

City of Morning Sun

**Independent Auditor's Report
Financial Statements and Supplementary Information
Independent Auditor's Report on Internal Control and Compliance
Schedule of Findings and Questioned Costs**

June 30, 2012

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City of Morning Sun

Officials

<u>Name</u>	<u>Title</u>	<u>Term Expires</u>
Bill Minnis	Mayor	December, 2013
Bill Spearman	Mayor Pro-tem	December, 2013
Jerry Malone	Council Member	December, 2013
Barb Pealer	Council Member	December, 2013
Brian Belzer	Council Member	December, 2015
Roger Hobbs	Council Member	December, 2015
Angie Malone	City Clerk	Not Elected
Fran McElhinney	Treasurer	Not Elected



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Independent Auditor's Report

Honorable Mayor and Members of City Council
City of Morning Sun, Iowa

We have audited the accompanying financial statements of the governmental activities, the business type activities, each major fund and the aggregate remaining fund information of the City of Morning Sun, Iowa (City) as of and for the year ended June 30, 2012, which collectively comprise the City's basic financial statements listed in the table of contents. These financial statements are the responsibility of the City's management. Our responsibility is to express opinions 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 our audit provides a reasonable basis for our opinions.

The financial statements referred to above include only the primary government of the City, which consists of all funds, organizations, institutions, agencies, departments and offices that comprise the City's legal entity. The financial statements do not include financial data for the City's separate component unit, which accounting principles generally accepted in the United States of America require to be reported with the financial data of the City's primary government. As a result, the primary government financial statements do not purport to, and do not present fairly the cash basis financial position of the reporting entity of the City as of June 30, 2012, and the changes in its cash basis financial position for the year then ended in conformity with the basis of accounting described in Note 1. Also, as permitted by the Code of Iowa, the accounting records of the City have not been audited for all prior years. Accordingly, we were unable to satisfy ourselves as to the distribution by fund of the total fund balance at July 1, 2011.

In our opinion, except for the effects of such adjustments, if any, as might have been determined to be necessary had we been able to verify the distribution by fund of the total fund balance at July 1, 2011 as discussed in the preceding paragraph, the financial statements referred to above present fairly, in all material respects, the respective cash basis financial position of the governmental activities, the business type activities, each major fund and the aggregate remaining fund information of the City as of June 30, 2012, and the respective changes in cash basis financial position for the year then ended in conformity with the basis of accounting described in Note 1.

In accordance with *Government Auditing Standards*, we have also issued our report dated November 13, 2012 on our consideration of the City's internal control over financial reporting and 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 control over financial reporting or compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the City of Morning Sun's basic financial statements. The supplementary information included in Schedules 1 through 3, is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information is the responsibility of management and was derived from and related directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in our audit of the basic financial statements and, in our opinion, except for the effects of such adjustments, if any, as might have been determined to be necessary had we been able to verify the distribution by fund of the total fund balance at July 1, 2011, as discussed in the third paragraph, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

Our audit was conducted for the purpose of forming opinions on the financial statement that collectively comprise the City's basic financial statements. The budgetary comparison information on pages 15 through 16 is not a required part of the basic financial statements. This information has not been subjected to the auditing procedures applied in the audit of the basic financial statements, and accordingly, we do not express an opinion or provide any assurance on it.

The City has not presented Management's Discussion and Analysis that accounting principles generally accepted in the United States have determined is necessary to supplement, although not required to be part of, the basic financial statements.

CPA Associates PC

November 13, 2012

BASIC FINANCIAL STATEMENTS

City of Morning Sun
Statement of Activities and Net Assets - Cash Basis
As of and for the Year Ended June 30, 2012

	Disbursements	Program Receipts			Net (Disbursements) Receipts and Changes in Cash Basis Net Assets		
		Charges for Services	Operating Grants, Contributions and Restricted Interest	Capital Grants, Contributions and Restricted Interest	Governmental Activities	Business Type Activities	Total
Functions / Programs:							
Governmental activities:							
Public safety	\$ 60,356	\$ 28,185	\$ 3,811	\$ -	\$ (28,360)	\$ -	\$ (28,360)
Public works	96,425	-	79,296	-	(17,129)	-	(17,129)
Culture and recreation	40,404	1,386	1,140	-	(37,878)	-	(37,878)
Community and economic development	200	-	-	-	(200)	-	(200)
General government	137,016	-	-	-	(137,016)	-	(137,016)
Debt service	47,533	-	-	-	(47,533)	-	(47,533)
Capital projects	21,617	-	-	-	(21,617)	-	(21,617)
Total governmental activities	<u>403,551</u>	<u>29,571</u>	<u>84,247</u>	<u>-</u>	<u>(289,733)</u>	<u>-</u>	<u>(289,733)</u>
Business type activities:							
Water	109,848	132,080	-	-	-	22,232	22,232
Gas	248,743	290,453	-	-	-	41,710	41,710
Sewer	58,933	86,191	-	-	-	27,258	27,258
Sanitation	57,123	57,663	-	-	-	540	540
Total business type activities	<u>474,647</u>	<u>566,387</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>91,740</u>	<u>91,740</u>
Total	<u>\$ 878,198</u>	<u>\$ 595,958</u>	<u>\$ 84,247</u>	<u>\$ -</u>	<u>(289,733)</u>	<u>91,740</u>	<u>(197,993)</u>
General Receipts and Transfers:							
Property tax levied for:							
General purposes					144,731	-	144,731
Tax increment financing					71,496	-	71,496
Local option sales tax					44,177	-	44,177
Unrestricted investment earnings					3,557	14	3,571
Miscellaneous					23,059	375	23,434
Total general receipts and transfers					<u>287,020</u>	<u>389</u>	<u>287,409</u>
Change in cash basis net assets					(2,713)	92,129	89,416
Cash basis net assets beginning of year					<u>69,206</u>	<u>434,634</u>	<u>503,840</u>
Cash basis net assets end of year					<u>\$ 66,493</u>	<u>\$ 526,763</u>	<u>\$ 593,256</u>
Cash Basis Net Assets							
Restricted:							
Expendable:							
Tax increment financing					\$ 161,978	\$ -	\$ 161,978
Equipment purposes					-	47,141	47,141
Unrestricted					<u>(95,485)</u>	<u>479,622</u>	<u>384,137</u>
Total cash basis net assets					<u>\$ 66,493</u>	<u>\$ 526,763</u>	<u>\$ 593,256</u>

See notes to financial statements.

City of Morning Sun
Statement of Cash Receipts, Disbursements and Changes in Cash Balances
Governmental Funds
As of and for the Year Ended June 30, 2012

	<u>Special Revenue</u>					<u>Total</u>
	<u>General</u>	<u>Road Use</u>	<u>Urban Renewal Tax Increment</u>	<u>Debt Service</u>	<u>Other Nonmajor Governmental</u>	
Receipts:						
Property tax	\$ 128,441	\$ -	\$ -	\$ 16,290	\$ -	\$ 144,731
Tax increment financing collections	-	-	71,496	-	-	71,496
Other taxes	44,177	-	-	-	-	44,177
Use of money and property	3,491	-	-	65	-	3,556
Licenses and permits	1,665	-	-	-	-	1,665
Intergovernmental	-	79,296	-	-	1,140	80,436
Charges for services	26,520	-	-	-	1,386	27,906
Miscellaneous	15,493	-	-	-	11,378	26,871
Total receipts	<u>219,787</u>	<u>79,296</u>	<u>71,496</u>	<u>16,355</u>	<u>13,904</u>	<u>400,838</u>
Disbursements:						
Operating:						
Public safety	60,356	-	-	-	-	60,356
Public works	11,630	84,795	-	-	-	96,425
Culture and recreation	27,152	-	-	-	13,252	40,404
Community and economic development	200	-	-	-	-	200
General government	137,016	-	-	-	-	137,016
Debt service	-	-	-	47,533	-	47,533
Capital projects	-	-	21,617	-	-	21,617
Total disbursements	<u>236,354</u>	<u>84,795</u>	<u>21,617</u>	<u>47,533</u>	<u>13,252</u>	<u>403,551</u>
Excess (deficiency) of receipts over disbursements	(16,567)	(5,499)	49,879	(31,178)	652	(2,713)
Other financing sources (uses):						
Operating transfers in	-	-	-	21,000	-	21,000
Operating transfers out	-	-	(21,000)	-	-	(21,000)
Net change in cash balances	(16,567)	(5,499)	28,879	(10,178)	652	(2,713)
Cash balances beginning of year	<u>(79,480)</u>	<u>-</u>	<u>133,099</u>	<u>-</u>	<u>15,587</u>	<u>69,206</u>
Cash balances end of year	<u>\$ (96,047)</u>	<u>\$ (5,499)</u>	<u>\$ 161,978</u>	<u>\$ (10,178)</u>	<u>\$ 16,239</u>	<u>\$ 66,493</u>
Cash Basis Fund Balances						
Restricted:						
Tax increment financing	\$ -	\$ -	\$ 161,978	\$ -	\$ -	\$ 161,978
Assigned for:						
Library purposes	-	-	-	-	16,239	16,239
Unassigned	<u>(96,047)</u>	<u>(5,499)</u>	<u>-</u>	<u>(10,178)</u>	<u>-</u>	<u>(111,724)</u>
Total cash basis fund balances	<u>\$ (96,047)</u>	<u>\$ (5,499)</u>	<u>\$ 161,978</u>	<u>\$ (10,178)</u>	<u>\$ 16,239</u>	<u>\$ 66,493</u>

See notes to financial statements.

City of Morning Sun
Statement of Cash Receipts, Disbursements and Changes in Cash Balances
Proprietary Funds
As of and for the Year Ended June 30, 2012

	Enterprise Funds						Total
	Water	Gas	Sewer	Sanitation	Equipment Reserve	Other Nonmajor Proprietary	
Operating Receipts:							
Charges for services	\$ 132,080	\$ 290,453	\$ 86,191	\$ 57,663	\$ -	\$ -	\$ 566,387
Total operating receipts	<u>132,080</u>	<u>290,453</u>	<u>86,191</u>	<u>57,663</u>	<u>-</u>	<u>-</u>	<u>566,387</u>
Operating Disbursements:							
Business type activities	64,647	246,433	55,699	57,123	-	6,500	430,402
Total operating disbursements	<u>64,647</u>	<u>246,433</u>	<u>55,699</u>	<u>57,123</u>	<u>-</u>	<u>6,500</u>	<u>430,402</u>
Excess (deficiency) of operating receipts over (under) operating disbursements	<u>67,433</u>	<u>44,020</u>	<u>30,492</u>	<u>540</u>	<u>-</u>	<u>(6,500)</u>	<u>135,985</u>
Non-operating receipts (disbursements):							
Interest on investments	-	8	6	-	-	-	14
Miscellaneous	-	154	-	-	-	6,721	6,875
Capital projects	(33,212)	(2,310)	(3,234)	-	-	-	(38,756)
Debt service	(11,989)	-	-	-	-	-	(11,989)
Net non-operating receipts (disbursements)	<u>(45,201)</u>	<u>(2,148)</u>	<u>(3,228)</u>	<u>-</u>	<u>-</u>	<u>6,721</u>	<u>(43,856)</u>
Excess (deficiency) of receipts over disbursements	22,232	41,872	27,264	540	-	221	92,129
Non-operating receipts (disbursements)	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
Net change in cash balances	22,232	41,872	27,264	540	-	221	92,129
Cash balances beginning of year	<u>(15,048)</u>	<u>291,566</u>	<u>121,227</u>	<u>(10,252)</u>	<u>47,141</u>	<u>-</u>	<u>434,634</u>
Cash balances end of year	<u>\$ 7,184</u>	<u>\$ 333,438</u>	<u>\$ 148,491</u>	<u>\$ (9,712)</u>	<u>\$ 47,141</u>	<u>\$ 221</u>	<u>\$ 526,763</u>
Cash Basis Fund Balances							
Restricted for equipment purposes	\$ -	\$ -	\$ -	\$ -	\$ 47,141	\$ -	\$ 47,141
Unrestricted	<u>7,184</u>	<u>333,438</u>	<u>148,491</u>	<u>(9,712)</u>	<u>-</u>	<u>221</u>	<u>479,622</u>
Total cash basis fund balances	<u>\$ 7,184</u>	<u>\$ 333,438</u>	<u>\$ 148,491</u>	<u>\$ (9,712)</u>	<u>\$ 47,141</u>	<u>\$ 221</u>	<u>\$ 526,763</u>

See notes to financial statements.

City of Morning Sun
Notes to Financial Statements

Note 1. Summary of Significant Accounting Policies

The City of Morning Sun (City) is a political subdivision of the State of Iowa located in Louisa County. It was incorporated in 1867 and operates under the Home Rule provisions of the Constitution of Iowa. The City operates under the Mayor-Council form of government with the Mayor and Council Members elected on a non-partisan basis. The City provides numerous services to citizens, including public safety, public works, culture, recreation, community and economic development and general government services. The City also provides gas, water, refuse collection and sewer utilities for its citizens.

Reporting Entity

For financial reporting purposes, the City has included all funds, organizations, agencies, boards, commissions and authorities. The City has also considered all potential component units for which it is financially accountable and other organizations for which the nature and significance of their relationship with the City are such that exclusion would cause the City's financial statements to be misleading or incomplete. The Governmental Accounting Standards Board (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 City to impose its will on that organization or (2) the potential for the organization to provide specific benefits to or impose specific financial burdens on the City.

Excluded Component Units

Morning Sun Fire Department (Fire Department) is a component unit of the City of Morning Sun. The Fire Department exists for the purpose of serving the City of Morning Sun and surrounding township. The Fire Department meets the definition of component unit since the entity serves the City. The financial statements of Morning Sun Fire Department have not been audited and, accordingly, the component unit has not been presented in the accompanying primary government audited financial statements.

Jointly Governed Organizations

The City participates in several jointly governed organizations that provide goods or services to the citizenry of the City, but do not meet the criteria of a joint venture since there is no ongoing financial interest or responsibility by the participating governments. City officials are members of the Des Moines County Regional Solid Waste Commission.

The City officials are also members of the Planning & Zoning Commission and Board of Adjustments, Louisa Development Group, and Iowa Rural Water Association.

Basis of Presentation

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

City of Morning Sun
Notes to Financial Statements

Note 1. Summary of Significant Accounting Policies (continued)

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

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

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

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

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

The City reports the following major governmental funds:

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

Special Revenue:

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

The Urban Renewal Tax Increment Fund is used to account for tax increment financing collections and the repayment of tax increment financing indebtedness.

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

The City reports the following major proprietary funds:

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

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

The Gas Fund accounts for the operation and maintenance of the City's gas system.

City of Morning Sun
Notes to Financial Statements

Note 1. Summary of Significant Accounting Policies (continued)

The Sanitation Fund accounts for the operation and maintenance of the City's solid waste collection system.

The Equipment Reserve Fund accounts for funds set aside for major equipment purchase in the water and sewer departments.

Measurement Focus and Basis of Accounting

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

Under the terms of grant agreements, the City funds certain programs by a combination of specific cost-reimbursement grants, categorical block grants and general receipts. Thus, when program disbursements are paid, there are both restricted and unrestricted cash basis net assets available to finance the program. It is the City's policy to first apply cost-reimbursement grant resources to such programs, followed by categorical block grants and then by general receipts.

When a disbursement in governmental funds can be paid using either restricted or unrestricted resources, the City's policy is generally to first apply the disbursement toward restricted fund balance and then to less-restrictive classifications - committed, assigned and then unassigned.

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

Governmental Cash Basis Fund Balances

In the governmental fund financial statements, cash basis fund balances are classified as follows:

Restricted - Amounts restricted to specific purposes when constraints placed on the use of the resources are either externally imposed by creditors, grantors, or state or federal laws or imposed by law through constitutional provisions or enabling legislation.

Assigned - Amounts the Council intends to use for specific purpose.

Unassigned - All amounts not included in other spendable classifications.

Budgets and Budgetary Accounting

The budgetary comparison and related disclosures are reported as Other Information.

City of Morning Sun
Notes to Financial Statements

Note 1. Summary of Significant Accounting Policies (continued)

Subsequent Events

The City performed an evaluation of subsequent events through November 13, 2012, which is the date the financial statements were issued. There have been no subsequent events that would require disclosure or recognition in the financial statements as of June 30, 2012.

Recently Adopted Accounting Pronouncements

In February 2009, the Governmental Accounting Standards Board (GASB) issued Statement Number 54, *Fund Balance Reporting and Governmental Fund Type Definitions*, which provides clearer fund balance classifications that can be more consistently applied and by clarifying the existing governmental fund type definitions. The statement establishes fund balance classifications that comprise a hierarchy based primarily on the extent to which a government is bound to observe constraints imposed upon the use of the resources reported in governmental funds. The City adopted this statement on July 1, 2011.

Note 2. Cash and Pooled Investments

The City's deposits at June 30, 2012 were entirely covered by federal depository insurance or by the State Sinking Fund in accordance with Chapter 12C of the Code of Iowa. This chapter provides for additional assessments against the depositories to insure there will be no loss of public funds.

The City is authorized by statute to invest public funds in obligations of the United States government, its agencies and instrumentalities; certificates of deposit or other evidences of deposit at federally insured depository institutions approved by the City Council 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 City's investments are categorized to give an indication of the level of risk assumed by the City at year end. The City's investments are all Level 1 which means that the investments are insured or registered or the securities are held by the City or its agent in the City's name.

The City's investments at June 30, 2012 were entirely in certificates of deposit.

City of Morning Sun
Notes to Financial Statements

Note 3. Bonds and Notes Payable

Annual debt service requirements to maturity for general obligation bonds, sewer and water revenue bonds and other debt are as follows:

Year Ended June 30	General Obligation Bonds		Revenue Bond		Total	
	Principal	Interest	Principal	Interest	Principal	Interest
2013	\$ 40,806	\$ 6,917	\$ 10,000	\$ 2,640	\$ 50,806	\$ 9,557
2014	42,607	5,368	10,000	2,340	52,607	7,708
2015	44,430	3,747	11,000	2,040	55,430	5,787
2016	29,000	2,280	11,000	1,740	40,000	4,020
2017	11,000	1,410	11,000	1,410	22,000	2,820
2018-2020	<u>36,000</u>	<u>2,160</u>	<u>36,000</u>	<u>2,160</u>	<u>72,000</u>	<u>4,320</u>
	<u>\$ 203,843</u>	<u>\$ 21,882</u>	<u>\$ 89,000</u>	<u>\$ 12,330</u>	<u>\$ 292,843</u>	<u>\$ 34,212</u>

Revenue Bonds

The City has pledged future water customer receipts, net of specified operating disbursements, to repay \$183,000 in water revenue notes issued in June 1, 2000. The notes are payable solely from water customer net receipts and are payable through 2020. The total principal and interest remaining to be paid on the notes is \$101,330. For the current year, principal and interest paid and total customer net receipts were \$11,940 and \$67,433, respectively.

The resolutions providing for the issuance of the water revenue bond include the following provisions.

- (a) The bond will only be redeemed from the future earnings of the enterprise activity and the bond holders hold a lien on the future earnings of the funds.
- (b) Water user charges must be established at a level which produces and maintains net revenues at a level not less than 110% of principal and interest requirements of the next fiscal year.

Note 4. Pension and Retirement Benefits

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

Most regular plan members are required to contribute 5.38% of their annual covered salary and the City is required to contribute 8.07% of covered salary. Certain employees in special risk occupations and the City contribute an actuarially determined contribution rate. Contributions are established by state statute. The City's contribution to IPERS for the year ended June 30, 2012 was \$12,472, equal to the required contributions.

City of Morning Sun
Notes to Financial Statements

Note 5. Compensated Absences

City employees accumulate a limited amount of earned but unused vacation hours for subsequent use or for payment upon termination, retirement or death. These accumulations are not recognized as disbursements by the City until used or paid. The City's approximate liability for earned vacation payments payable to employees at June 30, 2012, primarily relating to the General Fund, is \$8,891 based on rates of pay as of June 30, 2012.

Note 6. Related Party Transactions

Business transactions between the City and City officials or employees totaled \$12,511 during the year ended June 30, 2012.

Note 7. Major Supplier

The City purchases energy (gas) for resale. The total amount purchased was \$146,233 from Clayton Energy.

Note 8. Other Postemployment Benefits (OPEB)

Plan Description - The City operates a single-employer retiree benefit plan which provides medical/prescription drug benefits for retirees and their spouses. There are 3 active and no retired members in the plan. Retired participants must be age 55 or older at retirement.

The medical/prescription drug benefits are provided through a fully-insured plan with Wellmark. Retirees under age 65 pay the same premium for the medical/prescription drug benefits as active employees.

Funding Policy - The contribution requirements of plan members are established and may be amended by the City. The City currently finances the benefit plan on a pay-as-you-go basis. The most recent active member monthly premiums for the City and plan members is \$964.96 for family coverage. For the year ended June 30, 2012, the City contributed \$27,200 and plan members eligible for benefits contributed \$5,939 to the plan.

Note 9. Deficit Fund Balances

The following funds had a deficit balance at year end:

General fund	\$ 96,047
Road use fund	5,499
Debt service fund	10,178
Sanitation fund	9,712

The deficit balances were a result of costs incurred prior to availability of funds.

City of Morning Sun
Notes to Financial Statements

Note 10. Interfund Transfers

The detail of interfund transfers for the year ended June 30, 2012 is as follows:

Transfer to:	Transfer from:	
Debt service	Urban renewal tax increment	\$ 21,000

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

Note 11. Risk Management

The City is a member in the Iowa Communities Assurance Pool, as allowed by Chapter 670.7 of the Code of Iowa. The Iowa Communities Assurance Pool (Pool) is a local government risk-sharing pool whose 663 members include various governmental entities throughout the State of Iowa. The Pool was formed in August 1986 for the purpose of managing and funding third-party liability claims against its members. The Pool provides coverage and protection in the following categories: general liability, automobile liability, automobile physical damage, public officials liability, police professional liability, property, inland marine, and boiler/machinery. There have been no reductions in insurance coverage from prior years.

Each member's annual casualty contributions to the Pool fund current operations and provide capital. Annual operating contributions are those amounts necessary to fund, on a cash basis, the Pool's general and administration expenses, claims, claim expenses and reinsurance expenses due and payable in the current year, plus all or any portion of any deficiency in capital. Capital contributions are made during the first six years of membership and are maintained to equal 150% of the total current members' basis rates or to comply with the requirements of any applicable regulatory authority having jurisdiction over the Pool.

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

The City's property and casualty contributions to the risk pool are recorded as disbursements from its operating funds at the time of payment to the risk pool. The City's contribution to the Pool for the year ended June 30, 2012 was \$14,138.

The Pool uses reinsurance and excess risk-sharing agreements to reduce its exposure to large losses. The Pool retains general, automobile, police professional, and public officials' liability for risks up to \$350,000 per claim. Claims exceeding \$350,000 are reinsured in an amount not to exceed \$2,650,000 per claim. For members requiring specific coverage from \$3,000,000 to \$12,000,000, such excess coverage is also reinsured. Property and automobile physical damage risks are retained by the Pool up to \$150,000 each occurrence, each location, with excess coverage reinsured by The Travelers Insurance Company.

City of Morning Sun
Notes to Financial Statements

Note 11. Risk Management (continued)

The Pool's intergovernmental contract with its members provides that in the event a casualty claim or series of claims exceeds the amount of risk-sharing protection provided by the member's risk-sharing certificate, or in the event that a series of casualty claims exhausts total members' equity plus any reinsurance and any excess risk-sharing recoveries, then payment of such claims shall be the obligation of the respective individual member. As of June 30, 2012, settled claims have not exceeded the risk pool or reinsurance company coverage since the Pool's inception.

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

The City also carries commercial insurance purchased from other insurers for coverage associated with workmen's compensation. The City assumes liability for any deductibles and claims in excess of coverage limitations. Settled claims resulting from these risks have not exceeded commercial insurance coverage in any of the past three fiscal years.

OTHER INFORMATION

**City of Morning Sun
Budgetary Comparison Schedule
of Receipts, Disbursements and Changes in Balances -
Budget and Actual (Cash Basis) - All Governmental Funds and Proprietary Funds
Other Information
Year Ended June 30, 2012**

	Governmental Funds <u>Actual</u>	Proprietary Funds <u>Actual</u>	Less Funds not Required to be Budgeted	Net	<u>Budgeted Amounts</u>		Final to Net <u>Variance</u>
					<u>Original</u>	<u>Final</u>	
Receipts:							
Property tax	\$ 144,731	\$ -	\$ -	\$ 144,731	\$ 143,166	\$ 143,166	\$ 1,565
Tax increment financing collections	71,496	-	-	71,496	45,000	45,000	26,496
Other city taxes	44,177	-	-	44,177	37,118	47,118	(2,941)
Use of money and property	3,556	14	-	3,570	3,400	3,400	170
Licenses and permits	1,665	-	-	1,665	1,300	1,300	365
Intergovernmental	80,436	-	-	80,436	123,834	123,834	(43,398)
Charges for service	27,906	566,387	-	594,293	643,310	559,310	34,983
Miscellaneous	<u>26,871</u>	<u>6,875</u>	<u>-</u>	<u>33,746</u>	<u>2,075</u>	<u>2,075</u>	<u>31,671</u>
Total receipts	<u>400,838</u>	<u>573,276</u>	<u>-</u>	<u>974,114</u>	<u>999,203</u>	<u>925,203</u>	<u>48,911</u>
Disbursements:							
Public safety	60,356	-	-	60,356	52,205	69,092	8,736
Public works	96,425	-	-	96,425	90,834	100,980	4,555
Culture and recreation	40,404	-	-	40,404	40,015	40,015	(389)
Community and economic development	200	-	-	200	1,472	1,472	1,272
General government	137,016	-	-	137,016	115,530	146,880	9,864
Debt service	47,533	11,989	-	59,522	41,875	61,830	2,308
Capital projects	21,617	38,756	-	60,373	-	-	(60,373)
Business type activities	<u>-</u>	<u>430,402</u>	<u>-</u>	<u>430,402</u>	<u>643,310</u>	<u>567,210</u>	<u>136,808</u>
Total disbursements	<u>403,551</u>	<u>481,147</u>	<u>-</u>	<u>884,698</u>	<u>985,241</u>	<u>987,479</u>	<u>102,781</u>
Excess (deficiency) of receipts over disbursements	(2,713)	92,129	-	89,416	13,962	(62,276)	151,692
Other financing sources, net	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
Net change in cash balances	(2,713)	92,129	-	89,416	13,962	(62,276)	151,692
Cash balances beginning of year	<u>69,206</u>	<u>434,634</u>	<u>-</u>	<u>503,840</u>	<u>444,376</u>	<u>516,311</u>	<u>(12,471)</u>
Cash balances end of year	<u>\$ 66,493</u>	<u>\$ 526,763</u>	<u>\$ -</u>	<u>\$ 593,256</u>	<u>\$ 458,338</u>	<u>\$ 454,035</u>	<u>\$ 139,221</u>

See accompanying independent auditor's report.

City of Morning Sun
Notes to Other Information - Budgetary Reporting

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

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

Formal and legal budgetary control is based upon nine major classes of disbursements known as functions, not by fund. These nine functions are: public safety, public works, health and social services, culture and recreation, community and economic development, general government, debt service, capital projects, and business type activities. Function disbursements required to be budgeted include disbursements for the General Fund, Special Revenue Funds, Debt Service Fund, Capital Projects Funds and Proprietary Funds. Although the budget document presents function disbursements by fund, the legal level of control is at the aggregated function level, not by fund. During the year, budget amendments increased budgeted disbursements by \$2,238. The budget amendments are reflected in the final budgeted amounts.

During the year ended June 30, 2012, disbursements exceeded the amounts budgeted in the culture and recreation and capital projects functions.

SUPPLEMENTARY INFORMATION

City of Morning Sun
Schedule of Cash Receipts, Disbursements and Changes in Cash Balances
Nonmajor Governmental Funds
As of and for the Year Ended June 30, 2012

	<u>Library Grants</u>
Receipts:	
Charges for service	\$ 1,386
Intergovernmental	1,140
Miscellaneous	<u>11,378</u>
Total receipts	<u>13,904</u>
Disbursements:	
Culture and recreation	<u>13,252</u>
Total disbursements	<u>13,252</u>
Excess (deficiency) of receipts over disbursements	\$ <u>652</u>
Net change in cash balances	\$ 652
Cash balances beginning of year	<u>15,587</u>
Cash balances end of year	\$ <u>16,239</u>

See accompanying independent auditor's report.

**City of Morning Sun
Statement of Indebtedness
Year Ended June 30, 2012**

<u>Obligation</u>	<u>Date of Issuance</u>	<u>Interest Rates</u>	<u>Amount Originally Issued</u>	<u>Balance Beginning of Year</u>	<u>Issued During Year</u>	<u>Redeemed During Year</u>	<u>Balance End of Year</u>	<u>Interest Paid</u>	<u>Interest Due and Unpaid</u>
General obligation bonds:									
Water improvement	07/06/00	3.00%	\$ 182,000	\$ 97,000	\$ -	\$ 9,000	\$ 88,000	\$ 2,910	\$ -
Sewer improvement	12/13/96	3.00%	242,000	81,000	-	15,000	66,000	2,430	-
Iowa State Bank	04/03/08	5.00%	105,000	<u>65,213</u>	<u>-</u>	<u>15,370</u>	<u>49,843</u>	<u>2,734</u>	<u>-</u>
Total				<u>243,213</u>	<u>-</u>	<u>39,370</u>	<u>203,843</u>	<u>8,074</u>	<u>-</u>
Revenue bonds/notes:									
Water revenue capital loan notes	06/01/00	3.00%	183,000	<u>98,000</u>	<u>-</u>	<u>9,000</u>	<u>89,000</u>	<u>2,940</u>	<u>-</u>
Total				<u>98,000</u>	<u>-</u>	<u>9,000</u>	<u>89,000</u>	<u>2,940</u>	<u>-</u>
Total of all debt				<u>\$ 341,213</u>	<u>\$ -</u>	<u>\$ 48,370</u>	<u>\$ 292,843</u>	<u>\$ 11,014</u>	<u>\$ -</u>

See accompanying independent auditor's report.

**City of Morning Sun
Bond and Note Maturities
June 30, 2012**

General Obligation Bonds:

Year Ending <u>June 30,</u>	Interest <u>Rate</u>	Sewer Improvement Bond Dec 1, 1996 <u>Amount</u>	Interest <u>Rate</u>	Water Improvement Bond June 1, 2000 <u>Amount</u>	Interest <u>Rate</u>	Garland Land Iowa State Bank April 3, 2008 <u>Amount</u>	<u>Total</u>
2013	3.00%	\$ 15,000	3.00%	\$ 10,000	5.00%	\$ 15,806	\$ 40,806
2014	3.00%	16,000	3.00%	10,000	5.00%	16,607	42,607
2015	3.00%	17,000	3.00%	10,000	5.00%	17,430	44,430
2016	3.00%	18,000	3.00%	11,000	-	-	29,000
2017	-	-	3.00%	11,000	-	-	11,000
2018	-	-	3.00%	12,000	-	-	12,000
2019	-	-	3.00%	12,000	-	-	12,000
2020	-	-	3.00%	12,000	-	-	12,000
		<u>\$ 66,000</u>		<u>\$ 88,000</u>		<u>\$ 49,843</u>	<u>\$ 203,843</u>

Revenue Bonds:

Year Ending <u>June 30,</u>	Interest <u>Rate</u>	Water Revenue June 1, 2000 <u>Amount</u>
2013	3.00%	\$ 10,000
2014	3.00%	10,000
2015	3.00%	11,000
2016	3.00%	11,000
2017	3.00%	11,000
2018	3.00%	12,000
2019	3.00%	12,000
2020	3.00%	12,000
		<u>\$ 89,000</u>

See accompanying independent auditor's report.



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

Honorable Mayor and
Members of the City Council:

We have audited the accompanying financial statements of the governmental activities, the business type activities, each major fund and the aggregate remaining fund information of the City of Morning Sun, Iowa (City), as of and for the year ended June 30, 2012, which collectively comprise the City's basic financial statements listed in the table of contents, and have issued our report thereon dated November 13, 2012. Our report expressed unqualified opinions on the financial statements which were prepared in conformity with an other comprehensive basis of accounting. We conducted our audit in accordance with 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

The management of the City is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered the City's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the City's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the City'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 all deficiencies, significant deficiencies or material weaknesses have been identified. However, as described in the accompanying Schedule of Findings and Questioned Costs, we identified certain deficiencies in internal control over financial reporting that 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 City'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 and Questioned Costs to be material weaknesses.

Compliance and Other Matters

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

Comments involving statutory and other legal matters about the City's operations for the year ended June 30, 2012 are based exclusively on knowledge obtained from procedures performed during our audit of the financial statements of the City. Since our audit was based on tests and samples, not all transactions that might have had an impact on the comments were necessarily audited. The comments involving statutory and other legal matters are not intended to constitute legal interpretations of those statutes.

The City's responses to the findings identified in our audit are described in the accompanying Schedule of Findings and Questioned Costs. While we have expressed our conclusions on the City's responses, we did not audit the City's 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 officials, employees and citizens of the City and other parties to whom the City may report, including federal awarding agencies and pass-through entities, and is not intended to be and should not be used by anyone other than these specified parties.

We would like to acknowledge the many courtesies and assistance extended to us by personnel of the City 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 13, 2012

City of Morning Sun
Schedule of Findings and Questioned Costs
Year Ended June 30, 2012

Part I: Findings Related to the Financial Statements

INTERNAL CONTROL DEFICIENCIES:

I-A-12 Preparation of Financial Statements - The City does not have an internal control system designed to provide for the preparation of the financial statements on the basis of cash receipts and disbursements, which is a comprehensive basis of accounting other than 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 population to the City of Morning Sun. 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.

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 City's management and those charged with governance should decide whether to accept the degree of risk associated with this condition.

Response - The City 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.

I-B-12 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 City Council and management should continue to provide oversight and direction based upon their direct knowledge of the City's operations and day-to-day contact with employees to control and safeguard assets.

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

Conclusion - Response accepted.

City of Morning Sun
Schedule of Findings and Questioned Costs
Year Ended June 30, 2012

I-C-12 Utility Billing Errors - Changes to customer utility billings are not reviewed. During our utility testing, the number of units charged the minimum rate for commercial sewer customers was not correct. The number of units subject to the minimum charge is 2,000 units per the City ordinance, but the utility billing system was set up to charge 3,000 units at the minimum charge.

Recommendation - Procedures should be established to require an independent review of any changes that are made to customer utility accounts. The Council or a Council-designated independent person should review the changes.

Response - The City will establish and implement procedures for the review of utility billings changes.

Conclusion - Response accepted.

INSTANCES OF NON-COMPLIANCE:

No matters were reported.

City of Morning Sun
Schedule of Findings and Questioned Costs
Year Ended June 30, 2012

Part II: Other Findings Related to Required Statutory Reporting

II-A-12 Certified Budget - Disbursements during the year ended June 30, 2012 exceeded the amounts budgeted in the culture and recreation and capital projects functions. Chapter 384.20 of the Code of Iowa states, in part, "Public monies may not be expended or encumbered except under an annual or continuing appropriation."

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

Response - The budget will be amended in the future, if applicable.

Conclusion - Response accepted.

II-B-12 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.

II-C-12 Travel Expense - No disbursements of City money for travel expenses of spouses of City officials or employees were noted.

II-D-12 Bond Coverage - Surety bond coverage of City officials and employees is in accordance with statutory provisions. The amount of coverage should be reviewed annually to insure that the coverage is adequate for current operations.

II-E-12 Council Minutes - No transactions were found that we believe should have been approved in the Council minutes but were not.

II-F-12 Revenue Notes - No instances of non-compliance with the revenue bond and note resolutions were noted.

II-G-12 Deposits and Investments - The City has not approved a written investment policy as required by Chapter 12B.10B of the Code of Iowa.

Recommendation - The City should approve a written investment policy as required by Chapter 12B.10B of the Code of Iowa.

Response - An investment policy will be drafted and adopted as recommended.

Conclusion - Response accepted.

**City of Morning Sun
Schedule of Findings and Questioned Costs
Year Ended June 30, 2012**

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

II-H-12 Financial Condition - The following funds had a deficit balance at year end:

General fund	\$ 96,047
Road use fund	5,499
Debt service fund	10,178
Sanitation fund	9,712

Recommendation - The City should monitor the progress of the cash receipts and disbursements in these funds and review the control procedures throughout the period so the receipts collected cover the disbursements made from these funds.

Response - We will consider this.

Conclusion - Response accepted.

II-I-12 Business Transactions - Business transactions between the City and City officials or employees are detailed as follows:

<u>Name, Title, and Business Connection</u>	<u>Transactions</u>	<u>Amount</u>
Brenda Springsteen, Employee Spouse is owner of Springsteen Tiling	Install water lines	\$ 12,511

The transaction with the employee represents a conflict of interest since it was not entered into through competitive bidding in accordance with Chapter 362.5(3)(j) of the Code of Iowa.

Recommendation - The City should consult legal counsel to determine the disposition of this matter.

Response - The City will consult legal counsel.

Conclusion - Response accepted.

II-J-12 Local Option Sales Tax - Local option sales tax collections were posted directly to the General Fund rather than into a Special Revenue Fund.

Recommendation - The City should establish a Special Revenue Fund for local option sales tax receipts, disbursements and balances to demonstrate compliance with the City's referendum for the use of the tax.

Response - We will do this.

Conclusion - Response accepted.

City of Morning Sun
Schedule of Findings and Questioned Costs
Year Ended June 30, 2012

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

II-K-12 Delinquent Utility Accounts - At June 30, 2012, two employees or council members had delinquent utility accounts.

Recommendation - We recommend that the City emphasizes to employees and council members that they are setting an example to the community by their actions.

Response - We will encourage employees and council members to pay their utility bills by their due date.

Conclusion - Response accepted.