

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

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

June 30, 2012

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**Keokuk Municipal Water Works,
A Component Unit of the City of Keokuk
Board of Trustees
June 30, 2012**

<u>Trustee</u>	<u>Title</u>	<u>Term Expires</u>
Edward Johnstone	Trustee, Chairman	November 1, 2017
Mike Hausch	Trustee, Vice Chairman	November 1, 2017
Bruce Brandt	Trustee	November 1, 2013
John Beaird	Trustee	November 1, 2015
Dave Bogner	Trustee	November 1, 2015
Bill Cole	Manager	
Shari Dunagan	Office Manager	



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Independent Auditor's Report

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

We have audited the accompanying statement of net assets of the proprietary fund of the Keokuk Municipal Water Works (Water Works), a Component Unit of the City of Keokuk, as of June 30, 2012, and the related statement of revenues, expenses and changes in fund net assets and the statement of cash flows of its proprietary fund for the year then ended. These financial statements are the responsibility of the Water Works' management. Our responsibility is to express an opinion on these financial statements based on our audit.

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

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

In our opinion, except for the omission of the information described in the preceding paragraph, the financial statements referred to above present fairly, in all material respects, the financial position of the Water Works at June 30, 2012, and the changes in its net assets and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated November 20, 2012 on our consideration of the Water Works' internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grants, and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing and not to provide an opinion on internal controls over financial reporting or compliance. That report is an integral part of the audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 4 through 9 and budgetary comparison on pages 22 through 23 be present to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Our audits were conducted for the purpose of forming an opinions on the financial statements that collectively comprise the Water Works' financial statements as a whole. The supplemental information included on pages 24 through 25 is presented for purposes of additional analysis and is not a required part of the financial statements. The supplemental information is the responsibility of management and was derived from and relates 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 the audit of the 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 auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.

CPA Associates PC

November 20, 2012

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

The following Management Discussion and Analysis (MD&A) of the Keokuk Municipal Water Works' activities and financial performance provides the reader with an introduction and overview to the financial statements of the Keokuk Municipal Water Works (Water Works) for the fiscal year ended June 30, 2012. The information contained in this MD&A should be considered in conjunction with the Water Works' basic financial statements.

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

Financial Operations Highlights

As a result of this year's operations, assets exceeded liabilities by \$23.4 million (net assets) for the fiscal year reported. This compares to the previous year when assets exceeded liabilities by \$22.3 million. The net assets increased by \$1,089,085 or 4.9%.

Total net assets are comprised of the following:

- Net assets invested in capital assets (e.g., main extensions, buildings, improvements, and equipment), less the related indebtedness outstanding used to acquire those capital assets is \$20,101,785. This balance represents resources allocated to capital assets. These capital assets, less accumulated depreciation, are shown at depreciated cost of \$35,660,739.
- Restricted net assets of \$2,017,623 represent resources that are subject to external restrictions such as grantors, laws, debt covenants or regulations.
- Unrestricted net assets of \$1,273,060 represent resources that can be used at the discretion of management and the Board of Trustees.

During the year, revenues increased \$283,400, or 4.23%, while operating expenses increased \$215,100, or 3.92%. The increase in revenues is due to an increase in water rates.

Net nonoperating expenses increased \$43,500 or 10.00% and are primarily attributable to the increase in interest expense.

The Water Works also recognized capital contributions of \$281,625 in the current year related to an EDA grant received for the water tower construction project.

Using This Annual Report

The Water Works is governed by a Board of Trustees, appointed by the Mayor and approved by the City Council. The Water Works is organized as an Enterprise Fund and is a component unit of the City of Keokuk, Iowa. This discussion and analysis is intended to serve as an introduction to the Water Works' basic financial statements. The annual report consists of a series of financial statements and other information as follows:

- Management's Discussion and Analysis introduces the basic financial statements and provides an analytical overview of the Keokuk Municipal Water Works' financial activities.

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

Using This Annual Report (continued)

- The Financial Statements consist of a Statement of Net Assets, Statement of Revenues, Expenses and Changes in Fund Net Assets, and Statement of Cash Flows. These provide information about the activities of the Water Works as a whole and present an overall view of the Water Works' finances.
- The Financial Statements tell how services were financed in the short term as well as what remains for future spending.
- Notes to Financial Statements provide additional information essential to a full understanding of the data provided in the basic financial statements.
- Required Supplementary Information further explains and supports the financial statements with a comparison of the Water Works' budget for the year.

Financial Position Summary

Net assets may serve over time as a useful indicator of the Water Works' financial position. The Water Works' net assets exceeded liabilities by \$23.4 million at June 30, 2012, an increase of \$1,089,085 from 2011.

A condensed summary of the Water Works' net assets at June 30, 2012 and 2011 is shown below:

	2012	2011
Assets:		
Current, restricted and other assets	\$ 4,798,520	\$ 4,393,883
Capital assets	<u>35,660,739</u>	<u>35,419,603</u>
Total assets	<u>\$ 40,459,259</u>	<u>\$ 39,813,486</u>
Liabilities:		
Current liabilities	\$ 2,726,837	\$ 3,060,603
Long-term debt	<u>14,339,954</u>	<u>14,449,500</u>
	17,066,791	17,510,103
Net Assets:		
Invested in capital assets, net of related debt	20,101,785	19,852,103
Restricted funds	2,017,623	2,098,539
Unrestricted	<u>1,273,060</u>	<u>352,741</u>
Total liabilities and net assets	<u>\$ 40,459,259</u>	<u>\$ 39,813,486</u>

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

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

Summary of Operations and Changes in Net Assets

	2012	2011
Net operating revenues	\$ 6,986,677	\$ 6,703,300
Net operating expenses	<u>5,700,969</u>	<u>5,485,856</u>
Net operating income	<u>1,285,708</u>	<u>1,217,444</u>
Nonoperating income and expenses:		
Interest income	66,346	79,506
Interest expense and amortization	<u>(544,594)</u>	<u>(514,295)</u>
Net nonoperating expense	<u>(478,248)</u>	<u>(434,789)</u>
Capital contributions	<u>281,625</u>	<u>871,461</u>
Increase in net assets	<u>\$ 1,089,085</u>	<u>\$ 1,654,116</u>

Revenues

A summary of revenues for the year ended June 30, 2012, and the amount and percentage of change in relation to prior year amounts, is as follows:

	2012 <u>Amount</u>	% of <u>Total</u>	Increase (Decrease) from Prior <u>Year</u>	% Increase (Decrease)
Operating				
Water sales	\$ 6,859,948	93.53	\$ 269,327	4.09
Miscellaneous charges	74,382	1.01	15,395	26.10
Service charges and penalties	<u>52,347</u>	<u>0.71</u>	<u>(1,345)</u>	(2.51)
Total operating	6,986,677	95.25	283,377	4.23
Nonoperating income				
Interest income	66,346	0.90	(13,161)	(16.55)
Capital contributions - EDA grant	<u>281,625</u>	<u>3.85</u>	<u>(589,836)</u>	(67.68)
Total revenues	<u>\$ 7,334,648</u>	<u>100.00</u>	<u>\$ (319,620)</u>	(4.18)

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

Expenses

A summary of expenses for the year ended June 30, 2012, and the amount and percentage of change in relation to prior year amounts, is as follows:

	<u>2012</u> <u>Amount</u>	<u>% of</u> <u>Total</u>	<u>Increase</u> <u>(Decrease)</u> <u>from Prior</u> <u>Year</u>	<u>% Increase</u> <u>(Decrease)</u>
Operating				
Operating expenses	\$ 4,393,645	70.35	\$ 90,563	2.10
Depreciation	<u>1,307,324</u>	<u>20.93</u>	<u>124,550</u>	10.53
Total operating	5,700,969	91.28	215,113	3.92
Nonoperating expense				
Interest expense and amortization	<u>544,594</u>	<u>8.72</u>	<u>30,300</u>	5.89
Total expenses	<u>\$ 6,245,563</u>	<u>100.00</u>	<u>\$ 245,413</u>	4.09

The increase in expenses during the fiscal year is primarily attributable to depreciation expense.

Summary of Cash Flow Activities

The following shows a summary of the major sources and uses of cash and cash equivalents for the years ended June 30, 2012 and 2011. Cash equivalents are considered to be cash-on-hand, bank deposits and highly liquid investments with an original maturity of three months or less.

	2012	2011
Net cash provided by operating activities	\$ 2,478,470	\$ 2,335,094
Net cash provided (used) by investing activities	(432,762)	585,099
Net cash used by capital and related financing activities	<u>(2,256,789)</u>	<u>(2,490,600)</u>
Net increase (decrease) in cash and cash equivalents	(211,081)	429,593
Cash and cash equivalents, beginning of year	<u>2,055,364</u>	<u>1,625,771</u>
Cash and cash equivalents, end of year	<u>\$ 1,844,283</u>	<u>\$ 2,055,364</u>

Financial Statements

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

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

Long-term Debt

At June 30, 2012, the Water Works had \$15,558,954 in debt outstanding. This debt is from refinancing of the 1995 and 1996 Bonds in April 2004 and January 2005; 2008 debt of \$3.8 million for water filters; \$1.6 million Forgivable Loan and \$2.7 million 2010 bonds issued in connection with the water tower construction project and a \$50,954 interim loan and disbursement agreement for the planning and design of the chlorine generation system.

Capital Acquisitions and Construction Activities

At June 30, 2012, the Water Works had \$53,054,502 in capital assets. Capital expenditures totaled \$1,943,039, a decrease of 61% over 2011. A summary of projects follows:

Distribution System:

- Purchase of Meters

Water Treatment Plant:

- Control System
- Carbon Feed Pumps
- High Service Pump
- Backwash Pump
- Engineering for Chlorine Generation System
- Sludge handling facility, pumps and equipment

Water Tower South 7th Street:

- Engineering and construction of water tower

Equipment:

- Air Compressor

Property:

- 2215 Johnson Street

Transportation:

- 2011 Chevy Malibu
- 2012 Ford XL F150

Mains:

- 7th and 8th on Des Moines Street
- 19th and 20th on Franklin Street

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

Economic Factors

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

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

For the fiscal year ending June 30, 2012, the Water Works has already entered into the following capital improvement projects:

Water Plant:

- Engineering and design for the Chlorine Generation System located at the water plant at 118 North Water Street.

Request for Information

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

**Keokuk Municipal Water Works,
A Component Unit of the City of Keokuk
Statement of Net Assets - Proprietary Fund
June 30, 2012**

Assets	
Current Assets	
Cash and cash equivalents	\$ 421,140
Accrued interest receivable	33,375
Accounts receivable	752,489
Grant receivable	200,000
Prepaid expenses	93,850
Total current assets	<u>1,500,854</u>
Restricted Assets	
Cash and cash equivalents	1,423,143
Accounts receivable	261,488
Certificates of deposit	783,825
Guaranteed investment contracts	737,750
	<u>3,206,206</u>
Property, Plant and Equipment	
Property, plant and equipment, at cost	53,054,502
Less accumulated depreciation	<u>(17,393,763)</u>
	<u>35,660,739</u>
Other Assets	
Unamortized bond issuance costs, net of accumulated amortization of \$237,032	<u>91,460</u>
	<u>\$ 40,459,259</u>
Liabilities	
Current Liabilities	
Accounts payable	\$ 369,338
State sales tax payable	4,835
Accrued salaries and vacation	281,480
Accrued interest payable	114,788
Current portion long-term debt	1,219,000
Due to city - sewer and garbage charges	465,255
Consumer water meter deposits	176,403
Consumer sewer meter deposits	95,738
Total current liabilities	<u>2,726,837</u>
Long-term Debt, net of current portion	<u>14,339,954</u>
	<u>17,066,791</u>
Net Assets	
Invested in capital assets, net of related debt	20,101,785
Restricted	
Sinking fund	332,469
Reserve fund	1,433,575
Improvement fund	251,579
Unrestricted	1,273,060
	<u>23,392,468</u>
	<u>\$ 40,459,259</u>

See notes to financial statements.

**Keokuk Municipal Water Works,
A Component Unit of the City of Keokuk
Statement of Revenues, Expenses and Changes in Fund Net Assets - Proprietary Fund
For the Year Ended June 30, 2012**

Operating Revenues	
Water sales	\$ 6,859,948
Miscellaneous charges	74,382
Service charges and penalties	<u>52,347</u>
Total operating revenues	<u>6,986,677</u>
Operating Expenses	
Operating expenses	4,393,645
Depreciation	<u>1,307,324</u>
Total operating expenses	<u>5,700,969</u>
Net operating income	<u>1,285,708</u>
Nonoperating income (expenses)	
Interest income	66,346
Interest expense	(501,864)
Amortization	<u>(42,730)</u>
Total nonoperating expenses	<u>(478,248)</u>
807,460	
Capital contributions - EDA grant	<u>281,625</u>
Change in net assets	1,089,085
Net assets, beginning of year	<u>22,303,383</u>
Net assets, end of year	<u>\$ 23,392,468</u>

See notes to financial statements.

**Keokuk Municipal Water Works,
A Component Unit of the City of Keokuk
Statement of Cash Flows - Proprietary Fund
For the Year Ended June 30, 2012**

Cash Flows from Operating Activities	
Receipts from customers	\$ 6,754,716
Receipts from service charges and miscellaneous	130,989
Meter deposits received, net	12,140
Payments to suppliers	(3,140,217)
Payments to employees	(1,079,158)
Payments for interfund services	<u>(200,000)</u>
Net cash provided by operating activities	<u>2,478,470</u>
Cash Flows from Capital and Related Financing Activities	
Purchases of capital assets	(1,943,039)
Capital grant received	243,860
Principal payments on long-term debt	(1,117,000)
Principal borrowings on long-term debt	1,108,454
Interest payments on long-term debt	<u>(549,064)</u>
Net cash used by capital and related financing activities	<u>(2,256,789)</u>
Cash Flows from Investing Activities	
Purchases of certificates of deposit	(568,720)
Redemptions of certificates of deposit	78,000
Interest income	<u>57,958</u>
Net cash used by investing activities	<u>(432,762)</u>
Net decrease in cash and cash equivalents	(211,081)
Cash and cash equivalents, beginning of year	<u>2,055,364</u>
Cash and cash equivalents, end of year	<u>\$ 1,844,283</u>
Reconciliation of Operating Income to Net Cash Provided by Operating Activities	
Operating income	\$ 1,285,708
Adjustments to reconcile operating income to net cash provided by operating activities:	
Depreciation expense	1,307,324
Changes in assets and liabilities:	
Receivables and prepaids	(121,575)
Accounts payable and accrued expenses	<u>7,013</u>
Net cash provided by operating activities	<u>\$ 2,478,470</u>
Supplemental Disclosure of Noncash Capital and Related Financing Activities	
Equipment purchases financed through accounts payable	\$ 291,618
Capitalized interest on assets under construction	42,842

See notes to financial statements.

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

Note 1. Summary of Significant Accounting Policies

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

Reporting Entity

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

The Governmental Accounting Standards Board (GASB) has set forth criteria to be considered in determining financial accountability. These criteria include appointing a voting majority of an organization's governing body, and (1) the ability of the entity to impose its will on that organization, or (2) the potential for the organization to provide specific benefits to, or impose specific financial burdens on, the entity.

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

Measurement Focus, Basis of Accounting and Financial Statement Presentation

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

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

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

Note 1. Summary of Significant Accounting Policies (continued)

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

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

Assets, Liabilities and Fund Equity

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

Cash and Cash Equivalents

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

Accounts Receivable

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

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

Restricted Assets

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

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

Note 1. Summary of Significant Accounting Policies (continued)

Amortization of Water Revenue Refunding Capital Loan Note Fees

During the prior years, the Water Works incurred costs of \$328,492 in connection with the 2004A, 2005A, 2008 and 2010 Series Water Revenue Refunding Capital Loan Notes. These costs are being ratably amortized on a monthly basis over the life of the Capital Loan Notes until the first call date. The amortization expense for the year ended June 30, 2012 was \$42,730.

Property and Equipment

Property and equipment are accounted for at historical cost. Property and equipment is defined by the Water Works as assets with an estimated useful life in excess of one year. Property and equipment is depreciated using the straight line method over the following estimated useful lives:

Buildings	10-30 years
Plant and Tanks	10-100 years
Distribution system, meters and hydrants	10-80 years
Machinery and equipment	5-30 years

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

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

Compensated Absences

Water Works employees accumulate a limited amount of earned but unused vacation and sick leave hours for subsequent use or for payment upon termination, retirement or death. The Water Works' liability for accumulated vacation and sick leave has been computed based on rates in effect at June 30, 2012.

Budgets and Budgetary Accounting

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

Use of Estimates

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

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

Note 2. Restricted Assets

Restricted assets consist of the following as of June 30, 2012:

	Cash and cash equivalents	Accounts receivable	Certificates of deposit	Guaranteed investment contract
Sewer, garbage and landfill	\$ 203,767	\$ 261,488	\$ -	\$ -
Consumer water meter deposits	176,403	-	-	-
Consumer sewer meter deposits	7,738	-	88,000	-
Sinking fund	332,469	-	-	-
Reserve fund	-	-	695,825	737,750
Improvement fund	251,579	-	-	-
General regulatory and system improvements	451,187	-	-	-
	<u>\$ 1,423,143</u>	<u>\$ 261,488</u>	<u>\$ 783,825</u>	<u>\$ 737,750</u>
Total restricted assets				

Note 3. Property and Equipment

Changes in property and equipment as June 30, 2012 consist of the following:

	Balance Beginning of year	Increases	Decreases	Balance End of year
Property and equipment not being depreciated/amortized:				
Land	\$ 458,266	\$ 3,500	\$ -	\$ 461,766
Construction in progress	7,264,249	900,256	(8,057,868)	106,637
Total capital assets not being depreciated/amortized	<u>7,722,515</u>	<u>903,756</u>	<u>(8,057,868)</u>	<u>568,403</u>
Property and equipment being depreciated/amortized:				
Building	397,739	71,978	-	469,717
Plant and tanks	36,753,694	8,535,824	-	45,289,518
Distribution system, meters and hydrants	5,847,010	24,663	-	5,871,673
Machinery and equipment	797,634	70,107	(12,550)	855,191
Total property and equipment being depreciated/amortized	<u>43,796,077</u>	<u>8,702,572</u>	<u>(12,550)</u>	<u>52,486,099</u>
Less accumulated depreciation/amortization for:				
Building	235,307	11,229	-	246,536
Plant and tanks	12,981,304	1,173,651	-	14,154,955
Distribution system, meters and hydrants	2,228,354	93,296	-	2,321,650
Machinery and equipment	654,024	29,148	(12,550)	670,622
Total accumulated depreciation/amortization	<u>16,098,989</u>	<u>1,307,324</u>	<u>(12,550)</u>	<u>17,393,763</u>
Total property and equipment, net	<u>\$ 35,419,603</u>	<u>\$ 8,299,004</u>	<u>\$ (8,057,868)</u>	<u>\$ 35,660,739</u>

For the year ended June 30, 2012, the Water Works capitalized interest of \$42,842, for the interest costs incurred relating to the construction of the property.

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

Note 4. Pension and Retirement Benefits

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

Plan members are required to contribute 5.38% of their annual salary and the Water Works is required to contribute 8.07% of annual covered payroll. Contribution requirements are established by State statute. The Water Works' contribution to IPERS for the years ended June 30, 2012, 2011 and 2010 was \$85,404, \$74,124 and \$67,013, respectively, which was equal to the required contribution.

Note 5. Deposits

The Water Works' 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 Water Works is authorized by statute to invest public funds in obligations of the United States government, its agencies and instrumentalities; certificates of deposit or other evidences of deposit at federally-insured depository institutions approved by the Water Works and the Treasurer of the State of Iowa; prime eligible bankers acceptances; certain high-rated commercial paper; perfected repurchase agreements; certain registered open-end management investment companies; certain joint investment trusts; and warrants or improvement certificates of a drainage district.

Note 6. Bonds and Long-Term Debt

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

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

Note 6. Bonds and Long-Term Debt (continued)

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

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

On February 10, 2010, the Water Works issued \$3,777,000 in Water Revenue Refunding Capital Loan Notes. The Water Works entered into an escrow agreement with Wells Fargo Bank, N.A., the trustee of the master trust of the Iowa Finance Authority, and deposited the proceeds from the notes. The proceeds are to be used to fund the water tower construction project. These notes mature semi-annually beginning June 1, 2010 through June 1, 2031, with a 3.00% interest rate.

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

On December 7, 2011, the Water Works entered into an interim loan and disbursement agreement with Iowa Finance Authority for the planning and design phase of the Chlorine Generation System. This agreement matures December 7, 2014, with an interest rate of 0.00%.

A summary of changes in long-term debt for the year ended June 30, 2012 is as follows:

	Balance Beginning of Year	Increases	Decreases	Balance End of Year	Due Within One Year
2004A Series Revenue notes	\$ 4,900,000	\$ -	\$ (470,000)	\$ 4,430,000	\$ 485,000
2005A Series Revenue notes	3,165,000	-	(295,000)	2,870,000	310,000
2008 Series Revenue notes	3,180,000	-	(215,000)	2,965,000	220,000
2010 Series Revenue notes	2,719,500	1,057,500	(137,000)	3,640,000	141,000
2010 Series Revenue notes	1,603,000	-	-	1,603,000	63,000
Interim Loan and Disbursement Agreement	-	50,954	-	50,954	-
Total Revenue notes	<u>\$ 15,567,500</u>	<u>\$ 1,108,454</u>	<u>\$ (1,117,000)</u>	<u>\$ 15,558,954</u>	<u>\$ 1,219,000</u>

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

Note 6. Bonds and Long-Term Debt (continued)

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

Year Ending June 30,	\$7,000,000 Water Revenue Refunding Capital Loan Notes Series 2004A		\$4,505,000 Water Revenue Refunding Capital Loan Notes Series 2005A		\$3,800,000 Water Revenue Capital Loan Notes Series 2008	
	Principal	Interest	Principal	Interest	Principal	Interest
	2013	\$ 485,000	\$ 173,474	\$ 310,000	\$ 127,432	\$ 220,000
2014	500,000	156,627	320,000	114,734	235,000	107,213
2015	520,000	138,318	330,000	101,188	240,000	99,018
2016	540,000	118,363	350,000	86,738	245,000	90,288
2017	560,000	96,628	365,000	71,005	255,000	80,911
2018-2022	1,825,000	143,697	1,195,000	105,039	1,445,000	240,322
2023-2027	-	-	-	-	325,000	10,495
	<u>\$ 4,430,000</u>	<u>\$ 827,107</u>	<u>\$ 2,870,000</u>	<u>\$ 606,136</u>	<u>\$ 2,965,000</u>	<u>\$ 742,972</u>

Year Ending June 30,	\$3,777,000 Water Revenue Refunding Capital Loan Notes Series 2010		\$1,603,000 Forgivable Loan Water Revenue Capital Loan Notes Series 2010		Interim Loan and Disbursement Agreement Principal	Total	
	Principal	Interest	Principal	Interest		Principal	Interest
	2013	\$ 141,000	\$ 109,200	\$ 63,000		\$ 48,060	\$ -
2014	146,000	104,970	64,000	46,200	-	1,265,000	529,744
2015	151,000	100,590	66,000	44,280	50,954	1,357,954	483,394
2016	156,000	96,060	69,000	42,300	-	1,360,000	433,749
2017	161,000	91,380	71,000	40,230	-	1,412,000	380,154
2018-2022	886,000	381,330	389,000	167,950	-	5,740,000	1,038,338
2023-2027	1,039,000	239,460	458,000	105,540	-	1,822,000	355,495
2028-2031	960,000	73,200	423,000	32,220	-	1,383,000	105,420
	<u>\$ 3,640,000</u>	<u>\$ 1,196,190</u>	<u>\$ 1,603,000</u>	<u>\$ 526,780</u>	<u>\$ 50,954</u>	<u>\$ 15,558,954</u>	<u>\$ 3,899,185</u>

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

A. Rate Covenant

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

B. Sinking Fund

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

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

Note 6. Bonds and Long-Term Debt (continued)

C. Reserve Fund

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

D. Improvement Fund

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

Note 7. Risk Management

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

Note 8. Major Customers

Water sales to one major customer was \$4,800,115 for the year ended June 30, 2012, representing approximately 69% of the total operating revenue for the year. At June 30, 2012, the amount due from this customer was \$472,729, which is included in accounts receivable.

Note 9. Related Party Transactions

The Water Works had business transactions with one employee amounting to \$5,222 during the year ended June 30, 2012.

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

Note 10. Related Organization

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

The Water Works provides billing service for sewer and garbage for the City of Keokuk and collects fees for these services. Total fees collected for the City were \$2,621,463 and billing service fees received by Water Works amounted to \$23,444 for the year ending June 30, 2012. Amounts due to the City as of June 30, 2012 were \$465,255 for sewer and garbage charges and \$1,726 for vehicle cost reimbursement.

The Water Works made a payment in lieu of taxes to the City of Keokuk for \$200,000 for the year ended June 30, 2012.

Note 11. Subsequent Events

The Water Works performed an evaluation of subsequent events through November 20, 2012, which is the date the financial statements were issued. The Water Works borrowed an additional \$39,156 from the Interim Loan and Disbursement Agreement with Iowa Finance Authority.

Note 12. Prospective Accounting Change

GASB has issued two Statements not yet implemented by the Water Works. Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*, will be effective for the Water Works for the fiscal year ending June 30, 2013. This Statement redefines the components of the statement of net assets. In the year that Statement No. 63 is implemented, the prior year financial statements will be retroactively restated for comparison perspective. Statement No. 65, *Items Previously Reported as Assets and Liabilities*, will be effective for the Water Works for the fiscal year ending June 30, 2014. This Statement establishes accounting and financial reporting standards that reclassify, as deferred outflows of resources or deferred inflows of resources, certain items that were previously reported as assets and liabilities and recognizes, as outflows of resources or inflows of resources, certain items that were previously reported as assets and liabilities. In the year that Statement No. 65 is implemented, the beginning net assets will be retroactively restated for prior periods presented. The Water Works' management has not yet determined the effect these Statements will have on the Water Works' financial statements.

**Keokuk Municipal Water Works,
A Component Unit of the City of Keokuk
Required Supplementary Information
Comparison of Cash Receipts and Disbursements - Actual to Budget
Year Ended June 30, 2012**

	<u>Actual</u>	<u>Budgeted Amounts Final</u>	<u>Budgeted Amounts Original</u>	<u>Variance: Favorable (Unfavorable)</u>
Receipts	\$ 6,897,845	\$ 6,747,578	\$ 6,747,578	\$ 150,267
Disbursements	<u>6,362,414</u>	<u>6,978,517</u>	<u>5,955,256</u>	<u>616,103</u>
Net	535,431	(230,939)	792,322	766,370
Other financing sources, net	<u>(746,512)</u>	<u>230,939</u>	<u>(792,322)</u>	<u>(977,451)</u>
Changes in cash and cash equivalents	<u>\$ (211,081)</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ (211,081)</u>

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

Changes in cash and cash equivalents, as presented above	\$ (211,081)
Add: Cash expenditures for property, plant and equipment capitalized under GAAP	1,943,039
Add: Cash expenditures for long-term debt interest payments capitalized under GAAP	42,842
Add: Cash expenditures for long-term debt principal payments	1,117,000
Add: Change in accounts receivable and prepaids	121,575
Add: Change in accrued interest receivable	8,388
Add: Change in accrued interest payable	4,358
Add: Change in grant receivable	37,765
Add: Cash expenditure for purchases of certificates of deposit	568,720
Subtract: Cash receipts from redemption of certificates of deposit	(78,000)
Subtract: Change in accounts payable and accrued expenses	(7,013)
Subtract: Amortization expense	(42,730)
Subtract: Depreciation expense	(1,307,324)
Subtract: Cash proceeds for long-term debt issuance	<u>(1,108,454)</u>
Changes in net assets, as presented in Statement of Revenues, Expenses and Changes in Fund Net Assets	<u>\$ 1,089,085</u>

See accompanying independent auditor's report.

Keokuk Municipal Water Works
A Component Unit of the City of Keokuk
Required Supplementary Information
Notes to Required Supplementary Information - Actual to Budget
Year Ended June 30, 2012

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

Formal and legal budgetary control is based upon classes of disbursements known as functions, not by fund or category type. The Water Works' disbursements are budgeted in the business type activities function. The Water Works' budget is reflected in the original and final budgeted amount. During the year, a budget amendment increased disbursements by \$1,023,000. This budget amendment is reflected in the final budgeted amounts.

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

See accompanying independent auditor's report.

**Keokuk Municipal Water Works,
A Component Unit of the City of Keokuk
Schedule of Changes in Assets Restricted
for Landfill, Sewer and Garbage Charges
Year Ended June 30, 2012**

	Landfill Charges	Sewer Charges	Garbage Charges	Total
Restricted asset balance, July 1, 2011	\$ -	\$ 296,597	\$ 146,430	\$ 443,027
Fees				
Landfill service charges	65	-	-	65
Sewer service charges	-	1,925,848	-	1,925,848
Garbage service charges	-	-	695,615	695,615
Less: billing adjustments	-	(17,141)	(6,318)	(23,459)
	65	1,908,707	689,297	2,598,069
Expenditures				
To the City of Keokuk	(65)	(1,881,468)	(694,308)	(2,575,841)
	(65)	(1,881,468)	(694,308)	(2,575,841)
Restricted asset balance, June 30, 2012	\$ -	\$ 323,836	\$ 141,419	\$ 465,255
Restricted asset balance is composed of the following:				
Cash and cash equivalents	\$ 9	\$ 148,996	\$ 54,762	\$ 203,767
Accounts receivable	(9)	174,840	86,657	261,488
	\$ -	\$ 323,836	\$ 141,419	\$ 465,255

See accompanying independent auditor's report.

**Keokuk Municipal Water Works,
A Component Unit of the City of Keokuk
Schedule of Changes in Assets Restricted for
Water Revenue Capital Loan Notes Debt Service
Year Ended June 30, 2012**

	Water Revenue Notes Sinking Fund	Water Revenue Notes Reserve Fund	Water Revenue Notes Improvement Fund	Total
Restricted asset balance, June 30, 2011	\$ <u>412,554</u>	\$ <u>1,433,575</u>	\$ <u>252,410</u>	\$ <u>2,098,539</u>
Receipts				
Transfers from (to) operations	<u>1,585,979</u>	<u>-</u>	<u>(831)</u>	<u>1,585,148</u>
Expenditures				
Note principal payments	(1,117,000)	-	-	(1,117,000)
Note interest payments	<u>(549,064)</u>	<u>-</u>	<u>-</u>	<u>(549,064)</u>
	<u>(1,666,064)</u>	<u>-</u>	<u>-</u>	<u>(1,666,064)</u>
Restricted asset balance, June 30, 2012	\$ <u>332,469</u>	\$ <u>1,433,575</u>	\$ <u>251,579</u>	\$ <u>2,017,623</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***

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

We have audited the accompanying financial statements of the proprietary fund of Keokuk Municipal Water Works (Water Works), A Component Unit of the City of Keokuk, as of and for the year ended June 30, 2012, which collectively comprise the basic financial statements listed in the table of contents, and have issued our report thereon dated November 20, 2012. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Water Works' internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Water Works' internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Water Works' internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses and therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. However, as described in the accompanying Schedule of Findings and Responses, 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 that a material misstatement of the Water Works' financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiencies described in Part I of the accompanying Schedule of Findings and Responses to be material weaknesses.

Compliance and Other Matters

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

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

This report is intended solely for the information and use of the officials, employees and citizens of Keokuk Municipal Water Works and other parties to whom the Water Works may report, including federal awarding agencies and pass-through entities. This report is not intended to be and should not be used by anyone other than these specified parties.

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

CPA Associates PC

November 20, 2012

**Keokuk Municipal Water Works,
A Component Unit of the City of Keokuk
Schedule of Findings and Responses
For the Year Ended June 30, 2012**

Part I: Findings Related to the Financial Statements

MATERIAL WEAKNESSES

I-A-12 Preparation of Financial Statements - The Water Works does not have an internal control system designed to provide for the preparation of the financial statements in accordance with accounting principles generally accepted in the United States of America. Therefore, as auditors, we were requested to draft the financial statements and accompanying notes to the financial statements. This circumstance is not unusual for a governmental entity similar in size to the Water Works. It is the responsibility of management and those charged with governance to make the decision whether to accept the degree of risk associated with this condition because of cost or other considerations.

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

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

Conclusion - Response accepted.

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 Board of Trustees and management should continue to provide oversight and direction based upon their direct knowledge of the Water Works' operations and day-to-day contact with employees to control and safeguard assets.

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

Conclusion - Response accepted.

Instances of Noncompliance:

No matters were noted.

**Keokuk Municipal Water Works,
A Component Unit of the City of Keokuk
Schedule of Findings and Responses
For the Year Ended June 30, 2012**

Part II: Other Findings Related to Required Statutory Reporting

- II-A-12 Deposits and Investments - The Water Works has adopted a written investment policy as required by Chapter 12B.10B of the Code of Iowa.
- II-B-12 Travel Expense - No expenditures of Water Works money for travel expenses of spouses of Water Works members or employees were noted.
- II-C-12 Board Minutes - No transactions were found that we believe should have been approved in the Water Works minutes but were not.
- II-D-12 Questionable Disbursements - No disbursements were found that did not meet the requirements of public purpose as defined in the Attorney General's opinion dated April 25, 1979.
- II-E-12 Certified Budget - Disbursements during the year ended June 30, 2012 did not exceed budget amounts.
- II-F-12 Business Transactions with Water Works Officials and Employees - Business transactions between Water Works officials or employees are detailed as follows:

<u>Name, Title, and Business Connection</u>	<u>Transactions</u>	<u>Amount</u>
Mike Haney, Employee	Mowing	\$ 5,222

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

- II-G-12 Revenue Bonds and Notes - No instances of noncompliance with the revenue bond and note resolutions were noted.
- II-H-12 Unclaimed Property - Chapter 556.11 of the Code of Iowa requires a public utility to report and remit obligations, including checks outstanding for more than one to two years, to the State Treasurer's office annually. The Water Works did not remit these obligations as required.

Recommendation - The outstanding checks should be reviewed annually and items over two years old should be remitted to the State Treasurer's Office as required.

Response - Management is in the process of researching the outstanding checks and remitting funds to the State of Iowa.

Conclusion - Response accepted.