

**Financial Statements and Reports of
Independent Certified Public Accountant
Rural Water District No. 6
Nowata County, Oklahoma
June 30, 2011**

**TURNER & ASSOCIATES, PLC
Certified Public Accountants
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**Rural Water District No. 6
Nowata County, Oklahoma
Water District Officials
June 30, 2011**

Board of Directors

Jerry Pearsall
Vincent Pritchett
Jeff Plumber
Lloyd Johnson
Gary Minnerath

Chairman
Vice-Chairman
Secretary/Treasurer
Member
Member

Rural Water District No. 6
Nowata County, Oklahoma
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Independent Auditor's Report

Board of Directors
Rural Water District No. 6
Nowata County, Oklahoma

We have audited the accompanying financial statements of the business-type activities of the Rural Water District No. 6, Nowata County, Oklahoma, as of and for the year ended June 30, 2011, which 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 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 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 audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the business-type activities of the Rural Water District No. 6, Nowata County, Oklahoma as of June 30, 2011, and the changes in financial position and cash flows thereof 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 September 8, 2011, on our consideration of the Rural Water District No. 6, Nowata County, Oklahoma's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on 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 Rural Water District No. 6, Nowata County, Oklahoma 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.

TURNER & Associates, PLC

Vinita, OK
September 8, 2011



**REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND COMPLIANCE
AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS
PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS**

Board of Directors
Rural Water District No. 6
Nowata County, Oklahoma

We have audited the financial statements of the business-type activities of the Rural Water District No. 6, Nowata County, Oklahoma, as of and for the year ended June 30, 2011, which comprise the District's basic financial statements and have issued our report thereon dated September 8, 2011. The Rural Water District No. 6, Nowata County, Oklahoma did not present the Management's Discussion and Analysis that accounting principles generally accepted in the United States of America require to supplement, although not to be part of, the basic financial statements. 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 the Rural Water District No. 6, Nowata County, Oklahoma's internal control over financial reporting as a basis for designing our audit procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Rural Water District No. 6, Nowata County, Oklahoma's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Rural Water District No. 6, Nowata County, Oklahoma's internal control over financial reporting.

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. However, as described in the accompanying schedule of findings and questioned costs, we identified certain deficiencies in internal control over financial reporting, describe in the accompanying schedule of findings and questioned costs that we consider to be material weaknesses in 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. We consider the deficiencies, 2011-1 and 2011-4 described in the accompanying schedule of findings and questioned costs to be material weaknesses.

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. We consider the deficiencies, 2011-2 and 2011-3 described in the accompanying schedule of findings and questioned costs to be significant deficiencies.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Rural Water District No. 6, Nowata County, Oklahoma's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grants 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 an instance of noncompliance or other matter that is required to be reported under *Government Auditing Standards* and which is described in the accompanying schedule of findings and responses as item 2011-5.

The Rural Water District No. 6, Nowata County, Oklahoma's response to the findings identified in our audit is described in the accompanying schedule of findings and responses. We did not audit the Rural Water District No. 6, Nowata County's response and, accordingly, we express no opinion on it.

This report is intended solely for the information and use of the Board of Directors, management, and the Oklahoma State Auditor and is not intended to be and should not be used by anyone other than these specified parties.

TURNER & ASSOCIATES, PLLC

Vinita, OK
September 8, 2011

Rural Water District No. 6
Nowata County, Oklahoma
Balance Sheet
June 30, 2011

	June 30, 2011	June 30, 2010 (Memo Only)
ASSETS		
Current Assets		
Cash and Equivalents	\$ 138,895.18	\$ 134,198.03
Accounts Receivable	24,623.15	23,514.37
Other Accrued Receivables	-	34,658.10
Inventory	44,730.00	73,377.36
Prepaid Expenses	3,142.39	3,824.09
Total Current Assets	211,390.72	269,571.95
Non-current Assets		
Capital Assets		
Property, Plant and Equipment, net	475,108.38	366,682.31
Land	10,488.70	10,488.70
Construction in Progress	-	46,774.90
Total Capital Assets	485,597.08	423,945.91
TOTAL ASSETS	\$ 696,987.80	\$ 693,517.86
LIABILITIES AND NET ASSETS		
Current Liabilities		
Accounts Payable	\$ 13,783.29	\$ 9,797.78
Net Assets		
Invested in Capital Assets, net of Related Debt	485,597.08	423,945.91
Unrestricted	197,607.43	259,774.17
Total Net Assets	683,204.51	683,720.08
TOTAL LIABILITIES AND NET ASSETS	\$ 696,987.80	\$ 693,517.86

The accompanying Notes to the Financial Statements are an integral part of this statement.

Rural Water District No. 6
Nowata County, Oklahoma
Statement of Revenues, Expenses and Changes in Net Assets
For the Year Ended June 30, 2011

	<u>June 30, 2011</u>	<u>June 30, 2010</u> (Memo Only)
Operating Revenues		
Water Revenues	\$ 163,316.87	\$ 142,786.18
Penalties and Fees	4,771.24	3,433.15
Reimbursements	-	34,658.10
Other Operating Revenues	<u>7,536.89</u>	<u>5,271.32</u>
Total Operating Revenues	<u>175,625.00</u>	<u>186,148.75</u>
Operating Expenses		
Accounting	16,806.40	16,411.57
Depreciation	22,689.46	20,185.96
Insurance	4,105.50	3,648.02
Miscellaneous	1,701.88	1,395.99
Office Expense	2,620.09	2,534.86
Operator	12,033.00	12,200.00
Postage & Freight	1,545.00	1,412.65
Repairs and Maintenance	18,965.39	7,640.00
Supplies	29,165.54	7,316.17
Telephone	2,120.14	1,679.41
Testing	440.00	430.00
Utilities	5,638.44	6,140.12
Water Purchases	<u>77,805.05</u>	<u>99,521.48</u>
Total Operating Expenses	<u>195,635.89</u>	<u>180,516.23</u>
Operating Income (Loss)	(20,010.89)	5,632.52
Non-Operating Revenues (Expenses)		
Interest Income	245.32	194.02
Capital Contributions		
Membership Fees	<u>19,250.00</u>	<u>8,750.00</u>
Net Income (Loss)	(515.57)	14,576.54
Net Assets, Beginning of Year	<u>683,720.08</u>	<u>669,143.54</u>
Net Assets, End of Year	<u>\$ 683,204.51</u>	<u>\$ 683,720.08</u>

The accompanying Notes to the Financial Statements are an integral part of this statement.

Rural Water District No. 6
Nowata County, Oklahoma
Statement of Cash Flows
For the Year Ended June 30, 2011

Cash Flows from Operating Activities		
Cash Inflows:		
Payments Received from Customers	\$	209,174.32
Cash Outflows:		
Payments to Suppliers for Goods and Services		(168,279.22)
Net Cash Provided (Used) by Operating Activities		<u>40,895.10</u>
Cash Flows from Capital and Related Financing Activities		
Purchase of Capital Assets		(55,693.27)
Membership Fees Received		19,250.00
Net Cash Provided (Used) by Capital and Related Financing Activities		<u>(36,443.27)</u>
Cash Flows from Investing Activities		
Interest Received		245.32
Net Cash Provided (Used) by Investing Activities		<u>245.32</u>
Net Cash Inflow (Outflow) from All Activities		4,697.15
Cash and Cash Equivalents at Beginning of Year		134,198.03
Cash and Cash Equivalents at End of Year	\$	<u>138,895.18</u>
Reconciliation of Operating Income (Loss) to Net Cash		
Provided by Operating Activities:		
Operating Income (Loss)	\$	(20,010.89)
Depreciation		22,689.46
(Increase) Decrease in:		
Accounts Receivable		(1,108.78)
Other Accrued Receivables		34,658.10
Prepaid Expenses		681.70
Increase (Decrease) in:		
Accounts Payable		3,985.51
Net Cash Provided (Used) by Operating Activities	\$	<u>40,895.10</u>

The accompanying Notes to the Financial Statements are an integral part of this statement.

Rural Water District No. 6
Nowata County, Oklahoma
Notes to the Financial Statements
For the Year Ended June 30, 2011

The following notes to the financial statements are an integral part of Rural Water District No. 6's financial statements.

I. Summary of Significant Accounting Policies

Rural Water District No. 6, Nowata 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 water to the members of the District it serves. Membership in the water district consists of water users who have paid the required membership and connection fees. The District is exempt from federal and state income taxes.

The membership consists of approximately 321 users, each entitled one vote. The Board of Directors consists of 5 members serving one to three-year terms. The vacant Board seats are elected at the annual meeting, and following, the Board of Directors meet and elect a chairman, vice-chairman and secretary/treasurer. All Board members serve without pay.

The accounting policies of the District conform to generally accepted accounting principles applicable to governmental units. The District complies with generally accepted accounting principles and applies all relevant Government Accounting Standards Board (GASB) pronouncements. In addition, the District applies Financial Accounting Standards Board (FASB) pronouncements and Accounting Principles Board opinions issued on or before November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements, in which case, GASB prevails. The District has elected not to follow FASB pronouncements issued since that date.

A. Financial Reporting Entity

The District complies with GASB Statement No. 14, "*The Financial Reporting Entity*." This statement establishes standards for defining and reporting on the financial reporting entity. It defines component units as legally separate organizations for which the elected officials of the primary government are financially accountable and other organizations for which the nature and significance of their relationship with a primary government are such that exclusion would cause the reporting entity's financial statements to be misleading or incomplete.

The District considered all potential component units in determining what organizations should be included in the financial statements. Based on these criteria, there are no component units to include in the District's financial statements.

Rural Water District No. 6
Nowata County, Oklahoma
Notes to the Financial Statements
For the Year Ended June 30, 2011

I. Summary of Significant Accounting Policies (continued)

B. Basis of Presentation

The District's fund is an enterprise fund. Enterprise funds are proprietary funds used to account for business-like activities provided to the general public. These activities are financed primarily by user charges and the measurement of financial activity focuses on net income measurement similar to the private sector.

C. Measurement Focus and Basis of Accounting

Measurement focus is a term used to describe *which* transactions are recorded within the various financial statements. Basis of accounting refers to *when* transactions are recorded regardless of the measurement focus applied.

The proprietary funds utilize an "*economic resources*" measurement focus. The accounting objectives of this measurement focus are the determination of operating income, changes in net assets (or cost recovery), financial position and cash flows. All assets and liabilities (whether current or noncurrent) associated with their activities are reported. Proprietary fund equity is classified as net assets.

All proprietary funds utilize the accrual basis of accounting. Under the accrual basis of accounting, revenues are recognized when earned and expenses are recorded when the liability is incurred or economic asset used.

Proprietary funds distinguish *operating* revenues and expenses from *nonoperating* items. Operating revenues and expenses generally result from providing services in connection with a proprietary fund's principal ongoing operations. The principal operating revenues of the District's enterprise fund is charges to customers for sales and services. The District also recognizes as operating revenue the portion of tap fees intended to recover the cost of connecting new customers to the system. Operating expenses for enterprise funds include the cost of sales and services, administrative expenses and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

D. Assets, Liabilities and Net Assets

1. Cash and Cash Equivalents

For purposes of the statement of cash flows, the District considers all cash on hand, demand deposits, and highly liquid investments, with an original maturity of three months or less when purchased, to be cash and cash equivalents.

Rural Water District No. 6
Nowata County, Oklahoma
Notes to the Financial Statements
For the Year Ended June 30, 2011

I. Summary of Significant Accounting Policies (continued)

D. Assets, Liabilities and Net Assets (continued)

2. Fair Value of Financial Instruments

The District's financial statements include cash and investments. The District's estimates of the fair value of all financial instruments do not differ materially from the aggregate carrying values of its financial instruments recorded in the accompanying balance sheet. The carrying amount of these financial instruments approximates fair value because of the short maturity of these instruments.

3. Inventory of Supplies and Materials

Inventories of the district consist of material and supplies used in operations. Material and supplies are reported as expenses immediately when purchased. For any significant inventory that exists at year-end, a journal entry is made to reflect the amount on hand.

4. Accounts Receivable

Accounts receivable consists primarily of charges for water sales. Management considers the accounts to be fully collectible.

5. Prepaid Expenses

Prepaid expenses represent the unexpired premiums on general liability and workman's compensation insurance policies.

6. Capital Assets

The water storage and delivery system and furniture and equipment are recorded at cost. Donated capital assets are reported at estimated fair market value at the date of donation.

The cost of normal maintenance and repairs that do not add to the value of the asset or materially extend asset lives are not capitalized.

All reported capital assets are depreciated on the straight-line basis over the estimated useful lives ranging from five to fifty years.

The board determines on an item by item basis whether to capitalize or expense.

Rural Water District No. 6
Nowata County, Oklahoma
Notes to the Financial Statements
For the Year Ended June 30, 2011

I. Summary of Significant Accounting Policies (continued)

D. Assets, Liabilities and Net Assets (continued)

7. Equity Classifications

Equity is classified as net assets and displayed in three components:

- a. Invested in capital assets, net of related debt --- Consists of capital assets including restricted capital assets, net of accumulated depreciation and reduced by the outstanding balances of any mortgages, notes, or other borrowings that are attributable to the acquisition, construction or improvement of those assets.
- b. Restricted net assets --- Consists of net assets with constraints placed on the use either by (1) external groups such as creditors, grantors, contributors, or laws or regulations of other governments; or (2) law through constitutional provisions or enabling legislation.
- c. Unrestricted net assets --- All other net assets that do not meet the definition of “restricted” or “invested in capital assets, net of related debt.”

8. Use of Estimates

The preparation of financial statements in conformity with U.S. 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. Actual results could differ from those estimates.

II. Detailed Notes Concerning the Funds

A. Cash and Investments

Authorized Investments. The district’s policy for eligible investments is governed by State statutes which, in general, allow the District to invest in obligations of the United States and insured or collateralized Certificate of Deposits.

Custodial Credit Risk – Deposits. Custodial credit risk is the risk that in the event of a bank failure, the District’s deposits may not be returned to it. The District’s cash deposits, including interest-bearing certificates of deposit, are maintained in financial institutions. The District does not have a deposit policy for custodial credit risk. As of June 30, 2011, none of the District’s investments were exposed to custodial credit risk because they were uninsured or uncollateralized.

Interest rate risk. This 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. 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.

Rural Water District No. 6
Nowata County, Oklahoma
Notes to the Financial Statements
For the Year Ended June 30, 2011

II. Detailed Notes Concerning the Funds (continued)

B. Accounts Receivable

Following is an aged schedule of accounts receivable as of June 30, 2011:

<u>0-30 Days</u>	<u>31-60 Days</u>	<u>61-90 Days</u>	<u>Over 90 Days</u>	<u>Total</u>
\$ 21,102.21	\$ 1,046.29	\$ 525.37	\$ 1,949.28	\$ 24,623.15

C. Changes in Capital Assets

Capital asset activity for the year was as follows:

	<u>Beginning of Year</u>	<u>Additions</u>	<u>Deletions</u>	<u>End of Year</u>
Depreciable Capital Assets				
Water Distribution System	\$ 661,036.45	\$ 128,220.53	\$ -	\$ 789,256.98
Building	62,540.64	-	-	62,540.64
Office Equipment	4,250.00	-	-	4,250.00
Other Equipment	1,705.45	2,895.00	-	4,600.45
Total Capital Assets	<u>729,532.54</u>	<u>131,115.53</u>	<u>-</u>	<u>860,648.07</u>
Less: Accumulated Depreciation	<u>(362,850.23)</u>	<u>(22,689.46)</u>	<u>-</u>	<u>(385,539.69)</u>
Net Depreciable Assets	<u>366,682.31</u>	<u>108,426.07</u>	<u>-</u>	<u>475,108.38</u>
Non-depreciable Assets				
Land	10,488.70	-	-	10,488.70
Construction in Progress	46,774.90	-	46,774.90	-
Total Non-Depreciable Assets	<u>57,263.60</u>	<u>-</u>	<u>46,774.90</u>	<u>10,488.70</u>
Net Book Value	<u>\$ 423,945.91</u>	<u>\$ 108,426.07</u>	<u>\$ 46,774.90</u>	<u>\$ 485,597.08</u>

III. Other Information

A. Risk Management

The District 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 purchases commercial insurance to cover these risks, including general and auto liability, property damage, and public officials liability. There were no significant reductions in insurance coverage from the prior year. Settled claims resulting from these risks have not exceeded commercial insurance coverage in any of the past three fiscal years.

**Rural Water District No. 6
Nowata County, Oklahoma
Notes to the Financial Statements
For the Year Ended June 30, 2011**

III. Other Information (continued)

B. Rates and Fees

Current rates include a \$15.00 minimum charge and then \$5.13 per 1,000 gallons.

**Rural Water District No. 6
Nowata County, Oklahoma
Schedule of Findings and Responses
For the Year Ended June 30, 2011**

FINDINGS - FINANCIAL STATEMENT AUDIT

2011-1 Material Weakness in Internal Control over Financial Reporting – Preparation of Financial Statements in Accordance with GAAP

Criteria:

The government's management is responsible for internal controls over financial reporting. This includes controls over the fair and complete presentation of the government's annual financial statements in accordance with generally accepted accounting principles (GAAP). The preparation of financial statements in accordance with GAAP requires internal controls over both (1) recording, processing, and summarizing accounting data (i.e. maintaining internal books and records, and (2) reporting government-wide and fund financial statements, including related footnotes (i.e. external financial reporting). Professional audit standards clearly indicate that the external financial statement auditor cannot perform any part of management's control activities or be a component of the internal controls over financial reporting.

Condition:

As is the case with many smaller and medium-sized entities, the government has historically relied extensively on its independent external auditors to provide the necessary expertise to assist in the preparation of the financial statements and footnotes as part of its controls over the external financial reporting process. Accordingly, the government's ability to prepare financial statements in accordance with GAAP is based, in part, on its external auditors, who cannot by definition be considered a part of the government's internal controls.

Cause:

The government lacks the necessary knowledge, expertise and education relative to preparing GAAP financial statements. As a result, management has elected to use outside assistance from the external auditors to assist in meeting its responsibilities relative to preparing its annual financial statements.

Effect or Potential Effect:

As a result of this condition, without reliance on its external auditors, the government lacks the necessary internal controls over the preparation of financial statements in accordance with GAAP. This condition also places the auditor in a questionable position regarding auditor independence as a result of potentially performing part of management's functions.

Recommendation:

The government should consider designing and implementing sufficient internal controls over financial reporting by obtaining the necessary knowledge, expertise, and continuing education to prepare financial statements in accordance with generally accepted account principles without reliance on the external financial statement auditor.

Client Response:

The District does not believe it is cost effective, due to the size of the entity, to hire someone else to prepare the financial statements. They will continue to rely on the auditing firm to draft the financial statements from their accounting information.

**Rural Water District No. 6
Nowata County, Oklahoma
Schedule of Findings and Responses
For the Year Ended June 30, 2011**

2011-2 Controls over Inventory

Criteria:

Internal controls should be in place over the receipt, disbursements and recording of inventory items. Inventory should be reconciled on a monthly and annual basis to prevent or detect material misstatements in the financial statements, including disclosures.

Condition:

Inventory is not currently being recorded. The district relies on the auditor to determine any inventory amounts that should be recorded.

Cause:

The District does not currently have any policies and procedures in place to specify the correct treatment for inventory.

Effect:

An adjustment to record inventory was required in the amount of \$28,647.36.

Recommendation:

In order to maintain accurate accounting records, the implementation of an inventory control system is crucial. Governmental proprietary funds should recognize inventories as assets when purchased and report as expenses when used (consumption method). To ensure the completion of these steps, an inventory policy should be added into the District's policy and procedures manual.

Client Response:

Normally the district does not maintain an inventory balance that is material to the financial statements. The district intends to use the entire inventory on one project and after it is complete will not have a significant amount of inventory.

**Rural Water District No. 6
Nowata County, Oklahoma
Schedule of Findings and Responses
For the Year Ended June 30, 2011**

2011-3 Segregation of Duties

Criteria:

Incompatible accounting duties should be performed by different individuals when possible.

Condition:

The bookkeeper opens the mail, makes deposits, prepares checks, receives bank statements/ canceled checks and prepares the bank reconciliations. The bookkeeper also records all receipts and disbursements and makes all journal entries in the accounting software.

Cause:

The district relies on one person to perform all accounting duties.

Effect:

The potential effect is the loss of assets due to not being able to detect losses from fraud or error.

Recommendation:

Separation of duties is one of the most effective controls to prevent or detect misappropriations of assets. When possible, incompatible duties should be performed by different individuals. For example, the responsibility for authorizing transactions, recording transactions, and maintaining custody of assets should be assigned to different people in the District to the extent possible.

Client Response:

The District does not believe it is cost effective, due to the size of the entity, to hire someone else to perform accounting function.

Rural Water District No. 6
Nowata County, Oklahoma
Schedule of Findings and Responses
For the Year Ended June 30, 2011

2011-4 Material Adjusting Journal Entries

Criteria:

The government's management is responsible for internal controls over accounting and financial reporting. This responsibility includes the design and implantation of controls over the fair and complete presentation of the government's annual financial statements in accordance with generally accepted accounting principles (GAAP) from trial balances derived from the government's accounting records. For trial balances to be both complete and accurate, the government must have effective internal controls over recording, processing, summarizing, and adjusting accounting data. As evidence of effective internal controls over accounting and financial reporting, there should generally be few, if any, material adjustments to the trial balances required that are detected and corrected solely as a result of the financial statement audit. In other words, government management should not rely on the external auditor to detect and correct material misstatements in the books and records as part of its internal control, but rather should have its own procedures designed and in place that are independent of the external auditor to provide reasonable, although not absolute, assurance that material misstatements will be detected and corrected in its trial balances prior to audit.

Condition:

The government's trial balances for the year ended June 30, 2011, required a number of material adjusting journal entries in order for the financial statements to be prepared in accordance with GAAP. These necessary adjusting entries, identified solely as a result of the financial statement audit, included such adjustments as the following: adjusting cash and investments, adjusting inventory, adjusting accounts receivable and accounts payable; adjusting prepaid insurance, accrued interest, capitalizing assets and recording depreciation.

Cause:

The government's accounting and financial reporting staff lacks the necessary knowledge, expertise and education, relative to the complex nature of applying GAAP applicable to state and local governments, sufficient to provide reasonable assurance that the trial balances used for preparing the GAAP financial statements are complete and accurate prior to audit. As a result, management has had to rely on the external auditors to identify and correct a number of material misstatements in the trial balances.

Effect:

As a result of this condition, without reliance on its external auditors, the government lacks the necessary internal controls over the completeness and accuracy of the trial balances that are used in the preparation of its financial statements in accordance with GAAP. This condition can result in undetected and uncorrected material misstatements in the financial statements that are not detected by management and may also not be detected by the financial statement audit. In addition, if management's intentions are to continue to rely on the external auditor to detect and correct material misstatements, this condition could place the auditor in a questionable position regarding auditor independence as a result of the auditor performing part of management's functions regarding to the trial balances.

**Rural Water District No. 6
Nowata County, Oklahoma
Schedule of Findings and Responses
For the Year Ended June 30, 2011**

2011-4 Material Adjusting Journal Entries (continued)

Recommendation:

The government should consider designing and implementing sufficient internal controls over the completeness and accuracy of trial balances by obtaining the necessary knowledge, expertise, and continuing education to apply GAAP in the development of working trial balances that will be used to prepare the government's annual financial statements. This could be achieved through employment of qualified accounting staff or the outsourcing of these control activities to a qualified accounting firm other than the external auditor.

Client Response:

The District does not believe it is cost effective, due to the size of the entity, to hire someone else to prepare the adjusting journal entries for the financial statements. They will continue to rely on the auditing firm to prepare the adjusting journal entries for the financial statements from their accounting information.

**Rural Water District No. 6
Nowata County, Oklahoma
Schedule of Findings and Responses
For the Year Ended June 30, 2011**

2011-5 Preparation of Annual Budget

Criteria:

According to Title 82 of the Oklahoma Statutes Section 1324.18, paragraph A, Board of Directors shall annually prepare an estimated budget for the coming year, adjust rates if necessary, to produce sufficient revenue required by such budget.

Condition:

The District did not complete a budget for the year ended June 30, 2011.

Effect or Potential Effect:

The District did not comply with Oklahoma Statutes. The budget serves as a monitoring tool for the board and management. It can be used to determine how well the system is being managed.

Recommendation:

To comply with the Oklahoma Statutes, we recommend that a budget be completed at the end of your fiscal year for the next fiscal year. Information used to prepare the budget could include (1) history of the system, past years income and expenses, (2) long range plans, what the district wants to accomplish the upcoming year as well as long term, (3) funding, where you plan to get the funds to complete these projects, such as savings, loans, grants, etc.

Client Response:

None.