

★ Roll Call Number

Agenda Item Number

33

Date September 22, 2008

Receipt of Des Moines Water Works 2007 Financial Report and Statements of Receipts and Disbursements for Sewer, Solid Waste and Stormwater.

Moved by _____ to

COUNCIL ACTION	YEAS	NAYS	PASS	ABSENT
COWNIE				
COLEMAN				
HENSLEY				
KIERNAN				
MAHAFFEY				
MEYER				
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

Des Moines Water Works

Report to the Board of Water Works Trustees

July 15, 2008

McGladrey & Pullen
Certified Public Accountants

McGladrey & Pullen

Certified Public Accountants

July 15, 2008

Board of Water Works Trustees
Des Moines Water Works
2201 George Flagg Parkway
Des Moines, Iowa 50321

We are pleased to present this report related to our audit of the basic financial statements of Des Moines Water Works for the years ended December 31, 2007 and 2006. This report summarizes certain matters required by professional standards to be communicated to you in your oversight responsibility for Des Moines Water Works' financial reporting process. Also included is a summary of recently issued accounting standards that may affect future financial reporting by Des Moines Water Works.

This report is intended solely for the information and use of the Board of Water Works Trustees and management and is not intended to be and should not be used by anyone other than these specified parties. It will be our pleasure to respond to any questions you have regarding this report. We appreciate the opportunity to continue to be of service to Des Moines Water Works.

McGladrey & Pullen, LLP

Contents

Required Communications	1 – 3
Summary of Significant Accounting Estimates	4
Summary of Uncorrected Misstatements	5
Recently Issued Accounting Standards	6 – 7
Exhibit A – Certain Written Communications Between Management and Our Firm	
Representation Letter	
Written Communication on Accounting, Auditing or Operational Matters (Management Letter)	
Exhibit B – Letter Communicating Significant Deficiencies and Material Weaknesses	

Required Communications

Statement on Auditing Standards No. 114 requires the auditor to communicate certain matters to keep those charged with governance adequately informed about matters related to the financial statement audit that are, in our professional judgment, significant and relevant to the responsibilities of those charged with governance in overseeing the financial reporting process. The following summarizes these communications:

Area	Comments
Auditor’s Responsibility Under Professional Standards	<p>Our responsibility under auditing standards generally accepted in the United States of America and <i>Government Auditing Standards</i> issued by the Comptroller General of the United States has been described to you in our arrangement letter dated December 21, 2007.</p>
Accounting Practices	<p>Adoption of, or Change in, Accounting Policies</p> <p>Management has the ultimate responsibility for the appropriateness of the accounting policies used by the Des Moines Water Works. In the current year, Des Moines Water Works adopted the following Governmental Accounting Standards Board (GASB) Statements.</p> <ul style="list-style-type: none"> • GASB Statement No. 43, <i>Financial Reporting For Postemployment Benefit Plans Other Than Pension Plans</i>. This Statement establishes uniform financial reporting standards for other postemployment benefit plans (OPEB plans) and supersedes existing guidance. The adoption of this Statement had no effect on Water Works in the current year. • GASB Statement No. 48, <i>Sales and Pledges of Receivables and Future Revenues and Intra-Entity Transfers of Assets and Future Revenues</i>. This Statement establishes accounting and financial reporting standards for transactions in which a government receives, or is entitled to, resources in exchange for future cash flows generated by collecting specific receivables or specific future revenues. It also provides disclosure requirements for a government that pledges or commits future cash flows from a specific revenue source. In addition, this Statement establishes accounting and financial reporting standards for intra-entity transfers of assets and future revenues. The effect of the adoption of this Statement to Water Works was the addition of note disclosures regarding pledged revenue for long-term obligations.

Area	Comments
	<p>Significant or Unusual Transactions</p> <p>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.</p>
	<p>Alternative Treatments Discussed with Management</p> <p>We did not discuss with management any alternative treatments within generally accepted accounting principles for accounting policies and practices related to material items during the current audit period.</p>
<p>Management’s Judgments and Significant Accounting Estimates</p>	<p>Summary information about the process used by management in formulating particularly sensitive accounting estimates and about our conclusions regarding the reasonableness of those estimates is in the attached “Summary of Significant Accounting Estimates”.</p>
<p>Audit Adjustments</p>	<p>Audit adjustments recorded by Des Moines Water Works are attached with the representation letter included with Exhibit A.</p>
<p>Uncorrected Misstatements</p>	<p>Uncorrected misstatements are summarized in the attached Summaries of Uncorrected Misstatements.</p>
<p>Disagreements with Management</p>	<p>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.</p>
<p>Consultations with Other Accountants</p>	<p>We are not aware of any consultations management had with other accountants about accounting or auditing matters.</p>
<p>Significant Issues Discussed with Management</p>	<p>Following is a description of significant issues arising from the audit that were discussed with management:</p> <ul style="list-style-type: none"> • Recording of retainages payable on open contracts. • Inventory being recorded based on purchase order price versus actual invoice price.
<p>Difficulties Encountered in Performing the Audit</p>	<p>We did not encounter any difficulties in dealing with management during the audit.</p>

Area	Comments
Letter Communicating Significant Deficiencies and Material Weaknesses	We have separately communicated the significant deficiency and a material weakness identified during our audit of the financial statements and this communication is attached as Exhibit B.
Certain Written Communications Between Management and Our Firm	Copies of certain written communications between our firm and the management of the entity are attached as Exhibit A.

Des Moines Water Works

**Summary of Significant Accounting Estimates
Year Ended December 31, 2007**

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. You may wish to monitor throughout the year the process used to compute and record these accounting estimates. The following describes the significant accounting estimates reflected in the entity's December 31, 2007 financial statements:

Area	Accounting Policy	Estimation Process	Comments
Pension Plan Assumptions	Pension plan accounting and disclosure is based upon numerous assumptions and estimates, including the expected rate of investment return on retirement plan assets, the interest rate used to determine the present value of liabilities and certain employee-related factors.	The employee-related factors include turnover, retirement age and mortality. These factors and the estimated discount rate and rate of return are based upon historical and general market data.	We analyzed the Water Works' methodology and concluded the estimates are reasonable.
Depreciable Life and Salvage Value of Capital Assets	The depreciable life of capital assets is set at the estimated useful life of the related asset. Salvage value is based upon an estimate of what the value of the property will be when the Water Works is through using the related asset.	The determination is made at the time the asset is placed into service and involves various judgments and assumptions, including resale value of used equipment, estimated useful life and prior experience.	We believe the estimates and process used by the Water Works is proper.
Fair Value of Financial Instruments	The Water Works records the estimated fair value of its investments.	Investment securities are based on quoted market prices.	We tested the propriety of information underlying management's estimates. Based on our procedures, we conclude that management's approach is reasonable.

Des Moines Water Works

**Summary of Uncorrected Misstatements
Year Ended December 31, 2007**

During the course of our audit, we accumulated uncorrected misstatements that were determined by management to be immaterial, both individually and in the aggregate, to the balance sheets, statements of revenues, expenses and changes in net assets and cash flows and to the related financial statement disclosures. Following is a summary of those differences:

Description:	Debit (Credit) to Correct the Misstatements				
	Assets	Liabilities	Net Assets	Revenue	Expense
Carryover impact from previous years:					
Revenue adjustment	\$ -	\$ -	\$ (242,000)	\$ 242,000	\$ -
Inventory overstatement	-	-	37,000	-	(37,000)
Current misstatement, known errors, revenue adjustment	-	-	242,000	(242,000)	-
Current misstatement, project error, inventory understatement	70,000	-	-	-	70,000
Subtotal	<u>\$ 70,000</u>	<u>\$ -</u>	<u>37,000</u>	<u>\$ -</u>	<u>\$ 33,000</u>
Effect of current year passed adjustments on net assets			(107,000)		
Total			<u>\$ (70,000)</u>		

Recently Issued Accounting Standards

The GASB has issued several statements not yet implemented by Des Moines Water Works. Des Moines Water Works' management has not yet determined the effect these Statements will have on Des Moines Water Works' financial statements. However, Des Moines Water Works plans to implement all standards by the required dates. The Statements which might impact Des Moines Water Works are as follows:

GASB Statement No. 45, Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions

This Statement, issued June 2004, will be effective for Des Moines 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. 49, Accounting and Financial Reporting for Pollution Remediation Obligations

This Statement, issued November 2006, will be effective for Des Moines Water Works beginning with its year ending December 31, 2008. This Statement addresses accounting and financial reporting standards for pollution (including contamination) remediation obligations, which are obligations to address the current or potential detrimental effects of existing pollution by participating in pollution remediation activities, such as site assessments and cleanups. This standard requires the government to estimate the components of expected pollution remediation outlays and determine whether the outlays for those components should be accrued as a liability or, if appropriate, capitalized when goods and services are acquired.

GASB Statement No. 50, Pension Disclosures, an amendment of GASB Statement Nos. 25 and 27

This Statement, issued May 2007, will be effective for Des Moines Water Works beginning with its year ending December 31, 2008. This Statement more closely aligns the financial reporting requirements for pensions with those for other postemployment benefits (OPEB) and, in doing so, enhances information disclosed in notes to the financial statements or presented as required supplementary information (RSI) by pension plans and by employers that provide pension benefits.

GASB Statement No. 51, Accounting and Financial Reporting for Intangible Assets

This Statement, issued July 2007, will be effective for Des Moines Water Works beginning with its year ending December 31, 2010. This Statement provides guidance regarding how to identify, account for and report intangible assets. The new standard characterizes an intangible asset as an asset that lacks physical substance, is nonfinancial in nature and has an initial useful life extending beyond a single reporting period.

***GASB Statement No. 52, Land and Other
Real Estate Held as Investments by
Endowments***

This Statement, issued November 2007, will be effective for Des Moines Water Works beginning with its year ending December 31, 2009. This Statement establishes consistent standards for the reporting of land and other real estate held as investments. Endowments were previously required to report their land and other real estate held for investment purposes at historical cost. However, such investments are reported at fair value by similar entities, such as pension plans. The Statement requires endowments to report land and other real estate investments at fair value. The changes in the fair value are to be reported as investment income.

**Exhibit A - Certain Written Communications Between Management
and Our Firm**



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.dmw.com

July 15, 2008

McGladrey & Pullen, LLP
201 North Harrison Street
Suite 300
Davenport, Iowa 52801

In connection with your audits of the basic financial statements of Des Moines Water Works, Iowa as of and for the years ended December 31, 2007 and 2006, we confirm that we are responsible for the fair presentation in the financial statements of financial position, changes in financial position, and cash flows in conformity with accounting principles generally accepted in the United States of America.

We confirm to the best of our knowledge and belief, as of July 15, 2008, the following representations made to you during your audits:

1. The financial statements referred to above are fairly presented in conformity with accounting principles generally accepted in the United States of America.
2. There are no organizations that are a part of this reporting entity or with which we have a relationship, as these organizations are defined in Section 2100 of the Governmental Accounting Standards Board's Codification of Governmental Accounting and Financial Reporting Standards, that are:
 - a. Component units.
 - b. Other organizations for which the nature and significance of their relationship with Des Moines Water Works are such that exclusion would cause the reporting entity's financial statements to be misleading or incomplete.
 - c. Jointly governed organizations in which we participated.
3. We are responsible for compliance with laws and regulations applicable to Des Moines Water Works including adopting, approving and amending budgets.
4. We have identified and disclosed to you all laws and regulations that have a direct and material effect on the determination of financial statement amounts including legal and contractual provisions for reporting specific activities.
5. We have made available to you:
 - a. All financial records and related data of all funds and activities, including those of all programs, departments, projects, activities, etc., in existence at any time during the period covered by your audit.
 - b. All minutes of the meetings of the governing board and committees of board members or summaries of actions of recent meetings for which minutes have not yet been prepared.

6. We have no knowledge of fraud or suspected fraud affecting the entity involving:
 - a. Management or employees who have significant roles in the internal control.
 - b. Others where the fraud could have a material effect on the financial statements.
7. We acknowledge our responsibility for the design and implementation of programs and controls to provide reasonable assurance that fraud is prevented and detected.
8. We have no knowledge of any allegations of fraud or suspected fraud affecting Des Moines Water Works received in communications from employees, former employees, analysts, regulators, short sellers or others.
9. We have informed you of all significant deficiencies, including material weaknesses, in the design or operation of internal controls that could adversely affect the entity's ability to record, process, summarize, and report financial data.
10. There have been no communications from regulatory agencies concerning noncompliance with, or deficiencies in, financial reporting practices.
11. We have no plans or intentions that may materially affect the carrying value or classification of assets and liabilities.
12. The following have been properly recorded and/or disclosed in the financial statements:
 - a. Related party transactions, including those with other organizations for which the nature and significance of their relationship with Des Moines Water Works are such that exclusion would cause the reporting entity's financial statements to be misleading or incomplete as defined in Section 2100 of the Governmental Accounting Standards Board's Codification of Governmental Accounting and Financial Reporting Standards, and interfund transactions, including interfund accounts and advances receivable and payable, sale and purchase transactions, interfund transfers, long-term loans, leasing arrangements, and guarantees, all of which have been recorded in accordance with the economic substance of the transaction and appropriately classified and reported.
 - b. The fair value of investments.
 - c. Contractual obligations for construction and purchase of real property or equipment not included in the liabilities or encumbrances recorded on the books.
 - d. Debt issue provisions.
 - e. All significant estimates and material concentrations known to management which are required to be disclosed in accordance with the AICPA's Statement of Position 94-6, *Disclosure of Certain Significant Risks and Uncertainties*. Significant estimates are estimates at the balance sheet date which could change materially within the next year. Concentrations refer to volumes of business, revenues, available sources of supply, or markets for which events could occur which would significantly disrupt normal finances within the next year.
 - f. The effect on the financial statements of GASB Statement Nos. 45, 49, 50, 51 and 52 which have been issued, but which we have not yet adopted.
 - g. Deposits and investment securities category of custodial credit risk.

13. We are responsible for making the accounting estimates included in the financial statements. Those estimates reflect our judgment based on our knowledge and experience about past and current events and our assumptions about conditions we expect to exist and courses of action we expect to take. In that regard, adequate provisions have been made:
 - a. To reduce receivables to their estimated net collectable amounts.
 - b. To reduce obsolete, damaged, or excess inventories to their estimated net realizable values.
 - c. For risk retention, including uninsured losses or loss retentions (deductibles) attributable to events occurring through December 31, 2007 and/or for expected retroactive insurance premium adjustments applicable to periods through December 31, 2007.
 - d. For pension obligations, post-retirement benefits other than pensions and deferred compensation agreements attributable to employee services rendered through December 31, 2007.

14. There are no:
 - a. Material transactions that have not been properly recorded in the accounting records underlying the financial statements.
 - b. Violations or possible violations of laws or regulations whose effects should be considered for disclosure in the financial statements or as a basis for recording a loss contingency. In that regard, we specifically represent that we have not been designated as, or alleged to be, a "potentially responsible party" by the Federal Environmental Protection Agency or any equivalent state agencies in connection with any environmental contamination.
 - c. Other material liabilities or gain or loss contingencies that are required to be accrued or disclosed by Statement of Financial Accounting Standards No. 5 and/or GASB Statement No. 10.
 - d. Guarantees, whether written or oral, under which the Government is contingently liable.
 - e. Arrangements with financial institutions involving compensating balances or other arrangements involving restrictions on cash balances.
 - f. Line of credit or similar arrangements.
 - g. Agreements to repurchase assets previously sold.
 - h. Security agreements in effect under the Uniform Commercial Code.
 - i. Any other liens or encumbrances on assets or revenues or any assets or revenues which were pledged as collateral for any liability or which were subordinated in any way.
 - j. Any liabilities which are subordinated in any way to any other actual or possible liabilities.
 - k. Debt issue repurchase options or agreements, or sinking fund debt repurchase ordinance requirements.
 - l. All leases and material amounts of rental obligations under long-term leases.
 - m. Authorized but unissued bonds and/or notes.
 - n. Risk financing activities.

- o. Derivative financial instruments.
 - p. Special and extraordinary items.
 - q. Arbitrage rebate liabilities.
 - r. Impairment of capital assets.
 - s. Investments, intangibles, and other assets which have permanently declined in value to their realizable values.
 - t. Material losses to be sustained in the fulfillment of, or from the inability to fulfill, any service commitments.
 - u. Material losses to be sustained as a result of purchase commitments.
 - v. Environmental clean up obligations.
15. There are no unasserted claims or assessments that our lawyer has advised us are probable of assertion and must be disclosed in accordance with Statement of Financial Accounting Standards No. 5 and/or GASB Statement No. 10.
16. We have no direct or indirect, legal or moral, obligation for any debt of any organization, public or private, that is not disclosed in the financial statement.
17. We have satisfactory title to all owned assets.
18. We have complied with all aspects of contractual agreements that would have a material effect on the financial statements in the event of noncompliance.
19. Net asset components invested in capital assets, net of related debt; restricted; and unrestricted are properly classified and, if applicable, approved.
20. Capital assets, including infrastructure assets, are properly capitalized, reported and depreciated.
21. Required supplementary information is properly measured and presented.
22. We are responsible for and have reviewed and approved the proposed adjustments to the trial balances identified during the audit, which are included in the summarized schedule of posted adjustments and will post all adjustments accordingly. These adjustments are attached as Appendix A. We have reviewed, approved, and are responsible for overseeing the preparation and completion of the basic financial statements and related notes.
23. We appropriately adopted:
- a. GASB Statement No. 43, *Financial Reporting For Postemployment Benefit Plans Other Than Pension Plans*, issued April 2004. This Statement establishes uniform financial reporting standards for other postemployment benefit plans (OPEB plans) and supersedes existing guidance. The adoption of this statement had no effect on Water Works in the current year.

- b. Statement No. 48, *Sales and Pledges of Receivables and Future Revenues and Intra-Entity Transfers of Assets and Future Revenues*, issued September 2006. This Statement establishes accounting and financial reporting standards for transactions in which a government receives, or is entitled to, resources in exchange for future cash flows generated by collecting specific receivables or specific future revenues. It also provides disclosure requirements for a government that pledges or commits future cash flows from a specific revenue source. In addition, this Statement establishes accounting and financial reporting standards for intra-entity transfers of assets and future revenues. The effect of the adoption of this Statement to Water Works was the addition on note disclosures regarding pledged revenue for long-term obligations.
24. In connection with your audit, conducted in accordance with *Government Auditing Standards*, we confirm:
- a. We are responsible for:
 - i. Compliance with the laws, regulations and provisions of contracts and grant agreements applicable to Des Moines Water Works.
 - ii. Establishing and maintaining effective internal control over financial reporting.
 - b. We have identified and disclosed to you:
 - i. All laws, regulations and provisions of contracts and grant agreements that have a direct and material effect on the determinations of financial statement amounts or other financial data significant to audit objectives.
 - ii. Violations (and possible violations) of laws, regulations, and provisions of contracts and grant agreements whose effects should be considered for disclosure in the auditor's report on noncompliance.
 - c. We have taken timely and appropriate steps to remedy fraud, illegal acts, violations of provisions of contracts or grant agreements, or abuse that has been reported.
 - d. We have a process to track the status of audit findings and recommendations.
 - e. We have identified for you previous financial audits, attestation engagements, performance audits, or other studies related to the objectives of the audit being undertaken and the corrective action taken to address significant findings and recommendations.
 - f. We have provided you with our views on your reported findings, conclusions, and recommendations, as well as our planned corrective actions.
 - g. We have reviewed, approved and taken full responsibility for the financial statements and related notes.
 - h. We have reviewed, approved and taken full responsibility for all accrual adjustments and an acknowledgement of the auditor's role in the preparation of the adjustments.
25. In connection with the reports on Billing and Collection Agent for the City of Des Moines, Iowa for the Storm Management charges, Sewer Service charges and Solid Waste Collection charges:
- a. The financial statements are 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.
 - b. We are responsible for compliance with the contract with the City of Des Moines, Iowa.

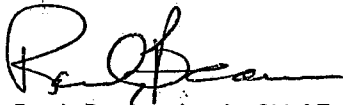
No events or transactions have occurred subsequent to the balance sheet date that would require adjustment to, or disclosure in, the financial statements.

During the course of your audit, you may have accumulated records containing data which should be reflected in our books and records. All such data have been so reflected. Accordingly, copies of such records in your possession are no longer needed by us.

As of and for the year ended December 31, 2007, we believe the effects of the uncorrected misstatements aggregated by you and summarized below are immaterial, both individually and in the aggregate, to the basic financial statements. For purposes of this representation, we consider items to be material, regardless of their size, if they involve the misstatement or omission of accounting information that, in light of surrounding circumstances, makes it probable that the judgment of a reasonable person relying on the information would be changed or influenced by the omission or misstatement.

Description:	Debit (Credit) to Correct the Misstatements				
	Assets	Liabilities	Net Assets	Revenues	Expense
Carryover impact from previous years:					
Revenue adjustment	\$ -	\$ -	\$ (242,000)	\$ 242,000	\$ -
Inventory overstatement	-	-	37,000	-	(37,000)
Current misstatement, known errors, revenue adjustment	-	-	242,000	(242,000)	-
Current misstatement, project error, inventory understatement	70,000	-	-	-	70,000
Subtotal	<u>\$ 70,000</u>	<u>\$ -</u>	<u>37,000</u>	<u>\$ -</u>	<u>\$ 33,000</u>
Effect of current year passed adjustments on net assets			(107,000)		
Total			<u>\$ (70,000)</u>		

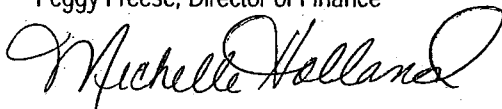
Des Moines Water Works



Randy Beavers, Interim Chief Executive Officer



Peggy Freese, Director of Finance



Michelle Holland, Controller

Des Moines Water Works:DMWW

0204

Year End: December 31, 2007

Trial balance

Date: 01/01/2007 To 12/31/2007

Prepared by 1 on 04/07/2008 Manager Review AB41 04/28/2008	Prepared by 2 Partner Review AB41 04/28/2008	Prepared by 3 Reviewed by 4	Incharge Review on 04/07/2008 Reviewed by 5
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Number	Date	Name	Account No	Reference	Debit	Credit	Net Income (Loss)	Amount Chg
Net Income (Loss) Before Adjustments							5,582,183.74	
2	12/31/2007	Construction In Progress	108100		150,981.13			
2	12/31/2007	Transfer to Capital	805100			150,981.13		
Client entry (To transfer remaining balance of Capital Expenditures to CIP.)					150,981.13	150,981.13	5,713,164.87	150,981.13
3	12/31/2007	Investment Income	901100	4005	392,661.19			
3	12/31/2007	Interest Expense	902100	4005		392,661.19		
To properly show capitalized interest as a reduction of interest expense instead of an increase in investment income.					392,661.19	392,661.19	5,713,164.87	0.00
5	12/31/2007	Construction In Progress	108100	4005	61,490.00			
5	12/31/2007	Capital Services	801500	4005	61,490.00			
5	12/31/2007	Transfer to Capital	805100	4005		61,490.00		
5	12/31/2007	Interest Expense	902100	4005		61,490.00		
Client entry (Adjust capitalized interest to actual.)					122,980.00	122,980.00	5,774,654.87	61,490.00
6	12/31/2007	Construction In Progress	108100		716,058.44			
6	12/31/2007	Contracts Payable	201200			716,058.44		
6	12/31/2007	Capital Services	801500		716,058.44			
6	12/31/2007	Transfer to Capital	805100			716,058.44		
To record retainages payable on open contracts.					1,432,116.88	1,432,116.88	5,774,654.87	0.00
					2,098,739.20	2,098,739.20	5,774,654.87	212,471.13

McGladrey & Pullen

Certified Public Accountants

Randy Beavers, Interim CEO
Peggy Freese, CFO
Des Moines Water Works
Des Moines, Iowa

In connection with our audit of the financial statements of Des Moines Water Works as of and for the year ended December 31, 2007, we identified deficiencies in internal control over financial reporting (control deficiencies).

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect financial statement misstatements on a timely basis. A deficiency in design exists when a control necessary to meet the control objective is missing, or when an existing control is not properly designed so that even if the control operates as designed, the control objective is not always met. A deficiency in operation exists when a properly designed control does not operate as designed or when the person performing the control does not possess the necessary authority or qualifications to perform the control effectively.

A significant deficiency is a control deficiency, or a combination of control deficiencies, that adversely affects the entity's ability to authorize, initiate, record, process or report financial data reliably in accordance with accounting principles generally accepted in the United States of America such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected.

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

We have separately communicated, to you and the Board of Water Works Trustees, an identified deficiency that we determined to be a material weakness. Certain control deficiencies that have been orally communicated to you by us are not repeated herein.

Following is a description of another identified control deficiency that we determined did not constitute a significant deficiency or material weakness:

- The inventory system used by Des Moines Water Works calculates inventory costs using purchase order price rather than actual invoice price. There are some compensating controls in place by Water Works to mitigate the instances of having differences between the two prices before the inventory is ordered. However, it is still possible, as noted through our sample testing of inventory, for inventory to be recorded at a price that is different than actual invoice. We recommend Des Moines Water Works investigate with their inventory software vendor as to whether a change could be made within the software program to calculate using actual invoice price to ensure inventory is being valued properly.

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

McGladrey & Pullen, LLP

Davenport, Iowa
July 15, 2008

Exhibit B – (If significant deficiencies and material weaknesses are not part of the financial statements and is issued as a separate letter, include letter here).

McGladrey & Pullen

Certified Public Accountants

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

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

We have audited the financial statements of Des Moines Water Works as of and for the years ended December 31, 2007 and 2006, and have issued our report thereon dated July 15, 2008. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

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

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

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

Finding: Des Moines Water Works did not record retainages payable on construction projects that had not been completed as of year-end.

Condition: Des Moines Water Works had several open construction projects as of December 31, 2007 in which retainages payable had not been accrued for or construction-in-progress recorded for the services completed as of year-end.

Context: Pervasive to all open construction projects/contracts. Based on invoices received by Des Moines Water Works subsequent to year-end, an additional \$716,000 of retainages payable and construction-in-progress was recorded by Water Works during the audit.

Effect: Contracts payable and construction-in-progress for the year was understated.

Recommendation: We recommend Des Moines Water Works record retainages payable on all construction projects for the period when services were performed.

Response and corrective action plan: Des Moines Water Works had been recording retainages payable for construction contracts that were completed as of year-end. Des Moines Water Works will start recording retainages payable and the related construction-in-progress for all construction projects still in progress at year-end.

The Des Moines Water Works response to the above finding identified in our audit is described above.

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

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, we believe the significant deficiency described above is a material weakness.

Compliance and Other Matters

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

We noted certain matters that we reported to management of Des Moines Water Works in a separate letter dated July 15, 2008.

We did not audit Des Moines Water Works' response above and, accordingly, we express no opinion on it.

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

McGladrey & Pullen, LLP

Davenport, Iowa
July 15, 2008

Des Moines Water Works

Financial Report
12.31.2007

Contents

Independent Auditor's Report	1 – 2
Management's discussion and analysis	3 – 9
Basic financial statements	
Balance sheets	10 – 11
Statements of revenues, expenses and changes in net assets	12
Statements of cash flows	13 – 14
Statements of plan net assets	15
Statements of changes in plan net assets	16
Notes to basic financial statements	17 – 32
Required supplementary information	
Schedule of contributions from the employer	33
Note to required supplementary information	34

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 years ended December 31, 2007 and 2006, 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 audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free 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 audits provide 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, 2007 and 2006 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.

In accordance with *Government Auditing Standards*, we have also issued our report dated July 15, 2008, 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 audits.

The Management's Discussion and Analysis on pages 3 through 9 and pension plan schedule on pages 33 and 34 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 required supplementary information. However, we did not audit the information and express no opinion on it.

McGladrey & Pullen, LLP

Davenport, Iowa
July 15, 2008

