



OFFICE OF AUDITOR OF STATE
STATE OF IOWA

David A. Vaudt, CPA
Auditor of State

State Capitol Building
Des Moines, Iowa 50319-0004

Telephone (515) 281-5834 Facsimile (515) 242-6134

NEWS RELEASE

FOR RELEASE

June 12, 2008

Contact: Andy Nielsen
515/281-5834

Auditor of State David A. Vaudt today released an audit report on the City of Castalia, Iowa.

The City has implemented new reporting standards for the year ended June 30, 2007, with significant changes in content and structure of the financial statements. The new financial statements now include a Statement of Activities and Net Assets which provides information about the activities of the City as a whole. Also included is Management's Discussion and Analysis of the City's financial statements.

The City's receipts totaled \$97,745 for the year ended June 30, 2007. The receipts included \$15,840 in property tax, \$16,511 from local option sales tax, \$50,663 from charges for service, \$10,105 from operating grants, contributions and restricted interest and \$4,626 from unrestricted interest on investments.

Disbursements for the year totaled \$77,593, and included \$24,453 for general government, \$9,865 for culture and recreation and \$6,625 for public works. Also, disbursements for business type activities totaled \$34,895.

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

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CITY OF CASTALIA

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

JUNE 30, 2007

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City of Castalia

Officials

<u>Name</u>	<u>Title</u>	<u>Term Expires</u>
Margaret Jones	Mayor	Jan 2008
Larry Brockway	Mayor Pro tem	Jan 2008
Joe Moellers (Appointed)	Council Member	Nov 2007
Wayne Corett	Council Member	Jan 2008
Kevin Smith	Council Member	(Resigned)
Dennis Wilkins	Council Member	Jan 2008
Jamie Smith	Council Member	Jan 2010
Chris Bodensteiner	Clerk	Indefinite
Matt Erickson	Attorney	Indefinite
Richard Zahasky	Attorney	Indefinite

City of Castalia



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Independent Auditor's Report

To the Honorable Mayor and
Members of the City Council:

We have audited the accompanying financial statements of the governmental activities, the business type activities, each major fund and the aggregate remaining fund information of the City of Castalia, Iowa, as of and for the year ended June 30, 2007, which collectively comprise the City's basic financial statements listed in the table of contents. These financial statements are the responsibility of the City of Castalia's management. Our responsibility is to express opinions on these financial statements based on our audit.

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

As described in Note 1, these financial statements were prepared on the basis of cash receipts and disbursements, which is a comprehensive basis of accounting other than U.S. generally accepted accounting principles. Also, as permitted by the Code of Iowa, the accounting records of the City have not been audited for all prior years. Accordingly, we were unable to satisfy ourselves as to the distribution by fund of the total fund balance at July 1, 2006.

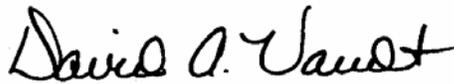
In our opinion, except for the effects of such adjustments, if any, as might have been determined to be necessary had we been able to verify the distribution by fund of the total fund balance at July 1, 2006, as discussed in the preceding paragraph, the financial statements referred to above present fairly, in all material respects, the respective cash basis financial position of the governmental activities, the business type activities, each major fund and the aggregate remaining fund information of the City of Castalia as of June 30, 2007, and the respective changes in cash basis financial position for the year then ended in conformity with the basis of accounting described in Note 1.

As described in Note 6, during the year ended June 30, 2007, the City adopted Governmental Accounting Standards Board Statement No. 34, Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments; Statement No. 37, Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments: Omnibus; Statement No. 38, Certain Financial Statement Note Disclosures; and Statement No. 41, Budgetary Comparison Schedule – Perspective Differences.

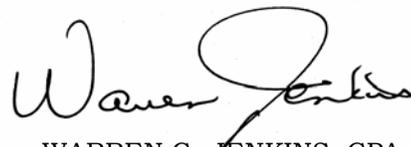
In accordance with Government Auditing Standards, we have also issued our report dated June 2, 2008 on our consideration of the City of Castalia's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and 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 compliance. That report is an integral part of an audit performed in accordance with Government Auditing Standards and should be considered in assessing the results of our audit.

Management's Discussion and Analysis and budgetary comparison information on pages 7 through 11 and 24 through 25 are not required parts of the basic financial statements, but are supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. We did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the City of Castalia's basic financial statements. Other supplementary information included in Schedules 1 and 2 are presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in our audit of the basic financial statements and, in our opinion, except for the effects of such adjustments, if any, as might have been determined to be necessary had we been able to verify the distribution by fund of the total fund balance at July 1, 2006, as discussed in the third paragraph, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.



DAVID A. VAUDT, CPA
Auditor of State



WARREN G. JENKINS, CPA
Chief Deputy Auditor of State

June 2, 2008

MANAGEMENT'S DISCUSSION AND ANALYSIS

The City of Castalia provides this Management's Discussion and Analysis of its financial statements. This narrative overview and analysis of the financial activities is for the fiscal year ended June 30, 2007. We encourage readers to consider this information in conjunction with the City's financial statements, which follow.

Because the City is implementing new reporting standards for this fiscal year with significant changes in content and structure, and since the City is not required to be audited annually, much of the information is not easily comparable to prior years. Comparative data has been provided if available.

2007 FINANCIAL HIGHLIGHTS

- The cash basis net assets of the City's governmental activities increased approximately \$6,000 due, in part, to an increase in local option sales tax collections from the prior year and a decrease in spending from the prior year.
- The cash basis net assets of the City's business type activities increased approximately \$14,000, primarily due to a decrease in disbursements from the prior year.

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 the City's financial activities.

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

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

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

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

Other Supplementary Information provides detailed information about the City's outstanding debt.

BASIS OF ACCOUNTING

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

REPORTING THE CITY'S FINANCIAL ACTIVITIES

Government-wide Financial Statement

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

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

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

- Governmental Activities include public safety, public works, culture and recreation, community and economic development and general government. Property tax and state and federal grants finance most of these activities.
- Business Type Activities include the water and sewer system. This activity is financed primarily by user fees and related charges.

Fund Financial Statements

The City has two kinds of funds:

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

The required financial statement for governmental funds is a statement of cash receipts, disbursements and changes in cash balances.

2) Proprietary funds account for the City's Enterprise Fund. Enterprise Funds are used to report business type activities. The City maintains Enterprise Funds to provide information for the water and sewer funds, which are major funds of the City.

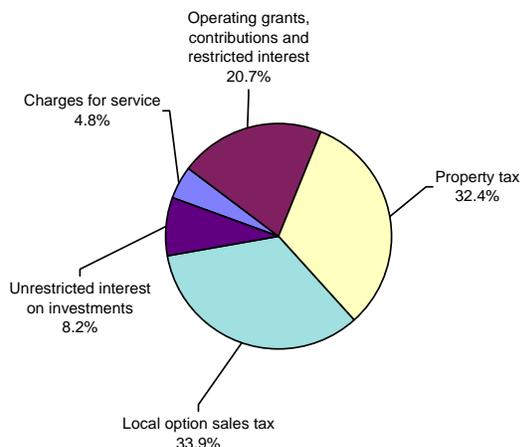
The required financial statement for proprietary funds is a statement of cash receipts, disbursements and changes in cash balances.

GOVERNMENT-WIDE FINANCIAL ANALYSIS

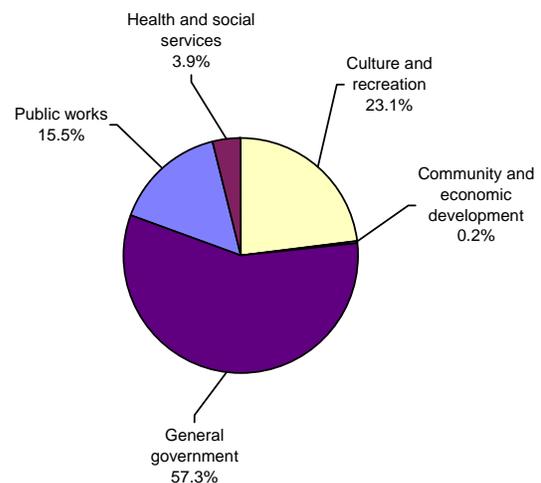
Net assets may serve over time as a useful indicator of financial position. The City's cash balance for governmental activities increased from a year ago, increasing from \$147,464 to \$153,594. The analysis that follows focuses on the changes in cash basis net assets of governmental activities.

Changes in Cash Basis Net Assets of Governmental Activities	
	Year ended June 30, 2007
Receipts:	
Program receipts:	
Charges for service	\$ 2,361
Operating grants, contributions and restricted interest	10,105
General receipts:	
Property tax	15,840
Local option sales tax	16,511
Unrestricted interest on investments	4,011
Total receipts	<u>48,828</u>
Disbursements:	
Public works	6,625
Health and social services	1,666
Culture and recreation	9,865
Community and economic development	89
General government	24,453
Total disbursements	<u>42,698</u>
Change in cash basis net assets	6,130
Cash basis net assets beginning of year	<u>147,464</u>
Cash basis net assets end of year	<u>\$ 153,594</u>

Receipts by Source



Disbursements by Function



The cost of all governmental activities this year was \$42,698. However, as shown in the Statement of Activities and Net Assets on pages 14-15, the amount taxpayers ultimately financed for these activities was only \$30,232 because some of the cost was paid by those directly benefited from the programs (\$2,361) or by other governments and organizations that subsidized certain programs with grants, contributions and restricted interest (\$10,105). The City paid for the remaining "public benefit" portion of governmental activities with approximately \$36,362 in tax (some of which could only be used for certain programs) and other receipts, such as interest and general entitlements.

<u>Changes in Cash Basis Net Assets of Business Type Activities</u>	
	Year ended June 30, 2007
Receipts:	
Program receipts:	
Charges for service:	
Water	\$ 20,640
Sewer	27,662
General receipts:	
Unrestricted interest on investments	615
Total receipts	<u>48,917</u>
Disbursements:	
Water	15,048
Sewer	19,847
Total disbursements	<u>34,895</u>
Change in cash basis net assets	14,022
Cash basis net assets beginning of year	<u>45,256</u>
Cash basis net assets end of year	<u>\$ 59,278</u>

Total business type activities cash basis net assets increased from a year ago, from \$45,256 to \$59,278. The overall increase is a result of a decrease in disbursements from the prior year.

INDIVIDUAL MAJOR GOVERNMENTAL FUND ANALYSIS

As the City of Castalia completed the year, its governmental funds reported a combined fund balance of \$153,594, an increase of approximately \$6,000 from last year's total of \$147,464. The following are the major reasons for the changes in fund balances of the major funds from the prior year.

- The General Fund cash balance increased 3%, or \$3,855, over the prior year to a year-end balance of \$131,025.
- The Special Revenue, Road Use Tax Fund cash balance increased \$2,393 to a balance of \$22,542 at the fiscal year end, due in part to less road work completed than was planned.

INDIVIDUAL MAJOR BUSINESS TYPE FUND ANALYSIS

- The Water Fund cash balance increased \$5,592 to \$6,033. Disbursements decreased, due in part to water line work completed during fiscal year 2006.
- The Sewer Fund cash balance increased \$8,430 to a year-end balance of \$53,245. This increase was due primarily to a decrease in disbursements during the current year due to the sewer line extension project completed during fiscal year 2006.

BUDGETARY HIGHLIGHTS

During the year ended June 30, 2007, the City did not amend its budget.

The City's receipts were \$40,324 more than budgeted. This was due, in part, to the City collecting more than was budgeted for local option sales tax and water and sewer charges for service.

Total disbursements were \$37,593 more than budgeted. This was primarily due to the fact the City did not budget business type activities for the fiscal year ended June 30, 2007.

DEBT ADMINISTRATION

At June 30, 2007, the City had sewer revenue notes of \$250,790 outstanding.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGET AND RATES

The City of Castalia's elected officials considered many factors when setting the fiscal year 2008 budget, tax rates and fees charged for the City's utilities. Over 30% of the houses have people living on fixed incomes. We may need to consider raising future water rates if repairs are necessary to the City's water system. In addition, we collect a local option sales tax which the City is able to use for any lawful purpose the City Council deems necessary. All of these factors were taken into account when planning the fiscal year 2008 budget.

CONTACTING THE CITY'S FINANCIAL MANAGEMENT

This financial report is designed to provide our citizens, taxpayers, customers and creditors with a general overview of the City's finances and to show the City's accountability for the money it receives. If you have questions about this report or need additional financial information, contact Chris Bodensteiner, City Clerk, 1518 Centennial Road, Ossian, IA 52161-8006.

City of Castalia

Basic Financial Statements

City of Castalia

Statement of Activities and Net Assets – Cash Basis

As of and for the year ended June 30, 2007

	Disbursements	Program Receipts	
		Charges for Service	Operating Grants, Contributions and Restricted Interest
Functions/Programs:			
Governmental activities:			
Public safety	\$ -	40	-
Public works	6,625	-	9,018
Health and social services	1,666	-	-
Culture and recreation	9,865	-	1,087
Community and economic development	89	-	-
General government	24,453	2,321	-
Total governmental activities	42,698	2,361	10,105
Business type activities:			
Water	15,048	20,640	-
Sewer	19,847	27,662	-
Total business type activities	34,895	48,302	-
Total	\$ 77,593	50,663	10,105
General Receipts:			
Property and other city tax levied for general purposes			
Local option sales tax			
Unrestricted interest on investments			
Total general receipts			
Change in cash basis net assets			
Cash basis net assets beginning of year			
Cash basis net assets end of year			
Cash Basis Net Assets			
Restricted:			
Streets			
Debt service			
Other purposes			
Unrestricted			
Total cash basis net assets			

See notes to financial statements.

Net (Disbursements) Receipts and Changes in Cash Basis Net Assets		
Governmental Activities	Business Type Activities	Total
40	-	40
2,393	-	2,393
(1,666)	-	(1,666)
(8,778)	-	(8,778)
(89)	-	(89)
(22,132)	-	(22,132)
(30,232)	-	(30,232)
-	5,592	5,592
-	7,815	7,815
-	13,407	13,407
(30,232)	13,407	(16,825)
15,840	-	15,840
16,511	-	16,511
4,011	615	4,626
36,362	615	36,977
6,130	14,022	20,152
147,464	45,256	192,720
\$ 153,594	59,278	212,872
\$ 22,542	-	22,542
-	16,376	16,376
27	-	27
131,025	42,902	173,927
\$ 153,594	59,278	212,872

Exhibit B

City of Castalia

Statement of Cash Receipts, Disbursements
and Changes in Cash Balances
Governmental Funds

As of and for the year ended June 30, 2007

	Special Revenue			Total
	General	Road Use Tax	Nonmajor Activity	
Receipts:				
Property tax	\$ 15,840	-	-	15,840
Local option sales tax	16,511	-	-	16,511
Licenses and permits	505	-	-	505
Use of money and property	4,100	-	1	4,101
Intergovernmental	-	9,018	-	9,018
Miscellaneous	2,223	-	630	2,853
Total receipts	39,179	9,018	631	48,828
Disbursements:				
Operating:				
Public works	-	6,625	-	6,625
Health and social services	1,666	-	-	1,666
Culture and recreation	9,116	-	749	9,865
Community and economic development	89	-	-	89
General government	24,453	-	-	24,453
Total disbursements	35,324	6,625	749	42,698
Excess (deficiency) of receipts over (under) disbursements	3,855	2,393	(118)	6,130
Cash balances beginning of year	127,170	20,149	145	147,464
Cash balances end of year	\$ 131,025	22,542	27	153,594
Cash Basis Fund Balances				
Unreserved:				
General fund	\$ 131,025	-	-	131,025
Special revenue funds	-	22,542	27	22,569
Total cash basis fund balances	\$ 131,025	22,542	27	153,594

See notes to financial statements.

City of Castalia

Statement of Cash Receipts, Disbursements
and Changes in Cash Balances
Proprietary Funds

As of and for the year ended June 30, 2007

	Enterprise		
	Water	Sewer	Total
Operating receipts:			
Charges for service	\$ 20,640	27,662	48,302
Operating disbursements:			
Business type activities	15,048	5,898	20,946
Excess of operating receipts over operating disbursements	5,592	21,764	27,356
Non-operating receipts (disbursements):			
Interest on investments	-	615	615
Debt service	-	(13,949)	(13,949)
Total non-operating receipts (disbursements)	-	(13,334)	(13,334)
Excess of receipts over disbursements	5,592	8,430	14,022
Cash balances beginning of year	441	44,815	45,256
Cash balances end of year	\$ 6,033	53,245	59,278
Cash Basis Fund Balances			
Reserved for debt service	\$ -	16,376	16,376
Unreserved	6,033	36,869	42,902
Total cash basis fund balances	\$ 6,033	53,245	59,278

See notes to financial statements.

City of Castalia

Notes to Financial Statements

June 30, 2007

(1) Summary of Significant Accounting Policies

The City of Castalia is a political subdivision of the State of Iowa located in Winneshiek County. It was first incorporated in 1903 and operates under the Home Rule provisions of the Constitution of Iowa. The City operates under the Mayor-Council form of government with the Mayor and Council Members elected on a non-partisan basis. The City provides numerous services to citizens, including public safety, public works, culture and recreation, community and economic development and general government services. The City also provides water and sewer utilities for its citizens.

A. Reporting Entity

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

Jointly Governed Organizations

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

B. Basis of Presentation

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

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

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

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

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

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

The City reports the following major governmental funds:

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

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

The City reports the following major proprietary funds:

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

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

C. Measurement Focus and Basis of Accounting

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

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

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

D. Budgets and Budgetary Accounting

The budgetary comparison and related disclosures are reported as Required Supplementary Information. During the year ended June 30, 2007, disbursements exceeded the amounts budgeted in the health and social services, culture and recreation, general government and business-type activities functions.

(2) Cash and Pooled Investments

The City's deposits in banks at June 30, 2007 were entirely covered by federal depository insurance or by the State Sinking Fund in accordance with Chapter 12C of the Code of Iowa. This chapter provides for additional assessments against the depositories to insure there will be no loss of public funds.

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

The City had no investments meeting the disclosure requirements of Governmental Accounting Standards Board Statement Number 3, as amended by Statement No. 40.

(3) Notes Payable

Annual debt service requirements to maturity for sewer revenue notes are as follows:

Year Ending June 30,	Principal	Interest	Total
2008	\$ 3,290	10,659	13,949
2009	3,430	10,519	13,949
2010	3,576	10,373	13,949
2011	3,728	10,221	13,949
2012	3,886	10,062	13,948
2013-2017	22,055	47,690	69,745
2018-2022	27,157	42,588	69,745
2023-2027	33,439	36,305	69,744
2028-2032	41,176	28,569	69,745
2033-2037	50,702	19,043	69,745
2038-2042	58,351	7,732	66,083
Total	\$ 250,790	233,761	484,551

The resolution providing for the issuance of the sewer revenue notes includes the following provisions.

- (a) The notes will only be redeemed from future earnings of the enterprise activity and the note holders hold a lien on the future earnings of the funds.
- (b) Sufficient monthly transfers shall be made to a sewer revenue note sinking account within the Enterprise Funds for the purpose of making the note principal and interest payments when due.
- (c) Additional monthly transfers of \$117 shall be made to a sewer revenue reserve account until a balance of \$13,949 has been accumulated. Funds may be used to pay principal and interest when and if funds are not available in the sinking account. This account is fully funded as of June 30, 2007.

(4) Pension and Retirement Benefits

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

Most regular plan members are required to contribute 3.70% of their annual covered salary and the City is required to contribute 5.75% of covered salary. Contribution requirements are established by state statute. The City's contribution to IPERS for the year ended June 30, 2007 was \$735, equal to the required contribution for the year.

(5) Risk Management

The city is a member in the Iowa Communities Assurance Pool, as allowed by Chapter 670.7 of the Code of Iowa. The Iowa communities Assurance Pool (Pool) is a local government risk-sharing pool whose 556 members include various governmental entities throughout the State of Iowa. The Pool was formed in August 1986 for the purpose of managing and funding third-party liability claims against its members. The Pool provides coverage and protection in the following categories: general liability, automobile liability, automobile physical damage, public officials liability, police professional liability, property, inland marine, and boiler/machinery. There have been no reductions in insurance coverage from prior years.

Each member's annual casualty contributions to the Pool fund current operations and provide capital. Annual operating contributions are those amounts necessary to fund, on a cash basis, the Pool's general and administrative expenses, claims, claims expenses and reinsurance expenses due and payable in the current year, plus all or any portion of any deficiency in capital. Capital contributions are made during the first six years of membership and are maintained to equal 300 percent of the total current members' basis rates or to comply with the requirements of any applicable regulatory authority having jurisdiction over the Pool.

The Pool also provides property coverage. Members who elect such coverage make annual operating contributions which are necessary to fund, on a cash basis, the Pool's general and administrative expenses and reinsurance premiums, all of which are due and payable in the current year, plus all or any portion of any deficiency in

capital. Any year-end operating surplus is transferred to capital. Deficiencies in operations are offset by transfers from capital and, if insufficient, by the subsequent year's members contributions.

The City's property and casualty contributions to the risk pool are recorded as disbursements from its operating funds at the time of payment to the risk pool. The City's contributions to the Pool for the year ended June 30, 2007 were \$1,971.

The Pool uses reinsurance and excess risk-sharing agreements to reduce its exposure to large losses. The Pool retains general, automobile, police professional, and public officials' liability risks up to \$350,000 per claim. Claims exceeding \$350,000 are reinsured in an amount not to exceed \$2,650,000 per claim and \$5,000,000 in aggregate per year. For members requiring specific coverage from \$3,000,000 to \$10,000,000, such excess coverage is also reinsured. Property and automobile physical damage risks are retained by the Pool up to \$100,000 each occurrence, each location, with excess coverage reinsured on an individual-member basis.

The Pool's intergovernmental contract with its members provides that in the event a casualty claim or series of claims exceeds the amount of risk-sharing protection provided by the member's risk-sharing certificate, or in the event a series of casualty claims exhaust total members' equity plus any reinsurance and any excess risk-sharing, then payment of such claims shall be the obligations of the respective individual member. As of June 30, 2007, settled claims have not exceeded the risk pool or reinsurance coverage since the pool's inception.

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

(6) Accounting Change

Governmental Accounting Standards Board Statement No. 34, Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments; Statement No. 37, Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments: Omnibus; Statement No. 38, Certain Financial Statement Note Disclosures, and Statement No. 41, Budgetary Comparison Schedule – Perspective Differences, were implemented for the year ended June 30, 2007. The statements create new basic financial statements for reporting the City's financial activities. The financial statements now include a government-wide financial statement and fund financial statements which present information for individual major funds rather than by fund type. Nonmajor funds are presented in total in one column.

Implementation of these standards had no effect on the beginning balances of the City.

Required Supplementary Information

City of Castalia

Budgetary Comparison Schedule
of Receipts, Disbursements, and Changes in Balances -
Budget and Actual (Cash Basis) – All Governmental Funds and Proprietary Funds

Required Supplementary Information

Year ended June 30, 2007

	Governmental Funds Actual	Proprietary Funds Actual	Total	Budgeted Amounts Original/ Final	Final to Total Variance
Receipts:					
Property tax	\$ 15,840	-	15,840	14,949	891
Other city tax	16,511	-	16,511	492	16,019
Licenses and permits	505	-	505	465	40
Use of money and property	4,101	615	4,716	1,350	3,366
Intergovernmental	9,018	-	9,018	14,665	(5,647)
Charges for service	-	48,302	48,302	25,000	23,302
Miscellaneous	2,853	-	2,853	500	2,353
Total receipts	48,828	48,917	97,745	57,421	40,324
Disbursements:					
Public safety	-	-	-	350	350
Public works	6,625	-	6,625	12,000	5,375
Health and social services	1,666	-	1,666	450	(1,216)
Culture and recreation	9,865	-	9,865	5,000	(4,865)
Community and economic development	89	-	89	600	511
General government	24,453	-	24,453	21,600	(2,853)
Business type activities	-	34,895	34,895	-	(34,895)
Total disbursements	42,698	34,895	77,593	40,000	(37,593)
Excess (deficiency) of receipts over (under) disbursements	6,130	14,022	20,152	17,421	2,731
Balances beginning of year	147,464	45,256	192,720	236,347	(43,627)
Balances end of year	\$ 153,594	59,278	212,872	253,768	(40,896)

See accompanying independent auditor's report.

City of Castalia

Notes to Required Supplementary Information – Budgetary Reporting

June 30, 2007

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

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

Formal and legal budgetary control is based upon ten major classes of disbursements known as functions, not by fund. These ten functions are: public safety, public works, health and social services, culture and recreation, community and economic development, general government, debt service, capital projects, business type activities and non-program. Function disbursements required to be budgeted include disbursements for the General Fund, the Special Revenue Funds and the Proprietary Funds. Although the budget document presents function disbursements by fund, the legal level of control is at the aggregated function level, not by fund. There were no budget amendments during the fiscal year.

During the year ended June 30, 2007, disbursements exceeded the amounts budgeted in the health and social services, culture and recreation, general government and business type activities functions.

City of Castalia

Other Supplementary Information

City of Castalia
Schedule of Indebtedness
Year ended June 30, 2007

Obligation	Date of Issue	Interest Rates	Amount Originally Issued
Revenue notes: Sewer	Jul 1, 2002	4.25%	\$ 266,100

See accompanying independent auditor's report.

Balance Beginning of Year	Issued During Year	Redeemed During Year	Balance End of Year	Interest Paid
253,946	-	3,156	250,790	10,793

Schedule 2

City of Castalia

Note Maturities

June 30, 2007

Year Ending June 30,	Revenue Notes	
	Sewer	
	Issued Jul 1, 2002	
	Interest Rates	Amount
2008	4.25%	\$ 3,290
2009	4.25	3,430
2010	4.25	3,576
2011	4.25	3,728
2012	4.25	3,886
2013	4.25	4,052
2014	4.25	4,224
2015	4.25	4,403
2016	4.25	4,590
2017	4.25	4,786
2018	4.25	4,989
2019	4.25	5,201
2020	4.25	5,422
2021	4.25	5,652
2022	4.25	5,893
2023	4.25	6,143
2024	4.25	6,404
2025	4.25	6,676
2026	4.25	6,960
2027	4.25	7,256
2028	4.25	7,564
2029	4.25	7,886
2030	4.25	8,221
2031	4.25	8,570
2032	4.25	8,935
2033	4.25	9,314
2034	4.25	9,710
2035	4.25	10,123
2036	4.25	10,553
2037	4.25	11,002
2038	4.25	11,470
2039	4.25	11,957
2040	4.25	12,465
2041	4.25	12,995
2042	4.25	9,464
Total		<u>\$ 250,790</u>

See accompanying independent auditor's report.



OFFICE OF AUDITOR OF STATE
STATE OF IOWA

David A. Vaudt, CPA
Auditor of State

State Capitol Building
Des Moines, Iowa 50319-0004

Telephone (515) 281-5834 Facsimile (515) 242-6134

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

To the Honorable Mayor and
Members of the City Council:

We have audited the accompanying financial statements of the governmental activities, the business type activities, each major fund and the aggregate remaining fund information of the City of Castalia, Iowa, as of and for the year ended June 30, 2007, which collectively comprise the City's basic financial statements listed in the table of contents, and have issued our report thereon dated June 2, 2008. Our report on the financial statements, which were prepared in conformity with an other comprehensive basis of accounting, expressed qualified opinions since we were unable to satisfy ourselves as to the distribution by fund of the total fund balance at July 1, 2006. Except as noted in the Independent Auditor's Report, we conducted our audit in accordance with U.S. generally accepted auditing standards and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

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

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed below, we identified certain deficiencies in internal control over financial reporting that we consider to be significant deficiencies, including deficiencies we consider to be material weaknesses.

A control deficiency exists when the design or operation of the control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the City of Castalia's ability to initiate, authorize, record, process, or report financial data reliably in accordance with an other comprehensive basis of accounting such that there is more than a remote likelihood a misstatement of the City of Castalia's financial statements that is more than inconsequential will not be prevented or detected by the City of Castalia's internal control. We consider the deficiencies in internal control described in the accompanying Schedule of Findings to be significant deficiencies in internal control over financial reporting.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood a material misstatement of the financial statements will not be prevented or detected by the City of Castalia's internal control.

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, of the significant deficiencies described above, we consider items (A), (B) and (C) to be material weaknesses.

Compliance and Other Matters

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

Comments involving statutory and other legal matters about the City's operations for the year ended June 30, 2007 are based exclusively on knowledge obtained from procedures performed during our audit of the financial statements of the City. Since our audit was based on tests and samples, not all transactions that might have had an impact on the comments were necessarily audited. The comments involving statutory and other legal matters are not intended to constitute legal interpretations of those statutes.

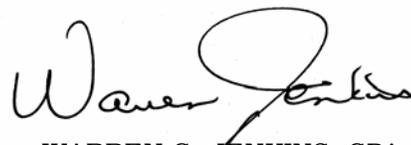
The City of Castalia's responses to findings identified in our audit are described in the accompanying Schedule of Findings. While we have expressed our conclusions on the City's responses, we did not audit the City of Castalia's responses and, accordingly, we express no opinion on them.

This report, a public record by law, is intended solely for the information and use of the officials, employees and citizens of the City of Castalia and other parties to whom the City of Castalia may report. This report is not intended to be and should not be used by anyone other than these specified parties.

We would like to acknowledge the many courtesies and assistance extended to us by personnel of the City of Castalia 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.



DAVID A. VAUDT, CPA
Auditor of State



WARREN G. JENKINS, CPA
Chief Deputy Auditor of State

June 2, 2008

City of Castalia

Schedule of Findings

Year ended June 30, 2007

Findings Related to the Financial Statements:

SIGNIFICANT DEFICIENCIES:

- (A) Segregation of Duties – One important aspect of internal control is the segregation of duties among employees to prevent an individual employee from handling duties which are incompatible. When duties are properly segregated, the activities of one employee act as a check on those of another. One person had control over each of the following areas for the City:
- (1) Accounting system – performance of all general accounting functions and having custody of assets.
 - (2) Cash – initiating cash receipts and disbursement transactions, handling and recording cash and reconciling.
 - (3) Investments – detailed record keeping, custody of investments and reconciling earnings.
 - (4) Long term debt – recording and reconciling.
 - (5) Receipts – collecting, depositing, journalizing and recording.
 - (6) Utility receipts – billing, collecting, depositing, recording and reconciling.
 - (7) Disbursements – purchasing, check signing, recording and reconciling.
 - (8) Payroll – preparing and distributing.
 - (9) Financial reporting – preparing, recording and reconciling.

Recommendation – We realize segregation of duties is difficult with a limited number of office employees. However, the City should review its control activities to obtain the maximum internal control possible under the circumstances. The City should utilize current personnel and officials to provide additional control through review of financial transactions, reconciliations and reports. Such reviews should be performed by independent persons and should be evidenced by initials or signature of the reviewer and the date of the review.

Response – A Councilperson will be appointed to check, date and initial all bills before payment and presentment to the Council. That Councilperson will also go over all bank statements, reconciliations and reports, then initial and date.

Conclusion – Response accepted.

- (B) Reconciliation of Utility Billings, Collections and Delinquent Accounts – Utility billings, collections and delinquent accounts were not reconciled throughout the fiscal year.

Recommendation – Procedures should be established to reconcile monthly utility billings, collections and delinquent accounts and reconcile collections to bank deposits. The City Council or a Council-designated independent person should

City of Castalia

Schedule of Findings

Year ended June 30, 2007

review the reconciliations and monitor delinquencies. The independent reviewer should also initial and date the reconciliation after their review.

Response – The Council will see the reconciliation of monthly utility bills, collections and delinquent accounts, and reconcile collections to bank deposit. The Council will appoint a Councilperson to review the reconciliation and initial and date after reviewing.

Conclusion – Response accepted.

- (C) Monthly Financial Reports and Bank Reconciliations – Complete monthly financial reports were not prepared and provided to City officials for their review and approval. Also, complete monthly bank to book reconciliations were not prepared, including all City bank accounts and investments.

Recommendations – Monthly financial reports and bank to book reconciliations should be prepared, including all City funds, bank accounts and investments. Variances, if any, should be investigated and resolved in a timely manner. Monthly financial reports and bank to book reconciliations should be provided to City officials each month for their review and approval.

Response – All bank statements will be reconciled to books and presented to the Council at monthly meetings.

Conclusion – Response acknowledged. In addition, monthly financial reports by individual fund and account should be prepared and provided to the City Council.

- (D) Receipts – The City does not issue receipts for City collections. Additionally, checks received were not restrictively endorsed at the time of receipt.

Recommendation – Prenumbered receipts should be issued at the time of collection for all City collections to provide control over the proper collection and recording of these collections. All checks received by the City should be restrictively endorsed at the time of receipt.

Response – We will start the prenumbered receipts for City collections. All checks will be stamped for deposit only, City of Castalia, before leaving City Hall.

Conclusion – Response acknowledged. To strengthen controls over receipts, checks should be restrictively endorsed upon receipt.

- (E) Disbursements – The City Code allows for certain disbursements to be paid prior to City Council approval as approved by Resolution of the Council. The City has not approved a disbursement approval resolution.

Recommendation – If desired, the City should approve a written disbursement approval resolution allowing the City Clerk to pay certain bills prior to approval in accordance with the City Code.

City of Castalia

Schedule of Findings

Year ended June 30, 2007

Response – The City will have their attorney draw up a written disbursement resolution allowing the Clerk and Mayor to be able to pay certain bills prior to monthly approval by the Council.

Conclusion – Response accepted.

- (F) Payroll – Although wages and salaries are approved, no time sheets or time cards are required to support hours worked.

Recommendation – The City should establish written procedures for keeping time cards or time sheets for all City employees.

Response – The City has started monthly time sheets for each City employee. These will be turned in for monthly payment approval.

Conclusion – Response accepted.

INSTANCES OF NON-COMPLIANCE:

No matters were noted.

City of Castalia

Schedule of Findings

Year ended June 30, 2007

Other Findings Related to Required Statutory Reporting:

- (1) Certified Budget – Disbursements during the year ended June 30, 2007 exceeded the amounts budgeted in the health and social services, culture and recreation, general government and business type activities functions. Chapter 384.20 of the Code of Iowa states, in part, “Public monies may not be expended or encumbered except under an annual or continuing appropriation.”

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

Response – The future budgets will be amended to meet disbursements not already budgeted.

Conclusion – Response accepted.

- (2) Questionable Disbursements – No disbursements we believe may not meet the requirements of public purpose as defined in an Attorney General’s opinion dated April 25, 1979 were noted.
- (3) Travel Expense – No disbursements of City money for travel expenses of spouses of City officials or employees were noted.
- (4) Business Transactions – Business transactions between the City and City officials or employees are detailed as follows:

Name, Title, and Business Connection	Transaction Description	Amount
Larry Brockway, Council Member	Meter reading	\$ 750
Chris Bodensteiner, City Clerk	Mowing – not bid	1,800
	Mowing – bid	805

The transaction with Council Member Brockway may represent a conflict of interest and appears to violate Chapter 372.13(8) of the Code of Iowa, which states, in part, “an elected city officer is not entitled to receive any other compensation for any other city office or city employment during the officer’s tenure in office.”

In accordance with Chapter 362.5(11) of the Code of Iowa, the transactions with the City Clerk do not appear to represent conflicts of interest since the mowing which was not bid was less than \$2,500 during the year.

Recommendation – The City should consult legal counsel to determine the disposition of the matter with Council Member Brockway.

Response – We will have the City Attorney look into the matter concerning Council Member Larry Brockway as meter reader and hire someone else.

Conclusion – Response accepted.

City of Castalia

Schedule of Findings

Year ended June 30, 2007

- (5) Bond Coverage – Surety bond coverage of City officials and employees is in accordance with statutory provisions. The amount of coverage should be reviewed annually to insure coverage is adequate for current operations.
- (6) Council Minutes – No transactions were found that we believe should have been approved in the Council minutes but were not.

Minutes were posted but did not include total disbursements by fund, a summary of receipts and the list of claims allowed, including the vendor, purpose and total of the claim, as required by Chapter 372.13(6) of the Code of Iowa.

The minutes record did not show information sufficient to indicate the vote of each council member present as required by Chapter 21.3 of the Code of Iowa.

Additionally, the City did not post annual gross salaries as required by an Attorney General's opinion dated April 12, 1978 and Chapter 372.13(6) of the Code of Iowa.

Recommendation – The City should post minutes as required by the Code of Iowa. In addition, the minutes posted should include total disbursements by fund, a summary of receipts and a list of claims, including vendor, purpose and total. The minutes should indicate the vote of each member as required. The annual gross salaries/wages should be posted as required.

Response – The minutes will reflect the vote of each member if it is not a unanimous decision. The annual gross wages of each employee/Council person will be posted.

Conclusion – Response acknowledged. In addition, the minutes posted should include total disbursements by fund, a summary of receipts and a list of claims, including vendor, purpose and total.

- (7) Deposits and Investments – No instances of non-compliance with the deposit and investment provisions of Chapters 12B and 12C of the Code of Iowa and the City's investment policy were noted, except as follows:

Although the City has an approved investment policy, the policy contains references to an outdated portion of the Code of Iowa, Chapter 452.

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

Response – The City Attorney will be contacted to write a new investment policy as required by Chapter 12B.10B of the Code of Iowa.

Conclusion – Response accepted.

- (8) Sewer Revenue Notes – No instances of non-compliance with the provisions of the City's sewer revenue note resolution were noted.

The City does not maintain a revenue note register, including the principal and interest due and payable throughout the term of the issue.

City of Castalia

Schedule of Findings

Year ended June 30, 2007

Recommendation – The City should maintain a sewer revenue note register which includes, at a minimum, the principal and interest due and payable for each year through maturity of the issue.

Response – We now have a note register which includes the principal and interest due and payable each year through maturity in 2042.

Conclusion – Response accepted.

- (9) Water Rates – The City approved water rates and fees by resolution of the City Council. Chapter 384.84 of the Code of Iowa requires utility rates be established by ordinance of the City Council.

Recommendation – The City should establish water rates and fees in accordance with Chapter 384.84 of the Code of Iowa.

Response – We will be holding a public hearing and set new water rates by an ordinance our City Attorney will draw up for us.

Conclusion – Response accepted.

- (10) Electronic Check Retention – Chapter 554D.114 of the Code of Iowa allows the City to retain cancelled checks in an electronic format and requires retention in this manner to include an image of both the front and back of each cancelled check. The City retains cancelled checks through electronic image, but does not obtain an image of the back of each cancelled check as required.

Recommendation – The City should obtain an image of both the front and back of each cancelled check as required.

Response – The City has contacted the bank and requested both the front and back of each check are included in the monthly bank statement.

Conclusion – Response accepted.

- (11) Petition for Audit – Except as noted, all items included in the petition for audit have been resolved.

City of Castalia

Staff

This audit was performed by:

Michelle B. Meyer, CPA, Manager
John G. Vanis, CGFM, Senior Auditor
Mike P. Piehl, Assistant Auditor


Andrew E. Nielsen, CPA
Deputy Auditor of State