MARION WATER DEPARTMENT
A COMPONENT UNIT OF THE
CITY OF MARION, IOWA

MARION, IOWA

JUNE 30, 2011

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Officials

Name	Title	Term Expires
	(Before January 1, 2011)	
Mary Ann McComas	Chairperson	November 1, 2012
Gregory O. Hapgood	Trustee	November 1, 2010
Robert A. Anderson	Trustee	November 1, 2014
Todd R. Steigerwaldt	General Manager	Indefinite
	(After January 1, 2011)	
Robert A. Anderson	Chairperson	November 1, 2014
Mary Ann McComas	Trustee	November 1, 2012
Gregory O. Hapgood	Trustee	November 1, 2016
Todd R. Steigerwaldt	General Manager	Indefinite

HOGAN • HANSEN
A Professional Corporation
Certified Public Accountants and Consultants

Independent Auditor's Report

To the Board of Trustees
Marion Water Department
Marion, Iowa

We have audited the accompanying financial statements of the Marion Water Department, a component unit of the City of Marion, Iowa, at June 30, 2011 which collectively comprise the Marion Water Department's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the Marion Water Department's 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, 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.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Marion Water Department at June 30, 2011, and the results of its operations and 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 January 20, 2012 on our consideration of the Department's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations and contracts. 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 on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

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The accompanying Management's Discussion and Analysis and schedule of funding progress for the retiree health plan on pages 4 through 7 and 21 are not required parts of the basic financial statements but are supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted primarily of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

HOGAN - HANSEN

HOGAN - HANSEN

Cedar Rapids, Iowa
January 20, 2012

Management's Discussion and Analysis

As management of the Marion Water Department, we offer readers of the Department's financial statements this narrative and analysis of the financial statements of the Marion Water Department for the fiscal year ended June 30, 2011, with a comparison to the prior fiscal year's results. We encourage readers to consider this information in conjunction with the Department's financial statements which follow.

FINANCIAL HIGHLIGHTS

The assets of the Marion Water Department exceeded its liabilities at the close of June 30, 2011 by $14,453,208 (net assets). Of this amount, $1,979,685 (unrestricted net assets) may be used to meet the Department's ongoing obligations to citizens and creditors.

The Department's net assets increased by $1,297,282 for the year ended June 30, 2011.

The Water Department had debt obligations of $3,500,000 at June 30, 2011 resulting from amounts drawn down on a $3,500,000 SRF construction loan during the year.

OVERVIEW OF THE FINANCIAL STATEMENTS

This discussion and analysis is intended to serve as an introduction to the Marion Water Department's basic financial statements. The Department is a single-purpose enterprise component unit of the City of Marion, Iowa. The Department provides water to its customers at rates designed to recover the cost of providing the water, including costs associated with installation and maintenance of water pumping, storage and transmission systems. The Department also bills customers for sewer and garbage charges for the City of Marion. The Department remits all sewer and garbage fees collected to the City of Marion and charges the City an administrative fee for performing this service. As a result, the Department prepares financial statements in a manner similar to a private-sector business.

The statement of net assets presents information on all of the Department’s assets and liabilities, with the difference between the two reported as net assets. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of the Department is improving or deteriorating.

The statement of revenue, expenses and changes in net assets presents information showing how the Department’s net assets changed during the year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of the related cash flows. Thus, revenue and expenses are reported in this statement for some transactions that will result in cash flows in the following year.

The statement of cash flows presents information showing major sources and uses of cash by four types of activities. The activities are operating; noncapital financing; capital and related financing; and investing. Also included is a schedule which reconciles income from operations to net cash provided by operating activities.

The basic financial statements can be found on pages 8 through 10 of this report.

The notes to the financial statements provide additional information that is essential to a full understanding of the data provided in the basic financial statements. Notes are considered to be an integral part of financial statements prepared in accordance with generally accepted accounting principles. The notes to the financial statements can be found on pages 11 through 20 of this report.

FINANCIAL ANALYSIS

Statements of Net Assets

This section discusses and analyzes significant differences between this and the prior fiscal year. The following is a summary of the composition of net assets at June 30:

	2011	**2010**
Cash and cash equivalents	$ 3,634,518	$ 1,773,487
Other assets	695,921	395,114
Capital assets	14,474,874	11,430,136
Total Assets	**18,805,313**	**13,598,737**
Current liabilities	892,205	194,482
Long-term liabilities	3,459,900	248,329
Total Liabilities	**4,352,105**	**442,811**
Net Assets		
Invested in capital assets, net of debt	12,473,523	11,340,536
Unrestricted	1,979,685	1,815,390
Total Net Assets	**$ 14,453,208**	**$ 13,155,926**

Net assets invested in capital assets are by far the largest portion of the Department's net assets, 86% at June 30, 2011, and reflect its net investment in capital assets (e.g., land, water plant distribution system and equipment). The Utility uses these capital assets to provide water and services to the citizens; consequently, these assets are not available for future spending.

Unrestricted net assets may be used to meet the Department's ongoing obligations to citizens and creditors. It is the Department's intention to use these assets for future operating purposes and capital asset acquisition and improvements.

Net assets increased mainly due to capital contributions of new subdivisions totaling $474,736 for the fiscal year 2011 as well as an increase in water sales resulting from a rate increase and increased usage. At both June 30, 2011 and 2010, the Department reported positive balances in all categories of net assets.

Governmental activities. Since the Department is a single-purpose enterprise, it has no activities classified as "governmental".

Statement of Revenue, Expenses and Changes in Net Assets

The following is a summary of the changes in net assets for the years ended June 30:

	2011	2010
Operating revenue	$ 3,036,161	$ 2,322,105
Operating expenses	2,196,502	2,160,510
Net Operating Income (Loss)	839,659	161,595
Net nonoperating revenue	27,887	40,858
Net capital contributions	429,736	438,300
Changes in Net Assets	1,297,282	640,753
Net Assets - Beginning of Year	13,155,926	12,515,173
Net Assets - End of Year	**$ 14,453,208**	**$ 13,155,926**

Operating revenue is the Department's primary source of revenue and is generated from water sales and other services to customers. For 2011, operating revenue increased $714,056 from 2010.

Operating expenses totaled $2,196,502 for 2011, a $35,992 increase from 2010. These expenses represent the Department's costs to provide water and services to customers. Operating expenses included depreciation expense of $403,459 and $357,362 for the years ended June 30, 2011 and 2010, respectively.

Net nonoperating revenue includes interest income, insurance recoveries, rent from leasing space and debt service payments. Net nonoperating revenue decreased by $12,971 between 2011 and 2010. The decrease was due mainly to a decrease in interest income as well as debt service payments for the SRF construction loan paid during the year.

Capital contributions of $474,736 were received from contractors due to subdivision development. The Department also transferred $45,000 of land to the City of Marion that it purchased during the year which will be used for a future well site.

BUDGETARY HIGHLIGHTS

Each year, the City Council adopts a budget using the cash basis of accounting which differs from the accrual basis of accounting used for the accompanying financial statements. The Department's budget is included in the total business-type activities budget of the City.

CAPITAL ASSETS AND LONG-TERM DEBT

The Department's investment in capital assets amounted to approximately $14.5 million and $11.4 million at June 30, 2011 and 2010, respectively, (net of accumulated depreciation of approximately $3.8 million and $3.4 million at June 30, 2011 and 2010, respectively). This investment in capital assets includes land, construction in progress, buildings, wells and towers, distribution system, equipment and vehicles.
The following is a summary of the capital assets, at cost, at June 30:

	2011	2010
Land	$ 429,126	$ 429,126
Construction in progress	2,511,719	124,180
Building, wells and towers	2,026,926	2,018,976
Distribution system	12,680,054	11,832,885
Equipment and vehicles	650,358	444,819
Accumulated depreciation	(3,823,309)	(3,419,850)
Total	**$ 14,474,874**	**$ 11,430,136**

The following table reconciles the change in capital assets:

	2011	2010
Beginning balance	$ 11,430,136	$ 10,660,743
Additions	1,105,658	1,021,716
Retirements - net of depreciation	—	(14,436)
Transfer of capital assets	(45,000)	—
Depreciation	(403,459)	(357,362)
Construction in progress	2,387,539	119,475
Ending Balance	**$ 14,474,874**	**$ 11,430,136**

Long-Term Debt

At June 30, 2011, the Department had a $3,500,000 note outstanding, compared to $89,600 last year, as shown below.

Outstanding Debt at Year End

	June 30,	
	2011	2010
SRF Loan Payable	**$ 3,500,000**	**$ 89,600**

Debt increased as a result of obtaining an SRF construction loan to finance costs of constructing improvements to the Municipal Waterworks System.

ECONOMIC FACTORS

The unemployment rate for Linn County at June 30, 2011 was 6%, which is where it was the previous year and less than the national unemployment rate of 9%.

Retail sales are also reported on a fiscal year, April 1 to March 31, basis. For fiscal year 2010 (April 1, 2009 to March 31,2010), retail sales were $333.3 million for Marion and $3.204 billion for Linn County. For fiscal year 2009, retail sales were $351.8 million for Marion and $3.487 billion for Linn County.

The total value of building permits for fiscal year 2011 was approximately $37.7 million, which is down from the fiscal year 2010 amount of $62.8 million. In fiscal year 2010, there was the construction of a middle school and athletic facilities for the two local school districts as well as some larger commercial projects. There were no such type large projects in fiscal year 2011.

NEXT YEAR'S BUDGET AND RATES

The Marion Water Board of Trustees has established a FY 2011-12 budget with no adjustment in water rates and $2.50 increase in monthly meter service charge. The Board of Trustees, under provisions of Section 388 of the Code of Iowa, establishes and approves the budget for the Department. As a component unit of the City of Marion, the Department's budget is filed for record as part of the City of Marion's budget.

FINANCIAL INFORMATION CONTACT

The Department's financial statements are designed to present users (citizens, customers and prospective customers) with a general overview of the Department's finances and to demonstrate the Department's accountability. If you have questions about the report or need additional financial information, please contact the Marion Water Department General Manager, City Hall, 1225 - 6th Avenue, Suite 150, Marion, Iowa 52302.

Basic Financial Statements

Statement of Net Assets

At June 30, 2011

Assets	
Current Assets	
Cash and cash equivalents	$ 2,030,504
Receivables (net of allowance for uncollectible amounts)	
Trade accounts	153,828
Accrued interest	1,498
Unbilled revenue	325,491
Inventories	181,854
Total Current Assets	**2,693,175**
Restricted Assets	
Bond issuance costs (net of accumulated amortization - $1,750)	**33,250**
Capital Assets	
Land	429,126
Construction in progress	2,511,719
Buildings, wells and towers	2,026,926
Distribution system	12,680,054
Equipment and vehicles	650,358
Totals	18,298,183
Less accumulated depreciation	(3,823,309)
Total Capital Assets	**14,474,874**
Restricted Assets	
Cash - customer deposits	105,365
Cash equivalents - loan proceeds restricted for capital projects	1,498,649
Total Restricted Assets	**1,604,014**
Total Assets	**$ 18,805,313**
Liabilities and Net Assets	
Current Liabilities	
Accounts payable	$ 554,811
Self-insured premiums and estimated claims	20,244
Accrued interest	5,610
Accrued expenses	33,525
Compensated absences	45,650
Current maturities of SRF loan payable	127,000
Total Current Liabilities	**786,840**
Liabilities Payable From Restricted Assets - Customer Deposits	**105,365**
Long-Term Liabilities	
SRF loan payable	3,373,000
Net OPEB liability	86,900
Total Long-Term Liabilities	**3,459,900**
Total Liabilities	**4,352,105**
Net Assets	
Invested in capital assets, net of related debt	12,473,523
Unrestricted	1,979,685
Total Net Assets	**14,453,208**
Total Liabilities and Net Assets	**$ 18,805,313**

Statement of Revenue, Expenses and Changes in Net Assets

Year Ended June 30, 2011

Operating Revenue	
Water sales	$ 2,614,917
Billing and collection fees	88,002
Other sales and services	302,207
Miscellaneous	31,035
Total Operating Revenue	**3,036,161**
Operating Expenses	
Salaries and benefits	940,001
Contractual services	727,586
Commodities	119,734
Depreciation	403,459
Other	5,722
Total Operating Expenses	**2,196,502**
Operating Income	**839,659**
Nonoperating Revenue (Expenses)	
Interest income	24,271
Insurance recoveries	47,776
Lease and rental fees, net of expense	12,973
Interest expense	(46,633)
Amortization of bond issue costs	(1,750)
Loan servicing fee	(8,750)
Total Nonoperating Revenue	**27,887**
Change in Net Assets Before Contributions	**867,546**
Capital contributions	474,736
Capital contributions to primary government	(45,000)
Change in Net Assets	**1,297,282**
Net Assets - Beginning of Year	13,155,926
Net Assets - End of Year	**$ 14,453,208**

See accompanying notes to the financial statements.

Statement of Cash Flows

Year Ended June 30, 2011

Cash Flows From Operating Activities	
Cash received from customers	$ 2,886,364
Cash collected on behalf of primary government	4,738,296
Cash paid to primary government	(4,738,296)
Cash paid to employees	(908,013)
Cash paid to suppliers	(899,969)
Net Cash Provided by Operating Activities	**1,078,382**
Cash Flows From Noncapital Financing Activities	
Lease and rental fees received	**12,973**
Cash Flows From Capital and Related Financing Activities	
Acquisition of capital assets	(2,626,500)
Insurance recoveries	47,776
Proceeds from long-term borrowing	3,531,400
Repayment of long-term debt	(121,000)
Interest paid on SRF loan	(41,023)
Bond issue costs and fees paid	(43,750)
Net Cash Provided by Capital and Related Financing Activities	**746,903**
Cash Flows From Investing Activities	
Interest received on savings and certificates of deposit	**22,773**
Net Increase in Cash	**1,861,031**
Cash - Beginning of Year	1,773,487
Cash - End of Year	**$ 3,634,518**
Reconciliation of Operating Income to Net Cash Provided by Operating Activities	
Operating income	$ 839,659
Adjustments to Reconcile Operating Income to Net Cash Provided by Operating Activities	
Depreciation	403,459
Increase in trade accounts and unbilled revenue receivable	(152,146)
Increase in inventories	(113,913)
Increase in accounts payable	66,986
Increase in accrued expenses	31,988
Increase in liabilities payable from restricted assets	2,349
Net Cash Provided by Operating Activities	**$ 1,078,382**
Reconciliation of Cash to Specific Assets Included on the Balance Sheet	
Cash and cash equivalents	$ 2,030,504
Restricted cash	1,604,014
	$ 3,634,518

See accompanying notes to the financial statements.

(1) Summary of Significant Accounting Policies and Other Matters

Reporting Entity

The Marion Water Department (Department) is a municipal utility that is a political subdivision and component unit of the City of Marion, Iowa, located in Linn County. The Department provides water to customers within the City. The Department is governed by a Board of Trustees appointed by the City of Marion, Iowa, City Council and is managed by an administrator. All activities with which the Board has oversight responsibility are included in the financial statements. These financial statements of the Department are presented in accordance with accounting principles generally accepted in the United States of America as prescribed by the Governmental Accounting Standards Board (GASB).

Measurement Focus and Basis of Accounting

The Department is accounted for on the flow of economic resources measurement focus and uses the accrual basis of accounting. Under this method, revenue is recorded when earned and expenses are recorded when incurred.

The Department applies all applicable GASB pronouncements, as well as the following pronouncements unless these pronouncements conflict with or contradict GASB pronouncements: Financial Accounting Standards Board Statements and Interpretations, Accounting Principles Board Opinions and Accounting Research Bulletins of the Committee on Accounting Procedure.

The Department distinguishes operating revenue and expenses from nonoperating items. Operating revenue and expenses generally result from providing services and producing and delivering goods in connection with the Department’s principal ongoing operations. All revenue and expenses not meeting this definition are reported as nonoperating revenue and expenses.

Use of Estimates

Management uses estimates and assumptions in preparing financial statements. Those estimates and assumptions affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities and the reported revenue and expenses.

Trade Accounts Receivable

Utility sales are billed bimonthly. Payment is due within 20 days of billing. After proper notice, unless other arrangements are made by the customer, service may be discontinued to customers with unpaid bills 30 days or more past due. Uncollected accounts are normally written off against water sales after 90 days. Historically, account balances written off have not been material. Department management estimates that all trade accounts receivable as shown on the balance sheet will be collectible.

Unbilled Revenue Receivable

Sales of water used from the time of the last meter reading prior to June 30 that have not been billed and the resulting receivable is not included in trade receivables. The Department estimates unbilled revenue based on the proportion of unbilled days in June to the number of days in the billing period times the amount billed in July. The result is reported as unbilled revenue receivable.

(1) Summary of Significant Accounting Policies and Other Matters

The following accounting policies are followed in preparing the financial statements:

Cash - For purposes of the statement of cash flows, the Department considers all highly liquid debt instruments purchased with original maturities of three months or less to be cash equivalents.

Inventories - Inventories are valued at cost using the first-in/first-out method and consist of materials and supplies. Inventories are recorded as expenses when consumed rather than when purchased.

Restricted Assets - Restricted assets are customer deposits restricted for application to unpaid customer accounts or for refund to customers.

Capital Assets - Capital assets consist of property, equipment and vehicles and infrastructure assets (e.g. buildings, wells, towers and distribution system which are immovable and of value only to the Department). Capital assets are recorded at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at estimated fair value at the date of donation. The costs of normal maintenance and repair not adding to the value of the asset or materially extending asset lives are not capitalized. Reportable capital assets are defined by the Department as assets with initial, individual costs in excess of $5,000.

Capital assets of the Department are depreciated using the straight-line method over the following estimated useful lives.

Asset Class	Estimated Useful Lives
Buildings, wells and towers...	10 - 40 Years
Distribution system..	5 - 50 Years
Equipment and vehicles..	5 - 10 Years

Compensated Absences - Department employees accumulate a limited amount of earned but unused vacation hours for subsequent use or for payment upon termination, death or retirement. In addition, Department employees who elect an early separation agreement at retirement may receive the benefits outlined as follows: three and one-half months of salary as well as the equivalent of two years of health insurance coverage paid by the Department.

Operating Revenue - The Department defines operating revenue as revenue derived from the sale of water billing and collection fees and other sales and services provided to customers. Nonoperating revenue is defined as anything other than revenue from the sale of water.

Budgeting - The Department's budget is included as part of the City's budget and is prepared on the cash basis of accounting. Disbursements are for legal budget compliance, combined for all City proprietary activities. Budget amounts for capital outlay, debt service and transfers out are presented on a combined basis only. The Utility's budget and comparison to cash basis activity is as follows:

Business-Type Activity - Water	
Actual disbursements..	$ 2,298,635
Budgeted disbursements	5,444,289
Actual Disbursements Under Budget	**$ (3,145,654)**

(1) Summary of Significant Accounting Policies and Other Matters

Restricted Resources - The Department first applies restricted resources when an expense is incurred for purposes for which both restricted and unrestricted net assets are available. Unrestricted resources are used once the restricted resources have been depleted.

(2) Cash Flow Statement Supplementary Information

Schedule of Noncash Investing and Financing Activities

Amortization of Bond Issue Costs	**$ 1,750**
Cost of capital asset acquisitions	$ 3,493,197
Amounts payable - current year	(391,961)
Contributed capital	(474,736)
Cash Paid for Acquisition of Capital Assets	**$ 2,626,500**
Contribution of Capital Asset to Primary Government	**$ 45,000**

(3) Deposits and Investments

The Department's deposits are 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 Department 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 Board of Trustees 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.

The Department had no investments meeting the disclosure requirements of GASB Statement No. 3, as amended by Statement No. 40.

(4) Restricted Assets

Restricted assets represent monies set aside to provide security for deposits and advances. At June 30, 2011, $105,365 of cash was restricted for customer deposits or for refunds to customers.

(5) Capital Assets

Capital asset activity for the year was as follows:

	Balance Beginning of Year	Increases	Decreases	Balance End of Year
Business-Type Activities				
Capital Assets Not Being Depreciated				
Land	$ 429,126	$ 45,000	$ 45,000	$ 429,126
Construction in progress	124,180	2,387,539	—	2,511,719
Total Capital Assets Not Being Depreciated	553,306	2,432,539	45,000	2,940,845
Capital Assets Being Depreciated				
Buildings, wells and towers	2,018,976	7,950	—	2,026,926
Distribution system	11,832,885	847,169	—	12,680,054
Equipment and vehicles	444,819	205,539	—	650,358
Total Capital Assets Being Depreciated	14,296,680	1,060,658	—	15,357,338
Less Accumulated Depreciation for				
Buildings, wells and towers	817,021	42,982	—	860,003
Distribution system	2,375,016	304,429	—	2,679,445
Equipment	227,813	56,048	—	283,861
Total Accumulated Depreciation	3,419,850	403,459	—	3,823,309
Net Capital Assets Being Depreciated	10,876,830	657,199	—	11,534,029
Net Capital Assets	**$ 11,430,136**	**$ 3,089,738**	**$ 45,000**	**$ 14,474,874**

(6) Long-Term Liabilities

A summary of changes in long-term liabilities for the year ended June 30, 2011 is as follows:

	Balance Beginning of Year	Increases	Decreases	Balance End of Year	Due Within One Year	Interest Rate
SRF loan payable - planning and design	$ 89,600	$ 31,400	$ 121,000	$ —	$ —	0.0%
SRF loan payable - construction	—	3,500,000	—	3,500,000	127,000	3.0
Net OPEB liability	55,713	31,187	—	86,900	—	N/A
Total	**$ 145,313**	**$ 3,562,587**	**$ 121,000**	**$ 3,586,900**	**$ 127,000**	

(6) Long-Term Liabilities

SRF Loan Payable

In August, 2009, the Department obtained a $150,750 State Revolving Fund Planning and Design Loan from the Iowa Finance Authority for the purpose of paying the costs of planning and designing improvements to the Municipal Waterworks System. The loan was interest free and payable in full in August, 2012.

In October, 2010, the Department, through the City of Marion, issued water revenue bonds (Build America Bonds) in the amount of $3.5 million to repay the planning loan and fund the remaining costs of the planning and designing and constructing improvements and extensions to the Municipal Waterworks System. In December, 2010, the Build America Bond agreement was to draw all remaining funds and place them in the custody of an escrow agent.

The loan bears interest at 3%, of which 1.05% is reimbursed to the Department through the Build America Bond program. The agreement also requires the Department to annually pay a 0.25% servicing fee on the outstanding principal balance. At June 30, 2011, of the $3,500,000 authorized, the Department had received $2,001,351, which includes a $35,000 loan initiation fee and $121,000 to payoff the planning and design loan. The remaining balance of $1,498,649 is being held in trust, and the Department will request the remaining funds as the project progresses.

The loan is payable in semiannual installments and is payable in full in June, 2031; however, the repayment schedule has not been finalized since the Department has not fully completed the project. Annual principal and interest payments on the bonds are expected to be paid from net receipts. Total principal and interest remaining to be paid on the bonds is $4,288,814. For the current year, interest paid and total customer net receipts were $46,633 and $1,243,118, respectively. No principal was paid during the year ended June 30, 2011.

The resolution providing for the issuance of the water revenue bonds (Build America Bonds) includes the following provisions:

a. The bond is payable from the net revenue of the Utility.

b. Produce and maintain net revenue at a level not less than 110% of the amount of principal and interest due during the fiscal year.

c. Sufficient monthly transfers shall be made to the water revenue bond sinking fund for the purpose of making principal and interest payments when due.

(6) Long-Term Liabilities

Annual debt service requirements to maturity for the water revenue bonds at June 30, 2011 are as follows:

	Principal	Net Interest (After Build America Bond Reimburse-ment - 1.05%)
Year Ending June 30,		
2012	$ 127,000	$ 68,250
2013	131,000	65,774
2014	135,000	63,219
2015	140,000	60,587
2016	144,000	57,857
2017-2021	795,000	245,213
2022-2026	933,000	162,494
2027-2031	1,095,000	65,420
Total	**$ 3,500,000**	**$ 788,814**

(7) Retirement Plan

Plan Description

The Department 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 4.5% of their annual salary and the employer is required to contribute 6.95% of annual covered payroll. Contribution requirements are established by state statute. The Utility’s contribution to IPERS for the years ended June 30, 2011, 2010 and 2009 were $52,456, $49,471 and $46,586, respectively, equal to the required contributions for each year.

Deferred Compensation Plan

The Department offers its employees a deferred compensation plan under Internal Revenue Code Section 457. The plan allows Department employees to defer a portion of their current salary until future years. The employee becomes eligible to withdraw funds upon termination, retirement, death or unforeseeable emergency.

The Department deposits all amounts of compensation deferred under the plan to the fiduciary designated by the employee.

(8) Other Postemployment Benefits (OPEB)

Plan Description
The Department operates a single-employer retiree benefit plan which provides medical/prescription drug benefits for retirees and their spouses in combination with the City of Marion. There are 12 active and 3 retired department members in the plan. Participants must be age 55 or older at retirement.

The medical/prescription drug coverage is provided through a fully insured plan with Wellmark. Retirees under age 65 pay the same premium for the medical/prescription drug benefit as active employees, which results in an implicit subsidy and an OPEB liability.

Funding Policy
The contribution requirements of plan members are established and may be amended by the Department. The Department currently finances the retiree benefit plan on a pay-as-you-go basis.

Annual OPEB Cost and Net OPEB Obligation
The Department's annual OPEB cost is calculated based on the annual required contribution (ARC), an amount actuarially determined in accordance with GASB Statement No. 45. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and amortize any unfunded actuarial liabilities over a period not to exceed 30 years.

The following table shows the components of the Department's share of annual OPEB cost for June 30, 2011, the amount actually contributed to the plan and changes in the Department's share of net OPEB obligation:

Annual required contribution	$ 32,367
Interest on net OPEB obligation	1,420
Adjustment to annual required contribution	(2,600)
Annual OPEB Cost	31,187
Contributions made	—
Increase in Net OPEB Obligation	31,187
Net OPEB Obligation - Beginning of Year	55,713
Net OPEB Obligation - End of Year	**$ 86,900**

For calculation of the net OPEB obligation, the actuary has set the transition day as July 1, 2008. The end-of-year net OPEB obligation was calculated by the actuary as the cumulative difference between the actuarially determined funding requirements and the actual contributions for the year ended June 30, 2011.

The Department's share of the annual OPEB cost, the percentage of annual OPEB cost contributed to the plan and the net OPEB obligation are summarized as follows:

Year Ended June 30,	Annual OPEB Cost	Percentage of Annual OPEB Cost Contributed	Net OPEB Obligation
2009	$ 28,161	0%	$ 28,161
2010	27,552	0	55,713
2011	31,187	0	86,900

(8) Other Postemployment Benefits (OPEB)

Funded Status and Funding Progress

As of July 1, 2010, the most recent actuarial valuation date for the period of July 1, 2010 through June 30, 2011, the actuarial accrued liability was $309,000, with no actuarial value of assets, resulting in an unfunded actuarial accrued liability (UAAL) of $309,000. The covered payroll (annual payroll of active employees covered by the plan) was approximately $777,000, and the ratio of the UAAL to the covered payroll was 40%. As of June 30, 2011, there were no trust fund assets.

Actuarial Methods and Assumptions

Actuarial valuations of an ongoing plan involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality and the healthcare cost trend. Actuarially determined amounts are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future. The schedule of funding progress, presented as required supplementary information in the section following the Notes to Financial Statements, will present multiyear trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liabilities for benefits.

Projections of benefits for financial reporting purposes are based on the plan as understood by the employer and the plan members and include the types of benefits provided at the time of each valuation and the historical pattern of sharing of benefit costs between the employer and plan members to that point. The actuarial methods and assumptions used include techniques that are designed to reduce the effects of short-term volatility in actuarial accrued liabilities and the actuarial value of assets, consistent with the long-term perspective of the calculations.

As of the July 1, 2010 actuarial valuation date, the frozen entry age actuarial cost method was used. The actuarial assumptions includes a 2.5% discount rate based on the Department’s funding policy. The projected annual health cost trend rate is 6%.

Mortality rates are from the 94 Group Annuity Mortality Table Projected to 2000, applied on a gender-specific basis. Annual retirement was assumed at the rate of retirement by attained age after becoming eligible to retire and continue health coverage and termination probabilities were assumed at a modest rate for active employees while no turnover was assumed after the benefit start date.

The UAAL is being amortized as a level percentage of projected payroll expense on an open basis over 30 years.

(9) Compensated Absences

Department employees accumulate vacation and sick leave hours for subsequent use or, in the case of the accumulated vacation pay, for payment upon termination, retirement or death. The accumulations are not recognized as disbursements by the Department until used or paid in its cash basis records. The Department's liability for earned compensated absences payable to employees as accrued to the GAAP basis financial statements at June 30, 2011 was as follows:

Type of Benefit	Amount
Vacation..	$ 45,650

This liability has been computed based on rates of pay and rates for payroll taxes and IPERS as of June 30, 2011. Sick leave is payable when used. No amounts of sick leave were accrued at June 30, 2011.

(10) Related Party Transactions

The Department bills and collects for sewer and garbage services provided for the City of Marion to its residents. During the year ended June 30, 2011, the Department collected and remitted to the City of Marion $3,403,805 for sewer and $1,334,491 for garbage service. Fees earned by the Department from the City of Marion during the year for this service totaled $88,002, of which $7,226 was receivable at June 30, 2011.

(11) Local Government Risk Pool

Health Insurance

The Department has chosen to participate in the City of Marion’s risk financing program for risks associated with the employee's health insurance plan. The Department self-funds health insurance claims arising from the Department's employees to a stop-loss insured amount of $30,000 per participant and a 125% aggregate stop-loss amount based on the "pure premiums" amount multiplied by the number of single and family contracts covered during the contract year. The total cost of these benefits is transferred from the Water Fund based upon the number of employees and the type of plan (single or family) chosen by the employee. Amounts charged are approximately $350 per month single and $874 per month family which is an amount based on past claim history. The amount transferred will be adjusted over a reasonable period of time so that the Medical Benefits Fund receipts and disbursements are approximately equal. Claims paid totaled $104,248 during the year ended June 30, 2011. At June 30, 2011, the Department's share of estimated claims incurred but unpaid was approximately $16,300 based upon an actuarial determination.

Iowa Municipalities Workers' Compensation Association

The Department obtains its workers' compensation coverage through the City of Marion, which is a member in the Iowa Municipal Workers' Compensation Association (IMWCA). The Association is a local government risk-sharing pool whose approximately 500 members include various municipal and county governments throughout the State of Iowa. The Pool was formed in July, 1981 to formulate, develop and

(11) Local Government Risk Pool

administer, on behalf of the member governments, a program of joint self-insurance to stabilize costs related to members' workers' compensation liabilities. Program components include claims management, member education and loss control services. There have been no reductions in insurance coverage from prior years.

Each member pays annual premiums determined by using applicable standard rates for the exposure to risk and applicable experience modification factors of the National Council on Compensation Insurance. Each member may be subject to additional premiums to pay its pro rata share of claims which exceeds the Association's resources available to pay such claims. A distribution to members may also be made if the Association has excess monies remaining after payment of claims and expenses.

The Department's premium contributions to the Association are recorded as expenditures from its operating funds at the time of payment to the risk pool. Premiums paid to the Association for the year ended June 30, 2011 were $12,387.

The Association uses reinsurance and excess risk-sharing agreements to reduce its exposure to large losses. Claims exceeding $750,000 are reinsured in an amount not to exceed $2,000,000 per occurrence.

Members may withdraw from the Association at any time provided they provide assets for settlement of all pending claims.

(12) Risk Management

The Department is exposed to various risks of loss related to torts; theft; damage to and destruction of assets; errors and omissions; injuries to employees; and natural disasters. These risks are covered by the purchase of commercial insurance. Settled claims from these risks have not exceeded commercial insurance coverage in the past fiscal year.

(13) Commitments

Construction

The Department is involved in construction of capital assets and agreements to purchase capital assets. At June 30, 2011, the Department was committed to approximately $1,100,000 in construction and purchase agreements.

(14) Subsequent Events

Management has evaluated subsequent events through January 20, 2011, the date which the financial statements were available to be issued.

Subsequent to June 30, 2011, the Department entered into various agreements to purchase capital assets totaling approximately $10,000.

Required Supplementary Information

Schedule of Funding Progress for the Retiree Health Plan

Year Ended June 30,	Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) (b)	Unfunded AAL (UAAL) (b-a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll [(b-a)/c]
2009	7-1-08	$ —	$ 293,077	$ 293,077	0%	$ 771,000	38%
2010	7-1-08	—	293,077	293,077	0	752,000	39
2011	7-1-10	—	309,000	309,000	0	777,000	40

See Note 8 in the accompanying Notes to the Financial Statements for the plan description, funding policy, annual OPEB cost and net OPEB obligation, funded status and funding progress.

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

To the Board of Trustees
Marion Water Department
Marion, Iowa

We have audited the accompanying financial statements of the Marion Water Department, as of and for the year ended June 30, 2011, and have issued our report thereon dated January 20, 2012. 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 Department's 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 our opinion on the effectiveness of the internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Department'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 was not designed to identify all deficiencies in internal control over financial reporting 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 described in the accompanying schedule of findings, we identified certain deficiencies in internal control over financial reporting we consider to be material weaknesses.

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 a material misstatement of the Marion Water Department's financial statements will not be prevented or detected and corrected on a timely basis. We consider the deficiencies in internal control described in Part I of the accompanying schedule of findings as Items 11-IC-1, 11-IC-2, 11-IC-3 and 11-IC-4 to be material weaknesses.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Department's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations and contracts, 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*.

Comments involving statutory and other legal matters about the Department's operations for the year ended June 30, 2011 are based exclusively on knowledge obtained from procedures performed during our audit of the financial statements of the Department. 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.

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

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

Hogan - Hansen

HOGAN - HANSEN

Cedar Rapids, Iowa
January 20, 2012

Part I: Findings Related to the Financial Statements

11-IC-1 Segregation of Duties

Prior Year Finding and Recommendation - One important aspect of internal control is the segregation of duties among employees to prevent an individual employee from handling duties which are incompatible. We noted that certain functions are not entirely segregated.

With a limited number of office employees, segregation of duties is difficult. However, the Department management should review its control procedures to obtain the maximum internal control possible under the circumstances, segregate duties to the extent possible with existing personnel and utilize administrative personnel to provide additional control through review of financial transactions and reports.

Current Year Finding - We found the same condition existed. We reiterate our prior year recommendation.

Department's and City's Response - The City Council and Board of Trustees are aware of the condition. We will review procedures and make changes when appropriate.

Auditor's Conclusion - Response accepted.

11-IC-2 Financial Statement Preparation

Prior Year Finding and Recommendation - The Department does not have a system of internal controls that fully prepares financial statements and disclosures that are fairly presented in conformity with generally accepted accounting principles. As is inherent in many organizations of this size, the Department has management and employees who, while knowledgeable and skillful, do not have the time to maintain the current knowledge and expertise to fully apply generally accepted accounting principles in preparing the financial statements and the related disclosures. The Department should obtain additional knowledge through reading relevant accounting literature and attending local professional education courses.

Current Year Finding - We found the same condition existed. We reiterate our prior year recommendation.

Department's Response - The Department is aware of the condition and will consider obtaining additional knowledge where cost effective but will continue to rely on its audit firm for assistance with drafting the financial statements and disclosures.

Auditor's Conclusion - Response accepted.

11-IC-3 Capitalization of Assets

Finding - Through our testing of inventory and fixed assets, we noted that the Department had capitalized fire hydrants which were still in inventory.

Auditor's Recommendation - The Department should only capitalize assets that have been placed in service. A spreadsheet would be a useful tool and can be updated throughout the year and then used to update the fixed asset listing once the asset has been placed in service.

Department's Response - The Department will consider a process to track the assets on a spreadsheet as they are placed in service and only capitalize those that were placed in service during the year.

Auditor's Conclusion - Response accepted.

11-IC-4 Recording of SRF Loan Proceeds and Escrow Account

Finding - Through our testing of cash and loans payable, we noted the Department had not recorded proceeds of the SRF loan that were held in escrow at Wells Fargo.

Auditor's Recommendation - The Department should implement procedures to ensure all assets and liabilities of the Department are recorded in the Department's accounting system.

Department's Response - The Department will review its internal controls and make changes to ensure that all assets and liabilities are identified and recorded in a timely manner.

Auditor's Conclusion - Response accepted.

Part II: Compliance and Other Matters

11-C-1 Budget - Operating cash disbursements during the year ended June 30, 2011 did not exceed the amounts budgeted.

11-C-2 Questionable Disbursements - We noted no disbursements that may not meet the requirements of public purpose as defined in an Attorney General's opinion dated April 25, 1979.

11-C-3 Travel Expense - No disbursements of Department money for travel expenses of spouses of the Department officials or employees were noted.

11-C-4 Business Transactions - No business transactions between the Department's officials or employees and the Department were noted.

11-C-5 Bond Coverage - Surety bond coverage of Department officials and employees is in accordance with statutory provisions. The amount of coverage should be reviewed annually to ensure that the coverage is adequate for current operations.

11-C-6 Board of Trustee Minutes - No transactions were found that we believe should have been approved in the Trustee minutes that were not.

11-C-7 Deposits and Investments - No instances of noncompliance with the deposit and investment provisions of Chapters 12B and 12C of the Code of Iowa and the Department's investment policy were noted.

11-C-8 Revenue Bonds - The provisions of the water revenue bonds (Build America Bonds) require the Department to establish an account to be known as the “Water Revenue Bond Sinking Fund” which requires monthly amounts be set aside equal to 1/6th of the installment of interest coming due on the next succeeding interest installment date and an amount equal to 1/12th of the installment of principal coming due on such bonds on the next succeeding principal payment date until the full amount of such installment is on deposit in the sinking fund.

The Department failed to make these monthly transfers.

Auditor’s Recommendation - The Department should make monthly transfers to the sinking fund.

Department’s Response - The Department will make transfers in accordance with the loan agreement.

Auditor’s Conclusion - Response accepted.