

CITY OF UNDERWOOD
INDEPENDENT AUDITORS' REPORTS
BASIC FINANCIAL STATEMENTS
AND SUPPLEMENTARY INFORMATION
SCHEDULE OF FINDINGS

JUNE 30, 2007

Table of Contents

| | | <u>Page</u> |
|---|-----------------|-------------|
| Officials | | 3 |
| Independent Auditors' Report | | 5-6 |
| Management's Discussion and Analysis | | 7-12 |
| Basic Financial Statements: | <u>Exhibit</u> | |
| Government-wide Financial Statement: | | |
| Statement of Activities and Net Assets – Cash Basis | A | 14-15 |
| Governmental Fund Financial Statements: | | |
| Statement of Cash Receipts, Disbursements and Changes in Cash Balances | B | 16-17 |
| Reconciliation of the Statement of Cash Receipts, Disbursements and Changes in Cash Balances to the Statement of Activities and Net Assets | C | 18 |
| Proprietary Fund Financial Statements: | | |
| Statement of Cash Receipts, Disbursements and Changes in Cash Balances | D | 19 |
| Reconciliation of the Statement of Cash Receipts, Disbursements and Changes in Cash Balances to the Statement of Activities and Net Assets | E | 20 |
| Notes to Financial Statements | | 21-30 |
| Required Supplementary Information: | | |
| Budgetary Comparison Schedule of Receipts, Disbursements and Changes in Balances - Budget and Actual (Cash Basis) – All Governmental Funds and Proprietary Funds | | 32-33 |
| Notes to Required Supplementary Information – Budgetary Reporting | | 34 |
| Other Supplementary Information: | <u>Schedule</u> | |
| Statement of Cash Receipts, Disbursements and Changes in Cash Balances - Nonmajor Governmental Funds | 1 | 36 |
| Schedule of Indebtedness | 2 | 37-38 |
| Bond and Note Maturities | 3 | 39-40 |
| Schedule of Receipts by Source and Disbursements by Function – All Governmental Funds | 4 | 41 |
| Independent Auditors' Report on Internal Control over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with <i>Government Auditing Standards</i> | | 43-44 |
| Schedule of Findings | | 45-48 |

City of Underwood

Officials

| <u>Name</u> | <u>Title</u> | <u>Term Expires</u> |
|-----------------|----------------|---------------------|
| Craig Zenor | Mayor | January 2008 |
| Shawn McKee | Council Member | January 2008 |
| Rhonda Johnson | Council Member | January 2008 |
| Robert Dose | Council Member | January 2008 |
| Edward Freuck | Council Member | January 2010 |
| Jim Pingel | Council Member | January 2010 |
| | | |
| Kelly Groskurth | City Clerk | Indefinite |
| Lea Voss | Treasurer | Indefinite |
| Scott Peters | Attorney | Indefinite |

City of Underwood

November 7, 2007

Independent Auditors' Report

To the Honorable Mayor and
Members of the City Council:

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 Underwood, Iowa, as of and for the year ended June 30, 2007, 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 Underwood's management. Our responsibility is to express opinions 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 require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe 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.

In our opinion, 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 Underwood as of June 30, 2007, 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*, we have also issued our reports dated November 7, 2007 on our consideration of the City of Underwood'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. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the 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 our audit.

Continued...

Independent Auditor's Report
City of Underwood

Management's Discussion and Analysis and budgetary comparison information on pages 7 through 12 and 32 through 34 are not required parts of the basic financial statements, but are supplementary information required by the Governmental Accounting Standards Board. We applied limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, 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 the City of Underwood's basic financial statements. We previously audited, in accordance with the standards referred to in the second paragraph of this report, the financial statements for the three years ended June 30, 2006 (none of which are presented herein) and expressed unqualified opinions on those 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 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.

MANAGEMENT'S DISCUSSION AND ANALYSIS

As management of the City of Underwood, we offer readers of the City of Underwood's financial statements this narrative overview and analysis of the financial activities of the City of Underwood for the fiscal year ending June 30, 2007. This section should be read in conjunction with the financial statements and the accompanying notes that follow.

2007 Financial Highlights

- Receipts of the City's governmental activities increased by 12.20%, or approximately \$69,000 from fiscal 2006 to fiscal 2007. Property tax increased approximately \$19,000. Tax increment financing increased approximately \$36,000. Intergovernmental receipts increased \$25,000.
- Disbursements increased 3.5%, or approximately \$23,000, in fiscal 2007 from fiscal 2006. Public safety, community & economic development, culture and recreation, and debt service disbursements increased \$79,628, \$15,453, \$9,944, and \$5,182, respectively. Public works, general government, and capital projects disbursements decreased \$19,941, \$9,964, and \$57,079, respectively.
- The City's total cash basis net assets increased 42.5%, or approximately \$175,000, from June 30, 2006 to June 30, 2007. Of this amount, the assets of the governmental activities increased approximately \$117,000 the assets of the business type activities increased by approximately \$58,000.

USING THIS ANNUAL REPORT

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

Management's Discussion and Analysis 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 non-major governmental 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 limitation 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, culture and recreation, community and economic development, general government, and debt service. Property tax and state and federal grants finance most of these activities.
- Business Type Activities include the solid waste removal, and the sanitary sewer system. This activity is 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 Urban Renewal Tax Increment, and 3) the Debt Service 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 two Enterprise Funds to provide separate information for the solid waste (garbage) fund and the sewer fund. The Sewer Fund is considered to be a major fund of the City.

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

Reconciliations between the government-wide statement and the fund financial statements follow the fund financial statements.

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 moderately from a year ago, increasing from \$333 thousand to \$450 thousand. 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) | | |
|---|----------------------------|-------------|
| | <u>Year Ended June 30,</u> | |
| | <u>2007</u> | <u>2006</u> |
| Receipts and other financing sources: | | |
| Property tax | \$ 231 | 212 |
| Tax increment financing collections | 112 | 76 |
| Other city tax | 85 | 91 |
| Licenses and permits | 6 | 8 |
| Use of money and property | 13 | 3 |
| Intergovernmental | 155 | 130 |
| Charges for service | 10 | 16 |
| Special assessments | 0 | 0 |
| Miscellaneous | 21 | 28 |
| | 633 | 564 |
| Disbursements and other financing uses: | | |
| Public safety | 245 | 165 |
| Public works | 42 | 62 |
| Health and social services | 0 | 0 |
| Culture and recreation | 22 | 12 |
| Community and economic development | 123 | 108 |
| General government | 117 | 127 |
| Debt service | 97 | 92 |
| Capital projects | 28 | 85 |
| | 674 | 651 |
| Excess (deficiency) of receipts over (under) disbursements | <41> | <87> |
| Other financing sources (uses), net | 158 | 153 |
| Net change in cash basis net assets | 117 | 66 |
| Cash basis net assets beginning of year | 333 | 267 |
| Cash basis net assets end of year | 450 | 333 |

The total receipts for governmental activities increased by 12.2%, or \$69,000. The total cost of all programs and services increased by approximately \$23,000 or 3.5%, with no new programs added this year.

The City property tax rates remained the same.

The cost of all governmental activities this year was \$674 thousand compared to \$651 thousand last year.

As shown in the statement of Activities and Net Assets, the amount taxpayers ultimately financed for these activities was only \$483 thousand, due to costs paid by those directly benefited from the programs (\$16,000) or by other governments, organizations that subsidized certain programs with grants, contributions and restricted interest (\$134,000) and by a capital grant received (\$41,000).

| Changes in Cash Basis Net Assets of Business Type Activities (Expressed in Thousands) | | |
|--|----------------------------|-------------|
| | <u>Year ended June 30,</u> | |
| | <u>2007</u> | <u>2006</u> |
| Operating receipts | | |
| Charges for service | 134 | 118 |
| Special assessments | 2 | 1 |
| Miscellaneous | <u>12</u> | <u>2</u> |
| | 148 | 121 |
| Operating disbursements | | |
| Sewer | 52 | 62 |
| Garbage | <u>31</u> | <u>29</u> |
| | <u>83</u> | <u>91</u> |
| Excess (deficiency) of operating receipts over (under) operating disbursements | 65 | 30 |
| Nonoperating receipts (disbursements) and transfer | | |
| Debt Service | (26) | (34) |
| Transfers | <u>19</u> | <u>21</u> |
| | <u>(7)</u> | <u>(13)</u> |
| Net change in cash basis net assets | 58 | 17 |
| Cash basis net assets beginning of year | <u>77</u> | <u>60</u> |
| Cash basis net assets end of year | 135 | 77 |

Total business type activities receipts for the fiscal year were \$148 thousand compared to \$121 thousand last year. This increase was due primarily to an increase in sewer charges and being more strict with past due accounts to the Proprietary Fund. The cash balance increased by approximately \$58,000 from the prior year. Total disbursements for the fiscal year decreased due to recording actual hours worked versus a percentage of hours worked in each area and a new garbage contract.

INDIVIDUAL MAJOR GOVERNMENTAL FUND ANALYSIS

As the City of Underwood completed the year, its governmental funds reported a combined fund balance of \$450,163, an increase of \$116,697 above last year's total of \$333,466. The following are the major reasons for the changes in fund balances of the major funds from the prior year.

- The General Fund balance at the end of the year was \$156,789 an increase of \$39,589 from prior year.
- The Urban Renewal Tax Increment Fund balance at the end of the fiscal year was \$70,817 a decrease of \$26,319 from the previous year. The decrease was the result of the Low-Moderate Income Housing Assistance Program disbursed to qualified applicants.
- The Debt Service Fund cash balance was to \$5,508 an increase of \$3,729 from prior year.
- The Road Use Tax Fund balance at the end of the fiscal year was \$193,882 increase of \$78,531.
- The Local Option Sales Tax Fund at the end of the fiscal year was \$0.

INDIVIDUAL MAJOR BUSINESS TYPE FUND ANALYSIS

- The Sewer Fund balance increased by \$52,370 to \$128,662 due to a rate increase and the monthly contract with Peoples Services decreased due to only needing them for lab work.
- The Garbage Fund balance increased by \$5396 to \$6513.

BUDGETARY HIGHLIGHTS

Over the course of the year, the City budget was amended by \$181,000 for revenues and \$214,000 for disbursements. Revenues increased due to bond proceeds received and sale of equipment and for "transfer-in" that was not recorded in the original budget. Disbursements increased do to purchasing a new fire truck and a capital improvement project. Overall the City received \$236,000 less in revenues than budgeted due to grant awards anticipated, but not funded, TIF revenues and intergovernmental revenues were less than expected. However, the City disbursements were \$222,000 less than budgeted.

DEBT ADMINISTRATION

At June 30, 2007, the City had approximately \$521,000 in bonds and other long-term debt, compared to approximately \$447,000 last year as shown below:

Outstanding Debt at Year End
(Expressed in Thousands)

| | Year ended June 30, | |
|---|---------------------|------------|
| | 2007 | 2006 |
| General obligation notes and bonds | 470 | 345 |
| Urban renewal tax increment financing revenue bonds | 0 | 28 |
| Revenue Bonds | 51 | 74 |
| | <u>521</u> | <u>447</u> |
| Anticipatory warrants | 0 | 70 |

Debt increased as a result of issuing a GO Bond for a new fire truck.

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 and tax increment financing debt was \$460,000 at fiscal year end. The city has entered into tax increment financing rebate agreements for the purpose of residential economic development which principal balances totaled \$351,800 at fiscal year end. That debt, while not a general obligation of the City, is subject to the constitutional debt limit of the City. That, coupled with the debt of \$460,000 noted above, is below the City's constitutional debt limit of \$1.9 million.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES

The City of Underwood's elected and appointed officials and citizens considered many factors when setting the fiscal year 2008 budget, tax rates, and fees that will be charged for various City activities.

These indicators were taken into account when adopting the budget for fiscal year 2008. The operating budget for 2008 is \$681 thousand, a decrease of 40% under the final 2007 budget. Property tax rate will remain the same as last year. The regular taxable valuation increased 10.5% from \$15.6 million in 2007 to \$17.2 million in 2008. The tax rate for debt service stayed the same at \$3.5 per thousand of taxable valuation.

Budgeted disbursements are expected to decrease by approximately \$272,000 from 2007 due to capital improvement projects. No major programs were cut and no major new programs were added to the 2007 budget.

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 Kelly Groskurth, City Clerk, 218 Second Street, Underwood, Iowa.

City of Underwood
Basic Financial Statements

City of Underwood
Statement of Activities and Net Assets – Cash Basis
As of and for the year ended June 30, 2007

| | | Program Receipts | |
|------------------------------------|---------------|---------------------|--|
| | Disbursements | Charges for Service | Operating Grants Contributions and Restricted Interest |
| Functions/Programs: | | | |
| Governmental activities: | | | |
| Public safety | \$ 244,708 | 9,143 | 53,965 |
| Public works | 41,769 | - | 59,834 |
| Culture and recreation | 22,324 | 700 | - |
| Community and economic development | 123,243 | 3,324 | 7,202 |
| General government | 116,766 | 2,566 | 13,354 |
| Debt service | 96,850 | - | - |
| Capital projects | 28,072 | - | - |
| Total governmental activities | 673,732 | 15,733 | 134,355 |
| Business type activities: | | | |
| Sewer | 78,749 | 111,590 | - |
| Garbage | 31,108 | 36,504 | - |
| Total business type activities | 109,857 | 148,094 | - |
| Total | \$ 783,589 | 163,827 | 134,355 |

General Receipts:

Property tax levied for:
 General purposes
 Tax increment financing
 Debt service
Local option sales tax
Grants and contributions not restricted to specific purpose
Unrestricted interest on investments
Anticipatory warrants issued
Anticipatory warrants redeemed
Note proceeds
Sale of assets
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.

| Capital Grants Contributions and Restricted Interest | Net (Disbursement) Receipts and Changes in Cash Basis Net Assets | | |
|---|---|-----------------------------|------------------|
| | Governmental Activities | Business Type Activities | Total |
| - | (181,600) | - | (181,600) |
| - | 18,065 | - | 18,065 |
| - | (21,624) | - | (21,624) |
| - | (112,717) | - | (112,717) |
| - | (100,846) | - | (100,846) |
| - | (96,850) | - | (96,850) |
| 40,506 | 12,434 | - | 12,434 |
| <u>40,506</u> | <u>(483,138)</u> | <u>-</u> | <u>(483,138)</u> |
| - | - | 32,841 | 32,841 |
| - | - | 5,396 | 5,396 |
| - | - | <u>38,237</u> | <u>38,237</u> |
| <u>40,506</u> | <u>(483,138)</u> | <u>38,237</u> | <u>(444,901)</u> |
| \$ | 172,886 | - | 172,886 |
| | 112,347 | - | 112,347 |
| | 67,789 | - | 67,789 |
| | 76,249 | - | 76,249 |
| | 855 | - | 855 |
| | 12,346 | 467 | 12,813 |
| | 185,000 | - | 185,000 |
| | (254,575) | - | (254,575) |
| | 174,000 | - | 174,000 |
| | 72,000 | - | 72,000 |
| | <u>(19,062)</u> | <u>19,062</u> | <u>-</u> |
| | <u>599,835</u> | <u>19,529</u> | <u>619,364</u> |
| | 116,697 | 57,766 | 174,463 |
| | <u>333,466</u> | <u>77,409</u> | <u>410,875</u> |
| \$ | <u>450,163</u> | <u>135,175</u> | <u>585,338</u> |
| \$ | 193,882 | - | 193,882 |
| | 70,817 | - | 70,817 |
| | 5,508 | 21,207 | 26,715 |
| | 23,167 | - | 23,167 |
| | <u>156,789</u> | <u>113,968</u> | <u>270,757</u> |
| \$ | <u>450,163</u> | <u>135,175</u> | <u>585,338</u> |

City of Underwood
Statement of Cash Receipts, Disbursements
and Changes in Cash Balances - Governmental Funds
As of and for the year ended June 30, 2007

| | General | Special Revenue | | |
|--|-------------------|-----------------|-----------------------------|------------------------|
| | | Road Use Tax | Urban Renewal Tax Increment | Local Option Sales Tax |
| Receipts | | | | |
| Property tax | \$ 121,987 | - | - | - |
| Tax increment financing collections | - | - | 112,347 | - |
| Other city tax | 5,720 | - | - | 76,249 |
| Licenses and permits | 5,840 | - | - | - |
| Use of money and property | 12,346 | - | 512 | - |
| Intergovernmental | 54,820 | 59,834 | - | - |
| Charges for service | 9,893 | - | - | - |
| Miscellaneous | 13,354 | - | 6,690 | - |
| Total receipts | <u>223,960</u> | <u>59,834</u> | <u>119,549</u> | <u>76,249</u> |
| Disbursements | | | | |
| Operating: | | | | |
| Public safety | 244,708 | - | - | - |
| Public works | - | 37,127 | - | - |
| Culture and recreation | 18,966 | - | - | - |
| Community and economic development | 5,534 | - | 117,303 | - |
| General government | 80,467 | - | - | - |
| Debt service | - | - | 28,565 | - |
| Capital projects | - | - | - | - |
| Total disbursements | <u>349,675</u> | <u>37,127</u> | <u>145,868</u> | <u>-</u> |
| Excess (deficiency) of receipts over (under) disbursements | (125,715) | 22,707 | (26,319) | 76,249 |
| Other financing sources (uses): | | | | |
| Sale of capital assets | 72,000 | - | - | - |
| Note proceeds | 174,000 | - | - | - |
| Anticipatory warrants issued | 185,000 | - | - | - |
| Anticipatory warrants redeemed | (254,575) | - | - | - |
| Operating transfers in | - | 57,187 | - | - |
| Operating transfers out | (11,121) | (1,363) | - | (76,249) |
| Total other financing sources (uses) | <u>165,304</u> | <u>55,824</u> | <u>-</u> | <u>(76,249)</u> |
| Net change in cash balances | 39,589 | 78,531 | (26,319) | - |
| Cash balances beginning of year | <u>117,200</u> | <u>115,351</u> | <u>97,136</u> | <u>-</u> |
| Cash balances end of year | \$ <u>156,789</u> | <u>193,882</u> | <u>70,817</u> | <u>-</u> |
| Cash Basis Fund Balances | | | | |
| Reserved for debt service | \$ - | - | - | - |
| Unreserved: | | | | |
| General fund | 156,789 | - | - | - |
| Special revenue funds | - | 193,882 | 70,817 | - |
| Total cash basis fund balances | \$ <u>156,789</u> | <u>193,882</u> | <u>70,817</u> | <u>-</u> |

See notes to financial statements.

Exhibit B

| Debt Service | Other Nonmajor Governmental Funds | Total |
|-----------------|--|----------------|
| 65,910 | 43,644 | 231,541 |
| - | - | 112,347 |
| 1,879 | 1,535 | 85,383 |
| - | - | 5,840 |
| - | - | 12,858 |
| - | 40,006 | 154,660 |
| - | - | 9,893 |
| - | 500 | 20,544 |
| <u>67,789</u> | <u>85,685</u> | <u>633,066</u> |
| - | - | 244,708 |
| - | 4,642 | 41,769 |
| - | 3,358 | 22,324 |
| - | 406 | 123,243 |
| - | 36,299 | 116,766 |
| 68,285 | - | 96,850 |
| - | 28,072 | 28,072 |
| <u>68,285</u> | <u>72,777</u> | <u>673,732</u> |
| (496) | 12,908 | (40,666) |
| - | - | 72,000 |
| - | - | 174,000 |
| - | - | 185,000 |
| - | - | (254,575) |
| 4,225 | 8,259 | 69,671 |
| - | - | (88,733) |
| <u>4,225</u> | <u>8,259</u> | <u>157,363</u> |
| 3,729 | 21,167 | 116,697 |
| <u>1,779</u> | <u>2,000</u> | <u>333,466</u> |
| <u>5,508</u> | <u>23,167</u> | <u>450,163</u> |
| 5,508 | - | 5,508 |
| - | - | 156,789 |
| <u>-</u> | <u>23,167</u> | <u>287,866</u> |
| <u>5,508</u> | <u>23,167</u> | <u>450,163</u> |

City of Underwood
 Reconciliation of the Statement of Cash
 Receipts, Disbursements and Changes in Cash Balances
 to the Statement of Activities and Net Assets -
 Governmental Funds
 As of and for the year ended June 30, 2007

| | | |
|--|----|---------|
| Total governmental funds cash balances | \$ | 450,163 |
| <i>Adjustments</i> | | |
| None | | - |
| Cash basis net assets of governmental activities | \$ | 450,163 |
| | | |
| Net change in cash balances | \$ | 116,697 |
| <i>Adjustments</i> | | |
| None | | - |
| Change in cash balance of governmental activities | \$ | 116,697 |

See notes to financial statements.

City of Underwood
Statement of Cash Receipts, Disbursements and Changes in Cash Balances
Proprietary Funds
As of and for the year ended June 30, 2007

| | Enterprise Funds | | |
|---|------------------|---------|----------|
| | Sewer | Garbage | Total |
| Operating receipts: | | | |
| Charges for service | \$ 97,679 | 36,056 | 133,735 |
| Special assessment | 1,455 | 448 | 1,903 |
| Miscellaneous | 12,456 | - | 12,456 |
| Total operating receipts | 111,590 | 36,504 | 148,094 |
| Operating disbursements: | | | |
| Business type activities | 52,580 | 31,108 | 83,688 |
| Total operating disbursements | 52,580 | 31,108 | 83,688 |
| Excess of operating receipts over operating disbursements | 59,010 | 5,396 | 64,406 |
| Non-operating receipts (disbursements): | | | |
| Interest on investments | 467 | - | 467 |
| Debt service | (26,169) | - | (26,169) |
| Total non-operating receipts (disbursements) | (25,702) | - | (25,702) |
| Excess of receipts over disbursements | 33,308 | 5,396 | 38,704 |
| Operating transfers in | 19,062 | - | 19,062 |
| Net change in cash balances | 52,370 | 5,396 | 57,766 |
| Cash balances beginning of year | 76,292 | 1,117 | 77,409 |
| Cash balances end of year | \$ 128,662 | 6,513 | 135,175 |
| Cash Basis Fund Balances | | | |
| Reserved for debt service | \$ 21,207 | - | 21,207 |
| Unreserved | 107,455 | 6,513 | 113,968 |
| Total cash basis fund balances | \$ 128,662 | 6,513 | 135,175 |

See notes to financial statements.

City of Underwood
 Reconciliation of the Statement of Cash Receipts, Disbursements
 and Changes in Cash Balances
 to the Statement of Activities and Net Assets –
 Proprietary Funds
 As of and for the year ended June 30, 2007

| | | |
|---|----|---------|
| Total enterprise funds cash balances | \$ | 135,175 |
| <i>Adjustments</i> | | |
| None | | - |
| Cash basis net assets of business type activities | \$ | 135,175 |
| | | |
| Net change in cash balances | \$ | 57,766 |
| <i>Adjustments</i> | | |
| None | | - |
| Change in cash balance of business type activities | \$ | 57,766 |

See notes to financial statements.

City of Underwood
Notes to Financial Statements
June 30, 2007

NOTE (1) Summary of Significant Accounting Policies

The City of Underwood is a political subdivision of the State of Iowa located in Pottawattamie County. It was first incorporated in 1882 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 sewer and garbage utilities for its citizens.

A. Reporting Entity

For financial reporting purposes, the City of Underwood 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 following boards and commissions: Pottawattamie County Assessor's Conference Board, City Assessor's Conference Board and Pottawattamie County Emergency Management Commission.

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 Underwood
Notes to Financial Statements
June 30, 2007

NOTE (1) Summary of Significant Accounting Policies - Continued

B. Basis of Presentation - 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 charges and the capital improvement costs that are not paid from other funds.

Special Revenue:

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

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

City of Underwood
Notes to Financial Statements
June 30, 2007

NOTE (1) Summary of Significant Accounting Policies - Continued

B. Basis of Presentation – Continued

Special Revenue - Continued:

The Local Option Sales Tax Fund is used to account for the receipts from the tax authorized by referendum and used for the relief of property taxes and utility charges.

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

The City reports the following major proprietary funds:

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

The Garbage Fund accounts for the operation of the City's solid waste disposal.

C. Measurement Focus and Basis of Accounting

The City of Underwood 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, 2007, disbursements did not exceed the amounts budgeted.

City of Underwood
Notes to Financial Statements
June 30, 2007

NOTE (1) Summary of Significant Accounting Policies - Continued

E. Property Tax Calendar

The City's property tax rates were extended against the assessed valuation of the City as of January 1, 2005, to compute the amounts which became liens on property on July 1, 2006. These taxes were due and payable in two installments on September 30, 2006 and March 31, 2007, at the Pottawattamie County Treasurer's Office. These taxes are recognized as income to the City when they are received from the county.

NOTE (2) Cash and Pooled Investments

The City's deposits in banks at June 30, 2007 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 cash, which consists of cash in bank and certificates of deposit, totaled \$585,338.

NOTE (3) Bonds and Notes Payable

Annual debt service requirements to maturity of general obligation bonds and revenue notes are as follows:

| Year Ended June 30, | <u>General Obligation Bonds</u> | | <u>Revenue Notes</u> | | <u>Total</u> | |
|------------------------|---------------------------------|-----------------|----------------------|-----------------|------------------|-----------------|
| | <u>Principal</u> | <u>Interest</u> | <u>Principal</u> | <u>Interest</u> | <u>Principal</u> | <u>Interest</u> |
| 2008 | \$ 72,982 | 20,127 | 16,323 | 1,923 | 89,305 | 22,050 |
| 2009 | 76,361 | 17,155 | 16,999 | 1,247 | 93,360 | 18,402 |
| 2010 | 80,100 | 13,784 | 17,807 | 439 | 97,907 | 14,223 |
| 2011 | 65,962 | 10,248 | - | - | 65,962 | 10,248 |
| 2012 | 57,921 | 7,491 | - | - | 57,921 | 7,491 |
| 2013 | 116,587 | 10,598 | - | - | 116,587 | 10,598 |
| Total | \$ <u>469,913</u> | <u>79,403</u> | <u>51,129</u> | <u>3,609</u> | <u>521,042</u> | <u>83,012</u> |

Interest costs paid during the year ended June 30, 2007 totaled \$22,670.

The Code of Iowa requires that principal and interest on general obligation bonds be paid from the Debt Service Fund.

City of Underwood
Notes to Financial Statements
June 30, 2007

NOTE (3) Bonds and Notes Payable - Continued

The City has a general obligation debt limit of approximately \$1,900,000 which was not exceeded during the year ended June 30, 2007.

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

- a) The notes will only be redeemed from the future earnings of the sewer enterprise activity, and the note holders hold a lien on the future earnings of the fund.
- b) Sufficient monthly transfers shall be made to the sewer revenue note sinking account for the purpose of making the note principal and interest payments when due.

The City has complied with the provisions of the resolution.

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 3.7% of their annual salary and the City is required to contribute 5.75% of annual covered payroll. Contribution requirements are established by State statute. The City's contribution to IPERS for the years ended June 30, 2007, 2006, and 2005, was \$4,851, \$4,132, and \$4,877, respectively, equal to the required contributions for each year.

NOTE (5) Anticipatory Warrants

Anticipatory warrants are warrants which are legally drawn on City funds but are not paid for lack of funds, in accordance with Chapter 74 of the Code of Iowa. The warrants bear interest at rates in effect at the time the warrants are first presented for redemption.

The City issued \$185,000 in anticipatory warrants, at 3.95% interest per annum, for purchase of a fire truck. During the year ended June 30, 2007, the City redeemed \$254,575 in anticipatory warrants leaving no warrants outstanding.

City of Underwood
Notes to Financial Statements
June 30, 2007

NOTE (6) 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 approximate liability for earned vacation and comp time termination payments payable to employees at June 30, 2007, primarily relating to the General Fund is \$654. This liability is computed on rates of pay effective as of June 30, 2007.

NOTE (7) Interfund Transfers

The detail of interfund transfers for the year ended June 30, 2007 is as follows:

| Transfer to | Transfer from | Amount |
|----------------------------------|--|------------------|
| Special Revenue: Road Use Tax | Special Revenue: Local Option Sales Tax | \$ 57,187 |
| Special Revenue: Insurance | General | 4,876 |
| Debt Service | General | 4,225 |
| Capital Projects | General | 2,020 |
| | Special Revenue: Road Use Tax | 1,363 |
| Proprietary: Sewer | Special Revenue: Local Option Sales Tax | <u>19,062</u> |
| | | <u>\$ 88,733</u> |

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

NOTE (8) Related Party Transactions

The City has two urban renewal tax increment financing development rebate agreements with a City Council member. See Note 10 – McKee Development Agreements.

City of Underwood
Notes to Financial Statements
June 30, 2007

NOTE (9) Risk Management

The City is a member in the Iowa Communities Assurance Pool, as allowed by Chapter 670.7 of the Code of Iowa. The Iowa Communities Assurance Pool (Pool) is a local government risk-sharing pool whose 556 members include various governmental entities throughout the State of Iowa. The Pool was formed in August 1986 for the purpose of managing and funding third-party liability claims against its members. The Pool provides coverage and protection in the following categories: general liability, automobile liability, automobile physical damage, public officials' liability, police professional liability, property, inland marine, and boiler/machinery. There have been no reductions in insurance coverage from prior years.

Each member's annual casualty contributions to the Pool fund current operations and provide capital. Annual operating contributions are those amounts necessary to fund, on a cash basis, the Pool's general and administrative expenses, claims, claims expenses and reinsurance expenses due and payable in the current year, plus all or any portion of any deficiency in capital. Capital contributions are made during the first six years of membership and are maintained to equal 300 percent of the total current members' basis rates or to comply with the requirements of any applicable regulatory authority having jurisdiction over the Pool.

The Pool also provides property coverage. Members who elect such coverage make annual operating contributions which are necessary to fund, on a cash basis, the Pool's general and administrative expenses and reinsurance premiums, all of which are due and payable in the current year, plus all or any portion of any deficiency in capital. Any year-end operating surplus is transferred to capital. Deficiencies in operations are offset by transfers from capital and, if insufficient, by the subsequent year's member contributions.

The City's property and casualty contributions to the risk pool are recorded as disbursements from its operating funds at the time of payment to the risk pool. The City's annual contributions to the Pool for the year ended June 30, 2007 were \$18,749.

The Pool uses reinsurance and excess risk-sharing agreements to reduce its exposure to large losses. The Pool retains general, automobile, police professional, and public officials' liability risks up to \$350,000 per claim. Claims exceeding \$350,000 are reinsured in an amount not to exceed \$2,650,000 per claim and \$5,000,000 in aggregate per year. For members requiring specific coverage from \$3,000,000 to \$10,000,000, such excess coverage is also reinsured. Property and automobile physical damage risks are retained by the Pool up to \$100,000 each accident, each location, with excess coverage reinsured on an individual member basis.

City of Underwood
Notes to Financial Statements
June 30, 2007

NOTE (9) Risk Management - Continued

The Pool's intergovernmental contract with its members provides that in the event a casualty claim or series of claims exceeds the amount of risk-sharing protection provided by the member's risk-sharing certificate, or in the event that a series of casualty claims exhausts total members' equity plus any reinsurance and any excess risk-sharing recoveries, then payment of such claims shall be the obligation of the respective individual member. As of June 30, 2007, settled claims have not exceeded the risk pool or reinsurance company coverage since the Pool's inception.

Members agree to continue membership in the Pool for a period of not less than one full year. After such period, a member who has given 60 days' prior written notice may withdraw from the Pool. Upon withdrawal, payments for all claims and claims expenses become the sole responsibility of the withdrawing member, regardless of whether a claim was incurred or reported prior to the member's withdrawal. Members withdrawing within the first six years of membership may receive a partial refund of their capital contributions. If a member withdraws after the sixth year, the member is refunded 100 percent of its capital contributions. However, the refund is reduced by an amount equal to the annual operating contribution which the withdrawing member would have made for the one-year period following withdrawal.

The City also carries workmen's compensation insurance purchased from Iowa Municipal Workers Compensation Association. The City assumes liability for any deductions, and claims in excess of coverage limitations. Settled claims resulting from these risks have not exceeded commercial insurance coverage in any of the past three fiscal years.

NOTE (10) Urban Renewal Tax Increment Financing Development Agreements

McKee Development Agreements

On February 8, 2000, the City entered into an agreement with McKee Contracting. The developer agreed to provide improvements to certain property within the City's Urban Renewal South Area for the purpose of constructing housing units. In exchange, the City agreed to make urban renewal increment tax payments to the Developer semi-annually of eligible costs of approximately \$28,000. If tax increment financing collections are available, these payments will be made December 1 and June 1 of each fiscal year, beginning December 1, 2002 and continue for nine fiscal years or until the total has been paid. The City shall retain 42.82% of the urban renewal tax increment revenue for the purpose of providing assistance to low and moderate income families, and pay the remaining 57.18% to the developer. The City paid \$8,273 of principal during the year on the agreement.

City of Underwood
Notes to Financial Statements
June 30, 2007

NOTE (10) Urban Renewal Tax Increment Financing Development Agreements - Continued

McKee Development Agreements - Continued

On December 10, 2003, the City entered into an agreement with McKee Contracting. The developer agreed to provide improvements to certain property within the City's Field Crest Urban Renewal Area for the purpose of constructing housing units. The total costs to be incurred on the project over a period of 16 years, are to be approximately \$1,688,339. In exchange, the City agreed to make urban renewal increment tax payments to the developer semi-annually. If tax increment financing collections are available, these payments will be made December 1 and June 1 of each fiscal year, beginning on the first December 1 for which incremental tax revenues become available with respect to each Phase of the development, and continuing for a total of ten years for each of the Phases. There are six Phases of construction from the years 2004 through 2020. The City paid the developer \$9,772 of principal during the year.

HLH Development Agreement

On January 9, 2001, the City entered into an agreement with HLH Development, L.C. The developer agreed to provide improvements to certain property within the City's Urban Renewal South Area legally described as Eagle Landing for the purpose of constructing housing units. In exchange, the City agreed to make urban renewal tax increment payments to the Developer semi-annually of eligible costs of approximately \$300,785 plus interest of 6% per annum calculated from December 1, 2000. If tax increment financing collections are available, these payments will be made December 1 and June 1 of each fiscal year, beginning December 1, 2003 and continue for nine fiscal years or until the total has been paid. The City shall retain 20% of urban renewal tax increment revenue for the purpose of providing assistance to low and moderate income families and pay the remaining 80% to the developer. The City paid the developer \$45,422 for interest costs during the year.

NOTE (11) Commitments

The City has entered into an agreement for law enforcement services. The fee for the fiscal year ending June 30, 2008 is \$12,040.

The City has signed an agreement for solid waste collection services through March 2010 at a cost of \$9.50 per month per household or commercial unit, to be increased by \$.25 in April 2008 and again in 2010 by an economic factor while negotiating the contract.

In June 2007, the City signed a contract for a street improvement project for \$65,416.

NOTE (12) Subsequent Event

In July 2007, the City approved a street overlay project for \$41,280.

Required Supplementary Information

City of Underwood
 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, 2007

| | Governmental Funds <u>Actual</u> | Proprietary Funds <u>Actual</u> | <u>Actual</u> |
|---|--|---------------------------------------|----------------|
| Receipts | | | |
| Property tax | \$ 231,541 | - | 231,541 |
| Tax increment financing collections | 112,347 | - | 112,347 |
| Other city tax | 85,383 | - | 85,383 |
| Licenses and permits | 5,840 | - | 5,840 |
| Use of money and property | 12,858 | 467 | 13,325 |
| Intergovernmental | 154,660 | - | 154,660 |
| Charges for service | 9,893 | 133,735 | 143,628 |
| Special assessments | - | 1,903 | 1,903 |
| Miscellaneous | 20,544 | 12,456 | 33,000 |
| Total receipts | <u>633,066</u> | <u>148,561</u> | <u>781,627</u> |
| Disbursements | | | |
| Public safety | 244,708 | - | 244,708 |
| Public works | 41,769 | - | 41,769 |
| Culture and recreation | 22,324 | - | 22,324 |
| Community and economic development | 123,243 | - | 123,243 |
| General government | 116,766 | - | 116,766 |
| Debt service | 96,850 | - | 96,850 |
| Capital projects | 28,072 | - | 28,072 |
| Business type activities | - | 109,857 | 109,857 |
| Total disbursements | <u>673,732</u> | <u>109,857</u> | <u>783,589</u> |
| Excess (deficiency) of receipts over (under) disbursements | (40,666) | 38,704 | (1,962) |
| Other financing sources, net | <u>157,363</u> | <u>19,062</u> | <u>176,425</u> |
| Excess (deficiency) of receipts and other financing sources over (under) disbursements and other financing uses | 116,697 | 57,766 | 174,463 |
| Balances beginning of year | <u>333,466</u> | <u>77,409</u> | <u>410,875</u> |
| Balances end of year | <u>\$ 450,163</u> | <u>135,175</u> | <u>585,338</u> |

See accompanying independent auditors' report.

| Original Budgeted Amounts | Final Budgeted Amounts | Budget to Actual Variance |
|---------------------------------|------------------------------|---------------------------------|
| 232,821 | 232,821 | (1,280) |
| 167,400 | 167,400 | (55,053) |
| 81,796 | 81,796 | 3,587 |
| 7,465 | 7,465 | (1,625) |
| 2,126 | 2,126 | (11,199) |
| 128,202 | 172,202 | (17,542) |
| 135,965 | 135,965 | 7,663 |
| - | - | 1,903 |
| - | - | 33,000 |
| 755,775 | 799,775 | (18,148) |
| 237,040 | 252,040 | 7,332 |
| 70,849 | 70,849 | 29,080 |
| 35,090 | 35,090 | 12,766 |
| 176,267 | 176,267 | 53,024 |
| 128,380 | 128,380 | 11,614 |
| 183,290 | 205,290 | 108,440 |
| 31,993 | 71,993 | 43,921 |
| 121,399 | 121,399 | 11,542 |
| 984,308 | 1,061,308 | 277,719 |
| (228,533) | (261,533) | 259,571 |
| 252,000 | 252,000 | (75,575) |
| 23,467 | (9,533) | 183,996 |
| 350,818 | 350,818 | 60,057 |
| 374,285 | 341,285 | 244,053 |

City of Underwood
Notes to Required Supplementary Information – Budgetary Reporting
June 30, 2007

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 Internal Service Funds and Fiduciary Funds. The annual budget may be amended during the year utilizing similar statutorily prescribed procedures.

Formal and legal budgetary control is based upon major classes of disbursements known as functions, not by fund or fund type. These functions are: public safety, public works, health and social services, culture and recreation, community and economic development, general government, debt service, capital projects and business type activities. Function disbursements required to be budgeted include disbursements for the General Fund, Special Revenue Funds, Debt Service Fund, Capital Projects Funds and Proprietary Funds. Although the budget document presents function disbursements by fund, the legal level of control is at the aggregated function level, not by fund. During the year, one budget amendment increased budgeted disbursements by \$77,000. The budget amendment is reflected in the final budgeted amounts.

During the year ended June 30, 2007, disbursements did not exceed the amended amounts budgeted.

Other Supplementary Information

City of Underwood
 Statement of Cash Receipts, Disbursements
 and Changes in Cash Balances
 Nonmajor Governmental Funds
 As of and for the year ended June 30, 2007

| | Special Revenue | | | Capital Projects | Total |
|---|-----------------|----------------------|-----------|---------------------|--------|
| | Emergency | Employee Benefits | Insurance | | |
| Receipts: | | | | | |
| Property tax | \$ 4,065 | 24,428 | 15,151 | - | 43,644 |
| Other city tax | 143 | 859 | 533 | - | 1,535 |
| Intergovernmental | - | - | - | 40,006 | 40,006 |
| Miscellaneous | - | - | - | 500 | 500 |
| Total receipts | 4,208 | 25,287 | 15,684 | 40,506 | 85,685 |
| Disbursements: | | | | | |
| Operating: | | | | | |
| Public works | - | 4,642 | - | - | 4,642 |
| Culture and recreation | - | 3,358 | - | - | 3,358 |
| Community and economic development | - | 406 | - | - | 406 |
| General government | - | 17,550 | 18,749 | - | 36,299 |
| Capital projects | - | - | - | 28,072 | 28,072 |
| Total disbursements | - | 25,956 | 18,749 | 28,072 | 72,777 |
| Excess (deficiency) of receipts over (under) disbursements | 4,208 | (669) | (3,065) | 12,434 | 12,908 |
| Other financing sources: | | | | | |
| Operating transfers in | - | - | 4,876 | 3,383 | 8,259 |
| Net change in cash balances | 4,208 | (669) | 1,811 | 15,817 | 21,167 |
| Cash balances beginning of year | 3,922 | 13,895 | - | (15,817) | 2,000 |
| Cash balances end of year | \$ 8,130 | 13,226 | 1,811 | - | 23,167 |
| Cash Basis Fund Balances | | | | | |
| Unreserved: | | | | | |
| Special revenue funds | \$ 8,130 | 13,226 | 1,811 | - | 23,167 |
| Total cash basis fund balances | \$ 8,130 | 13,226 | 1,811 | - | 23,167 |

See accompanying independent auditors' report.

City of Underwood
Schedule of Indebtedness
Year ended June 30, 2007

| Obligation | Date of Issue | Interest Rates | Amount Originally Issued |
|---|------------------|-------------------|--------------------------------|
| General obligation bonds: | | | |
| Street improvements | Nov 20, 2001 | 4.75 % | \$ 170,000 |
| Special services truck | Feb 28, 2003 | 4.27 % | 100,000 |
| Street improvements | Jun 16, 2003 | 3.86 % | 150,000 |
| Street improvements | Feb 24, 2006 | 3.95% | 75,000 |
| Fire truck | Jun 21, 2007 | 4.90 % | 174,000 |
| | | | |
| Urban renewal tax increment financing (TIF) revenue bonds: | | | |
| South district | Jun 24, 2002 | 3.95 % | \$ 110,000 |
| | | | |
| Revenue notes: | | | |
| Sewer improvement | Oct 15, 1999 | 5.25 % | \$ 92,000 |
| Sewer improvement | Feb 28, 2003 | 4.10 % | 110,000 |
| | | | |
| Anticipatory warrants: | | | |
| Fire truck | Varies | 3.95% | \$ 260,000 |

See accompanying independent auditors' report.

Schedule 2

| <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> |
|--|-----------------------------------|-------------------------------------|------------------------------------|--------------------------|--|
| 103,308 | - | 16,894 | 86,414 | 4,709 | - |
| 69,238 | - | 4,570 | 64,668 | 1,585 | - |
| 110,875 | - | 14,044 | 96,831 | 4,180 | - |
| 62,000 | - | 14,000 | 48,000 | 2,473 | - |
| <u>-</u> | <u>174,000</u> | <u>-</u> | <u>174,000</u> | <u>-</u> | <u>-</u> |
| <u>345,421</u> | <u>174,000</u> | <u>49,508</u> | <u>469,913</u> | <u>12,947</u> | <u>-</u> |
| | | | | | |
| <u>27,500</u> | <u>-</u> | <u>27,500</u> | <u>-</u> | <u>1,065</u> | <u>-</u> |
| | | | | | |
| 7,719 | - | 7,719 | - | 203 | - |
| 66,752 | - | 15,623 | 51,129 | 2,623 | - |
| <u>74,471</u> | <u>-</u> | <u>23,342</u> | <u>51,129</u> | <u>2,826</u> | <u>-</u> |
| | | | | | |
| <u>69,575</u> | <u>185,000</u> | <u>254,575</u> | <u>-</u> | <u>5,832</u> | <u>-</u> |

City of Underwood
Bond and Note Maturities
June 30, 2007

| Year Ending June 30, | General Obligation | | | | | |
|-------------------------|---|------------------|------------------------------------|------------------|---|------------------|
| | Street Improvements Issued Nov. 20, 2001 | | Rescue Unit Issued Feb 28, 2003 | | Street Improvements Issued Jun. 16, 2003 | |
| | Interest Rate | Amount | Interest Rate | Amount | Interest Rate | Amount |
| 2008 | 4.75% | \$ 17,705 | 4.27% | \$ 9,656 | 3.86% | \$ 14,628 |
| 2009 | 4.75% | 18,556 | 4.27% | 10,073 | 3.86% | 15,198 |
| 2010 | 4.75% | 19,448 | 4.27% | 10,507 | 3.86% | 15,790 |
| 2011 | 4.75% | 20,382 | 4.27% | 10,960 | 3.86% | 16,405 |
| 2012 | 4.75% | 10,323 | 4.27% | 11,434 | 3.86% | 17,045 |
| 2013 | - | - | - | 12,038 | 3.86% | 17,765 |
| 2014 | - | - | - | - | - | - |
| 2015 | - | - | - | - | - | - |
| 2016 | - | - | - | - | - | - |
| Total | | \$ 86,414 | | \$ 64,668 | | \$ 96,831 |

See accompanying independent auditors' report.

Schedule 3

| Bonds | | | Revenue Notes | | | |
|---|------------------|-----------------------------------|----------------------|------------------------------|------------------|------------------|
| Street Improvements Issued Feb. 24, 2006 | | Fire Truck Issued Jun 21, 2007 | | Sewer Issued Feb 28, 2003 | | |
| Interest Rate | Amount | Interest Rate | Amount | Total | Interest Rate | Amount |
| 3.95% | \$ 15,000 | 4.90 % | \$ 15,993 | \$ 72,982 | 4.10 % | \$ 16,323 |
| 3.95% | 16,000 | 4.90 % | 16,534 | 76,361 | 4.10 % | 16,999 |
| 3.95% | 17,000 | 4.90 % | 17,355 | 80,100 | 4.10 % | 17,757 |
| - | - | 4.90 % | 18,215 | 65,962 | - | - |
| - | - | 4.90 % | 19,119 | 57,921 | - | - |
| - | - | 4.90 % | 20,067 | 49,870 | - | - |
| - | - | 4.90 % | 21,062 | 21,062 | - | - |
| - | - | 4.90 % | 22,107 | 22,107 | - | - |
| - | - | 4.90 % | 23,548 | 23,548 | - | - |
| | <u>\$ 48,000</u> | | <u>\$ 174,000</u> | <u>\$ 469,913</u> | | <u>\$ 51,079</u> |

City of Underwood
 Schedule of Receipts By Source and Disbursements By Function -
 All Governmental Funds
 For the Last Four Years

| | <u>2007</u> | <u>2006</u> | <u>2005</u> | <u>2004</u> |
|-------------------------------------|-------------------|----------------|----------------|----------------|
| Receipts | | | | |
| Property tax | \$ 231,541 | 212,017 | 205,970 | 150,760 |
| Tax increment financing collections | 112,347 | 76,287 | 98,565 | 215,569 |
| Other city tax | 85,383 | 90,562 | 76,458 | 76,087 |
| Licenses and permits | 5,840 | 7,936 | 8,683 | 6,022 |
| Use of money and property | 12,858 | 3,378 | 1,252 | 989 |
| Intergovernmental | 154,660 | 129,724 | 148,400 | 122,607 |
| Charges for service | 9,893 | 15,763 | 37,616 | 40,562 |
| Special assessments | - | 15 | 168 | - |
| Miscellaneous | <u>20,544</u> | <u>28,412</u> | <u>10,762</u> | <u>64,361</u> |
| Total | <u>\$ 633,066</u> | <u>564,094</u> | <u>587,874</u> | <u>676,957</u> |
| Disbursements | | | | |
| Operating: | | | | |
| Public safety | \$ 244,708 | 165,080 | 80,432 | 40,519 |
| Public works | 41,769 | 61,710 | 96,443 | 105,362 |
| Health and social services | - | - | 650 | 650 |
| Culture and recreation | 22,324 | 12,380 | 23,735 | 48,998 |
| Community and economic development | 123,243 | 107,790 | 97,029 | 141,126 |
| General government | 116,766 | 126,730 | 112,466 | 116,604 |
| Debt service | 96,850 | 91,668 | 125,109 | 161,316 |
| Capital projects | <u>28,072</u> | <u>85,151</u> | <u>-</u> | <u>-</u> |
| Total | <u>\$ 673,732</u> | <u>650,509</u> | <u>535,864</u> | <u>614,575</u> |

See accompanying independent auditors' report.

City of Underwood

November 7, 2007

Independent Auditors' 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:

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 Underwood, Iowa, as of and for the year ended June 30, 2007, which collectively comprise the City's basic financial statements listed in the table of contents and have issued our report thereon dated November 7, 2007. Our report expressed unqualified opinions 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 Underwood's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing our opinion on the effectiveness of City of Underwood's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of City of Underwood's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed below, we identified control deficiencies in internal control over financial reporting that we consider to be significant deficiencies and other deficiencies we consider to be material weaknesses.

Continued...

City of Underwood
Independent Auditors' Report on
Internal Control and Compliance and Other Matters

A control deficiency exists when the design or operation of the control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects City of Underwood's ability to initiate, authorize, record, process, or report financial data reliably in accordance with an other comprehensive basis of accounting such that there is more than a remote likelihood a misstatement of City of Underwood's financial statements that is more than inconsequential will not be prevented or detected by City of Underwood's internal control. We consider the deficiency in internal control described in Part I of the accompanying Schedule of Findings to be a significant deficiency in internal control over financial reporting.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood a material misstatement of the financial statements will not be prevented or detected by City of Underwood's internal control.

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, we believe the significant deficiency described above is a material weakness.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the City of Underwood'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, 2007 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.

City of Underwood's responses to findings identified in our audit are described in the accompanying Schedule of Findings. While we have expressed our conclusions on the City's responses, we did not audit City of Underwood's responses and, accordingly, we express no opinion on them.

City of Underwood
Independent Auditors' Report on
Internal Control and Compliance and Other Matters

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

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

City of Underwood
Schedule of Findings
Year Ended June 30, 2007

Part I: Findings Related to the Financial Statements:

SIGNIFICANT DEFICIENCIES:

I-A-07 Segregation of Duties

Comment – One important aspect of internal control is the segregation of duties among employees to prevent an individual employee from handling duties which are incompatible. The cash receipts listing, bank deposits, posting of the cash receipts to the cash receipts journal, reconciling and reporting, are at times all done by the same person.

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 – The City Treasurer does a monthly review of the bank statements, bank reconciliations, and general history detail.

Conclusion – Response accepted.

INSTANCES OF NON-COMPLIANCE:

No matters were reported.

City of Underwood
Schedule of Findings
Year Ended June 30, 2007

Part II: Other Findings Related to Statutory Reporting:

II-A-07 Certified Budget

Disbursements during the year ended June 30, 2007 did not exceed the amended budgeted amounts.

II-B-07 Entertainment Expense

We noted no disbursements for parties, banquets or other entertainment for employees that we believe may constitute an unlawful expenditure from public funds as defined in an Attorney General's opinion dated April 25, 1979.

II-C-07 Travel Expense

No disbursements of City money for travel expenses of spouses of City officials or employees were noted.

II-D-07 Business Transactions

Comment - Business transactions between the City and City officials or employees are detailed.

| <u>Name, Title and Business Connection</u> | <u>Transaction Description</u> | <u>Amount</u> |
|--|--------------------------------|---------------|
| Craig Zenor, Mayor | Contract Services | \$ <u>160</u> |

In accordance with Chapter 362.5(10) of the Iowa Code, the above transactions with the Mayor and Council Members do not appear to represent a conflict of interest since the total transactions with the individuals did not exceed \$2,500 during the fiscal year.

The City also made principal payments of \$18,045 on urban renewal tax increment financing rebate agreements held with developer and Council Member Shawn McKee. Holding such agreements with a council member may represent a conflict of interest.

Recommendation – The City should seek legal advice on these matters.

Response – We will do this.

Conclusion – Response accepted.

City of Underwood
Schedule of Findings
Year Ended June 30, 2007

Part II: Other Findings Related to Statutory Reporting (Continued):

II-E-07 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.

II-F-07 Council Minutes

No transactions were found that we believe should have been approved in the Council minutes but were not.

II-G-07 Deposits and Investments

Comment – The City has not adopted a written investment policy.

Recommendation – The City should adopt a written investment policy that complies with the provisions of Chapter 12B.10B of the Code of Iowa.

Response – We will do this.

Conclusion – Response accepted.

II-H-07 Revenue Note

The City is in compliance with the provisions of the sewer revenue note resolution.

II-I-07 Excess Balances

Comment – The cash balances in the Special Revenue Fund, Road Use Tax Account and the Enterprise Fund, Sewer Account at June 30, 2007 were in excess of the disbursements made from each fund during the year.

Recommendation – The City should consider the necessity of maintaining the excess balances.

Response – The excess balances are considered necessary for the payment of future project costs.

Conclusion – Response accepted.

NEWS RELEASE

Schroer & Associates, P.C. today released an audit report on the City of Underwood, Iowa.

The City's receipts totaled \$1,212,627 for the year ended June 30, 2007, a 41 percent increase from 2006. The receipts included \$240,675 in property tax, \$112,347 from tax increment financing collections, \$163,827 from charges for service, \$134,355 from operating grants, contributions and restricted interest, \$40,506 from capital grants, contributions and restricted interest, \$76,249 from local option sales tax, \$12,813 from unrestricted investment earnings and \$72,000 from the sale of general fixed assets, \$174,000 in note proceeds and \$185,000 in anticipatory warrants, and \$855 for grants not restricted to a specific purpose.

Disbursements for the year totaled \$1,038,164, a 34 percent increase from the prior year, and included \$244,708 for public safety, \$116,766 for general government, and \$123,243 for community and economic development. Also, disbursements for business type activities totaled \$109,857 and \$254,575 in anticipatory warrants redeemed.

A copy of the audit report is available for review in the Office of Auditor of State and the City Clerk's office.

August 30, 2005

To the Honorable Mayor and
Members of the City Council
City of Underwood
218 Second Street – Box 40
Underwood, IA 51576

We have compiled the annual financial report of the City of Underwood for the year ended June 30, 2005, included in the accompanying prescribed form in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants.

Our compilation was limited to presenting in the form prescribed by the State of Iowa information that is the representation of management. We have not audited or reviewed the financial statements referred to above, and accordingly, do not express an opinion or any other form of assurance on them. These financial statements were compiled by us from financial statements for that same period that we previously audited, as indicated in our report dated August 30, 2005.

These financial statements are presented in accordance with the requirements of the State of Iowa, which differ from generally accepted accounting principles. Accordingly, these financial statements are not designed for those who are not informed about such differences.

November 7, 2007

Kelly
City of Underwood
P.O. Box 40
218 Second Street
Underwood, IA 51576

Dear Kelly:

Enclosed is a draft copy of the audit for the City of Underwood. Please review and let me know if we need to make any changes.

Also enclosed is the management representation letter needed for our file. Please sign and have the mayor sign and return to me in the envelope provided.

Sincerely,

SCHROER & ASSOCIATES, P.C.

Diane McGrain
Shareholder

DM/sh
Enc.

December 12, 2007

David Vaudt
Office of State Auditor
PO Box 333
Des Moines, IA 50302-0333

Dear Sir:

We have enclosed for your records the following information regarding the audit of the City of Underwood for the year ended June 30, 2007.

- 2 copies of the audit report
- 1 copy of the news release
- 1 copy of the number of hours worked
- 1 copy of the invoice

Sincerely,

SCHROER & ASSOCIATES, P.C.

Diane McGrain
Shareholder

DM/sh
Enc.

December 12, 2007

Kelly
City of Underwood
P.O. Box 40
218 Second Street
Underwood, IA 51576

Dear Kelly:

We have filed the required copies of your audit report with the Office of Auditor of State. A filing fee is required to be paid based on your final amended budget according to the following schedule:

| <u>Budgeted Expenditures (In millions of dollars)</u> | <u>Fee Amount</u> |
|---|-------------------|
| Under 1 | \$100.00 |
| At least 1, but less than 3 | \$175.00 |
| At least 3, but less than 5 | \$250.00 |
| At least 5, but less than 10 | \$425.00 |
| At least 10, but less than 25 | \$625.00 |
| 25 and over | \$850.00 |

You are required to send the appropriate filing fee. The check should be made payable to "Auditor of State" and mailed to Office of Auditor of State, PO Box 333, Des Moines, IA 50302-0333.

If you have any questions, please do not hesitate to call me at 712-322-8734.

Sincerely,

SCHROER & ASSOCIATES, P.C.

Diane McGrain
Shareholder

DM/sh

City of Underwood

Hours Worked: 47