

★ **Roll Call Number**

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Agenda Item Number

AA

Date August 21, 2006

Receipt of Des Moines Water Works 2005 Financial Report and Statements of Cash Receipts and Disbursements for Sewer, Solid Waste and Stormwater.

Moved by _____ to receive and file comments.

COUNCIL ACTION	YEAS	NAYS	PASS	ABSENT
COWNIE				
COLEMAN				
HENSLEY				
MAHAFFEY				
KIERNAN				
VLASSIS				
TOTAL				

MOTION CARRIED

APPROVED

Mayor

CERTIFICATE

I, DIANE RAUH, City Clerk of said City hereby certify that at a meeting of the City Council of said City of Des Moines, held on the above date, among other proceedings the above was adopted.

IN WITNESS WHEREOF, I have hereunto set my hand and affixed my seal the day and year first above written.

City Clerk

McGladrey & Pullen

Certified Public Accountants

July 5, 2006

Board of Water Works Trustees
Des Moines Water Works
Des Moines, Iowa

This letter is intended to inform the Board of Water Works Trustees about significant matters related to the conduct of the annual audit so it can appropriately discharge its oversight responsibility and that we comply with our professional responsibilities to the Board.

In addition to our report on your financial statements, we have provided, under separate cover, a letter dated April 6, 2006, concerning a significant deficiency in internal control that we noted during our audit of the Des Moines Water Works' financial statements for the year ended December 31, 2005.

The following summarizes various matters which must be communicated to you under auditing standards generally accepted in the United States of America.

The Auditor's Responsibility Under Auditing Standards Generally Accepted in the United States of America

Our audit of the financial statements of the Des Moines Water Works for the year ended December 31, 2005 was conducted in accordance with auditing standards generally accepted in the United States of America, and *Government Auditing Standards* issued by the Comptroller General of the United States. Those standards require we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether caused by error, fraudulent financial reporting or misappropriation of assets. 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. Accordingly, the audit was designed to obtain reasonable, rather than absolute, assurance about the financial statements. We believe our audit accomplished that objective.

In accordance with *Government Auditing Standards*, we have also performed tests of controls over internal control over financial reporting and tests of compliance with certain provisions of laws, regulations, contracts and grant agreements that contribute to the evidence supporting our opinion on the financial statements. However, they do not provide a basis for opining on the Water Work's internal control over financial reporting or on compliance and other matters.

Management Judgments and Accounting Estimates

Accounting estimates are an integral part of the preparation of financial statements and are based upon management's current judgment. The process used by management encompasses their knowledge and experience about past and current events and certain assumptions about future events. Management has informed us they used all the relevant facts available to them at the time to make the best judgments about accounting estimates and we considered this information in the scope of our audit. Estimates significant to the financial statements include such items as accrued sick leave for probable future eligible participants.

Audit Adjustments

There were a few audit adjustments made to the original trial balance presented to us to begin our audit. Adjustments are not uncommon during the course of an audit. Prior to recording the adjustment, it is standard to complete a review and discussion with management to ensure a thorough understanding of the cause is obtained and that the calculation of the adjustment amount is accurate. Of the adjustments that were recorded, the following is a description of the adjustments that could, in our judgment, either individually or in the aggregate, have a significant effect on the Water Works' financial reporting process:

- Accrued sick leave liability
- Accounts and contracts payable

In addition, during the year ended December 31, 2005, the Water Works' Pension Plan was advised that certain pooled separate accounts specifically set aside for guaranteed benefits of retired participants receiving benefits should be included in the Plan's net assets. As a result, the net assets available for benefits as of December 31, 2004, have been retroactively restated to include the fair value of the investments applicable to December 31, 2004. This restatement had the effect of increasing the net assets available for benefits as of December 31, 2004 by \$17,507,663 as compared to the amount previously reported in Note 11 of the financial statements.

Accounting Policies and Alternative Treatments

Management and the Board have the ultimate responsibility for the appropriateness of the accounting policies used by the Water Works.

In the current year, the Des Moines Water Works implemented the following Governmental Accounting Standards Board (GASB) Statements:

- GASB Statement No. 40, *Deposit and Investment Risk Disclosures*. This Statement established and modified disclosure requirements related to investment risks related to credit risk, concentration of credit risk, interest rate risk and foreign currency risk. As an element of interest rate risk, this Statement requires certain disclosures of investments that have fair values that are highly sensitive to changes in interest rates. This Statement also established and modified disclosure requirements for deposit risks.
- GASB Statement No. 42, *Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries*. This Statement requires governments to report the effects of capital asset impairment in their financial statements when it occurs and requires all governments to account for insurance recoveries in the same manner. This Statement had no effect to the Water Works' financial statements.

As of December 31, 2005, GASB also had issued several statements not yet implemented by the Water Works. The statements which might impact the Water Works are as follows:

- GASB Statement No. 43, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*, issued April 2004, will be effective for the Water Works beginning with its year ending December 31, 2007. This Statement establishes uniform financial reporting standards for other postemployment benefit plans (OPEB plans) and supercedes existing guidance.
- GASB Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, issued June 2004, will be effective for the Water Works beginning with its year ending December 31, 2008. This Statement establishes standards for the measurement, recognition and display of other postemployment benefits expenses and related liabilities or assets, note disclosures and, if applicable, required supplementary information in the financial reports.
- GASB Statement No. 46, *Net Assets Restricted by Enabling Legislation*, an amendment of GASB Statement No. 34, issued December 2004, will be effective for the Water Works beginning with its year ending December 31, 2006. This Statement establishes and modifies requirements related to restrictions of net assets resulting from enabling legislation.

- GASB Statement No. 47, *Accounting for Termination Benefits*, issued June 2005, will be effective for the Water Works beginning with its year ending December 31, 2006. This Statement establishes accounting standards for termination benefits. In financial statements prepared on the accrual basis of accounting, employers should recognize a liability and expense for voluntary termination benefits (early retirement incentives) when the offer is accepted and the amount can be estimated. A liability for involuntary termination benefits (severance benefits) should be recognized when a plan of termination has been approved by those with the authority to commit the government to the plan, the plan has been communicated to the employees and the amount can be estimated.

We did not identify any significant or unusual transactions or significant accounting policies in controversial or emerging areas for which there is a lack of authoritative guidance or consensus.

Other Information in Documents Containing Audited Financial Statements

We are not aware of any other documents that contain the audited basic financial statements. If such documents were to be published, we would have a responsibility to determine that such financial information was not materially inconsistent with the audited statements of the Des Moines Water Works.

Disagreements with Management

We encountered no disagreements with management over the application of significant accounting principles, the basis for management's judgments on any significant matters, the scope of the audit or significant disclosures to be included in the financial statements.

Consultations with Other Accountants

We are not aware of any consultations management had with other accountants about accounting or auditing matters.

Major Issues Discussed with Management Prior to Retention

No major issues were discussed with management prior to our retention to perform the aforementioned audit.

Difficulties Encountered in Performing the Audit

We did not encounter any difficulties in dealing with management relating to the performance of the audit.

Closing

We will be pleased to respond to any questions you have about the foregoing. We appreciate the opportunity to continue to be of service to the Des Moines Water Works.

This report is intended solely for the information and use of the Board of Trustees and management and is not intended to be and should not be used by anyone other than the specified parties.

McGladrey & Pullen, LLP

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McGladrey & Pullen

Certified Public Accountants

Independent Auditor's Report

Board of Water Works Trustees
Des Moines Water Works
Des Moines, Iowa

We have audited the accompanying basic financial statements of Des Moines Water Works (Water Works) as of and for the year ended December 31, 2005, as listed in the table of contents. These financial statements are the responsibility of the Des Moines Water Works' management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and *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 that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Des Moines Water Works as of December 31, 2005 and the changes in its financial position and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

As described in Note 11, the 2004 financial statements have been restated to properly recognize investments in retired life funds for the Des Moines Water Works Pension Plan. The adjustment described in Note 11 was derived from information provided to the Pension Plan administrator and certified by the custodian as complete and accurate.

In accordance with *Government Auditing Standards*, we have also issued our report dated April 6, 2006, on our consideration of Water Work's internal control over financial reporting and our tests of 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 the internal control over financial reporting or on 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.

The management's discussion and analysis on pages 3 through 7 and pension plan schedule on pages 29 and 30 is not a required part of the basic financial statements but are supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

McGladrey & Pullen, LLP

Davenport, Iowa
April 6, 2006

Des Moines Water Works

Management's Discussion and Analysis Year Ended December 31, 2005

Our Management's Discussion and Analysis (MD&A) of Des Moines Water Works' (Water Works) financial performance provides an overview of the utility's financial activities for the years ended December 31, 2005 and 2004. Please consider this information in conjunction with the financial statements and the accompanying notes to basic financial statements that follow this section.

Overview of Business

The service area of the Water Works has expanded significantly since its emergence as a public water utility in 1919. In addition to serving customers within the City of Des Moines, Water Works provides wholesale water service based on long-term water contracts to surrounding municipalities and rural water districts, accounting for roughly 25 percent of total water revenues. This service area spans approximately 400 square miles, including most of Polk County and communities in eastern Dallas County and northern Warren County. The utility also provides billing and collection services on a contractual basis to wholesale customers and billing and collection services to the City of Des Moines for wastewater treatment, solid waste collection and the storm water utility.

As the utility's service area has expanded, so too has the need for water storage facilities, booster stations and additional treatment capacity to meet peak demand requirements. The most economical approach for the Water Works has involved utilizing these facilities to supply multiple customers. Contractual service users share in the cost of these joint-use facilities, which allows for meeting peak use demands and also allows some users to participate in lower off-peak or purchased capacity water rates. Financial participation in the construction of these facilities includes initial cash contributions or payments of debt service for the improvements and operating and maintenance costs. Ownership of these facilities is maintained by the Water Works.

The water sources for the system are the Raccoon River and Des Moines River, an underground infiltration gallery, and wells along the Raccoon River near Maffitt Reservoir. These four sources are used to provide adequate supply in the most cost-effective combination. The utility operates two treatment plants, with one of those plants being operated remotely. An additional treatment plant is currently being developed in the northern segment of the utility's service area to meet growing demand in that area.

Governance of the Water Works is vested in a five-member Board appointed by the Mayor of the City of Des Moines with approval of the City Council. Trustees serve for six-year staggered terms. The Board has complete control of Water Works' management, and employs approximately 215 full-time and 15 part-time or seasonal employees.

The utility has adopted an annual activity-based budgeting methodology and performs an annual cost of service study to assist the Board in rate-setting policy.

Financial Highlights

- Water Works' net assets increased as a result of operations. As of December 31, 2005 and 2004, total assets were \$229,668,231 and \$216,076,105 respectively; total liabilities were \$61,009,355 and \$50,601,691, respectively, resulting in net assets of \$168,658,876 and \$165,474,414, respectively.
- Operating revenues of \$35,018,884 increased 3.49 percent over 2004, while operating expenses increased approximately 5.70 percent to \$33,111,759.
- During the year, Water Works had operating income of \$1,907,125 and change in net assets of \$3,184,462. This compares to operating income of \$2,508,827 and change in net assets of \$1,132,114 reported in 2004.

Des Moines Water Works

Management's Discussion and Analysis Year Ended December 31, 2005

Overview of the Financial Statements

Management's Discussion and Analysis (MD&A) serves as an introduction to the financial statements, and the MD&A represents management's examination and analysis of the Water Work's financial condition and performance. The financial statements report information about the utility using full accrual accounting methods as utilized by similar entities in the private sector.

The balance sheet provides information about the Water Works' assets, liabilities and net assets, thereby measuring the Water Works' liquidity and solvency. Liquidity is a measure of the utility's ability to meet current obligations (those due within one year). Solvency is a similar concept, but measures the ongoing ability to meet obligations over a longer term.

The statement of revenues, expenses and changes in net assets presents the results of the Water Works' revenues and expenses over the course of the fiscal year and provides information about the utility's recovery of costs. Water rates are established by the Board of Trustees and are based on the utility's annual Cost of Service Study. The Cost of Service Study estimates annual revenue requirements through an analysis of operational and maintenance expenses, debt service requirements, anticipated capital needs, and return on capital. The Study provides a core of information not only for the trustees and staff at Des Moines Water Works, but also for the customers ultimately affected by our decisions.

The statement of cash flows presents cash receipts, cash disbursements and net changes in cash resulting from operations, noncapital financing activities, capital and related financing activities and investing activities. This statement details where cash resources come from and how they are used.

The notes to basic financial statements provide required disclosures and other information that are essential to a full understanding of data provided in the statements. The notes supplement the basic financial statements by presenting information about the Water Works' accounting policies, significant account balances and activities, material risks, obligations, commitments, and contingencies.

Condensed Financial Information

The following condensed financial information serves as the key financial data and indicators for management, monitoring, and planning.

Condensed Balance Sheet Information

	2005	2004	% Change
Current assets	\$ 7,515,627	\$ 6,657,593	12.89%
Capital assets, net	198,755,238	195,002,073	1.92
Other noncurrent assets	23,397,366	14,416,439	62.30
Total assets	229,668,231	216,076,105	6.29
Current liabilities	14,063,412	12,438,321	13.07
Other noncurrent liabilities	19,755,943	6,375,370	209.88
Long-term debt	27,190,000	31,788,000	(14.46)
Total liabilities	61,009,355	50,601,691	20.57
Invested in capital assets, net of related debt	167,080,017	159,149,800	4.98
Restricted	19,372,427	11,087,959	74.72
Unrestricted	(17,793,568)	(4,763,345)	273.55
Total net assets	\$ 168,658,876	\$ 165,474,414	1.92

Des Moines Water Works

Management's Discussion and Analysis Year Ended December 31, 2005

Condensed Revenues, Expenses and Changes in Net Assets

	2005	2004	% Change
Water sales	\$ 30,001,396	\$ 28,311,841	5.97%
Billing and collection services	807,839	828,280	(2.47)
Connection fees	500,542	1,600,449	(68.72)
Purchased capacity	968,347	609,672	58.83
Other sales and services	2,740,760	2,486,171	10.24
Total operating revenues	35,018,884	33,836,413	3.49
Investment income	517,567	130,551	296.45
Other	173,043	223,090	(22.43)
Capital contributions	2,116,739	103,440	1,946.34
Total revenues	37,826,233	34,293,494	10.30
Labor and benefits	13,566,345	12,489,111	8.63
Chemicals and power	4,162,646	3,469,381	19.98
Insurance	899,619	886,855	1.44
Purchased services	2,559,800	3,283,872	(22.05)
Materials, supplies and equipment	3,003,276	2,937,966	2.22
Depreciation	8,734,782	8,024,984	8.84
Other	185,291	235,417	(21.29)
Total operating expenses	33,111,759	31,327,586	5.70
Interest expense	1,530,012	1,833,794	(16.57)
Total expenses	34,641,771	33,161,380	4.46
Change in net assets	3,184,462	1,132,114	181.28
Net assets, beginning of year	165,474,414	164,342,300	0.69
Net assets, end of year	\$ 168,658,876	\$ 165,474,414	1.92

Financial Analysis

Current assets increased 12.89 percent due largely to higher cash balances at year-end compared to 2004. This increase is due largely to the timing of the payment for the annual contribution to the Pension Plan. A corresponding current liability has also been recorded. Other noncurrent assets increased approximately 62 percent as a result of receiving over \$14,000,000 in payments related to revised Wholesale Water Purchase Agreements with several surrounding municipalities. This is offset by an increase in total current and noncurrent deferred revenue.

Current liabilities increased 13.07 percent due to increases in deferred revenue related to purchased capacity agreements of \$708,900 and construction contracts payable of \$512,291. The current portion of long-term debt also increased \$188,000 due to the issuance of Water Revenue Bonds, Series 2004A in 2004. Fees collected for other entities also increased \$162,757 over 2004 due to the timing of year-end remittances.

Noncurrent liabilities include deferred revenue being amortized over a period of 10 to 20 years. These balances increased over 200 percent from 2004 due to the additional purchased capacity agreements discussed above. Noncurrent liabilities include the pension liability which will be paid through future pension contributions.

Des Moines Water Works

Management's Discussion and Analysis Year Ended December 31, 2005

Long-term debt decreased 14.46 percent in 2005 due to principal payments made during 2005 totaling \$4,410,000, and the reclassification of \$4,598,000 scheduled 2006 debt service payments to short term, resulting in a net decrease in long term debt of \$4,598,000.

Water sales increased 5.97 percent as a result of slightly higher water pumpage compared to 2004.

Connection fees decreased 68.72 percent due to the higher connection fees of approximately \$1,600,000 received from the City of Polk City to connect to new feeder main serving customers in that area in 2004. These fees can fluctuate widely from year to year depending on the level of development experienced within the utility's service areas.

Purchased capacity revenues increased 58.83 percent as a result of the continued amortization of deferred revenue. This deferred revenue represents current year cash contributions to fund the Saylorville Water Treatment Plant and previous years' cash contributions from wholesale customers to fund the Maffitt Water Treatment Plant. Financial participation in the construction of the plants allows users to participate in lower purchased capacity water rates. Deferred revenue balances are amortized to purchase capacity revenue over the length of the contract, generally 10 to 20 years.

Effective January 5, 2004, per 28E agreement with the City of Des Moines, Des Moines Water Works assumed management of operations of the Des Moines Botanical Center. Operations include room rentals, catering and café, gift shop, and special events. Botanical Center revenues of \$492,942 and \$476,000 for 2005 and 2004, respectively, are included in Water Works' financial results.

Labor and benefits increased 8.63 percent due to rate increases averaging 3.4 percent across the utility partially offset by increased labor charged to capital projects compared to 2004. In addition, recording of the accrued benefits to employees under the age of 55 contributed to the increase.

Purchased services decreased 22.05 percent compared to 2004 due to higher than normal expenses experienced in 2004 related to the utility's new customer relationship management system (CRM) being placed into service in February 2004. In recent years, Water Works has contracted with outside consultants to develop the software and, during the development phase of the project, those contractor expenses were capitalized. After implementation in February 2004, consultants were still utilized during a transitional period through year-end; however, those costs were not eligible for capitalization, causing 2004 operating expenses to be higher than normal.

Materials and supplies increased 2.22 percent as a result of increased pumpage in 2005.

Other expenses decreased 21.29 percent due to a decrease of approximately \$46,000 in losses on bad accounts. The implementation of the new customer relationship management system in 2004 identified a larger than normal number of accounts requiring a one time write-off.

Investment income increased 296.45 percent due to higher investment balances as a result of purchased capacity funds received and slightly higher investment returns. Interest expense decreased in 2005 primarily due to the refunding of the Water Revenue Bonds Series 1997 that occurred in 2004.

Des Moines Water Works

Management's Discussion and Analysis Year Ended December 31, 2005

Capital contributions increased 1,946.34 percent in 2005 due to contributions totaling \$804,212 from the cities of Clive, Waukee and West Des Moines for the water main constructed along University Avenue. All other capital contributions of \$1,312,527 in 2005 are related to contributions of water mains by subdividers. These contributions can fluctuate widely from year to year, depending on the status of construction and the timing of inspections performed by Water Works' staff.

The aforementioned fluctuations result in an overall increase in net assets of 1.92 percent, the result of 3.49 percent increase in operating revenues, an increase in operating expenses of 5.70 percent, and 514.19 percent increase in nonoperating revenues.

Capital Assets and Debt Administration

During 2005, net capital assets increased \$3,753,165 or 1.92 percent. In addition to replacing deteriorating water mains, the utility is responsible for relocating mains affected by the I-235 freeway expansion project. The utility is also engaged in a multi-year capital project to implement radio frequency meter reading for all customers within the City of Des Moines. There were no significant changes to the condition of infrastructure assets, nor were there any changes made to standard service lives of those assets.

Water Works' long-term debt was \$31,788,000 and \$36,198,000 as of December 31, 2005 and 2004, respectively. The decrease is due to scheduled principal payments.

Economic Factors

Due to the Water Works' large concentration of residential customers, weather impacts revenue to a greater degree than do economic cycles. Water Works budgets revenues and expenses based on anticipated consumption for a "normal" weather year. A water rate increase of 15.3 percent was budgeted for 2006 for one class of wholesale customer. This was based on the results of the annual cost of service study which indicated costs to serve those customers exceeded their water rates.

Requests for Information

If the reader has questions or would like additional information, please direct the request to: Peggy Freese, Treasurer, 2201 George Flagg Parkway, Des Moines, Iowa 50321-1190.

Liabilities and Net Assets

Current liabilities payable from current assets:

Accounts payable	\$ 2,184,305
Accrued wages and benefits	393,184
Compensated absences (Note 4)	1,119,047
Deferred revenue (Note 1)	1,321,235
Special deposits	113,112
Construction payables	4,002,450
Water revenue bonds interest payable	92,851
Current portion of long-term debt (Note 4)	4,598,000
Fees collected for other entities	239,228
Total current liabilities	<u>14,063,412</u>

Long-term debt, less current installments (Note 4)	27,190,000
Compensated absences (Note 4)	793,170
Deferred revenue (Note 1)	18,379,733
Pension liability (Note 5)	583,040
	<u>46,945,943</u>
Total liabilities	<u>61,009,355</u>

Net assets:	
Invested in capital assets, net of related debt	167,080,017
Restricted (bond indentures)	19,372,427
Unrestricted	(17,793,568)
Total net assets	<u>168,658,876</u>

Commitments (Note 8)

Total liabilities and net assets	<u>\$ 229,668,231</u>
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Des Moines Water Works

**Statement of Revenues, Expenses and Changes in Net Assets
Year Ended December 31, 2005**

Operating revenues:	
Water sales	\$ 30,969,743
Other sales and services	3,548,599
Connection fees	500,542
Total operating revenues	<u>35,018,884</u>
Operating expenses:	
Labor	10,888,101
Insurance	899,619
Group insurance	1,064,948
Pension benefits (including social security)	1,613,296
Purchased services	2,559,800
Materials, supplies and equipment	3,003,276
Chemicals	2,048,517
Utilities, net	2,114,129
Depreciation	8,734,782
Other	185,291
Total operating expenses	<u>33,111,759</u>
Operating income	<u>1,907,125</u>
Nonoperating revenue (expense):	
Investment income	517,567
Interest expense	(1,530,012)
Land use income	153,792
Other	19,251
Nonoperating revenue (expense), net	<u>(839,402)</u>
Income before contributions	1,067,723
Capital contributions	<u>2,116,739</u>
Change in net assets	3,184,462
Net assets, beginning of year	<u>165,474,414</u>
Net assets, end of year	<u><u>\$ 168,658,876</u></u>

See Notes to Basic Financial Statements.

Des Moines Water Works

Statement of Cash Flows
Year Ended December 31, 2005

Cash flows from operating activities:	
Cash received from customers	\$ 48,937,555
Cash paid to suppliers	(10,045,769)
Cash paid to employees and for payroll taxes	(13,494,900)
Net cash provided by operating activities	<u>25,396,886</u>
Cash flows from capital and related financing activities:	
Principal payments on long-term debt	(4,410,000)
Acquisition, construction and removal cost of capital assets	(10,663,129)
Contributions received	804,212
Interest paid	(1,308,110)
Net cash used in capital and related financing activities	<u>(15,577,027)</u>
Cash flows from investing activities:	
Proceeds from maturities of investments	66,231,580
Purchase of investments	(74,942,348)
Interest received	379,295
Land use income and other	173,043
Net cash used in investing activities	<u>(8,158,430)</u>
Net increase in cash	1,661,429
Cash, beginning of year	486,968
Cash, end of year	<u>\$ 2,148,397</u>
Reconciliation of cash to the balance sheet:	
Cash	\$ 1,364,730
Restricted assets, cash	783,667
Total cash at end of year	<u>\$ 2,148,397</u>

(Continued)

Des Moines Water Works

Statement of Cash Flows (Continued)
Year Ended December 31, 2005

Reconciliation of operating income to net cash provided by operating activities:

Operating income	\$ 1,907,125
Adjustments to reconcile operating income to net cash, depreciation	8,734,782
Change in:	
Accounts receivable, billed	333,772
Accounts receivable, unbilled	37,147
Other receivables	6,554
Inventories - materials and supplies	(121,408)
Prepaid expense	74,327
Other assets	108,168
Accounts payable	(87,675)
Accrued wages and benefits and compensated absences	946,914
Pension liability	24,150
Deferred revenue	13,272,153
Special deposits	(1,880)
Fees collected for other entities	162,757
Net cash provided by operating activities	<u>\$ 25,396,886</u>

Schedule of noncash capital and related financing activities:

Contributions of water mains from contractors in aid of construction	\$ 1,312,527
Acquisition of capital assets through construction payables	512,291

Schedule of noncash investing activities, net depreciation of the fair value of investments (28,580)

See Notes to Basic Financial Statements.

**Des Moines Water Works
Pension Plan**

**Statement of Plan Net Assets
December 31, 2005**

Assets

Investments, contracts with insurance companies, pooled separate accounts

\$ 36,800,591

Employer contributions receivable

896,000

37,696,591

Liabilities

Net assets held in trust for pension benefits

-

\$ 37,696,591

See Notes to Basic Financial Statements.

**Des Moines Water Works
Pension Plan**

**Statement of Changes in Plan Net Assets
Year Ended December 31, 2005**

Additions:

Investment income, including net appreciation in the fair value of investments, interest and dividends (Note 2)	\$ 2,812,996
Employer contributions	<u>896,000</u>
Total additions	<u><u>3,708,996</u></u>

Deductions:

Benefit payments	1,484,685
Administrative expenses	<u>63,346</u>
Total deductions	<u><u>1,548,031</u></u>

Net increase

2,160,965

Net assets held in trust for pension benefits:

Beginning of year, as restated (Note 11)	<u>35,535,626</u>
End of year	<u><u>\$ 37,696,591</u></u>

See Notes to Basic Financial Statements.

Des Moines Water Works

Notes to Basic Financial Statements

Note 1. Nature of Business, Reporting Entity and Significant Accounting Policies

Nature of business:

Des Moines Water Works (Water Works) is managed and controlled by the Board of Water Works Trustees of the City of Des Moines, Iowa (the Board), which exists under the provisions of Chapter 388 and other relevant statutes of the Code of Iowa. The five-member Board is appointed by the Mayor of Des Moines with the approval of the City Council. Trustees serve for six-year staggered terms.

Water Works is exempt from federal income tax pursuant to Internal Revenue Code Section 115 which provides for exemption of divisions of state and local governments.

Water Works provides water and other services to retail and wholesale customers in the City of Des Moines (the City) and surrounding communities.

In September 1993, the Governmental Accounting Standards Board (GASB) issued Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities that Use Proprietary Fund Accounting*. The Statement provides that Water Works should apply all GASB pronouncements, as well as the following pronouncements issued on or before November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements: Statements and Interpretations of the Financial Accounting Standards Board (FASB), Accounting Principles Board (APB) Opinions and Accounting Research Bulletins (ARB) of the Committee on Accounting Procedures. In addition, Water Works may also apply all FASB Statements and Interpretations issued after November 30, 1989, except for those that conflict with or contradict GASB pronouncements. Water Works has elected to not apply all FASB, APB, and ARB materials issued after November 30, 1989.

Reporting entity:

Accounting principles generally accepted in the United States of America require that the reporting entity include (1) the primary government, (2) organizations for which the primary government is financially accountable and (3) other organizations for which the nature and significance of their relationship with the primary government are such that exclusion would cause the reporting entity's financial statements to be misleading or incomplete. The Water Works has authority to issue bonded debt without the approval of another government. It has the right to sue and be sued, and has the right to buy, sell, lease or mortgage property in its own name. Based on these criteria, the Water Works is considered a primary government and there are no other organizations or agencies whose financial statements should be combined and presented with these financial statements.

Significant accounting policies:

Basis of accounting and measurement focus: The economic measurement focus and the accrual basis of accounting are used by the Water Works. Under the accrual basis of accounting, revenue is recognized when earned and expenses are recognized when the liability has been incurred. Under this basis of accounting, all assets and all liabilities associated with the operation of the Water Works are included in the balance sheet.

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

Des Moines Water Works

Notes to Basic Financial Statements

Note 1. Nature of Business, Reporting Entity and Significant Accounting Policies (Continued)

Cash and investments: For the purpose of the statement of cash flows, Water Works considers cash balances maintained in demand deposit accounts at financial institutions to be cash. Excess cash invested temporarily in financial institutions is considered an investing activity and is not considered to be cash.

Investments as of December 31, 2005 were in U.S. government or agency obligations and are stated at fair value, based on quoted market prices.

Revenue recognition: Customers served by Water Works are billed on a monthly cyclical basis based on usage. Water Works accrues estimated unbilled water revenues for services rendered from the last billing date through year-end.

Operating revenues and expenses: Operating revenues include revenues resulting from the sale of water and related services. Operating expenses include expenses for water treatment, distribution, depreciation, customer service, sales, administrative and general. Nonoperating revenues and expenses include those derived from capital and related financing activities, noncapital financing activities, and investing activities. Revenues from the sale of water are based on billing rates, which are applied to customer's consumption of water.

Transactions with the City of Des Moines: Water Works provides water service to the City without charge except for the Sewage Treatment Works, Des Moines International Airport and city golf courses. The value (computed at the commercial rate) of the service provided without charge was approximately \$646,432 and \$706,040 in 2005 and 2004, respectively.

Water Works has an agreement to pay the City a Payment in Lieu of Taxes (PILOT). This amount was calculated in 1998 by applying the City millage rate for police and fire to the value of buildings and land operated and controlled by Water Works located within the City at that time. Total PILOT payments were \$234,000 in 2005 and 2004.

Water Works has also agreed to match annual contributions of the City (up to \$50,000) toward an industrial development corporation. Payments of \$50,000 were made in 2005 and 2004.

Billings and Collection Agent Services: Water Works serves as the billing and collection agent for fees related to sewage treatment, solid waste, and storm water collection for certain political subdivisions (including the City). Separate accounting records are maintained by Water Works for these collection services. Fees collected not yet remitted by Water Works to the applicable entity totaled approximately \$239,228 and \$76,471 as of December 31, 2005 and 2004, respectively. These fees have been reflected in Water Works' balance sheet and were remitted to the City and other political subdivisions subsequent to year-end. Processing fees billed to the City and other political subdivisions for billing and collection services provided by Water Works totaled approximately \$808,000 and \$828,000 in 2005 and 2004, respectively. The City's fees reflect only the incremental expenses incurred by Water Works to bill and collect the City's charges, rather than an equal sharing of the costs. Water Works bears the total cost of meter reading, cash processing, and statement preparation and mailing.

Inventories: Inventories are stated at the lower of average cost or market. The costs of these materials and supplies are recorded as an expense at the time they are relieved from inventory for use.

Des Moines Water Works

Notes to Basic Financial Statements

Note 1. Nature of Business, Reporting Entity and Significant Accounting Policies (Continued)

Restricted assets – cash and investments: Water Works is required, under the water revenue bond resolutions, to reserve certain assets to provide for payment of the bonds and interest for protection of the bondholders, and for the improvement and extension of facilities. Disbursement of these assets is restricted by the purpose of the respective funds.

Capital assets: Capital assets are recorded at cost and depreciated utilizing the straight-line method over estimated useful lives as follows:

Buildings, equipment and machinery	3-85 years
Supply system	20-85 years
Distribution system	10-85 years

Expenditures for maintenance, repairs and minor replacements are charged to operations. Expenditures for major repairs and betterments are capitalized. Water Works' capitalization threshold is \$500. When capital assets are retired or otherwise disposed, the cost and related accumulated depreciation are removed from the accounts and any resulting gains or losses are included in the statement of revenues, expenses and changes in net assets. Included in capital assets are the interest capitalized during construction in accordance with accounting principles generally accepted in the United States of America. No interest was capitalized in 2005.

Net assets: Net assets represent the difference between assets and liabilities in the financial statements. Net assets invested in capital assets, net of related debt, consists of capital assets, net of accumulated depreciation, reduced by the outstanding balance of any long-term debt used for acquisition, construction, or improvement of those assets. Net assets are reported as restricted when there are limitations imposed on their use through external restrictions imposed by creditors, grantors, or laws or regulations of other governments.

The Water Works' policy is to first apply restricted resources when an expense is incurred for purposes for which both restricted and unrestricted net assets are available.

Rates: The Board has full authority to establish rates. As part of the rate-setting process, Water Works performs an annual Cost of Service Study to determine the cost of operations. This Study is based on a standard water industry model. Based upon the Study, rates are set to fund future operations. Costs related to operations and maintenance, depreciation based on estimated replacement cost of capital assets (which differs from depreciation expense recorded for financial reporting purposes), debt service and return on capital are factored into the rate design as well as demand factors from various customer classes.

Deferred revenue: During 1996 and years subsequent, Water Works entered into contractual agreements with other political subdivisions to sell treatment capacity to these entities. In exchange for purchasing these amounts of capacity, the political subdivisions will be able to purchase water at a lower wholesale water rate. Purchasers were offered the option of cash payment or participating in issues of water revenue bonds. During 2005, Water Works entered into additional contractual agreements for treatment capacity in the Saylorville Water Treatment Plant, in the amount of \$47,490,500, of which \$14,240,500 was collected in cash during 2005. The remainder will be part of the water revenue bonds to be issued during 2006 and discussed in Note 10. For entities choosing to pay cash in advance, Water Works records these amounts as deferred revenue and amortizes the amounts into income over periods of ten to twenty years. For entities participating in the bond issues, Water Works recognizes this revenue on a monthly basis, as the entities are billed and as the principal and interest payments become due on the bonds. As of December 31, 2005, Water Works has \$19,700,968 of deferred revenue and has recognized \$3,640,098 of revenue during 2005 relating to the sale of treatment capacity.

Des Moines Water Works

Notes to Basic Financial Statements

Note 1. Nature of Business, Reporting Entity and Significant Accounting Policies (Continued)

Compensated absences: Vacation and personal leave are accrued as a liability as it is earned. Sick leave benefits do not vest; however, upon retirement an employee may receive pay for 90% of his or her accumulated sick leave up to a maximum of 810 hours. The maximum payable to employees who are eligible for retirement has been recorded as a liability as well as an estimate for employees who are probable of becoming eligible in the future.

Debt financing costs and discounts: Costs incurred to issue water revenue bonds and the Water Revenue Capital Loan note are capitalized. These costs, and the discounts on the water revenue bonds, are amortized over the terms of the bonds and note utilizing a method which approximates the effective interest method.

Fiduciary fund type: The Water Works also includes a pension trust fund, fiduciary fund type. Pension trust funds are accounted for in essentially the same manner as the enterprise fund, using the same measurement focus and basis of accounting. Plan member contributions are recognized in the period in which contributions are due. Employer contributions to the plan are recognized when due and the employer has made a formal commitment to provide the contributions. Benefits and refunds are recognized when due and payable in accordance with the terms of the plan. The Pension Trust Fund accounts for the assets of the Des Moines Water Works Pension Plan. This plan is included in the reporting entity due to the Water Works' significant administrative involvement and due to the Board of the Plan consisting of the Water Works' Board members.

Note 2. Cash and Investments

The Governmental Accounting Standards Board (GASB) Statement No. 40, *Deposit and Investment Risk Disclosures*, requires state and local governments to disclose certain risks. The disclosures required by GASB Statement No. 40 provide readers with information concerning the credit and interest risks associated with the Water Works' deposits and investments.

Authorized investments: Water Works is authorized to invest utility funds in interest bearing accounts at banks on the State of Iowa's Approved Bank List; obligations of the US government, its agencies and instrumentalities; certificates of deposit at federally insured Iowa depository institutions approved by the Code of Iowa, Chapter 12C; and repurchase agreements if the underlying collateral consists of obligations of the US government, its agencies and instrumentalities. The Water Works' investment policy prohibits investments in reverse repurchase agreements and futures and options contracts. In addition, investing pursuant to the following investment practices is prohibited: trading of securities for speculation of the realization of short-term trading gains; a contract providing for the compensation of an agent or fiduciary based upon the performance of the invested assets or if a fiduciary or third party has failed to produce requested records within a reasonable time.

Interest rate risk: Interest rate risk is the risk that changes in market interest rates will adversely affect the fair value of an investment. Generally, the longer the maturity of an investment, the greater the sensitivity of its fair value to changes in market interest rates. In an effort to limit exposure to fair value losses arising from interest rate risk, the Water Works' investment policy places maturity limitations on both operating funds and nonoperating funds. Operating funds are defined as those that are reasonably expected to be expended during the current budget year or within 15 months. Operating funds may only be invested in authorized instruments that mature within 397 days. Funds not identified as operating may be invested in investments with maturities longer than 397 days, but less than 1,726 days. All investments, however, shall have maturities that are consistent with the needs and uses of the utility.

Information about the sensitivity of the fair value of the Water Work's investments to market interest rate fluctuations is provided by the table on the following page. All investments held by Water Works have maturity dates within nine months of December 31, 2005.

Des Moines Water Works

Notes to Basic Financial Statements

Note 2. Cash and Investments (Continued)

Type	Fair Value December 31, 2005	Within 3 Months	Within 6 Months	Within 9 Months
Federal Home Loan Bank	\$ 8,871,947	\$ 7,058,388	\$ -	\$ 1,813,559
Federal Home Loan Mortgage Corp.	2,035,198	749,190	987,244	298,764
Federal Home Loan Mortgage Corp. Discount Notes	6,071,720	6,071,720	-	-
Federal National Mortgage Corp.	4,267,825	3,274,075	993,750	-
InterAmerican Development Bank Note	259,168	259,168	-	-
	<u>\$ 21,505,858</u>	<u>\$ 17,412,541</u>	<u>\$ 1,980,994</u>	<u>\$ 2,112,323</u>

The Water Works also has an investment in land purchased with the intent to sell; however, no commitment for sale exists as of December 31, 2005. The land is recorded at the lower of cost or market at \$624,562.

Credit risk: Generally, credit risk is the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment. This is measured by the assignment of a rating by a nationally recognized statistical rating organization.

As of December 31, 2005, the Water Works' investments were rated as follows:

Type	S&P Rating	Moody's Rating
Federal Home Loan Bank	AAA	Aaa
Federal Home Loan Mortgage Corporation	AAA	AAA
Federal Home Loan Mortgage Corporation Discount Notes	A-1+	Prime-1
Federal National Mortgage Corporation	AAA	AAA
InterAmerican Development Bank Note	AAA	AAA

Concentration of credit risk: The policy defines diversification requirements for the Water Works' investments. Invested assets shall be diversified to eliminate the risk of loss resulting from over concentration of assets in a specific maturity, a specific issuer or a specific class of security. Portfolio maturities shall be staggered in a way that avoids undue concentration of assets in a specific maturity sector. Liquidity practices shall be followed to ensure that funds required for the next disbursement date and next payroll date are covered through maturity investments, marketable US Treasury bills or cash on hand. Risks of market price volatility shall be controlled through maturity diversification so that aggregate price losses on investments with maturities approaching one year shall not be greater than coupon interest and investment income received from the balance of the portfolio.

Des Moines Water Works

Notes to Basic Financial Statements

Note 2. Cash and Investments (Continued)

More than 5% of the utility's investments are in the following investments:

Type	Percent of Total
Federal Home Loan Bank	41.3%
Federal Home Loan Mortgage Corporation	9.5
Federal Home Loan Mortgage Corporation Discount Notes	28.2
Federal National Mortgage Corporation	19.8

The Water Works' investments during the year did not vary substantially from those at year-end in amounts or level or risk.

Custodial credit risk: The custodial credit risk for deposits and investments is the risk that, in the event of the failure of a depository financial institution or counterparty (for example, broker-dealer) to a transaction, a government will not be able to recover deposits or will not be able to recover collateral securities or value of investments that are in the possession of an outside party. Deposits in financial institutions as of December 31, 2005 and throughout the year are covered by federal depository insurance or the State Sinking Fund in accordance with Chapter 12C, Code of Iowa. This Chapter provides additional assessments against the depositories to ensure there is no loss of public funds. Water Works' bank balances and book balances of deposits were \$2,933,835 and \$2,148,397 as of December 31, 2005, respectively.

Pension Plan Deposits and Investments

Deposits: As of December 31, 2005, the Plan held no deposits.

Investments: The Plan's investments in pooled separate accounts are stated at fair value based on quoted market prices of the investments held in each account as determined by Principal Life Insurance Company (Principal). Purchases and sales of securities are recorded on a trade date basis. Dividends are recorded on the exdividend date.

Asset allocation strategy: The Des Moines Water Works Pension Plan's named fiduciary asset allocation strategy shall identify target allocations to eligible asset classes and, where appropriate, suitable ranges within which each asset class can fluctuate as a percent of the total fund. Each asset class is to remain suitably invested at all times in either cash (or cash equivalents) or permitted securities within each class. The assets classes may be rebalanced from time to time to take advantage of tactical misvaluations across major asset classes or investment styles, or to align the current asset mix with strategic targets.

Authorized investments: The Des Moines Water Works Pension Plan's investment policy permits the Named Fiduciary to consider all asset classes allowed by ERISA as acceptable investment options and to select one or more customized investment portfolios and retain an investment manager to manage the assets of each such portfolio. The following assets classes are permitted for Plan investment options: Stable Value, Domestic Fixed Income, International or Foreign Fixed Income, Real Estate, Domestic Stock, International or Foreign Stock and Balanced/Asset allocation.

Des Moines Water Works

Notes to Basic Financial Statements

Note 2. Cash and Investments (Continued)

GASB Statement No. 40 requires plan investments to disclose an indication of the level of credit risk, concentration of credit risk and interest rate risk assumed by the Plan. These risk disclosures only pertain to fixed income investments. As of December 31, 2005, the Plan had investments listed in the table below. Amounts are shown in dollars. Effective duration is shown in years. Investments held by the Plan were not subject to custodial credit risk or foreign currency risk.

	Fair Value	Effective Duration
Fixed income investments:		
Bond and mortgage account	\$ 8,503,177	4.30
Inflation protection account	658,981	6.35
High yield account	680,280	3.84
Preferred securities account	665,963	4.11
Total fair value of fixed income investments	<u>10,508,401</u>	
Other investments	<u>26,292,190</u>	
Total investments	<u><u>\$ 36,800,591</u></u>	

Interest rate risk: Interest rate risk is the risk that changes in market interest rates will adversely affect the fair value of an investment. Generally, the longer the maturity of an investment the greater the sensitivity of its fair value to changes in market interest rates.

Credit risk and concentration of credit risk: Generally, credit risk is the risk that an issuer of an investment will not fulfill its obligations to the holder of the investment. This is measured by the assignment of a rating by a nationally recognized statistical rating organization. The following is a credit analysis for the Plan's fixed income investments as compiled by Morningstar, Inc. after reviewing the ratings assigned the underlying holdings of a fund by Standard & Poor's or Moody's. The display represents the percentage of assets/bonds which meets the corresponding credit score and the average credit score for each investment.

Fixed Income Investment	US									Average
	Govt.	AAA	AA	A	BBB	BB	B	Below B	NR/NA	
Bond and mortgage separate account	14.98	43.73	6.85	13.06	13.38	3.83	3.23	0.94	-	AA
Inflation protection separate account	78.15	15.32	0.22	0.25	0.98	4.27	0.75	-	0.06	AAA
High yield separate account	-	-	-	-	2.90	29.43	53.72	13.95	-	B
Preferred securities separate account	-	1.19	4.60	52.76	39.58	1.87	-	-	-	A

Des Moines Water Works

Notes to Basic Financial Statements

Note 3. Capital Assets

Capital assets activity for the year ended December 31, 2005 is as follows:

	Beginning Balance	Increases	Decreases	Ending Balance
Capital assets not being depreciated:				
Land	\$ 4,835,402	\$ -	\$ -	\$ 4,835,402
Construction-in-process	9,495,208	11,175,419	9,118,143	11,552,484
Total capital assets not being depreciated	14,330,610	11,175,419	9,118,143	16,387,886
Capital assets being depreciated:				
Buildings, equipment and machinery	114,937,413	1,194,625	43,394	116,088,644
Supply system	39,323,267	20,941	-	39,344,208
Distribution system	107,647,162	9,215,105	-	116,862,267
Total capital assets being depreciated	261,907,842	10,430,671	43,394	272,295,119
Less accumulated depreciation for:				
Buildings, equipment and machinery	42,462,245	5,954,016	43,394	48,372,867
Supply system	9,975,228	715,740	-	10,690,968
Distribution system	28,798,906	2,065,026	-	30,863,932
Total accumulated depreciation	81,236,379	8,734,782	43,394	89,927,767
Total capital assets being depreciated, net	180,671,463	1,695,889	-	182,367,352
Net capital assets	\$ 195,002,073	\$ 12,871,308	\$ 9,118,143	\$ 198,755,238

Note 4. Noncurrent Liabilities

As of December 31, 2005, Water Works' debt consists of Revenue Refunding Bonds, Series 2001; Water Revenue Refunding Bonds, Series 2004 A & B; and Water Revenue Capital Loan Note, Series 2003 (through the Drinking Water State Revolving Fund (SRF)). Interest on these bonds and note is payable semiannually on June 1 and December 1, with principal payable on December 1. Series 2001 bonds mature on December 1, 2007 and Series 2004 Series A & B mature on December 1, 2024 and 2017, respectively. The Series 2003 note matures on December 1, 2022. The bonds and note are redeemable at the option of Water Works prior to their maturity in whole or, from time to time, in part, in any order of maturity and within a maturity by lot, at a price of par plus accrued interest to call date.

Des Moines Water Works

Notes to Basic Financial Statements

Note 4. Noncurrent Liabilities (Continued)

Changes in long-term obligations for the year ended December 31, 2005 are as follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Amounts Due Within One Year
Water Revenue Bonds:					
Series 2001	\$ 8,760,000	\$ -	\$ 3,165,000	\$ 5,595,000	\$ 3,325,000
Series 2004 A & B	25,220,000	-	1,150,000	24,070,000	1,175,000
Water Revenue Capital, Series 2003	2,218,000	-	95,000	2,123,000	98,000
Compensated absences	956,941	1,912,217	956,941	1,912,217	1,119,047
	<u>\$ 37,154,941</u>	<u>\$ 1,912,217</u>	<u>\$ 5,366,941</u>	<u>\$ 33,700,217</u>	<u>\$ 5,717,047</u>

A summary of the aggregate principal and interest requirements outstanding for the Water Revenue Refunding Bonds, Series 2001 is as follows:

Maturing During Year Ending December 31:	Interest Rate	Annual Principal Payment	Annual Interest Payment	Total Annual Payment
2006	3.40%	\$ 3,325,000	\$ 194,770	\$ 3,519,770
2007	3.60	2,270,000	81,720	2,351,720
		<u>\$ 5,595,000</u>	<u>\$ 276,490</u>	<u>\$ 5,871,490</u>

A summary of the aggregate principal and interest requirements outstanding for the Water Revenue Refunding Bonds, Series 2004 A is as follows:

Maturing During Year Ending December 31:	Interest Rate	Annual Principal Payment	Annual Interest Payment	Total Annual Payment
2006	3.00%	\$ 255,000	\$ 253,181	\$ 508,181
2007	3.00	260,000	245,531	505,531
2008	3.00	265,000	237,731	502,731
2009	3.00	275,000	229,781	504,781
2010	3.25	285,000	221,531	506,531
2011-2015	3.25 - 4.00	1,570,000	954,069	2,524,069
2016-2020	4.00	1,905,000	621,844	2,526,844
2021-2024	4.00 - 4.25	1,865,000	199,787	2,064,787
		<u>\$ 6,680,000</u>	<u>\$ 2,963,455</u>	<u>\$ 9,643,455</u>

Des Moines Water Works

Notes to Basic Financial Statements

Note 4. Noncurrent Liabilities (Continued)

A summary of the aggregate principal and interest requirements outstanding for the Water Revenue Refunding Bonds, Series 2004 B is as follows:

Maturing During Year Ending December 31:	Interest Rate	Annual Principal Payment	Annual Interest Payment	Total Annual Payment
2006	2.50%	\$ 920,000	\$ 602,575	\$ 1,522,575
2007	2.50	970,000	579,575	1,549,575
2008	3.00	1,380,000	550,475	1,930,475
2009	3.00	1,420,000	509,075	1,929,075
2010	3.00	1,465,000	466,475	1,931,475
2011-2015	3.00 - 4.00	8,185,000	1,579,950	9,764,950
2016-2017	4.00	3,050,000	169,600	3,219,600
		<u>\$ 17,390,000</u>	<u>\$ 4,457,725</u>	<u>\$ 21,847,725</u>

A summary of the aggregate principal and interest requirements outstanding for the Water Revenue Capital Loan Note is as follows:

Maturing During Year Ending December 31:	Interest Rate	Annual Principal Payment	Annual Interest Payment	Total Annual Payment
2006	3.00%	\$ 98,000	\$ 63,690	\$ 161,690
2007	3.00	100,000	60,750	160,750
2008	3.00	103,000	57,750	160,750
2009	3.00	107,000	54,660	161,660
2010	3.00	110,000	51,450	161,450
2011-2015	3.00	600,000	205,830	805,830
2016-2020	3.00	696,000	110,250	806,250
2021-2022	3.00	309,000	13,980	322,980
		<u>\$ 2,123,000</u>	<u>\$ 618,360</u>	<u>\$ 2,741,360</u>

The water revenue bond and water revenue capital loan note resolutions (Resolutions) provide that net revenue (as defined in the Resolutions) of Water Works is pledged for the purpose of paying Series 2001, Series 2003 and Series 2004 bonds. The Resolutions further require that sufficient monies be set aside to meet current expenses of Water Works. All remaining monies are to be segregated and restricted in separate special reserves. These special reserves are reflected as restricted assets on the balance sheet. The Resolutions also require that the issuer maintain insurance coverage of a kind and in an amount which usually would be carried by private companies engaged in a similar kind of business. Water Works maintains fire and extended coverage insurance in the amount of \$244,495,342 per occurrence on building and contents; in addition, liability insurance is maintained.

Des Moines Water Works

Notes to Basic Financial Statements

Note 5. Pension Plan

Water Works has a noncontributory defined benefit single employer pension plan, established by the Board, called the Des Moines Water Works Pension Plan (the Plan). All full-time Water Works employees and employees who work at least 1,040 hours in a calendar year or work during two consecutive calendar quarters are eligible to participate in the Plan. Benefits vest after five years of continuous service and normal retirement is allowed at or after age 65. Early retirement is allowed without a reduction in benefits beginning at age 55 if the employee's combined years of service and age are 85 or greater and is allowed with reduced benefits for vested employees with less than 30 years of service beginning at age 55. The pension benefit formula is based upon a percentage of covered compensation and the number of years of service with Water Works, as defined by the Plan document. The amount of the contribution is determined by the Board. The Plan also provides death and disability benefits to vested employees. Benefits are established by the Plan administrator. The Plan issues a publicly available financial report that includes financial statements and required supplementary information. The report may be obtained by writing to or calling the Water Works.

Water Works' annual pension cost and net pension liability for the three years ended 2005 were as follows:

	2005	2004	2003
Annual required contribution (ARC)	\$ 941,548	\$ 896,193	\$ 931,470
Interest	41,917	36,084	22,134
Adjustment to annual required contribution	(63,315)	(54,822)	(32,283)
Annual pension cost (APC)	920,150	877,455	921,321
Contributions made	896,000	800,000	735,000
Increase in net pension liability	(24,150)	(77,455)	(186,321)
Net pension (liability), beginning of year	(558,890)	(481,435)	(295,114)
Net pension (liability), end of year	<u>\$ (583,040)</u>	<u>\$ (558,890)</u>	<u>\$ (481,435)</u>
Percentage of APC contributed	97.4%	91.1%	79.8%

The pension benefit liability was computed as part of the annual actuarial valuation performed as of January 1, 2005 using the aggregate actuarial cost method. The aggregate actuarial cost method does not identify or separately amortize unfunded actuarial liabilities. The actuarial assumptions used to compute the pension benefit liability included (a) 7.5% investment rate of return (net of administrative expenses) and (b) projected salary increases of 5.0%. These amounts were computed using the 1983 Group Annuity Mortality Table with a 3.0% cost of living factor increase included.

Des Moines Water Works

Notes to Basic Financial Statements

Note 6. Postretirement Health Care Benefits

Water Works provides certain postretirement health care benefits, in accordance with the policy established by the Board, to all employees who retire from Water Works after attaining age 55. As of December 31, 2005, 64 retirees receive postretirement health care benefits. Water Works provides a Medicare supplement or equivalent amount to all employees who retire after attaining age 55, if the sum of their age and years of service are at least 85 or for those who retire after attaining age 65 regardless of length of service. Employees who retire prior to attaining age 65 with the sum of their age and years of service less than 85 receive a discounted benefit as provided by the plan document. Water Works recognizes the cost of providing postretirement health care benefits by expensing the annual insurance premiums which were approximately \$100,804 and \$88,024 for 2005 and 2004, respectively.

Note 7. Risk Management

Water Works is exposed to various risks of loss related to torts, theft of, damage to and destruction of assets; errors and omissions, injuries to employees, natural disasters and malpractice.

Water Works purchases commercial insurance for property and casualty, workers' compensation, employee health, life and dental insurance. During the last three years, settled claims have not exceeded insurance coverage.

Note 8. Commitments

Approximately \$1,087,000 related to 2005 contracts has been formally committed as of December 31, 2005. In addition, the Board has approved approximately \$35,900,000 of expenditures for capital acquisitions and improvements, all of which are expected to be expended in 2006.

In 1983, Water Works determined additional water resources would be required for future customer needs. As a result, the Board has contracted with the United States of America – Army Corps of Engineers, through the state of Iowa, for water supply storage in the Saylorville Reservoir Project continuing through the life of the project. Under the contract, Water Works is required to pay a portion of future major renovation costs of the project. Water Works also pays a portion of the annual operation and maintenance costs of the project. Water Works' portion of operation and maintenance costs was approximately \$6,300 in 2005 and 2004.

On January 5, 2004, the Water Works and City of Des Moines, Iowa entered into a 28E Agreement for the operation, management and maintenance of the Botanical Center. The Water Works is responsible for the management and operation of the Botanical Center for the City. All revenues generated and expenses incurred for the operation are retained by Water Works. The agreement exists for an initial term of January 5, 2004 through December 31, 2009 and may renew on and after January 1, 2010 for not more than three successive three-year terms. Water Works and the City Council will meet jointly no later than July 1, 2007 to evaluate the agreement and determine if it will continue.

For the years ended December 31, 2005 and 2004, revenues generated by the Botanical Center were approximately \$492,000 and \$476,000, respectively. Expenses were approximately \$900,000 for each year.

Des Moines Water Works

Notes to Basic Financial Statements

Note 9. Pending GASB Statements

Water Works implemented the following Governmental Accounting Standards Board (GASB) Statements during the year ended December 31, 2005:

- GASB Statement No. 40, *Deposit and Investment Risk Disclosures*. This Statement established and modified disclosure requirements related to investment risks related to credit risk, concentration of credit risk, interest rate risk and foreign currency risk. As an element of interest rate risk, this Statement requires certain disclosures of investments that have fair values that are highly sensitive to changes in interest rates. This Statement also established and modified disclosure requirements for deposit risks.
- GASB Statement No. 42, *Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries*. This Statement requires governments to report the effects of capital asset impairment in their financial statements when it occurs and requires all governments to account for insurance recoveries in the same manner. This Statement had no effect to the Water Works financial statements.

As of December 31, 2005, the Governmental Accounting Standards Board (GASB) also had issued several statements not yet implemented by the Water Works. The statements which might impact Water Works are as follows:

- GASB Statement No. 43, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*, issued April 2004, will be effective for Water Works beginning with its year ending December 31, 2007. This Statement establishes uniform financial reporting standards for other postemployment benefit plans (OPEB plans) and supercedes existing guidance.
- GASB Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, issued June 2004, will be effective for Water Works beginning with its year ending December 31, 2008. This Statement establishes standards for the measurement, recognition and display of other postemployment benefits expenses and related liabilities or assets, note disclosures and, if applicable, required supplementary information in the financial reports.
- GASB Statement No. 46, *Net Assets Restricted by Enabling Legislation*, an amendment of GASB Statement No. 34, issued December 2004, will be effective for Water Works beginning with its year ending December 31, 2006. This Statement establishes and modifies requirements related to restrictions of net assets resulting from enabling legislation.
- GASB Statement No. 47, *Accounting for Termination Benefits*, issued June 2005, will be effective for the Water Works beginning with its year ending December 31, 2006. This Statement establishes accounting standards for termination benefits. In financial statements prepared on the accrual basis of accounting, employers should recognize a liability and expense for voluntary termination benefits (early retirement incentives) when the offer is accepted and the amount can be estimated. A liability for involuntary termination benefits (severance benefits) should be recognized when a plan of termination has been approved by those with the authority to commit the government to the plan, the plan has been communicated to the employees and the amount can be estimated.

The Water Works' management has not yet determined the effect these Statements will have on Water Works' financial statements.

Des Moines Water Works

Notes to Basic Financial Statements

Note 10. Subsequent Event

On March 1, 2006 Des Moines Water Works issued \$52,435,000 Water Revenue Bonds, Series 2006. Interest is due on December 1 and June 1, commencing December 1, 2006. Principal is due on December 1, commencing on December 1, 2006 through 2026 in annual installments of \$575,000 to \$3,560,000. The bonds maturing on or after December 1, 2015, are callable at the option of the Water Works on any date on or after December 1, 2014, at a price of par plus accrued interest.

The bond proceeds will be used to finance capital improvements relating to the construction of a new Saylorville Water Treatment Plant (\$36,105,000), construction and renovation of water lines in the Pleasant Hill suburb (\$9,880,000) and purchase of the Southeast Polk Rural Water System (\$6,450,000). Water Works purchased the Southeast Polk Rural Water System on April 3, 2006 for approximately \$9,248,000.

Note 11. Restatement of Prior Year – Net Assets Held in Trust for Pension Benefits

During the year ended December 31, 2005, the Des Moines Water Works Pension Plan was advised that certain pooled separate accounts specifically set aside for guaranteed benefits of retired participants receiving benefits should be included in the Plan's net assets. As a result, the net assets available for benefits as of December 31, 2004, have been restated to include the fair value of the investments applicable to December 31, 2004.

Net assets available for benefits as of December 31, 2004, as previously reported	\$ 18,027,963
Adjustment for retired life funds	17,507,663
Net assets available for benefits as of December 31, 2004, as restated	<u>\$ 35,535,626</u>

**Des Moines Water Works
Pension Plan**

**Required Supplementary Information
Schedule of Contributions from the Employer
December 31, 2005**

Year Ended December 31:	Annual Required Contribution	Actual Contribution	Percentage Contribution
2000	\$ 629,754	\$ 547,685	86.97%
2001	793,691	478,000	60.22
2002	735,168	466,000	63.39
2003	931,470	735,000	78.91
2004	896,193	800,000	89.27
2005	941,548	896,000	95.16

See Note to Required Supplementary Information.

**Des Moines Water Works
Pension Plan**

Note to Required Supplementary Information

The information presented in the required supplementary schedule was determined as part of the actuarial valuations at the dates indicated. Additional information as of the latest actuarial valuation follows:

Actuarial valuation:	
Frequency	Annual
Latest date	January 1, 2005
Cost method	Aggregate cost method
Amortization	Not applicable under Aggregate Cost Method. The Aggregate Cost Method does not identify or separately amortize unfunded actuarial liabilities. They are amortized through normal cost.
Asset valuation method	Fair value is adjusted by spreading the expected value minus the actual value over four years. The total actuarial value of assets falls within the applicable corridor limits.
Assumptions:	
Investment rate of return	7.5%
Salary increases	5.0% annual increases until retirement
Retirement age	The later of meeting the rule of 85 or age 58, but not later than age 65.
Mortality	1983 Group Annuity Table (male) (set back 0 for males and 6 for females)
Rate of withdrawal	V Table from August 1992 Pension Forum, multiplied by 0.60
Cost of living	3.0% to project benefits and compensation limitations

In addition to the above assumptions, an estimate of the Plan's expenses is included in normal cost.

Since the Plan uses the Aggregate Cost Method, a schedule of funding progress is not required as that method does not identify or separately amortize unfunded actuarial liabilities.

**Board of Water Works Trustees, Billing and Collection
Agent for the Sewer Service Charges for the
City of Des Moines, Iowa**

Statements of Cash Receipts and Disbursements

For the Years Ended December 31, 2005 and 2004
(With Independent Auditor's Report Thereon)

McGladrey & Pullen

Certified Public Accountants

Independent Auditor's Report

Board of Water Works Trustees,
Billing and Collection Agent for
the Sewer Service Charges for
the City of Des Moines, Iowa

We have audited the accompanying statements of cash receipts and disbursements of Board of Water Works Trustees, Billing and Collection Agent for the Sewer Service Charges for the City of Des Moines, Iowa (the Agent), for the years ended December 31, 2005 and 2004. This financial statement is the responsibility of the Agent. Our responsibility is to express an opinion on this financial statement based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the statements of cash receipts and disbursements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the statements of cash receipts and disbursements. An audit also includes assessing the accounting principles used and significant estimates made by the Agent, as well as evaluating the overall presentation of the statements of cash receipts and disbursements. We believe that our audit provides a reasonable basis for our opinion.

The accompanying financial statement was prepared for the purpose of complying with a contractual agreement with the City of Des Moines, Iowa as described in Note 1 to the financial statement. The statement does not purport to, and does not present fairly the financial position of the Board of Water Works Trustees or the Des Moines Water Works, in conformity with accounting principles generally accepted in the United States of America.

As described in Note 2, these financial statements were prepared on the basis of cash receipts and disbursements, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America.

In our opinion, the financial statement referred to above presents fairly, in all material respects, the cash receipts and disbursements of the Agent for the year ended December 31, 2005 and 2004, on the basis of accounting described in Note 2.

McGladrey & Pullen, LLP

Davenport, Iowa
April 6, 2006

**Board of Water Works Trustees, Billing and Collection Agent
For the Sewer Service Charges for the City of Des Moines, Iowa**

**Statements of Cash Receipts and Disbursements
For the Years Ended December 31, 2005 and 2004**

	2005	2004
Cash receipts, sewer service charges	\$ 23,246,814	\$ 21,496,409
Cash disbursements:		
Remittances to the City of Des Moines	22,944,010	21,377,686
Billing and collection services	227,684	223,321
Total disbursements	23,171,694	21,601,007
Receipts over (under) disbursements	75,120	(104,598)
Cash balance, beginning of year	64,365	168,963
Cash balance, end of year	\$ 139,485	\$ 64,365

See Notes to Statements of Cash Receipts and Disbursements.

**Board of Water Works Trustees, Billing and Collection Agent
For the Sewer Service Charges for the City of Des Moines, Iowa**

Notes to Statements of Cash Receipts and Disbursements

Note 1. Reporting Entity and Nature of Business

The statements of cash receipts and disbursements included in this report reflect only the cash receipts and disbursements related to the agreement with the Des Moines Water Works and the City of Des Moines, Iowa for billing and collection agent for the Sewer Service charges.

The Des Moines Water Works serves as the billing and collection Agent for the Sewer Service Charges for the City of Des Moines, Iowa. Billings are prepared monthly in conjunction with water bills and are based on water usage.

Note 2. Basis of Accounting

These statements are prepared on the cash basis of accounting; therefore, uncollected billings for Sewer Service Charges of \$2,149,257 and \$2,282,869 as of December 31, 2005 and 2004, respectively, are not reflected in the statements of cash receipts and disbursements.

**Board of Water Works Trustees, Billing and Collection
Agent for the Solid Waste Collection Charges for the
City of Des Moines, Iowa**

Statements of Cash Receipts and Disbursements

For the Years Ended December 31, 2005 and 2004
(With Independent Auditor's Report Thereon)

McGladrey & Pullen

Certified Public Accountants

Independent Auditor's Report

Board of Water Works Trustees,
Billing and Collection Agent for the
Solid Waste Collection Charges for
the City of Des Moines, Iowa

We have audited the accompanying statements of cash receipts and disbursements of Board of Water Works Trustees, Billing and Collection Agent for the Solid Waste Collection Charges for the City of Des Moines, Iowa (the Agent), for the years ended December 31, 2005 and 2004. This financial statement is the responsibility of the Agent. Our responsibility is to express an opinion on this financial statement based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the statements of cash receipts and disbursements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the statements of cash receipts and disbursements. An audit also includes assessing the accounting principles used and significant estimates made by the Agent, as well as evaluating the overall presentation of the statements of cash receipts and disbursements. We believe that our audit provides a reasonable basis for our opinion.

The accompanying financial statement was prepared for the purpose of complying with a contractual agreement with the City of Des Moines, Iowa as described in Note 1 to the financial statement. The statement does not purport to, and does not present fairly the financial position of the Board of Water Works Trustees or the Des Moines Water Works, in conformity with accounting principles generally accepted in the United States of America.

As described in Note 2, this financial statement was prepared on the basis of cash receipts and disbursements, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America.

In our opinion, the financial statement referred to above presents fairly, in all material respects, the cash receipts and disbursements of the Agent for the years ended December 31, 2005 and 2004, on the basis of accounting described in Note 2.

McGladrey & Pullen, LLP

Davenport, Iowa
April 6, 2006

**Board of Water Works Trustees, Billing and Collection Agent
For the Solid Waste Collection Charges for the City of Des Moines, Iowa**

**Statements of Cash Receipts and Disbursements
For the Years Ended December 31, 2005 and 2004**

	2005	2004
Cash receipts, solid waste collection charges	\$ 9,049,108	\$ 8,743,962
Cash disbursements:		
Remittances to the City of Des Moines	8,810,317	8,589,633
Billing and collection services	213,671	209,154
Total disbursements	9,023,988	8,798,787
Receipts over (under) disbursements	25,120	(54,825)
Cash balance, beginning of year	24,115	78,940
Cash balance, end of year	<u>\$ 49,235</u>	<u>\$ 24,115</u>

See Notes to Statements of Cash Receipts and Disbursements.

**Board of Water Works Trustees, Billing and Collection Agent
For the Solid Waste Collection Charges for the City of Des Moines, Iowa**

Notes To Financial Statements

Note 1. Reporting Entity and Nature of Business

The statements of cash receipts and disbursements included in this report reflect only the cash receipts and disbursements related to the agreement with the Des Moines Water Works and the City of Des Moines, Iowa for billing and collection agent for the Solid Waste Collection charges.

The Des Moines Water Works serves as the billing and collection agent for the solid waste collection charges for the City of Des Moines, Iowa. Billings are prepared monthly in conjunction with water bills and are billed in advance of the service period covered.

Note 2. Basis of Accounting

These statements are prepared on the cash basis of accounting; therefore, uncollected billings for solid waste collection charges of \$974,428 and \$947,934 as of December 31, 2005 and 2004, respectively, are not reflected in the statements of cash receipts and disbursements.

**Board of Water Works Trustees, Billing and Collection
Agent for the Storm Water Management Charges for the
City of Des Moines, Iowa**

Statements of Cash Receipts and Disbursements

For the Years Ended December 31, 2005 and 2004
(With Independent Auditor's Report Thereon)

McGladrey & Pullen

Certified Public Accountants

Independent Auditor's Report

Board of Water Works Trustees,
Billing and Collection Agent for the
Storm Water Management Charges for
the City of Des Moines, Iowa

We have audited the accompanying statements of cash receipts and disbursements of Board of Water Works Trustees, Billing and Collection Agent for the Storm Water Management Charges for the City of Des Moines, Iowa (the Agent), for the years ended December 31, 2005 and 2004. This financial statement is the responsibility of the Agent. Our responsibility is to express an opinion on this financial statement based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the statements of cash receipts and disbursements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the statements of cash receipts and disbursements. An audit also includes assessing the accounting principles used and significant estimates made by the Agent, as well as evaluating the overall presentation of the statements of cash receipts and disbursements. We believe that our audit provides a reasonable basis for our opinion.

The accompanying financial statement was prepared for the purpose of complying with a contractual agreement with the City of Des Moines, Iowa as described in Note 1 to the financial statement. The statement does not purport to, and does not present fairly the financial position of the Board of Water Works Trustees or the Des Moines Water Works, in conformity with accounting principles generally accepted in the United States of America.

As described in Note 2, this financial statement was prepared on the basis of cash receipts and disbursements, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America.

In our opinion, the financial statement referred to above presents fairly, in all material respects, the cash receipts and disbursements of the Agent for the year ended December 31, 2005 and 2004, on the basis of accounting described in Note 2.

McGladrey & Pullen, LLP

Davenport, Iowa
April 6, 2006

**Board of Water Works Trustees, Billing and Collection Agent
For the Storm Water Management Charges for the City of Des Moines, Iowa**

Notes to Statements of Cash Receipts and Disbursements

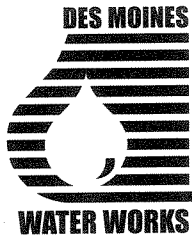
Note 1. Reporting Entity and Nature of Business

The statements of cash receipts and disbursements included in this report reflect only the cash receipts and disbursements related to the agreement with the Des Moines Water Works and the City of Des Moines, Iowa for billing and collection agent for the Storm Water Management charges.

The Des Moines Water Works serves as the billing and collection agent for the Storm Water Management charges for the City of Des Moines, Iowa. Billings are prepared monthly in conjunction with water bills and are billed subsequent to the service period covered.

Note 2. Basis of Accounting

These statements are prepared on the cash basis of accounting; therefore, uncollected billings for Storm Water Management charges of \$959,009 and \$914,300 as of December 31, 2005 and 2004, respectively, are not reflected in the statements of cash receipts and disbursements.



DES MOINES WATER WORKS

Board of Water Works Trustees
L.D. McMullen, Ph.D., P.E., CEO and General Manager

2201 George Flagg Parkway • Des Moines, Iowa 50321-1190 • (515) 283-8755 • www.dmww.com

August 3, 2006

Ms. Diane Rauh
City Clerk, City of Des Moines
E 1st & Locust
Des Moines, IA 50307

SUBJECT: Des Moines Water Works - 2005 Audit Reports

Dear Ms. Diane Rauh:

Audited financial statements and accompanying reports for Des Moines Water Works for the 2005 calendar year are enclosed. These reports were prepared by McGladrey & Pullen.

The enclosed information was presented and received by the Board of Water Works Trustees at their meeting held July 25, 2006.

Sincerely,

Kay Modde, CPA
Controller

Enclosures