

**Keokuk Municipal Waterworks,
A Component Unit of the City of Keokuk**

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

June 30, 2013

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**Keokuk Municipal Waterworks,
A Component Unit of the City of Keokuk
Board of Trustees
June 30, 2013**

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



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Independent Auditor's Report

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

Report on the Financial Statements

We have audited the accompanying financial statements of the proprietary fund of Keokuk Municipal Waterworks (Waterworks), a component unit of the City of Keokuk, as of and for the year ended June 30, 2013, and the related notes to the financial statements, which collectively comprise the Waterworks' 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.

Basis for Qualified Opinion

As discussed in Note 1, the Waterworks did not record or disclose the net annual required contribution for other postemployment benefits (OPEB) or the OPEB net liability obligation as required by Governmental Accounting Standards Board Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*. The amount by which this departure would affect liabilities, net position and operating expenses has not been determined.

Qualified Opinion

In our opinion, except for the omission of the information described in the "Basis for Qualified Opinion" paragraph, the financial statements referred to above present fairly, in all material respects, the respective financial position of Keokuk Municipal Waterworks as of June 30, 2013, and the respective changes in financial position, and, where applicable, cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As described in Note 12 to the financial statements, as of July 1, 2012, the Waterworks adopted new accounting guidance, GASB Statement No. 65, *Items Previously Reported as Assets and Liabilities*, and made error corrections for property, plant and equipment and inventory. Our opinion is not modified with respect to these matters.

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 5 through 10 and 24 through 25 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, which 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 Waterworks' basic financial statements. The supplementary information included on pages 26 through 27 is presented for purposes of additional analysis and is not a required part of the basic financial statements. The schedule of expenditures of federal awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is also not a required part of the basic financial statements.

The supplementary information included on pages 26 through 27 and schedule of expenditures of federal awards is the responsibility of management and was derived from and relate 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 supplementary information included on pages 26 through 27 and schedule of expenditures of federal awards is fairly stated in all material respects in relation to the basic financial statements as a whole.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated January 20, 2014, on our consideration of the Waterworks' 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 the Waterworks' internal control over financial reporting and compliance.

CPA Associates PC

January 20, 2014

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

The following Management's Discussion and Analysis (MD&A) of Keokuk Municipal Waterworks' activities and financial performance provides the reader with an introduction and overview to the financial statements of Keokuk Municipal Waterworks (Waterworks) for the fiscal year ended June 30, 2013. The information contained in this MD&A should be considered in conjunction with the Waterworks' basic financial statements.

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

Financial Operations Highlights

As a result of this year's operations, assets exceeded liabilities by \$25.7 million (net position) for the fiscal year reported. This compares to the previous year when assets exceeded liabilities by \$23.2 million. The net position increased by \$2,552,249 or 10.9%.

The following comprises total net position:

- Net position invested in capital assets (e.g., main extensions, buildings, improvements, and equipment), less the related indebtedness outstanding used to acquire those capital assets is \$21,937,809. This balance represents resources allocated to capital assets. These capital assets, less accumulated depreciation, are shown at depreciated cost of \$35,972,586.
- Restricted net position of \$1,703,417 represents resources that are subject to external restrictions such as grantors, laws, debt covenants or regulations.
- Unrestricted net position of \$2,093,709 represents resources that can be used at the discretion of management and the Board of Trustees.

During the year, revenues increased \$293,500, or 4.20%, while operating expenses increased \$237,700, or 4.18%. The increase in revenues is due to an increase in water rates, rate effective January 2012, and Roquette America has increased water usage..

Net nonoperating expenses decreased \$24,000, or 5.02%, and are primarily attributable to the decrease in interest expense.

The Waterworks also recognized capital contributions of \$1,603,000 in the current year related to the State Revolving Loan debt forgiveness received for the water tower construction project.

Using This Annual Report

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

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

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

Using This Annual Report (continued)

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

Financial Position Summary

Net position may serve over time as a useful indicator of the Waterworks' financial position. The Waterworks' net position exceeded liabilities by \$25.7 million at June 30, 2013, an increase of \$2,552,249 from 2012.

A condensed summary of the Waterworks' net position at June 30, 2013 and 2012 is shown below:

	2013	2012 (Restated)
Assets		
Current and restricted assets	\$ 5,200,093	\$ 4,767,391
Capital assets	<u>35,972,586</u>	<u>35,482,086</u>
Total assets	<u>\$ 41,172,679</u>	<u>\$ 40,249,477</u>
Liabilities		
Current liabilities	\$ 3,294,365	\$ 2,726,837
Long-term debt	<u>12,143,379</u>	<u>14,339,954</u>
	15,437,744	17,066,791
Net Position		
Invested in capital assets, net of related debt	21,937,809	19,923,132
Restricted funds	1,703,417	2,017,623
Unrestricted	<u>2,093,709</u>	<u>1,241,931</u>
Total liabilities and net position	<u>\$ 41,172,679</u>	<u>\$ 40,249,477</u>

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

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

Summary of Operations and Changes in Net Position

	2013	2012 (Restated)
Net operating revenues	\$ 7,280,156	\$ 6,986,677
Net operating expenses	<u>5,919,315</u>	<u>5,681,636</u>
Net operating income	<u>1,360,841</u>	<u>1,305,041</u>
Nonoperating income and expenses:		
Interest income	62,121	66,346
Interest expense	<u>(473,713)</u>	<u>(501,864)</u>
Net nonoperating expense	<u>(411,592)</u>	<u>(435,518)</u>
Capital contributions	<u>1,603,000</u>	<u>281,625</u>
Increase in net position	<u>\$ 2,552,249</u>	<u>\$ 1,151,148</u>

Revenues

A summary of revenues for the year ended June 30, 2013, and the amount and percentage of change in relation to prior year amounts, is as follows:

	2013 Amount	% of Total	Increase (Decrease) from Prior Year	% Increase (Decrease)
Operating				
Water sales	\$ 7,167,702	80.13	\$ 307,754	4.49
Miscellaneous charges	56,073	0.63	(18,309)	(24.61)
Service charges and penalties	<u>56,381</u>	<u>0.63</u>	<u>4,034</u>	7.71
Total operating	7,280,156	81.39	293,479	4.20
Nonoperating income				
Interest income	62,121	0.69	(4,225)	(6.37)
Capital contributions -				
State Revolving Loan	<u>1,603,000</u>	<u>17.92</u>	<u>1,321,375</u>	469.20
Total revenues	<u>\$ 8,945,277</u>	<u>100.00</u>	<u>\$ 1,610,629</u>	21.96

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

Expenses

A summary of expenses for the year ended June 30, 2013, and the amount and percentage of change in relation to prior year amounts, is as follows:

	2013 Amount	% of Total	Increase (Decrease) from Prior Year	% Increase (Decrease)
Operating				
Operating expenses	\$ 4,538,476	70.99	\$ 153,956	3.51
Depreciation	<u>1,380,839</u>	<u>21.60</u>	<u>83,723</u>	6.45
Total operating	5,919,315	92.59	237,679	4.18
Nonoperating expense				
Interest expense	<u>473,713</u>	<u>7.41</u>	<u>(28,151)</u>	(5.61)
Total expenses	<u>\$ 6,393,028</u>	<u>100.00</u>	<u>\$ 209,528</u>	3.39

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

Summary of Cash Flow Activities

The following shows a summary of the major sources and uses of cash and cash equivalents for the years ended June 30, 2013 and 2012. Cash equivalents are considered to be cash on hand, bank deposits and highly liquid investments with an original maturity of three months or less.

	2013	2012
Net cash provided by operating activities	\$ 2,758,613	\$ 2,478,470
Net cash provided (used) by investing activities	536,104	(432,762)
Net cash used by capital and related financing activities	<u>(2,186,119)</u>	<u>(2,256,789)</u>
Net increase (decrease) in cash and cash equivalents	1,108,598	(211,081)
Cash and cash equivalents, beginning of year	<u>1,844,283</u>	<u>2,055,364</u>
Cash and cash equivalents, end of year	<u>\$ 2,952,881</u>	<u>\$ 1,844,283</u>

Financial Statements

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

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

Long-term Debt

At June 30, 2013, the Waterworks had \$14,034,777 in debt outstanding. This debt is from refinancing of the 1995, 1996 and 2010 bonds in April 2013; 2008 debt of \$3.8 million for water filters; and \$1.6 million bonds issued in connection with the chlorine generation system construction project.

Capital Acquisitions and Construction Activities

At June 30, 2013, the Waterworks had \$54,360,911 in capital assets. Capital expenditures totaled \$1,956,678, a increase of 1% over 2012. A summary of projects follows:

Distribution System

- Purchase of Meters
- Purchase of Hydrants

Water Treatment Plant

- Filters
- Sludge System
- Controls
- VFD
- Prefilters
- Chlorine Generation System

Equipment

- Filters

Office Building

- Awning

Transportation

- 2013 Ford F-150

Mains

- 7th to 10th on Ridge Street
- 19th and 20th on Franklin Street
- 306 - 415 Hickory Terrace
- 2414 Plank Road
- 4th Street - 15th Street Grand Avenue

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

Economic Factors

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

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

For the fiscal year ending June 30, 2013, the Waterworks has already entered into the following capital improvement projects:

Mains

- 4th Street - 15th Street Grand Avenue

Water Plant

- Chlorine Generation System located at the water plant at 118 North Water Street.

Request for Information

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

**Keokuk Municipal Waterworks,
A Component Unit of the City of Keokuk
Statement of Net Position - Proprietary Fund
June 30, 2013**

Assets	
Current Assets	
Cash and cash equivalents	\$ 936,630
Certificates of deposit	25,145
Accrued interest receivable	14,967
Accounts receivable	732,617
Inventories	71,523
Prepaid expenses	<u>103,609</u>
Total current assets	<u>1,884,491</u>
Restricted Assets	
Cash and cash equivalents	2,016,251
Accounts receivable	258,496
Certificates of deposit	303,105
Guaranteed investment contracts	<u>737,750</u>
	<u>3,315,602</u>
Property, Plant and Equipment	
Property, plant and equipment, at cost	54,360,911
Less accumulated depreciation	<u>(18,388,325)</u>
	<u>35,972,586</u>
	<u>\$ 41,172,679</u>
Liabilities	
Current Liabilities	
Accounts payable	\$ 308,909
State sales tax payable	1,887
Accrued salaries and vacation	293,214
Accrued interest payable	82,752
Current portion long-term debt	1,891,398
Due to city - sewer and garbage charges	445,045
Consumer water meter deposits	175,422
Consumer sewer meter deposits	<u>95,738</u>
Total current liabilities	3,294,365
Long-term Debt, net of current portion	<u>12,143,379</u>
	<u>15,437,744</u>
Net Position	
Invested in capital assets, net of related debt	21,937,809
Restricted	
Sinking fund	427,738
Reserve fund	1,025,679
Improvement fund	250,000
Unrestricted	<u>2,093,709</u>
	<u>25,734,935</u>
	<u>\$ 41,172,679</u>

See notes to financial statements.

**Keokuk Municipal Waterworks,
A Component Unit of the City of Keokuk
Statement of Revenues, Expenses and Changes in Fund Net Position - Proprietary Fund
For the Year Ended June 30, 2013**

Operating Revenues	
Water sales	\$ 7,167,702
Miscellaneous charges	56,073
Service charges and penalties	<u>56,381</u>
Total operating revenues	<u>7,280,156</u>
Operating Expenses	
Operating expenses	4,538,476
Depreciation	<u>1,380,839</u>
Total operating expenses	<u>5,919,315</u>
Net operating income	<u>1,360,841</u>
Nonoperating income (expenses)	
Interest income	62,121
Interest expense	<u>(473,713)</u>
Total nonoperating expenses	<u>(411,592)</u>
	949,249
Capital contributions - State Revolving Loan	<u>1,603,000</u>
Change in net position	2,552,249
Net position, beginning of year, restated	<u>23,182,686</u>
Net position, end of year	<u>\$ 25,734,935</u>

See notes to financial statements.

**Keokuk Municipal Waterworks,
A Component Unit of the City of Keokuk
Statement of Cash Flows - Proprietary Fund
For the Year Ended June 30, 2013**

Cash Flows from Operating Activities	
Receipts from customers	\$ 7,171,315
Receipts from service charges and miscellaneous	111,495
Meter deposits received, net	(981)
Payments to suppliers	(3,191,477)
Payments to employees	(1,131,739)
Payments for interfund services	<u>(200,000)</u>
Net cash provided by operating activities	<u>2,758,613</u>
Cash Flows from Capital and Related Financing Activities	
Purchases of capital assets	(1,956,678)
Capital grant received	200,000
Principal payments on long-term debt	(11,206,000)
Principal borrowings on long-term debt	11,284,823
Interest payments on long-term debt	<u>(508,264)</u>
Net cash used by capital and related financing activities	<u>(2,186,119)</u>
Cash Flows from Investing Activities	
Purchases of certificates of deposit	(25,145)
Redemptions of certificates of deposit	480,720
Interest income	<u>80,529</u>
Net cash provided by investing activities	<u>536,104</u>
Net increase in cash and cash equivalents	1,108,598
Cash and cash equivalents, beginning of year	<u>1,844,283</u>
Cash and cash equivalents, end of year	<u>\$ 2,952,881</u>
Reconciliation of Operating Income to Net Cash Provided by Operating Activities	
Operating income	\$ 1,360,841
Adjustments to reconcile operating income to net cash provided by operating activities:	
Depreciation expense	1,380,839
Changes in assets and liabilities:	
Receivables, inventories and prepaids	1,913
Accounts payable and accrued expenses	<u>15,020</u>
Net cash provided by operating activities	<u>\$ 2,758,613</u>
Supplemental Disclosure of Noncash Capital and Related Financing Activities	
Equipment purchases financed through accounts payable	\$ 203,764
Capitalized interest on assets under construction	2,515
Long-term debt forgiveness	1,603,000

See notes to financial statements.

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

Note 1. Summary of Significant Accounting Policies

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

Reporting Entity

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

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

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

Measurement Focus, Basis of Accounting and Financial Statement Presentation

The financial statements of the Waterworks are prepared in accordance with accounting principles generally accepted in the United States of America. The Waterworks' reporting entity applies all relevant GASB pronouncements, except for GASB Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, which has not been implemented. The Waterworks has not determined the impact of this departure on the financial statements. During the year ended June 30, 2013, the Waterworks adopted GASB Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*, GASB Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position* and GASB Statement No. 65, *Items Previously Reported as Assets and Liabilities*.

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

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

Note 1. Summary of Significant Accounting Policies (continued)

The financial statements are accounted for using the flow of economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

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

Assets, Liabilities and Net Position

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

Cash and Cash Equivalents

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

Accounts Receivable

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

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

Restricted Assets

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

Inventories

Inventories, which consist of chemical supplies, are recognized at cost at the time they are purchased.

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

Note 1. Summary of Significant Accounting Policies (continued)

Property and Equipment

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

Buildings	10-40 years
Plant and tanks	5-100 years
Distribution system, meters and hydrants	15-80 years
Machinery and equipment	5-40 years

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

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

Compensated Absences

Waterworks employees accumulate a limited amount of earned but unused vacation and sick leave hours for subsequent use or for payment upon termination, retirement or death. The Waterworks' liability for accumulated vacation and sick leave has been computed based on rates in effect at June 30, 2013.

Budgets and Budgetary Accounting

The budgetary comparison and related disclosures are reported as Required Supplementary Information. During the year ended June 30, 2013, disbursements exceeded the amounts budgeted.

Use of Estimates

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

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

Note 2. Restricted Assets

Restricted assets consist of the following as of June 30, 2013:

	Cash and Cash Equivalents	Accounts Receivable	Certificates of Deposit	Guaranteed Investment Contract
Sewer, garbage and landfill	\$ 186,549	\$ 258,496	\$ -	\$ -
Consumer water meter deposits	175,422	-	-	-
Consumer sewer meter deposits	7,738	-	88,000	-
Sinking fund	427,738	-	-	-
Reserve fund	72,824	-	215,105	737,750
Improvement fund	250,000	-	-	-
General regulatory and system improvements	<u>895,980</u>	<u>-</u>	<u>-</u>	<u>-</u>
Total restricted assets	<u>\$ 2,016,251</u>	<u>\$ 258,496</u>	<u>\$ 303,105</u>	<u>\$ 737,750</u>

Note 3. Property and Equipment

Changes in property and equipment as June 30, 2013 consist of the following:

	Balance Beginning of year	Increases	Decreases	Balance End of year
Property and equipment not being depreciated:				
Land	\$ 461,766	\$ -	\$ -	\$ 461,766
Construction in progress	<u>106,637</u>	<u>1,584,006</u>	<u>(10,639)</u>	<u>1,680,004</u>
Total property and equipment not being depreciated	<u>568,403</u>	<u>1,584,006</u>	<u>(10,639)</u>	<u>2,141,770</u>
Property and equipment being depreciated/amortized:				
Building	469,717	4,391	-	474,108
Plant and tanks	44,779,115	98,722	(21,896)	44,855,941
Distribution system, meters and hydrants	5,871,673	173,435	(14,143)	6,030,965
Machinery and equipment	<u>855,191</u>	<u>21,424</u>	<u>(18,488)</u>	<u>858,127</u>
Total property and equipment being depreciated/amortized	<u>51,975,696</u>	<u>297,972</u>	<u>(54,527)</u>	<u>52,219,141</u>
Less accumulated depreciation/amortization for:				
Building	246,536	12,366	-	258,902
Plant and tanks	13,823,205	1,244,644	(21,896)	15,045,953
Distribution system, meters and hydrants	2,321,650	93,975	(14,143)	2,401,482
Machinery and equipment	<u>670,622</u>	<u>29,854</u>	<u>(18,488)</u>	<u>681,988</u>
Total accumulated depreciation/amortization	<u>17,062,013</u>	<u>1,380,839</u>	<u>(54,527)</u>	<u>18,388,325</u>
Total property and equipment, net	<u>\$ 35,482,086</u>	<u>\$ 501,139</u>	<u>\$ (10,639)</u>	<u>\$ 35,972,586</u>

For the year ended June 30, 2013, the Waterworks capitalized interest of \$2,515, for the interest costs incurred relating to the construction of the property.

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

Note 4. Pension and Retirement Benefits

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

Plan members are required to contribute 5.78% of their annual salary and the Waterworks is required to contribute 8.67% of annual covered payroll. Contribution requirements are established by State statute. The Waterworks' contribution to IPERS for the years ended June 30, 2013, 2012 and 2011 was \$96,381, \$85,404 and \$74,124, respectively, which was equal to the required contribution.

Note 5. Deposits

The Waterworks' deposits at June 30, 2013 were entirely covered by Federal depository insurance or by the state sinking fund in accordance with Chapter 12C of the Code of Iowa. This Chapter provides for additional assessments against the depositories to insure there will be no loss of public funds.

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

Note 6. Bonds and Long-Term Debt

On April 1, 2004, the Waterworks issued \$7,000,000 in Water Revenue Refunding Capital Loan Notes. The proceeds were used to advance refund \$6,650,000 of 1995 Water Revenue Capital Loan Notes on the call date of April 1, 2006. These notes mature semi-annually beginning October 1, 2006 through April 1, 2020, with interest rates from 1.90% to 4.55%. Notes maturing after April 1, 2013 may be called for redemption and paid before maturity on said date or any date thereafter at par plus accrued interest in whole or in part, in order of maturity. During the year ended June 30, 2013, the Waterworks called the notes for redemption through the issuance of the 2013B series revenue notes.

On January 27, 2005, the Waterworks issued \$4,505,000 in Water Revenue Refunding Capital Loan Notes. The proceeds were used to advance refund \$4,330,000 of 1996 Water Revenue Capital Loan Notes on the call date of April 1, 2006. These notes mature semi-annually beginning October 1, 2006 through April 1, 2020, with interest rates from 2.65% to 5.00%. Notes maturing after April 1, 2013 may be called for redemption and paid before maturity on said date or any date thereafter at par plus accrued interest in whole or in part, in order of maturity. During the year ended June 30, 2013, the Waterworks called the notes for redemption through the issuance of the 2013B series revenue notes.

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

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

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

On February 10, 2010, the Waterworks issued \$3,777,000 in Water Revenue Refunding Capital Loan Notes. The proceeds were used to fund the water tower construction project. These notes mature semi-annually beginning June 1, 2010 through June 1, 2031, with a 3.00% interest rate. During the year ended June 30, 2013, the Waterworks called the notes for redemption through the issuance of the 2013B series revenue notes.

On February 10, 2010, the Waterworks issued \$1,603,000 in Forgivable Loan Water Revenue Capital Loan Notes. The proceeds were used to fund the water tower construction project. During the year ended June 30, 2013, the Waterworks received the certificate of completion and the loan was forgiven. Accordingly, the Waterworks recognized capital contributions of \$1,603,000 for the year ended June 30, 2013.

On December 7, 2011, the Waterworks entered into an interim loan and disbursement agreement with Iowa Finance Authority for the planning and design phase of the Chlorine Generation System. This agreement matures December 7, 2014, with a zero interest rate. This loan was repaid with the issuance of the 2013A series revenue notes during the year ended June 30, 2013.

On March 27, 2013, the Waterworks issued \$10,000,000 in Water Revenue Refunding Capital Loan Notes. The Waterworks entered into an escrow agreement with Wells Fargo Bank, N.A. and deposited the proceeds from the refunding notes. The proceeds were used to advance refund 2004 Water Revenue Refunding Capital Loan Notes and 2005 Water Revenue Refunding Capital Loan Notes on the call date of April 1, 2013, and 2010 Water Revenue Capital Loan Notes. These notes mature semi-annually beginning October 1, 2013 through April 1, 2031, with interest rates from 1.85% to 3.10%. Notes maturing after April 1, 2019 may be called for redemption and paid before maturity on said date or any date thereafter at par plus accrued interest in whole or in part, in order of maturity. The notes were issued at a premium and the unamortized premium as of June 30, 2013 is \$37,419.

On April 12, 2013, the Waterworks issued \$1,600,000 in Water Revenue Capital Loan Notes. The Waterworks entered into an escrow agreement with Wells Fargo Bank, N.A., the trustee of the master trust of the Iowa Finance Authority, and deposited the proceeds from the notes. The proceeds are to be used to fund the Chlorine Generation System project. Upon completion of the project and receipt by the State of Iowa of a certification of completion from the Waterworks, \$480,000 of the outstanding debt will be forgiven. The remaining notes mature semi-annually beginning June 1, 2013 through June 1, 2032, with a 2.00% interest rate. As of June 30, 2013, the Waterworks had not received all of the notes proceeds and the certification of completion. Subsequent to June 30, 2013, the Waterworks received note proceeds of \$347,642 and obtained the certification of completion.

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

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

A summary of changes in long-term debt for the year ended June 30, 2013 is as follows:

	Balance Beginning of Year	Increases	Decreases	Balance End of Year	Due Within One Year
2004A Series Revenue notes	\$ 4,430,000	\$ -	\$ (4,430,000)	\$ -	\$ -
2005A Series Revenue notes	2,870,000	-	(2,870,000)	-	-
2008 Series Revenue notes	2,965,000	-	(220,000)	2,745,000	235,000
2010 Series Revenue notes	3,640,000	-	(3,640,000)	-	-
2010 Series Revenue notes	1,603,000	-	(1,603,000)	-	-
2013B Series Revenue notes	-	10,037,419	-	10,037,419	1,129,398
2013A Series Revenue notes	-	1,298,358	(46,000)	1,252,358	527,000
Interim Loan and Disbursement Agreement	50,954	56,319	(107,273)	-	-
Total Revenue notes	<u>\$ 15,558,954</u>	<u>\$ 11,392,096</u>	<u>\$ (12,916,273)</u>	<u>\$ 14,034,777</u>	<u>\$ 1,891,398</u>

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

Year Ending June 30,	\$3,800,000 Water Revenue Capital Loan Notes Series 2008		\$10,000,000 Water Revenue Refunding Capital Loan Notes Series 2013B		\$1,600,000 Water Revenue Capital Loan Notes Series 2013A		Total	
	Principal	Interest	Principal	Interest	Principal	Interest	Principal	Interest
2014	\$ 235,000	\$ 107,213	\$ 1,129,398	\$ 215,448	\$ 527,000	\$ 20,834	\$ 1,891,398	\$ 343,495
2015	240,000	99,018	1,154,398	190,580	48,000	17,973	1,442,398	307,571
2016	245,000	90,288	1,179,405	167,580	49,000	17,133	1,473,405	275,001
2017	255,000	80,911	1,199,393	144,080	50,000	16,275	1,504,393	241,266
2018	265,000	70,868	1,224,397	120,180	51,000	15,400	1,540,397	206,448
2019-2023	1,505,000	179,949	2,393,921	334,270	270,000	63,263	4,168,921	577,482
2024-2028	-	-	1,054,070	190,533	257,358	50,243	1,311,428	240,776
2029-2032	-	-	702,437	42,975	-	-	702,437	42,975
	<u>\$ 2,745,000</u>	<u>\$ 628,247</u>	<u>\$10,037,419</u>	<u>\$ 1,405,646</u>	<u>\$ 1,252,358</u>	<u>\$ 201,121</u>	<u>\$14,034,777</u>	<u>\$ 2,235,014</u>

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

A. Rate Covenant

The Waterworks covenants to continue in effect rates for services rendered to be sufficient to produce gross revenues adequate to pay expenses of operation and maintenance and to maintain a balance of net revenues equal to at least 125% of the principal and interest on the 2008, 2013A and 2013B Series notes as they become due.

B. Sinking Fund

For the 2008, 2013A and 2013B Series notes, the Sinking Fund requirement is an amount on deposit equal to the monthly amount of the next principal and interest payment.

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

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

C. Reserve Fund

For the 2008, 2013A and 2013B Series notes, the Reserve Fund requirement is an amount equal to the lesser of (a) the maximum principal and interest coming due on the notes in any fiscal year, (b) 10% of the stated principal of the notes, or (c) 125% of the average annual debt service on the notes. Amounts on deposit in the Reserve Fund shall be solely for the purpose of paying principal and interest on the notes. The Reserve Fund is to be valued on April 1st of each year and whenever the amount on deposit is less than the Reserve Fund requirement. The Waterworks is required to make monthly deposits in an amount equal to 25% of the amount required to be deposited in the Sinking Fund until the Reserve Fund has been restored.

D. Improvement Fund

For the 2008 and 2013A Series notes, the Improvement Fund requirement is \$250,000. Money on deposit in the Improvement Fund shall be used for the purpose of paying principal and interest on the notes when there are insufficient balances in the Sinking Fund and Reserve Fund. Funds may also be used to pay the costs of extraordinary maintenance expenses or repairs, renewals and replacement. Whenever it shall become necessary to use the money on deposit in the Improvement Fund, the Waterworks shall deposit \$21,000 per month until the amount on deposit is restored to \$250,000. There is no Improvement Fund requirement for the 2013B Series note.

Note 7. Risk Management

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

Note 8. Major Customers

Water sales to one major customer totaled \$5,109,661 for the year ended June 30, 2013, representing approximately 70% of the total operating revenue for the year. At June 30, 2013, the amount due from this customer was \$462,895, which is included in accounts receivable.

Note 9. Related Party Transactions

During the year ended June 30, 2013, the Waterworks had business transactions with one employee amounting to \$1,550.

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

Note 10. Related Organization

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

The Waterworks provides billing service for sewer and garbage for the City of Keokuk and collects fees for these services. Total fees collected for the City were \$2,723,089 and billing service fees received by Waterworks amounted to \$22,380 for the year ending June 30, 2013. Amounts due to the City as of June 30, 2013 were \$445,045 for sewer and garbage charges and \$1,939 for vehicle cost reimbursement.

For the year ended June 30, 2013, the Waterworks made a payment in lieu of taxes to the City of Keokuk for \$200,000.

Note 11. Subsequent Events

The Waterworks performed an evaluation of subsequent events through January 20, 2014, which is the date the financial statements were issued. The Waterworks borrowed an additional \$347,642 from the 2013A Water Revenue Capital Loan Notes with Iowa Finance Authority. The Waterworks also obtained its project's certification of completion and was notified of the notes debt forgiveness of \$480,000 subsequent to year end.

Note 12. Prior Period Adjustment

During the year ended June 30, 2013, the following adjustments were recorded to correct errors identified in the current year:

- Disposal of sludge facility equipment where the physical equipment was disposed prior to June 30, 2012.
- Value of chemical inventories used in the water purification process.

Furthermore, net position was adjusted for the adoption of GASB No. 65, which resulted in the elimination of prepaid debt issuance costs. The cumulative effect of the change on net assets as of June 30, 2013 is a decrease of \$209,782.

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

Note 12. Prior Period Adjustment (continued)

The financial statements for the year ended June 30, 2013 have been restated as follows:

	Invested in capital assets, net of related debt	Unrestricted	Net Position
	<u> </u>	<u> </u>	<u> </u>
As previously reported, June 30, 2012	\$ 20,101,785	\$ 1,273,060	\$23,392,468
Correction of fixed asset disposal	(178,653)	-	(178,653)
Correction of inventory	-	60,331	60,331
Accounting adjustment GASB No. 65	<u>-</u>	<u>(91,460)</u>	<u>(91,460)</u>
As restated	<u>\$ 19,923,132</u>	<u>\$ 1,241,931</u>	<u>\$23,182,686</u>

The Statement of Revenues, Expenses and Changes in Fund Net Position - Proprietary Fund for the year ended June 30, 2012 proforma is as follows:

	Change in Net Position
	<u> </u>
As previously reported, June 30, 2012	\$ 1,089,085
Correction of fixed asset disposal	10,208
Correction of inventory	9,125
Accounting adjustment GASB No. 65	<u>42,730</u>
As proforma	<u>\$ 1,151,148</u>

**Keokuk Municipal Waterworks,
A Component Unit of the City of Keokuk
Required Supplementary Information
Comparison of Cash Receipts and Disbursements - Actual to Budget
For the Year Ended June 30, 2013**

	<u>Actual</u>	<u>Budgeted Amounts - Final</u>	<u>Budgeted Amounts - Original</u>	<u>Variance: Favorable (Unfavorable)</u>
Receipts	\$ 19,302,756	\$ 8,857,741	\$ 8,857,741	\$ 10,445,015
Disbursements	<u>18,194,158</u>	<u>8,857,741</u>	<u>8,857,741</u>	<u>(9,336,417)</u>
Changes in cash and cash equivalents	<u>\$ 1,108,598</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 1,108,598</u>

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

Changes in cash and cash equivalents, as presented above	\$ 1,108,598
Add: Cash expenditures for property, plant and equipment capitalized under GAAP	1,956,678
Add: Cash expenditures for long-term debt interest payments capitalized under GAAP	2,515
Add: Cash expenditures for long-term debt principal payments	11,313,273
Add: Change in accrued interest payable	32,036
Add: Cash expenditure for purchases of certificates of deposit	25,145
Add: Long-term debt forgiveness	1,603,000
Subtract: Cash receipts from redemption of certificates of deposit	(480,720)
Subtract: Change in accounts receivable, inventory and prepaids	(1,913)
Subtract: Change in accrued interest receivable	(18,408)
Subtract: Change in grant receivable	(200,000)
Subtract: Change in accounts payable and accrued expenses	(15,020)
Subtract: Depreciation expense	(1,380,839)
Subtract: Cash proceeds for long-term debt issuance	<u>(11,392,096)</u>
Changes in net position, as presented in the Statement of Revenues, Expenses and Changes in Fund Net Position	<u>\$ 2,552,249</u>

See accompanying independent auditor's report.

Keokuk Municipal Waterworks
A Component Unit of the City of Keokuk
Required Supplementary Information
Notes to Required Supplementary Information - Actual to Budget
Year Ended June 30, 2013

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

Formal and legal budgetary control is based upon classes of disbursements known as functions, not by fund or category type. The Waterworks' disbursements are budgeted in the business type activities function. The Waterworks' budget is reflected in the original and final budgeted amounts. The Waterworks' budget was not amended during the year.

During the year ended June 30, 2013, disbursements exceeded the amounts budgeted due to the 2013 debt refinance.

See accompanying independent auditor's report.

**Keokuk Municipal Waterworks,
A Component Unit of the City of Keokuk
Schedule of Changes in Assets Restricted
for Landfill, Sewer and Garbage Charges
For the Year Ended June 30, 2013**

	<u>Landfill Charges</u>	<u>Sewer Charges</u>	<u>Garbage Charges</u>	<u>Total</u>
Restricted asset balance, June 30, 2012	\$ -	\$ 323,836	\$ 141,419	\$ 465,255
Fees				
Landfill service charges	45	-	-	45
Sewer service charges	-	2,024,007	-	2,024,007
Garbage service charges	-	-	699,082	699,082
Less billing adjustments	<u>-</u>	<u>(14,504)</u>	<u>(5,561)</u>	<u>(20,065)</u>
	<u>45</u>	<u>2,009,503</u>	<u>693,521</u>	<u>2,703,069</u>
Expenditures				
To the City of Keokuk	<u>(45)</u>	<u>(2,030,587)</u>	<u>(692,647)</u>	<u>(2,723,279)</u>
	<u>(45)</u>	<u>(2,030,587)</u>	<u>(692,647)</u>	<u>(2,723,279)</u>
Restricted asset balance, June 30, 2013	<u>\$ -</u>	<u>\$ 302,752</u>	<u>\$ 142,293</u>	<u>\$ 445,045</u>
Restricted asset balance is composed of the following:				
Cash and cash equivalents	\$ -	\$ 137,482	\$ 49,067	\$ 186,549
Accounts receivable	<u>-</u>	<u>165,270</u>	<u>93,226</u>	<u>258,496</u>
	<u>\$ -</u>	<u>\$ 302,752</u>	<u>\$ 142,293</u>	<u>\$ 445,045</u>

See accompanying independent auditor's report.

**Keokuk Municipal Waterworks,
A Component Unit of the City of Keokuk
Schedule of Changes in Assets Restricted for
Water Revenue Capital Loan Notes Debt Service
For the Year Ended June 30, 2013**

	Water Revenue Notes Sinking Fund	Water Revenue Notes Reserve Fund	Water Revenue Notes Improvement Fund	Total
Restricted asset balance, June 30, 2012	\$ <u>332,469</u>	\$ <u>1,433,575</u>	\$ <u>251,579</u>	\$ <u>2,017,623</u>
Receipts				
Transfers from (to) operations	1,809,533	(407,896)	(1,579)	1,400,058
Transfers from bond proceeds	<u>10,000,000</u>	<u>-</u>	<u>-</u>	<u>10,000,000</u>
	<u>11,809,533</u>	<u>(407,896)</u>	<u>(1,579)</u>	<u>11,400,058</u>
Expenditures				
Note principal payments	(11,206,000)	-	-	(11,206,000)
Note interest payments	<u>(508,264)</u>	<u>-</u>	<u>-</u>	<u>(508,264)</u>
	<u>(11,714,264)</u>	<u>-</u>	<u>-</u>	<u>(11,714,264)</u>
Restricted asset balance, June 30, 2013	\$ <u>427,738</u>	\$ <u>1,025,679</u>	\$ <u>250,000</u>	\$ <u>1,703,417</u>

See accompanying independent auditor's report.

Keokuk Municipal Waterworks
Schedule of Expenditures of Federal Awards
June 30, 2013

Federal Agency/Pass-Through Agency Program - Grant Title	CFDA Number	Grantor Program Number	Program Disbursements
U.S. Environmental Protection Agency programs: Pass-through programs from Iowa Finance Authority Capitalization Grants for Drinking Water State Revolving Loan Funds	66.468*	FS-56-11-DWSRF-019	\$ <u>943,499</u>
Total			\$ <u>943,499</u>

* Major Program

Basis of Presentation - The Schedule of Expenditures of Federal Awards includes the federal grant activity of the Keokuk Municipal Waterworks and is presented on the accrual basis. The information on 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 this schedule may differ from amounts presented in, or used in the preparation of, the basic financial statements.



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

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

We have audited 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, the financial statements of the proprietary fund of Keokuk Municipal Waterworks (Waterworks), A Component Unit of the City of Keokuk, as of and for the year ended June 30, 2013, and the related notes to the financial statements, which collectively comprise the Waterworks' basic financial statements, and have issued our report thereon dated January 20, 2014.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Waterworks' internal control over financial reporting to determine the audit procedures 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 the Waterworks' internal control. Accordingly, we do not express an opinion on the effectiveness of the Waterworks' internal control over financial reporting.

Our consideration of internal control was for the limited purpose described in the preceding paragraph 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. However, as described in the accompanying schedule of findings and questioned costs, we identified a deficiency in internal control we consider to be a material weakness.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect and correct misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility a material misstatement of the Waterworks' financial statements will not be prevented or detected and corrected on a timely basis. We consider the deficiencies in internal control described in Part II of the accompanying schedule of findings and questioned costs as item II-A-13 to be a material weakness.

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

Compliance and Other Matters

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

Waterworks' Responses to Findings

The Waterworks' responses to the findings identified in our audit are described in the accompanying schedule of findings and questioned costs. The Waterworks' responses were not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on them.

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

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

CPA Associates PC

January 20, 2014



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**Independent Auditor's Report on Compliance
with Requirements That Could Have a Direct and Material Effect
on Each Major Program and on Internal Control Over Compliance in Accordance
with OMB Circular A-133**

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

Report on Compliance for Each Major Federal Program

We have audited Keokuk Municipal Waterworks' (Waterworks) compliance with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) Circular A-133 *Compliance Supplement* that could have a direct and material effect on the Waterworks' major federal program for the year ended June 30, 2013. The Waterworks' major federal program is identified in the summary of independent 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 grant agreements applicable to its federal program.

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for the Waterworks' major federal program 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 the Waterworks' compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

We believe our audit provides a reasonable basis for our opinion on compliance for the major federal program. However, our audit does not provide a legal determination of the Waterworks' compliance.

Opinion on Major Federal Program

In our opinion, the Waterworks complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on its major federal program for the year ended June 30, 2013.

Other Matters

The results of our auditing procedures disclosed an instance of noncompliance which is required to be reported in accordance with OMB Circular A-133 and is described as item II-A-13 in the accompanying Schedule of Findings and Questioned Costs. However, we did not identify any instances of noncompliance.

Report on Internal Control Over Compliance

The management of the Waterworks 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 the Waterworks' internal control over compliance with the types of requirements that could have a direct and material effect on a major federal program in order to determine the auditing procedures appropriate in the circumstances for the purpose of expressing our opinion on compliance for the 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 the Waterworks' internal control over compliance.

Our consideration of internal control over compliance was for the limited purpose described in the preceding paragraph 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. However, as discussed below, we identified a deficiency in internal control over compliance we considered to be a material weakness.

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 a combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility 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, yet important enough to merit attention by those charged with governance. We consider the deficiency in internal control over compliance described in the accompanying Schedule of Findings and Questioned Costs as item III-A-13 to be a material weakness.

The Waterworks' response to the internal control over compliance finding identified in our audit is reported in the accompanying schedule of findings and questioned costs. The Waterworks' 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.

Report on the Schedule of Expenditures of Federal Awards Required by OMB Circular A-133

We have audited the financial statements of the proprietary fund of the Waterworks as of and for the year ended June 30, 2013, and the related notes to the financial statements, which collectively comprise the Waterworks' basic financial statements. We issued our report dated January 20, 2014, which contained modified opinions on those financial statements. 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 is presented for purposes of additional analysis as required by OMB Circular A-133 and is not a required part of the basic financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the 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 financial statements as a whole.

CPA Associates PC

January 20, 2014

**Keokuk Municipal Waterworks,
A Component Unit of the City of Keokuk
Schedule of Findings and Questioned Costs
For the Year Ended June 30, 2013**

Part I: Summary of the Independent Auditor's Results

- a) A qualified opinion was issued on the financial statements.
- b) A material weakness in internal control over financial reporting was disclosed by the audit of the financial statements.
- c) The audit did not disclose any noncompliance that is material to the financial statements.
- d) A material weakness in internal control over major programs was disclosed by the audit of the financial statements.
- e) An unqualified opinion was issued on compliance with requirements applicable to the major program.
- f) The audit disclosed no audit findings required to be reported in accordance with Office of Management and Budget Circular A-133, Section .510(a).
- g) The major federal program is as follows:
 - CFDA Number 66.468 - Environmental Protection Agency - Capitalization Grants for Drinking Water State Revolving Loan Funds
- h) The dollar threshold used to distinguish between Type A and Type B programs was \$300,000.
- i) The Waterworks did not qualify as a low-risk auditee.

Part II: Findings Related to the Financial Statements

MATERIAL WEAKNESS

II-A-13 Segregation of Duties - One important aspect of the internal control structure is the segregation of duties among employees to prevent one individual employee from handling a transaction from its inception to its completion. Management has not separated incompatible activities of personnel, thereby creating risks related to the safeguarding of cash and the accuracy of the financial statements.

Recommendation - We realize that with a limited number of office employees, segregation of duties is difficult. However, the Board of Trustees and management should continue to provide oversight and direction based upon their direct knowledge of the Waterworks' operations and day-to-day contact with employees to control and safeguard assets.

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

Conclusion - Response accepted.

Instances of Noncompliance:

No matters were noted.

**Keokuk Municipal Waterworks,
A Component Unit of the City of Keokuk
Schedule of Findings and Questioned Costs
For the Year Ended June 30, 2013**

Part III: Findings Related to Federal Awards

MATERIAL WEAKNESS

- III-A-13 Segregation of Duties Over Federal Receipts - Keokuk Municipal Waterworks did not properly segregate collection, deposit and recordkeeping for receipts, including those related to federal programs. See item II-A-13.

Instances of Noncompliance:

No matters were noted.

Part IV: Other Findings Related to Required Statutory Reporting

- IV-A-13 Deposits and Investments - The Waterworks has adopted a written investment policy as required by Chapter 12B.10B of the Code of Iowa.

- IV-B-13 Travel Expense - No expenditures of Waterworks money for travel expenses of spouses of Waterworks members or employees were noted.

- IV-C-13 Board Minutes - No transactions were found that we believe should have been approved in the Waterworks minutes but were not.

- IV-D-13 Mileage Reimbursement - The Waterworks reimbursed employee mileage expenses based on an outdated Internal Revenue Service (IRS) reimbursement rate. The total impact of the outdated reimbursement rate was a overpayment to employees of \$31.16 for the year ended June 30, 2013.

Recommendation - The Waterworks should follow the current IRS mileage reimbursement rates when reimbursing employees for use of a personal vehicle for business trips.

Response - The Waterworks will follow recommended IRS reimbursement rates.

Conclusion - Response accepted.

- IV-E-13 Meal Reimbursement - The Waterworks Union Contract, Article 26, Section 5 states that employees required to work over a mealtime hour are allowed to be reimbursed for their meal, but only to the extent of the actual cost of the meal, not exceeding \$4.00 for breakfast, \$4.50 for lunch and \$5.00 for dinner. Certain reimbursements were noted that exceeded the allowable amount and totaled \$252.27 for the year ended June 30, 2013.

Recommendation - The Waterworks should follow policy when reimbursing employees for meal expenses and document the number of employees included if purchasing meals for more than one individual.

Response - The Waterworks will comply with the Union Contract regarding meal reimbursement.

Conclusion - Response accepted.

**Keokuk Municipal Waterworks,
A Component Unit of the City of Keokuk
Schedule of Findings and Questioned Costs
For the Year Ended June 30, 2013**

IV-F-13 Questionable Disbursements - Certain disbursements were noted that may not meet the requirements of public purpose as defined in the Attorney General's opinion dated April 25, 1979 since the public benefits to be derived have not been clearly documented. These disbursements are detailed as follows:

<u>Paid To</u>	<u>Purpose</u>	<u>Amount</u>
Hy-Vee	Food for recognition lunches	\$ 205.85
Walgreens	Soda for Christmas party	14.08
Dollar General	Food for Christmas party	6.50
The Hawkeye	Employee annual luncheon	239.42
Penny Hotop	Cookies for board meetings and lunches	306.94
YMCA	Membership dues	171.50
American Legion	Membership dues	35.00
Keokuk Chamber	Appreciation gifts	176.75
Willow Tree	Sympathy gifts	64.20

According to the opinion, it is possible for such disbursements to meet the test of serving a public purpose under certain circumstances, although such items are certainly subject to a deserved close scrutiny. The line between a proper and an improper purpose is very thin.

Recommendation - The Waterworks' Board of Trustees should determine and document the public purpose served by these disbursements before authorizing any further payments. If this practice is continued, the Waterworks should establish written policies and procedures, including the requirements for proper documentation.

Response - The Waterworks Board of Trustees will establish written policies and procedures in determining the public purpose of disbursements.

Conclusion - Response accepted.

IV-G-13 Certified Budget - Disbursements during the year ended June 30, 2013 exceeded budget amounts due to the refinance of the Waterworks' primary debt obligations.

Recommendation - The Waterworks should amend its budget as required by State of Iowa Code.

Response - The Waterworks' management accepts full responsibility for not recommending the budget be amended in the amount of ten million (\$10,000,000) dollars, due to refinancing of current debt. In the future, the Waterworks will amend the budget as required by the State of Iowa Code.

Conclusion - Response accepted.

**Keokuk Municipal Waterworks,
A Component Unit of the City of Keokuk
Schedule of Findings and Questioned Costs
For the Year Ended June 30, 2013**

IV-H-13 Business Transactions with Waterworks Officials and Employees - Business transactions between Waterworks officials or employees are detailed as follows:

<u>Name, Title, and Business Connection</u>	<u>Transactions</u>	<u>Amount</u>
Mike Haney, Employee	Mowing	\$ 1,550

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

IV-I-13 Revenue Bonds and Notes - No instances of noncompliance with the revenue bond and note resolutions were noted.

IV-J-13 Unclaimed Property - Chapter 556.11 of the Code of Iowa requires a public utility to report and remit obligations, including checks outstanding for more than one to two years, to the State Treasurer's office annually. The Waterworks did not remit these obligations as required.

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

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

Conclusion - Response accepted.

IV-K-13 Unsupported Expense Reimbursements - For the year ended June 30, 2013, the Waterworks' reimbursed employees for expenses in the amount of \$1,282.43 without obtaining independent supporting documentation (e.g. store receipt or invoice for dues).

Recommendation - The Waterworks should only reimburse employees when the proper documentation is submitted to validated the expenditure.

Response - The Waterworks Board of Trustees will establish written policies of procedures for all reimbursement to employees.

Conclusion - Response accepted.