

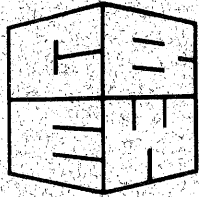
**KEYSTONE RURAL GAS DISTRICT #1  
TULSA COUNTY  
Sand Springs, Oklahoma**

**BASIC FINANCIAL STATEMENTS  
October 31, 2011**

KEYSTONE RURAL GAS DISTRICT #1  
TULSA COUNTY  
Sand Springs, Oklahoma

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## INDEPENDENT AUDITOR'S REPORT

February 21, 2012

Board of Directors  
Keystone Rural Gas District No. 1  
Tulsa County  
Sand Springs, Oklahoma

We have audited the accompanying financial statements of Keystone Rural Gas District No. 1, Tulsa County, Sand Springs, Oklahoma (the District), as of and for the years ended October 31, 2011 and 2010, which collectively comprise the District's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the District's management. Our responsibility is to express opinions 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 the 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 opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Keystone Rural Gas District No. 1, Tulsa County, Sand Springs, Oklahoma as of October 31, 2011 and 2010, and the changes in financial position and cash flows thereof for the years then ended in conformity with accounting principals generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued a report dated February 21, 2012, on our consideration of the Keystone Rural Gas District No. 1's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and 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 District has not presented the Management's Discussion and Analysis required by the Governmental Accounting Standards Board (GASB) that the GASB has determined is necessary to supplement, although not required to be part of, the basic financial statements.

CBEW Professional Group, LLP  
Certified Public Accountants

**KEYSTONE RURAL GAS DISTRICT NO. 1  
TULSA COUNTY  
Sand Springs, Oklahoma**

**STATEMENT OF NET ASSETS  
October 31, 2011 and 2010**

	<u>October 31, 2011</u>	<u>October 31, 2010</u>
<b>Current assets:</b>		
Cash and cash equivalents (Note 1)	\$ 226,178	\$ 298,755
Investments (Note 1)	154,131	153,506
Receivables (net of allowance for uncollectible)	-	8,068
Prepaid insurance	5,277	5,106
Inventory	12,549	12,464
<b>Total current assets</b>	<u>398,135</u>	<u>477,899</u>
<b>Capital assets:</b>		
Buildings, gas system, equipment and vehicles net of depreciation (Note 3)	<u>341,434</u>	<u>390,018</u>
<b>Total capital assets</b>	<u>341,434</u>	<u>390,018</u>
<b>Total assets</b>	<u>\$ 739,568</u>	<u>\$ 867,916</u>
<b>Current liabilities:</b>		
Accounts payable	\$ 14,209	\$ 14,071
Payroll liabilities payable	2,472	(1,747)
Sales tax payable	10	13
Interest payable	-	510
Customer pre-payments	7,540	-
Customer deposits	54,980	52,945
Current portion of notes payable (Note 2)	-	35,935
<b>Total current liabilities</b>	<u>79,211</u>	<u>101,727</u>
<b>Long-term liabilities:</b>		
Notes payable (Note 2)	<u>0</u>	<u>84,384</u>
<b>Total long-term liabilities</b>	<u>0</u>	<u>84,384</u>
<b>Total liabilities</b>	<u>79,211</u>	<u>186,111</u>
<b>Net assets:</b>		
Invested in capital assets, net of related debt	341,434	269,699
Temporarily restricted	-	-
Unrestricted	<u>318,922</u>	<u>412,107</u>
<b>Total net assets</b>	<u>\$ 660,356</u>	<u>\$ 681,805</u>

The accompanying notes are an integral part of the basic financial statements.

**KEYSTONE RURAL GAS DISTRICT NO. 1  
TULSA COUNTY  
Sand Springs, Oklahoma**

**STATEMENT OF ACTIVITIES  
For the Year Ended October 31, 2011 and 2010**

	<u>October 31, 2011</u>	<u>October 31, 2010</u>
<b>Revenues:</b>		
Gas sales	\$ 481,211	\$ 600,495
Late Fees	6,092	10,305
Meter Svc/Tap Fees	2,425	2,724
Other income	411	3,202
	<hr/>	<hr/>
<b>Total revenues</b>	<b>490,139</b>	<b>616,726</b>
	<hr/>	<hr/>
<b>Expenses:</b>		
Accounting and legal	17,690	13,223
Bad debt	1,705	(4,561)
Board Compensation	3,945	3,893
Contract services	26,351	14,365
Depreciation	55,273	56,115
Equipment Rental	-	65
Fuel	7,858	4,187
Gas purchases	133,809	177,527
Gas transportation costs	40,098	38,172
Insurance	30,844	29,352
Miscellaneous	462	279
Office supplies and postage	9,295	12,904
Payroll taxes	9,725	7,905
Postage	5,180	3,085
Repair and maintenance	35,678	29,722
Retirement contributions	2,892	3,043
Salaries	120,351	120,698
Telephone	5,277	3,253
Uniforms	2,180	2,112
Utilities	3,640	3,386
	<hr/>	<hr/>
<b>Total expenses</b>	<b>512,254</b>	<b>518,725</b>
	<hr/>	<hr/>
<b>Operating income</b>	<b>(22,115)</b>	<b>98,001</b>
	<hr/>	<hr/>
<b>Other income and expense:</b>		
Interest income	2,109	3,219
Interest expense	(1,443)	(7,110)
	<hr/>	<hr/>
<b>Total other income and expense</b>	<b>666</b>	<b>(3,891)</b>
	<hr/>	<hr/>
<b>Change in net assets-Net income</b>	<b>(21,449)</b>	<b>94,110</b>
	<hr/>	<hr/>
<b>Net assets - beginning of year</b>	<b>681,805</b>	<b>587,695</b>
	<hr/>	<hr/>
<b>Net assets - end of year</b>	<b>\$ 660,356</b>	<b>\$ 681,805</b>
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The accompanying notes are an integral part of the basic financial statements.

**KEYSTONE RURAL GAS DISTRICT NO. 1  
TULSA COUNTY  
Sand Springs, Oklahoma**

**STATEMENT OF CHANGES IN NET ASSETS  
For the Year Ended October 31, 2011 and 2010**

	<u>Net Assets (Unrestricted)</u>	<u>Net Assets (Temporarily Restricted)</u>	<u>Total Net Assets</u>
<b>Balance - beginning of year 10/31/09</b>	\$ 587,695	\$ -	\$ 587,695
Change in net assets	<u>94,110</u>	<u>-</u>	<u>94,110</u>
<b>Balance - end of year 10/31/10</b>	<u>\$ 681,805</u>	<u>\$ -</u>	<u>\$ 681,805</u>
<b>Balance - beginning of year 10/31/10</b>	\$ 681,805	\$ -	\$ 681,805
Change in net assets	<u>(21,449)</u>	<u>-</u>	<u>(21,449)</u>
<b>Balance - end of year 10/31/11</b>	<u>\$ 660,356</u>	<u>\$ -</u>	<u>\$ 660,356</u>

The accompanying notes are an integral part of the basic financial statements.

**KEYSTONE RURAL GAS DISTRICT NO. 1  
TULSA COUNTY  
Sand Springs, Oklahoma**

**STATEMENT OF CASH FLOWS  
For the Year Ended October 31, 2011 and 2010**

	<u>October 31, 2011</u>	<u>October 31, 2010</u>
<b>Cash flows from operating activities:</b>		
Cash received from customers	\$ 505,491	\$ 628,519
Cash payments to suppliers for goods and contractors and other services	<u>(451,101)</u>	<u>(466,092)</u>
<b>Net cash provided by operating activities</b>	<u>54,390</u>	<u>162,427</u>
 <b>Cash flows from capital and related financing activities:</b>		
Acquisition & construction of capital assets	(6,689)	-
Principal paid on debt	(120,319)	(33,815)
Proceeds received from notes	-	-
Interest paid on debt	(1,443)	(7,110)
<b>Net cash used in capital and related financing activities</b>	<u>(128,451)</u>	<u>(40,925)</u>
 <b>Cash flows from investing activities:</b>		
(Purchase) liquidation of investments	(624)	(100,513)
Interest income	2,108	3,219
<b>Net cash provided by investing activities</b>	<u>1,484</u>	<u>(97,294)</u>
 <b>Net increase (decrease) in cash</b>	<u>(72,577)</u>	<u>24,208</u>
 <b>Cash and cash equivalents at beginning of year</b>	<u>298,755</u>	<u>274,547</u>
 <b>Cash and cash equivalents at end of year</b>	<u>\$ 226,178</u>	<u>\$ 298,755</u>
 <b>Reconciliation of operation income to net cash provided by operating activities:</b>		
Operating income (loss)	\$ <u>(22,115)</u>	\$ <u>98,001</u>
 <b>Adjustments to reconcile net income to net cash provided by operating activities:</b>		
Depreciation	55,273	56,115
Changes in assets and liabilities:		
(Increase) decrease in accounts receivable	8,068	11,809
(Increase) decrease in prepaid expenses	(171)	-
(Increase) decrease in inventory	(85)	(16)
Increase (decrease) in customer deposits	2,035	(1,370)
Increase (decrease) in customer pre-payments	7,540	-
Increase (decrease) in interest payable	(510)	(132)
Increase (decrease) in accounts payable	138	1,896
Increase (decrease) in sales tax payable	(3)	13
Increase (decrease) in payroll taxes payable	<u>4,219</u>	<u>(3,888)</u>
 <b>Total adjustments</b>	<u>76,505</u>	<u>64,427</u>
 <b>Net cash provided by operating activities</b>	<u>\$ 54,390</u>	<u>\$ 162,428</u>

The accompanying notes are an integral part of the basic financial statements.

**KEYSTONE RURAL GAS DISTRICT NO. 1  
TULSA COUNTY  
Sand Springs, Oklahoma**

**NOTES TO THE BASIC FINANCIAL STATEMENTS  
October 31, 2011 and 2010**

**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

Keystone Rural Gas District, Tulsa County, Oklahoma (the District), was created under the provisions of Title 82, O.S. 1981, Sections 1324.1-1324.26 inclusive, for the purpose of providing natural gas to the members it serves. Membership in the gas district consists of gas users who have paid the required membership and connection fees. The District is exempt from federal and state income taxes.

The more significant of the government's accounting policies are described below.

**A. Reporting Entity**

Keystone Rural Gas District No. 1 is an independent, self-contained reporting entity with no associated component units. It is operated in a manner similar to a private business enterprise where the cost (expenses, including depreciation) of providing gas services is financed through user charges. The District purchases the majority of its gas from the Tiger, Inc.

**B. Measurement Focus, Basis of Accounting and Basis of Presentation – Fund Accounting**

The accompanying financial statements have been prepared on the accrual basis of accounting in accordance with Generally Accepted Accounting Principles (GAAP) promulgated in the United States of America. The accounting and financial reporting treatment is accounted for on a flow of economic resources measurement focus. With this measurement focus, all assets and liabilities associated with the operation are included on the statement of net assets. The operating statements present increases (e.g., revenues) and decreases (e.g., expenses) in net total assets. Depreciation expense is provided for capital assets based upon estimated useful lives.

Financial activity is accounted for on the flow of economic resources measurement focus using the accrual basis of accounting. Under this method, revenues are recorded when earned and expenses are recorded at the time liabilities are incurred. In compliance with the Governmental Accounting Standards Board (GASB) Statement No. 29 PCPPA has elected to only apply Financial Accounting Standards Board (FASB), Accounting Principles Board (APB) and Accounting Research Board (ARB) materials issued on or before November 30, 1989 that do not conflict with GASB.

**C. Assets, Liabilities and Equity**

**1. Deposits and Investments**

Oklahoma Statutes authorize the District to invest in certificates of deposit, repurchase agreements, passbooks, bankers' acceptances, and other available bank investments provided that all deposits are fully covered by approved securities pledged to secure those funds. In addition, the District can invest in direct debt securities of the United States unless such an investment is expressly prohibited by law.

All the bank deposits are held at one financial institution and are carried at cost. For purposes of statements of cash flows, the District considers cash and all highly liquid investments with an initial maturity of three months or less to be cash equivalents.



**KEYSTONE RURAL GAS DISTRICT NO. 1  
TULSA COUNTY  
Sand Springs, Oklahoma**

**NOTES TO THE BASIC FINANCIAL STATEMENTS  
October 31, 2011 and 2010**

**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

**C. Assets, Liabilities and Equity (Continued)**

**1. Deposits and Investments (Continued)**

*Custodial Credit Risk*

At October 31, 2011, the District held deposits of approximately \$380,109 at financial institutions. The District's cash deposits, including interest-bearing certificates of deposit, are entirely covered by Federal Depository Insurance (FDIC) or direct obligation of the U.S. Government insured or collateralized with securities held by the District or by its agent in the District's name.

*Investment Interest Rate Risk*

The District does not have a formal investment policy that limits investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates.

*Investment Credit Risk*

The District has no policy that limits its investment choices other than the limitation of state law as follows:

- a. Direct obligations of the U.S. Government, its agencies and instrumentalities to which the full faith and credit of the U.S. Government is pledged, or obligations to the payment of which the full faith and credit of the State is pledged.
- b. Certificates of deposits or savings accounts that are either insured or secured with acceptable collateral with in-state financial institutions, and fully insured certificates of deposit or savings accounts in out-of-state financial institutions.
- c. With certain limitation, negotiable certificates of deposit, prime bankers acceptances, prime commercial paper and repurchase agreements with certain limitations.
- d. County, municipal or school district tax supported debt obligations, bond or revenue anticipation notes, money judgments, or bond or revenue anticipation notes of public trusts whose beneficiary is a county, municipality or school district.
- e. Notes or bonds secured by mortgage or trust deed insured by the Federal Housing Administrator and debentures issued by the Federal Housing Administrator, and in obligations of the National Mortgage Association.
- f. Money market funds regulated by the SEC and in which investments consist of the investments mentioned in the previous paragraphs (a.-d.).

The investments held at October 31, 2011 are as follows:

Type	Weighted Average Maturity (Months)	Credit Rating	Market Value	Cost
Investments				
Certificate of deposit	21.60	N/A	154,131	154,131
Total investments			<u>\$ 154,131</u>	<u>\$ 154,131</u>

**KEYSTONE RURAL GAS DISTRICT NO. 1  
TULSA COUNTY  
Sand Springs, Oklahoma**

**NOTES TO THE BASIC FINANCIAL STATEMENTS  
October 31, 2011 and 2010**

**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

**C. Assets, Liabilities and Equity (Continued)**

**1. Deposits and Investments (Continued)**

*Concentration of Investment Credit Risk*

The District places no limit on the amount it may invest in any one issuer. The District has the following of credit risk: 100% in Certificates of deposit.

**2. Fair Value of Financial Instruments**

The District's financial instruments include cash and cash equivalents, accounts receivable, accounts payable and notes payable. The District's estimate of the fair value of all financial instruments does not differ materially from the aggregate carrying values of its financial instruments recorded in the accompanying statement of net assets. The carrying amount of these financial instruments approximates fair value because of the short maturity of these instruments.

**3. Estimates**

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Accordingly, actual results could differ from those estimates.

**4. Inventories**

Inventories consist primarily of gas line supplies for the addition of new gas lines and repair of old gas lines. Inventory is valued at cost, principally on a first-in, first-out basis, but not in excess of market.

**5. Capital Assets**

Additions to the gas storage delivery system and other equipment are recorded at cost or, if contributed property, at their estimated fair value at time of contribution. Repairs and maintenance are recorded as expenses; renewals and betterments are capitalized. Non-cash contributions relate to both existing and new members of the District. If installation of gas lines is required to a member's property, the District performs this service for the member at cost. The member's payment for such installation is recorded as a capital asset contribution. The District maintains a capitalization threshold of \$500 and an estimated useful life in excess of two (2) years.

Depreciation has been calculated on each class of depreciable property using the straight-line method. Estimated useful lives are as follows:

Gas system	10-50 years
Buildings	10-25 years
Equipment	7-20 years
Office equipment	7-10 years
Vehicles	5 years

**KEYSTONE RURAL GAS DISTRICT NO. 1  
TULSA COUNTY  
Sand Springs, Oklahoma**

**NOTES TO THE BASIC FINANCIAL STATEMENTS  
October 31, 2011 and 2010**

**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

**C. Assets, Liabilities and Equity (Continued)**

**6. Compensated Absences**

It is the District's policy to permit employees to accumulate earned but unused vacation and sick time. Full-time employees are granted vacation and sick leave benefits in varying amounts to specified maximums depending on tenure. The District has not accrued compensated absences because the amount, if any, would not be material to the financial statements.

**7. Customer Deposits**

The District requires that every customer pay a cash deposit upon opening or re-establishing an account with the District to guarantee payment on the account for gas service rendered. When the service is terminated, the deposit is refunded or applied to the outstanding balance due the District. The District maintains a cash reserve sufficient for payment of these deposits. The reserve amount is included in the District's cash and cash equivalents. Interest earned on customer deposits is used for operations of the District.

**8. Subsequent Events**

Subsequent events have been evaluated through February 21, 2012, which is the date the financial statements were available to be issued.

**D. Revenues, Expenses and Other Changes in Net Assets**

**1. Operating Revenues and Expenses**

Operating revenues and expenses are principally from gas sales and connection fees charged to new system subscribers. Customer gas consumption is determined by monthly meter readings taken by District personnel. The gas sales from subscriber gas consumption billed but unpaid at the District's year-end are recognized as revenue in the current year and reported in the statement of net assets as accounts receivable. Operating expense consist of those costs necessary to operate and maintain the gas distribution system and for general administration of the District.

**2. Non-Operating Revenue and Expenses**

Non-operating revenues and expenses consist of investment earnings, interest expense incurred on the District's notes payable and gains and losses on sales or the abandonment of long-lived assets.

**3. Bad Debts**

The District uses the direct write-off method for recognizing bad debts. Under the direct write-off method, accounts receivable are charged to income during the period they are determined to be uncollectible. The use of this method does not result in a material difference from the valuation method required by generally accepted accounting principles.

**KEYSTONE RURAL GAS DISTRICT NO. 1  
TULSA COUNTY  
Sand Springs, Oklahoma**

**NOTES TO THE BASIC FINANCIAL STATEMENTS  
October 31, 2011 and 2010**

**2. LONG-TERM DEBT**

Long-term debt consists of one note with American Heritage Bank. The notes are secured by the gas system.

American Heritage Bank #4712601 – 15 year note originated on June 1, 1998, payable in monthly installments of \$3,423 at 5% interest

The following is a summary of long-term debt transactions during the year:

	Balance October 31, 2010	Additions	Reductions	Balance October 31, 2011
American Heritage Bank	120,319	-	120,319	-
Total	\$ 120,319	\$ -	\$ 120,319	\$ -

**3. CAPITAL ASSETS**

The following is a summary of changes in property, plant and equipment.

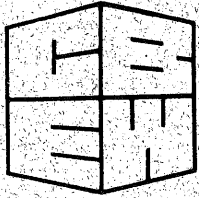
	Balance October 31, 2010	Additions	Deletions	Balance October 31, 2011
Buildings	61,511	-	-	61,511
Gas System & Equipment	999,309	6,689	-	1,005,998
Office equipment	9,916	-	1,481	8,435
Vehicles	47,386	-	-	47,386
Total	1,118,122	6,689	1,481	1,123,330
Less accumulated depreciation	728,104	55,273	1,481	781,896
Net	\$ 390,018	\$ (48,584)	\$ -	\$ 341,434

**4. RISK MANAGEMENT**

Keystone Rural Gas District No. 1 is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. The District continues to carry commercial insurance for these risks, including general and auto liability, property damage, and public officials liability. Settled claims resulting from these risks have not exceeded the commercial insurance coverage in any of the past three fiscal years.

**KEYSTONE RURAL GAS DISTRICT #1  
TULSA COUNTY  
Sand Springs, Oklahoma**

**REPORT REQUIRED BY *GOVERNMENT AUDITING STANDARDS*  
October 31, 2011**



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**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**

February 21, 2012

Board of Directors  
Keystone Rural Gas District No. 1  
Tulsa County  
Sand Springs, Oklahoma

We have audited the basic financial statements of the Keystone Rural Gas District No. 1, Tulsa County, Sand Springs, Oklahoma (the District), as of and for the year ended October 31, 2011, and have issued our report thereon dated February 21, 2012. 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. The District did not present the Management's Discussion and Analysis required by the Governmental Accounting Standards Board.

Internal Control Over Financial Reporting

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

A *deficiency in internal control* 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 and correct misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above. However, we identified certain deficiencies in internal control over financial reporting, described in the accompanying schedule of findings and responses that we consider to be significant deficiencies in internal control over financial reporting. The finding reference number is 11-1. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Keystone Rural Gas District No. 1  
February 21, 2012

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the District's 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*.

The District's response to the finding identified in our audit is described in the accompanying schedule of findings and responses. We did not audit the District's response and, accordingly, we express no opinion on it.

This report is intended solely for the information and use of management, all applicable federal and state agencies, and is not intended to be and should not be used by anyone other than these specified parties.

*CBEW Professional Group, LLP*

CBEW Professional Group, LLP  
Certified Public Accountants

**KEYSTONE RURAL GAS DISTRICT #1  
TULSA COUNTY  
Sand Springs, Oklahoma**

**SCHEDULE OF FINDINGS AND RESPONSES  
For the Year Ended October 31, 2011**

11-1. Internal Control – Segregation of Duties

Criteria: The segregation of duties and responsibilities between different individuals for custody of assets, recordkeeping for those assets and reconciliation of those asset accounts is an important control activity needed to adequately protect the entity's assets and ensure accurate financial reporting.

Condition: Presently the same individual that receives utility service related cash payments is also responsible for service billing and adjustment, also balances the daily cash drawer, posts payments to subsidiary accounts receivable ledger and reconciles the monthly bank statements. In addition, only limited oversight is provided over this individual in the conduct of their daily functions.

Cause: The district's limited size and staffing resources have made it difficult for management to provide sufficient staffing to fully segregate incompatible duties in a cost-effective manner.

Effect or Potential Effect: Without sufficient segregation of duties, the risk significantly increases that errors and fraud related to utility billing and collection activities, including misappropriation of assets, could occur and not be detected within a timely basis.

Recommendation: We recommend that management and the board should consider a formal evaluation of their risks associated with this lack of duties segregation over utility cash and receivables. In response to the identified risks, consideration should be given to identifying and implementing controls that could help mitigate the risks associated with lack of segregation of duties, such as providing increased management oversight and an independent reconciliation of accounts. For example, the entity might consider soliciting the assistance of independent volunteer labor to perform certain functions including to act as compensating procedures where applicable.

Responsible Official's Response: The district concurs with the recommendation, although, the cost to correct this condition might exceed the benefit, the district has made certain changes in procedures that will improve the overall lack of segregation of duties and has implemented compensating procedures as appropriate.