



OFFICE OF AUDITOR OF STATE
STATE OF IOWA

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NEWS RELEASE

FOR RELEASE _____ February 4, 2005

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515/281-5834

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

The City has implemented new reporting standards for the year ended June 30, 2004, 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 \$1,519,183 for the year ended June 30, 2004. The receipts included \$319,481 in property tax, \$15,823 from tax increment financing, \$591,516 from charges for service, \$86,213 from operating grants, contributions and restricted interest, \$36,515 from capital grants, contributions and restricted interest, \$131,432 from grants and contributions not restricted to specific purpose, \$23,307 from unrestricted interest on investments, \$313,975 from note proceeds and \$921 from other general receipts.

Disbursements for the year totaled \$1,456,220, and included \$249,564 for public works, \$243,090 for capital projects and \$144,262 for culture and recreation. Also, disbursements for business type activities totaled \$469,083.

This report contains recommendations to the City Council and other City officials. For example, the City should review its internal control procedures and segregate duties to the extent possible, establish policies and procedures regarding the use and operation of its computer system and reconcile utility billings, collections and delinquencies for each billing period. The City's responses are included in the audit report.

A copy of the audit report is available for review in the Office of Auditor of State and the City Clerk's office.

#

CITY OF EARLHAM

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

JUNE 30, 2004

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City of Earlham

Officials

<u>Name</u>	<u>Title</u>	<u>Term Expires</u>
(Before January 2004)		
Richard Rothert	Mayor	Jan 2004
Truman Payne	Council Member	Jan 2004
William Hunter	Council Member	Jan 2004
Doug Waugh	Council Member	Jan 2006
Jeff Beisner	Council Member	Jan 2006
Andrew Arnburg	Council Member	Jan 2006
(After January 2004)		
Richard Rothert	Mayor	Jan 2008
Doug Waugh	Council Member	Jan 2006
Jeff Beisner	Council Member	Jan 2006
Andrew Arnburg	Council Member	Jan 2006
Bob Derrickson	Council Member	(Deceased)
Alan Howarth (Appointed)	Council Member	Jan 2006
Scott Petersen	Council Member	Jan 2008
Marilyn Sesker	Clerk/Treasurer	Indefinite
Samuel Braland	Attorney	Indefinite

City of Earlham



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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 Earlham, Iowa, as of and for the year ended June 30, 2004, 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 Earlham'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, Chapter 11 of the Code of Iowa and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States. Those standards and provisions 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.

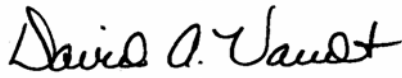
In our opinion, the financial statements referred to above present fairly, in all material respects, the respective cash basis financial position of the governmental activities, the business type activities, each major fund and the aggregate remaining fund information of the City of Earlham as of June 30, 2004, 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 9, during the year ended June 30, 2004, 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 August 19, 2004 on our consideration of the City of Earlham's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grants. That report is an integral part of an audit performed in accordance with Government Auditing Standards and should be read in conjunction with this report in considering the results of our audit.

Management's Discussion and Analysis and budgetary comparison information on pages 7 through 12 and 28 through 30 are not required parts of the basic financial statements, but are supplementary information required by the Governmental Accounting Standards Board. We applied limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. We did not audit the information and express no opinion on it.

Our audit was performed for the purpose of forming opinions on the financial statements that collectively comprise the City of Earlham's basic financial statements. We previously audited, in accordance with the standards referred to in the second paragraph of this report, the financial statements for the year ended June 30, 2003 (which are not presented herein) and expressed an unqualified opinion on those financial statements. Other supplementary information included in Schedules 1 through 4 is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in our audit of the basic financial statements and, in our opinion, 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

August 19, 2004

MANAGEMENT'S DISCUSSION AND ANALYSIS

The City of Earlham 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, 2004. 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, much of the information is not easily comparable to prior years. However, in future years, comparisons will be more meaningful and will go further in explaining the City's financial position and results of operations.

2004 FINANCIAL HIGHLIGHTS

- Receipts of the City's governmental activities increased 6%, or \$43,106, from fiscal 2003 to fiscal 2004. Property tax increased approximately \$38,000.
- Disbursements for the City's governmental activities decreased 29%, or \$404,710, from fiscal 2003 to fiscal 2004. General government disbursements increased \$43,377, while public safety and capital projects disbursements decreased \$74,769 and \$448,375, respectively.
- The City's total cash basis net assets increased 6.4%, or \$62,963, from June 30, 2003 to June 30, 2004. Of this amount, the assets of the governmental activities increased \$59,940 and the assets of the business type activities increased \$3,023.

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 of the City's budget for the year.

Other Supplementary Information provides detailed information about the nonmajor governmental funds.

Basis of Accounting

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

REPORTING THE CITY'S FINANCIAL ACTIVITIES

Government-wide Financial Statement

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

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

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

- Governmental Activities include public safety, public works, culture and recreation, community and economic development, general government, debt service and capital projects. Property tax and state and federal grants finance most of these activities.
- Business Type Activities include the waterworks and the sanitary sewer system. These activities are financed primarily by user charges.

Fund Financial Statements

The City has two kinds of funds:

1) Governmental funds account for most of the City's basic services. These focus on how money flows into and out of those funds, and the balances at year-end that are available for spending. The governmental funds include: 1) the General Fund, 2) the Special Revenue Funds, such as Road Use Tax and Tax Increment Financing, 3) the Debt Service Fund, 4) the Capital Projects Fund and 5) the Permanent Fund. The governmental fund financial statements provide a detailed, short-term view of the City's general government operations and the basic services it provides. Governmental fund information helps determine whether there are more or fewer financial resources that can be spent in the near future to finance the City's programs.

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

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

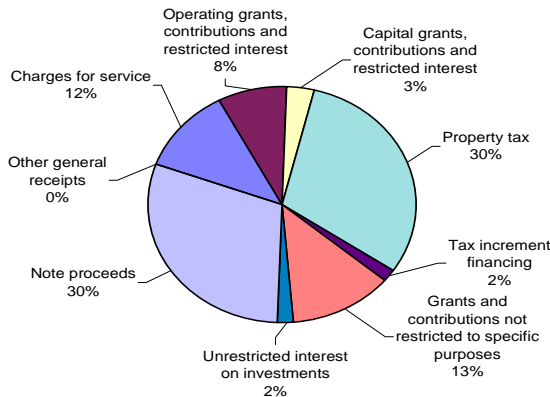
The required financial statement for proprietary funds is a statement of cash receipts, disbursements and changes in cash balances.

GOVERNMENT-WIDE FINANCIAL ANALYSIS

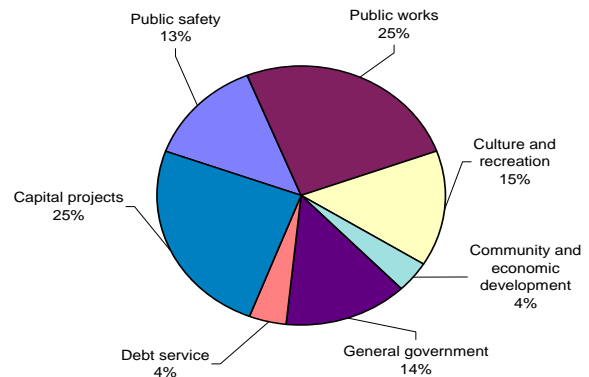
Net assets may serve over time as a useful indicator of financial position. The analysis that follows focuses on the changes in cash balances for governmental activities.

<u>Changes in Cash Basis Net Assets of Governmental Activities</u>	
	<u>Year ended June 30, 2004</u>
Receipts:	
Program receipts:	
Charges for service	\$ 122,743
Operating grants, contributions and restricted interest	86,213
Capital grants, contributions and restricted interest	36,515
General receipts:	
Property tax	319,481
Tax increment financing	15,823
Grants and contributions not restricted to specific purposes	131,432
Unrestricted interest on investments	19,974
Note proceeds	313,975
Other general receipts	921
Total receipts	<u>1,047,077</u>
Disbursements:	
Public safety	132,968
Public works	249,564
Culture and recreation	144,262
Community and economic development	37,472
General government	137,550
Debt service	42,231
Capital projects	243,090
Total disbursements	<u>987,137</u>
Increase in cash basis net assets	59,940
Cash basis net assets beginning of year	<u>319,593</u>
Cash basis net assets end of year	<u>\$ 379,533</u>

Receipts by Source



Disbursements by Function



The City's total receipts for governmental activities were \$1,047,077. The total cost of all programs and services was \$987,137, with no new programs added this year.

The City increased property tax rates for 2004 by an average of 12 percent. This increase, plus the increase in the total assessed valuation, raised the City's property tax receipts by approximately \$38,000 in 2004.

The cost of all governmental activities this year was \$987,137. As shown in the Statement of Activities and Net Assets, the amount taxpayers ultimately financed for these activities was only \$741,666 because some of the cost was paid by those directly benefited from the programs (\$122,743) or by other governments and organizations that subsidized certain programs with grants, contributions and restricted interest (\$122,728).

Changes in Cash Basis Net Assets of Business Type Activities

	Year ended June 30, 2004
Receipts:	
Program receipts:	
Charges for service:	
Water	\$ 284,801
Sewer	183,972
General receipts:	
Unrestricted interest on investments	3,333
Total receipts	<u>472,106</u>
Disbursements:	
Water	329,251
Sewer	139,832
Total disbursements	<u>469,083</u>
Increase in cash basis net assets	3,023
Cash basis net assets beginning of year	<u>657,795</u>
Cash basis net assets end of year	<u><u>\$ 660,818</u></u>

Total business type activities receipts for the fiscal year were \$472,106 compared to \$505,742 last year. Total disbursements for the fiscal year increased by 16.9% to a total of \$469,083.

INDIVIDUAL MAJOR GOVERNMENTAL FUND ANALYSIS

As the City of Earlham completed the year, its governmental funds reported a combined fund balance of \$379,533, an increase of \$59,940 from last year’s total of \$319,593. 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 decreased \$58,558 from the prior year to \$34,639. This decrease is attributable to the purchase of a rescue unit.
- The Road Use Tax Fund cash balance of \$152,147 did not change significantly from the prior year.
- The Library Trust Fund cash balance of \$380,090 did not change significantly from the prior year.
- The Fire/Rescue Department Fund cash balance of \$39,893 did not change significantly from the prior year.
- The Capital Projects Fund cash balance increased by \$134,444 to (\$281,259) during the fiscal year. This increase was due to the receipt of note proceeds.
- The Permanent Fund (Cemetery Perpetual Care) cash balance of \$65,946 did not change significantly from the prior year.

INDIVIDUAL MAJOR BUSINESS TYPE FUND ANALYSIS

- The Water Fund cash balance decreased by \$43,124 to \$281,475, due primarily to an additional employee and a water main project.
- The Sewer Fund cash balance increased by \$46,147 to \$379,343, due primarily to a rate increase for adding an additional cell to the lagoon.

BUDGETARY HIGHLIGHTS

Over the course of the year, the City amended its budget one time. The amendment was approved on June 14, 2004. The amendment provided for additional disbursements for capital projects and in certain City departments. The City issued capital loan notes and had sufficient cash balances to absorb these additional costs.

DEBT ADMINISTRATION

At June 30, 2004, the City had \$2,890,789 in outstanding notes and other long-term debt, compared to \$2,680,931 last year, as shown below.

	Outstanding Debt at Year-End	
	June 30,	
	2004	2003
General obligation capital loan notes	\$ 270,000	-
Water service agreement	1,135,564	1,145,103
Sewer revenue notes	1,260,000	1,270,000
TIF revenue notes	70,000	80,000
Lease purchase agreements	155,225	185,828
Total	<u>\$2,890,789</u>	<u>2,680,931</u>

The Constitution of the State of Iowa limits the amount of general obligation debt cities can issue to 5% of the assessed value of all taxable property within the City's corporate limits. The City's outstanding general obligation debt of \$1,630,789 is significantly below its constitutional debt limit of \$2.5 million.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES

The City of Earlham's elected and appointed officials and department heads considered many factors when setting the fiscal year 2005 budget, tax rates and fees that will be charged for various City activities.

When adopting the budget for fiscal year 2005, the Council requested departments to be conservative in budget askings. Although property tax valuations did not change, the tax base increased providing additional revenue. However, the City expects lower revenues from the state leading to a reduction of approximately \$16,000 in General Fund revenues. The City has issued general obligation debt to finance street projects set to begin in 2005. The City has added no major new programs to the 2005 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 Marilyn Sesker, City Clerk, 140 South Chestnut Ave, Earlham, Iowa.

Basic Financial Statements

City of Earlham

Statement of Activities and Net Assets – Cash Basis

As of and for the year ended June 30, 2004

	Disbursements	Program Receipts		
		Charges for Service	Operating Grants, Contributions and Restricted Interest	Capital Grants, Contributions and Restricted Interest
Functions / Programs:				
Governmental activities:				
Public safety	\$ 132,968	199	43,040	-
Public works	249,564	85,535	-	-
Culture and recreation	144,262	35,635	43,173	-
Community and economic development	37,472	-	-	-
General government	137,550	1,374	-	-
Debt service	42,231	-	-	-
Capital projects	243,090	-	-	36,515
Total governmental activities	987,137	122,743	86,213	36,515
Business type activities:				
Water	329,251	284,801	-	-
Sewer	139,832	183,972	-	-
Total business type activities	469,083	468,773	-	-
Total	\$ 1,456,220	591,516	86,213	36,515
General Receipts:				
Property tax levied for:				
General purposes				
Tax increment financing				
Debt service				
Grants and contributions not restricted to specific purpose				
Unrestricted interest on investments				
Note proceeds				
Miscellaneous				
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:				
Debt service				
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
(89,729)	-	(89,729)
(164,029)	-	(164,029)
(65,454)	-	(65,454)
(37,472)	-	(37,472)
(136,176)	-	(136,176)
(42,231)	-	(42,231)
(206,575)	-	(206,575)
(741,666)	-	(741,666)
-	(44,450)	(44,450)
-	44,140	44,140
-	(310)	(310)
(741,666)	(310)	(741,976)
287,996	-	287,996
15,823	-	15,823
31,485	-	31,485
131,432	-	131,432
19,974	3,333	23,307
313,975	-	313,975
921	-	921
801,606	3,333	804,939
59,940	3,023	62,963
319,593	657,795	977,388
\$ 379,533	660,818	1,040,351
\$ -	155,871	155,871
379,533	504,947	884,480
\$ 379,533	660,818	1,040,351

City of Earlham

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

As of and for the year ended June 30, 2004

	Special Revenue		
	General	Road Use Tax	Library Trust
Receipts:			
Property tax	\$ 287,996	-	-
Tax increment financing	-	-	-
Licenses and permits	10,157	-	-
Use of money and property	5,536	-	13,989
Intergovernmental	48,563	108,107	-
Charges for service	101,330	-	-
Special assessments	-	-	-
Miscellaneous	49,424	1,507	-
Total receipts	<u>503,006</u>	<u>109,614</u>	<u>13,989</u>
Disbursements:			
Operating:			
Public safety	123,083	-	-
Public works	129,391	120,173	-
Culture and recreation	144,019	-	193
Community and economic development	37,472	-	-
General government	137,550	-	-
Debt service	-	-	-
Capital projects	-	-	-
Total disbursements	<u>571,515</u>	<u>120,173</u>	<u>193</u>
Excess (deficiency) of receipts over (under) disbursements	<u>(68,509)</u>	<u>(10,559)</u>	<u>13,796</u>
Other financing sources (uses):			
Note proceeds (net of \$2,025 discount)	-	-	-
Operating transfers in	24,951	-	(9,951)
Operating transfers out	(15,000)	-	-
Total other financing sources (uses)	<u>9,951</u>	<u>-</u>	<u>(9,951)</u>
Net change in cash balances	(58,558)	(10,559)	3,845
Cash balances beginning of year	93,197	162,706	376,245
Cash balances end of year	<u>\$ 34,639</u>	<u>152,147</u>	<u>380,090</u>
Cash Basis Fund Balances			
Unreserved:			
General fund	\$ 34,639	-	-
Special revenue funds	-	152,147	380,090
Debt service fund	-	-	-
Capital projects fund	-	-	-
Permanent fund	-	-	-
Total cash basis fund balances	<u>\$ 34,639</u>	<u>152,147</u>	<u>380,090</u>

See notes to financial statements.

Fire/Rescue Department	Capital Projects	Permanent Cemetery Perpetual Care	Nonmajor Governmental Funds	Total
-	-	-	31,485	319,481
-	-	-	15,823	15,823
-	-	-	-	10,157
369	-	22	58	19,974
-	22,525	-	-	179,195
-	-	921	-	102,251
-	11,055	-	-	11,055
15,016	2,935	-	6,284	75,166
15,385	36,515	943	53,650	733,102
9,885	-	-	-	132,968
-	-	-	-	249,564
-	-	-	50	144,262
-	-	-	-	37,472
-	-	-	-	137,550
-	-	-	42,231	42,231
-	216,048	-	27,042	243,090
9,885	216,048	-	69,323	987,137
5,500	(179,533)	943	(15,673)	(254,035)
-	313,975	-	-	313,975
-	-	-	-	15,000
-	-	-	-	(15,000)
-	313,975	-	-	313,975
5,500	134,442	943	(15,673)	59,940
34,393	(415,701)	65,003	3,750	319,593
39,893	(281,259)	65,946	(11,923)	379,533
-	-	-	-	34,639
39,893	-	-	17,813	589,943
-	-	-	(29,736)	(29,736)
-	(281,259)	-	-	(281,259)
-	-	65,946	-	65,946
39,893	(281,259)	65,946	(11,923)	379,533

City of Earlham

City of Earlham

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

As of and for the year ended June 30, 2004

	Enterprise Funds		
	Water	Sewer	Total
Operating receipts:			
Use of money and property	\$ 1,326	2,007	3,333
Charges for service	279,297	183,972	463,269
Miscellaneous	5,504	-	5,504
Total operating receipts	<u>286,127</u>	<u>185,979</u>	<u>472,106</u>
Operating disbursements:			
Business type activities	254,443	41,445	295,888
Total operating disbursements	<u>254,443</u>	<u>41,445</u>	<u>295,888</u>
Excess of operating receipts over operating disbursements	31,684	144,534	176,218
Non-operating disbursements:			
Debt service	(74,808)	(98,387)	(173,195)
Net change in cash balances	(43,124)	46,147	3,023
Cash balances beginning of year	324,599	333,196	657,795
Cash balances end of year	<u>\$ 281,475</u>	<u>379,343</u>	<u>660,818</u>
Cash Basis Fund Balances			
Reserved for debt service	\$ 98,513	57,358	155,871
Unreserved	182,962	321,985	504,947
Total cash basis fund balances	<u>\$ 281,475</u>	<u>379,343</u>	<u>660,818</u>

See notes to financial statements.

City of Earlham

Notes to Financial Statements

June 30, 2004

(1) Summary of Significant Accounting Policies

The City of Earlham is a political subdivision of the State of Iowa located in Madison County. It was first incorporated in 1870 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, health and social services, 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 Earlham 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.

These financial statements present the City of Earlham (the primary government) and its component unit. The component unit discussed below is included in the City's reporting entity because of the significance of its operational or financial relationship with the City.

Blended Component Unit

The Earlham Fire/Rescue Department was established as a non-profit corporation in accordance with Chapter 504A of the Code of Iowa. The Department is legally separate from the City but is so intertwined with the City that it is, in substance, the same as the City. The Department is reported as part of the City and blended in the Special Revenue Funds. The Department receives donations for the benefit of the Earlham Fire Department. These donations are to be used to purchase items which are not included in the City's budget.

Jointly Governed Organizations

The City also 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: Madison County Assessor's Conference Board, Madison County Joint E911 Service Board, and Madison County Emergency Management Commission.

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 services.

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.

Special Revenue:

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

The Library Trust Fund is used to account for restricted donations to the City's Public Library.

The Fire/Rescue Department Fund is used to account for donations to the Fire/Rescue Department and for purchases of items not in the City's budget.

The Capital Projects Fund is used to account to all resources used in the acquisition and construction of capital facilities.

Permanent Fund - The Cemetery Perpetual Care Fund is used to account for resources that are legally restricted to the extent that only earnings, and not principal, may be used for purposes of maintaining the City's cemetery.

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 waste water treatment and sanitary sewer system.

C. Measurement Focus and Basis of Accounting

The City of Earlham 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.

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, 2004, disbursements exceeded the amounts budgeted in the public works and general government functions.

(2) Cash and Pooled Investments

The City's deposits in banks at June 30, 2004 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's investments are categorized to give an indication of the level of risk assumed by the City at year end. The City's investments are all Category 1, which means the investments are insured or registered or the securities are held by the City or its agent in the City's name.

The City's investments at June 30, 2004 are as follows:

Type	Carrying Amount	Fair Value
Common Stock	\$ 111,900	153,030

(3) Long-Term Debt

Lease Purchase Agreements

The City has entered into lease purchase agreements to lease a pumper and rescue box. The following is a schedule of the future minimum lease payments, including interest ranging from 5.75% to 7.25% per annum, and the present value of net minimum payments under agreements in effect at June 30, 2004:

Year Ending June 30,	Pumper	Rescue Box	Total
2005	\$ 21,254	10,445	31,699
2006	21,254	10,445	31,699
2007	21,253	10,446	31,699
2008	21,253	10,446	31,699
2009	21,253	-	21,253
2010-2011	42,507	-	42,507
Total minimum lease payments	148,774	41,782	190,556
Less amount representing interest	(28,725)	(6,606)	(35,331)
Present value of net minimum lease payments	\$ 120,049	35,176	155,225

Payments under lease purchase agreements during the year ended June 30, 2004 totaled \$43,301.

Water Service Agreement

The Warren Water District has entered into a loan with the USDA to construct a water supply distribution system.

The City has entered into a water service agreement with the Warren Water District to purchase 345,000 gallons per day and pay a fee for connection to the system.

The City owns capacity in the water line, is responsible for a portion of the loan and makes monthly payments to the Warren Water District.

A schedule of the City's portion of annual debt service requirements to maturity for the loan is as follows:

Year Ending June 30,	Water Service Agreement	
	Principal	Interest
2005	\$ 10,040	57,964
2006	10,567	57,437
2007	11,121	56,883
2008	11,705	56,299
2009	12,319	55,685
2010-2014	71,996	268,024
2015-2019	92,974	247,046
2020-2024	120,064	219,956
2025-2029	155,047	184,973
2030-2034	200,224	139,796
2035-2039	258,563	81,457
2040-2042	180,944	13,951
Total	\$ 1,135,564	1,439,471

Notes Payable

The City entered into State Revolving Fund loan and disbursement agreements during the years ended June 30, 2002 and 2003 to finance a lagoon project. Since the City is still drawing funds on the 2003 revenue notes, a formal repayment schedule has not yet been adopted for that debt.

Annual debt service requirements for tax increment financing (TIF) revenue notes and sewer revenue notes are as follows:

Year Ending June 30,	TIF Revenue Notes		Sewer Revenue Notes CS192180 01		Sewer Revenue Notes CS192180 02		Total	
	Principal	Interest	Principal	Interest	Principal	Interest	Principal	Interest
	2005	\$ 10,000	5,105	47,000	33,270	7,000	4,530	64,000
2006	10,000	4,405	49,000	31,860	7,000	4,320	66,000	40,585
2007	10,000	3,695	50,000	30,390	7,000	4,110	67,000	38,195
2008	10,000	2,975	52,000	28,890	7,000	3,900	69,000	35,765
2009	10,000	2,245	53,000	27,330	7,000	3,690	70,000	33,265
2010 - 2014	20,000	2,260	292,000	111,690	39,000	15,120	351,000	129,070
2015 - 2019	-	-	338,000	65,190	46,000	8,850	384,000	74,040
2020 - 2024	-	-	228,000	13,800	31,000	1,890	259,000	15,690
Total	\$ 70,000	20,685	1,109,000	342,420	151,000	46,410	1,330,000	409,515

The resolution providing for the issuance of the sewer revenue notes issued under a loan agreement between the City of Earlham, the Iowa Finance Authority, the Iowa Department of Natural Resources and Wells Fargo Bank Iowa, N.A. includes the following provisions:

- (a) The notes will only be redeemed from the future earnings of the enterprise activity and the note holders hold a lien on the future earnings of the funds.
- (b) Monthly transfers of 1/6 of the installment of interest next due and 1/12 of the installment of principal next due shall be made to the sewer revenue note and interest sinking account.

- (c) Additional monthly transfers of 25 percent of the amount required to be deposited in the sewer revenue note and interest sinking account shall be made to the sewer reserve account until \$97,500 is accumulated and maintained.
- (d) All funds remaining after payment of all maintenance and operating expenses and the transfers to the restricted accounts noted above can be used to retire any subordinate obligations and then can be used for any lawful purpose.
- (e) Notes maturing after June 1, 2005 may be called for redemption by the issuer and paid before maturity on June 1, 2005 or any interest payment date thereafter.

The City has not made the transfers to the sewer reserve account as required by the sewer revenue note resolution.

A formal repayment schedule has not been adopted for the general obligation capital loan notes since repayment will be combined with a planned additional issue.

(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.

Plan members are required to contribute 3.70% of their annual covered salary and the City is required to contribute 5.75% of annual covered payroll, except for police employees, in which case the percentages are 5.93% and 8.90%, respectively. For the year ended June 30, 2003, the contribution rates for police employees and the City were 6.04% and 9.07%, respectively, and for the year ended June 30, 2002, the contribution rates for police employees and the City were 6.20% and 9.29%, respectively. Contribution requirements are established by state statute. The City's contributions to IPERS for the years ended June 30, 2004, 2003 and 2002 were \$13,581, \$13,785 and \$14,336, respectively, equal to the required contributions for each year.

(5) Compensated Absences

City employees accumulate a limited amount of earned but unused vacation, sick leave and compensatory time hours for subsequent use or for payment upon termination, retirement or death. These accumulations are not recognized as disbursements by the City until used or paid. The City's approximate liability for earned vacation and sick leave termination payments payable to employees at June 30, 2004, primarily relating to the General Fund, is as follows:

Type of Benefit	Amount
Vacation	\$ 8,900
Sick leave	19,900
Compensatory time	<u>6,000</u>
Total	<u>\$ 34,800</u>

This liability has been computed based on rates of pay in effect at June 30, 2004.

(6) Interfund Transfers

The detail of interfund transfers for the year ended June 30, 2004 is as follows:

Transfer to	Transfer from	Amount
General: Library General	General: General	\$ 15,000
	Special Revenue: Library Trust	<u>9,951</u>
Total		<u>\$ 24,951</u>

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

(7) Risk Management

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

(8) Deficit Fund Balances

The Capital Projects Fund had a deficit balance of \$281,259 at June 30, 2004. The deficit balance was a result of project costs incurred prior to availability of funds. The deficit will be eliminated upon receipt of special assessments from benefited property owners. The Debt Service Fund had a deficit balance of \$29,736 at June 30, 2004 because the City called several bonds early in previous years.

(9) 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, 2004. 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 Earlham
 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, 2004

	Governmental Funds Actual	Proprietary Funds Actual	Less Funds not Required to be Budgeted
Receipts:			
Property tax	\$ 319,481	-	-
Tax increment financing	15,823	-	-
Other city tax	-	-	-
Licenses and permits	10,157	-	-
Use of money and property	19,974	3,333	391
Intergovernmental	179,195	-	-
Charges for service	102,251	463,269	921
Special assessments	11,055	-	-
Miscellaneous	75,166	5,504	15,016
Total receipts	733,102	472,106	16,328
Disbursements:			
Public safety	132,968	-	9,885
Public works	249,564	-	-
Culture and recreation	144,262	-	-
Community and economic development	37,472	-	-
General government	137,550	-	-
Debt service	42,231	-	-
Capital projects	243,090	-	-
Business type activities	-	469,083	-
Total disbursements	987,137	469,083	9,885
Excess (deficiency) of receipts over (under) disbursements	(254,035)	3,023	6,443
Other financing sources, net	313,975	-	-
Excess of receipts and other financing sources over disbursements and other financing uses	59,940	3,023	6,443
Balances beginning of year	319,593	657,795	99,396
Balances end of year	\$ 379,533	660,818	105,839

See accompanying independent auditor's report.

Net	Budgeted Amounts		Final to Net Variance
	Original	Final	
319,481	307,861	307,861	11,620
15,823	87,090	87,090	(71,267)
-	12,970	12,970	(12,970)
10,157	12,650	12,850	(2,693)
22,916	22,400	22,400	516
179,195	220,899	224,834	(45,639)
564,599	774,220	832,643	(268,044)
11,055	6,000	6,000	5,055
65,654	69,262	69,262	(3,608)
<u>1,188,880</u>	<u>1,513,352</u>	<u>1,575,910</u>	<u>(387,030)</u>
123,083	151,819	164,669	41,586
249,564	225,340	247,340	(2,224)
144,262	160,095	176,510	32,248
37,472	69,500	69,500	32,028
137,550	85,913	96,208	(41,342)
42,231	43,329	43,329	1,098
243,090	70,000	328,000	84,910
469,083	619,961	718,181	249,098
<u>1,446,335</u>	<u>1,425,957</u>	<u>1,843,737</u>	<u>397,402</u>
(257,455)	87,395	(267,827)	10,372
<u>313,975</u>	<u>-</u>	<u>270,000</u>	<u>43,975</u>
56,520	87,395	2,173	54,347
<u>877,992</u>	<u>875,528</u>	<u>875,258</u>	<u>2,734</u>
<u>934,512</u>	<u>962,923</u>	<u>877,431</u>	<u>57,081</u>

City of Earlham

Notes to Required Supplementary Information – Budgetary Reporting

June 30, 2004

In accordance with the Code of Iowa, the City Council annually adopts a budget on the cash basis following required public notice and hearing for all funds except the Fire/Rescue Department and Cemetery Perpetual Care 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, Special Revenue Funds, Debt Service Fund, Capital Projects Fund and Proprietary Funds. Although the budget document presents function disbursements by fund, the legal level of control is at the aggregated function level, not by fund. During the year, one budget amendment increased budgeted disbursements by \$417,780. The budget amendment is reflected in the final budgeted amounts.

During the year ended June 30, 2004, disbursements exceeded the amounts budgeted in the public works and general government functions.

Other Supplementary Information

City of Earlham

City of Earlham

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

As of and for the year ended June 30, 2004

	Special Revenue			Total
	Tax Increment Financing	Community Center	Debt Service	
Receipts:				
Property tax	\$ -	-	31,485	31,485
Tax increment financing	15,823	-	-	15,823
Use of money and property	-	58	-	58
Miscellaneous	-	6,284	-	6,284
Total receipts	15,823	6,342	31,485	53,650
Disbursements:				
Operating:				
Culture and recreation	-	50	-	50
Debt service	-	-	42,231	42,231
Capital projects	27,042	-	-	27,042
Total disbursements	27,042	50	42,231	69,323
Excess (deficiency) of receipts over (under) disbursements	(11,219)	6,292	(10,746)	(15,673)
Cash balances beginning of year	22,740	-	(18,990)	3,750
Cash balances end of year	\$ 11,521	-	(29,736)	3,750
Cash Basis Fund Balances				
Unreserved:				
Special revenue funds	\$ 11,521	6,292	-	17,813
Debt service fund	-	-	(29,736)	(29,736)
Total cash basis fund balances	\$ 11,521	6,292	(29,736)	(11,923)

See accompanying independent auditor's report.

City of Earlham
Schedule of Indebtedness
Year ended June 30, 2004

Obligation	Date of Issue	Interest Rates	Amount Originally Issued
Tax increment financing revenue notes	Jun 1, 1999	6.60-7.55%	\$ 100,000
Water service agreement	Jun 1, 2002	5.125%	\$ 1,154,167
State Revolving Fund sewer revenue notes:			
CS192180 01	Oct 24, 2001	3.00%	\$ 1,200,000
CS192180 02	Jun 25, 2002	3.00	250,000
Total			
General obligation capital loan notes	Jun 8, 2004	2.00%	\$ 270,000
Lease purchase agreements:			
Truck	Nov 9, 1998	5.75%	\$ 52,355
Pumper	Apr 23, 2002	5.50	150,038
Rescue box	Sept 16, 2002	7.25	42,656
Total			

See accompanying independent auditor's report.

Balance Beginning of Year	Issued During Year	Redeemed During Year	Balance End of Year	Interest Paid
80,000	-	10,000	70,000	5,790
1,145,103	-	9,539	1,135,564	58,465
1,155,000	-	46,000	1,109,000	34,650
115,000	46,000	10,000	151,000	4,247
\$ 1,270,000	46,000	56,000	1,260,000	38,897
-	270,000	-	270,000	-
10,971	-	10,971	-	631
132,201	-	12,152	120,049	9,102
42,656	-	7,480	35,176	2,965
\$ 185,828	-	30,603	155,225	12,698

City of Earlham

Note Maturities

June 30, 2004

Year Ending June 30,	TIF Revenue Notes Issued June 1, 1999		Water Service Agreement	
	Interest Rates	Amount	Interest Rates	Amount
2005	7.00%	\$ 10,000	5.125%	\$ 10,040
2006	7.10	10,000	5.125	10,567
2007	7.20	10,000	5.125	11,121
2008	7.30	10,000	5.125	11,705
2009	7.40	10,000	5.125	12,319
2010-2014	7.50	20,000	5.125	71,996
2015-2019		-	5.125	92,974
2020-2024		-	5.125	120,064
Total		<u>\$ 70,000</u>		<u>\$1,135,564</u>

See accompanying independent auditor's report.

Year Ending June 30,	Sewer Revenue Notes					Total
	CS192180 01		CS192180 02			
	Interest Rates	Amount	Interest Rates	Amount		
2005	3.00%	\$ 47,000	3.00%	\$ 7,000		54,000
2006	3.00	49,000	3.00	7,000		56,000
2007	3.00	50,000	3.00	7,000		57,000
2008	3.00	52,000	3.00	7,000		59,000
2009	3.00	53,000	3.00	7,000		60,000
2010-2014	3.00	292,000	3.00	39,000		331,000
2015-2019	3.00	338,000	3.00	46,000		384,000
2020-2024	3.00	228,000	3.00	31,000		259,000
Total		<u>\$ 1,109,000</u>		<u>\$ 151,000</u>		<u>1,260,000</u>

Schedule 4

City of Earlham

Schedule of Receipts By Source and Disbursements By Function -
All Governmental Funds

For the Last Two Years

	<u>2004</u>	<u>2003</u>
Receipts:		
Property tax	\$ 319,481	281,806
Tax increment financing	15,823	16,411
Licenses and permits	10,157	11,075
Use of money and property	19,974	22,716
Intergovernmental	179,195	171,169
Charges for service	102,251	104,976
Special assessments	11,055	7,728
Miscellaneous	75,166	74,115
	<u> </u>	<u> </u>
Total	<u>\$ 733,102</u>	<u>689,996</u>
Disbursements:		
Operating:		
Public safety	\$ 132,968	207,737
Public works	249,564	209,642
Culture and recreation	144,262	142,631
Community and economic development	37,472	-
General government	137,550	94,173
Debt service	42,231	46,199
Capital projects	243,090	691,465
	<u> </u>	<u> </u>
Total	<u>\$ 987,137</u>	<u>1,391,847</u>

See accompanying independent auditor's report.

**Independent Auditor's Report on Compliance
and on Internal Control over Financial Reporting**

City of Earlham



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 Compliance
and on Internal Control over Financial Reporting

To the Honorable Mayor and
Members of the City Council:

We have audited the financial statements of the City of Earlham, Iowa, as of and for the year ended June 30, 2004, and have issued our report thereon dated August 19, 2004. Our report expressed unqualified opinions on the financial statements which were prepared in conformity with an other comprehensive basis of accounting. We conducted our audit in accordance with U.S. generally accepted auditing standards, Chapter 11 of the Code of Iowa and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States.

Compliance

As part of obtaining reasonable assurance about whether the City of Earlham's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, 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 that are required to be reported under Government Auditing Standards. However, we noted certain immaterial instances of non-compliance that are described in the accompanying Schedule of Findings.

Comments involving statutory and other legal matters about the City's operations for the year ended June 30, 2004 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. Prior year statutory comments have been resolved except for items (2), (9), (10) and (11).

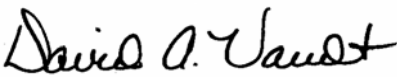
Internal Control Over Financial Reporting

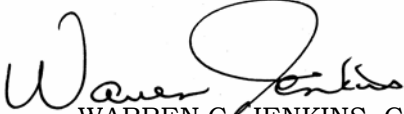
In planning and performing our audit, we considered the City of Earlham's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. However, we noted certain matters involving the internal control over financial reporting and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the City of Earlham's ability to record, process, summarize and report financial data consistent with the assertions of management in the financial statements. Reportable conditions are described in the accompanying Schedule of Findings.

A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, of the reportable conditions described above, we believe items (A) and (B) are material weaknesses. Prior year reportable conditions have been resolved except for items (A), (B), (C), (D) and (E).

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 Earlham and other parties to whom the City of Earlham 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 Earlham 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

August 19, 2004

City of Earlham

City of Earlham
Schedule of Findings
Year ended June 30, 2004

Findings Related to the Financial Statements:

INSTANCES OF NON-COMPLIANCE:

No matters were noted.

REPORTABLE CONDITIONS:

- (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 that are incompatible. One individual has control over the following areas for the City:

- (1) Accounting system – performance of all general accounting functions and custody of assets.
- (2) Bank reconciliation – preparation and maintenance of accounting records.
- (3) Investments – investing, recording and custody.
- (4) Receipts – collecting, depositing, journalizing and posting.
- (5) Utility receipts – billing, collecting, depositing, posting and reconciling.

Recommendation – We realize segregation of duties is difficult with a limited number of office employees. However, the City should review its operating procedures to obtain the maximum internal control possible under the circumstances.

Response – Procedures will be reviewed to provide maximum internal control.

Conclusion – Response accepted.

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

Recommendation – Procedures should be established to reconcile utility billings, collections and delinquencies for each billing period. The Council or other independent person should review the reconciliation and monitor delinquencies.

Response – Implemented for July billing.

Conclusion – Response accepted.

- (C) Payroll – Timesheets for supervisors did not indicate they had been approved before the payroll was prepared.

Recommendation – There should be written documentation each time sheet was reviewed and approved before payroll warrants are prepared.

Response – The Clerk reviews each timesheet prior to entering information in computer. I will make a bigger effort to initial timesheets at review.

Conclusion – Response accepted.

City of Earlham

Schedule of Findings

Year ended June 30, 2004

- (D) Dual Signed Checks – The City Council adopted a policy that requires all checks written for \$1,500 or more to be signed by the City Clerk and Mayor. Five checks written over \$1,500 were not dual signed. Also, one check over \$1,500 was not signed at all.

Recommendation – The City should enforce the policy to dual sign checks over \$1,500.

Response – The Mayor approves all checks in excess of \$1,500. If it is not convenient for him to sign, we get his verbal approval or have mayor pro tem initial.

Conclusion – Response acknowledged. Checks should be signed as required by City policy.

- (E) Electronic Data Processing Systems – During our review of internal control, the existing control activities in the City's computer based systems were evaluated in order to determine activities, from a control standpoint, were designed to provide reasonable assurance regarding the achievement of objectives in the reliability of financial reporting, effectiveness and efficiency of operations, and compliance with applicable laws and regulations. The following weaknesses in the City's computer based systems were noted:

The City does not have written policies for:

- Logging off unattended computers.
- Password privacy and confidentiality.
- Backups for personal computer hard drives.
- Requiring the use of an anti-virus program on computers.
- Ensuring only software licensed to the City is installed on computers
- Usage of the internet
- Personal use of computer equipment and software

Also, the City does not have a written disaster recovery plan.

Recommendation – The City should develop written policies addressing the above items in order to improve the City's control over computer based systems. A written disaster recovery plan should be developed.

Response – This will be corrected.

Conclusion – Response accepted.

City of Earlham

Schedule of Findings

Year ended June 30, 2004

Other Findings Related to Statutory Reporting:

- (1) Official Depositories – A resolution naming official depositories has been approved by the City Council. The maximum deposit amounts stated in the resolution were exceeded during the year ended June 30, 2004.

Recommendation – The City should review its maximum deposit amounts to determine the indicated maximums are sufficient for City business activity.

Response – This will be corrected by increasing the maximum deposit.

Conclusion – Response accepted.

- (2) Certified Budget – Disbursements during the year ended June 30, 2004 exceeded the amounts budgeted in the public works and general government 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 amount in accordance with Chapter 384.18 of the Code of Iowa before disbursements were allowed to exceed the budget.

Response – More care will be taken to amend budget prior to exceeding budgeted amount.

Conclusion – Response accepted.

- (3) Questionable Disbursements – No disbursements that may not meet the requirements of public purpose as defined in an Attorney General's opinion dated April 25, 1979 were noted.

- (4) Travel Expense – No disbursements of City money for travel expenses of spouses of City officials or employees were noted.

- (5) Business Transactions – No business transactions between the City and City officials were noted.

- (6) 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 the coverage is adequate for current operations.

- (7) Council Minutes – Except as noted below, no transactions were found that we believe should have been approved in the Council minutes but were not.

The City minutes did not reflect the purpose of one closed session that was held.

Recommendation – The City should document in the minutes the purpose of all closed sessions held.

Response – This will not be done again.

Conclusion – Response accepted.

City of Earlham

Schedule of Findings

Year ended June 30, 2004

(8) 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.

(9) Revenue Notes – The City has established the Sewer Revenue Sinking Account and the Sewer Reserve Account required by the revenue note resolution. However, the City did not make the required transfers to the Sewer Reserve Account.

Recommendation – City officials should review the revenue note resolution and comply with the provisions of the resolution. The City should also periodically review the accounts to ensure the required transfers have been made and established rates will result in sufficient funds to meet future obligations.

Response – Transfer will be made to Sewer Reserve. Resolutions will be monitored.

Conclusion – Response accepted.

(10) Vacation Usage – The City does not have a written policy regarding pay-out in lieu of use of vacation time during employment.

Recommendation – The City should adopt a written policy regarding pay-out in lieu of use of vacation time during employment. That policy should include prior written approval from the Council.

Response – Will be addressed in Employee Policy revision.

Conclusion – Response accepted.

(11) Financial Condition – The Capital Projects Fund had a deficit balance at June 30, 2004 of \$281,259. Also at June 30, 2004, the Debt Service Fund had a deficit balance of \$29,736.

Recommendation – The City should investigate alternatives to eliminate these deficits in order to return the accounts to a sound financial position.

Response – We will investigate options to turn this around.

Conclusion – Response accepted.

(12) Library Investment Policy – The Library does not have a written investment policy. Also, the Library purchased common stock during the fiscal year in violation of Chapter 12B.10(5) of the Code of Iowa.

Recommendation – The Library should develop investment policies that comply with Chapter 12 of the Code of Iowa. Also, the Library investments should be reviewed to ensure they are in compliance with Chapter 12B.10(5) of the Code of Iowa.

Response – The Library Board will be encouraged to develop an investment policy in compliance with Chapter 12 of the Iowa Code and review investments to ensure they are in compliance with Chapter 12B.10(5) of the Code of Iowa.

Conclusion – Response accepted.

City of Earlham

Schedule of Findings

Year ended June 30, 2004

- (13) 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 and retain an image of both the front and back of each cancelled check as required.

Response – We have requested front and back imaging.

Conclusion – Response accepted.

- (14) Utility Rates – Commercial garbage rates being charged to customers did not agree with the contracted rates resulting in commercial customers being undercharged. Also, improper water usage rates were charged to customers using more than 10,000 gallons a month resulting in customers being overcharged.

Recommendation – The City should periodically review the rates entered into their utility system.

Response – These items have been corrected.

Conclusion – Response accepted.

- (15) Overpayment of Employee – Beginning January 1, 2004, a City employee assumed the responsibilities of the Zoning Administrator. However, when the additional hourly rate was applied to the employee's salary, the result was an overpayment of approximately \$230 from January 1, 2004 to June 30, 2004.

Recommendation – The City should review seek reimbursement for the amount overpaid.

Response – Issue has been resolved. Employee volunteered to reimburse City for overpayment.

Conclusion – Response accepted.

- (16) Credit Card Usage Policy – The City has several credit cards with which it purchases items for City use. However, there is no written credit card usage policy documenting allowable uses for the City credit cards.

Recommendation – The City should develop a credit card usage policy to ensure proper use of the City's credit cards.

Response – This will be included in Employee Policy revision.

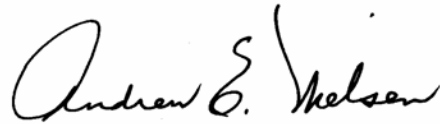
Conclusion – Response accepted.

City of Earlham

Staff

This audit was performed by:

Joe T. Marturello, CIA, Manager
Shawn P. Limback, CPA, Staff Auditor
Trevor L. Theulen, Assistant Auditor

A handwritten signature in black ink that reads "Andrew E. Nielsen". The signature is written in a cursive style with a large, looped initial "A".

Andrew E. Nielsen, CPA
Deputy Auditor of State