal to the required contribution for the year.

CITY OF SHELL ROCK, IOWA
 NOTES TO FINANCIAL STATEMENTS
 JUNE 30, 2006

(5) **Compensated Absences**

City employees accumulate a limited amount of earned but unused vacation, comp time and sick leave 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 approximate liability for earned vacation payable, comp time payable, and sick leave payable to employees at June 30, 2006, primarily relating to the General Fund, is as follows:

<u>Type of Benefit</u>	<u>Amount</u>
Vacation	\$ 5,994
Comp time	2,468
Sick leave	25,577
Total	<u>\$ 34,039</u>

This liability has been computed based on rates of pay in effect at June 30, 2006.

(6) **Risk Management**

The City of Shell Rock 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 did not exceed commercial insurance coverage in the past fiscal year.

(7) **Interfund Transfers**

The detail of interfund transfers for the year ended June 30, 2006 is as follows:

<u>Transfer to</u>	<u>Transfer from</u>	<u>Amount</u>
General	Special Revenue:	
	Employee Benefits	\$ 31,191
	Local Option Sales Tax	12,000
	Permanent:	
	Capital Improvements	36,728
		<u>\$ 79,919</u>
Debt Service	Special Revenue:	
	Local Option Sales Tax	\$ 35,000
	Capital Projects:	
	Street Improvement Project	10,436
	Enterprise:	
	Water	15,420
		<u>\$ 60,856</u>
Permanent:	Capital Improvements	
	General	\$ 33,887
	Special Revenue:	
	Street Special Assessment	16,445
		<u>\$ 50,332</u>

CITY OF SHELL ROCK, IOWA
 NOTES TO FINANCIAL STATEMENTS
 JUNE 30, 2006

(7) Interfund Transfers - continued

<u>Transfer to</u>	<u>Transfer from</u>	<u>Amount</u>
Enterprise:		
Water Depreciation	Enterprise:	
	Water	\$ 1,200
Sewer Depreciation	Enterprise:	
	Sewer	1,200
		<u>\$ 2,400</u>
Total		<u>\$193,507</u>

Transfers generally move resources from the fund statutorily required to collect the resources to the fund statutorily required to disburse the resources.

(8) Commitments

At June 30, 2006, the following construction commitments had been made:

<u>Project</u>	<u>Total Contract</u>	<u>Costs Incurred To Date</u>
Boyd Building Tuck pointing	\$ 9,170	\$ -
International Dump Truck	42,000	-
Street Repair	<u>9,718</u>	<u>-</u>
Total	<u>\$ 60,888</u>	<u>\$ -</u>

Required Supplementary Information

CITY OF SHELL ROCK, IOWA
 BUDGETARY COMPARISON SCHEDULE OF RECEIPTS, DISBURSEMENTS
 AND CHANGES IN BALANCES
 BUDGET AND ACTUAL (CASH BASIS) - ALL
 GOVERNMENTAL FUNDS AND PROPRIETARY FUNDS
 REQUIRED SUPPLEMENTARY INFORMATION
 YEAR ENDED JUNE 30, 2006

	<u>Governmental Funds Actual</u>	<u>Proprietary Funds Actual</u>	<u>Less Funds Not Required to be Budgeted</u>
RECEIPTS:			
Property tax	\$ 351,673	\$ -	\$ -
Tax increment financing	6,154	-	-
Other city tax	64,362	-	-
Licenses and permits	4,752	-	-
Use of money and property	13,709	2,536	-
Intergovernmental	216,199	-	-
Charges for service	41,361	286,905	-
Special assessments	19,362	-	-
Miscellaneous	46,836	-	-
Total receipts	<u>\$ 764,408</u>	<u>\$ 289,441</u>	<u>\$ -</u>
DISBURSEMENTS:			
Public safety	\$ 150,208	\$ -	\$ -
Public works	138,823	-	-
Health and social services	4,355	-	-
Culture and recreation	133,704	-	-
Community and economic development	112,826	-	-
General government	134,547	-	-
Debt service	116,007	-	-
Capital projects	-	-	-
Business type activities	-	276,755	-
Total disbursements	<u>\$ 790,470</u>	<u>\$ 276,755</u>	<u>\$ -</u>
Excess (deficiency) of receipts over (under) disbursements	\$ (26,062)	\$ 12,686	\$ -
Other financing sources, net	<u>15,420</u>	<u>(15,420)</u>	<u>-</u>
Excess (deficiency) of receipts and other financing sources over (under) disbursements and other financing uses	\$ (10,642)	\$ (2,734)	\$ -
Balance beginning of year	<u>1,089,747</u>	<u>294,969</u>	<u>-</u>
Balance end of year	<u>\$ 1,079,105</u>	<u>\$ 292,235</u>	<u>\$ -</u>

See Accompanying Independent Auditor's Report.

<u>Net</u>	<u>Budgeted Amounts</u>		<u>Final to Net Variance</u>
	<u>Original</u>	<u>Final</u>	
\$ 351,673	\$ 340,117	\$ 340,117	\$ 11,556
6,154	-	-	6,154
64,362	66,265	66,265	(1,903)
4,752	9,355	9,355	(4,603)
16,245	20,520	20,520	(4,275)
216,199	141,000	186,000	30,199
328,266	327,445	327,445	821
19,362	7,000	7,000	12,362
46,836	49,300	59,300	(12,464)
<u>\$1,053,849</u>	<u>\$ 961,002</u>	<u>\$ 1,016,002</u>	<u>\$ 37,847</u>
\$ 150,208	\$ 168,171	\$ 191,971	\$ 41,763
138,823	171,585	201,585	62,762
4,355	10,700	10,700	6,345
133,704	130,479	192,444	58,740
112,826	5,457	30,457	(82,369)
134,547	136,205	201,205	66,658
116,007	117,340	117,340	1,333
-	3,000	3,000	3,000
276,755	299,572	299,572	22,817
<u>\$1,067,225</u>	<u>\$1,042,509</u>	<u>\$ 1,248,274</u>	<u>\$ 181,049</u>
\$ (13,376)	\$ (81,507)	\$ (232,272)	\$ 218,896
<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
\$ (13,376)	\$ (81,507)	\$ (232,272)	\$ 218,896
<u>1,384,716</u>	<u>1,163,937</u>	<u>1,163,937</u>	<u>220,779</u>
<u>\$1,371,340</u>	<u>\$1,082,430</u>	<u>\$ 931,665</u>	<u>\$ 439,675</u>

CITY OF SHELL ROCK, IOWA
NOTES TO REQUIRED SUPPLEMENTARY INFORMATION - BUDGETARY REPORTING
JUNE 30, 2006

The budgetary comparison is presented as Required Supplementary Information in accordance with Governmental Accounting Standards Board Statement No. 41 for governments with significant budgetary perspective differences resulting from not being able to present budgetary comparisons for the General Fund and each major Special Revenue Fund.

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. These ten functions are: public safety, public works, health and social services, culture and recreation, community and economic development, general government, debt service, capital projects, business type activities and non-program. Function disbursements required to be budgeted include disbursements for the General Fund, the Special Revenue Funds, the Debt Service Fund, the Capital Projects Funds, the Permanent Fund and the Proprietary Funds. Although the budget document presents function disbursements by fund, the legal level of control is at the aggregated function level, not by fund. During the year, one budget amendment increased budgeted disbursements. The budget amendment is reflected in the final budgeted amounts.

During the year ended June 30, 2006, disbursements exceeded the amount budgeted in the community and economic development function.

Other Supplementary Information

CITY OF SHELL ROCK, 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		
	Employee Benefits	Local Option Sales Tax	Tax Increment Financing
RECEIPTS:			
Property tax	\$ 31,191	\$ -	\$ -
Tax increment financing	-	-	-
Other city tax	-	59,747	-
Use of money and property	-	-	-
Special assessments	-	-	-
Miscellaneous	-	-	-
Total receipts	\$ 31,191	\$ 59,747	\$ -
DISBURSEMENTS:			
Operating:			
Culture and recreation	\$ -	\$ -	\$ -
Community and economic development	-	-	19,468
Total disbursements	\$ -	\$ -	\$ 19,468
Excess (deficiency) of receipts over (under) disbursements	\$ 31,191	\$ 59,747	\$ (19,468)
Other financing uses:			
Operating transfers out	(31,191)	(47,000)	-
Net change in cash balances	\$ -	\$ 12,747	\$ (19,468)
Cash balances beginning of year	-	12,959	41,073
Cash balances end of year	\$ -	\$ 25,706	\$ 21,605
Cash Basis Fund Balances:			
Unreserved:			
Special revenue funds	\$ -	\$ 25,706	\$ 21,605
Capital projects funds	-	-	-
Total cash basis fund balances	\$ -	\$ 25,706	\$ 21,605

See Accompanying Independent Auditor's Report.

Revenue			Capital Projects		
Tax Increment Financing-Wosepka	Revolving Economic Development	Street Special Assessment	Library Building Project	Street Improvement Project	Total
\$ -	\$ -	\$ -	\$ -	\$ -	\$ 31,191
6,154	-	-	-	-	6,154
-	-	-	-	-	59,747
-	1,043	-	-	-	1,043
-	-	7,179	-	10,056	17,235
-	-	-	2,335	-	2,335
<u>\$ 6,154</u>	<u>\$ 1,043</u>	<u>\$ 7,179</u>	<u>\$ 2,335</u>	<u>\$ 10,056</u>	<u>\$ 117,705</u>
\$ -	\$ -	\$ -	\$ 4,163	\$ -	\$ 4,163
3,077	-	-	-	-	22,545
<u>\$ 3,077</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 4,163</u>	<u>\$ -</u>	<u>\$ 26,708</u>
\$ 3,077	\$ 1,043	\$ 7,179	\$ (1,828)	\$ 10,056	\$ 90,997
-	-	(16,445)	-	(10,436)	(105,072)
\$ 3,077	\$ 1,043	\$ (9,266)	\$ (1,828)	\$ (380)	\$ (14,075)
-	65,828	9,266	15,334	380	144,840
<u>\$ 3,077</u>	<u>\$ 66,871</u>	<u>\$ -</u>	<u>\$ 13,506</u>	<u>\$ -</u>	<u>\$ 130,765</u>
\$ 3,077	\$ 66,871	\$ -	\$ -	\$ -	\$ 117,259
-	-	-	13,506	-	13,506
<u>\$ 3,077</u>	<u>\$ 66,871</u>	<u>\$ -</u>	<u>\$ 13,506</u>	<u>\$ -</u>	<u>\$ 130,765</u>

CITY OF SHELL ROCK, IOWA
SCHEDULE OF CASH RECEIPTS, DISBURSEMENTS AND
CHANGES IN CASH BALANCES
NONMAJOR PROPRIETARY FUNDS
AS OF AND FOR THE YEAR ENDED JUNE 30, 2006

	<u>Enterprise Funds</u>			<u>Total</u>
	<u>Customer Deposits</u>	<u>Water Depreciation</u>	<u>Sewer Depreciation</u>	
Operating Receipts:				
Charges for service	\$ 3,780	\$ -	\$ -	\$ 3,780
Operating Disbursements:				
Business type activities	<u>1,775</u>	<u>-</u>	<u>-</u>	<u>1,775</u>
Excess of operating receipts over operating disbursements	\$ 2,005	\$ -	\$ -	\$ 2,005
Non-operating receipts:				
Interest on investments	<u>39</u>	<u>375</u>	<u>155</u>	<u>569</u>
Excess of receipts over disbursements	\$ 2,044	\$ 375	\$ 155	\$ 2,574
Other financing sources:				
Operating transfers in	<u>-</u>	<u>1,200</u>	<u>1,200</u>	<u>2,400</u>
Net change in cash balances	\$ 2,044	\$ 1,575	\$ 1,355	\$ 4,974
Cash balances beginning of year	<u>16,892</u>	<u>23,303</u>	<u>10,013</u>	<u>50,208</u>
Cash balances end of year	<u>\$ 18,936</u>	<u>\$ 24,878</u>	<u>\$ 11,368</u>	<u>\$ 55,182</u>
Cash Basis Fund Balances:				
Reserved for other	<u>\$ 18,936</u>	<u>\$ 24,878</u>	<u>\$ 11,368</u>	<u>\$ 55,182</u>

See Accompanying Independent Auditor's Report.

CITY OF SHELL ROCK, IOWA
 SCHEDULE OF INDEBTEDNESS
 YEAR ENDED JUNE 30, 2006

<u>Obligation</u>	<u>Date of Issue</u>	<u>Interest Rates</u>	<u>Amount Originally Issued</u>
General Obligation Bonds:			
Essential Corporate Purpose	01/01/04	1.75-4.00%	\$ 835,000
Essential Corporate Purpose	01/01/94	3.60-5.60	150,000
Total indebtedness			

See Accompanying Independent Auditor's Report.

<u>Balance Beginning of Year</u>	<u>Issued During Year</u>	<u>Redeemed During Year</u>	<u>Balance End of Year</u>	<u>Interest Paid</u>	<u>Interest Due and Unpaid</u>
\$760,000	\$ -	\$ 75,000	\$685,000	\$ 25,188	\$ -
<u>15,000</u>	<u>-</u>	<u>15,000</u>	<u>-</u>	<u>840</u>	<u>-</u>
<u><u>\$775,000</u></u>	<u><u>\$ -</u></u>	<u><u>\$ 90,000</u></u>	<u><u>\$685,000</u></u>	<u><u>\$ 26,028</u></u>	<u><u>\$ -</u></u>

CITY OF SHELL ROCK, IOWA
BOND MATURITIES
JUNE 30, 2006

<u>Year</u> <u>Ending</u> <u>June 30,</u>	<u>GENERAL OBLIGATION BONDS</u>	
	<u>Essential</u>	
	<u>Corporate Purpose</u>	
	<u>Issued January 1, 2004</u>	
	<u>Interest Rates</u>	<u>Amount</u>
2007	2.60%	\$ 75,000
2008	2.90	80,000
2009	3.10	80,000
2010	3.35	85,000
2011	3.60	85,000
2012	3.75	90,000
2013	3.90	95,000
2014	4.00	<u>95,000</u>
Total		<u>\$685,000</u>

See Accompanying Independent Auditor's Report.



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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:

I have audited the accompanying financial statements of the governmental activities, business type activities, each major fund and the aggregate remaining fund information of the City of Shell Rock, Iowa, as of and for the year ended June 30, 2006, which collectively comprise the City's basic financial statements listed in the table of contents and have issued my report thereon dated November 8, 2006. My report on the financial statements, which were prepared in conformity with an other comprehensive basis of accounting, expressed a qualified opinion since I was unable to satisfy myself as to the distribution by fund of the total fund balance at July 1, 2005. I conducted my 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 my audit, I considered the City of Shell Rock's internal control over financial reporting in order to determine my auditing procedures for the purpose of expressing my opinions on the financial statements and not to provide an opinion on the internal control over financial reporting. However, I noted certain matters involving the internal control over financial reporting and its operation that I consider to be reportable conditions. Reportable conditions involve matters coming to my attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in my judgment, could adversely affect the City of Shell Rock'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.

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. 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, of the reportable conditions described above, I believe items II-A-06 and II-C-06 are material weaknesses.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the City of Shell Rock's financial statements are free of material misstatement, I performed tests of its compliance with certain provisions of laws, regulations and contracts, non-compliance with which could have a direct and material effect on the determination of financial 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 no instances of non-compliance or other matters that are required to be reported under Government Auditing Standards. However, I noted certain immaterial instances of non-compliance or other matters that are described in Part IV 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 my audit of the financial statements of the City. 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.

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 Shell Rock and other parties to whom the City of Shell Rock may report. This report is not intended to be and should not be used by anyone other than these specified parties.

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



November 8, 2006

CITY OF SHELL ROCK, IOWA
Schedule of Findings
Year Ended June 30, 2006

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

- (a) Qualified opinions were issued on the financial statements, which were prepared in conformity with an other comprehensive basis of accounting, since I was unable to satisfy myself as to the distribution by fund of the total fund balance at July 1, 2005.
- (b) Reportable conditions in internal control over financial reporting were disclosed by the audit of the financial statements, including material weaknesses.
- (c) The audit did not disclose any noncompliance which is material to the financial statements.

Part II: Findings Related to the Financial Statements:

INSTANCES OF NON-COMPLIANCE:

No matters were noted.

REPORTABLE CONDITIONS:

II-A-06 Segregation of Duties - One important aspect of internal control is the segregation of duties among employees to prevent an individual employee from handling duties which are incompatible. I noted that certain accounting functions are not properly segregated.

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

Response - We will review procedures and make changes to improve internal control where possible.

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

II-B-06 Information Systems Controls - The City does not have a written disaster recovery plan. Also, adequate fire protection of computers and files does not exist.

Recommendation - The City should implement the controls necessary to protect the processing of computer information.

Response - We will do this.

Conclusion - Response accepted.

CITY OF SHELL ROCK, IOWA
Schedule of Findings
Year Ended June 30, 2006

Part II: Findings Related to the Financial Statements: - continued

II-C-06 Bank Signature Cards - I noted that the bank signature cards were not current.

Recommendation - All bank authorized signature cards should be reviewed and updated. Only current City employees, board members, or council members should be authorized signers.

Response - We will review all signature cards and update them per guidelines recommended.

Conclusion - Response accepted.

Part III: Findings and Questioned Costs for Federal Awards:

Not applicable

Part IV: Other Findings Related to Statutory Reporting:

IV-A-06 Certified Budget - Disbursements during the year ended June 30, 2006 exceeded the amount budgeted in the community and economic development function. Chapter 384.20 of the Code of Iowa states in part that public monies may not be expended or encumbered except under an annual or continuing appropriation.

Recommendation - The budget should have been amended in accordance with Chapter 384.18 of the Code of Iowa before disbursements were allowed to exceed the budget.

Response - We will do this in the future.

Conclusion - Response accepted.

IV-B-06 Questionable Disbursements - No disbursements were noted that I believe may not meet the requirements of public purpose as defined in an Attorney General's opinion dated April 25, 1979.

IV-C-06 Travel Expense - No disbursements of City money for travel expenses of spouses of City officials or employees were noted.

IV-D-06 Business Transactions - No business transactions between the City and City officials or employees were noted.

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

IV-F-06 Council Minutes - No transactions were found that I believe should have been approved in the Council minutes but were not.

CITY OF SHELL ROCK, IOWA
Schedule of Findings
Year Ended June 30, 2006

Part IV Other Findings Related to Statutory Reporting: - continued

IV-G-06 Deposits and Investments - The interest rate on certain time certificates of deposit did not meet the minimum rate of interest set by the State Rate Setting Committee.

Recommendation - The City should be aware of the current allowable rates to insure that at least the minimum rate is received for all investments. The certificates of deposit, when renewed, should be renewed at a rate of interest which conforms with current rates for public funds on the date of renewal. The City should seek reimbursement of the additional interest due on the certificates.

Response - These certificates will be renewed at an allowable rate and the bank has agreed to reimburse the additional interest.

Conclusion - Response accepted.

IV-H-06 Payment of General Obligation Bonds - I noted that general obligation debt was paid from the Enterprise Fund - Water Account, and not from the Debt Service Fund, as required by Chapter 384.4 of the Code of Iowa.

Recommendation - The City should make general obligation debt payments from the Debt Service Fund as required by the Code.

Response - We will do this.

Conclusion - Response accepted.

