

ALGONA MUNICIPAL UTILITIES

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

December 31, 2012

T. P. ANDERSON & COMPANY, P.C.
Certified Public Accountants

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**OFFICIALS
ALGONA MUNICIPAL UTILITIES**

December 31, 2012

<u>Title</u>	<u>Name of Official</u>	<u>Term Expires</u>
Chairman	Jay Geving	May 2015
Chairman Pro Tem	Walter Krahenbuhl	May 2017
Trustee	David Golwitzer	May 2018
Trustee	Karen Schaaf	May 2014
Trustee	Julie Murphy	May 2013
General Manager	John Bilsten	
Comptroller	Brien Rindone	



T.P. ANDERSON & COMPANY, P.C.
CERTIFIED PUBLIC ACCOUNTANTS AND CONSULTANTS

INDEPENDENT AUDITOR'S REPORT

To the Board of Trustees
Algona Municipal Utilities
Algona, Iowa

Report on the Financial Statements

We have audited the accompanying financial statements of each major fund of Algona Municipal Utilities, a component unit of the City of Algona, Iowa as of and for the years ended December 31, 2012 and 2011, and the related notes to the financial statements, which collectively comprise the Utilities' basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express opinions on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of each major fund of Algona Municipal Utilities, as of December 31, 2012 and 2011, and the respective changes in financial position and cash flows thereof for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the *management's discussion and analysis and budgetary comparison information* on pages 4-8 and 39-41 be presented 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.

Other Information

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the basic financial statements. The accompanying schedule of expenditures of federal awards, as required by Office of Management and Budget Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations and the other information, including the comparative summaries of electric, water and communication statistics are presented for purposes of additional analysis and are not a required part of the basic financial statements.

The Schedule of Expenditures of Federal Awards is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the 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 basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the Schedule of Expenditures of Federal Awards is fairly stated, in all material respects, in relation to the basic financial statements as a whole.

The comparative summaries of electric, water, and communication statistics has not been subjected to the auditing procedures applied in the audit of the basic financial statements, and accordingly, we do not express an opinion or provide any assurance on it.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated May 21, 2013 on our consideration of the Algona Municipal Utilities' internal control over financial reporting and on our 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 our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance.

That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering Algona Municipal Utilities internal control over financial reporting and compliance.

JP Anderson & Company, P.C.

May 21, 2013

MANAGEMENT'S DISCUSSION AND ANALYSIS

Algona Municipal Utilities (AMU) provides this Management's Discussion and Analysis of its financial statements. This narrative overview and analysis of the financial activities is for the year ended December 31, 2012. We encourage readers to consider this information in conjunction with the Utilities' financial statements, which follow.

2012 FINANCIAL HIGHLIGHTS

- ◆ AMU's operating revenues increased by 5%, or approximately \$711,000 from calendar year 2011 to calendar year 2012.
- ◆ Operating expenses increased by 4%, or approximately \$588,000 in 2012 from 2011.
- ◆ AMU's net assets decreased 1%, or approximately \$148,000 during 2012.

USING THIS ANNUAL 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 AMU's financial activities.

Fund Financial Statements report AMU's operations 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.

Required Supplementary Information further explains and supports the financial statements with a comparison of AMU's budget for the year.

The supplementary information, the Schedule of Expenditures of Federal Awards, provides details of various federal programs benefiting Algona Municipal Utilities.

The Other Supplementary Information in Schedules 1 through 3 is unaudited and provides detailed information about the usage levels of each utility.

REPORTING THE UTILITIES' FINANCIAL ACTIVITIES

Fund Financial Statements

AMU utilizes one kind of fund:

- 1) Proprietary funds account for AMU's enterprise funds. Enterprise Funds are used to report business type activities. AMU maintains three Enterprise Funds to provide separate information for the electric, water, and communications funds; all are considered to be major funds of the utility.

The required financial statements for proprietary funds include a statement of net position, a statement of revenues, expenses and changes in fund net position and a statement of cash flows.

The condensed statement of net position, shown below, shows how assets and liabilities have changed from 2011 to 2012. Current assets (including restricted cash) decreased approximately \$5.5 million from 2011 to 2012,

due primarily to the use of bond proceeds for various construction projects during the year. Total assets remained virtually the same while liabilities increased by \$151,000 resulting in the decrease in net position of approximately \$148,000 dollars during the year.

Net Assets of Business Type Activities (Expressed in Thousands)		
	Year ended December 31,	
	2012	2011
Current and other assets	\$ 20,057	\$ 25,437
Capital assets (net of depreciation)	31,813	26,430
Total assets	51,870	51,867
Long-term debt outstanding	20,529	21,597
Other liabilities	4,688	3,469
Total liabilities	25,217	25,066
Net position:		
Invested in capital assets, net of related debt	19,190	20,515
Restricted	1,709	576
Unrestricted	5,754	5,710
Total net position	\$ 26,653	\$ 26,801

INDIVIDUAL MAJOR FUND ANALYSIS

As AMU completed the year, its enterprise funds reported a combined fund balance of \$26.7 million, a decrease of approximately \$148,000 under last year's total of \$26.8 million. The following are the major reasons for the changes in fund net position of the major funds from the prior year:

- For the year, the Electric Fund total revenues were \$11.5 million, an increase of approximately \$1.0 million from 2011. Sales to customers actually increased about \$620,000, while the Sales for Resale decreased \$88,000. AMU also received a \$300,000 USDA grant in 2012, which was added to the new AMU Revolving Loan Fund and immediately loaned out to the Kossuth County Agricultural and Motorsports Museum.

Operating expenses were up in 2012 by approximately \$522,000. The main areas of focus for the increases were purchased power related costs. The purchased power costs increased \$643,000 during 2012.

Transfers to the City of Algona also increased significantly during 2012 as a result of transferring the joint revolving loan fund assets to the City as they had been administering the project.

For the year the Electric Utility net position decreased \$373,014.

- At year end, the Water Fund had approximately \$1,039,000 in total revenues which was up from \$945,000 in 2011; an increase of \$94,000. The Water Fund's operating expenses for 2012 decreased by \$7,000 to \$785,000. Total Revenues increased due to an increase in Sales to Customers. The operating expenses decreased in 2011 due to normal operations.

The Water Utility net position increased approximately \$214,000 to approximately \$3.1 million in 2012.

- In the Communications Fund for the year, revenues were up by \$93,000 (\$3,458,000 in 2012 and \$3,365,000 – 2011). The customer counts are as follows: Cable – 1,873 and 1,911; Internet – 1,836 and 1,784; Telephone – 1,580 and 1,632; for the years ended December 31, 2012 and 2011, respectively. The fund’s operating expense for the year was \$3,204,000, up from \$3,130,000 (an increase of \$74,000). The increased operating expenses were due mainly to increased headend programming costs. For the year, the fund showed an increase in net position of \$10,604.

The following analysis focuses on the change in net position for the combined divisions of AMU.

Changes in Net Position of Business Type Activities (Expressed in Thousands)		
ar ended December 31,	2012	2011
Revenues:		
Program revenues:		
Operating revenue	\$ 15,246	\$ 14,535
General revenues:		
Unrestricted investment earnings	148	144
Grant proceeds	552	-
Other general revenues	49	156
Total revenues	<u>15,995</u>	<u>14,835</u>
Program expenses:		
Business type activities	16,144	14,969
Total expenses	<u>16,144</u>	<u>14,969</u>
Increase (decrease) in net position	(149)	(134)
Net position beginning of year	<u>26,801</u>	<u>26,935</u>
Net position end of year	<u>\$ 26,652</u>	<u>\$ 26,801</u>

BUDGETARY HIGHLIGHTS

AMU did not amend their budget during 2012.

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets –

At December 31, 2012, AMU had approximately \$31.8 million (net of depreciation) invested in a broad range of capital assets, including land, buildings, infrastructure, equipment, and vehicles. This is an increase (including additions and deletions net of depreciation) of approximately \$5.38 million, or 20 percent, over 2011.

Capital Assets of Business Type Activities at Year End (Expressed in Thousands)		
	Year ended December 31,	
	2012	2011
Land	\$ 319	\$ 319
Construction in progress	5,137	1,128
Buildings and improvements	2,036	2,044
Equipment and vehicles	768	803
Infrastructure	23,553	22,136
Total	\$ 31,813	\$ 26,430

The largest additions to capital assets included the downtown alleyway project and continued capital improvements at NEAL 4 for the electric and water main improvements for the water fund.

LONG TERM DEBT/LIABILITIES

At December 31, 2012, AMU had approximately \$18 million in revenue bonds outstanding compared to \$19 million at December 31, 2011, as shown below. AMU's liability for deferred compensation increased from approximately \$176,000 to \$237,000.

Outstanding Debt of Business Type Activities at Year End (Expressed in Thousands)		
	Year ended December 31,	
	2012	2011
Revenue bonds	\$ 17,975	\$ 19,051
Deferred compensation	237	176
Total	\$ 18,212	\$ 5,698

At December 31, 2012 and 2011 the Communications Fund owed the Electric Fund \$3,440,000 under an interfund loan agreement established to finance the AMU broadband telecommunications network. The loan agreement calls for interest to accrue at 3.58% per year and to be repaid within 180 months.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES

Algona Municipal Utility's appointed officials consider many factors when setting the calendar year 2012 budget including fees that will be charged for the services the Utilities' provide, for future expansions, and capital improvements.

These factors were taken into account when adopting the budget for fiscal year 2012. Amounts available for appropriation in the operating budget are \$17.35 million, an increase of 12 percent from the 2011 budget. The budget is likely to closer reflect the cash receipts received as estimated based on 2011 results and projected usage from customers. Budgeted disbursements are expected to increase by approximately \$2.18 million. Again, the 2012 budget was set to more closely reflect the actual results as estimated based on 2011 results and expenditures on improvements to the Utility Infrastructure.

Algona Municipal Utilities remains committed to investing in the necessary capital improvements and major

maintenance items on each distribution system enabling continued delivery of the utmost in reliable products and services. Some examples are listed below:

- Algona Municipal Utilities Electric and Communications department will complete an extensive reconstruction project encompassing a 24 block area of downtown Algona. The project includes conversion from overhead to underground electric, construction of fiber to the premise and joint paving of alleys with the City of Algona in an 8 block area. The completed project will increase efficiency and reliability within the electric distribution system. The fiber to the premise portion of the project will increase bandwidth potential for the ever growing demand of Internet bandwidth.
- AMU will expand the fiber to the premise system throughout the entire communications service territory in future years.
- AMU is continuing to deploy its Advanced Metering Infrastructure (AMI) through replacement of electric and water meters, and a new meter reading system. Algona Municipal Utilities will benefit from participation in a US Department of Energy (DOE) Grant through the Iowa Association of Municipal Utilities (IAMU).
- Algona Municipal Utilities and the City of Algona were able to replace **447** street light fixtures on major road ways with new LED street light fixtures in 2012 as part of an Energy Efficiency Conservation Block Grant through the State of Iowa utilizing DOE grant funds. Over the next several years, AMU and the City will continue to replace existing street light fixtures with new LED fixtures.
- Algona Municipal Utilities and Skylink will be upgrading the cellular service in Algona to provide 4G service.
- Algona Municipal Utilities is reviewing several options that will allow us to provide advanced telephone service to Algona while being able to reduce our operating costs.
- Each year, the water distribution system replaces undersized water mains and continues to loop the distribution system. These improvements to the water distribution system increased fire protection, enhance water quality and provide increased water pressure and flow to a growing water distribution system. System improvements are also accomplished each year to serve new development in Algona.
- The improvements being done at the George Neal Generating Station #4 will extend the life of the plant over 25 years and also reduce the environmental impact.

CONTACTING THE UTILITIES' FINANCIAL MANAGEMENT

This financial report is designed to provide our citizens, taxpayers, customers, and creditors with a general overview of AMU's finances and to show the Utilities' accountability for the money it receives. If you have questions about this report or need additional financial information, contact management at 104 West Call Street in Algona.

**ALGONA MUNICIPAL UTILITIES
A COMPONENT UNIT OF THE CITY OF ALGONA**

**PROPRIETARY FUNDS
STATEMENTS OF NET POSITION
DECEMBER 31:**

	ENTERPRISE	
	ELECTRIC	
	2012	2011
Utility plant:		
Property and equipment	\$ 52,517,072	\$ 50,038,766
Less accumulated depreciation	(32,573,765)	(31,272,961)
	<u>19,943,307</u>	<u>18,765,805</u>
Construction in progress	4,928,990	1,053,000
Utility Plant - Net	<u>24,872,297</u>	<u>19,818,805</u>
Restricted funds		
Cash and cash equivalents	8,386,214	14,687,304
Short-term investments	210,928	156,293
	<u>8,597,142</u>	<u>14,843,597</u>
Current Assets:		
Cash and cash equivalents	2,006,021	1,239,365
Accounts receivable (net of allowance for doubtful accounts)	813,911	672,917
Unbilled usage	184,274	166,603
Accounts receivable -interfund	128,622	128,622
Investments	-	-
Inventory	1,300,637	1,140,664
Prepaid expenses	44,665	61,589
Accrued interest receivable	-	-
Accrued interest receivable - interfund loan	123,489	123,152
	<u>4,601,619</u>	<u>3,532,912</u>
Other assets:		
Investment in joint venture	175,662	175,662
Interfund loan receivable	3,440,000	3,440,000
Deferred charges - debt issuance cost	173,555	186,101
Economic development loans receivable	619,011	533,867
	<u>4,408,228</u>	<u>4,335,630</u>
Total assets	<u>\$ 42,479,286</u>	<u>\$ 42,530,944</u>

See Notes to Financial Statements

FUNDS					
WATER		COMMUNICATIONS		TOTAL	
2012	2011	2012	2011	2012	2011
\$ 6,607,229	\$ 5,962,661	\$ 6,260,896	\$ 6,274,025	\$ 65,385,197	\$ 62,275,452
(2,992,069)	(2,876,187)	(3,143,242)	(2,824,016)	(38,709,076)	(36,973,164)
3,615,160	3,086,474	3,117,654	3,450,009	26,676,121	25,302,288
45,946	50,951	162,165	24,065	5,137,101	1,128,016
3,661,106	3,137,425	3,279,819	3,474,074	31,813,222	26,430,304
\$ 134,039	\$ 309,164	-	-	8,520,253	14,996,468
5,407	4,350	20,907	15,520	237,242	176,163
139,446	313,514	20,907	15,520	8,757,495	15,172,631
515,601	674,544	1,093,840	1,081,859	3,615,462	2,995,768
74,736	61,709	267,851	207,581	1,156,498	942,207
31,720	25,361	-	-	215,994	191,964
-	40,572	-	-	128,622	169,194
-	-	-	-	-	-
34,923	33,272	11,511	19,492	1,347,071	1,193,428
22,202	21,329	22,427	18,970	89,294	101,888
-	-	-	-	-	-
-	-	-	-	123,489	123,152
679,182	856,787	1,395,629	1,327,902	6,676,430	5,717,601
-	-	214,285	210,396	389,947	386,058
-	-	-	-	3,440,000	3,440,000
-	-	-	-	173,555	186,101
-	-	-	-	619,011	533,867
-	-	214,285	210,396	4,622,513	4,546,026
\$ 4,479,734	\$ 4,307,726	\$ 4,910,640	\$ 5,027,892	\$ 51,869,660	\$ 51,866,562

**ALGONA MUNICIPAL UTILITIES
A COMPONENT UNIT OF THE CITY OF ALGONA**

**PROPRIETARY FUNDS
STATEMENTS OF NET POSITION - continued
DECEMBER 31:**

	ENTERPRISE	
	ELECTRIC	
	2012	2011
Liabilities:		
Current liabilities:		
Accounts payable	\$ 1,647,616	\$ 744,240
Accounts payable - City of Algona	187,283	123,450
Accounts payable - interfund	-	40,572
Retainage and contracts payable	90,573	-
Accrued taxes	133,673	138,939
Accrued wages and compensated absences	272,982	229,698
Accrued interest payable	46,154	48,917
Deferred revenue	-	-
Revenue bonds payable	870,000	825,000
	<u>3,248,281</u>	<u>2,150,816</u>
Noncurrent liabilities		
Revenue bonds payable - net of current portion	13,895,000	14,765,000
Interfund loan - payable	-	-
Accrued OPEB	157,414	118,158
	<u>14,052,414</u>	<u>14,883,158</u>
Other liabilities		
Deferred compensation liability	210,928	156,293
	<u>17,511,623</u>	<u>17,190,267</u>
Fund Net Position		
Net investment in capital assets	16,918,836	18,473,805
Restricted - bond covenant	1,574,675	442,304
Unrestricted (deficit)	6,474,152	6,424,568
Total net position	<u>\$ 24,967,663</u>	<u>\$ 25,340,677</u>

See Notes to Financial Statements

FUNDS					
WATER		COMMUNICATIONS		TOTAL	
2012	2011	2012	2011	2012	2011
37,257	\$ 19,265	\$ 121,065	\$ 125,790	\$ 1,805,938	\$ 889,295
2,318	12,184	138,837	134,935	328,438	270,569
-	-	128,622	128,622	128,622	169,194
13,869	-	-	-	104,442	-
3,380	3,139	62,668	63,159	199,721	205,237
47,129	43,439	79,098	62,787	399,209	335,924
3,109	2,249	123,489	123,152	172,752	174,318
-	-	184,650	172,848	184,650	172,848
75,000	75,000	182,518	175,100	1,127,518	1,075,100
<u>182,062</u>	<u>155,276</u>	<u>1,020,947</u>	<u>986,393</u>	<u>4,451,290</u>	<u>3,292,485</u>
1,155,000	1,230,000	1,797,154	1,981,137	16,847,154	17,976,137
-	-	3,440,000	3,440,000	3,440,000	3,440,000
27,979	22,896	56,254	40,068	241,647	181,122
<u>1,182,979</u>	<u>1,252,896</u>	<u>5,293,408</u>	<u>5,461,205</u>	<u>20,528,801</u>	<u>21,597,259</u>
5,407	4,350	20,907	15,520	237,242	176,163
<u>1,370,448</u>	<u>1,412,522</u>	<u>6,335,262</u>	<u>6,463,118</u>	<u>25,217,333</u>	<u>25,065,907</u>
2,431,106	2,007,425	(160,181)	34,074	19,189,761	20,515,304
134,039	134,164	-	-	1,708,714	576,468
544,141	753,615	(1,264,441)	(1,469,300)	5,753,852	5,708,883
<u>\$ 3,109,286</u>	<u>\$ 2,895,204</u>	<u>\$ (1,424,622)</u>	<u>\$ (1,435,226)</u>	<u>\$ 26,652,327</u>	<u>\$ 26,800,655</u>

**ALGONA MUNICIPAL UTILITIES
A COMPONENT UNIT OF THE CITY OF ALGONA**

**PROPRIETARY FUNDS
STATEMENTS OF REVENUES, EXPENSES
AND CHANGES IN FUND NET POSITION**

DECEMBER 31:

	ENTERPRISE	
	ELECTRIC	
	2012	2011
Operating revenues:		
Sale of electricity:		
Residential and commercial	\$ 7,914,391	\$ 7,294,060
Sales for resale	2,523,878	2,611,900
Service provided to City of Algona	34,123	63,663
Sales to other utilities	103,545	94,850
Sale of water	-	-
Cable TV fees	-	-
Internet fees	-	-
Telephone service	-	-
Cell phone revenue	-	-
Miscellaneous and merchandising	195,824	191,010
Return from investment in AMU-Skylink LC	-	-
Total operating revenue	10,771,761	10,255,483
Operating expenses:		
Generation and power purchased	7,199,101	6,555,504
Transmission-distribution maintenance	411,205	408,999
Meter reading supplies and labor	149,702	164,999
Sales	38,945	38,265
General and other	785,791	765,622
Administration and general	355,226	490,471
Rebates and other expenses	171,101	119,051
Merchandise, jobbing and construction	7,647	19,468
Property tax and insurance	211,887	224,201
Depreciation	1,402,589	1,413,598
Free service to the City of Algona	320,371	331,904
Source of supply	-	-
Maintenance of mains, services and meters	-	-
Maintenance of distribution and equipment	-	-
Headend programming	-	-
Customer accounts	-	-
Total operating expenses	11,053,565	10,532,082
Income from operations	\$ (281,804)	\$ (276,599)

See Notes to Financial Statements

FUNDS					
WATER		COMMUNICATIONS		TOTAL	
2012	2011	2012	2011	2012	2011
\$ -	\$ -	\$ -	\$ -	\$ 7,914,391	\$ 7,294,060
-	-	-	-	2,523,878	2,611,900
-	-	-	-	34,123	63,663
-	-	-	-	103,545	94,850
998,132	895,033	-	-	998,132	895,033
-	-	1,123,865	1,103,906	1,123,865	1,103,906
-	-	832,871	806,180	832,871	806,180
-	-	1,317,666	1,284,177	1,317,666	1,284,177
-	-	66,810	62,631	66,810	62,631
18,827	18,814	112,545	88,293	327,196	298,117
-	-	3,889	20,647	3,889	20,647
<u>1,016,959</u>	<u>913,847</u>	<u>3,457,646</u>	<u>3,365,834</u>	<u>15,246,366</u>	<u>14,535,164</u>
-	-	-	-	7,199,101	6,555,504
-	-	-	-	411,205	408,999
-	-	-	-	149,702	164,999
-	-	-	-	38,945	38,265
-	-	-	-	785,791	765,622
258,333	245,444	696,794	663,605	1,310,353	1,399,520
-	-	-	-	171,101	119,051
18,676	19,661	56,899	53,171	83,222	92,300
-	-	84,960	81,647	296,847	305,848
159,346	124,605	366,352	405,627	1,928,287	1,943,830
44,244	38,145	143,463	144,486	508,078	514,535
161,834	177,594	-	-	161,834	177,594
90,686	127,275	-	-	90,686	127,275
-	-	193,466	168,287	193,466	168,287
-	-	1,530,602	1,477,563	1,530,602	1,477,563
51,935	59,150	131,329	135,981	183,264	195,131
<u>785,054</u>	<u>791,874</u>	<u>3,203,865</u>	<u>3,130,367</u>	<u>15,042,484</u>	<u>14,454,323</u>
\$ 231,905	\$ 121,973	\$ 253,781	\$ 235,467	\$ 203,882	\$ 80,841

**ALGONA MUNICIPAL UTILITIES
A COMPONENT UNIT OF THE CITY OF ALGONA**

**PROPRIETARY FUNDS
STATEMENTS OF REVENUES, EXPENSES
AND CHANGES IN FUND NET POSITION - continued**

DECEMBER 31:

	ENTERPRISE	
	ELECTRIC	
	2012	2011
Non-operating income and (expense)		
Interest income	\$ 143,819	\$ 134,552
Interest expense	(323,958)	(68,698)
Grant income	551,742	-
Miscellaneous	23,648	127,019
Donations	(97,997)	(65,297)
Gain (loss) on disposition of assets	9,756	(3,141)
Total non-operating income (expense)	<u>307,010</u>	<u>124,435</u>
Income(loss) before other revenues, expenses and transfers	25,206	(152,164)
Other revenues, expenses, gains, losses and transfers		
Capital contribution - capital grant	71,780	-
Transfer to City of Algona	(470,000)	-
Total other income, expense, and transfers	<u>(398,220)</u>	<u>-</u>
Increase (decrease) in net position	(373,014)	(152,164)
Net position, beginning	<u>25,340,677</u>	<u>25,492,841</u>
Net position, ending	<u><u>\$ 24,196,429</u></u>	<u><u>\$ 25,340,677</u></u>

See Notes to Financial Statements

FUNDS						
WATER		COMMUNICATIONS		TOTAL		
2012	2011	2012	2011	2012	2011	
\$ 2,207	\$ 5,633	\$ 2,336	\$ 3,349	\$ 148,362	\$ 143,534	
(39,662)	-	(208,865)	(215,869)	(572,485)	(284,567)	
-	-	-	-	551,742	-	
19,901	25,090	5,560	4,019	49,109	156,128	
(269)	(59)	-	-	(98,266)	(65,356)	
-	(70,937)	(42,208)	(90,575)	(32,452)	(164,653)	
(17,823)	(40,273)	(243,177)	(299,076)	46,010	(214,914)	
214,082	81,700	10,604	(63,609)	249,892	(134,073)	
-	-	-	-	71,780	-	
-	-	-	-	(470,000)	-	
-	-	-	-	(398,220)	-	
214,082	81,700	10,604	(63,609)	(148,328)	(134,073)	
2,895,204	2,813,504	(1,435,226)	(1,371,617)	26,800,655	26,934,728	
\$ 3,109,286	\$ 2,895,204	\$ (1,424,622)	\$ (1,435,226)	\$ 26,652,327	\$ 26,800,655	

**ALGONA MUNICIPAL UTILITIES
A COMPONENT UNIT OF THE CITY OF ALGONA**

**PROPRIETARY FUNDS
STATEMENTS OF CASH FLOWS
DECEMBER 31:**

	ENTERPRISE	
	ELECTRIC	
	2012	2011
Cash flows from operating activities:		
Cash receipts from customers	\$ 10,203,873	\$ 9,869,010
Cash receipts from interfund services	219,099	223,472
Other operating cash receipts	34,699	28,592
Cash payments to suppliers	(7,197,969)	(7,299,237)
Cash payments to employees	(1,228,833)	(1,286,551)
Cash payments for interfund services	-	-
Net cash provided by operating activities	<u>2,030,869</u>	<u>1,535,286</u>
Cash flows from noncapital financing activities:		
Transfer to the City of Algona	(175,000)	-
Donations	(97,997)	(65,297)
Net cash (used) by noncapital financing activities	<u>(272,997)</u>	<u>(65,297)</u>
Cash flows from capital and related financing activities:		
Deferred compensation payments	-	(15,051)
Deferred compensation deposits	-	28,557
Acquisition and construction of capital assets	(6,395,121)	(1,535,443)
Repayment of revenue bonds	(825,000)	(480,000)
Proceeds from bond issuances	-	14,065,230
Grant received	540,000	-
Proceeds from sale of assets	40,421	12,608
Cash payments for interest	(499,592)	(68,100)
Net cash provided (used) by capital and related financing activities	<u>(7,139,292)</u>	<u>12,007,801</u>
Cash flows from investing activities:		
Interest received during the year	143,482	134,552
Principal received on economic development loan	55,043	43,962
Issuance of new economic development loans	(375,187)	(46,400)
Proceeds from redemption of investments	-	15,051
Purchase of investments	-	(28,557)
Miscellaneous income	23,648	141,627
Net cash provided (used) by investing activities	<u>\$ (153,014)</u>	<u>\$ 260,235</u>

See Notes to Financial Statements

FUNDS					
WATER		COMMUNICATIONS		TOTAL	
2012	2011	2012	2011	2012	2011
\$ 993,746	\$ 922,900	\$ 3,338,851	\$ 3,239,486	\$ 14,536,470	\$ 14,031,396
-	-	-	-	219,099	223,472
-	-	-	47,417	34,699	76,009
(282,844)	(357,271)	(2,214,413)	(2,103,602)	(9,695,226)	(9,760,110)
(179,504)	(189,199)	(392,333)	(416,237)	(1,800,670)	(1,891,987)
(90,477)	(94,850)	(128,622)	(128,622)	(219,099)	(223,472)
<u>440,921</u>	<u>281,580</u>	<u>603,483</u>	<u>638,442</u>	<u>3,075,273</u>	<u>2,455,308</u>
-	-	-	-	(175,000)	-
(269)	(59)	-	-	(98,266)	(65,356)
<u>(269)</u>	<u>(59)</u>	<u>-</u>	<u>-</u>	<u>(273,266)</u>	<u>(65,356)</u>
-	-	-	-	-	(15,051)
-	-	-	-	-	28,557
(683,026)	(989,427)	(214,305)	(286,156)	(7,292,452)	(2,811,026)
(75,000)	(65,000)	(176,565)	(169,223)	(1,076,565)	(714,223)
-	-	-	-	-	14,065,230
-	-	-	-	540,000	-
-	-	-	-	40,421	12,608
(38,802)	(46,341)	(208,528)	(215,869)	(746,922)	(330,310)
<u>(796,828)</u>	<u>(1,100,768)</u>	<u>(599,398)</u>	<u>(671,248)</u>	<u>(8,535,518)</u>	<u>10,235,785</u>
2,207	5,633	2,336	3,349	148,025	143,534
-	-	-	-	55,043	43,962
-	-	-	-	(375,187)	(46,400)
-	-	-	-	-	15,051
-	-	-	(50,000)	-	(78,557)
<u>19,901</u>	<u>25,090</u>	<u>5,560</u>	<u>4,019</u>	<u>49,109</u>	<u>170,736</u>
<u>\$ 22,108</u>	<u>\$ 30,723</u>	<u>\$ 7,896</u>	<u>\$ (42,632)</u>	<u>\$ (123,010)</u>	<u>\$ 248,326</u>

**ALGONA MUNICIPAL UTILITIES
A COMPONENT UNIT OF THE CITY OF ALGONA**

**PROPRIETARY FUNDS
STATEMENTS OF CASH FLOWS - continued
DECEMBER 31:**

	ENTERPRISE	
	ELECTRIC	
	2012	2011
Net increase (decrease) in cash and cash equivalents	\$ (5,534,434)	\$ 13,738,025
Cash and cash equivalents-beginning of year	15,926,669	2,188,644
Cash and cash equivalents-end of year	<u>10,392,235</u>	<u>15,926,669</u>
Restricted funds	8,386,214	14,687,304
Current assets	2,006,021	1,239,365
	<u>10,392,235</u>	<u>15,926,669</u>
Reconciliation of operating income to net cash provided by operating activities:		
Income from operations	(281,804)	(276,599)
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation	1,402,589	1,413,598
Loss (gain) from investment in AMU-Skylink LC	-	-
Change in accounts receivable	(64,252)	(145,428)
Change in unbilled usage	(17,671)	11,019
Change in accounts receivable - interfund	-	-
Change in prepaid expenses	16,924	63,946
Change in inventory	(159,973)	(254,189)
Change in accounts payable and retainages payable	1,057,782	654,283
Change in accrued taxes	(5,266)	16,461
Change in accrued wages and compensated absences	43,284	12,809
Change in deferred revenue	-	-
Change in OPEB liability	39,256	39,386
Net cash provided by operating activities	<u>\$ 2,030,869</u>	<u>\$ 1,535,286</u>

Non-cash investing and financing transactions:

The Electric Fund transferred \$235,000 of Receivables associated with the revolving loan fund established separate from the USDA revolving loan funds to the City of Algona as they will now manage that program.

See Notes to Financial Statements

FUNDS					
WATER		COMMUNICATIONS		TOTAL	
2012	2011	2012	2011	2012	2011
\$ (334,068)	\$ (788,524)	\$ 11,981	\$ (75,438)	\$ (5,856,521)	\$ 91,690
983,708	1,772,232	1,081,859	1,157,297	17,992,236	1,264,306
649,640	983,708	1,093,840	1,081,859	12,135,715	17,992,236
134,039	309,164	-	-	8,520,253	14,996,468
515,601	674,544	1,093,840	1,081,859	3,615,462	2,995,768
649,640	983,708	1,093,840	1,081,859	12,135,715	17,992,236
231,905	121,973	253,781	235,467	203,882	80,841
159,346	124,605	366,352	405,627	1,928,287	1,943,830
-	-	(3,889)	(20,647)	(3,889)	(20,647)
(13,027)	6,610	(60,270)	(36,759)	(137,549)	(175,577)
(6,359)	2,443	-	-	(24,030)	13,462
40,572	-	-	-	40,572	-
(873)	(3,901)	(3,457)	(7,118)	12,594	52,927
(1,651)	11,835	7,981	2,367	(153,643)	(239,987)
21,994	9,636	(823)	35,384	1,078,953	699,303
241	268	(491)	(1,941)	(5,516)	14,788
3,690	479	16,311	12,706	63,285	25,994
-	-	11,802	-	11,802	-
5,083	7,632	16,186	13,356	60,525	60,374
\$ 440,921	\$ 281,580	\$ 603,483	\$ 638,442	\$ 3,075,273	\$ 2,455,308

**ALGONA MUNICIPAL UTILITIES
A COMPONENT UNIT OF THE CITY OF ALGONA**

NOTES TO FINANCIAL STATEMENTS

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Algona Municipal Utilities (AMU) is a component unit of the City of Algona whose funds are reported under separate cover utilizing a fiscal year ending June 30. The City of Algona is a political subdivision of the State of Iowa located in Kossuth County. It was first incorporated in 1872 and operates under the Home Rule provisions of the Constitution of Iowa. AMU Board of Trustees operates the Utilities by the authority of Chapters 384 and 388 of the Code of Iowa. AMU provides electric, water, cable tv, internet, telephone, cell phone sales and service, and data services on a user charge basis to the general public and other governmental units within Kossuth County, Iowa.

A. Reporting Entity

For financial reporting purposes, AMU has included all funds, organizations, agencies, boards, commissions and authorities. AMU has also considered all other potential component units for which it is financially accountable, and other organizations for which the nature and significance of their relationship with AMU are such that exclusion would cause AMU'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 AMU 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 AMU. AMU has no component units which meet the Governmental Accounting Standards Board criteria.

B. Basis of Presentation

Fund Financial Statements – Separate financial statements are provided for proprietary funds. Major individual proprietary funds are reported as separate columns in the fund financial statements.

AMU reports the following major proprietary funds:

Enterprise:

The Electric Fund is used to account for the operation and maintenance of AMU's electric system.

**ALGONA MUNICIPAL UTILITIES
A COMPONENT UNIT OF THE CITY OF ALGONA**

NOTES TO FINANCIAL STATEMENTS

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES-continued

The Water Fund is used to account for the operation and maintenance of AMU's water system.

The Communications Fund is used to account for the cable tv, internet, telephone, cellular service, and data services systems.

C. Measurement Focus and Basis of Accounting

AMU maintains its financial records on the accrual basis of accounting in conformity with accounting principles generally accepted in the United States. Revenues are recognized when earned and expenses are recorded when the liabilities are incurred.

AMU applies all applicable GASB pronouncements, as well as Financial Accounting Standards Board pronouncements unless those pronouncements conflict with or contradict GASB pronouncements. .

Proprietary funds distinguish operating revenues and expenses from non-operating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. The principal operating revenues of AMU are charges to customers for sales and services. Operating expenses include cost of sales and services, administrative expenses and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

D. Budgets and Budgetary Accounting

The budgetary comparison and related disclosures are reported as Required Supplementary Information.

E. Utility Plant and Depreciation

The utility plant is stated at original cost when first devoted to public service. Expenditures for additions and betterments (including labor charges) are capitalized, while expenditures for repairs and maintenance are charged to

**ALGONA MUNICIPAL UTILITIES
A COMPONENT UNIT OF THE CITY OF ALGONA**

NOTES TO FINANCIAL STATEMENTS

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES-continued

operations as incurred. Interest costs incurred during construction periods are also capitalized. The costs of assets retired or sold and the related accumulated depreciation are eliminated from the accounts in the year of disposal, with the resulting gain or loss credited or charged to operations. The straight-line method is used for computing depreciation with estimated useful lives ranging from two to fifty years.

F. Revenue, Unbilled Usage, Deferred Revenue, and Accounts Receivable

Revenues are based on billing rates applied to customers' consumption. Unbilled usage represents revenues based upon estimated consumption for the period between the last billing dates at the end of the year. Deferred revenue represents amounts billed for cable TV, internet, telephone, and data services that had not yet been delivered at the end of the year. The allowance method is used to account for uncollectible accounts receivable. As of December 31, 2012 and 2011, \$5,700 and \$8,238 respectively of accounts receivable were older than 90 days. The 2012 and 2011 past due accounts are primarily associated with the electric utility. AMU charges 1.5% per month on past due accounts.

The Communications Utility also has receivables from Carrier Access Billing (CABS) that are separate from customer charges. As of December 31, 2012 and 2011, \$139,212 and \$64,791 in (CABS) receivables were older than 90 days.

The balance of the allowance for doubtful accounts as of December 31 2012 and 2011 were as follows:

	Electric	Water	Communications
December 31, 2012	\$ 31,400	\$ 3,800	\$ 71,572
December 31, 2011	\$ 31,900	\$ 3,800	\$ 92,000

G. Inventory

Inventory is valued at the lower of cost or market. Cost is determined on a first-in, first-out method for materials and supplies, and the average cost method for fuel.

**ALGONA MUNICIPAL UTILITIES
A COMPONENT UNIT OF THE CITY OF ALGONA**

NOTES TO FINANCIAL STATEMENTS

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES-continued

H. Bond Issue Costs

Unamortized bond issue costs are amortized over the life of the bonds using the same percentage as the principal paid in a given year to the total debt by issue.

I. Joint Plant Ownership

Under a joint ownership agreement with other utilities, AMU has a 2.937% undivided interest in a 640 MW electric generation station known as George Neal Generating Station Unit No. 4. As of December 31, 2012 and 2011, AMU's interest in this plant represents a total investment of \$11,633,431 and \$11,172,848 included in property and equipment respectively. Accumulated depreciation associated with the Utilities' ownership in this plant totaled \$(10,003,693) and \$(9,886,772) at December 31, 2012 and 2011 respectively. Operating costs and depreciation associated with this plant are reflected in the statement of income.

AMU also has a 4.18% undivided interest in the Lehigh-Webster Transmission System. As of December 31, 2012 and 2011, AMU's interest in the system represents a total investment of \$364,770 included in property and equipment. Accumulated depreciation associated with the AMU's ownership in this plant totaled \$(364,770) and \$(364,770) at December 31, 2012 and 2011 respectively. Operating costs and depreciation associated with this system are reflected in the statement of income.

AMU has an 11.1% undivided interest in the Iowa Distributed Wind Generation Project (IDWGP). IDWGP is a consortium of seven municipal electric utilities that jointly own and operate three 750 KW wind turbine generators at a site six miles southeast of the City of Algona. As of December 31, 2012 and 2011, AMU's interest in the system represents a total investment of \$164,418 included in property and equipment. Accumulated depreciation associated with the AMU's ownership in this plant totaled \$(117,497) and \$(109,677) at December 31, 2012 and 2011 respectively. AMU, through a contractual relationship with IDWGP, provides operating, maintenance, and site management for the project. In addition, AMU currently purchases the majority of the electricity produced by the project.

**ALGONA MUNICIPAL UTILITIES
A COMPONENT UNIT OF THE CITY OF ALGONA**

NOTES TO FINANCIAL STATEMENTS

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES-continued

J. Interest Capitalization

AMU capitalizes interest costs incurred on funds used to construct property, plant, and equipment. The capitalized interest is recorded as part of the asset to which it relates and is written off over the asset's estimated useful life.

K. Net Position

Net position reflects the difference between assets plus deferred outflows of resources and liabilities plus deferred inflows of resources in the financial statements. Net position invested in capital assets, net of related debt consists of capital assets net of related accumulated depreciation, reduced by the balance of long term debt used to acquire or construct those assets. Net position is reported as restricted when there are limitations placed on their use through external restrictions imposed by creditors, grantors, or laws and regulations increased by unspent debt proceeds of bonds issuance net of related debt. Unrestricted net position consists of net position that does not meet the definition of invested in capital assets net of related debt or restricted.

AMU's policy is to first apply restricted resources when an expense is incurred for purposes for which both restricted and unrestricted net position is available.

L. Rate Matters

The rates charged by AMU are established by the Board of Trustees and, as a municipal system, are not subject to the regulation of the Utilities Division of the Department of Commerce of the State of Iowa.

M. Cash and Cash Equivalents

For the purpose of the statement of cash flows, AMU considers all highly liquid debt instruments purchased with a maturity of less than three months to be cash equivalents.

N. Contracts

AMU joined, through a contractual agreement, the North Iowa Municipal Electric

**ALGONA MUNICIPAL UTILITIES
A COMPONENT UNIT OF THE CITY OF ALGONA**

NOTES TO FINANCIAL STATEMENTS

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES-continued

Cooperative Association (NIMECA) in 2009. NIMECA is a cooperative consisting of 12 member municipalities that consolidates the electric resources of its members and serves as a joint power supply.

NOTE 2 - CASH AND INVESTMENTS

AMU's deposits at December 31, 2012 and 2011 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 ensure there will be no loss of public funds.

AMU 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 AMU's Board of Trustees; prime eligible bankers acceptances; certain high rated commercial paper; perfected repurchase agreements; certain registered open-end management investment companies; certain joint investment trusts; warrants or improvement certificates of a drainage district.

AMU's investments are categorized to give an indication of the level of risk assumed by AMU at year-end. AMU's investments are all category 1, which means that the investments are insured or registered or the securities are held by AMU or its agent in AMU's name.

AMU had investments in the Iowa Public Agency Investments Trust at December 31, 2012 and 2011, which are valued at an amortized cost of \$361,838 and \$18,836 respectively pursuant to Rule 2a-7 under the Investment Company Act of 1940 and are not subject to risk categorization.

Credit Risk – The Electric Utility had \$10,180,792 and \$14,340,696 included as cash on the Statement of Net Position at December 31, 2012 and 2011 that was held in a money market rated AAAM by Stanadard & Poors.

Interest rate risk – The Utilities' investment policy limits the investment of operating funds (funds expected to be expended in the current budget year or within 15 months of receipt) in instruments that mature within 397 days. Funds not identified as operating funds may be invested in investments with maturities longer than 397 days but the maturities shall be consistent with the needs and use of the Utilities. Reconciliation of

**ALGONA MUNICIPAL UTILITIES
A COMPONENT UNIT OF THE CITY OF ALGONA**

NOTES TO FINANCIAL STATEMENTS

NOTE 2 - CASH AND INVESTMENTS - continued

the Utilities' cash and cash equivalents and temporary cash and investments for the years ended December 31, 2012 and 2011 is as follows:

	December 31, 2012			
	Electric Utility	Water Utility	Communications Utility	Total
Cash and cash equivalents				
Restricted	8,386,214	134,039	-	10,232,888
Current assets	2,006,021	515,601	1,093,840	1,902,827
	<u>10,392,235</u>	<u>649,640</u>	<u>1,093,840</u>	<u>12,135,715</u>
Investments				
Restricted	210,928	5,407	20,907	237,242
Unrestricted	-	-	-	-
	<u>210,928</u>	<u>5,407</u>	<u>20,907</u>	<u>237,242</u>
Total cash and cash equivalents and investments	<u>\$ 10,603,163</u>	<u>655,047</u>	<u>1,114,747</u>	<u>\$ 12,372,957</u>
	December 31, 2011			
	Electric Utility	Water Utility	Communications Utility	Total
Cash and cash equivalents				
Restricted	14,687,304	309,164	-	14,996,468
Current assets	1,239,365	674,544	1,081,859	2,995,768
	<u>15,926,669</u>	<u>983,708</u>	<u>1,081,859</u>	<u>17,992,236</u>
Investments				
Restricted	156,293	4,350	15,520	176,163
	<u>156,293</u>	<u>4,350</u>	<u>15,520</u>	<u>176,163</u>
Total cash and cash equivalents and investments	<u>\$ 16,082,962</u>	<u>988,058</u>	<u>1,097,379</u>	<u>\$ 18,168,399</u>

NOTE 3 – INTERFUND LOAN

Management authorized interfund loans from the Electric Fund to the Communications Fund not to exceed \$5,540,000 dedicated to finance the construction of the AMU broadband telecommunications network. All monies transferred shall be repaid to the originating account within 180 months with interest at the rate of 3.58% per annum. As

**ALGONA MUNICIPAL UTILITIES
A COMPONENT UNIT OF THE CITY OF ALGONA**

NOTES TO FINANCIAL STATEMENTS

NOTE 3 – INTERFUND LOAN - continued

of December 31, 2012 and 2011 the outstanding balance on the interfund loan was \$3,440,000.

This interfund loan is reflected on the Electric Department Balance Sheet as an Other Asset. It is reflected on the Communication Department Balance Sheet as a Noncurrent Liability. Accrued interest as of December 31, 2012 and 2011 of \$123,489 and \$123,152 is also reflected on the Electric Department Balance Sheet as Accrued Interest Receivable – Interfund Loan and the Communication Department Balance Sheet as Accrued Interest Payable - Interfund Loan.

NOTE 4 – ECONOMIC DEVELOPMENT LOAN FUND

AMU has established a revolving loan fund in conjunction with the City of Algona. To date, \$330,000 has been lent to the City of Algona under this program.

From these funds, money was lent by the City of Algona for various economic development projects. This money is to be repaid by the City of Algona as they receive payments from the various borrowers. Effective in 2012, AMU transferred the receivables and all cash on for this program to the City of Algona. As of December 31, 2011 the balance due AMU under the program was \$235,000.

NOTE 5 – USDA ECONOMIC DEVELOPMENT LOAN FUND

In conjunction with the USDA (United States Rural Development), AMU has established a separate revolving loan fund. The funding for the program came from two separate \$300,000 grants from the USDA supplemented by \$120,000 of matching funds provided by AMU.

This program has made four separate loans to local charitable organizations/governmental organizations to assist in furthering economic development in the Algona area. As of December 31, 2012 and 2011 notes receivable under this program amounted to \$619,011 and \$298,867.

NOTE 5 – REVENUE BONDS PAYABLE

The following is a summary of changes in long-term debt for the years ended December 31, 2012 and 2011.

**ALGONA MUNICIPAL UTILITIES
A COMPONENT UNIT OF THE CITY OF ALGONA**

NOTES TO FINANCIAL STATEMENTS

NOTE 5 – REVENUE BONDS PAYABLE-continued

Electric Utility:

	Balance 1/1/12	Issued	Repaid	Balance 12/31/12
Business type activities:				
Revenue Bonds – Series 2008	\$ 1,345,000	-	\$ 500,000	\$ 845,000
Revenue Bonds – Series 2011	14,245,000	-	325,000	13,920,000
	<u>15,590,000</u>	-	<u>825,000</u>	<u>14,765,000</u>

	Balance 1/1/11	Issued	Repaid	Balance 12/31/11
Business type activities:				
Revenue Bonds – Series 2008	\$ 1,825,000	-	480,000	\$ 1,345,000
Revenue Bonds – Series 2011	-	14,245,000	-	14,245,000
	<u>1,825,000</u>	<u>14,245,000</u>	<u>480,000</u>	<u>15,590,000</u>

Water Utility:

	Balance 1/1/12	Issued	Repaid	Balance 12/31/12
Business type activities:				
Revenue Bonds – issued October 5, 2010	\$ 1,305,000	-	75,000	\$ 1,230,000
	<u>\$ 1,305,000</u>	-	<u>75,000</u>	<u>\$ 1,230,000</u>

	Balance 1/1/11	Issued	Repaid	Balance 12/31/11
Business type activities:				
Revenue Bonds – issued October 5, 2010	1,370,000	-	65,000	1,305,000
	<u>1,370,000</u>	-	<u>65,000</u>	<u>1,305,000</u>

Communications Utility:

	Balance 1/1/12	Issued	Repaid	Balance 12/31/12
Business type activities:				
Revenue Bonds–Series 2005	340,976	-	31,020	309,956
Revenue Bonds–Series 2010	1,815,261	-	145,545	1,669,716
	<u>2,156,237</u>	-	<u>176,565</u>	<u>1,979,672</u>

**ALGONA MUNICIPAL UTILITIES
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NOTES TO FINANCIAL STATEMENTS

NOTE 5 – REVENUE BONDS PAYABLE-continued

	Balance 1/1/11	Issued	Repaid	Balance 12/31/11
Business type activities:				
Revenue Bonds–Series 2005	\$ 370,460	-	29,484	340,976
Revenue Bonds–Series 2010	1,955,000	-	139,739	1,815,261
	<u>2,325,460</u>	<u>-</u>	<u>169,223</u>	<u>2,156,237</u>

Annual debt service requirements to maturity for the revenue bonds are as follows:

Year Ending December 31,	Electric Series 2008 Interest 3.25%-4.00%		Electric Series 2011 Interest 2.0%-4.0%		Total	
	Principal	Interest	Principal	Interest	Principal	Interest
	2013	525,000	33,800	345,000	426,838	870,000
2014	320,000	12,800	580,000	419,938	900,000	432,738
2015	-	-	920,000	408,338	920,000	408,338
2016	-	-	940,000	389,938	940,000	389,938
2017	-	-	960,000	371,138	960,000	371,138
2018-2022	-	-	5,240,000	1,468,064	5,240,000	1,468,064
2023-2026	-	-	4,935,000	494,676	4,935,000	494,676
	<u>845,000</u>	<u>46,600</u>	<u>13,920,000</u>	<u>3,978,930</u>	<u>14,795,000</u>	<u>4,025,530</u>

Year Ending December 31,	Communications Series 2005 Interest 5.09%		Communications Series 2010 Interest 5.45%		Total	
	Principal	Interest	Principal	Interest	Principal	Interest
	2013	32,499	15,160	150,019	64,263	182,518
2014	34,192	13,467	156,076	58,206	190,268	71,673
2015	35,974	11,685	1,363,621	51,887	1,399,595	63,572
2016	37,848	9,811	-	-	37,848	9,811
2017	39,820	7,839	-	-	39,820	7,839
2018-2020	129,623	10,630	-	-	129,623	10,630
	<u>309,956</u>	<u>68,592</u>	<u>1,669,716</u>	<u>174,356</u>	<u>1,979,672</u>	<u>242,948</u>

**ALGONA MUNICIPAL UTILITIES
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NOTES TO FINANCIAL STATEMENTS

NOTE 5 – REVENUE BONDS PAYABLE-continued

Years Ending December 31:	Water Series 2010	
	Principal	Interest
2013	75,000	37,303
2014	75,000	35,082
2015	80,000	34,302
2016	85,000	32,702
2017	85,000	30,790
2018-2022	485,000	115,395
2023-2025	345,000	26,850
	1,230,000	312,424

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

Series 2008 and 2011 Electric Revenue Bonds:

- A. The bonds will only be redeemed from the earnings of the enterprise activity and the bondholders hold a lien on the future earnings of the funds.
- B. Sufficient monthly transfers shall be made to the Electric Revenue Bond Sinking Fund for the purpose of making the note principal and interest payments when due.
- C. A reserve fund shall be established and maintained at a level equal to or less than \$1,362,800. The reserve was fully funded at December 31, 2012 and 2011.
- D. Rates will be charged at a level sufficient to produce “Net Revenues” of not less than 125% of the principal and interest due on the bonds.

Series 2010 Water Revenue Bonds:

- A. Sufficient monthly transfers shall be made to the Water Revenue Bond Sinking Fund for the purpose of making the note principal and interest payments when due.
- B. A reserve fund shall be established and maintained at a level equal to or less than \$117,886. The reserve was fully funded at December 31, 2012 and 2011.
- C. Rates will be charged at a level sufficient to generate “Net Revenues” of not less than 125% of the principal and interest requirements on the bonds.

**ALGONA MUNICIPAL UTILITIES
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NOTES TO FINANCIAL STATEMENTS

NOTE 5 – REVENUE BONDS PAYABLE-continued

Series 2005 and 2010 Communications Revenue Bonds:

- A. Sufficient monthly transfers shall be made to the Communications Revenue Bond Sinking Fund for the purpose of making the note principal and interest payments when due.
- B. Rates will be charged at a level sufficient to generate “Net Revenues” of not less than 110% of the principal and interest requirements on the bonds.

NOTE 6 – INTEREST COSTS

During the years ended December 31, 2012 and 2011, the interest incurred and expensed by the Electric Fund was \$323,958 and \$66,700 respectively. The Electric Fund incurred \$172,871 and \$36,312 in interest that was capitalized in 2012 and 2011, respectively.

During the years ended December 31, 2012 and 2011, the interest incurred by the Communication Fund was \$208,865 and \$215,869 respectively. The Electric Fund recognized interest income of \$123,489 and \$123,152 from the interfund loan during 2012 and 2011.

During the years ended December 31, 2012 and 2011, the interest incurred and expensed by the Water Fund was \$39,662 and \$-0- respectively. The Water Fund incurred \$-0- and \$41,740 in interest that was capitalized in 2012 and 2011 respectively.

NOTE 7 – RESTRICTED FUNDS

As of December 31, 2012 Restricted Funds consisted of the following.

	Electric	Water	Communication	Total
Bond Sinking	110,887	9,359	-	120,246
Bond Reserve	1,362,800	124,680	-	1,487,480
Unspent Bond proceeds	6,811,539	-	-	6,811,539
Restricted note funds	8,285,226	134,039	-	8,419,265
Revolving loan fund	100,988	-	-	100,988
Deferred Compensation	210,928	5,407	20,907	237,242
	8,597,142	139,446	20,907	8,757,495

**ALGONA MUNICIPAL UTILITIES
A COMPONENT UNIT OF THE CITY OF ALGONA**

NOTES TO FINANCIAL STATEMENTS

NOTE 7 – RESTRICTED FUNDS - continued

As of December 31, 2011 Restricted Funds consisted of the following.

	Electric	Water	Communication	Total
Bond Sinking	109,337	9,484	-	118,821
Bond Reserve	1,362,800	124,680	-	1,487,480
Unspent bond proceeds	13,094,054	175,000	-	13,269,054
Restricted note funds	14,566,191	309,164	-	14,875,355
Revolving loan fund	121,113	-	-	121,113
Deferred Compensation	156,293	4,350	15,520	176,163
	14,843,597	313,514	15,520	15,172,631

The Bond Funds are restricted as stated in Note 5. The deferred compensation fund assets are maintained in a 457(b) plan.

NOTE 8 - PENSION AND RETIREMENT BENEFITS

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

Plan members are required to contribute 5.78% (5.38% through June 30, 2012) of their annual salary and AMU is required to contribute 8.67% (8.07% through June 30, 2012) of annual covered payroll. Contribution requirements are established by state statute. AMU's contributions to IPERS for the years ended December 31, 2012, 2011, and 2010 were \$171,312, \$148,301, and \$130,042 respectively, equal to the required contributions for each year.

NOTE 9 - TRANSFERS TO CITY IN LIEU OF PROPERTY TAXES

By resolution of AMU's Board of Trustees, effective for 2010 and all following years, the Utility will make an annual Payment in Lieu of Taxes (PILOT) to the City using the following formula to determine annual transfer of funds:

**ALGONA MUNICIPAL UTILITIES
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NOTES TO FINANCIAL STATEMENTS

NOTE 9 - TRANSFERS TO CITY IN LIEU OF PROPERTY TAXES - continued

Electric Transfer: Electric sales are based on the past 5 years average sales in dollars for retail electric divided by the equivalent kWh to get a \$/kWh amount. This creates a base sales amount for the PILOT. This amount will then be multiplied by the current year retail kWh sales to get the sales before transfer number. The current year City Free Services and the annual Power Cost Adjustment amount are subtracted from the Sales before Transfer to determine the Revenues Subject to the 5% PILOT. The December Cash Transfer and City Property Taxes paid are subtracted to determine the final amount Due to the City.

Water Transfer: Water sales are based on the past 5 years average sales in dollars for retail water divided by the equivalent cubic feet to get a \$/cubic foot amount. This creates a base amount for the PILOT. This amount will then be multiplied by the current year retail cubic foot sales to get the sales before transfer number. The current year City Free Services amount is subtracted from the Sales before Transfer to determine the Revenues Subject to the 5% PILOT. The December Cash Transfer and City Property Taxes paid are subtracted to determine the final amount due to the City.

Communications Transfer: Communications sales are based on the gross revenue for cable TV minus wholesale headend service revenue, Internet sales, and Telephone sales to determine the sales before transfer number. The current year City Free Services amount is subtracted from the Sales before Transfer to determine the Revenues Subject to the 5% PILOT. The December Cash Transfer and City Property Taxes paid are subtracted to determine the final amount due to the City.

NOTE 10 – RISK MANAGEMENT

The Utility is exposed to various risks of loss related to torts; theft, damage to and destruction of assets; error and omissions; injuries to employees; and natural disasters. These risks are covered by the purchase of commercial insurance. Settled claims from these risks have not exceeded commercial insurance coverage in any of the past three calendar years. The Utility assumes liability for any deductibles and claims in excess of coverage limitations.

NOTE 11 - JOINT VENTURES

AMU has a 15% ownership interest in the Iowa Public Power Agency (IPPA). IPPA was formed under Iowa Code chapter 28E for the purpose of enabling smaller municipal utilities to own an interest in electric transmission lines. AMU's total equity position at December 31, 2012 and 2011 is approximately \$175,662 (classified as

**ALGONA MUNICIPAL UTILITIES
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NOTES TO FINANCIAL STATEMENTS

NOTE 11 - JOINT VENTURES -continued

Investment in Joint Venture). This funding was to assist the IPPA purchase a \$3.5 million share in a transmission line project, in partnership with MidAmerican Energy. Audited statements for the IPPA are available upon request at the AMU business office.

Condensed financial information for IPPA as of December 31, 2012 and 2011 is as follows:

	December 31, 2012	December 31, 2011
Total assets	\$ 3,805,083	\$ 3,924,611
Total liabilities	3,028,257	3,121,383
Member equity	776,826	803,228
	\$ 3,805,083	\$ 3,924,611
Revenues	651,592	555,365
Expenses	(299,226)	(303,201)
Change in net assets	\$ 352,366	\$ 252,164

AMU has a 50% ownership interest in AMU-Skylink LC (an LLC). AMU-Skylink LC is a LLC with a private for-profit member that has constructed a tower to provide Algona residents with wireless telephone access. AMU's investment in AMU-Skylink LC is reported as an Investment in Joint Venture on the Communication Fund balance sheet and is valued at \$214,285 and \$210,396 as of December 31, 2012 and 2011. Audited statements for AMU-Skylink LC are available upon request at the AMU business office. Condensed financial information for AMU-Skylink LC as of December 31, 2012 and 2011 is as follows:

	December 31, 2012	December 31, 2011
Total assets	\$ 504,281	\$ 511,149
Total liabilities	75,708	90,357
Member equity	428,573	420,792
	\$ 504,281	\$ 511,149
Revenues	356,496	333,709
Expenses	(348,715)	(292,415)
Net income	\$ 7,781	\$ 41,294

**ALGONA MUNICIPAL UTILITIES
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NOTES TO FINANCIAL STATEMENTS

NOTE 12 – COMPENSATED ABSENCES

AMU employees accumulate a limited amount of earned but unused vacation. The Utilities' approximate liability for earned vacation payments payable to employees at December 31, 2012 and 2011 is as follows:

Type of Benefit	Electric	Water	Communications	Total
December 31, 2012: Vacation	\$ 76,157	11,017	16,569	\$ 103,743
December 31, 2011: Vacation	\$ 69,291	11,195	18,229	\$ 98,715

NOTE 13 – CAPITAL ASSETS

Capital asset activity for the years ended December 31, 2012 and 2011 was as follows:

December 31, 2012

Electric Fund

Proprietary Activities	Balance Beginning of Year	Increases	Decreases	Balance End of Year
Capital assets not being depreciated:				
Land	\$ 256,366	-	-	\$ 256,366
Construction in progress	1,053,000	3,875,990	-	4,928,990
	2,728,366	3,875,990	-	5,185,356
Capital assets being depreciated:				
Buildings and improvements	2,730,473	68,963	-	2,799,436
Equipment and vehicles	2,194,354	90,628	28,264	2,256,718
Infrastructure	44,857,573	2,429,406	82,428	47,204,551
Total capital assets being depreciated	49,782,400	2,588,997	110,692	52,260,705
Less accumulated depreciation for:				
Buildings and improvements	869,875	66,196	-	936,071
Equipment and vehicles	1,552,991	135,392	28,264	1,660,119
Infrastructure, road network	28,850,095	1,201,001	73,522	29,977,574
Total accumulated depreciation	31,272,961	1,402,589	101,786	32,573,764
Total capital assets being depreciated, net	18,509,439			19,686,941
Business type activities capital assets, net	\$19,818,805			\$24,872,297

Water Fund

Proprietary Activities	Balance Beginning of Year	Increases	Decreases	Balance End of Year
Capital assets not being depreciated:				
Land	\$ 12,306	-	-	\$ 12,306

**ALGONA MUNICIPAL UTILITIES
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NOTES TO FINANCIAL STATEMENTS

NOTE 13 – CAPITAL ASSETS - continued

Construction in progress	50,951	45,946	50,951	45,946
	<u>63,257</u>	<u>45,946</u>	<u>50,951</u>	<u>58,252</u>
Capital assets being depreciated:				
Equipment and vehicles	282,628	32,004	22,075	292,557
Infrastructure	5,667,727	656,027	21,388	6,302,366
Total capital assets being depreciated	<u>5,950,355</u>	<u>688,031</u>	<u>43,463</u>	<u>6,594,923</u>
Less accumulated depreciation for:				
Equipment and vehicles	180,682	23,126	22,075	181,733
Infrastructure, road network	2,695,505	136,220	21,389	2,810,336
Total accumulated depreciation	<u>2,876,187</u>	<u>159,346</u>	<u>43,464</u>	<u>2,992,069</u>
Total capital assets being depreciated, net	<u>3,074,168</u>			<u>3,602,854</u>
Business type activities capital assets, net	<u>\$ 3,137,425</u>			<u>\$ 3,661,106</u>

Communications Fund

Proprietary Activities	Balance Beginning of Year	Increases	Decreases	Balance End of Year
Capital assets not being depreciated:				
Land	\$ 49,635	-	-	\$ 49,635
Construction in progress	24,065	138,100	-	162,165
	<u>73,700</u>	<u>138,100</u>	<u>-</u>	<u>211,800</u>
Capital assets being depreciated:				
Buildings and improvements	271,793	-	-	271,793
Equipment and vehicles	187,198	10,306	-	197,504
Infrastructure	5,765,399	91,755	115,190	5,741,964
Total capital assets being depreciated	<u>6,224,390</u>	<u>102,061</u>	<u>115,190</u>	<u>6,211,261</u>
Less accumulated depreciation for:				
Buildings and improvements	88,251	10,708	-	98,959
Equipment and vehicles	127,372	10,980	-	138,352
Infrastructure, road network	2,608,393	344,664	47,126	2,905,931
Total accumulated depreciation	<u>2,824,016</u>	<u>366,352</u>	<u>47,126</u>	<u>3,143,242</u>
Total capital assets being depreciated, net	<u>3,400,374</u>			<u>3,068,019</u>
Business type activities capital assets, net	<u>\$ 3,474,074</u>			<u>\$ 3,279,819</u>

December 31, 2011

Electric Fund

Proprietary Activities	Balance Beginning of Year	Increases	Decreases	Balance End of Year
Capital assets not being depreciated:				
Land	\$ 256,366	-	-	\$ 256,366
Construction in progress	2,472,000	947,905	2,366,905	1,053,000
	<u>2,728,366</u>	<u>947,905</u>	<u>2,366,905</u>	<u>1,309,366</u>

**ALGONA MUNICIPAL UTILITIES
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NOTES TO FINANCIAL STATEMENTS

NOTE 13 – CAPITAL ASSETS - continued

Capital assets being depreciated:				
Buildings and improvements	2,730,473	-	-	2,730,473
Equipment and vehicles	2,620,891	148,757	575,294	2,194,354
Infrastructure	42,665,059	2,826,681	634,167	44,857,573
Total capital assets being depreciated	<u>48,016,423</u>	<u>2,975,438</u>	<u>1,209,461</u>	<u>49,782,400</u>
Less accumulated depreciation for:				
Buildings and improvements	802,765	67,110	-	869,875
Equipment and vehicles	1,980,510	146,795	574,314	1,552,991
Infrastructure, road network	28,270,509	1,199,693	620,107	28,850,095
Total accumulated depreciation	<u>31,053,784</u>	<u>1,413,598</u>	<u>1,194,421</u>	<u>31,272,961</u>
Total capital assets being depreciated, net	<u>16,962,639</u>			<u>18,509,439</u>
Business type activities capital assets, net	<u>\$20,494,337</u>			<u>\$19,818,805</u>

Water Fund

Proprietary Activities	Balance Beginning of Year	Increases	Decreases	Balance End of Year
Capital assets not being depreciated:				
Land	\$ 12,306	-	-	\$ 12,306
Construction in progress	58,819	50,951	58,819	50,951
	<u>71,125</u>	<u>50,951</u>	<u>58,819</u>	<u>63,257</u>
Capital assets being depreciated:				
Equipment and vehicles	328,652	13,907	59,931	282,628
Infrastructure	4,963,292	985,113	280,678	5,667,727
Total capital assets being depreciated	<u>5,291,944</u>	<u>999,020</u>	<u>340,609</u>	<u>5,950,355</u>
Less accumulated depreciation for:				
Equipment and vehicles	221,507	19,106	59,931	180,682
Infrastructure, road network	2,799,191	105,499	209,185	2,695,505
Total accumulated depreciation	<u>3,020,698</u>	<u>124,605</u>	<u>269,116</u>	<u>2,876,187</u>
Total capital assets being depreciated, net	<u>2,271,246</u>			<u>3,074,168</u>
Business type activities capital assets, net	<u>\$ 2,342,371</u>			<u>\$ 3,137,425</u>

Communications Fund

Proprietary Activities	Balance Beginning of Year	Increases	Decreases	Balance End of Year
Capital assets not being depreciated:				
Land	\$ 49,635	-	-	\$ 49,635
Construction in progress	29,840	24,065	29,840	24,065
	<u>79,475</u>	<u>24,065</u>	<u>29,840</u>	<u>73,700</u>

**ALGONA MUNICIPAL UTILITIES
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NOTES TO FINANCIAL STATEMENTS

NOTE 13 – CAPITAL ASSETS - continued

Capital assets being depreciated:				
Buildings and improvements	271,793	-	-	271,793
Equipment and vehicles	172,482	14,716	-	187,198
Infrastructure	5,713,648	285,340	233,589	5,765,399
Total capital assets being depreciated	<u>6,157,923</u>	<u>300,056</u>	<u>233,589</u>	<u>6,224,390</u>
Less accumulated depreciation for:				
Buildings and improvements	77,543	10,708	-	88,251
Equipment and vehicles	118,923	8,449	-	127,372
Infrastructure, road network	2,356,812	386,470	134,889	2,608,393
Total accumulated depreciation	<u>2,553,278</u>	<u>405,627</u>	<u>134,889</u>	<u>2,824,016</u>
Total capital assets being depreciated, net	<u>3,604,645</u>			<u>3,400,374</u>
Business type activities capital assets, net	<u>\$ 3,704,734</u>			<u>\$ 3,474,074</u>

Depreciation expense was charged to the following functions:

Proprietary activities:	December 31, 2012	December 31, 2011
Electric	\$ 1,402,589	\$ 1,413,598
Water	159,346	124,605
Communications	366,352	405,627
	<u>\$ 1,928,287</u>	<u>\$ 1,943,830</u>

NOTE 14 – JOINT LEASE AGREEMENT

Algona Municipal Utilities constructed a distribution system to facilitate the implementation of the data services offered to area residents and businesses. Portions of this system and the office facilities maintained by the Electric utility are leased under a forty-year operating lease, requiring annual payments of \$128,622. As of December 31, 2012 and 2011, \$128,622 in lease payments due under this agreement was included in accounts payable. The future minimum lease payments are as follows:

Year Ending	
2013	\$ 128,622
2014	128,622
2015	128,622
2016	128,622
2017	128,622
2018-2022	643,110
2023-2027	643,110

**ALGONA MUNICIPAL UTILITIES
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NOTES TO FINANCIAL STATEMENTS

NOTE 14 – JOINT LEASE AGREEMENT -continued

2028-2032	643,110
2033-2037	643,110
2038-2042	643,110
2043	128,622
Total	\$ 3,987,282

NOTE 15 – DEFICIT NET ASSETS

The Communications Fund has a deficit balance of \$1,424,622 and \$1,435,226 as of December 31, 2012 and 2011 respectively.

NOTE 16 – OTHER POSTEMPLOYMENT BENEFITS (OPEB)

Plan Description. AMU operates a single-employer retiree benefit plan which provides medical/dental benefits for retirees and their spouses. There are 33 active and 2 retired members in the plan. Participants must be age 55 or older at retirement.

The medical/dental coverage is administered by Wellmark. Retirees receive 1 year of full health/dental benefits for every 10 years of service to AMU, which results in an explicit subsidy. Retirees under age 65 pay the same premium for the medical/dental benefit as active employees, which results in an implicit subsidy. The explicit and implicit subsidies result in an OPEB liability.

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

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

The following table shows the components of the AMU’s annual OPEB cost for the year ended December 31, 2012 and 2011, the amount actually contributed to the plan and changes in AMU’s net OPEB obligation:

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NOTES TO FINANCIAL STATEMENTS

NOTE 16 – OTHER POSTEMPLOYMENT BENEFITS (OPEB) – continued

	Electric	Water	Communications	Total
Annual required contribution	\$ 37,747	\$ 4,888	\$ 15,564	\$ 58,199
Interest on net OPEB obligation	1,509	195	622	2,326
Adjustment to annual required contribution	-	-	-	-
Annual OPEB cost	39,256	5,083	16,186	60,525
Net OPEB obligation beginning of year	118,158	22,896	40,068	181,122
Net OPEB obligation end of year	157,414	27,979	56,254	241,647

For calculation of the net OPEB obligation, the actuary has set the measurement date as December 31, 2012. The end of year net OPEB obligation was calculated by the actuary as the cumulative difference between the actuarially determined funding requirements and the actual contributions for the years ended December 31, 2012 and 2011.

For the years ended December 31, 2012 and 2011, AMU did not contribute to the medical plan.

AMU's annual OPEB cost, the percentage of annual OPEB cost contributed to the plan and the net OPEB obligation for the previous three years are as follows:

Year Ended	Annual OPEB Cost	Percentage of Annual OPEB Cost Contributed	Net OPEB Obligation
December 31, 2012	\$ 60,525	0%	\$ 241,647
December 31, 2011	\$ 60,374	0%	\$ 181,122
December 31, 2010	\$ 60,374	0%	\$ 120,748

Funded Status and Funding Progress. As of December 31, 2012, the most recent actuarial valuation date for the periods from January 1, 2012 through December 31, 2012 and January 1, 2011 through December 31, 2011, the actuarial accrued liability was \$466,935, with no actuarial value of assets, resulting in an unfunded actuarial accrued liability (UAAL) of \$466,935. The covered payroll (annual payroll of active employees covered by the plan) was approximately \$2.0 million and the ratio of the UAAL to covered payroll was 23% for 2012 and 23% for 2011. As of December 31, 2012 and 2011, there were no trust fund assets.

Actuarial Methods and Assumptions. Actuarial valuations of an ongoing plan involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future

**ALGONA MUNICIPAL UTILITIES
A COMPONENT UNIT OF THE CITY OF ALGONA**

NOTES TO FINANCIAL STATEMENTS

NOTE 16 – OTHER POSTEMPLOYMENT BENEFITS (OPEB) - continued

employment, mortality and the health care cost trend. Actuarially determined amounts are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future. The schedule of funding progress, presented as required supplementary information in the section following the Notes to Financial Statements, will present multiyear trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liabilities for benefits.

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

As of December 31, 2012 the actuarial measurement date, the unit credit actuarial cost method was used. The actuarial assumptions include a 4% discount rate based on AMU's funding policy. The projected annual medical trend rate is 10%. The ultimate medical trend rate is 5%. The medical trend rate is reduced 0.5% each year until reaching the 5% ultimate trend rate.

Mortality rates are from the RP2000 Combined Mortality Table Fully Generational. Annual retirement and termination probabilities were developed based on national averages.

Projected claim costs of the medical plan are \$628 per month for retirees less than age 65 and \$331 per month for retirees who have attained age 65. The salary increase rate was assumed to be 3% per year. The UAAL is being amortized as a level percentage of projected payroll expense on an open basis over 30 years.

NOTE 17 – ACCOUNTING CHANGE

Effective for the years ended December 31, 2012 and 2011 (restated retroactively) the Utilities have elected to treat the transfers to the City of Algona in lieu of property tax as an operating expense rather than a non-operating expense. The change in accounting resulted in decreased operating income (or and increase in the operating loss) while not affecting the overall change in net position. The following is a summary of the effect of the accounting change for each of the utilities.

ALGONA MUNICIPAL UTILITIES
A COMPONENT UNIT OF THE CITY OF ALGONA

NOTES TO FINANCIAL STATEMENTS

NOTE 17 – ACCOUNTING CHANGE - continued

<u>Electric Fund</u>	<u>2012</u>		<u>2011</u>	
	Current Method	Old Method	Current Method	Old Method
Operating expense				
Transfers to City in lieu of	\$ 320,371	\$ -	\$ 331,904	\$ -
Total operating expenses	11,053,565	10,733,194	10,532,082	10,200,178
Income (loss) from operations	(281,804)	38,567	(276,599)	55,305
Non-Operating income (expense)				
Transfers to City in lieu of	-	(320,371)	-	(331,904)
Total Non-operating income	307,010	(13,361)	124,435	(207,469)
<u>Water Fund</u>	<u>2012</u>		<u>2011</u>	
	Current Method	Old Method	Current Method	Old Method
Operating expense				
Transfers to City in lieu of	\$ 44,244	\$ -	\$ 38,145	\$ -
Total operating expenses	785,054	740,810	785,054	753,129
Income (loss) from operations	231,905	276,149	121,973	160,118
Non-Operating income (expense)				
Transfers to City in lieu of	-	(44,244)	-	(38,145)
Total Non-operating income	(17,823)	(62,067)	(40,273)	(78,418)
<u>Communications Fund</u>	<u>2012</u>		<u>2011</u>	
	Current Method	Old Method	Current Method	Old Method
Operating expense				
Transfers to City in lieu of	\$ 146,163	\$ -	\$ 144,486	\$ -
Total operating expenses	3,133,797	2,990,634	3,088,195	2,943,709
Income (loss) from operations	253,781	396,944	235,467	379,953
Non-Operating income (expense)				
Transfers to City in lieu of	-	(143,163)	-	(144,486)
Total Non-operating income	(243,177)	(386,340)	(299,076)	(443,562)

**ALGONA MUNICIPAL UTILITIES
A COMPONENT UNIT OF THE CITY OF ALGONA**

NOTES TO FINANCIAL STATEMENTS

NOTE 18 – RECLASSIFICATION OF BALANCES

Certain items on the Statement of Revenue, Expense, and Changes in Fund Net Position have been reclassified to be comparable to the amounts reported for 2012. The reclassification had no effect on the change in net position for 2011.

NOTE 19 – SUBSEQUENT EVENTS

In January 2013 the AMU approved a bid for the planned Fiber to Home electronics project amounting to \$1,266,992.

In preparing these financial statements, management has evaluated events and transactions for potential recognition or disclosure through May 21, 2013, the date the financial statements were issued.

Required Supplementary Information

ALGONA MUNICIPAL UTILITIES
A COMPONENT UNIT OF THE CITY OF ALGONA

BUDGETARY COMPARISON SCHEDULE
OF RECEIPTS, DISBURSEMENTS
BUDGET AND ACTUAL - ALL PROPRIETARY FUNDS

REQUIRED SUPPLEMENTARY INFORMATION

YEAR ENDED DECEMBER 31, 2012

	Proprietary Funds	<u>Budgeted Amounts</u>	Final to Net
	Actual	Original	Variance
Receipts:			
Charges for service	\$ 14,790,268	\$ 14,973,000	(182,732)
Miscellaneous	832,598	551,000	281,598
Other financing sources	-	-	-
	<u>15,622,866</u>	<u>15,524,000</u>	<u>98,866</u>
Disbursements:			
Program			
Business type activities	21,479,387	21,806,100	326,713
Transfers out	-	538,000	538,000
	<u>21,479,387</u>	<u>22,344,100</u>	<u>864,713</u>
Change in net assets	(5,856,521)	(6,820,100)	963,579
Balance beginning of year	17,992,236	14,015,911	3,976,325
Balance end of year	<u>\$ 12,135,715</u>	<u>\$ 7,195,811</u>	<u>4,939,904</u>

The budgetary presentation is based on a comprehensive basis of accounting which is different than that used to prepare the financial statements. The reconciliation from accounting principles generally accepted in the United States used for financial reporting and those used to prepare the budget is presented below.

	Financial Statements	Adjustments	Budgeted Basis
Revenues	\$ 16,067,359	\$ (444,493)	\$ 15,622,866
Disbursements	16,215,687	5,263,700	21,479,387
Other financing sources	-	-	-
Increase (decrease) in net position	<u>\$ (148,328)</u>	<u>\$ (5,708,193)</u>	<u>\$ (5,856,521)</u>

See Accompanying Independent Auditor's Report

**ALGONA MUNICIPAL UTILITIES
A COMPONENT UNIT OF THE CITY OF ALGONA**

NOTES TO REQUIRED SUPPLEMENTARY INFORMATION – BUDGETARY REPORTING

YEAR ENDED DECEMBER 31, 2012

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

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

Formal and legal budgetary control is based upon nine major classes of disbursements known as functions, not by fund or fund type. These nine functions are: public safety, public works, health and social services, culture and recreation, community and economic development, general government, debt service, capital projects, and business type activities. Function disbursements required to be budgeted include disbursements for the all Proprietary Funds. Although the budget document presents functional disbursements by fund, the legal level of control is at the aggregated function level, not by fund.

**ALGONA MUNICIPAL UTILITIES
A COMPONENT UNIT OF THE CITY OF ALGONA**

**SCHEDULE OF FUNDING PROGRESS FOR THE
RETIREE HEALTH PLAN
(In Thousands)**

Required Supplementary Information

Year Ended December 31	Actuarial Valuation Date	Actuarial Value of Assets	Actuarial Accrued Liability	Unfunded AAL (UAAL)	Funded Ratio	Covered Payroll	UAAL as a Percentage of Covered Payroll
		(a)	(b)	(c)	(a/b)	(c)	(b-a)/c
2012	December 31, 2012	-0-	\$467	\$467	0.00%	\$2,000	23.4%
2011	January 1, 2009	-0-	\$412	\$412	0.00%	\$1,900	21.7%
2010	January 1, 2009	-0-	\$412	\$412	0.00%	\$1,800	22.9%
2009	January 1, 2009	-0-	\$412	\$412	0.00%	\$1,682	24.5%

See Note 16 in the accompanying Notes to Financial Statements for the plan description, funding policy, annual OPEB Cost and net OPEB Obligation, funded status and funding progress.

Supplementary Information

**ALGONA MUNICIPAL UTILITIES
A COMPONENT UNIT OF THE CITY OF ALGONA**

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

For the Year Ended December 31, 2012

Grantor/Program	CFDA Number	Agency Pass-through Number	Program Expenditures
Direct:			
USAD Rural Development			
Rural Economic Loans and Grants	10.854		300,000
Indirect:			
Department of Energy			
Iowa Office of Energy Independence			
Energy Efficiency and Conservation			
Block Grant - ARRA	81.128	3367	283,357
Iowa Association of Municipal Utilities			
State Energy Program	81.041	SEP 09025	66,490
Electricity Delivery and Energy			
Reliability, Research, and Analysis	81.122	DE 0000359	5,290
			<u>655,137</u>

Basis of Presentation - The Schedule of Expenditures of Federal Awards includes the federal grant activity of Algona Municipal Utilities and is presented in conformity with an other comprehensive basis of accounting. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations. Therefore, some amounts presented in the schedule may differ from amounts presented in, or used in the preparation of, the basic financial statements.

Other Information

ALGONA MUNICIPAL UTILITIES

Schedule 1

**ELECTRIC DEPARTMENT
COMPARATIVE SUMMARIES OF ELECTRICITY DISTRIBUTED AND BILLED
YEAR ENDED DECEMBER 31,**

	<u>2012</u>	<u>2011</u>	<u>2010</u>
Sale of electricity:			
Sales to consumers	\$ 7,914,391	\$ 7,294,060	\$ 6,976,511
Sales to other utilities	137,668	158,513	172,685
Sales for resale	<u>2,523,878</u>	<u>2,611,900</u>	<u>2,779,925</u>
Total electricity sales	<u><u>10,575,937</u></u>	<u><u>10,064,473</u></u>	<u><u>9,929,121</u></u>
Kilowatt hours:			
Wind generation	4,967,953	5,039,658	5,414,064
Generated	146,943,092	136,291,041	147,441,387
Purchases	47,893,669	40,330,486	35,021,336
System losses (transmission)	<u>(3,433,574)</u>	<u>(3,276,633)</u>	<u>(3,146,534)</u>
Available for sale	196,371,140	178,384,552	184,730,253
Billed to consumers	111,282,762	105,640,353	104,747,725
Sales to other utilities	4,056,330	4,572,294	4,909,921
Sales for resale	76,950,778	64,123,797	74,412,947
Distribution loss	4,081,270	4,048,108	659,660
Distribution loss percent	3.42%	3.54%	0.60%
Revenue billed per kWh to consumers	\$ 0.0711	\$ 0.0690	\$ 0.0666
Peak hour demand in kilowatts	24,950	23,950	23,350
Services provided to the City			
Street lighting:			
Energy	\$ 34,123	\$ 63,663	\$ 68,147
Operation and Maintenance	<u>11,211</u>	<u>15,812</u>	<u>21,222</u>
	45,334	79,475	89,369
Other Maintenance Costs	3,743	8,233	8,404
Energy for Public Buildings, Parks and Other uses	<u>103,545</u>	<u>94,850</u>	<u>104,558</u>
	<u><u>\$ 152,622</u></u>	<u><u>\$ 182,558</u></u>	<u><u>\$ 202,331</u></u>
Year to date kWh sales			
Residential	31,256,589	31,717,225	32,746,988
Commercial	80,287,411	74,234,568	72,368,877
Area Lighting	639,629	1,242,163	1,317,932
Station Power	1,899,860	1,749,218	1,705,762
City	<u>1,255,603</u>	<u>1,269,473</u>	<u>1,518,087</u>
Total number of kWh sales	<u><u>115,339,092</u></u>	<u><u>110,212,647</u></u>	<u><u>109,657,646</u></u>

Unaudited - See Accompanying Independent Auditor's Report

ALGONA MUNICIPAL UTILITIES

Schedule 2

**WATER DEPARTMENT
COMPARATIVE SUMMARIES OF WATER PUMPED AND BILLED
YEAR ENDED DECEMBER 31,**

	<u>2012</u>	<u>2011</u>	<u>2010</u>
Total revenue billed	\$ 998,132	\$ 895,033	\$ 895,033
Cubic Foot			
Pumped	38,618,214	40,116,171	40,261,093
Billed	33,361,070	30,833,241	31,915,245
City of Algona	351,675	936,332	490,338
System loss	4,905,469	8,346,598	7,855,510
Percent loss	12.70%	20.81%	19.51%
Revenue billed per cubic foot	\$ 0.0296	\$ 0.0282	\$ 0.0265
Peak day-cubic footage pumped	203,128	173,133	159,374
Services provided to City			
Water for parks, disposal plant and public buildings	\$ 11,318	\$ 20,952	\$ 12,543
Public fire protection	19,690	19,620	18,450
	<u>\$ 31,008</u>	<u>\$ 40,572</u>	<u>\$ 30,993</u>

Unaudited - See Accompanying Independent Auditor's Report

ALGONA MUNICIPAL UTILITIES

Schedule 3

**COMMUNICATIONS
COMPARATIVE SUMMARIES OF CABLE, INTERNET, AND TELEPHONE
YEAR ENDED DECEMBER 31,**

	<u>2012</u>	<u>2011</u>	<u>2010</u>
Operating revenue:			
Cable TV	\$ 1,123,865	\$ 1,103,906	\$ 1,083,069
Internet	832,871	806,180	754,851
Telephone	1,317,666	1,284,177	1,128,424
Cell phone	66,810	62,631	77,040
Miscellaneous	<u>116,434</u>	<u>108,940</u>	<u>77,206</u>
Total operating revenue	<u><u>\$ 3,457,646</u></u>	<u><u>\$ 3,365,834</u></u>	<u><u>\$ 3,120,590</u></u>
Customers			
Cable TV	1,873	1,911	1,859
Internet	1,836	1,784	1,681
Telephone	1,580	1,632	1,603
Cell phone	512	532	519
Average monthly revenue per customer			
Cable TV	50.00	48.14	48.55
Internet	37.80	37.66	37.42
Telephone	69.50	65.57	58.66
Services provided to City			
Cable TV	\$ 1,786	\$ 1,786	\$ 1,786
Internet	4,470	4,378	4,173
Telephone	<u>957</u>	<u>1,143</u>	<u>1,054</u>
	<u><u>\$ 7,213</u></u>	<u><u>\$ 7,307</u></u>	<u><u>\$ 7,013</u></u>

Unaudited - See Accompanying Independent Auditor's Report



T.P. ANDERSON & COMPANY, P.C.
CERTIFIED PUBLIC ACCOUNTANTS AND CONSULTANTS

**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 Board of Trustees of the
Algona Municipal Utilities:

We have audited, in accordance with the 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, the financial statements of each major fund of Algona Municipal Utilities, as of and for the year ended December 31, 2012, and the related notes to the financial statements, which collectively comprise AMU's basic financial statements, and have issued our report thereon dated May 21, 2013.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered Algona Municipal Utilities' internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of Algona Municipal Utilities' internal control. Accordingly, we do not express an opinion on the effectiveness of Algona Municipal Utilities' internal control.

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 entity's financial statements will not be prevented, or detected and corrected on a timely basis. No material weaknesses in internal control were noted. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified. We did identify a certain deficiency in internal control, described in Part II of the Schedule of Findings and Questioned Costs as II-A-12 that we consider to be a significant deficiency.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Algona Municipal Utilities' financial statements are free from 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*.

Algona Municipal Utilities' response to the internal control finding identified in our audit is described in the accompanying schedule of findings and questioned costs. Algona Municipal Utilities' response was not subjected to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on the response.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

JP Anderson & Company, PC

May 21, 2013



T.P. ANDERSON & COMPANY, P.C.
CERTIFIED PUBLIC ACCOUNTANTS AND CONSULTANTS

Independent Auditor's Report on Compliance For Each Major Federal Program; Report on Internal Control Over Compliance; and Report on Schedule of Expenditures of Federal Awards Required by OMB Circular A-133

To the Board of Trustees of
Algona Municipal Utilities

Report on Compliance for Each Major Federal Program

We have audited Algona Municipal Utilities' compliance with the types of compliance requirements described in the *OMB Circular A-133 Compliance Supplement* that could have a direct and material effect on each of Algona Municipal Utilities' major federal programs for the year ended December 31, 2012. Algona Municipal Utilities' major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs.

Management's Responsibility

Management is responsible for compliance with the requirements of laws, regulations, contracts, and grants applicable to its federal programs.

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for each of Algona Municipal Utilities' major federal programs based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about Algona Municipal Utilities' compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

We believe that our audit provides a reasonable basis for our opinion on compliance for each major federal program. However, our audit does not provide a legal determination of Algona Municipal Utilities compliance.

Opinion on Each Major Federal Program

In our opinion, Algona Municipal Utilities complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended December 31, 2012.

Report on Internal Control Over Compliance

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

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. *A material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. *A significant deficiency in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance. Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, we identified a certain deficiency in internal control over compliance, as described in the accompanying schedule of findings and questioned costs as item III-A-12 that we consider to be a significant deficiency.

Algona Municipal Utilities' response to the internal control over compliance finding identified in our audit is described in the accompanying schedule of findings and questioned costs. Algona Municipal Utilities' response was not subjected to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on the response.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of OMB Circular A-133. Accordingly, this report is not suitable for any other purpose.

JP Anderson & Company, PC

May 21, 2013

ALGONA MUNICIPAL UTILITIES
A COMPONENT UNIT OF THE CITY OF ALGONA
SCHEDULE OF FINDINGS and QUESTIONED COSTS

Part I: Summary of the Independent Auditor's Results

- (a) Unqualified opinions were issued on the financial statements for each major fund.
- (b) A significant control deficiency in internal control over financial reporting was disclosed by the audit of the financial statements.
- (c) The audit did not disclose any non-compliance which is material to the financial statements.
- (d) A significant deficiency in internal control over the major programs were disclosed by the audit of the financial statements.
- (e) An unqualified opinion was issued on compliance with requirements applicable to each major program.
- (f) The major programs were CFDA Number 10.854 – Rural Economic Loans and Grants, and CFDA 81.041 State Energy Program.
- (h) The dollar threshold used to distinguish between Type A and Type B programs was \$300,000.
- (i) Algona Municipal Utilities did not qualify as a low-risk auditee.

ALGONA MUNICIPAL UTILITIES
A COMPONENT UNIT OF THE CITY OF ALGONA
SCHEDULE OF FINDINGS and QUESTIONED COSTS

Part II: Findings Related to the Financial Statements

INSTANCES OF NON-COMPLIANCE:

No matters were noted.

SIGNIFICANT CONTROL DEFICIENCY:

II-A-12 Monitoring – The audit of the financial statements revealed one adjustment that was material to the financial statements. The entry corrected the posting of grant money received to record fixed assets.

Criteria – A system of internal controls is to identify and detect and correct material adjustments.

Cause – The grant proceeds received were ultimately used to improve street lights benefiting the City of Algona and the adjustment did not have an effect on the change in net position for 2012.

Effect – Revenues and expenses were understated by \$175,000.

Recommendation – Grant proceeds received to finance the purchase of fixed assets should be reported on the Statement of Revenues, Expenses and Changes in Net Position.

Response and Corrective Action Plan – We will record grant revenues as you have recommended.

Conclusion – Response and Corrective Action Plan is accepted.

**ALGONA MUNICIPAL UTILITIES
A COMPONENT UNIT OF THE CITY OF ALGONA**

SCHEDULE OF FINDINGS and QUESTIONED COSTS

Part III: Findings and Questioned Costs for Federal Awards:

Instances of Non-Compliance:

**CFDA Number 10.854: Rural Economic Loans and Grants
Federal Award Year: 2012
U.S. Department Agriculture**

No matters were noted.

**CFDA Number 81.041: State Energy Program
Pass-through Agency Number: SEP 09025
Federal Award Year: 2012
U.S. Department of Energy
Passed through the Iowa Association of Municipal Utilities**

No matters were noted.

SIGNIFICANT CONTROL DEFICIENCY:

III-A-12 Monitoring – Audit procedures revealed the fact that Algona Municipal Utilities was subject to the Single Audit Requirements.

Criteria – Recipients of federal awards are required to track federal awards expended and be cognizant of all applicable audit requirements.

Cause – Certain grant proceeds received by Algona Municipal Utilities were spent to benefit the City of Algona even though they were expended by Algona Municipal Utilities. These expenditures were not initially believed to be federal awards expended.

Effect – Audit requirements applicable to Algona Municipal Utilities would not have been complied with.

Recommendation – All federal award programs and awards expended, along with the CFDA numbers for each program should be documented prior to or as federal funds are being expended.

Response and Corrective Action Plan – We will document all federal awards as you have recommended.

Conclusion – Response and Corrective Action Plan is accepted.

ALGONA MUNICIPAL UTILITIES
A COMPONENT UNIT OF THE CITY OF ALGONA
SCHEDULE OF FINDINGS and QUESTIONED COSTS

Part IV: Other Findings Related to Statutory Reporting:

- IV-A-12 Certified Budget - Disbursements for the year ended December 31, 2012 were within the budgeted limits.
- IV-B-12 Questionable Disbursement - We noted no questionable disbursements in regard to the requirements of public purpose as defined in an Attorney General's opinion dated April 25, 1979.
- IV-C-12 Travel Expense – No disbursements of AMU money for travel expenses of spouses of Utility officials or employees were noted.
- IV-D-12 Business Transactions – No transactions with AMU officials or employees were noted.
- IV-E-12 Bond Coverage – Surety bond coverage of Utility 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.
- IV-F-12 Board Minutes - No transactions were found that we believe should have been approved in the board minutes but were not.
- IV-G-12 Revenue Bonds – The electric revenue bonds have a covenant that requires the utility to generate net revenues equal to 125% of the next year's principal and interest requirements.
- Cause – Expenses for the electric utility have increased at a faster pace than the related revenues generated.
- Effect – Algona Municipal Utilities did not comply with the net revenue requirements for the electric revenue bonds.
- Recommendation – Rates should be adjusted in order to generate net revenues sufficient to comply with the revenue bond requirements.
- Response and Corrective Action Plan – We had a rate study conducted and approved changes to our electric rates in January of 2013.
- Conclusion – Response and Corrective Action Plan is accepted.

ALGONA MUNICIPAL UTILITIES
A COMPONENT UNIT OF THE CITY OF ALGONA
SCHEDULE OF FINDINGS and QUESTIONED COSTS

Part IV: Other Findings Related to Statutory Reporting - continued:

IV-H-12 Deposits and Investments - We noted no instances of noncompliance with the deposit and investment provisions of Chapter 12B and 12C of the Code of Iowa and the Utilities' investment policy.

IV-I-12 Telecommunication Services – No instance of noncompliance with Chapter 388.10 of the Code of Iowa were noted.

IV-J-12 Financial Condition – The Communications Fund had a deficit fund balance of \$1,424,622 at December 31, 2012.

Recommendation – AMU should investigate alternatives to eliminate the deficit in order to return this fund to a sound financial position.

Response – AMU is and has been conducting rate studies reviewing options to eliminate the deficit.

Conclusion – Response accepted.