



**OFFICE OF AUDITOR OF STATE
STATE OF IOWA**

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NEWS RELEASE

FOR RELEASE

November 7, 2006

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

The City's receipts totaled \$7,660,950 for the year ended June 30, 2006, a 33 percent decrease from 2005. The receipts included \$2,309,033 in property tax, \$368,655 from tax increment financing, \$2,358,140 from charges for service, \$1,514,952 from operating grants, contributions and restricted interest, \$343,948 from capital grants, contributions and restricted interest, \$653,652 from local option sales tax, \$76,428 from unrestricted interest on investments and \$36,142 from other general receipts. The significant decrease in receipts is due primarily to the issuance of bonds and notes during the year ended June 30, 2005.

Disbursements for the year totaled \$9,492,072, a 28 percent increase over the prior year, and included \$2,507,606 for debt service, \$1,333,908 for capital projects and \$1,126,278 for public safety. Also, disbursements for business type activities totaled \$2,329,173. The significant increase in disbursements is due primarily to the advance refunding of general obligation bonds.

A copy of the audit report is available for review at the City of Knoxville'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 KNOXVILLE

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

JUNE 30, 2006

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City of Knoxville

Officials

<u>Name</u>	<u>Title</u>	<u>Term Expires</u>
(Before January 2006)		
Craig Kelley	Mayor	Jan 2006
Forrest Pearson	Mayor Pro tem	Jan 2006
Dave Roozeboom	Council Member	Jan 2006
Sharon Dennison	Council Member	Jan 2008
Bob Edwards	Council Member	Jan 2008
Bob Wims	Council Member	Jan 2008
Dick Schrad	City Manager	Indefinite
Connie J. Stevens	City Clerk	Indefinite
Robert Stuyvesant	Attorney	Indefinite
(After January 2006)		
Harvey Sprafka	Mayor	Jan 2008
Sharon Dennison	Mayor Pro tem	Jan 2008
Bob Edwards	Council Member	Jan 2008
Bob Wims	Council Member	Jan 2008
Dave Roozeboom	Council Member	Jan 2010
Elsie Kemp	Council Member	Jan 2010
Dick Schrad	City Manager	Indefinite
Connie J. Stevens	City Clerk	Indefinite
Robert Stuyvesant	Attorney	Indefinite

City of Knoxville



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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 Knoxville, Iowa, as of and for the year ended June 30, 2006, 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 Knoxville'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.

The financial statements referred to above include only the primary government of the City of Knoxville, which consists of all funds, organizations, institutions, agencies, departments and offices that comprise the City's legal entity. The financial statements do not include financial data for the City's legally separate component unit, which U.S. generally accepted accounting principles require to be reported with the financial data of the City's primary government. As a result, the primary government financial statements do not purport to, and do not, present fairly the cash basis financial position of the reporting entity of the City of Knoxville as of June 30, 2006, and the changes in its cash basis financial position for the year then ended in conformity with the basis of accounting described in Note 1.

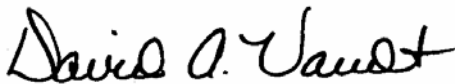
In our opinion, the financial statements referred to above present fairly, in all material respects, the respective cash basis financial position of the governmental activities, the business type activities, each major fund and the aggregate remaining fund information for the primary government of the City of Knoxville as of June 30, 2006, 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.

In accordance with Government Auditing Standards, we have also issued our report dated August 30, 2006 on our consideration of the City of Knoxville'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 12 and 34 through 36 are not required parts of the basic financial statements, but are supplementary information required by the Governmental Accounting Standards Board. We 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 Knoxville's basic financial statements. We previously audited, in accordance with the standards referred to in the second paragraph of this report, the primary government financial statements for the three years ended June 30, 2005 (which are not presented herein) and expressed unqualified opinions on those financial statements which were prepared in conformity with an other comprehensive basis of accounting. Other supplementary information included in Schedules 1 through 6, including the Schedule of Expenditures of Federal Awards required by U.S. Office of Management and Budget (OMB) Circular A-133, Audits of States, Local Governments and Non-Profit Organizations, 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 30, 2006

MANAGEMENT'S DISCUSSION AND ANALYSIS

The City of Knoxville 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, 2006. We encourage readers to consider this information in conjunction with the City's financial statements, which follow.

2006 FINANCIAL HIGHLIGHTS

- Receipts of the City's governmental activities decreased 24.9%, or approximately \$1,886,000, from fiscal 2005 to fiscal 2006. Bond proceeds decreased approximately \$2,219,000, operating grants, contributions and restricted interest increased approximately \$270,000 and property and other city tax increased approximately \$158,000.
- Disbursements for governmental activities increased 31.4%, or approximately \$1,710,000, in FY2006 from FY2005. Debt service and capital projects disbursements increased approximately \$1,595,000 and \$420,000, respectively, while community and economic development disbursements decreased approximately \$179,000.
- Receipts and transfers of the City's business type activities decreased 49.1%, or approximately \$1,896,000. Bond proceeds decreased approximately \$2,192,000, while operating grants, contributions and restricted interest increased approximately \$226,000.
- Disbursements for business type activities increased 18.9%, or approximately \$370,000.
- The City's total cash basis net assets decreased 21%, or approximately \$1,831,000, from June 30, 2005 to June 30, 2006. Of this amount, the assets of the governmental activities decreased approximately \$1,471,000 and the assets of the business type activities decreased approximately \$360,000.

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 and internal service funds. In addition, the Schedule of Expenditures of Federal Awards provides details of various federal programs benefiting the City.

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, 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, general government, debt service and capital projects. Property tax and state and federal grants finance most of these activities.
- Business Type Activities include the sanitary sewer system and municipal airport. These activities are 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, 2) the Special Revenue Funds, such as Road Use Tax and Urban Renewal Tax Increment, 3) the Debt Service Fund, 4) the Capital Projects Fund and 5) the Permanent Funds. 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 statements for governmental funds include a statement of cash receipts, disbursements and changes in cash balances.

2) Proprietary funds account for the City's Enterprise Funds and the Internal Service Funds. Enterprise Funds are used to report business type activities. The City maintains two Enterprise Funds to provide separate information for the airport and sanitary sewer operations. The Sewer Fund is considered to be a major fund of the City. Internal Service Funds are an accounting device used to accumulate and allocate costs internally among the City's various functions.

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

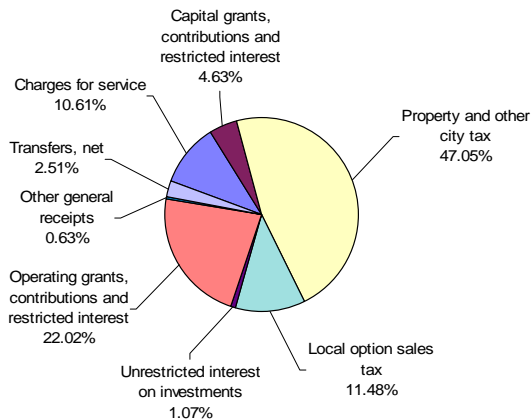
Reconciliations between the government-wide statement and the fund financial statements follow the fund financial statements.

GOVERNMENT-WIDE FINANCIAL ANALYSIS

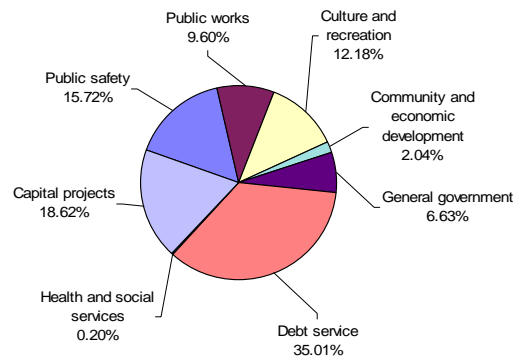
Net assets may serve over time as a useful indicator of financial position. The City's cash balance for governmental activities decreased from a year ago, decreasing from \$5.1 million to \$3.6 million. The analysis that follows focuses on the changes in cash basis net assets of governmental activities.

Changes in Cash Basis Net Assets of Governmental Activities		
	Year Ended June 30,	
	2006	2005
Receipts and transfers:		
Program receipts:		
Charges for service	\$ 603,904	573,175
Operating grants, contributions and restricted interest	1,253,236	983,483
Capital grants, contributions and restricted interest	263,812	610,629
General receipts:		
Property and other city tax	2,677,688	2,520,019
Local option sales tax	653,652	598,184
Grants and contributions not restricted to specific purposes	-	1,150
Unrestricted interest on investments	60,929	22,283
Note proceeds	-	2,219,288
Other general receipts	36,142	16,687
Transfers, net	142,679	32,704
Total receipts and transfers	5,692,042	7,577,602
Disbursements:		
Public safety	1,126,278	1,192,484
Public works	687,467	693,009
Health and social services	14,307	-
Culture and recreation	872,086	985,665
Community and economic development	146,308	325,700
General government	474,939	428,508
Debt service	2,507,606	913,064
Capital projects	1,333,908	914,329
Total disbursements	7,162,899	5,452,759
Increase (decrease) in cash basis net assets	(1,470,857)	2,124,843
Cash basis net assets beginning of year	5,060,196	2,935,353
Cash basis net assets end of year	\$ 3,589,339	5,060,196

Receipts by Source



Disbursements by Function



The City's total receipts for governmental activities decreased 24.9%, or \$1,886,000. The total cost of all programs and services increased by \$1,710,000, or 31.4%, with no new programs added this year. The major changes in receipts were bond proceeds decreased approximately \$2,219,000, operating grants, contributions and restricted interest increased \$270,000 and property and other City tax increased \$158,000.

The City increased property tax rates for 2006 by more than 5%.

Changes in Cash Basis Net Assets of Business Type Activities		
	Year ended June 30,	
	2006	2005
Receipts and transfers:		
Program receipts:		
Charges for service	\$ 1,754,236	1,615,403
Operating grants, contributions and restricted interest	261,716	35,592
Capital grants, contributions and restricted interest	80,136	18,985
General receipts:		
Unrestricted interest on investments	15,499	35,993
Bond proceeds	-	2,192,065
Transfers, net	(142,679)	(32,704)
Total receipts and transfers	1,968,908	3,865,334
Disbursements:		
Sewer	2,056,760	1,852,518
Airport	272,413	106,769
Total disbursements	2,329,173	1,959,287
Increase (decrease) in cash basis net assets	(360,265)	1,906,047
Cash basis net assets beginning of year	3,671,252	1,765,205
Cash basis net assets end of year	\$ 3,310,987	3,671,252

Total business type activities receipts and transfers for the fiscal year were approximately \$2 million compared to \$3.9 million last year. The decrease was due primarily to the receipt of approximately \$2,192,000 in general obligation bond proceeds during FY2005. The cash balance decreased by approximately \$360,000. Total disbursements for the year increased by 18.9% to a total of approximately \$2,329,000.

INDIVIDUAL MAJOR GOVERNMENTAL FUND ANALYSIS

As the City of Knoxville completed the year, its governmental funds reported a combined fund balance of \$2,864,075, a decrease of more than \$1,616,000 from last year's total of \$4,480,211. 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 \$55,008 from the prior year to a year-end balance of \$274,130. There were no significant changes in receipts or disbursements for the General Fund.
- The Road Use Tax Fund cash balance decreased by \$43,975 to \$179,679 during the fiscal year. There were no significant changes in receipts or disbursements for the Road Use Tax Fund.
- The Local Option Sales Tax (LOST) Fund cash balance decreased by \$185,980 to a year-end balance of \$34,084 on June 30, 2006. Disbursements related to street projects mentioned in the LOST ballot increased, specifically the Roche Street Reconstruction Project and the 2006 Street Improvements Project.

- The Urban Renewal Tax Increment Fund cash balance decreased \$2,230 to a year-end balance of \$934,111. Receipts decreased \$21,842 due largely to decreases in tax collections in the Highway 14 Urban Renewal Area TIF. Disbursements decreased \$51,015 as a result of decreased disbursements made under development agreements.
- The Debt Service Fund cash balance decreased by \$1,365,820 to a deficit year-end balance of \$42,721. The cash balance decreased due to refunding note proceeds of \$1,521,950 which were used to advance refund a general obligation bond issue at the crossover date of June 1, 2006.
- The Capital Projects Fund cash balance increased \$1,158 to \$685,058. Receipts increased by \$211,164 as work on the Stepping Stones Day Care Center, funded by a community development block grant, neared completion. Disbursements increased by \$145,618, most of which was for construction costs on the Stepping Stones Day Care Center.

INDIVIDUAL MAJOR BUSINESS TYPE FUND ANALYSIS

- The Sewer Fund cash balance decreased by \$434,830 to a year-end balance of \$3,197,184. In FY2005, the City received \$2,192,065 in bond proceeds while no debt was issued in FY2006. Disbursements increased \$213,270 related, in part, to the 2005 Sewer Rehabilitation project.

BUDGETARY HIGHLIGHTS

Over the course of the year, the City amended its budget one time. The amendment was approved on May 15, 2006. The budget was amended to reflect \$700,500 of road use tax receipts, \$235,000 for local option sales tax and \$100,000 for insurance reimbursements. There were no significant differences between the original and final budgetary amounts for disbursements.

Even with this budget amendment, the City exceeded the budget for the public works, health and social services, community and economic development, debt service and capital projects functions for the year ended June 30, 2006. Significant differences between the final budget and actual disbursements were for the advance refunding of a general obligation bond which was not included in the budget. There were no significant differences between the final budget and actual receipts.

DEBT ADMINISTRATION

At June 30, 2006, the City had \$9,615,341 in bonds and other long-term debt outstanding, compared to \$11,863,737 last year. The chart below segregates the City’s debt into its component parts.

	Outstanding Debt at Year-End	
	June 30,	
	2006	2005
General obligation bonds	\$ 4,275,000	6,140,000
General obligation capital loan notes	2,115,000	2,225,000
Sewer revenue bonds	3,130,000	3,390,000
Capital lease purchase agreement	95,341	108,737
Total	\$ 9,615,341	11,863,737

Debt decreased as a result of refunding older debt issuances.

City debt payments in FY 2006 reduced outstanding debt by \$2,248,396.

The City’s general obligation bond rating changed from A2 to A3 assigned by national rating agencies. 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 \$6,485,341 is significantly below its constitutional debt limit of approximately \$13 million.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES

Formulation of the FY2007 budget was again limited by several realities that hinder the City's fiscal health. The assessment limitation order, commonly known as property tax rollback, which has increased steadily since 1989, continues to erode the City's tax valuation base each year. The City's FY2007 assessed value has decreased \$2.5 million from the FY2006 level, a decrease of 1.64%. The City's General Fund receipts from property tax will decline \$23,302 from FY2006 levels. As a result, there are no new positions or services in the upcoming budget, though the City was able to retain all existing positions and services from FY2006.

Second, Road Use Tax Fund revenues are budgeted to remain consistent in FY2007 and remain insufficient to fund necessary public infrastructure improvements. Fortunately, the combined effects of the Sewer Rehabilitation Program and the local option sales tax enable infrastructure repairs annually.

Third, the State Legislature threatens annually to repeal replacement funding to cities for monies and credits provided to taxpayers. Should this threat of elimination materialize, certain City services would likely be jeopardized. There is nothing the City can do to proactively place itself a safe distance from this threat.

The FY2007 budget contains total receipts of \$6,559,353 and disbursements of \$7,392,002. This budget contains a number of "one-time" components, including:

- Disbursement of the \$2.2 million in sewer bond proceeds, issued in FY05, to equip the wastewater plant with a Supervisory Control and Data Acquisition (SCADA) system to electronically monitor the sewer system and to construct the Westside Sanitary Sewer Project.
- The local option sales tax collection will continue to be used for referendum identified street improvement projects, including reconstruction of the Dayton Street project. An 80% Surface Transportation Plan (20% local match) grant will be obtained to help finance this project.

The FY2007 budget contains debt service payments of \$1,274,613, comprising six separate bond and note issues. This represents a \$4,737 decrease.

The FY2007 levy is \$14.32815 per \$1,000 of assessed valuation, or an increase of \$0.41772 per \$1,000 of assessed valuation over that of FY2006. The City has reached its General Fund levy limit of \$8.10 per \$1,000 of assessed valuation and its Emergency Fund levy limit of \$0.27 per \$1,000 of assessed valuation. Special Revenue Fund levies have long been in place to support employee benefit costs.

These parameters were taken into account when adopting the budget for FY2007.

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 Dick Schrad, City Manager, 305 S. Third Street, Knoxville, IA 50138.

Basic Financial Statements

City of Knoxville

Statement of Activities and Net Assets – Cash Basis

As of and for the year ended June 30, 2006

	Disbursements	Program Receipts		
		Charges for Service	Operating Grants, Contributions and Restricted Interest	Capital Grants, Contributions and Restricted Interest
Functions/Programs:				
Governmental activities:				
Public safety	\$ 1,126,278	246,515	92,412	-
Public works	687,467	4,699	647,283	-
Health and social services	14,307	34,331	763	-
Culture and recreation	872,086	242,711	54,922	-
Community and economic development	146,308	23,366	380,699	-
General government	474,939	52,282	6,117	-
Debt service	2,507,606	-	71,040	-
Capital projects	1,333,908	-	-	263,812
Total governmental activities	7,162,899	603,904	1,253,236	263,812
Business type activities:				
Sewer	2,056,760	1,754,236	106,752	-
Airport	272,413	-	154,964	80,136
Total business type activities	2,329,173	1,754,236	261,716	80,136
Total	\$ 9,492,072	2,358,140	1,514,952	343,948
General Receipts:				
Property and other city tax levied for:				
General purposes				
Tax increment financing				
Debt service				
Local option sales tax				
Unrestricted interest on investments				
Sale of real property				
Miscellaneous				
Transfers				
Total general receipts and transfers				
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				
Local option sales tax				
Urban renewal tax increment				
Debt service				
Capital projects				
Customer deposits				
Senior Citizens				
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
(787,351)	-	(787,351)
(35,485)	-	(35,485)
20,787	-	20,787
(574,453)	-	(574,453)
257,757	-	257,757
(416,540)	-	(416,540)
(2,436,566)	-	(2,436,566)
(1,070,096)	-	(1,070,096)
(5,041,947)	-	(5,041,947)
-	(195,772)	(195,772)
-	(37,313)	(37,313)
-	(233,085)	(233,085)
(5,041,947)	(233,085)	(5,275,032)
1,810,354	-	1,810,354
368,655	-	368,655
498,679	-	498,679
653,652	-	653,652
60,929	15,499	76,428
12,500	-	12,500
23,642	-	23,642
142,679	(142,679)	-
3,571,090	(127,180)	3,443,910
(1,470,857)	(360,265)	(1,831,122)
5,060,196	3,671,252	8,731,448
\$ 3,589,339	3,310,987	6,900,326
\$ 179,679	-	179,679
34,084	-	34,084
934,111	-	934,111
-	1,867,653	1,867,653
685,058	-	685,058
-	42,432	42,432
20,787	-	20,787
799,734	-	799,734
935,886	1,400,902	2,336,788
\$ 3,589,339	3,310,987	6,900,326

City of Knoxville

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

As of and for the year ended June 30, 2006

	Special Revenue			
	General	Road Use Tax	Local Option Sales Tax	Urban Renewal Tax Increment
Receipts:				
Property tax	\$ 1,222,722	-	-	-
Tax increment financing	-	-	-	368,655
Other city tax	148,211	-	653,652	-
Licenses and permits	49,200	-	-	-
Use of money and property	109,197	-	-	-
Intergovernmental	98,300	647,282	263,812	-
Charges for service	439,924	-	-	-
Miscellaneous	50,095	-	-	-
Total receipts	2,117,649	647,282	917,464	368,655
Disbursements:				
Operating:				
Public safety	940,760	-	-	-
Public works	101,757	655,609	-	-
Health and social services	14,307	-	-	-
Culture and recreation	847,469	-	-	-
Community and economic development	140,252	-	-	-
General government	381,819	35,648	-	-
Debt service	-	-	-	177,737
Capital projects	-	-	1,103,444	-
Total disbursements	2,426,364	691,257	1,103,444	177,737
Excess (deficiency) of receipts over (under) disbursements	(308,715)	(43,975)	(185,980)	190,918
Other financing sources (uses):				
Sale of real property	12,500	-	-	-
Operating transfers in	424,558	-	-	-
Operating transfers out	(73,335)	-	-	(193,148)
Total other financing sources (uses)	363,723	-	-	(193,148)
Net change in cash balances	55,008	(43,975)	(185,980)	(2,230)
Cash balances beginning of year	219,122	223,654	220,064	936,341
Cash balances end of year	\$ 274,130	179,679	34,084	934,111
Cash Basis Fund Balances				
Reserved for Senior Citizens	\$ 20,787	-	-	-
Unreserved:				
General fund	253,343	-	-	-
Special revenue funds	-	179,679	34,084	934,111
Capital projects fund	-	-	-	-
Debt service fund	-	-	-	-
Permanent funds	-	-	-	-
Total cash basis fund balances	\$ 274,130	179,679	34,084	934,111

See notes to financial statements.

Debt Service	Capital Projects	Nonmajor	Total
482,469	-	424,202	2,129,393
-	-	-	368,655
16,210	-	15,219	833,292
-	-	-	49,200
71,268	20	11,267	191,752
-	380,699	-	1,390,093
-	-	-	439,924
-	1,653	49,506	101,254
569,947	382,372	500,194	5,503,563
-	-	146,971	1,087,731
-	-	-	757,366
-	-	-	14,307
-	-	18,022	865,491
-	4,750	-	145,002
-	-	-	417,467
2,329,869	-	-	2,507,606
-	376,464	-	1,479,908
2,329,869	381,214	164,993	7,274,878
(1,759,922)	1,158	335,201	(1,771,315)
-	-	-	12,500
394,102	-	60	818,720
-	-	(409,558)	(676,041)
394,102	-	(409,498)	155,179
(1,365,820)	1,158	(74,297)	(1,616,136)
1,323,099	683,900	874,031	4,480,211
(42,721)	685,058	799,734	2,864,075
-	-	-	20,787
-	-	-	253,343
-	-	602,872	1,750,746
-	685,058	-	685,058
(42,721)	-	-	(42,721)
-	-	196,862	196,862
(42,721)	685,058	799,734	2,864,075

City of Knoxville

City of Knoxville

Reconciliation of the Statement of Cash
Receipts, Disbursements and Changes in Cash Balances
to the Statement of Activities and Net Assets -
Governmental Funds

As of and for the year ended June 30, 2006

Total governmental funds cash balances (page 17) \$ 2,864,075

Amounts reported for governmental activities in the Statement of Activities and Net Assets are different because:

The Internal Service Funds are used by management to charge the costs of equipment and building replacement to individual funds. A portion of the assets of the Internal Service Funds are included in governmental activities in the Statement of Activities and Net Assets.

725,264

Cash basis net assets of governmental activities (page 15)

\$ 3,589,339

Net change in cash balances (page 17)

\$ (1,616,136)

Amounts reported for governmental activities in the Statement of Activities and Net Assets are different because:

The Internal Service Funds are used by management to charge the costs of equipment and building replacement to individual funds. A portion of the change in net assets of the Internal Service Funds is reported in governmental activities in the Statement of Activities and Net Assets.

145,279

Change in cash basis net assets of governmental activities (page 15)

\$ (1,470,857)

See notes to financial statements.

Exhibit D

City of Knoxville

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

As of and for the year ended June 30, 2006

	Enterprise			Internal Service
	Sewer	Nonmajor Airport	Total	
Operating receipts:				
Charges for service	\$ 1,739,596	-	1,739,596	296,976
Miscellaneous	14,640	-	14,640	-
Total operating receipts	1,754,236	-	1,754,236	296,976
Operating disbursements:				
Governmental activities:				
Public safety	-	-	-	38,547
Public works	-	-	-	18,869
Culture and recreation	-	-	-	6,595
Community and economic development	-	-	-	1,306
General government	-	-	-	57,472
Business type activities	1,657,858	272,413	1,930,271	11,009
Total operating disbursements	1,657,858	272,413	1,930,271	133,798
Excess (deficiency) of operating receipts over (under) operating disbursements	96,378	(272,413)	(176,035)	163,178
Non-operating receipts (disbursements):				
Intergovernmental	500	102,886	103,386	-
Interest on investments	121,751	39,536	161,287	9,658
Insurance reimbursement	-	91,805	91,805	-
Sale of equipment	-	-	-	11,046
Miscellaneous	-	873	873	-
Debt service	(437,505)	-	(437,505)	-
Total non-operating receipts (disbursements)	(315,254)	235,100	(80,154)	20,704
Excess (deficiency) of receipts over (under) disbursements	(218,876)	(37,313)	(256,189)	183,882
Transfers:				
Operating transfers in	-	73,275	73,275	-
Operating transfers out	(215,954)	-	(215,954)	-
Total transfers	(215,954)	73,275	(142,679)	-
Net change in cash balances	(434,830)	35,962	(398,868)	183,882
Cash balances beginning of year	3,632,014	(93,773)	3,538,241	712,996
Cash balances end of year	\$ 3,197,184	(57,811)	3,139,373	896,878
Cash Basis Fund Balances				
Reserved for:				
Debt service	\$ 1,867,653	-	1,867,653	-
Customer deposits	42,432	-	42,432	-
Unreserved	1,287,099	(57,811)	1,229,288	896,878
Total cash basis fund balances	\$ 3,197,184	(57,811)	3,139,373	896,878

See notes to financial statements.

City of Knoxville

Reconciliation of the Statement of Cash Receipts, Disbursements
and Changes in Cash Balances
to the Statement of Activities and Net Assets –
Proprietary Funds

As of and for the year ended June 30, 2006

Total enterprise funds cash balances (page 20) \$ 3,139,373

Amounts reported for business type activities in the Statement of Activities and Net Assets are different because:

The Internal Service Funds are used by management to charge the costs of equipment and building replacement to individual funds. A portion of the assets of the Internal Service Funds are included in business type activities in the Statement of Activities and Net Assets.

171,614

Cash basis net assets of business type activities (page 15)

\$ 3,310,987

Net change in cash balances (page 20)

\$ (398,868)

Amounts reported for business type activities in the Statement of Activities and Net Assets are different because:

The Internal Service Funds are used by management to charge the costs of equipment and building replacement to individual funds. A portion of the change in net assets of the Internal Service Funds is reported in business type activities in the Statement of Activities and Net Assets.

38,603

Change in cash basis net assets of business type activities (page 15)

\$ (360,265)

See notes to financial statements.

City of Knoxville

Notes to Financial Statements

June 30, 2006

(1) Summary of Significant Accounting Policies

The City of Knoxville is a political subdivision of the State of Iowa located in Marion County. It was first incorporated in 1853 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 sewer utilities for its citizens.

A. Reporting Entity

Except as discussed below, for financial reporting purposes, the City of Knoxville 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 Knoxville (the primary government) and exclude the City's component unit. The component unit discussed below is not included in the City's reporting entity although its operational or financial relationship with the city is significant.

Excluded Component Unit

The Knoxville Municipal Waterworks was established under Chapter 388 of the Code of Iowa, is legally separate from the City, but has the potential to provide specific benefits to or impose specific burdens on the City. The Municipal Waterworks is governed by a three-member board appointed by the Mayor and approved by the City Council. The Waterworks' operating budget is subject to the approval of the City Council. Complete financial statements of the component unit, which will issue separate financial statements, can be obtained from the Municipal Waterworks administrative office.

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: Marion County Assessor's Conference Board, Marion County Emergency Management Commission, Marion County Joint E911 Service Board, Marion County/Warren County Drug Task Force and Central Iowa Regional Transportation Planning Alliance.

Related Organization

The City Council Members are also responsible for appointing the members of the Low Rent Housing Board, but the City's accountability for this organization does not extend beyond making the appointments.

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.

Special Revenue:

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

The Local Option Sales Tax Fund is used to account for local option sales tax and related construction projects authorized by the local option sales tax resolution.

The Urban Renewal Tax Increment Fund is used to account for urban renewal projects financed by tax increment financing.

The Debt Service Fund is utilized to account for the payment of interest and principal on the City's general long-term debt.

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

The City reports the following major proprietary fund:

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

The City also reports the following proprietary funds:

The Airport Fund accounts for the operation and maintenance of the City's airport system.

Internal Service Funds are utilized to account for the financing of goods or services purchased by one department of the City and provided to other departments or agencies on a cost reimbursement basis.

C. Measurement Focus and Basis of Accounting

The City of Knoxville 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 incurred, 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, 2006, disbursements exceeded the amounts budgeted in the public works, health and social services, community and economic development, debt service and capital projects functions.

(2) Cash and Pooled Investments

The City's deposits in banks at June 30, 2006 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.

At June 30, 2006, the City had investments in the Iowa Public Agency Investment Trust which are valued at an amortized cost of \$1,106,695 pursuant to Rule 2a-7 under the Investment Company Act of 1940. The City's investment in the Iowa Public Agency Investment Trust is unrated.

(3) Bonds Payable

Annual debt service requirements to maturity for general obligation bonds, capital loan notes and revenue bonds are as follows:

Year Ending June 30,	General Obligation							
	Bonds		Capital Loan Notes		Sewer Revenue Bonds		Total	
	Principal	Interest	Principal	Interest	Principal	Interest	Principal	Interest
2007	\$ 345,000	191,000	270,000	72,224	265,000	129,089	880,000	392,313
2008	355,000	176,510	280,000	63,024	270,000	119,866	905,000	359,400
2009	375,000	161,403	290,000	53,999	285,000	110,159	950,000	325,561
2010	390,000	145,028	295,000	44,573	300,000	99,424	985,000	289,025
2011	240,000	127,737	340,000	34,936	310,000	87,761	890,000	250,434
2012 - 2016	1,380,000	475,110	640,000	45,605	1,420,000	247,573	3,440,000	768,288
2017 - 2020	1,190,000	131,270	-	-	280,000	13,160	1,470,000	144,430
Total	\$ 4,275,000	1,408,058	2,115,000	314,361	3,130,000	807,032	9,520,000	2,529,451

The Code of Iowa requires principal and interest on general obligation bonds be paid from the Debt Service Fund. However, during the year, \$39,821 of general obligation bond interest was paid from the Enterprise, Sewer Fund.

Sewer Revenue Bonds

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

- (a) The bonds will only be redeemed from the future earnings of the enterprise activity and the bond holders hold a lien on the future earnings of the funds.
- (b) Sufficient monthly transfers shall be made to a sewer revenue bond sinking account for the purpose of making the bond principal and interest payments when due.
- (c) Additional monthly transfers shall be made to a sewer revenue reserve account until a specific minimum balance has been accumulated. This account is restricted for the purpose of paying, at maturity, principal or interest on the bonds when insufficient money shall be available in the sinking account.
- (d) Sewer user rates shall be established at a level which produces and maintains net revenues at a level not less than 110% of the amount of principal and interest on the bonds falling due in the same year.

Capital Lease Purchase Agreement

The City entered into a capital lease purchase agreement to lease a rescue vehicle. The following is a schedule of the future minimum lease payments, including interest at 4.8% per annum, and the present value of net minimum lease payments under the agreement in effect at June 30, 2006:

Year Ending June 30,	Amount
2007	\$ 18,724
2008	18,724
2009	18,724
2010	18,724
2011	18,724
2012	18,723
Total minimum lease payments	112,343
Less amount representing interest	(17,002)
Present value of net minimum lease payments	<u>\$ 95,341</u>

Payments under the capital lease purchase agreement totaled \$18,724 during the year ended June 30, 2006.

(4) Pension and Retirement Benefits

Iowa Public Employees Retirement System

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. Employees in special risk occupations and the City contribute an actuarially determined contribution rate. Contribution requirements are established by state statute. The City's contributions to IPERS for the years ended June 30, 2006, 2005 and 2004 were \$63,362, \$68,480 and \$66,147, respectively, equal to the required contributions for each year.

Municipal Fire and Police Retirement System of Iowa

The City contributes to the Municipal Fire and Police Retirement System of Iowa (the Plan), which is a cost-sharing multiple-employer defined benefit pension plan administered by a Board of Trustees. The Plan provides retirement, disability and death benefits which are established by state statute to plan members and beneficiaries. The Plan issues a publicly available financial report that includes financial statements and required supplementary information. The report may be obtained by writing to Municipal Fire and Police Retirement System of Iowa, 2836 104th St., Urbandale, Iowa 50322.

Plan members are required to contribute 9.35% of earnable compensation and the City's contribution rate, based upon an actuarially determined normal contribution rate, can not be less than 17% of earnable compensation. Contribution requirements are established by state statute. The City's contributions to the Plan for the years ended June 30, 2006, 2005 and 2004 were \$134,773, \$127,596 and \$90,674, respectively, which met the required minimum contribution for each year.

(5) Compensated Absences

City employees accumulate a limited amount of earned but unused holiday and vacation hours for subsequent use or for payment upon termination, retirement or death. City employees may also accumulate a limited amount of earned but unused sick leave hours for payment of subsequent health benefit costs upon retirement. The City also allows employees to accumulate compensatory time during the fiscal year in lieu of overtime pay. These accumulations are not recognized as disbursements by the City until used or paid. The City's approximate liability for earned holiday, vacation, sick leave and compensatory time payable to employees at June 30, 2006, primarily relating to the General Fund, is as follows:

Type of Benefit	Amount
Holiday	\$ 12,000
Vacation	90,000
Sick leave	39,000
Compensatory time	<u>15,000</u>
Total	<u>\$ 156,000</u>

This liability has been computed based on rates of pay in effect at June 30, 2006.

(6) Interfund Transfers

The detail of interfund transfers for the year ended June 30, 2006 is as follows:

Transfer to	Transfer from	Amount
General	Special Revenue:	
	Liability, Property and Self Insurance	\$ 65,983
	Employee Benefits - Health	192,758
	FICA and IPERS Benefits	99,853
	Emergency	41,726
	Hotel Motel Sales Tax	9,238
	Enterprise:	
	Sewer	15,000
		<u>424,558</u>
Special Revenue:		
Aquatic Park Trust	General	60
Debt Service	Special Revenue:	
	Urban Renewal Tax Increment	193,148
	Enterprise:	
	Sewer	200,954
		<u>394,102</u>
Enterprise:		
Airport	General	73,275
Total		<u>\$ 891,995</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 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 531 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 member 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, 2006 were \$143,834.

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 \$2,000,000 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 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 exhausts total members' equity plus any reinsurance and any excess risk-sharing recoveries, then payment of such claims shall be the obligation of the respective individual member. As of June 30, 2006, 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 member's 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.

The City also carries commercial insurance purchased from other insurers for coverage associated with workers compensation, employee blanket bond, boiler and machinery and aviation liability. The City assumes liability for any deductibles and claims in excess of coverage limitations. The City assumes responsibility for workers compensation, employee blanket bond, and aviation liability claims in excess of \$1,000,000, \$75,000 and \$2,000,000, respectively. Settled claims resulting from these risks have not exceeded commercial insurance coverage in any of the past three fiscal years.

(8) Deficit Balances

At June 30, 2006, the City had deficit balances in the following funds:

Fund	Amount
Debt Service	\$ (42,721)
Enterprise:	
Airport	(57,811)

The City is reviewing alternatives to eliminate these deficits.

(9) Construction Commitments

The City has entered into construction contracts totaling \$4,731,370. As of June 30, 2006, costs of \$2,607,236 had been paid on the contracts. The remaining \$2,124,134 will be paid as work on these projects progresses.

(10) Interfund Receivable/Payable

In prior years, the General Fund loaned the Special Revenue, Urban Renewal Tax Increment Fund \$85,251 to pay for principal and interest due on the general obligation bonds prior to the collection of tax increment financing receipts. The loan is to be repaid, without interest, as tax increment financing receipts are collected. No payments were made during the year ended June 30, 2006.

(11) Economic Development Loans

On February 2, 2000, the City loaned \$25,000 to the Knoxville Chamber of Commerce to assist in funding a local business expansion. The interest free loan is to be repaid over five years. During the year ended June 30, 2006, no payment was received on the loan. The loan balance at June 30, 2006 was \$15,000.

(12) Community Economic Betterment Account Loan

On December 16, 2004, the City was awarded a \$200,000 Community Economic Betterment Account loan on behalf of Ultimate Truck Body from the Iowa Department of Economic Development. The loan consists of a \$50,000 conventional interest free loan and a \$150,000 forgivable loan. Repayment of the conventional loan is to be made in 48 equal monthly payments of \$1,042, with the first payment due on August 1, 2006. The balance outstanding on the conventional loan at June 30, 2006 was \$50,000. At the project completion date, if the business has fulfilled at least 50% of its job creation/retention requirement, \$3,409 will be forgiven for each new job created/retained for at least ninety days past the project completion date. Any balance will be amortized over a two year period in equal monthly payments, with 6% per annum interest.

(13) Development and Rebate Agreements

In prior years, the City entered into three development and rebate agreements to assist in certain urban renewal projects. The City agreed to rebate incremental taxes paid by the developers in exchange for infrastructure improvements, rehabilitation and development of commercial projects constructed by the developers as set forth in the urban renewal plan and the individual development and rebate agreements. The incremental taxes to be received by the City under Chapter 403.19 of the Code of Iowa from the developers will be rebated for a period ranging from ten to twenty years, beginning with the tax year in which the property taxes on the completed value of the improvements are first paid. The total amount to be rebated under the development and rebate agreement is not to exceed amounts ranging from \$85,931 to \$2,387,811. Certain agreements include provisions for payment of interest.

During the year ended June 30, 2006, the City rebated \$177,737 of incremental taxes to the developers, consisting of \$49,269 for principal and \$128,469 for interest. The outstanding principal balance on these agreements at June 30, 2006 is \$2,457,518.

No bonds or notes were issued for these projects. To the extent there are insufficient incremental taxes available on any payment date to make the required scheduled payment, the unpaid amount shall be carried over to the next payment date without accruing any further interest.

These agreements are not a general obligation of the City. However, the debt payment in the succeeding year is subject to the constitutional debt limitation of the City.

(14) Litigation

The City is subject to pending litigation. The probability of loss, if any, is undeterminable.

(15) Contingent Liability

In May 2000, the City entered into an agreement with Wal-Mart. In return for the construction of public improvements, the City would pay \$880,000 to Wal-Mart. As of June 30, 2006, Wal-Mart had not completed the public improvements to the City's specifications. The City anticipates paying Wal-Mart during fiscal year 2007 from the Special Revenue, Urban Renewal Tax Increment Fund.

(16) Employee Health Insurance Plan

The City established the Internal Service, Self Insurance Fund to account for the partial self funding of the City's health insurance benefit plan. The plan is funded by City contributions and is administered by Group Services, Inc. The City assumes liability for claims between \$250 and \$2,500 for single coverage and \$500 and \$5,000 for family coverage. Claims in excess of the deductible are insured through the purchase of insurance.

Payments to the Self Insurance Fund were recorded as disbursements by the operating funds. Payments to Group Services, Inc. for service fees and medical claims for the year ended June 30, 2006 were \$2,643.

City of Knoxville

Required Supplementary Information

City of Knoxville
 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, 2006

	Governmental Funds Actual	Proprietary Funds Actual	Less Funds not Required to be Budgeted
Receipts:			
Property tax	\$ 2,129,393	-	-
Tax increment financing	368,655	-	-
Other city tax	833,292	-	-
Licenses and permits	49,200	-	-
Use of money and property	191,752	170,945	9,658
Intergovernmental	1,390,093	103,386	-
Charges for service	439,924	2,047,618	308,022
Special assessments	-	-	-
Miscellaneous	101,254	107,318	-
Total receipts	5,503,563	2,429,267	317,680
Disbursements:			
Public safety	1,087,731	38,547	38,547
Public works	757,366	18,869	18,869
Health and social services	14,307	-	-
Culture and recreation	865,491	6,595	6,595
Community and economic development	145,002	1,306	1,306
General government	417,467	57,472	57,472
Debt service	2,507,606	-	-
Capital projects	1,479,908	-	-
Business type activities	-	2,378,785	11,009
Total disbursements	7,274,878	2,501,574	133,798
Excess (deficiency) of receipts over (under) disbursements	(1,771,315)	(72,307)	183,882
Other financing sources (uses), net	155,179	(142,679)	-
Excess (deficiency) of receipts and other financing sources over (under) disbursements and other financing uses	(1,616,136)	(214,986)	183,882
Balances beginning of year	4,480,211	4,251,237	712,996
Balances end of year	\$ 2,864,075	4,036,251	896,878

See accompanying independent auditor's report.

Total	Budgeted Amounts		Final to Total Variance
	Original	Final	
2,129,393	2,135,221	2,134,221	(4,828)
368,655	325,316	357,316	11,339
833,292	608,451	843,451	(10,159)
49,200	44,230	44,230	4,970
353,039	59,880	219,880	133,159
1,493,479	793,900	1,494,400	(921)
2,179,520	2,299,275	1,999,275	180,245
-	-	2,000	(2,000)
208,572	132,268	291,930	(83,358)
<u>7,615,150</u>	<u>6,398,541</u>	<u>7,386,703</u>	<u>228,447</u>
1,087,731	1,110,385	1,117,385	29,654
757,366	659,507	704,707	(52,659)
14,307	-	-	(14,307)
865,491	860,731	923,919	58,428
145,002	127,962	144,642	(360)
417,467	403,095	417,827	360
2,507,606	1,051,934	1,051,934	(1,455,672)
1,479,908	1,243,023	1,243,023	(236,885)
2,367,776	3,313,685	3,413,685	1,045,909
<u>9,642,654</u>	<u>8,770,322</u>	<u>9,017,122</u>	<u>(625,532)</u>
(2,027,504)	(2,371,781)	(1,630,419)	(397,085)
12,500	-	-	12,500
(2,015,004)	(2,371,781)	(1,630,419)	(384,585)
8,018,452	3,734,656	8,191,546	(173,094)
<u>6,003,448</u>	<u>1,362,875</u>	<u>6,561,127</u>	<u>(557,679)</u>

City of Knoxville

Notes to Required Supplementary Information – Budgetary Reporting

June 30, 2006

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 except Internal Service Funds and Fiduciary 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 and business type activities. Function disbursements required to be budgeted include disbursements for the General Fund, the Special Revenue Funds, the Debt Service Fund, the Capital Projects Fund, the Permanent Funds and the Enterprise 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 \$246,800. The budget amendment is reflected in the final budgeted amounts.

During the year ended June 30, 2006, disbursements exceeded the amounts budgeted in the public works, health and social services, community and economic development, debt service and capital projects functions.

Other Supplementary Information

City of Knoxville

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

As of and for the year ended June 30, 2006

						Special	
	Liability, Property and Self-Insurance	Employee Benefits - Health	FICA and IPERS Benefits	Police Retirement	Emergency	Hotel Motel Sales Tax	Urban Revitalization
Receipts:							
Property tax	\$ 76,594	198,572	108,316	-	40,720	-	-
Other city tax	2,751	7,121	3,884	-	1,463	-	-
Use of money and property	-	-	-	7,939	-	-	-
Miscellaneous	-	-	-	-	-	-	-
Total receipts	79,345	205,693	112,200	7,939	42,183	-	-
Disbursements:							
Operating:							
Public safety	-	-	-	134,773	-	-	-
Culture and recreation	-	-	-	-	-	-	-
Total disbursements	-	-	-	134,773	-	-	-
Excess (deficiency) of receipts over (under) disbursements	79,345	205,693	112,200	(126,834)	42,183	-	-
Other financing sources (uses):							
Operating transfers in	-	-	-	-	-	-	-
Operating transfers out	(65,983)	(192,758)	(99,853)	-	(41,726)	(9,238)	-
Total other financing sources (uses)	(65,983)	(192,758)	(99,853)	-	(41,726)	(9,238)	-
Net change in cash balances	13,362	12,935	12,347	(126,834)	457	(9,238)	-
Cash balances beginning of year	17,562	3,354	14,898	312,377	19,989	9,238	3,956
Cash balances end of year	\$ 30,924	16,289	27,245	185,543	20,446	-	3,956
Cash Basis Fund Balances							
Unreserved:							
Special revenue funds	\$ 30,924	16,289	27,245	185,543	20,446	-	3,956
Permanent funds	-	-	-	-	-	-	-
Total cash basis fund balances	\$ 30,924	16,289	27,245	185,543	20,446	-	3,956

See accompanying independent auditor's report.

Revenue									Permanent		
Revolving Loan	Self-Supported Municipal Improvement District	Police Department Trust	Rescue Donations	Library Gifts/Memorials	Recreation Donations	Auld Park Playground Trust	Aquatic Park Trust	Cemetery Perpetual Care	Reaver Trust	Total	
-	-	-	-	-	-	-	-	-	-	424,202	
-	-	-	-	-	-	-	-	-	-	15,219	
-	-	322	584	1,394	-	652	-	376	-	11,267	
-	-	21,790	1,202	19,331	-	-	-	7,183	-	49,506	
-	-	22,112	1,786	20,725	-	652	-	7,559	-	500,194	
-	-	2,190	10,008	-	-	-	-	-	-	146,971	
-	-	-	-	17,782	240	-	-	-	-	18,022	
-	-	2,190	10,008	17,782	240	-	-	-	-	164,993	
-	-	19,922	(8,222)	2,943	(240)	652	-	7,559	-	335,201	
-	-	-	-	-	-	-	60	-	-	60	
-	-	-	-	-	-	-	-	-	-	(409,558)	
-	-	-	-	-	-	-	60	-	-	(409,498)	
-	-	19,922	(8,222)	2,943	(240)	652	60	7,559	-	(74,297)	
161,203	1	9,981	41,831	50,335	7,167	32,896	(60)	188,803	500	874,031	
161,203	1	29,903	33,609	53,278	6,927	33,548	-	196,362	500	799,734	
161,203	1	29,903	33,609	53,278	6,927	33,548	-	-	-	602,872	
-	-	-	-	-	-	-	-	196,362	500	196,862	
161,203	1	29,903	33,609	53,278	6,927	33,548	-	196,362	500	799,734	

City of Knoxville

City of Knoxville

Statement of Cash Receipts, Disbursements
and Changes in Cash Balances
Internal Service Funds

As of and for the year ended June 30, 2006

	Equipment Replacement	Building Replacement	Self Insurance	Total
Operating receipts:				
Charges for service	\$ 284,380	-	12,596	296,976
Operating disbursements:				
Governmental activities:				
Public safety	38,547	-	-	38,547
Public works	18,869	-	-	18,869
Culture and recreation	6,595	-	-	6,595
Community and economic development	1,306	-	-	1,306
General government	28,513	26,316	2,643	57,472
Business type activities:				
Sewer	11,009	-	-	11,009
Total operating disbursements	104,839	26,316	2,643	133,798
Excess (deficiency) of operating receipts over (under) operating disbursements	179,541	(26,316)	9,953	163,178
Non-operating receipts:				
Interest on investments	9,658	-	-	9,658
Sale of equipment	11,046	-	-	11,046
Total non-operating receipts	20,704	-	-	20,704
Excess (deficiency) of receipts over (under) disbursements	200,245	(26,316)	9,953	183,882
Cash balances beginning of year	676,654	36,342	-	712,996
Cash balances end of year	\$ 876,899	10,026	9,953	896,878
Cash Basis Fund Balances				
Unreserved	\$ 876,899	10,026	9,953	896,878

See accompanying independent auditor's report.

City of Knoxville
Schedule of Indebtedness
Year ended June 30, 2006

Obligation	Date of Issue	Interest Rates	Amount Originally Issued
General obligation bonds:			
Corporate purpose	Apr 1, 1997	4.65 - 5.30%	\$ 1,875,000
General corporate purpose	May 1, 2000	5.05 - 5.70	3,230,000
Essential corporate purpose	Jan 15, 2005	2.25 - 4.30	2,200,000
Total			
General obligation capital loan notes:			
General corporate purpose	May 1, 2005	2.70 - 3.90%	\$ 700,000
General obligation refunding	May 1, 2005	3.25 - 4.00	1,525,000
Total			
Revenue bonds:			
Sewer	Mar 1, 2002	3.875 - 4.70%	\$ 3,000,000
Sewer refunding	Nov 17, 2003	1.50 - 4.00	995,000
Total			
Capital lease purchase agreement:			
Rescue vehicle	Aug 24, 2004	4.80%	\$ 108,737

See accompanying independent auditor's report.

Balance Beginning of Year	Issued During Year	Redeemed During Year	Balance End of Year	Interest Paid
1,530,000	-	1,530,000	-	80,930
2,410,000	-	220,000	2,190,000	126,855
2,200,000	-	115,000	2,085,000	77,843
<u>\$ 6,140,000</u>	<u>-</u>	<u>1,865,000</u>	<u>4,275,000</u>	<u>285,628</u>
700,000	-	40,000	660,000	26,525
1,525,000	-	70,000	1,455,000	55,920
<u>\$ 2,225,000</u>	<u>-</u>	<u>110,000</u>	<u>2,115,000</u>	<u>82,445</u>
2,570,000	-	165,000	2,405,000	111,224
820,000	-	95,000	725,000	26,460
<u>\$ 3,390,000</u>	<u>-</u>	<u>260,000</u>	<u>3,130,000</u>	<u>137,684</u>
<u>108,737</u>	<u>-</u>	<u>13,396</u>	<u>95,341</u>	<u>5,328</u>

City of Knoxville
Bond and Note Maturities

June 30, 2006

General Obligation Bonds							
Year Ending June 30,	Corporate Purpose Issued May 1, 2000			Essential Corporate Purpose Issued Jan 15, 2005		Total	
	Interest		Amount	Interest			
	Rates	Amount		Rates	Amount		
2007	5.05%	\$	230,000	2.50%	\$	115,000	345,000
2008	5.05		235,000	2.70		120,000	355,000
2009	5.10		250,000	2.90		125,000	375,000
2010	5.10		260,000	3.10		130,000	390,000
2011	5.15		110,000	3.25		130,000	240,000
2012	5.20		115,000	3.40		135,000	250,000
2013	5.25		120,000	3.50		145,000	265,000
2014	5.35		125,000	3.70		150,000	275,000
2015	5.45		135,000	3.80		155,000	290,000
2016	5.50		140,000	3.90		160,000	300,000
2017	5.60		150,000	4.00		170,000	320,000
2018	5.65		155,000	4.10		175,000	330,000
2019	5.70		165,000	4.20		185,000	350,000
2020			-	4.30		190,000	190,000
Total		\$	<u>2,190,000</u>		\$	<u>2,085,000</u>	<u>4,275,000</u>

General Obligation Capital Loan Notes							
Year Ending June 30,	General Corporate Purpose Issued May 1, 2005			General Obligation Refunding Issued May 1, 2005		Total	
	Interest		Amount	Interest			
	Rates	Amount		Rates	Amount		
2007	3.00%	\$	50,000	3.500%	\$	220,000	270,000
2008	3.10		50,000	3.250		230,000	280,000
2009	3.25		50,000	3.250		240,000	290,000
2010	3.35		50,000	3.250		245,000	295,000
2011	3.50		85,000	3.375		255,000	340,000
2012	3.60		90,000	3.500		265,000	355,000
2013	3.70		90,000			-	90,000
2014	3.80		95,000			-	95,000
2015	3.90		100,000			-	100,000
Total		\$	<u>660,000</u>		\$	<u>1,455,000</u>	<u>2,115,000</u>

See accompanying independent auditor's report.

Revenue Bonds					
Sewer Revenue		Sewer Revenue Refunding			
Issued Mar 1, 2002		Issued Nov 17, 2003			
Interest Rates	Amount	Interest Rates	Amount	Total	
4.00%	\$ 170,000	2.55%	\$ 95,000	265,000	
4.00	175,000	2.85	95,000	270,000	
4.10	185,000	3.15	100,000	285,000	
4.15	195,000	3.40	105,000	300,000	
4.15	205,000	3.60	105,000	310,000	
4.25	215,000	3.85	110,000	325,000	
4.37	225,000	4.00	115,000	340,000	
4.50	240,000		-	240,000	
4.55	250,000		-	250,000	
4.65	265,000		-	265,000	
4.70	280,000		-	280,000	
	-		-	-	
	-		-	-	
	-		-	-	
	<u>\$ 2,405,000</u>		<u>\$ 725,000</u>	<u>3,130,000</u>	

Schedule 5

City of Knoxville

Schedule of Receipts by Source and Disbursements by Function
All Governmental Funds

For the Last Four Years

	2006	2005	2004	2003
Receipts:				
Property tax	\$ 2,129,393	1,981,319	2,069,054	2,091,215
Tax increment financing	368,655	390,497	327,032	267,890
Other city tax	833,292	746,387	286,303	131,447
Licenses and permits	49,200	36,614	44,374	54,796
Use of money and property	191,752	48,159	42,281	59,040
Intergovernmental	1,390,093	1,502,408	805,600	1,023,225
Charges for service	439,924	467,822	423,250	316,449
Special assessments	-	-	14,329	5,688
Miscellaneous	101,254	130,398	93,178	166,818
Total	\$ 5,503,563	5,303,604	4,105,401	4,116,568
Disbursements:				
Operating:				
Public safety	\$ 1,087,731	1,173,206	1,143,333	1,246,442
Public works	757,366	713,930	728,691	716,802
Health and social services	14,307	-	-	-
Culture and recreation	865,491	963,405	954,891	998,489
Community and economic development	145,002	325,700	197,729	153,213
General government	417,467	414,694	423,033	394,567
Debt service	2,507,606	913,064	777,558	652,097
Capital projects	1,479,908	1,059,329	99,340	580,020
Total	\$ 7,274,878	5,563,328	4,324,575	4,741,630

See accompanying independent auditor's report.

City of Knoxville
 Schedule of Expenditures of Federal Awards
 Year ended June 30, 2006

Grantor/Program	CFDA Number	Agency Pass-through Number	Program Expenditures
Direct:			
U.S. Department of Transportation: Airport Improvement Program	20.106		\$ 74,928
Indirect:			
U.S. Department of Housing and Urban Development:			
Iowa Department of Economic Development:			
Community Development Block Grants/ State's Program	14.228	02-HSG-017	92,683
Community Development Block Grants/ State's Program	14.228	03-CF-050	285,761
			<u>378,444</u>
U.S. Department of Transportation:			
Iowa Department of Transportation:			
Highway Planning and Construction	20.205		243,158
Iowa Department of Public Safety:			
Alcohol Traffic Safety and Drunk Driving Prevention Incentive Grants	20.601		2,873
Total indirect			<u>624,475</u>
Total			<u>\$ 699,403</u>

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

See accompanying independent auditor's report.

City of Knoxville



OFFICE OF AUDITOR OF STATE
STATE OF IOWA

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

To the Honorable Mayor and
Members of the City Council:

We have audited the accompanying primary government financial statements of the governmental activities, the business type activities, each major fund and the aggregate remaining fund information of the City of Knoxville, Iowa, as of and for the year ended June 30, 2006, which collectively comprise the City's basic financial statements listed in the table of contents, and have issued our report thereon dated August 30, 2006. Our report expressed an unqualified opinion on the primary government 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 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 Knoxville's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinions on the financial statements and not to provide an opinion 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 Knoxville'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 Part II of the accompanying Schedule of Findings and Questioned Costs.

A material weakness is a reportable 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 caused by error or fraud 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 II-A-06, II-C-06, II-D-06 and II-E-06 are material weaknesses.

Compliance and Other Matters

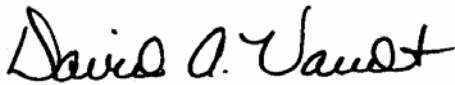
As part of obtaining reasonable assurance about whether the City of Knoxville's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, non-compliance with which could

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 Part IV of the accompanying Schedule of Findings and Questioned Costs.

Comments involving statutory and other legal matters about the City's operations for the year ended June 30, 2006 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.

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 Knoxville and other parties to whom the City of Knoxville may report, including federal awarding agencies and pass-through entities. This report is not intended to be and should not be used by anyone other than these specified parties.

We would like to acknowledge the many courtesies and assistance extended to us by personnel of the City of Knoxville 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 30, 2006



OFFICE OF AUDITOR OF STATE
STATE OF IOWA

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Independent Auditor's Report on Compliance with Requirements
Applicable to Each Major Program and on Internal Control over Compliance
in Accordance with OMB Circular A-133

To the Honorable Mayor and
Members of the City Council:

Compliance

We have audited the compliance of the City of Knoxville, Iowa, with the types of compliance requirements described in U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement that are applicable to its major federal program for the year ended June 30, 2006. The City of Knoxville's major federal program is identified in Part I of the accompanying Schedule of Findings and Questioned Costs. Compliance with the requirements of laws, regulations, contracts and grant agreements applicable to its major federal program is the responsibility of the City of Knoxville's management. Our responsibility is to express an opinion on the City of Knoxville's compliance based on our audit.

We conducted our audit of compliance in accordance with U.S. generally accepted auditing standards, the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States, and OMB Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether non-compliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the City of Knoxville's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on the City of Knoxville's compliance with those requirements.

In our opinion, the City of Knoxville complied, in all material respects, with the requirements referred to above that are applicable to its major federal program for the year ended June 30, 2006.

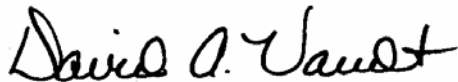
Internal Control Over Compliance

The management of the City of Knoxville is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts and grant agreements applicable to federal programs. In planning and performing our audit, we considered the City of Knoxville's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133.

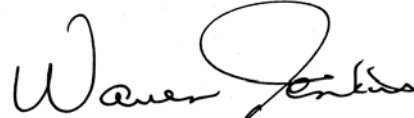
Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be material weaknesses. A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that noncompliance with applicable

requirements of laws, regulations, contracts, and grants caused by error or fraud that would be material in relation to a major federal program being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over compliance and its operation that we consider to be material weaknesses.

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 Knoxville and other parties to whom the City of Knoxville may report, including federal awarding agencies and pass-through entities. This report is not intended to be and should not be used by anyone other than these specified parties.



DAVID A. VAUDT, CPA
Auditor of State



WARREN G. JENKINS, CPA
Chief Deputy Auditor of State

August 30, 2006

City of Knoxville

Schedule of Findings and Questioned Costs

Year ended June 30, 2006

Part I: Summary of the Independent Auditor's Results:

- (a) Unqualified opinions were issued on the financial statements which 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.
- (b) Reportable conditions in internal control over financial reporting were disclosed by the audit of the financial statements, including material weaknesses.
- (c) The audit did not disclose any non-compliance which is material to the financial statements.
- (d) No material weaknesses in internal control over the major program were noted.
- (e) An unqualified opinion was issued on compliance with requirements applicable to the major program.
- (f) The audit disclosed no audit findings which are required to be reported in accordance with Office of Management and Budget Circular A-133, Section .510(a).
- (g) The major program was CFDA Number 14.228 – Community Development Block Grant/State's Program.
- (h) The dollar threshold used to distinguish between Type A and Type B programs was \$300,000.
- (i) The City of Knoxville did not qualify as a low risk auditee.

City of Knoxville

Schedule of Findings and Questioned Costs

Year ended June 30, 2006

Part II: Findings Related to the Financial Statements:

REPORTABLE CONDITIONS:

II-A-06 Segregation of Duties – One important element in designing internal control that safeguards assets and reasonably ensures the reliability of the accounting records is the concept of segregation of duties. When duties are properly segregated, the activities of one employee act as a check of those of another. One person has control over each of the following areas:

- (1) Cash – handling petty cash, reconciling and signing checks.
- (2) Receipts – opening mail, collecting receipts and recording receipts without independent reconciliation of recorded receipts to the deposit.

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 utilizing currently available personnel.

Response – The City has added a full time clerk/receptionist and we will segregate the mail, petty cash and receipting duties to the extent possible with currently existing personnel.

Conclusion – Response accepted.

II-B-06 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:

- Storage of backup tapes/disks off site.
- A disaster recovery plan.

Recommendation – The City should develop written policies addressing the above items in order to improve the City's internal control over computer based systems.

Response – The City currently maintains off-site storage of backup tapes and has a disaster recovery plan utilizing identical software installed in a neighboring City. Formalized declarations of these plans are currently being written.

Conclusion – Response accepted.

City of Knoxville

Schedule of Findings and Questioned Costs

Year ended June 30, 2006

II-C-06 Rescue Billings – One employee is responsible for collecting receipts, recording receipts and maintaining the accounts receivable records. Write-offs of delinquent rescue billings are not approved by an independent person. In addition, an initial listing of receipts is not prepared.

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 utilizing currently available personnel.

Response – We are currently unable to further segregate the accounts receivable functions for rescue billing. We will, however, be providing quarterly reports to the City Council of uncollectible billings, complete with explanations of efforts to collect those accounts, and will request Council authorization to write off those accounts.

Conclusion – Response accepted.

II-D-06 Rescue Billings Reconciliation – The Rescue Department provides billing and collection services for the City's rescue fees. The City does not prepare a reconciliation of rescue billings, collections and delinquencies.

Recommendation – The City should prepare a monthly rescue billing reconciliation report. The report should be reviewed for propriety.

Response – A monthly rescue reconciliation report will be prepared and reviewed by the City Manager.

Conclusion – Response accepted.

II-E-06 Recreation Center – One employee is responsible for opening the mail, collecting receipts, recording receipts and preparing the deposit. In addition, an initial listing of receipts is not prepared.

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 utilizing currently available personnel.

Response – The City is revising its personnel functions at the Recreation Center and these duties will be segregated to the extent possible given the position available.

Conclusion – Response accepted.

II-F-06 Records of Account – The Knoxville Senior Citizen Board and the Knoxville Friends of the Library maintained checking and savings accounts separate from the City Clerk's records. The transactions and the resulting balances were not reported to the Council each month and the transactions were not recorded in the Clerk's records. The City was not able to provide documentation the Knoxville Senior Citizen Board and Knoxville Friends of the Library had obtained separate legal status as of June 30, 2006. This was resolved for audit purposes.

City of Knoxville

Schedule of Findings and Questioned Costs

Year ended June 30, 2006

Recommendation – Chapter 384.20 of the Code of Iowa states, in part, “A city shall keep accounts which show an accurate and detailed statement of all public funds collected, received, or expended for any City purpose.” Until the Knoxville Senior Citizen Board and the Knoxville Friends of the Library demonstrate they are legally separate from the City, the monthly financial transactions should be included in the Clerk’s monthly financial reports.

Response – These are being requested from the Senior Citizen Board and Friends of the Library.

Conclusion – Response accepted.

II-G-06 Records of Account – The Knoxville Fireman’s Association maintained checking and savings accounts separate from the City Clerk’s records. The transactions and the resulting balances were not reported to the Council each month and the transactions were not recorded in the Clerk’s records. The City was not able to provide documentation the Association had obtained separate legal status as of June 30, 2006.

Recommendation – Chapter 384.20 of the Code of Iowa states, in part, “A city shall keep accounts which show an accurate and detailed statement of all public funds collected, received, or expended for any City purpose.” Until the Association demonstrates it is legally separate from the City, the monthly financial transactions should be included in the Clerk’s monthly financial reports.

Response – The Fireman’s Association has provided evidence of a federal employer identification number. We do not, however, have any evidence of IRS Code 501c(3) designation at this time and will continue to request this.

Conclusion – Response acknowledged. The City should continue to request financial information until such time as the Firemen’s Association documents it has obtained non-profit status.

INSTANCES OF NON-COMPLIANCE:

No matters were noted.

City of Knoxville

Schedule of Findings and Questioned Costs

Year ended June 30, 2006

Part III: Findings and Questioned Costs for Federal Awards:

INSTANCE OF NON-COMPLIANCE:

No matters were noted.

REPORTABLE CONDITIONS:

No material weaknesses in internal control over major programs were noted.

City of Knoxville

Schedule of Findings and Questioned Costs

Year ended June 30, 2006

Part IV: Findings Related to Required Statutory Reporting:

IV-A-06 Certified Budget – Disbursements during the year ended June 30, 2006 exceeded the amounts budgeted in the public works, health and social services, community and economic development, debt service and capital projects 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 accordance with Chapter 384.18 of the Code of Iowa before disbursements were allowed to exceed the budget.

Response – In the future, we will amend the budget before it is exceeded.

Conclusion – Response accepted.

IV-B-06 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.

IV-C-06 Travel Expense – No disbursements of City money for travel expenses of spouses of City officials or employees were noted.

IV-D-06 Business Transactions – Business transactions between the City and City officials or employees are detailed as follows:

<u>Name, Title, and Business Connection</u>	<u>Transaction Description</u>	<u>Amount</u>
Craig Kelley, Mayor, owner of Central Iowa Fasteners	Supplies and parts	\$ 278

In accordance with Chapter 362.5(10) of the Code of Iowa, the transactions with the Mayor do not appear to represent a conflict of interest since total transactions were less than \$1,500 during the fiscal year.

IV-E-06 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.

IV-F-06 Council Minutes – No transactions were found we believe should have been approved in the Council minutes but were not.

Although the minutes of Council proceedings were published, certain minutes did not contain a summary of all receipts and disbursements from each fund as required by Chapter 372.13(6) of the Code of Iowa.

City of Knoxville

Schedule of Findings and Questioned Costs

Year ended June 30, 2006

Recommendation – The Council should comply with Chapter 372.13(6) of the Code of Iowa and publish a summary of all receipts and disbursement from each fund.

Response – We will correct this situation.

Conclusion – Response accepted.

IV-G-06 Deposits and Investments – Except as noted below, deposits and investments were in compliance with Chapters 12B and 12C of the Code of Iowa and the City’s investment policy. Interest income from investments made from the Capital Projects Fund and the Enterprise, Sewer Fund have not been credited to these accounts. In accordance with Chapter 12C.9 of the Code of Iowa, interest earned on bond proceeds should be credited to the project fund for which the indebtedness was issued.

Recommendation – The City should comply with Chapter 12C.9 of the Code of Iowa.

Response – This will be corrected in the current budget year.

Conclusion – Response accepted.

IV-H-06 Revenue Bonds – The City has complied with the requirements of the revenue bond resolutions.

IV-I-06 Payment of General Obligation Bonds – Certain general obligation bond interest was paid from the Enterprise, Sewer Fund. Chapter 384.4 of the Code of Iowa states, in part, “Moneys pledged or available to service general obligation bonds, and received from sources other than property tax, must be deposited in the Debt Service Fund.”

Recommendation – The City should transfer from the Enterprise, Sewer Fund to the Debt Service Fund for future funding contributions. Payments of the bonds and interest should then be disbursed from the Debt Service Fund.

Response – This will be corrected in the current budget year.

Conclusion – Response accepted.

IV-J-06 Financial Condition – The City had deficit balances, as follows:

Fund	Balance	
	June 30, 2006	June 30, 2005
Debt Service	\$ (42,721)	1,323,099
Enterprise:		
Airport	(57,811)	(93,773)

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

City of Knoxville

Schedule of Findings and Questioned Costs

Year ended June 30, 2006

Response – The City will eliminate the deficit in the Debt Service Fund with future tax collections. The City is investigating other revenue sources for the Enterprise, Airport Fund to help reduce the deficit balance.

Conclusion – Response accepted.

IV-K-06 Transfers to Internal Service Funds – The Internal Service, Equipment Replacement and Building Replacement Funds were established to accumulate resources to replace City equipment, buildings and structures. Payments to Internal Service Funds from the operating funds are to be budgeted as disbursements if the disbursements from the Internal Service Fund are not budgeted. During the year ended June 30, 2006, transfers from the Special Revenue, Road Use Tax and Local Option Sales Tax Funds and Enterprise, Sewer Fund of \$88,768, \$146,000 and \$49,612, respectively, to the Internal Service, Equipment Replacement Fund were not appropriately budgeted. The transfers out were reclassified as disbursements in the operating funds and the transfers in were reclassified as receipts in the Internal Service Fund. Therefore, this was resolved for audit purposes.

Recommendation – Payments to the Internal Service Funds from the operating funds should be budgeted if the disbursements from the Internal Service Funds are not budgeted.

Response – This will be corrected in the current budget year.

Conclusion – Response accepted.

IV-L-06 Electronically Retained Checks – The City did not maintain the back side of electronically retained checks as required by Chapter 554D.114(5) of the Code of Iowa.

Recommendation – The City should maintain both sides of electronically retained checks in accordance with Chapter 554D.114(5) of the Code of Iowa.

Response – We are uncertain at this point how we will resolve this dilemma as we are not provided this service by our banking institution but will be working with them to provide a solution.

Conclusion – Response accepted.

IV-M-06 Unclaimed Property – The City has not reported unclaimed property of \$5,678 to the Treasurer of State as required by Chapter 556.11 of the Code of Iowa.

Recommendation – The City should report unclaimed property to the Treasurer of State as required by Chapter 556.11 of the Code of Iowa.

Response – This will be corrected in the current budget year.

Conclusion – Response accepted.

City of Knoxville

Schedule of Findings and Questioned Costs

Year ended June 30, 2006

IV-N-06 Interfund Loan – The Special Revenue, Urban Renewal Tax Increment Fund did not transfer any repayments on the General Fund interfund loan.

Recommendation – The City should transfer sufficient funds to repay the interfund loan.

Response – This will be corrected in the current budget year.

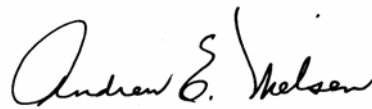
Conclusion – Response accepted.

City of Knoxville

Staff

This audit was performed by:

K. David Voy, CPA, Manager
Selina V. Johnson, CPA, Senior Auditor II
Ryan J. Sisson, Staff Auditor
Aaron P. Wagner, Assistant Auditor
Paula J. White, Assistant Auditor

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

Andrew E. Nielsen, CPA
Deputy Auditor of State