CITY OF SHELBY

INDEPENDENT AUDITOR'S REPORTS
BASIC FINANCIAL STATEMENTS
SUPPLEMENTARY AND OTHER INFORMATION
SCHEDULE OF FINDINGS

JUNE 30, 2012

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CITY OF SHELBY
OFFICIALS

Name	Title	Term Expires
	(Before January 2012)	
Lisa Juhl	Mayor	January 2012
Rod Robinson	Mayor Pro-tem/Council Member	January 2012
Jim Cunningham	Council Member	January 2012
Craig Davis	Council Member	January 2012
Kristen Lund	Council Member	January 2012
Bob Seitz	Council Member	January 2012
Christie Martin	City Clerk	Indefinite
Katie Goshorn	City Attorney	Indefinite
Patricia Morris	City Treasurer	Indefinite
	(After January 2012)	
Lisa Juhl	Mayor	January 2014
Brad Blum	Mayor Pro-tem/Council Member	January 2014
Doyle Gilland	Council Member	January 2014
Shawn Osbahr	Council Member	January 2016
Sheila Rihner	Council Member	January 2016
Bob Richmond	Council Member	January 2016
Christie Martin	City Clerk	Indefinite
Katie Goshorn	City Attorney	Indefinite
Patricia Morris	City Treasurer	Indefinite

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Licensed In:

Iowa
Missouri

August 10, 2012

Independent Auditor's Report

To the Honorable Mayor and
Members of the City Council:

I have audited the accompanying financial statements of the governmental activities, the business type activities, each major fund and the aggregate remaining fund information of the City of Shelby, Iowa, 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. My responsibility is to express opinions on these financial statements based on my audit.

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

As described in Note 1, these financial statements were prepared on the basis of cash receipts and disbursements, which is a comprehensive basis of accounting other than U.S. generally accepted accounting principles.

In my opinion, the financial statements referred to above present fairly, in all material respects, the respective cash basis financial position of the governmental activities, the business type activities, each major fund and the aggregate remaining fund information of the City of Shelby, Iowa 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.

Continued . . .

August 10, 2012

To the Honorable Mayor and
Members of the City Council:
Page Two

In accordance with *Government Auditing Standards*, I have also issued my report dated August 10, 2012 on my consideration of the City of Shelby's internal control over financial reporting and my tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of my testing of internal control over financial reporting and compliance and the results of that testing and not to provide an opinion on internal control over financial reporting or compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of my audit.

My audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the City of Shelby's basic financial statements. I previously audited, in accordance with the standards referred to in the second paragraph of this report, the financial statements for the four years ended June 30, 2010 (which are not presented herein) and expressed unqualified opinions on those financial statements which were prepared in conformity with an other comprehensive basis of accounting. The supplementary information included in Schedules 1 through 4 is presented for purposes of additional analysis, and is not a required part of the basic financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other auditing procedures applied in my audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with U.S. generally accepted auditing standards. In my opinion, the supplementary information is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

My audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the City of Shelby's basic financial statements. Management's Discussion and Analysis and the budgetary comparison information on pages 6 through 11 and 31 through 33 are presented for purposes of additional analysis and are 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, I do not express and opinion or provide any assurance on it.

Mayfield Associates, CPA, P.C.

MANAGEMENT'S DISCUSSION AND ANALYSIS

The City of Shelby provides this Management's Discussion and Analysis of its financial statements. This narrative overview and analysis of the financial activities is for the fiscal year ended June 30, 2012. We encourage readers to consider this information in conjunction with the City's financial statements, which follow.

2012 FINANCIAL HIGHLIGHTS

Receipts of the City's governmental activities increased 9.8%, or approximately $50,000, from fiscal year 2011 to fiscal year 212. Property tax increased 12.5%, or approximately $18,000.

Disbursements of the City's governmental activities decreased 10%, or approximately $61,000, in fiscal year 2012 from fiscal year 2011. Public works and capital projects decreased approximately $94,000 and $19,000, respectively. Public safety and general government increased approximately $32,000 and $18,000, respectively.

The City's total cash basis net assets increased 6.45%, or approximately $104,000, from June 30, 2011 to June 30, 2012. Of this amount, the assets of the governmental activities increased approximately $500 and the assets of the business type activities increased approximately $103,500.

USING THIS REPORT

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

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

The Government-wide Financial Statement consists of a Statement of Activities and Net Assets. This statement provides information about the activities of the City as a whole and presents an overall view of the City's finances.

The Fund Financial Statements tell how governmental services were financed in the short term as well as what remains for future spending. Fund financial statements report the City's operations in more detail than the government-wide financial statement by providing information about the most significant funds.

Notes to Financial Statements provide additional information essential to a full understanding of the data provided in the basic financial statements.

Other Information further explains and supports the financial statements with a comparison of the City's budget for the year.

Supplementary Information provides detailed information about the nonmajor governmental funds and the City's indebtedness.

BASIS OF ACCOUNTING

The City maintains its financial records on the basis of cash receipts and disbursements and the financial statements of the City are prepared on that basis. The cash basis of accounting does not give effect to accounts receivable, accounts payable and accrued items. Accordingly, the financial statements do not present financial position and results of operations of the funds in accordance with U.S. generally accepted accounting principles. Therefore, when reviewing the financial information and discussion within this annual report, readers should keep in mind the limitations resulting from the use of the cash basis of accounting.

REPORTING THE CITY'S FINANCIAL ACTIVITIES

Government-wide Financial Statement

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

The Statement of Activities and Net Assets presents the City's net assets. Over time, increases or decreases in the City's net assets may serve as a useful indicator of whether the financial position of the City is improving or deteriorating.

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

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

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

Fund Financial Statements

The City has two kinds of funds:

1) Governmental funds account for most of the City's basic services. These focus on how money flows into and out of those funds and the balances at year-end that are available for spending. The governmental funds include: 1) the General Fund, 2) the Special Revenue Funds, such as Toad Use Tax and Urban Renewal Tax Increment, 3) the Debt Service Fund, and 4) the Capital Projects Fund. The governmental fund financial statements provide a detailed, short-term view of the City's general government operations and the basic services it provides. Governmental fund information helps determine whether there are more or fewer financial resources that can be spent in the near future to finance the City's programs.

   The required financial statement for governmental funds is a Statement of Cash Receipts, Disbursements and Changes in Cash Balances.

2) Proprietary funds account for the City's Enterprise Funds which are used to report business type activities. The City maintains three Enterprise Funds to provide separate information for the Water, Sewer and Electric Funds, considered to be major funds of the City.

The required financial statement for proprietary funds is a Statement of Cash Receipts, Disbursements and changes in Cash Balances.

GOVERNMENT-WIDE FINANCIAL ANALYSIS

Net assets may serve over time as a useful indicator of financial position. The City's cash balance for governmental activities increased by $552 from a year ago.

Changes in Cash Basis Net Assets of Governmental Activities

	Year Ended June 30, 2012	Year Ended June 30, 2011
Receipts:		
Program receipts:		
Charges for services	$ 135,685	$ 115,167
Operating grants, contributions and restricted interest	71,634	73,232
Capital grants, contributions and restricted interest	6,700	-0-
General receipts:		
Property tax	158,829	141,160
Tax increment financing	128,133	129,851
Local option sales tax	47,533	45,371
Unrestricted investment earnings	1,467	2,614
Sale of property	8,800	1,575
Total receipts	558,781	508,970
Disbursements:		
Public safety	91,854	59,869
Public works	104,520	199,148
Culture and recreation	37,311	38,058
Community and economic development	168,411	168,354
General government	72,263	53,828
Debt service	83,870	81,738
Capital projects	-0-	18,865
Total disbursements	558,229	619,860
Change in cash basis net assets	552	(110,890)
Cash basis net assets, beginning of year	1,115,864	1,226,754
Cash basis net assets, end of year	$ 1,116,416	$ 1,115,864

The City's total receipts for governmental activities increased 9.8%, or approximately $50,000. The total cost of all programs and services decreased approximately $61,000, or 10%, with no new programs added this year. The significant decrease was due to street resurfacing paid for in July 2013.

The City maintained property tax rates at the same level for fiscal years 2012 and 2011. Property tax receipts increased 12.5%, or approximately $20,000 from the prior year due to increases in assessed valuation. Property tax rates will remain steady next year but increased assessed valuation will increase property tax receipts by 33%, or approximately $52,000.

The cost of all governmental activities this year was approximately $558,000 compared to approximately $620,000 last year. However, as shown in the Statement of Activities and Net Assets on pages 13-14, the amount taxpayers ultimately financed for these activities was approximately $344,000 because some of the cost was paid by those directly benefited from the programs (approximately $135,700) or by other governments and organizations which subsidized certain programs with grants, contributions and restricted interest (approximately $78,300). Overall, the City's governmental activities program receipts, including intergovernmental aid and fees for service, increased in fiscal year 2012.

Changes in Cash Basis Net Assets of Business Type Activities		
	Year Ended June 30, 2012	Year Ended June 30, 2011
Receipts:		
Program receipts:		
Charges for services:		
Water	$ 150,129	$ 128,310
Sewer	56,554	50,620
Electric	593,452	584,886
Operating grants, contributions and restricted interest	462	877
General receipts		
Unrestricted interest on investments	536	572
Total receipts	801,133	765,265
Disbursements:		
Water	170,900	155,030
Sewer	27,757	19,004
Electric	498,825	494,144
Total disbursements	697,482	668,178
Change in cash basis net assets	103,651	97,087
Cash basis net assets, beginning of year	498,801	401,714
Cash basis net assets, end of year	$ 602,452	$ 498,801

Total business type activities receipts for the fiscal year were approximately $801,000 compared to approximately $765,000 last year. This increase was due primarily to water and electric rate increases in fiscal year 2012. The cash balance increased approximately $103,500, or 20%, from the prior year. Total disbursements for the fiscal year increased 4% to approximately $697,000.

INDIVIDUAL MAJOR GOVERNMENTAL FUND ANALYSIS

As the City of Shelby completed the year, its governmental funds reported a combined fund balance of $1,116,416, an increase of more than $500 above last year's total of $1,115,864.

The General Fund cash balance increased $18,397 from the prior year to $434,800. A $65,000 transfer from the Fire Fund to cover the purchase of a new tanker accounts for the increase. The new tanker was purchased subsequent to year end.

The Special Revenue, Road Use Tax Fund cash balance increased $59,137 from the prior year to $114,959. Street resurfacing expenses of approximately $66,000 was disbursed subsequent to year end.

The Special Revenue, Local Option Tax Fund cash balance increased $10,092 from the prior year to $237,893. City Council has flexibility on the uses of local option taxes and directed their use for community and economic development and public works purposes.

The Special Revenue, Urban Renewal Tax Increment Fund was established to account for major urban renewal projects within the City. At the end of the fiscal year, the cash balance was $161,883, a decrease of $82,942 from the previous year. $83,870 was used to pay principal and interest on the Sewer Improvement Notes and $127,205 was payment for reimbursement repairs to the old school building, now part of the Shelby Preservation Revitalization Area.

The Special Revenue, Fire Fund cash balance decreased $30,509 from the prior year to $98,675. The reduction in cash balance was solely due to a $65,000 transfer to the general fund for the purchase of a new tanker subsequent to year end.

INDIVIDUAL MAJOR BUSINESS TYPE FUND ANALYSIS

The Enterprise, Water Fund cash balance decreased $20,738 to a deficit of $82,132. Council will be addressing the Water Fund deficit next fiscal year.

The Enterprise, Sewer Fund cash balance increased $29,210 to $206,327.

The Enterprise, Electric Fund cash balance increased $95,179 to $478,257, due primarily to consistent rate increases over the past several years.

BUDGETARY HIGHLIGHTS

Over the course of the year, the City amended its budget once on May 4, 2012, increasing intergovernmental revenue by $15,000 and increasing public safety disbursements by $15,000.

The City's receipts were $15,004 more than budgeted. The City received more property taxes due to increased assessed valuations and more water and electric revenue due to rate increases. The City's actual disbursements did not exceed budgeted amounts for the fiscal year, due primarily to a planned water main project that City employees completed without outside contractors and engineers, at a considerable cost savings for the City.

DEBT ADMINISTRATION

At June 30, 2012, the City had $447,000 of notes outstanding, compared to $567,000 last year, as shown below.

Outstanding Debt				
		Year Ended June 30, 2012		Year Ended June 30, 2011
General obligation notes	$	20,000	$	100,000
Revenue notes		427,000		467,000
Total	$	447,000	$	567,000

Scheduled principal and interest payments for the year ended June 30, 2012 were $120,000 and $17,880, respectively. The Constitution of the State of Iowa limits the amount of general obligation debt cities can issue to 5% of the assessed value of all taxable property within the City's corporate limits. The City's outstanding general obligation debt of $20,000 is significantly below its constitutional debt limit of approximately $2.8 million. Additional information about the City's long-term debt is presented in Note 3 to the financial statements.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGET AND RATES

The City of Shelby's elected and appointed officials and citizens considered many factors when setting the fiscal year 2013 budget, tax rates and fees charged for various City activities.

Amounts available for appropriation in the 2013 operating budget are approximately $1.2 million, a 12% decrease from the final fiscal year 2012 budget. Property tax receipts are budgeted to increase by 33%, primarily due to increases in assessed valuation. Tax rates for fiscal year 2013 have not changed from the prior year.

Budgeted disbursements are expected to decrease by approximately $238,581, or 13%. Approximately $66,000 is budgeted for water line projects.

If these estimates are realized, the City's budgeted cash balance is expected to decrease approximately $339,000 by the close of fiscal year 2013.

CONTACTING THE CITY'S FINANCIAL MANAGEMENT

This financial report is designed to provide our citizens, taxpayers, customers and creditors with a general overview of the City's finances and to show the City's accountability for the money it receives. If you have questions about this report or need additional financial information, contact Chris Martin, City Clerk, 419 East Street, Shelby, Iowa 51570.

BASIC FINANCIAL STATEMENTS

CITY OF SHELBY

STATEMENT OF ACTIVITIES AND NET ASSETS - CASH BASIS

AS OF AND FOR THE YEAR ENDED JUNE 30, 2012

		Program Receipts		
	Disbursements	Charges for Services	Operating Grants, Contributions and Restricted Interest	Capital Grants, Contributions and Restricted Interest
Functions / Programs:				
Governmental activities:				
Public safety	$ 91,854	$ 60,737	$ 416	$ 6,700
Public works	104,520	36,983	60,800	-0-
Cultures and recreation	37,311	6,250	1,238	-0-
Community and economic development	168,411	-0-	-0-	-0-
General government	72,263	31,715	6,954	-0-
Debt service	83,870	-0-	-0-	-0-
Capital projects	-0-	-0-	2,226	-0-
Total governmental activities	558,229	135,685	71,634	6,700
Business type activities:				
Water	170,900	150,129	-0-	-0-
Sewer	27,757	56,554	413	0-
Electric	498,825	593,451	49	-0-
Total business type activities	697,482	800,134	462	-0-
Total	$ 1,255,711	$ 935,819	$ 72,096	$ 6,700
General receipts:				
Property taxes levied for:				
General purposes				
Tax increment financing				
Local option sales tax				
Unrestricted investment earnings				
Sale of property				
Total general receipts				
Change in cash basis net assets				
Cash basis net assets, beginning of year				
Cash basis net assets, end of year				
Cash Basis Net Assets				
Restricted:				
Expendable:				
Streets				
Urban renewal				
Assigned				
Unrestricted				
Total cash basis net assets				

See notes to financial statements.

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

	Governmental Activities		Business Type Activities		Total
$	(24,001)	$	-0-	$	(24,001)
	(6,737)		-0-		(6,737)
	(29,823)		-0-		(29,823)
	(168,411)		-0-		(168,411)
	(33,594)		-0-		(33,594)
	(83,870)		-0-		(83,870)
	2,226		-0-		2,226
	(344,210)		-0-		(344,210)
	-0-		(20,771)		(20,771)
	-0-		29,210		29,210
	-0-		94,675		94,675
	-0-		103,114		103,114
	(344,210)		103,114		(241,096)
	158,829		-0-		158,829
	128,133		-0-		128,133
	47,533		-0-		47,533
	1,467		537		2,004
	8,800		-0-		8,800
	344,762		537		345,299
	552		103,651		104,203
	1,115,864		498,801		1,614,665
$	1,116,416	$	602,452	$	1,718,868
$	114,959	$	-0-	$	114,959
	161,883		-0-		161,883
	166,881		287,405		454,286
	672,693		315,047		987,740
$	1,116,416	$	602,452	$	1,718,868

CITY OF SHELBY

STATEMENT OF CASH RECEIPTS, DISBURSEMENTS AND CHANGES IN CASH BALANCES GOVERNMENTAL FUNDS

AS OF AND FOR THE YEAR ENDED JUNE 30, 2012

		Special Revenue		
	General	Road Use Tax	Local Option	TIF Urban Renewal
Receipts:				
Property tax	$ 158,829	$ -0-	$ -0-	$ -0-
Tax increment financing	-0-	-0-	-0-	128,133
Other city taxes	3,840	-0-	47,533	-0-
Licenses and permits	2,812	-0-	-0-	-0-
Use of money and property	6,532	-0-	-0-	-0-
Intergovernmental	6,700	60,800	-0-	-0-
Charges for service	63,945	-0-	-0-	-0-
Special assessments	1,810	-0-	-0-	-0-
Miscellaneous	14,738	-0-	-0-	-0-
Total receipts	259,206	60,800	47,533	128,133
Disbursements:				
Public safety	91,854	-0-	-0-	-0-
Public works	101,272	1,663	1,585	-0-
Culture and recreation	37,111	-0-	-0-	-0-
Community and economic development	5,350	-0-	35,856	127,205
General government	72,263	-0-	-0-	-0-
Debt service	-0-	-0-	-0-	-0-
Total disbursements	307,850	1,663	37,441	127,205
Excess (deficiency) of receipts over (under) disbursements	(48,644)	59,137	10,092	928
Other financing sources (uses):				
Sale of property	8,800	-0-	-0-	-0-
Operating transfer in	67,477	-0-	-0-	-0-
Operating transfer out	(9,236)	-0-	-0-	(83,870)
Total other financing sources (uses)	67,041	-0-	-0-	(83,870)
Net change in cash balances	18,397	59,137	10,092	(82,942)
Cash balances, beginning of year	416,403	55,822	227,801	244,825
Cash balances, end of year	$ 434,800	$ 114,959	$ 237,893	$ 161,883
Cash Basis Fund Balances				
Restricted for:				
Streets	$ -0-	$ 114,959	$ -0-	$ -0-
Urban Renewal purposes	-0-	-0-	-0-	161,883
Assigned	-0-	-0-	-0-	-0-
Unassigned	434,800	-0-	237,893	-0-
Total cash basis fund balances	$ 434,800	$ 114,959	$ 237,893	$ 161,883

See notes to financial statements.

EXHIBIT B

Fire Fund	Debt Service	Non-major	Total
$ -0-	$ -0-	$ -0-	$ 158,829
-0-	-0-	-0-	128,133
-0-	-0-	-0-	51,373
-0-	-0-	-0-	2,812
109	-0-	420	7,061
32,752	-0-	2,200	102,452
1,630	-0-	17,198	82,773
-0-	-0-	-0-	1,810
-0-	-0-	-0-	14,738
34,491	-0-	19,818	549,981
-0-	-0-	-0-	91,854
-0-	-0-	-0-	104,520
-0-	-0-	200	37,311
-0-	-0-	-0-	168,411
-0-	-0-	-0-	72,263
-0-	83,870	-0-	83,870
-0-	83,870	200	558,229
34,491	(83,870)	19,618	(8,248)
-0-	-0-	-0-	8,800
-0-	83,870	9,341	160,688
(65,000)	-0-	(2,582)	(160,688)
(65,000)	83,870	6,759	8,800
(30,509)	-0-	26,377	552
129,184	-0-	41,829	1,115,864
$ 98,675	$ -0-	$ 68,206	$ 1,116,416
$ -0-	$ -0-	$ -0-	$ 114,959
-0-	-0-	-0-	161,883
98,675	-0-	68,206	166,881
-0-	-0-	-0-	672,693
$ 98,675	$ -0-	$ 68,206	$ 1,116,416

EXHIBIT C

CITY OF SHELBY

STATEMENT OF CASH RECEIPTS, DISBURSEMENTS AND CHANGES IN CASH BALANCES PROPRIETARY FUNDS

AS OF AND FOR THE YEAR ENDED JUNE 30, 2012

	Enterprise			
	Water	Sewer	Electric	Total
Operating receipts:				
Charges for services	$ 148,179	$ 56,554	$ 591,018	$ 795,751
Operating disbursements:				
Business type activities	116,427	27,757	498,825	643,009
Excess (deficiency) of operating receipts over (under) operating disbursements	31,752	28,797	92,193	152,742
Non-operating receipts (disbursements)				
Customer deposits	1,950	-0-	2,434	4,384
Debt service	(54,473)	-0-	-0-	(54,473)
Interest on investments	33	413	552	998
Net non-operating	(52,490)	413	2,986	(49,091)
Net change in cash balances	(20,738)	29,210	95,179	103,651
Cash balances, beginning of year	(61,394)	177,117	383,078	498,801
Cash balances, end of year	$ (82,132)	$ 206,327	$ 478,257	$ 602,452
Cash Basis Fund Balances				
Restricted for debt service	$ -0-	$ 51,212	$ 236,193	$ 287,405
Unrestricted	(82,132)	155,115	242,064	315,047
Total cash basis fund balances	$ (82,132)	$ 206,327	$ 478,257	$ 602,452

See notes to financial statements.

NOTES TO FINANCIAL STATEMENTS

(1) Summary of Significant Accounting Policies

The City of Shelby is a political subdivision of the State of Iowa located in Shelby and Pottawattamie Counties. It was first incorporated in 1872 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 and recreation, community and economic development, and general government services. The City also provides water, sewer and electric utilities for its citizens.

A. Reporting Entity

For financial reporting purposes, the City of Shelby has included all funds, organizations, agencies, boards, commissions and authorities. The City has also considered all potential component units for which it is financially accountable and other organizations for which the nature and significance of their relationship with the City are such that exclusion would cause the City's financial statements to be misleading or incomplete. The Governmental Accounting Standards Board has set forth criteria to be considered in determining financial accountability. These criteria include appointing a voting majority of an organization's governing body, and (1) the ability of the City to impose its will on that organization or (2) the potential for the organization to provide specific benefits to or impose specific financial burdens on the City. The City has no component units which meet the Government Accounting Standards Board criteria.

Jointly Governed Organizations

The City participates in several jointly governed organizations that provide goods or services to the citizenry of the City but do not meet the criteria of a joint venture since there is no ongoing financial interest or responsibility by the participating governments. City officials are members of the following boards and commissions: Shelby County Assessor's conference Board, Shelby County Emergency Management Commission, Shelby County Landfill Commission and Shelby County Joint E911 Service Board.

B. Basis of Presentation

Government-wide Financial Statement - The Statement of Activities and Net Assets reports information on all of the non-fiduciary activities of the City. For the most part, the effect of inter-fund 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.

(1) Summary of Significant Accounting Policies (Continued)

B. Basis of Presentation (continued)

The Statement of Activities and Net Assets presents the City's non-fiduciary 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 not meeting the definition of the preceding categories. 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 non-major 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 capital improvement costs not paid from other funds.

Special Revenue:

The Road Use Tax Fund is used to account for the road use tax allocation from the State of Iowa to be used for road construction and maintenance.

The Local Option Sales Tax Fund is used to account for the local option sales tax from the State of Iowa for special purposes as determined by City Council.

(1) Summary of Significant Accounting Policies (Continued)

B. Basis of Presentation (continued)

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

The Fire Fund is used to account for resources accumulated for use by the fire department.

The Debt Service Fund is used 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 Enterprise, Water Fund accounts for the operation and maintenance of the City's water system.

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

The Enterprise, Electric Fund accounts for the operation and maintenance of the City's electric utility.

C. Measurement Focus and Basis of Accounting

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

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 fund balances.

(1) Summary of Significant Accounting Policies (Continued)

C. Measurement Focus and Basis of Accounting (continued)

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

D. Governmental Cash Basis Fund Balances

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

Nonspendable - Amounts which cannot be spent because they are legally or contractually required to be maintained intact.

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

Assigned - Amounts the City Council intends to use for specific purposes.

Unassigned - All amounts not included in the preceding classifications.

E. The budgetary comparison and related disclosures are reported as Other Information. During the year ended June 30, 2012, disbursements did not exceed amounts budgeted.

(2) Cash and Pooled Investments

The City's deposits in banks 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; 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.

(2) Cash and Pooled Investments (Continued)

At June 30, 2012, the City's deposits consisted of cash in bank and certificates of deposit as follows:

Cash in bank	$	407,866
Certificates of deposit		180,716
Total	$	588,582

In addition, the City had investments in the Iowa Public Agency Investment Trust which are valued at an amortized cost of $1,130,286 pursuant to Rule 2a-7 under the Investment Company Act of 1940.

Credit risk - The City's investment in the Iowa Public Agency Investment Trust is unrated.

(3) Bonds and Notes Payable

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

Year Ending June 30,	General Obligation Sewer Improvement Notes		Water Revenue Bonds	
	Principal	Interest	Principal	Interest
2013	$ 20,000	$ 780	$ 61,000	$ 13,590
2014	-0-	-0-	43,000	11,580
2015	-0-	-0-	44,000	10,290
2016	-0-	-0-	45,000	8,970
2017	-0-	-0-	48,000	7,620
2018	-0-	-0-	49,000	6,180
2019	-0-	-0-	51,000	4,710
2020	-0-	-0-	53,000	3,180
2021	-0-	-0-	53,000	1,590
Total	$ 20,000	$ 780	$ 447,000	$ 67,710

(3) Bonds and Notes Payable (Continued)

Year Ending June 30,	Total Principal	Total Interest
2013	$ 81,000	$ 14,370
2014	43,000	11,580
2015	44,000	10,290
2016	45,000	8,970
2017	48,000	7,620
2018	49,000	6,180
2019	51,000	4,710
2020	53,000	3,180
2021	53,000	1,590
Total	$ 467,000	$ 68,490

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

a) The bonds will only be redeemed from the future earnings of the enterprise activity and the bondholders hold a lien on the future earnings of the funds.

b) Sufficient month transfers shall be made to a water revenue bond sinking account within the Enterprise Fund for the purpose of making the bond principal and interest payments when due.

(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. Contribution requirements are established by state statute. The City's contributions to IPERS for the year ended June 30, 2012 was $9,617, equal to the required contribution for the year.

(5) 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 2 active and no retired members in the plan. 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 retiree benefit plan on a pay-as-you-go basis. The most recent active member monthly premiums for the City and the plan members are $385 for single coverage and $736 for family coverage. For the year ended June 30, 2012, the City contributed $19,844 and plan member eligible for benefits contributed $2,575 to the plan.

(6) Compensated Absences

City employees accumulate a limited amount of earned but unused vacation and compensatory 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. Sick leave hours accumulate but are not payable upon termination. The City's approximate liability for earned vacation and compensatory time payable to employees at June 30, 2010, primarily relating to the Water Fund, is as follows:

Type of Benefit		Amount
Vacation	$	5,467
Compensatory time		-0-
Total	$	5,467

This liability has been computed based on rates of pay in effect at June 30, 2012.

(7) Related Party Transactions

The City had business transactions between the City and City officials totaling $6,625 during the year ended June 30, 2012.

(8) Interfund Transfers

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

Transfer to	Transfer from		Amount
General	Special Revenue - Fire Fund	$	65,000
General	Special Revenue - Ambulance		2,477
Debt Service	Special Revenue - Urban Renewal		83,870
Special Revenue - Economic Development	General		2,688
Capital Projects	Capital Projects		105
Capital Projects	General		6,548
Total		$	160,688

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

(9) Risk Management

The City is a member in the Iowa Communities Assurance Pool, as allowed by Chapter 670.07 of the Code of Iowa. The Iowa Communities Assurance Pool (Pool) is a local government risk-sharing pool whose 634 members included various governmental entities throughout the State of Iowa. The Pool was formed in August 1986 for the purpose of managing and funding third-party liability claims against its members. The Pool provides coverage and protection in the following categories: general liability, automobile liability, automobile physical damage, public officials' liability, police professional liability, property, inland marine, and boiler/machinery. There have been no reductions in insurance coverage from prior years.

Each member's annual casualty contributions to the Pool fund current operations and provide capital. Annual operating contributions are those amounts necessary to fund, on a cash basis, the Pool's general and administrative expenses, claims, claims expenses and reinsurance expenses due and payable in the current year, plus all or any portion of the deficiency in capital. Capital contributions are made during the first six years of membership and are maintained to equal 200 percent of the total current members' basis rates or to comply with the requirements of any applicable regulatory authority having jurisdiction over the Pool.

(10) Risk Management (Continued)

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

The City's property and casualty contributions to the risk pool are recorded as disbursements from its operating funds at the time of payment to the risk pool. The City's contributions to the Pool for the year ended June 30, 2012 were $13,554.

The Pool uses reinsurance and excess risk-sharing agreements to reduce its exposure to large losses. The Pool retains general, automobile, police professional, and public officials' liability risks up to $365,000 per claim. Claims exceeding $350,000 are reinsured in an amount not to exceed $2,650,000 per claim and $10,000,000 in aggregate per year. For members requiring specific coverage from $3,000,000 to $10,000,000, such excess coverage is also reinsured. Property and automobile physical damage risks are retained by the Pool up to $150,000 each occurrence, each location, with excess coverage reinsured by The Travelers Insurance Company.

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 a series of casualty claims, exhausts total members' equity plus and 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, 2010, settle claims have not exceeded the risk pool or reinsurance 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. If a member withdraws after the sixth year, the member is refunded 100 percent of its casualty 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 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.

(12) Deficit Balance

The Enterprise Water Fund had a deficit balance of $82,132 at June 30, 2012. City Council is monitoring the effects of 2011 rate increases to bring the fund into sounder financial health.

REQUIRED SUPPLEMENTARY INFORMATION

CITY OF SHELBY

BUDGETARY COMPARISON SCHEDULE OF RECEIPTS, DISBURSEMENTS, AND CHANGES IN BALANCES - BUDGET AND ACTUAL (CASH BASIS) - ALL GOVERNMENTAL FUNDS AND PROPRIETARY FUNDS

REQUIRED SUPPLEMENTARY INFORMATION

YEAR ENDED JUNE 30, 2012

	Governmental Funds Actual	Proprietary Funds Actual
Receipts:		
Property tax	$ 158,829	$ -0-
Tax increment financing	128,133	-0-
Other city tax	51,373	-0-
Licenses and permits	2,812	-0-
Use of money and permits	7,061	998
Intergovernmental	102,452	-0-
Charges for services	82,773	800,135
Special assessments	1,810	-0-
Miscellaneous	14,738	-0-
Total receipts	549,981	801,133
Disbursements:		
Public safety	91,854	-0-
Public works	104,520	-0-
Culture and recreation	37,311	-0-
Community and economic development	168,411	-0-
General government	72,263	-0-
Debt service	83,870	-0-
Capital projects	-0-	-0-
Business type activities	-0-	697,482
Total disbursements	558,229	697,482
Excess (deficiency) of receipts over (under) disbursements	(8,248)	103,651
Other financing sources, net	8,800	-0-
Excess (deficiency) of receipts and other financing sources over (under) disbursements and other financing uses	552	103,651
Balances beginning of year	1,115,864	498,801
Balances end of year	$ 1,116,416	$ 602,452

See Accompanying Independent Auditor's Report.

Total	Budgeted Amounts Original	Budgeted Amounts Final	Final to Total Variance
$ 158,829	$ 162,484	$ 162,484	$ (3,655)
128,133	127,205	127,205	928
51,373	49,521	49,521	1,852
2,812	2,600	2,600	212
8,059	-0-	-0-	8,059
102,452	317,000	332,000	(229,548)
882,908	727,700	727,700	155,208
1,810	2,000	2,000	(190)
14,738	8,000	8,000	6,738
1,351,114	1,396,510	1,411,510	(60,396)
91,854	85,900	100,900	9,046
104,520	190,500	190,500	85,980
37,311	47,100	47,100	9,789
168,411	177,205	177,205	8,794
72,263	84,050	84,050	11,787
83,870	84,000	84,000	130
-0-	-0-	-0-	-0-
697,482	1,130,350	1,130,350	432,868
1,255,711	1,799,105	1,814,105	558,394
95,403	(402,595)	(402,595)	497,998
8,800	-0-	-0-	8,800
104,203	(402,595)	(402,595)	506,798
1,614,665	1,614,665	1,614,665	-0-
$ 1,718,868	$ 1,212,070	$ 1,212,070	$ 506,798

CITY OF SHELBY

NOTES TO REQUIRED SUPPLEMENTARY INFORMATION - BUDGETARY REPORTING

JUNE 30, 2012

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

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

Formal and legal budgetary control is based upon ten major classes of disbursements known as functions, not by fund or fund type. These ten functions are: public safety, public works, health and social services, culture and recreation, community and economic development, general government, debt service, capital projects, business type activities and non-program. Function disbursements required to be budgeted include disbursements for the General Fund, Special Revenue Funds, Debt Service Fund, Capital Projects Funds and Proprietary Funds. Although the budget document presents function disbursements by fund, the legal level of control is at the aggregated function level, not by fund. During the year, one budget amendment increased budgeted receipts and disbursements by $15,000. The budget amendments are reflected in the final budgeted amounts.

During the year ended June 30, 2012, disbursements did not exceed the amounts budgeted.

OTHER SUPPLEMENTARY INFORMATION

SCHEDULE 1

CITY OF SHELBY

STATEMENT OF CASH RECEIPTS, DISBURSEMENTS AND CHANGES IN CASH BALANCES -

NON-MAJOR GOVERNMENTAL FUNDS

AS OF AND FOR THE YEAR ENDED JUNE 30, 2012

		Special Revenue				
	Capital Projects	Ed Nelson Scholarship Fund	Nielsen Memorial Fund	Economic Development	Ambulance Fund	Total
Receipts:						
Use of money and property	$ 25	$ 57	$ 31	$ -0-	$ 307	$ 420
Charges for services	-0-	-0-	-0-	-0-	17,198	17,198
Intergovernmental	2,200	-0-	-0-	-0-	-0-	2,200
Total receipts	2,225	57	31	-0-	17,505	19,818
Disbursements:						
Operations:						
Culture and recreation	-0-	200	-0-	-0-	-0-	200
Community and economic dev	-0-	-0-	-0-	-0-	-0-	-0-
Total disbursements	-0-	200	-0-	-0-	-0-	200
Excess (deficiency) of receipts over (under) disbursements	2,225	(143)	31	-0-	17,505	19,618
Other financing sources (uses)						
Operating transfer in	6,653	-0-	-0-	2,688	-0-	9341
Operating transfer out	(105)	-0-	-0-	-0-	(2,477)	(2,582)
Total other financing sources (uses)	6,548	-0-	-0-	2,688	(2,477)	6759
Net change in cash balances	8,773	(143)	31	2,688	15,028	26,377
Cash balances beginning of year	(8,773)	3,180	1,464	(2,688)	48,646	41,829
Cash balances end year	$ -0-	$ 3,037	$ 1,495	$ -0-	$ 63,674	$ 68,206
Cash Basis Fund Balances						
Assigned	$ -0-	$ 3,037	$ 1,495	$ -0-	$ 63,674	$ 68,206
Total cash basis fund balances	$ -0-	$ 3,037	$ 1,495	$ -0-	$ 63,674	$ 68,206

See Accompanying Independent Auditor's Report.

CITY OF SHELBY
STATEMENT OF INDEBTEDNESS
YEAR ENDED JUNE 30, 2012

Obligation	Date of Issue	Interest Rates		Amount Originally Issued
General Obligation:				
Sewer Improvement Notes	Sep 14, 2006	3.87% - 3.90%	$	500,000
Revenue Bonds:				
Water Revenue Bond	Apr 1, 2001	3.00%	$	600,000
Water Improvement Bond	Oct 19, 2001	3.53%	$	200,000

SCHEDULE 2

Balance Beginning of Year	Issued During Year	Redeemed During Year	Balance End of Year	Interest Paid	Interest Due and Unpaid
$ 100,000	$ -0-	$ 80,000	$ 20,000	$ 3,870	$ 65
$ 100,000	$ -0-	$ 80,000	$ 20,000	$ 3,870	$ 65
352,000	-0-	30,000	322,000	10,560	805
115,000	-0-	10,000	105,000	3,450	263
$ 467,000	$ -0-	$ 40,000	$ 427,000	$ 14,010	$ 1,068

See Accompanying Independent Auditor's Report.

SCHEDULE 3

CITY OF SHELBY
BOND AND NOTE MATURITIES
JUNE 30, 2012

General Obligation Bonds

Year Ended June 30,	Sewer Bond Issued Sep 14, 2006 Interest Rate	Amount	Total
2013	3.90%	$ 20,000	$ 20,000
2014	--	-0-	-0-
2015	--	-0-	-0-
2016	--	-0-	-0-
2017	--	-0-	-0-
2018	--	-0-	-0-
2019	--	-0-	-0-
2020	--	-0-	-0-
2021	--	-0-	-0-
Total		$ 20,000	$ 20,000

Revenue Bonds

Year Ended June 30,	Water Revenue Bond Issued Apr 1, 2001 Interest Rate	Amount	Water Improvement Bond Issued Oct 19, 2001 Interest Rate	Amount	Total
2013	3.00%	$ 31,000	3.00%	$ 10,000	$ 41,000
2014	3.00%	32,000	3.00%	11,000	43,000
2015	3.00%	33,000	3.00%	11,000	44,000
2016	3.00%	34,000	3.00%	11,000	45,000
2017	3.00%	36,000	3.00%	12,000	48,000
2018	3.00%	37,000	3.00%	12,000	49,000
2019	3.00%	38,000	3.00%	13,000	51,000
2020	3.00%	40,000	3.00%	13,000	53,000
2021	3.00%	41,000	3.00%	12,000	53,000
Total		$ 322,000		$ 105,000	$ 427,000

See Accompanying Independent Auditors' Report.

CITY OF SHELBY

SCHEDULE OF RECEIPTS BY SOURCE AND DISBURSEMENTS BY FUNCTION - ALL GOVERNMENTAL FUNDS

FOR THE LAST SIX YEARS

	2012	2011	2010
Receipts:			
Property tax	$ 158,829	$ 141,160	$ 99,487
Tax Increment Financing	128,133	129,851	283,957
Other city taxes	51,373	53,099	47,827
Licenses and permits	2,812	2,793	2,075
Use of money and property	7,061	7,430	5,848
Intergovernmental	102,452	98,615	127,924
Charges for services	82,773	50,451	69,827
Special assessments	1,810	595	407
Miscellaneous	14,738	24,976	5,357
Total	$ 549,981	$ 508,970	$ 642,709
Disbursements:			
Public safety	$ 91,854	$ 59,869	$ 113,448
Public works	104,520	199,148	226,085
Culture and recreation	37,311	38,058	89,484
Economic development	168,411	168,354	85,899
General government	72,263	53,828	54,452
Debt service	83,870	81,738	85,184
Capital projects	-0-	18,865	5,166
Total	$ 558,229	$ 619,860	$ 659,718

See Accompanying Independent Auditor's Report.

	2009	2008	2007
Receipts:			
Property tax	$ 111,973	$ 93,862	$ 78,458
Tax Increment Financing	280,309	27,855	71,776
Other city taxes	48,846	46,200	35,700
Licenses and permits	1,206	2,728	993
Use of money and property	14,826	32,893	41,218
Intergovernmental	148,547	1,260,960	427,174
Charges for services	58,066	58,697	42,882
Special assessments	3,000	7,100	4,050
Miscellaneous	14,456	27,642	36,538
Total	$ 681,229	$ 1,557,937	$ 738,789
Disbursements:			
Public safety	$ 79,611	$ 55,512	$ 67,563
Public works	171,170	185,612	86,349
Culture and recreation	27,035	12,008	44,990
Economic development	101,711	148,769	151,450
General government	50,507	118,648	87,726
Debt service	150,281	87,916	6,773
Capital projects	70,686	1,118,127	575,550
Total	$ 651,001	$ 1,726,592	$ 1,020,401

See Accompanying Independent Auditor's Report.

INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS

MUXFELDT
ASSOCIATES, CPA, P.C.
Certified Public Accountant

August 10, 2012

Lonnie G. Muxfeldt
Certified Public Accountant

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INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS

To the Honorable Mayor and
Members of the City Council:

I have audited the accompanying financial statements of the governmental activities, the business type activities, each major fund and the aggregate remaining fund information of the City of Shelby, Iowa, 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 my report thereon dated August 10, 2012. My report expressed unqualified opinions on the financial statements which were prepared in conformity with an other comprehensive basis of accounting. I conducted my audit in accordance with U.S. generally accepted auditing standards and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing my audit, I considered the City of Shelby's internal control over financial reporting as a basis for designing my auditing procedures for the purpose of expressing my opinions on the financial statements, but not for the purpose of expressing my opinion of the effectiveness of the City of Shelby's internal control over financial reporting. Accordingly, I do not express an opinion on the effectiveness of the City of Shelby's internal control over financial reporting.

My 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, I identified certain deficiencies in internal control over financial reporting that I consider to be material weaknesses and other deficiencies I consider to be significant deficiencies.

Continued. . .

A deficiency in internal control exists when the design or operation of the control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A 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 of Shelby's financial statements will not be prevented or detected and corrected on a timely basis. I consider the deficiencies described in Part I of the accompanying Schedule of Findings as items I-A-12 and I-B-12 to be material weaknesses.

A significant deficiency is a deficiency, or a combination of deficiencies, in internal control which is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the City of Shelby's financial statements are free of material misstatement, I 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 my audit and, accordingly, I do not express such an opinion. The results of my tests disclosed no instances of non-compliance or other matters that are required to be reported under *Government Auditing Standards*. However, I noted certain immaterial instances of non-compliance that are described in the accompanying Schedule of Findings.

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 my audit of the financial statements of the City. Since my audit was based on tests and samples, not all transactions that might have had an impact on the comments were necessarily audited. The comments involving statutory and other legal matters are not intended to constitute legal interpretation of those statutes.

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

Continued. . .

August 10, 2012

To the Honorable Mayor and
Members of the City Council:
Page Three

This report, a public record by law, is intended solely for the information and use of the officials, employees and citizens of the City of Shelby and other parties to whom the City of Shelby may report, including federal awarding agencies and pass-through entities. This report is not intended to be and should not be used by anyone other than these specified parties.

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

Muffelt Associates, CPA, P.C.

CITY OF SHELBY
SCHEDULE OF FINDINGS
YEAR ENDED JUNE 30, 2012

PART I: Findings Related to the Financial Statements

INTERNAL CONTROL DEFICIENCIES;

I-A-12 Segregation of Duties

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

Recommendation - I realize that with only one full-time clerk and a part-time office employee, segregation of duties among employees is impossible. The City should review its control procedures to obtain the maximum internal control possible under the circumstances. For example, the part-time employee also serves as the City Treasurer and could easily review the receipts listings, bank deposits and postings to ensure procedures are being followed. On the disbursement side, the City Treasurer could review the claims list for completeness and City Council could sign the claims list as an indication of its supervision and approval.

Response - The recommended procedures are easily implemented without additional personnel. We will review our control procedures to incorporate the City Treasurer and City Council in a supervisory role.

Conclusion - Response accepted.

PART II: Findings Related to the Financial Statements (Continued)

I-B-12 Unrecorded Transfer

Comment - It was noted that a $81,935 transfer from the urban renewal fund to the debt service fund was not recorded for the year ended June 30, 2012. The oversight resulted in a potential deficit balance in the debt service fund. Adjustments were subsequently made to correctly report transfers and fund balances in the City's financial statements.

Recommendation - Tax increment financing funds the payments of principal and interest on the general obligation sewer bonds of the Interstate Project. Amounts equivalent to the principal and interest payments should be transferred to the debt service fund each year. Transfers should always be approved by Council resolution.

Response - The transfer was authorized by City Council but was inadvertently not recorded on the City's books. Authorized transfers will be recorded in the future.

Conclusion - Response accepted.

INSTANCES OF NON-COMPLIANCE:

No matters were noted.

CITY OF SHELBY
SCHEDULE OF FINDINGS
YEAR ENDED JUNE 30, 2012

PART II Other Findings Related to Statutory Reporting

II-A-12 Certified Budget - Disbursements during the year ended June 30, 2012, did not exceed the amounts budgeted in the governmental and business type activities functions.

II-B-12 Questionable Disbursements - I noted no disbursements for parties, banquets or other entertainment for employees that I believe may constitute an unlawful expenditure from public funds 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 Business Transactions - Business transactions between the City and City officials or employees are detailed as follows:

Name, Title, and Business Connection	Transaction Description		Amount
Doyle Gilland, Councilor Gilland Trucking	Trucking related to street maintenance	$	6,625

In accordance with Chapter 362.5(10) of the Code of Iowa, the transactions with the Councilor do not appear to represent a conflict of interest since it was entered into through competitive bidding in accordance with Chapter 362.5(3)(d) of the Code of Iowa.

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

The City did not published annual gross salaries in accordance with an Attorney General's opinion dated April 12, 1978.

Recommendation - The City should comply and publish annual gross salaries.

Response - We will publish annual gross salaries as required in the future.

Conclusion - Response accepted.

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

II-G-12 Deposits and Investments - No instances of noncompliance with the deposit and investment provisions of Chapter 12B and 12C of the Code of Iowa were noted.

II-H-12 Revenue Bonds and Notes - The City has complied with the revenue bond and note resolutions.

II-I-12 Financial Condition - The Enterprise Water Fund had a deficit balance of $82,132 at June 30, 2012.

Recommendation - The City should investigate alternatives to eliminate this deficit in order to return this fund to a sound financial position.

Response - City Council amended Ordinance No. 92 on March 1, 2011 and increased water rates to reduce the Water Fund deficit. City Council will monitor the Water Fund Deficit and propose further rate increases if necessary.

Conclusion - Response accepted.

CITY OF SHELBY

SHELBY, IOWA 51570

NEWS RELEASE

Muxfeldt Associates, CPA, P.C., 2309 B Chatburn Avenue, Harlan, Iowa, today released an audit report on the City of Shelby, Iowa.

The City's receipts totaled $1,359,914 for the year ended June 30, 2012, a 2.57 percent increase from 2011. The receipts included $158,829 in property tax, $128,133 from tax increment financing, $935,819 from charges for services, $72,096 from operating grants, contributions and restricted interest, $6,700 from capital grants, contributions and restricted interest, $47,533 for local option sales tax, $2,004 from unrestricted interest on investments and $8,800 from the sale of property.

Disbursements for the year totaled $1,255,711, a 6.26 per cent decrease from the prior year, and included $168,411 for community and economic development, $104,520 for public works, and $91,854 for public safety. Also, disbursements for business type activities totaled $697,482.

A copy of the audit report is available for review in the City Clerk's office, in the Office of Auditor of State and on the Auditor of State's web site at http://auditor.iowa.gov/reports/reports.htm.