

**Keokuk Municipal Water Works,  
A Component Unit of the City of Keokuk**

**Independent Auditor's Report  
Management's Discussion and Analysis  
Financial Statements and Supplemental Information  
Independent Auditor's Reports on Compliance and Internal Control  
Schedule of Findings**

**June 30, 2010**

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**Keokuk Municipal Water Works,  
A Component Unit of the City of Keokuk  
Board of Trustees  
June 30, 2010**

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<b><u>Trustee</u></b>	<b><u>Title</u></b>	<b><u>Term Expires</u></b>
Edward Johnstone	Trustee, Chairman	November 1, 2011
Mike Hausch	Trustee, Vice Chairman	November 1, 2011
Bruce Brandt	Trustee	November 1, 2013
John Beaird	Trustee	November 1, 2015
Dave Bogner	Trustee	November 1, 2015
Bill Cole	Manager	
Shari Dunagan	Office Manager	



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## Independent Auditor's Report

Board of Trustees  
Keokuk Municipal Water Works,  
A Component Unit of the City of Keokuk  
Keokuk, Iowa

We have audited the accompanying statement of net assets of the proprietary fund of the Keokuk Municipal Water Works (Water Works), a Component Unit of the City of Keokuk, as of June 30, 2010, and the related statement of revenues, expenses and changes in fund net assets and the statement of cash flows of its proprietary fund for the year then ended. These financial statements are the responsibility of the Water Works' management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As discussed in Note 1, the Water Works did not record or disclose the net annual required contribution for other postemployment benefits (OPEB) or the OPEB net liability obligation as required by Governmental Accounting Standards Board Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*.

In our opinion, except for the omission of the information described in the preceding paragraph, the financial statements referred to above present fairly, in all material respects, the financial position of the Water Works at June 30, 2010, and the changes in its net assets and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated November 16, 2010 on our consideration of the Water Works' internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grants, 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 internal controls over financial reporting or compliance. That report is an integral part of the audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Management's Discussion and Analysis information on pages 4 through 9 and budgetary comparison on pages 23 through 24 are not required as part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was made for the purpose of forming an opinion on the financial statements taken as a whole. The supplemental information included on pages 25 through 28 is presented for purposes of additional analysis and is not a required part of the basic financial statements. The accompanying Schedule of Expenditures of Federal Awards on Page 29 is presented for purposes of additional analysis as required by United States Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, 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 aforementioned financial statements and, in our opinion, is fairly stated in all material respects in relation to the aforementioned financial statements taken as a whole.

*CPA Associates PC*

November 16, 2010

**Keokuk Municipal Water Works,  
A Component Unit of the City of Keokuk  
Management's Discussion and Analysis**

The following Management Discussion and Analysis (MD&A) of the Keokuk Municipal Water Works' activities and financial performance provides the reader with an introduction and overview to the financial statements of the Keokuk Municipal Water Works (Water Works) for the fiscal year ended June 30, 2010. The information contained in this MD&A should be considered in conjunction with the Water Works' basic financial statements.

Following this MD&A are the basic financial statements of the Water Works together with the notes thereto which are essential to a full understanding of the data contained in the financial statements.

**Financial Operations Highlights**

As a result of this year's operations, assets exceeded liabilities by \$20.6 million (net assets) for the fiscal year reported. This compares to the previous year when assets exceeded liabilities by \$19.2 million. The net assets increased by \$1,252,125 or 6.5%.

Total net assets are comprised of the following:

- Net assets invested in capital assets (e.g., main extensions, buildings, improvements, and equipment), less the related indebtedness outstanding used to acquire those capital assets is \$18,465,590. This balance represents resources allocated to capital assets. These capital assets, less accumulated depreciation, are shown at depreciated cost of \$32,353,570.
- Restricted net assets of \$2,067,944 represent resources that are subject to external restrictions such as grantors, laws, debt covenants or regulations.
- Unrestricted net assets of \$115,733 represent resources that can be used at the discretion of management and the Board of Trustees.

During the year, revenues increased \$410,300, or 6.99%, while operating expenses increased \$304,400, or 5.93%. The increase in revenues is due to an increase in water usage and increase in water rates.

Net nonoperating expenses increased \$44,300 or 11.31% and are primarily attributable to the decrease in interest income.

The Water Works also recognized capital contributions of \$846,914 in the current year related to an EDA grant received for the water tower construction project.

**Using This Annual Report**

The Water Works is governed by a Board of Trustees, appointed by the Mayor and approved by the City Council. The Water Works is organized as an Enterprise Fund and is a component unit of the City of Keokuk, Iowa. This discussion and analysis is intended to serve as an introduction to the Water Works' basic financial statements. 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 Keokuk Municipal Water Works' financial activities.

**Keokuk Municipal Water Works,  
A Component Unit of the City of Keokuk  
Management's Discussion and Analysis**

**Using This Annual Report** (continued)

The Financial Statements consist of a Statement of Net Assets, Statement of Revenues, Expenses and Changes in Fund Net Assets, and Statement of Cash Flows. These provide information about the activities of the Water Works as a whole and present an overall view of the Water Works' finances.

The Financial Statements tell how services were financed in the short term as well as what remains for future spending.

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 Water Works' budget for the year.

**Financial Position Summary**

Net assets may serve over time as a useful indicator of the Water Works' financial position. The Water Works' net assets exceeded liabilities by \$20.6 million at June 30, 2010, an increase of \$1,252,125 from 2009.

A condensed summary of the Water Works' net assets at June 30, 2010 and 2009 is shown below:

	<b>2010</b>	<b>2009</b>
<b>Assets:</b>		
Current, restricted and other assets	\$ 4,889,778	\$ 5,915,954
Capital assets	<u>32,353,570</u>	<u>27,837,053</u>
Total assets	<u>\$ 37,243,348</u>	<u>\$ 33,753,007</u>
<b>Liabilities:</b>		
Current liabilities	\$ 3,656,101	\$ 2,160,865
Long-term debt	<u>12,937,980</u>	<u>12,195,000</u>
	16,594,081	14,355,865
<b>Net Assets:</b>		
Invested in capital assets, net of related debt	18,465,590	14,722,053
Restricted funds	2,067,944	2,041,040
Unrestricted	<u>115,733</u>	<u>2,634,049</u>
Total liabilities and net assets	<u>\$ 37,243,348</u>	<u>\$ 33,753,007</u>

The largest portion of the Water Works' net assets each year represents its investment in capital assets (e.g., main extensions, buildings, improvements, and equipment), less any related indebtedness outstanding used to acquire those capital assets.

**Keokuk Municipal Water Works,  
A Component Unit of the City of Keokuk  
Management's Discussion and Analysis**

**Summary of Operations and Changes in Net Assets**

	<b>2010</b>	<b>2009</b>
Net operating revenues	\$ 6,278,012	\$ 5,867,681
Net operating expenses	<u>5,436,931</u>	<u>5,132,482</u>
Net operating income	<u>841,081</u>	<u>735,199</u>
Nonoperating income and expenses:		
Interest income	107,695	181,061
Interest expense and amortization	<u>(543,565)</u>	<u>(572,683)</u>
Net nonoperating expense	<u>(435,870)</u>	<u>(391,622)</u>
Capital contributions	<u>846,914</u>	<u>-</u>
Increase in net assets	<u>\$ 1,252,125</u>	<u>\$ 343,577</u>

**Revenues**

A summary of revenues for the year ended June 30, 2010, and the amount and percentage of change in relation to prior year amounts, is as follows:

	<u>2010</u> <u>Amount</u>	<u>% of</u> <u>Total</u>	<u>Increase</u> <u>(Decrease)</u> <u>from Prior</u> <u>Year</u>	<u>% Increase</u> <u>(Decrease)</u>
Operating				
Metered sales	\$ 6,139,494	84.89	\$ 722,521	13.34
Flat rate sales	681	-	(1,313)	(65.85)
Miscellaneous charges	90,082	1.25	(32,176)	(26.32)
Service charges and penalties	<u>47,755</u>	<u>0.66</u>	<u>(278,701)</u>	<u>(583.61)</u>
Total operating	6,278,012	86.80	410,331	6.99
Nonoperating income				
Interest income	107,695	1.49	(73,366)	(40.52)
Capital contributions - EDA grant	<u>846,914</u>	<u>11.71</u>	<u>846,914</u>	100.00
Total revenues	<u>\$ 7,232,621</u>	<u>100.00</u>	<u>\$ 1,183,879</u>	19.57

**Keokuk Municipal Water Works,  
A Component Unit of the City of Keokuk  
Management's Discussion and Analysis**

**Expenses**

A summary of expenses for the year ended June 30, 2010, and the amount and percentage of change in relation to prior year amounts, is as follows:

	2010 <u>Amount</u>	% of <u>Total</u>	Increase (Decrease) from Prior <u>Year</u>	% Increase <u>(Decrease)</u>
Operating				
Operating expenses	\$ 4,369,306	73.06	\$ 104,672	2.45
Depreciation	<u>1,067,625</u>	<u>17.85</u>	<u>199,777</u>	23.02
Total operating	5,436,931	90.91	304,449	5.93
Nonoperating expense				
Interest expense and amortization	<u>543,565</u>	<u>9.09</u>	<u>(29,118)</u>	(5.08)
Total expenses	<u>\$ 5,980,496</u>	<u>100.00</u>	<u>\$ 275,331</u>	4.83

The increase in expenses during the fiscal year is primarily attributable in chemical expenses for the plant and payroll expenses.

**Summary of Cash Flow Activities**

The following shows a summary of the major sources and uses of cash and cash equivalents for the years ended June 30, 2010 and 2009. Cash equivalents are considered to be cash-on-hand, bank deposits and highly liquid investments with an original maturity of three months or less.

	2010	2009
Net cash provided by operating activities	\$ 1,819,469	\$ 1,463,222
Net cash provided by investing activities	863,662	2,119,893
Net cash used by capital and related financing activities	<u>(3,631,593)</u>	<u>(4,037,428)</u>
Net decrease in cash and cash equivalents	(948,462)	(454,313)
Cash and cash equivalents, beginning of year	<u>2,574,233</u>	<u>3,028,546</u>
Cash and cash equivalents, end of year	<u>\$ 1,625,771</u>	<u>\$ 2,574,233</u>

**Financial Statements**

The Water Works' financial statements are prepared on an accrual basis in accordance with accounting principles generally accepted in the United States of America promulgated by the Governmental Accounting Standards Board (GASB). The Water Works is structured as a single enterprise fund with revenues recognized when earned, not received. Expenses are recognized when incurred, not when they are paid. Capital assets are capitalized and (except land) are depreciated over their useful lives. See the notes to the financial statements for a summary of the Water Works' significant accounting policies.

**Keokuk Municipal Water Works,  
A Component Unit of the City of Keokuk  
Management's Discussion and Analysis**

**Long-term debt**

At June 30, 2010, the Water Works had \$13,887,980 in debt outstanding. This debt is from refinancing of the 1995 and 1996 Bonds in April 2004 and January 2005; 2008 debt of \$3.8 million to water filters; and additional debt of \$259,370 issued during the 2010 fiscal year to fund the water tower construction project.

**Capital Acquisitions and Construction Activities**

At June 30, 2010, the Water Works had \$47,306,627 in capital assets. Capital expenditures totaled \$4,086,831, an increase of 56% over 2009. A summary of projects follows:

Distribution System:

- Timea Street
- Belknap Place
- Grand Avenue
- Park Street and E Street as connections to South 7th Street Water Tower
- Purchase of Meters
- Purchase of Hydrants

Water Treatment Plant:

- Filter Building
- Filters
- Sludge Disposal Facility
- Sludge Disposal Equipment
- Fence

Water Tower South 7th Street:

- Site preparation, engineering and construction of water tower

Building:

- Meter/Distribution Shop Improvements 1402 7th Street
- Phone System 20 North 4th Street

**Keokuk Municipal Water Works,  
A Component Unit of the City of Keokuk  
Management's Discussion and Analysis**

**Economic Factors**

The Water Works continued to improve its financial position during the current fiscal year. However, the current condition of the economy in the country and local area continues to be a concern for Water Works' officials. Some of the realities that may potentially become challenges for the Water Works to meet are:

- Facilities at the Water Works require constant maintenance and upkeep.
- Water regulations continue to change; in order to meet these new standards, the Water Works must constantly upgrade and change, which could be a financial challenge.
- The Water Works' repair and replacement of mains is on-going, due to the age of the distribution system.
- Closing of businesses and declining population directly affect the income of the Water Works, especially any change with its major customer as disclosed in the Notes to Financial Statements.

For the fiscal year ending June 30, 2011, the Water Works has already entered into the following capital improvement projects:

Mains:

- Concert Street, High Street, completion of E Street and Park Street

Plant:

- Sludge Disposal Equipment and Facility, Lab remodel

Tower:

- Ongoing construction on South 7th Street Tower

The water tower and water main improvements for E Street, Park Street and Water Street are being funded with the aid of the State Revolving Loan Fund of up to \$3.8 million, a \$1.6 million forgivable loan, and Economic Stimulus funds of \$2 million.

**Request for Information**

This financial report is designed to provide a general overview of the Water Works' finances for all those interested. Questions concerning any of the information provided in this report or request for additional information should be addressed in writing to the Manager, Keokuk Municipal Water Works, 20 North Fourth Street, Keokuk, Iowa 52632.

**Keokuk Municipal Water Works,  
A Component Unit of the City of Keokuk  
Statement of Net Assets - Proprietary Fund  
June 30, 2010**

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<b>Assets</b>	
<b>Current Assets</b>	
Cash and cash equivalents	\$ 95,543
Accrued interest receivable	49,860
Accounts receivable	611,806
Grant receivable	609,438
Prepaid expenses	<u>98,508</u>
Total current assets	<u>1,465,155</u>
<b>Restricted Assets</b>	
Sewer, garbage and landfill:	
Cash and cash equivalents	184,348
Accounts receivable	<u>205,899</u>
	<u>390,247</u>
Consumer water meter deposits: Cash and cash equivalents	<u>161,546</u>
Consumer sewer meter deposits:	
Cash and cash equivalents	7,076
Certificates of deposit	<u>78,000</u>
	<u>85,076</u>
Sinking fund: Cash and cash equivalents	<u>384,369</u>
Reserve fund:	
Guaranteed investment contracts	737,750
Certificates of deposit	<u>695,825</u>
	<u>1,433,575</u>
Improvement fund: Cash and cash equivalents	<u>250,000</u>
General regulatory and system improvement: Cash and cash equivalents	<u>542,889</u>
	<u>3,247,702</u>
<b>Property, Plant and Equipment</b>	
Property, plant and equipment, at cost	47,306,627
Less accumulated depreciation	<u>(14,953,057)</u>
	<u>32,353,570</u>
<b>Other Assets</b>	
Unamortized bond issuance costs, net of accumulated amortization of \$151,571	<u>176,921</u>
	<u>\$ 37,243,348</u>

See notes to financial statements.

**Keokuk Municipal Water Works,  
A Component Unit of the City of Keokuk  
Statement of Net Assets - Proprietary Fund  
June 30, 2010**

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<b>Liabilities</b>	
<b>Current Liabilities</b>	
Accounts payable	\$ 1,647,245
State sales tax payable	541
Accrued salaries and vacation	299,112
Accrued interest payable	122,334
Current portion long-term debt	950,000
Due to city - sewer and garbage charges	388,686
Due to GRRW - landfill charges	1,561
Consumer water meter deposits	161,546
Consumer sewer meter deposits	<u>85,076</u>
Total current liabilities	<u>3,656,101</u>
<b>Long-term Debt, net of current portion</b>	<u>12,937,980</u>
	<u>16,594,081</u>
<b>Net Assets</b>	
Invested in capital assets, net of related debt	18,465,590
Restricted	
Sinking fund	384,369
Reserve fund	1,433,575
Improvement fund	250,000
Unrestricted	<u>115,733</u>
	<u>20,649,267</u>
	<u>\$ 37,243,348</u>

See notes to financial statements.

**Keokuk Municipal Water Works,  
A Component Unit of the City of Keokuk  
Statement of Revenues, Expenses and Changes in Fund Net Assets - Proprietary Fund  
For the Year Ended June 30, 2010**

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<b>Operating Revenues</b>	
Metered sales	\$ 6,139,494
Flat rate sales	681
Miscellaneous charges	90,082
Service charges and penalties	<u>47,755</u>
Total operating revenues	<u>6,278,012</u>
<b>Operating Expenses</b>	
Operating expenses	4,369,306
Depreciation	<u>1,067,625</u>
Total operating expenses	<u>5,436,931</u>
Net operating income	<u>841,081</u>
<b>Nonoperating income (expenses)</b>	
Interest income	107,695
Interest expense	(502,190)
Amortization	<u>(41,375)</u>
Total nonoperating expenses	<u>(435,870)</u>
Income (loss) before capital contributions	405,211
Capital contributions - EDA grant	<u>846,914</u>
Change in net assets	1,252,125
Net assets, beginning of year	<u>19,397,142</u>
Total nonoperating income	<u>\$ 20,649,267</u>

See notes to financial statements.

**Keokuk Municipal Water Works,  
A Component Unit of the City of Keokuk  
Statement of Cash Flows - Proprietary Fund  
For the Year Ended June 30, 2010**

<b>Cash Flows from Operating Activities</b>	
Receipts from customers	\$ 6,129,650
Receipts from service charges and miscellaneous	156,140
Meter deposits received, net	14,503
Payments to suppliers	(3,237,326)
Payments to employees	(1,043,498)
Payments for interfund services	<u>(200,000)</u>
Net cash provided by operating activities	<u>1,819,469</u>
<b>Cash Flows from Capital and Related Financing Activities</b>	
Purchases of capital assets	(4,086,831)
Capital grant received	237,476
Principal payments on long-term debt	(920,000)
Principal borrowings on long-term debt	1,692,980
Interest payments on long-term debt	(511,494)
Prepaid debt issuance costs	<u>(43,724)</u>
Net cash used by capital and related financing activities	<u>(3,631,593)</u>
<b>Cash Flows from Investing Activities</b>	
Purchases of certificates of deposit	(293,105)
Redemptions of certificates of deposit	1,073,000
Interest income	<u>83,767</u>
Net cash provided by investing activities	<u>863,662</u>
Net decrease in cash and cash equivalents	(948,462)
Cash and cash equivalents, beginning of year	<u>2,574,233</u>
Cash and cash equivalents, end of year	<u>\$ 1,625,771</u>
<b>Reconciliation of Operating Income to Net Cash Provided by Operating Activities</b>	
Operating income	\$ 841,081
Adjustments to reconcile operating income to net cash provided by operating activities:	
Depreciation expense	1,067,625
Changes in assets and liabilities:	
Receivables and prepaids	(66,465)
Accounts payable and accrued expenses	<u>(22,772)</u>
Net cash provided by operating activities	<u>\$ 1,819,469</u>
<b>Supplemental Disclosure of Noncash Capital and Related Financing Activities</b>	
Equipment purchases financed through accounts payable	\$ 1,494,264
Capitalized interest on assets under construction	3,048

See notes to financial statements.

**Keokuk Municipal Water Works,  
A Component Unit of the City of Keokuk  
Notes to Financial Statements**

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**Note 1. Summary of Significant Accounting Policies**

The Keokuk Municipal Water Works (Water Works) currently provides water for the residential and commercial needs of locations within the City of Keokuk, Iowa. The governing body of the Water Works is a Board of Trustees consisting of five members appointed by the City of Keokuk's Mayor and approved by the City of Keokuk's Council. The Board of Trustees has the responsibility for designated management and is accountable for fiscal matters relating to the Water Works.

Reporting Entity

For financial reporting purposes, the Water Works has included all funds, organizations, account groups, agencies, boards, commissions and authorities. The Water Works has also considered all potential component units for which it is financially accountable, and other organizations for which the nature and significance of their relationship with the Water Works are such that exclusion would cause the Water Works' financial statements to be misleading or incomplete.

The Governmental Accounting Standards Board (GASB) 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 entity 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 entity.

Based on the above criteria, there are no agencies or entities that should be combined with the financial statements of the Water Works. However, based on these criteria, the Water Works is a component unit of the City of Keokuk for financial reporting purposes. The City of Keokuk has financial accountability for the Water Works because it appoints a voting majority of the Water Works' Board of Trustees.

Measurement Focus, Basis of Accounting and Financial Statement Presentation

The financial statements of the Water Works are prepared in accordance with accounting principles generally accepted in the United States of America. The Water Works' reporting entity applies all relevant GASB pronouncements, except for GASB Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, which has not been implemented. The proprietary fund financial statements apply Financial Accounting Standards Board pronouncements and Accounting Principles Board Opinions issued on or before November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements, in which case, GASB prevails.

The accounts of the Water Works are organized on the basis of funds or account groups, each of which is considered to be a separate accounting entity. The transactions of each fund or account group are summarized by providing a separate set of self-balancing accounts which include its assets, liabilities, fund equity, revenues and expenses.

**Keokuk Municipal Water Works,  
A Component Unit of the City of Keokuk  
Notes to Financial Statements**

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**Note 1. Summary of Significant Accounting Policies (continued)**

The accounts of the Water Works are primarily organized as an enterprise fund, which is a proprietary fund type. Enterprise funds are used to account for operations (a) that are financed and operated in a manner similar to private business enterprises, where the intent of the governing body is that the costs (expenses, including depreciation) of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges or (b) where the governing body has decided that periodic determination of revenues earned, expenses incurred, and/or net income is appropriate for capital maintenance, public policy, management control, accountability, or other purposes.

The proprietary funds are accounted for using the flow of economic resources measurement focus. The accounting objectives are a determination of net income, financial position and changes in cash flow. All assets and liabilities associated with a proprietary fund's activities are included on its statement of net assets. Operating income reported in the proprietary fund financial statements includes revenues and expenses related to the primary, continuing operations of the fund. Principal operating revenues for the proprietary fund are charges to customers for services or rent. Principal operating expenses are the costs of providing goods or services and include administrative expenses and depreciation of capital assets. Other income and expenses are classified as nonoperating in the financial statements.

Assets, Liabilities and Fund Equity

The Statement of Net Assets is based on the following accounting policies:

Cash and Cash Equivalents

The Water Works considers all short-term investments with an original maturity of three months or less to be cash equivalents.

Accounts Receivable

Accounts receivable are recorded at the time the service is billed. Unbilled water usage for service consumed between periodic scheduled billing dates is estimated and is recognized as revenue in the period in which the service is provided.

The Water Works grants credit to customers, substantially all of whom are located in Keokuk, Iowa. The risk of loss on accounts receivable is the balance due at the time of default. Accounts receivable are considered past due after thirty days and charged off when management determines the account is uncollectible. Bad debts are charged to operations in the year in which the account is determined uncollectible. Because of the Water Works' ability to deny continued service to customers with past due bills, management believes uncollectible accounts are negligible; therefore, no allowance for uncollectible accounts has been recorded.

Restricted Assets

Restricted assets consist of cash and cash equivalents, certificates of deposit, guaranteed investment contract and accounts receivable. These funds are set aside for sewer, garbage and landfill fees collected for others, water and sewer meter deposits, bond sinking, bond improvement and bond reserve accounts. Water Works carries its investment in the guaranteed investment contract at cost since it is a nonparticipating contract that has a fixed interest rate.

**Keokuk Municipal Water Works,  
A Component Unit of the City of Keokuk  
Notes to Financial Statements**

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**Note 1. Summary of Significant Accounting Policies (continued)**

Property and Equipment

Property and equipment is stated at cost.

Depreciation expense for the year ended June 30, 2010 was \$1,067,625. Depreciation of property and equipment is computed by the straight line method at rates based on the estimated useful lives disclosed below.

As of June 30, 2010, the Water Works had property of \$4,362,718 not in service as the property was still being constructed. For the years ended June 30, 2010, the Water Works capitalized interest costs of \$3,048 relating to the construction of the property.

The cost of assets sold, retired, or otherwise disposed of and the related allowance for depreciation are eliminated from the accounts, and any resulting gain or loss is included in operations.

Expenditures for maintenance and repairs are charged against operations. Renewals and betterments that materially extend the life of an asset are capitalized.

Changes in property and equipment consist of the following:

	<u>Beginning</u>	<u>Additions</u>	<u>Deductions</u>	<u>Ending</u>	<u>Estimated Useful Lives</u>
Land	\$ 457,766	\$ -	\$ -	\$ 457,766	--
Building	318,172	62,856	3,654	377,374	10-30
Plant and Tanks	34,485,041	5,334,436	960	39,818,517	10-50
Distribution system, meters and hydrants	5,673,156	181,344	-	5,854,500	15-80
Machinery and equipment	<u>851,229</u>	<u>5,506</u>	<u>58,265</u>	<u>798,470</u>	5-20
	<u>\$ 41,785,364</u>	<u>\$ 5,584,142</u>	<u>\$ 62,879</u>	<u>\$ 47,306,627</u>	

Amortization of Water Revenue Refunding Capital Loan Note Fees

During the prior years, the Water Works incurred costs of \$284,768 in connection with the 2004A, 2005A and 2008 Series Water Revenue Refunding Capital Loan Notes. During the year ended June 30, 2010, the Water Works incurred costs of \$43,724 in connection with the 2010 Series Water Revenue Capital Loan Notes. These costs are being ratably amortized on a monthly basis over the life of the Capital Loan Notes until the first call date. The amortization expense for the year ended June 30, 2010 was \$41,375.

Compensated Absences

Water Works employees accumulate a limited amount of earned but unused vacation and sick leave hours for subsequent use or for payment upon termination, retirement or death. The Water Works' liability for accumulated vacation and sick leave has been computed based on rates in effect at June 30, 2010.

**Keokuk Municipal Water Works,  
A Component Unit of the City of Keokuk  
Notes to Financial Statements**

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**Note 1. Summary of Significant Accounting Policies (continued)**

Budgets and Budgetary Accounting

The budgetary comparison and related disclosures are reported as Required Supplementary Information. During the year ended June 30, 2010, disbursements did not exceed the amounts budgeted.

Use of Estimates

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

**Note 2. Pension and Retirement Benefits**

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

Plan members are required to contribute 4.30% of their annual salary and the Water Works is required to contribute 6.65% of annual covered payroll. Contribution requirements are established by State statute. The Water Works' contribution to IPERS for the years ended June 30, 2010, 2009 and 2008 was \$67,013, \$57,319 and \$50,291, respectively, which was equal to the required contribution.

**Note 3. Deposits**

The Water Works' deposits at June 30, 2010 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 Water Works 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 Water Works and the Treasurer of the State of Iowa; prime eligible bankers acceptances; certain high-rated commercial paper; perfected repurchase agreements; certain registered open-end management investment companies; certain joint investment trusts; and warrants or improvement certificates of a drainage district.

**Keokuk Municipal Water Works,  
A Component Unit of the City of Keokuk  
Notes to Financial Statements**

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**Note 4. Bonds and Long-Term Debt**

On April 1, 2004, the Water Works issued \$7,000,000 in Water Revenue Refunding Capital Loan Notes. The Water Works entered into an escrow agreement with Wells Fargo Bank, N.A. and deposited the proceeds from the refunding notes. The proceeds were used to advance refund \$6,650,000 of 1995 Water Revenue Capital Loan Notes on the call date of April 1, 2006. These notes mature semi-annually beginning October 1, 2006 through April 1, 2020, with interest rates from 1.90% to 4.55%. Notes maturing after April 1, 2013 may be called for redemption and paid before maturity on said date or any date thereafter at par plus accrued interest in whole or in part, in order of maturity.

On January 27, 2005, the Water Works issued \$4,505,000 in Water Revenue Refunding Capital Loan Notes. The Water Works entered into an escrow agreement with Wells Fargo Bank, N.A. and deposited the proceeds from the refunding notes. The proceeds were used to advance refund \$4,330,000 of 1996 Water Revenue Capital Loan Notes on the call date of April 1, 2006. These notes mature semi-annually beginning October 1, 2006 through April 1, 2020, with interest rates from 2.65% to 5.00%. Notes maturing after April 1, 2013 may be called for redemption and paid before maturity on said date or any date thereafter at par plus accrued interest in whole or in part, in order of maturity.

On June 25, 2008, the Water Works issued \$3,800,000 in Water Revenue Capital Loan Notes. These notes mature semi-annually beginning April 1, 2009 through April 1, 2023, with interest rates from 2.75% to 4.30%. Notes maturing after April 1, 2015 may be called for redemption and paid before maturity on said date or any date thereafter at par plus accrued interest in whole or in part, in order of maturity.

On February 10, 2010, the Water Works issued \$3,777,000 in Water Revenue Refunding Capital Loan Notes. The Water Works entered into an escrow agreement with Wells Fargo Bank, N.A., the trustee of the master trust of the Iowa Finance Authority, and deposited the proceeds from the notes. The proceeds are to be used to fund the water tower construction project. These notes mature semi-annually beginning June 1, 2010 through June 1, 2031, with a 3.00% interest rate. As of June 30, 2010, the Water Works has drawn down \$259,370. The future debt service requirements below use estimated debt payments based on the maximum loan amount. The final loan payment schedule will be determined after the project is complete and all draws on the note are complete.

On February 10, 2010, the Water Works issued \$1,603,000 in Forgivable Loan Water Revenue Capital Loan Notes. The Water Works entered into an escrow agreement with Wells Fargo Bank, N.A., the trustee of the master trust of the Iowa Finance Authority, and deposited the proceeds from the notes. The proceeds are to be used to fund the water tower construction project. This bond matures semi-annually beginning June 1, 2012 through June 1, 2031, with a 3.00% interest rate. As of June 30, 2010, the Water Works has drawn down \$1,433,610. The bond will be forgiven and no payments of interest, principal, or fees shall be due under the bond following completion of the water tower project and receipt by the State of Iowa of a certificate of completion from the Water Works. If the bond is not forgiven, principal and interest payments will begin June 1, 2012, with an interest rate of 3.00%. At June 30, 2010, the Water Works does not owe any interest, and therefore, the Water Works has not accrued any interest payable.

**Keokuk Municipal Water Works,  
A Component Unit of the City of Keokuk  
Notes to Financial Statements**

**Note 4. Bonds and Long-Term Debt (continued)**

Annual debt service requirements for Water Revenue Capital Loan Notes are as follows:

Year Ending June 30.	\$7,000,000 Water Revenue Refunding Capital Loan Notes Series 2004A		\$4,505,000 Water Revenue Refunding Capital Loan Notes Series 2005A		\$3,800,000 Water Revenue Capital Loan Notes Series 2008	
	Principal	Interest	Principal	Interest	Principal	Interest
2011	\$ 455,000	\$ 203,219	\$ 285,000	\$ 149,778	\$ 210,000	\$ 127,908
2012	470,000	189,010	295,000	139,137	215,000	121,634
2013	485,000	173,474	310,000	127,432	220,000	114,725
2014	500,000	156,627	320,000	114,734	235,000	107,213
2015	520,000	138,318	330,000	101,188	240,000	99,018
2016-2020	2,925,000	358,688	1,910,000	262,782	1,330,000	350,953
2021-2025	-	-	-	-	940,000	71,063
2026-2030	-	-	-	-	-	-
	<u>\$ 5,355,000</u>	<u>\$ 1,219,336</u>	<u>\$ 3,450,000</u>	<u>\$ 895,051</u>	<u>\$ 3,390,000</u>	<u>\$ 992,514</u>

  

Year Ending June 30.	\$3,777,000 Water Revenue Refunding Capital Loan Notes Series 2010		\$1,603,000 Forgivable Loan Water Revenue Capital Loan Notes Series 2010		Total	
	Principal	Interest	Principal	Interest	Principal	Interest
2011	\$ -	\$ 69,000	\$ -	\$ -	\$ 950,000	\$ 549,905
2012	137,000	113,310	1,000	24,045	1,118,000	587,136
2013	122,370	109,200	62,000	48,060	1,199,370	572,891
2014	-	-	64,000	46,200	1,119,000	424,774
2015	-	-	66,000	44,280	1,156,000	382,804
2016-2020	-	-	366,000	190,200	6,531,000	1,162,623
2021-2025	-	-	429,000	131,740	1,369,000	202,803
2026-2030	-	-	445,610	62,970	445,610	62,970
	<u>\$ 259,370</u>	<u>\$ 291,510</u>	<u>\$ 1,433,610</u>	<u>\$ 547,495</u>	<u>\$ 13,887,980</u>	<u>\$ 3,945,906</u>

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

**A. Rate Covenant**

The Water Works covenants to continue in effect rates for services rendered to be sufficient to produce gross revenues adequate to pay expenses of operation and maintenance and to maintain a balance of net revenues equal to at least 125% of the principal and interest on the 2004, 2005 and 2008 Series notes as they become due and at least 110% of principal and interest on the 2010 Series notes as they become due.

**B. Sinking Fund**

For the 2004, 2005 and 2008 Series notes, the Sinking Fund requirement is an amount on deposit equal to the monthly amount of the next principal and interest payment.

**Keokuk Municipal Water Works,  
A Component Unit of the City of Keokuk  
Notes to Financial Statements**

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**Note 4. Bonds and Long-Term Debt** (continued)

C. Reserve Fund

For the 2004, 2005 and 2008 Series notes, the Reserve Fund requirement is an amount equal to the lesser of (a) the maximum principal and interest coming due on the notes in any fiscal year, (b) 10% of the stated principal of the notes, or (c) 125% of the average annual debt service on the notes. Amounts on deposit in the Reserve Fund shall be solely for the purpose of paying principal and interest on the notes. The Reserve Fund is to be valued on April 1st of each year and whenever the amount on deposit is less than the Reserve Fund requirement. The Water Works is required to make monthly deposits in an amount equal to 25% of the amount required to be deposited in the Sinking Fund until the Reserve Fund has been restored.

D. Improvement Fund

For the 2004, 2005 and 2008 Series notes, the Improvement Fund requirement is \$250,000. Money on deposit in the Improvement Fund shall be used for the purpose of paying principal and interest on the notes when there are insufficient balances in the Sinking Fund and Reserve Fund. Funds may also be used to pay the costs of extraordinary maintenance expenses or repairs, renewals and replacement. Whenever it shall become necessary to use the money on deposit in the Improvement Fund, the Water Works shall deposit \$21,000 per month until the amount on deposit is restored to \$250,000.

**Note 5. Risk Management**

The Water Works is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. These risks are covered by the purchase of commercial liability insurance. Settled claims for these risks have not exceeded commercial insurance coverage for the past three years.

**Note 6. Major Customers**

Water sales to one major customer was \$4,224,664 for the year ended June 30, 2010, representing approximately 67% of the total operating revenue for the year. At June 30, 2010, the amount due from this customer was \$353,693, which is included in accounts receivable.

**Note 7. Related Party Transactions**

The Water Works had business transactions with one employees amounting to \$6,470 during the year ended June 30, 2010.

**Keokuk Municipal Water Works,  
A Component Unit of the City of Keokuk  
Notes to Financial Statements**

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**Note 8. Related Organization**

Based on criteria set by the GASB, the Keokuk Municipal Water Works is a component unit of the City of Keokuk for financial reporting purposes. The City of Keokuk has financial accountability for the Water Works under these criteria because it appoints a voting majority of the Water Works' Board of Trustees.

The Water Works provides billing service for sewer and garbage for the City of Keokuk and collects fees for these services. Total fees collected for the year ending June 30, 2010 totaled \$2,028,570. Amounts due to the City as of June 30, 2010 were \$388,686 for sewer and garbage charges and \$1,404 for vehicle cost reimbursement.

In previous years, the Water Works provided billing service for landfill fees for Great River Regional Waste (GRRW). Currently, the Water Works collects the past due fees for these services. Amount due to GRRW as of June 30, 2010 was \$1,561.

The Water Works made a payment in lieu of taxes to the City of Keokuk for \$200,000 for the year ended June 30, 2010.

**Note 9. Commitments and Contingencies**

As of June 30, 2010, the Water Works had ongoing contracts for the construction of a four million gallon water tower. The amount remaining on the contracts for the water tower is approximately \$2,856,000.

Subsequent to year end, the Water Works signed a contract for \$229,994 for the Grand Avenue main project.

**Note 10. Subsequent Events**

The Water Works performed an evaluation of subsequent events through November 16, 2010, which is the date the financial statements were available to be issued. The Water Works borrowed an additional \$1,736,222 from the 2010 Series Water Revenue notes for construction of the water tower subsequent to year end.

**Keokuk Municipal Water Works,  
A Component Unit of the City of Keokuk  
Notes to Financial Statements**

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**Note 11. Prospective Accounting Change**

The GASB has issued a Statement not yet implemented by the Water Works. Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions*, issued February 2009, will be effective for the Water Works for the fiscal year ending June 30, 2011. This Statement establishes accounting and financial reporting standards for all governments that report governmental funds. The fund balance for governmental funds should be reported in classifications that comprise a hierarchy based primarily on the extent to which the government is bound to honor constraints on the specific purposes for which amounts in those funds can be spent. In the year that Statement No. 54 is implemented, the beginning fund balance classifications will be retroactively restated for prior periods presented. The Water Works' management has not yet determined the effect this Statement will have on the Water Works' financial statements.

**Keokuk Municipal Water Works,  
A Component Unit of the City of Keokuk  
Required Supplementary Information  
Comparison of Revenues and Expenses - Actual to Budget  
Year Ended June 30, 2010**

	<u>Actual</u>	<u>Budgeted Amounts Original/Final</u>	<u>Variance: Favorable (Unfavorable)</u>	<u>Net as Percent of Budget</u>
Operating revenues				
Metered sales	\$ 6,139,494	\$ 6,697,781	\$ (558,287)	92 %
Flat rate sales	681	4,000	(3,319)	17 %
Miscellaneous charges	90,082	70,000	20,082	129 %
Service charges and penalties	<u>47,755</u>	<u>38,417</u>	<u>9,338</u>	124 %
Total operating revenues	<u>6,278,012</u>	<u>6,810,198</u>	<u>(532,186)</u>	
Operating expenses				
Operating expenses (Supplementary Schedule of Expenses)	4,369,306	4,890,973	521,667	89 %
Depreciation	<u>1,067,625</u>	<u>835,234</u>	<u>(232,391)</u>	128 %
Total operating expenses	<u>5,436,931</u>	<u>5,726,207</u>	<u>289,276</u>	95 %
Operating income	<u>841,081</u>	<u>1,083,991</u>		
Nonoperating income (expense)				
Interest income	107,695	150,000		
Property, plant and equipment	(4,086,831)	(6,735,000)		
Amortization	(41,375)	(44,766)		
Net long-term debt cash receipts (payments)	217,762	(1,429,093)		
Capital contributions - EDA grant	<u>846,914</u>	<u>-</u>		
	<u>(2,955,835)</u>	<u>(8,058,859)</u>		
Changes in net assets	<u>\$ (2,114,754)</u>	<u>\$ (6,974,868)</u>		

The following table is a reconciliation of the actual operating results presented consistent with the basis used to generate the budget to the operating results presented in the Statement of Revenues, Expenses and Changes in Fund Net Assets:

Changes in net assets, as presented above	\$ (2,114,754)
Add: Cash expenditures for property, plant and equipment capitalized under GAAP	4,086,831
Add: Cash expenditures for long-term debt interest payments capitalized under GAAP	3,048
Add: Cash expenditures for long-term debt principal payments	920,000
Add: Cash expenditures for long-term debt issuance costs capitalized under GAAP	43,724
Subtract: Cash proceeds for long-term debt issuance	(1,692,980)
Subtract: Change in accrued interest expense	<u>6,256</u>
Changes in net assets, as presented in Statement of Revenues, Expenses and Changes in Fund Net Assets	<u>\$ 1,252,125</u>

See accompanying independent auditor's report.

**Keokuk Municipal Water Works**  
**A Component Unit of the City of Keokuk**  
**Required Supplementary Information**  
**Notes to Required Supplementary Information - Actual to Budget**  
**Year Ended June 30, 2010**

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The Board of Trustees annually adopts a budget on the modified accrual basis following required public notice and hearing on all funds and submits it to the City Council. The annual budget may be amended during the year utilizing similar statutorily prescribed procedures.

Formal and legal budgetary control is based upon classes of disbursements known as functions, not by fund or category type. The Water Works' disbursements are budgeted in the business type activities function. The Water Works' budget is reflected in the original and final budgeted amount. The Water Works' budget was not amended during the year.

During the year ended June 30, 2010, disbursements did not exceed the amounts budgeted.

See accompanying independent auditor's report.

**Keokuk Municipal Water Works,  
A Component Unit of the City of Keokuk  
Supplementary Schedule of Expenses  
Year Ended June 30, 2010**

	<u>Actual</u>	<u>Final Budget</u>	<u>Actual Over (Under)Budget</u>
<b>Plant Operations and Maintenance</b>			
Supervision labor	\$ 120,869	\$ 113,161	\$ 7,708
Maintenance labor	74,255	115,000	(40,745)
Operation labor	278,514	248,982	29,532
Laboratory labor	39,710	39,171	539
Social security and IPERS	70,843	72,360	(1,517)
Health insurance	134,537	118,958	15,579
Flood control	3,502	21,000	(17,498)
Purification supplies	1,172,406	1,319,550	(147,144)
Utilities	454,219	425,000	29,219
Plant maintenance	183,679	200,000	(16,321)
Supplies	37,408	50,000	(12,592)
Sludge disposal	291,505	401,000	(109,495)
Education and travel	3,383	7,000	(3,617)
Intake	1,018	4,000	(2,982)
Generator expense	20,383	8,000	12,383
	<u>2,886,231</u>	<u>3,143,182</u>	<u>(256,951)</u>
<b>Distribution Maintenance</b>			
Supervision labor	52,799	50,431	2,368
Maintenance labor	49,802	36,296	13,506
Social security and IPERS	14,003	12,142	1,861
Health insurance	29,867	29,169	698
Main leaks	80,830	125,000	(44,170)
Valves	13,485	6,000	7,485
Maintenance	9,645	12,000	(2,355)
Building maintenance	10,822	6,000	4,822
Supplies	32,336	50,000	(17,664)
Hydrants	4,841	7,000	(2,159)
Intake	-	5,000	(5,000)
Storage	2,827	4,000	(1,173)
Education and travel	2,257	4,000	(1,743)
	<u>303,514</u>	<u>347,038</u>	<u>(43,524)</u>

See accompanying independent auditor's report.

**Keokuk Municipal Water Works,  
A Component Unit of the City of Keokuk  
Supplementary Schedule of Expenses  
Year Ended June 30, 2010**

	<u>Actual</u>	<u>Final Budget</u>	<u>Actual Over (Under)Budget</u>
<b>Meter Maintenance</b>			
Supervision labor	\$ 53,152	\$ 50,431	\$ 2,721
Maintenance labor	90,195	100,536	(10,341)
Meter reading labor	2,592	5,356	(2,764)
Social security and IPERS	21,468	21,885	(417)
Health insurance	44,107	39,869	4,238
Meter parts	5,379	10,000	(4,621)
Shop supplies	11,461	30,000	(18,539)
Education and travel	<u>1,343</u>	<u>2,500</u>	<u>(1,157)</u>
	<u>229,697</u>	<u>260,577</u>	<u>(30,880)</u>
<b>Administration</b>			
Management salaries	135,263	123,663	11,600
Office salaries	154,073	150,631	3,442
Board fees	1,475	1,500	(25)
Postage and shipping	28,300	32,000	(3,700)
Data processing expense	-	1,000	(1,000)
Office expense	39,918	41,280	(1,362)
Social security and IPERS	39,612	37,311	2,301
Vehicle maintenance	25,669	20,000	5,669
Engineering and legal	127,521	350,000	(222,479)
Health insurance	71,027	72,791	(1,764)
Insurance	102,079	91,000	11,079
Education and travel	1,627	5,000	(3,373)
Office building maintenance	10,655	12,000	(1,345)
To city in lieu of taxes	200,000	200,000	-
Bond fees	<u>12,645</u>	<u>2,000</u>	<u>10,645</u>
	<u>949,864</u>	<u>1,140,176</u>	<u>(190,312)</u>
<b>Total operating expenses</b>	<b><u>\$ 4,369,306</u></b>	<b><u>\$ 4,890,973</u></b>	<b><u>\$ (521,667)</u></b>

See accompanying independent auditor's report.

**Keokuk Municipal Water Works,  
A Component Unit of the City of Keokuk  
Schedule of Changes in Assets Restricted  
for Landfill, Sewer and Garbage Charges  
Year Ended June 30, 2010**

	<u>Landfill Charges</u>	<u>Sewer Charges</u>	<u>Garbage Charges</u>	<u>Total</u>
Restricted asset balance, June 30, 2009	\$ <u>2,344</u>	\$ <u>208,083</u>	\$ <u>138,038</u>	\$ <u>348,465</u>
Fees				
Sewer service charges	-	1,333,984	-	1,333,984
Garbage service charges	-	-	694,586	694,586
Less: billing adjustments	<u>-</u>	<u>(12,964)</u>	<u>(5,349)</u>	<u>(18,313)</u>
	<u>-</u>	<u>1,321,020</u>	<u>689,237</u>	<u>2,010,257</u>
Expenditures				
To the City of Keokuk	<u>(783)</u>	<u>(1,284,568)</u>	<u>(683,124)</u>	<u>(1,968,475)</u>
Restricted asset balance, June 30, 2010	\$ <u>1,561</u>	\$ <u>244,535</u>	\$ <u>144,151</u>	\$ <u>390,247</u>
Restricted asset balance is composed of the following:				
Cash and cash equivalents	\$ 8	\$ 123,964	\$ 60,376	\$ 184,348
Accounts receivable	<u>1,553</u>	<u>120,571</u>	<u>83,775</u>	<u>205,899</u>
	<u>\$ 1,561</u>	<u>\$ 244,535</u>	<u>\$ 144,151</u>	<u>\$ 390,247</u>

See accompanying independent auditor's report.

**Keokuk Municipal Water Works,  
A Component Unit of the City of Keokuk  
Schedule of Changes in Assets Restricted for  
Water Revenue Capital Loan Notes Debt Service  
Year Ended June 30, 2010**

	Water Revenue Notes Sinking Fund	Water Revenue Notes Reserve Fund	Water Revenue Notes Improvement Fund	Total
Restricted asset balance, June 30, 2009	\$ <u>357,465</u>	\$ <u>1,433,575</u>	\$ <u>250,000</u>	\$ <u>2,041,040</u>
Receipts				
Transfers from operations	1,458,398	-	-	1,458,398
Transfers from bond proceeds	-	-	-	-
	<u>1,458,398</u>	<u>-</u>	<u>-</u>	<u>1,458,398</u>
Expenditures				
Note principal payments	(920,000)	-	-	(920,000)
Note interest payments	(511,494)	-	-	(511,494)
	<u>(1,431,494)</u>	<u>-</u>	<u>-</u>	<u>(1,431,494)</u>
Restricted asset balance, June 30, 2010	\$ <u>384,369</u>	\$ <u>1,433,575</u>	\$ <u>250,000</u>	\$ <u>2,067,944</u>

See accompanying independent auditor's report.

**Keokuk Municipal Water Works  
Schedule of Expenditures of Federal Awards  
June 30, 2010**

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<u>Federal Agency/Pass-Through Agency Program - Grant Title</u>	<u>CFDA Number</u>	<u>Grantor Program Number</u>	<u>Program Disbursements</u>
U.S. Environmental Protection Agency programs:			
Pass-through programs from Iowa Finance Authority			
Capitalization Grants for Drinking Water State			
Revolving Loan Funds	66.468	DS0143R	\$ 191,080
ARRA - Capitalization Grants for Drinking Water State			
Revolving Loan Funds	66.468	DF0144R	<u>1,603,000</u>
			1,794,080
U.S. Department of Commerce			
Pass-through program from Economic Development Administration			
Public Works and Development Grant Program	11.300	05-01-04719	<u>846,914</u>
<b>Total</b>			<b>\$ <u>2,640,994</u></b>

**Basis of Presentation** - The Schedule of Expenditures of Federal Awards includes the federal grant activity of the Keokuk Municipal Water Works and is presented on the accrual basis. The information on this schedule is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of, the basic financial statements.

See accompanying independent auditor's report.



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**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***

Board of Trustees  
Keokuk Municipal Water Works,  
A Component Unit of the City of Keokuk  
Keokuk, Iowa

We have audited the accompanying financial statements of the proprietary fund of Keokuk Municipal Water Works (Water Works), A Component Unit of the City of Keokuk, as of and for the year ended June 30, 2010, which collectively comprise the basic financial statements listed in the table of contents, and have issued our report thereon dated November 16, 2010. We conducted our audit in accordance with auditing standards generally accepted in the United States of America 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 Water Works' internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Water Works' internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Water Works' internal control over financial reporting.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the Water Works' financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiencies described in Part II of the accompanying Schedule of Findings to be material weaknesses.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies or material weaknesses. We identified certain deficiencies in internal control over financial reporting, described in the accompanying Schedule of Findings, that we consider to be material weaknesses in internal control over financial reporting.

## Compliance and Other Matters

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

We noted certain matters that we reported to management of the Water Works in a separate letter dated November 16, 2010.

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

This report is intended solely for the information and use of the officials, employees and citizens of Keokuk Municipal Water Works and other parties to whom the Water Works may report, including federal awarding agencies and pass-through entities. 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 Water Works during the course of our audit. Should you have any questions concerning any of the above matters, we shall be pleased to discuss them with you at your convenience.

*CPA Associates PC*

November 16, 2010



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**Report on Compliance with Requirements Applicable  
to Each Major Program and Internal Control Over Compliance  
in Accordance with OMB Circular A-133**

Board of Trustees  
Keokuk Municipal Water Works,  
A Component Unit of the City of Keokuk  
Keokuk, Iowa

Compliance

We have audited the compliance of the Keokuk Municipal Water Works (Water Works) with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) Circular A-133, *Compliance Supplement* that are applicable to its major federal programs for the year ended June 30, 2010. The Water Works' major federal programs are identified in Part I of the accompanying Schedule of Findings. Compliance with the requirements of laws, regulations, contracts and grants applicable to its major federal programs is the responsibility of the Water Works' management. Our responsibility is to express an opinion on their compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States and OMB Circular A-133, *Audits of States, Local Governments and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on the major federal programs identified in the accompanying Schedule of Findings occurred. An audit includes examining, on a test basis, evidence about the Water Works' compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on the Water Works' compliance with those requirements.

In our opinion, the Water Works complied, in all material respects, with the requirements referred to above that are applicable to its major federal programs identified in the accompanying Schedule of Findings for the year ended June 30, 2010.

## Internal Control Over Compliance

Management of the Water Works is responsible for establishing and maintaining effective internal control over compliance with the compliance requirements referred to above. In planning and performing our audit, we considered the Water Works' internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the Water Works' internal control over compliance.

Our consideration of internal control over compliance was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over compliance that might be significant deficiencies or material weaknesses and, therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. However, as discussed below, we identified a certain deficiency in internal control over compliance that we consider to be a material weakness.

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. A material weakness in internal control over compliance is a deficiency, or combination of deficiencies, in internal control over compliance such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. We consider the deficiency in internal control over compliance described in Part III of the accompanying Schedule of Findings to be a material weakness.

The Water Works' responses to findings identified in our audit are described in the accompanying Schedule of Findings. We did not audit the Water Works' responses and, accordingly, we express no opinion on them.

This report, a public record by law, is intended solely for the information and use of the members and customers of the Keokuk Municipal Water Works and other parties to whom the Water Works may report, including federal awarding agencies and pass-through entities. 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 Keokuk Municipal Water Works during the course of our audit. Should you have any questions concerning any of the above matters, we shall be pleased to discuss them with you at your convenience.

*CPA Associates PC*

November 16, 2010

**Keokuk Municipal Water Works,  
A Component Unit of the City of Keokuk  
Schedule of Findings  
For the Year Ended June 30, 2010**

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

- a) A qualified opinion was issued on the financial statements.
- b) Material weaknesses in internal control over financial reporting were disclosed by the audit of the financial statements.
- c) The audit did not disclose any noncompliance that is material to the financial statements.
- d) A material weakness in internal control over major programs was disclosed by the audit of the financial statements.
- e) An unqualified opinion was issued on compliance with requirements applicable to the major programs.
- f) The audit disclosed no audit finding which was required to be reported in accordance with Office of Management and Budget Circular A-133, Section .510(a).
- g) The major federal programs are as follows:
  - CFDA Number 66.468 - Environmental Protection Agency - Capitalization Grants for Drinking Water State Revolving Loan Funds
  - CFDA Number 11.300 - Department of Commerce - Public Works and Development Grant Program
- h) The dollar threshold used to distinguish between Type A and Type B programs was \$300,000.
- i) The Water Works did not qualify as a low-risk auditee.

**Part II: Findings Related to the Financial Statements**

**MATERIAL WEAKNESSES**

II-A-10 Preparation of Financial Statements - The Water Works does not have an internal control system designed to provide for the preparation of the financial statements in accordance with accounting principles generally accepted in the United States of America. Therefore, as auditors, we were requested to draft the financial statements and accompanying notes to the financial statements. This circumstance is not unusual for a governmental entity similar in size to the Water Works. It is the responsibility of management and those charged with governance to make the decision whether to accept the degree of risk associated with this condition because of cost or other considerations.

Recommendation - We realize that obtaining the expertise necessary to prepare the financial statements, including all necessary disclosures, can be considered costly and ineffective. However, the Water Works' management and those charged with governance should decide whether to accept the degree of risk associated with this condition because of cost or other considerations.

Response - The Water Works will continue to review and monitor procedures currently in place and evaluate the risks to be accepted in preparation of the financial statements.

Conclusion - Response accepted.

**Keokuk Municipal Water Works,  
A Component Unit of the City of Keokuk  
Schedule of Findings  
For the Year Ended June 30, 2010**

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**Part II: Findings Related to the Financial Statements (continued)**

II-B-10 Segregation of Duties - One important aspect of the internal control structure is the segregation of duties among employees to prevent one individual employee from handling a transaction from its inception to its completion. Management has not separated incompatible activities of personnel, thereby creating risks related to the safeguarding of cash and the accuracy of the financial statements.

Recommendation - We realize that with a limited number of office employees, segregation of duties is difficult. However, the Board of Trustees and management should continue to provide oversight and direction based upon their direct knowledge of the Water Works' operations and day-to-day contact with employees to control and safeguard assets.

Response - The Water Works will continue to review operating procedures and segregate employee duties to the extent financially feasible to maximize internal control.

Conclusion - Response accepted.

**Instances of Noncompliance:**

No matters were noted.

**Part III: Findings Related to Federal Awards**

**MATERIAL WEAKNESS**

III-A-10 Segregation of Duties Over Federal Receipts - Keokuk Municipal Water Works did not properly segregate collection, deposit and recordkeeping for receipts, including those related to federal programs. See item II-B-10.

**Instances of Noncompliance:**

No matters were noted.

**Part IV: Other Findings Related to Required Statutory Reporting**

IV-A-10 Deposits and Investments - The Water Works has adopted a written investment policy as required by Chapter 12B.10B of the Code of Iowa.

IV-B-10 Travel Expense - No expenditures of Water Works money for travel expenses of spouses of Water Works members or employees were noted.

IV-C-10 Board Minutes - No transactions were found that we believe should have been approved in the Water Works minutes but were not.

IV-D-10 Questionable Disbursements - No disbursements were found that did not meet the requirements of public purpose as defined in the Attorney General's opinion dated April 25, 1979.

**Keokuk Municipal Water Works,  
A Component Unit of the City of Keokuk  
Schedule of Findings  
For the Year Ended June 30, 2010**

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**Part IV: Other Findings Related to Required Statutory Reporting (continued)**

IV-E-10 Certified Budget - Disbursements during the year ended June 30, 2010 did not exceed budget amounts.

IV-F-10 Business Transactions with Water Works Officials and Employees - Business transactions between Water Works officials or employees are detailed as follows:

<u>Name, Title, and Business Connection</u>	<u>Transactions</u>	<u>Amount</u>
Mike Haney, Employee	Mowing	\$ 6,470

The mowing transactions do not appear to represent a conflict of interest since it was entered into through competitive bidding in accordance with Chapter 362.5(4) of the Code of Iowa.

IV-G-10 Revenue Bonds and Notes - No instances of noncompliance with the revenue bond and note resolutions were noted.



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November 16, 2010

Board of Trustees  
Keokuk Municipal Water Works  
A Component Unit of the City of Keokuk  
Keokuk, Iowa

We have audited the financial statements of Keokuk Municipal Water Works (Water Works), A Component Unit of the City of Keokuk, for the year ended June 30, 2010, and have issued our report thereon dated November 16, 2010. Professional standards require that we provide you with information about our responsibilities under auditing standards generally accepted in the United States of America, *Government Auditing Standards*, and OMB Circular A-133, as well as certain information related to the planned scope and timing of our audit. We have communicated such information in our letter to you dated August 5, 2010. Professional standards also require that we communicate to you the following information related to our audit.

Significant Audit Findings

*Qualitative Aspects of Accounting Practices*

Management is responsible for the selection and use of appropriate accounting policies. The significant accounting policies used by the Water Works are described in Note 1 to the financial statements. No new accounting policies were adopted and the application of existing policies was not changed during the year ended June 30, 2010. We noted no transactions entered into by the Water Works during the year for which there is a lack of authoritative guidance or consensus. We noted no significant transactions that have not been recognized in the financial statements in the proper period.

Accounting estimates are an integral part of the financial statements prepared by management and are based on management's knowledge and experience about past and current events and assumptions about future events. Certain accounting estimates are particularly sensitive because of their significance to the financial statements and because of the possibility that future events affecting them may differ significantly from those expected. The most sensitive estimates affecting the financial statements were:

Management makes accounting estimates in the determination of the expenditures capitalized as property and equipment and the useful life of property and equipment for depreciation purposes. We evaluated key factors and assumptions used to develop the estimates in determining that they are reasonable in relation to the financial statements taken as a whole.

*Difficulties Encountered in Performing the Audit*

We encountered no significant difficulties in dealing with management in performing and completing our audit.

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*Corrected and Uncorrected Misstatements*

Professional standards require us to accumulate all known and likely misstatements identified during the audit, other than those that are trivial, and communicate them to the appropriate level of management. The attached schedule summarizes the prior year uncorrected misstatements of the financial statements. Management has determined that their effects are immaterial, both individually and in the aggregate, to the financial statements taken as a whole. The material misstatements detected as a result of audit procedures are as follows:

- Recognition of EDA grant revenue and related receivable
- Recognition of capital expenditures of \$1.5 million related to work performed on the water tower project before year end.
- Adjustment to accrued compensated absences to reflect actual benefit payout
- Adjustments to net assets for journal entries directly recorded to net assets during the year

*Disagreements with Management*

For purposes of this letter, professional standards define a disagreement with management as a financial accounting, reporting, or auditing matter, whether or not resolved to our satisfaction, that could be significant to the financial statements or the auditor's report. We are pleased to report that no such disagreements arose during the course of our audit.

*Management Representations*

We have requested certain representations from management that are included in the management representation letter dated November 16, 2010.

*Management Consultations with Other Independent Accountants*

In some cases, management may decide to consult with other accountants about auditing and accounting matters, similar to obtaining a "second opinion" on certain situations. If a consultation involves application of an accounting principle to the Water Works' financial statements or a determination of the type of auditor's opinion that may be expressed on those statements, our professional standards require the consulting accountant to check with us to determine that the consultant has all the relevant facts. To our knowledge, there were no such consultations with other accountants.

*Other Audit Findings or Issues*

We generally discuss a variety of matters, including the application of accounting principles and auditing standards, with management each year prior to retention as the Water Works' auditors. However, these discussions occurred in the normal course of our professional relationship and our responses were not a condition to our retention.

#### Year End Closing Process

Management made significant efforts to record the various accrual adjustments previously proposed as a part of the audit. Management's calculations for receivables, accrued wages and accounts payable (outside of the water tower project) were materially accurate. Furthermore, the audit did not identify any material expenditures made during the year that were not properly capitalized as property and equipment. We commend management for its efforts and ask management to continue working to make the necessary accrual adjustments prior to the audit.

#### Old Outstanding Checks

We noted during the course of the audit numerous old outstanding checks still being carried as part of the bank reconciliation items. The Water Works should review these checks and ensure they are abiding by the escheatment laws and appropriately remit funds to the appropriate state. The State of Iowa requires property unclaimed in excess of one to three years be remitted to the state.

#### Delinquent Water Bills

Through review of the past due delinquent register at June 30, 2010, we noted delinquent payments not only from the general public but from one Water Works employee. Consideration should be given to establishing policies that encourage employees to provide positive examples of financial responsibility and ensure employee accounts follow the same delinquent bill process as the general public.

#### Authorization for Expenditure Payments

During the course of our audit, we noted two transactions over \$5,000 that did not follow the current Board policy that requires checks over \$5,000 to have at least one Board member's signature.

#### Employee Compensation

During the course of our audit, we noted that the Water Works paid for country club dues for one employee and life insurance policies for three of the twenty-six employees. The Internal Revenue Code Section (IRC) considers country club dues and life insurance policy premiums that are not offered to all employees to be taxable fringe benefits, which should be included in the employees' annual compensation. The country club dues and life insurance premiums were not being accounted for as part of the payroll processing function. As a result, we noted the employees' compensation was not reported in accordance with the IRC. The country club dues and life insurance premiums should be included as employee compensation within the payroll system and properly coded as compensation in the general ledger.

#### *Departures from Accounting Principles Generally Accepted in the United States of America*

The Water Works did not record or disclose the net annual required contribution for other postemployment benefits (OPEB) or the OPEB net liability obligation as required by Government Accounting Standards Board (GASB) Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*. In our opinion, this practice is a departure from accounting principles generally accepted in the United States of America, and we have qualified our report on the basic financial statements dated November 16, 2010 for this departure.

Non-attest Services

We provide the Water Works with non-attest services pertaining to drafting the financial statements and related notes, proposing adjusting journal entries, calculating depreciation, preparing the Schedule of Expenditures of Federal Awards, and preparing the OMB Circular A-133 Data Collection Form (SF-SAC). In connection with these services, management has made all management-level decisions and performed all management functions, designated a management-level individual with suitable skill, knowledge or experience to oversee the services, evaluated the adequacy and results of the services performed, accepted responsibility for the results of the services, and established and maintained controls, including monitoring ongoing activities.

This information is intended solely for the use of Keokuk Municipal Water Works management and Board of Trustees and is not intended to be and should not be used for anyone other than these specified parties.

*CPA Associates PC*