

**LONE CHIMNEY WATER ASSOCIATION**

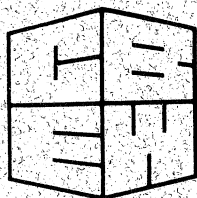
**BASIC FINANCIAL STATEMENTS**

**June 30, 2012**

# LONE CHIMNEY WATER ASSOCIATION

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**INDEPENDENT AUDITOR'S REPORT**

August 23, 2012

Board of Directors  
Lone Chimney Water Association

We have audited the accompanying financial statements of Lone Chimney Water Association (the Association), as of and for the year ended June 30, 2012 and 2011, which collectively comprise the Association's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the Association'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 Lone Chimney Water Association as of June 30, 2012 and 2011, 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 August 23, 2012, on our consideration of the Lone Chimney Water Association'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 Association has not presented Management's Discussion and Analysis that governmental accounting principles generally accepted in the United States of America require to be presented to supplement the basic financial statements. Such missing information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board (GASB), who considers it to be an essential part of the financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. Our opinion on the basic financial statements is not affected by this missing information.

*CBEW Professional Group, LLP*

CBEW Professional Group, LLP  
Certified Public Accountants

**LONE CHIMNEY WATER ASSOCIATION**  
**STATEMENT OF NET ASSETS**  
**June 30, 2012 and 2011**

	<b>June 30, 2012</b>	<b>June 30, 2011</b>
<b>Assets:</b>		
Cash and cash equivalents (Note 1)	\$ 341,651	\$ 68,187
Investments	401,990	400,811
Accounts receivables (net of allowance for uncollectible)	97,893	72,411
Unbilled revenues	94,612	92,932
County receivable	-	-
Prepaid insurance	29,201	28,787
Inventory (Note 1)	59,069	53,545
Temporarily restricted assets:		
Cash and cash equivalents (Note 1)	273,265	351,203
Restricted assets:		
Customer deposits (Note 1)	200	600
<b>Capital assets:</b>		
Land	270,707	270,707
Construction in process	124,199	-
Water system, buildings, improvements and equipment, net of depreciation (Notes 1 & 3)	4,160,679	4,474,562
<b>Other:</b>		
Loan issue costs, net of amortization	68,091	-
Easements, net of amortization	250,949	269,539
<b>Total assets</b>	<b>\$ 6,172,506</b>	<b>\$ 6,083,284</b>
<b>Liabilities:</b>		
Accounts payable	\$ 53,041	\$ 23,798
Customer deposits	200	600
Payroll taxes payable	712	1,576
Accrued Compensation	3,627	2,267
Interest payable	23,184	3,837
Notes payable (Note 2)	2,585,000	2,611,615
<b>Total liabilities</b>	<b>2,665,764</b>	<b>2,643,693</b>
<b>Net assets:</b>		
Invested in capital assets, net of related debt	1,846,386	2,133,654
Temporarily restricted (Note 1)	273,265	351,203
Unrestricted	1,387,091	954,734
<b>Total net assets</b>	<b>\$ 3,506,742</b>	<b>3,439,591</b>
<b>Total liabilities and net assets</b>	<b>6,172,506</b>	<b>\$ 6,083,284</b>

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

**LONE CHIMNEY WATER ASSOCIATION**  
**STATEMENT OF ACTIVITIES**  
For the Year Ended June 30, 2012 and 2011

	<u>June 30, 2012</u>	<u>June 30, 2011</u>
<b>Revenues:</b>		
Water sales	\$ 1,225,330	\$ 1,100,181
Late charges	-	-
Miscellaneous income	<u>17,790</u>	<u>2,250</u>
<b>Total revenues</b>	<u>1,243,120</u>	<u>1,102,431</u>
<b>Expenses:</b>		
Amortization	19,744	18,590
Bank charges	250	263
Contract services	-	-
Depreciation	342,924	339,818
Employee benefits	11,065	1,140
Insurance	113,158	103,768
Lab fees	20,865	18,184
Legal and accounting	5,580	6,200
Licenses and permits	619	66
Miscellaneous	7,144	-
Office supplies and postage	5,381	4,548
Payroll taxes	21,952	15,509
Rental expense	4,800	4,800
Repair and maintenance	50,016	81,863
Salaries	248,626	232,819
Supplies	123,731	141,560
Surveying	765	-
Telephone	7,079	6,699
Transportation	30,435	30,409
Travel	1,018	1,313
Utilities	<u>109,058</u>	<u>108,830</u>
<b>Total expenses</b>	<u>1,124,210</u>	<u>1,116,379</u>
<b>Operating income (loss)</b>	<u>118,910</u>	<u>(13,948)</u>
<b>Other income and expense:</b>		
Interest income	6,612	8,034
Grants	-	-
Trustee fees	(1,250)	(750)
Sale of assets	-	1,860
Interest expense	<u>(57,120)</u>	<u>(109,262)</u>
<b>Total other income and expense</b>	<u>(51,758)</u>	<u>(100,118)</u>
<b>Change in net assets-Net income (loss)</b>	67,152	(114,066)
<b>Net assets - beginning of year</b>	<u>3,439,590</u>	<u>3,553,657</u>
<b>Net assets - end of year</b>	<u>\$ 3,506,742</u>	<u>\$ 3,439,591</u>

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

**LONE CHIMNEY WATER ASSOCIATION**  
**STATEMENT OF CHANGES IN NET ASSETS**  
For the Year Ended June 30, 2012 and 2011

	<u>Net Assets (Unrestricted)</u>	<u>Net Assets (Temporarily Restricted)</u>	<u>Total Net Assets</u>
<b>Balance - beginning of year 6-30-10</b>	\$ 3,247,268	\$ 306,388	\$ 3,553,656
Change in net assets	<u>(158,881)</u>	<u>44,815</u>	<u>(114,066)</u>
<b>Balance - end of year 6-30-11</b>	\$ <u>3,088,387</u>	\$ <u>351,203</u>	\$ <u>3,439,590</u>
 <b>Balance - beginning of year 6-30-11</b>	 \$ 3,088,387	 \$ 351,203	 \$ 3,439,590
Change in net assets	<u>145,090</u>	<u>(77,938)</u>	<u>67,152</u>
<b>Balance - end of year 6-30-12</b>	\$ <u>3,233,477</u>	\$ <u>273,265</u>	\$ <u>3,506,742</u>

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

**LONE CHIMNEY WATER ASSOCIATION**  
**STATEMENT OF CASH FLOWS**  
For the Year Ended June 30, 2012 and 2011

	June 30, 2012	June 30, 2011
<b>Cash flows from operating activities:</b>		
Cash received from customers	\$ 1,215,958	\$ 1,100,273
Cash payments to suppliers for goods & contractors & other services	(737,743)	(743,688)
<b>Net cash provided by operating activities</b>	<u>478,215</u>	<u>356,585</u>
<b>Cash flows from capital and related financing activities:</b>		
Acquisition & construction of capital assets	(153,239)	(42,485)
Principal paid on debt	(2,611,615)	(77,452)
Interest paid on debt	(37,773)	(112,927)
Loan issue costs	(69,245)	-
Proceeds of issuance of debt	2,585,000	-
Uses of (payments to) reserve accounts	77,938	(44,815)
Proceeds from sale of assets	-	2,321
Trustee fees	(1,250)	(750)
<b>Net cash used in capital and related financing activities</b>	<u>(210,184)</u>	<u>(276,108)</u>
<b>Cash flows from investing activities:</b>		
(Purchase) liquidation of investments - unrestricted	(1,179)	(100,811)
Interest income	6,612	8,034
<b>Net cash provided by investing activities</b>	<u>5,433</u>	<u>(92,777)</u>
<b>Net increase (decrease) in cash</b>	273,464	(12,300)
<b>Cash and cash equivalents at beginning of year</b>	<u>68,187</u>	<u>80,487</u>
<b>Cash and cash equivalents at end of year</b>	<u>\$ 341,651</u>	<u>\$ 68,187</u>
<b>Reconciliation of operation income to net cash provided by operating activities:</b>		
Operating income (loss)	\$ 118,910	\$ (13,948)
<b>Adjustments to reconcile net income to net cash provided by operating activities:</b>		
Amortization	19,744	18,590
Depreciation	342,924	339,818
Changes in assets and liabilities:		
(Increase) decrease in accounts receivable	(25,482)	(1,810)
(Increase) decrease in unbilled revenues	(1,680)	(348)
(Increase) decrease in prepaid expenses	(414)	540
(Increase) decrease in inventory	(5,524)	7,742
Increase (decrease) in customer deposits	-	-
Increase (decrease) in accounts payable	29,241	4,631
Increase (decrease) in accrued compensation	1,360	2,267
Increase (decrease) in payroll taxes payable	(864)	(897)
<b>Total adjustments</b>	<u>359,305</u>	<u>370,533</u>
<b>Net cash provided by operating activities</b>	<u>\$ 478,215</u>	<u>\$ 356,585</u>

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

# **LONE CHIMNEY WATER ASSOCIATION**

## **NOTES TO THE BASIC FINANCIAL STATEMENTS**

**June 30, 2012 and 2011**

### **1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

Lone Chimney Water Association (the Association), an Oklahoma association of public agencies, was created pursuant to Title 74, O.S. 1981, Sections 1001-1008, the Oklahoma Interlocal Cooperation Act. The Association was formed to provide a centralized water treatment and distribution system for surrounding communities. The Association currently sells water wholesale to twelve rural water systems located in Payne, Pawnee, Noble and Lincoln counties. Also, the Association has residential customers who have paid the required meter installation fees. The system is comprised of the 564-acre Lone Chimney Lake, built in 1980-85, a modern water treatment plant completed in 1986, and about 70 miles of water distribution mains. Service to customers began in mid 1986. The Association is exempt from federal and state income taxes.

The Board of Directors consists of 9 members representing the water systems that are parties to long-term contracts with the Association (i.e., more than ten years) plus 1 representative of the other system customers serving 4-year terms. The vacant Board seats are elected at the annual meeting in July, and following, the Board of Directors meet and elect a chairman, vice-chairman, and secretary-treasurer. All Board members serve without pay.

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

#### **A. Reporting Entity**

Lone Chimney Water Association 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 and amortization) of providing water services is financed through user charges.

#### **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. Amortization expense is provided for easements based upon a 40 year life.

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 Association 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 Association can invest in direct debt securities of the United States unless such an investment is expressly prohibited by law.

For financial statement presentation and for purposes of statements of cash flows, the Association's cash and cash equivalents are considered to be cash on hand, demand deposits and certificates of deposit with a maturity date of three months or less.



# LONE CHIMNEY WATER ASSOCIATION

## NOTES TO THE BASIC FINANCIAL STATEMENTS June 30, 2012 and 2011

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

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

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

###### *Custodial Credit Risk*

At June 30, 2012, the Association held deposits of approximately \$1,017,106 at financial institutions. The Association'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 Association or by its agent in the Association's name.

###### *Investment Interest Rate Risk*

The Association 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 Association 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 cash and investments held at June 30, 2012 are as follows:

Type	Weighted Average Maturity (Months)	Credit Rating	Market Value	Cost
Investments				
Money Market	N/A	AAAm	\$ 615,116	\$ 615,116
Certificate of deposit	10.75	N/A	401,990	401,990
Total investments			<u>\$ 1,017,106</u>	<u>\$ 1,017,106</u>

###### Concentration of Investment Credit Risk

The Association places no limit on the amount it may invest in any one issuer. The Association has the following of credit risk: 39% in Certificates of deposit (\$401,990) and 61% in Money Market funds (\$615,116).

# **LONE CHIMNEY WATER ASSOCIATION**

## **NOTES TO THE BASIC FINANCIAL STATEMENTS**

**June 30, 2012 and 2011**

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

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

##### **2. Restricted Cash and Investments**

The restricted cash is the result of financial requirements of various note indentures between the Association and the Oklahoma Water Resources Board (OWRB) consist of funds held in reserve funds. Under the terms and provisions of the OWRB promissory note, these special funds are maintained with the Trustee bank for the benefit of the holders of the bond and are not subject to lien or attachment by any other creditors. Monies contained in the funds held by the Trustee are required to be continuously invested in authorized securities that mature not later than the respective dates when the funds shall be required for the purpose intended by the bonds. The funds are temporarily restricted but with prior written approval from OWRB, the funds can also be used for making improvements to the water system or for debt service. Under the terms and provisions of the promissory note, these funds may be maintained so long as the notes are outstanding. In addition, certain funds are restricted for customer deposits and are reflected as an asset and a corresponding liability.

##### **3. Fair Value of Financial Instruments**

The Association's financial instruments include cash and cash equivalents, accounts receivable, accounts payable and notes payable. The Association'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.

##### **4. 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.

##### **5. Inventories**

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

##### **6. Compensated Absences**

It is the Association's policy to permit employees to accumulate earned but unused vacation time. Full-time employees are granted vacation and sick leave benefits in varying amounts to specified maximums depending on tenure. The Association has accrued compensated absences and has reported the amount in the financial statements.

##### **7. Deferred Charges**

Loan issue costs are amortized ratably over the repayment period of the applicable bond using the straight-line method.

# LONE CHIMNEY WATER ASSOCIATION

## NOTES TO THE BASIC FINANCIAL STATEMENTS

June 30, 2012 and 2011

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

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

##### 8. Capital Assets

Additions to the water treatment and 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. The Association maintains a capitalization threshold of \$5,000 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:

Water treatment and delivery system	35-40 years
Buildings and improvements	10-40 years
Machinery and equipment	5-10 years
Office equipment	3-7 years
Boat ramps and docks	15-30 years

##### 9. Easements

Easement rights are being amortized on the straight-line method over the maximum 40-year period and are recorded at net on the financial statements.

##### 10. Net Assets

In the basic financial statements, net assets represent the difference between assets and liabilities. Net assets invested in capital assets, net of related debt, consists of capital assets, net of accumulated depreciation, reduced by the outstanding balances of any borrowing used for the acquisition, construction, or improvement of those assets. Net assets are reported as restricted when limitations on their use change the nature or normal understanding of the availability of the asset. Such constraints are either externally imposed by creditors, contributors, grantors, laws or other governments, or are imposed by law through constitutional provisions or enabling legislation. The Association applies restricted resources when an expense is incurred for purposes for which both restricted and unrestricted net assets are available.

### 2. LONG-TERM DEBT

Long-term debt consisted of two notes with the United States Department of Agriculture, Rural Development and two with Oklahoma Water Resources Board (OWRB). Now only one combined note exists. The note is secured by the water treatment plant and delivery system, dam, distribution lines, related equipment and water revenues derived from operations. Additional security has been pledged on the OWRB note by the eight members/owners of the Association. Each member/owner has pledged an amount equal to 150 percent of that member's relative ownership in the Association.

The notes are listed as follows:

Loan # 92-02 – Original amount of \$1,821,950, payable in monthly installments of \$8,801 for 40 years at 5% interest for the construction of the water treatment plant and delivery system, maturing in April of 2032. This loan was paid off and refinanced into the new loan.

Loan # 92-01 – Original amount of \$981,050, payable in monthly installments of \$4,111 for 40 years at 4.012% interest for the construction of the water treatment plant and delivery system, maturing in July of 2033. This loan was paid off and refinanced into the new loan.

# LONE CHIMNEY WATER ASSOCIATION

## NOTES TO THE BASIC FINANCIAL STATEMENTS

June 30, 2012 and 2011

### 2. LONG-TERM DEBT (Continued)

Loan OWRB – Original amount of \$600,000, payable in semi-annual installments for 26 years at an interest rate which is adjusted semi-annually, for expansion costs, refinance bank loan and set up a reserve fund, maturing in September of 2024. This loan was paid off and refinanced into the new loan.

Loan OWRB – Original amount of \$150,000, payable in semi-annual installments of \$5,269 for 20 years at 3.55% interest for water plant upgrades, maturing in September of 2026. This loan was paid off and refinanced into the new loan.

Loan OWRB – Original amount of \$2,585,000, payable in annual installments of varying amounts of principal and semi-annual installments of interest for 15 years at varying interest rates of .65% to 3.4% to combine all existing debt into one loan, maturing in September of 2027.

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

	Balance June 30, 2011	Additions	Reductions	Balance June 30, 2012	Current Portion
USDA Rural Dev. - 92-02	\$ 1,362,779	\$ -	\$ 1,362,779	\$ -	\$ -
USDA Rural Dev. - 92-01	699,284	-	699,284	-	-
OWRB	-	2,585,000	-	2,585,000	70,000
OWRB	424,750	-	424,750	-	-
OWRB	124,802	-	124,802	-	-
Total	<u>\$ 2,611,615</u>	<u>\$ 2,585,000</u>	<u>\$ 2,611,615</u>	<u>\$ 2,585,000</u>	<u>\$ 70,000</u>

Annual cash requirements to amortize these notes are as follows:

Year Ending June 30,	Payments Due
2013	\$ 147,994
2014	216,560
2015	214,320
2016	215,900
2017	212,420
2018-2022	1,062,100
2023-2027	1,056,055
2028	208,485
Total	<u>3,333,834</u>
Less interest	<u>(748,834)</u>
Note balance	<u>\$ 2,585,000</u>

**LONE CHIMNEY WATER ASSOCIATION**

**NOTES TO THE BASIC FINANCIAL STATEMENTS**

**June 30, 2012 and 2011**

**3. CAPTIAL ASSETS**

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

	Balance June 30, 2011	Additions	Deletions	Balance June 30, 2012
Non-depreciable assets:				
Land	\$ 270,707	\$ -	\$ -	\$ 270,707
Construction in process	-	124,199	-	124,199
Total non-depreciable assets	<u>270,707</u>	<u>124,199</u>	<u>-</u>	<u>394,906</u>
Depreciable assets:				
Dam & distrtribution lines	7,150,211	-	-	7,150,211
Clean water plant	3,081,900	-	-	3,081,900
Machinery & equipment	390,086	29,040	-	419,126
Manager's house & furnishings	182,669	-	-	182,669
Buildings	73,032	-	-	73,032
Shell road	43,366	-	-	43,366
Storage tank	58,905	-	-	58,905
Boat ramp and dock	94,256	-	-	94,256
Lagoon	84,608	-	-	84,608
Office equipment	25,759	-	-	25,759
Total depreciable assets	<u>11,184,792</u>	<u>29,040</u>	<u>-</u>	<u>11,213,832</u>
Less accumulated depreication	<u>(6,710,230)</u>	<u>(342,923)</u>	<u>-</u>	<u>(7,053,153)</u>
Net depreciable assets	<u>4,474,562</u>	<u>(313,883)</u>	<u>-</u>	<u>4,160,679</u>
Total net capital assets	<u>\$ 4,745,269</u>	<u>\$ (189,684)</u>	<u>\$ -</u>	<u>\$ 4,555,585</u>

**LONE CHIMNEY WATER ASSOCIATION**

**NOTES TO THE BASIC FINANCIAL STATEMENTS**

**June 30, 2012 and 2011**

**3. CAPTIAL ASSETS (Continued)**

	Balance June 30, 2010	Additions	Deletions	Balance June 30, 2011
Non-depreciable assets:				
Land	\$ 266,207	\$ 4,500	\$ -	\$ 270,707
Total non-depreciable assets	<u>266,207</u>	<u>4,500</u>	<u>-</u>	<u>270,707</u>
Depreciable assets:				
Dam & distribution lines	7,150,211	-	-	7,150,211
Clean water plant	3,081,900	-	-	3,081,900
Machinery & equipment	380,101	37,985	(28,000)	390,086
Manager's house & furnishings	182,669	-	-	182,669
Buildings	73,032	-	-	73,032
Shell road	43,366	-	-	43,366
Storage tank	58,905	-	-	58,905
Boat ramp and dock	94,256	-	-	94,256
Lagoon	84,608	-	-	84,608
Office equipment	25,759	-	-	25,759
Total depreciable assets	<u>11,174,807</u>	<u>37,985</u>	<u>(28,000)</u>	<u>11,184,792</u>
Less accumulated depreication	<u>(6,397,951)</u>	<u>(339,818)</u>	<u>27,539</u>	<u>(6,710,230)</u>
Net depreciable assets	<u>4,776,856</u>	<u>(301,833)</u>	<u>(461)</u>	<u>4,474,562</u>
Total net capital assets	<u>\$ 5,043,063</u>	<u>\$ (297,333)</u>	<u>\$ (461)</u>	<u>\$ 4,745,269</u>

## **LONE CHIMNEY WATER ASSOCIATION**

### **NOTES TO THE BASIC FINANCIAL STATEMENTS**

**June 30, 2012 and 2011**

#### **4. DEFERRED COMPENSATION PLAN**

The Association offers its employees a deferred compensation plan created in accordance with Internal Revenue Code Section 457. The 457 Plan, available to all employees, permits them to defer a portion of their salary until future years. A Roth retirement plan is also offered to all employees without the benefit of deferring a portion of their salary. The deferred compensation and Roth Plan are available to employees at termination of employment, retirement, death, or an unforeseeable emergency.

All amounts of compensation deferred under the plan, all property and rights purchased with those amounts, and all income attributable to those amounts, property, or rights are held in trust for the exclusive benefit of participants and their beneficiaries.

It is the opinion of the Association's management that it has no liability for losses under the plan, but does have the duty of due care that would be required of an ordinary prudent investor.

#### **5. RISK MANAGEMENT**

The Association 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 Association 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.

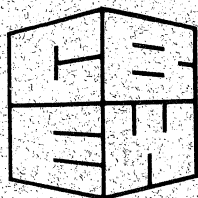
#### **6. SUBSEQUENT EVENTS**

Subsequent events have been evaluated through August 23, 2012, which is the date the financial statements were available to be issued and have determined that no additional information will need to be added to the financial statements.

**LONE CHIMNEY WATER ASSOCIATION**

**REPORT REQUIRED BY *GOVERNMENT AUDITING STANDARDS***  
**June 30, 2012**





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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**

August 23, 2012

Board of Directors  
Lone Chimney Water Association

We have audited the basic financial statements of the Lone Chimney Water Association (the Association), as of and for the year ended June 30, 2012, and have issued our report thereon dated August 23, 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 Association 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 Association'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 Association's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Association'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 we consider to be significant deficiencies in internal control over financial reporting. The finding reference numbers are 12-1 and 12-2. 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.

Lone Chimney Water Association  
August 23, 2012

Compliance over Other Matters

As part of obtaining reasonable assurance about whether the Association'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 Association's response to the finding identified in our audit is described in the accompanying schedule of findings and responses. We did not audit the Association's response and, according, we express no opinion on it.

This report is intended solely for the information of management, the board, 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

## LONE CHIMNEY WATER ASSOCIATION

### SCHEDULE OF FINDINGS AND RESPONSES For the Year Ended June 30, 2012

#### 12-1. 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. This finding was also noted in 2011.

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

#### 12-2. Internal Control – 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 implementation 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 controls, 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, 2012, 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: fixed asset purchases, depreciation, amortization, note payments and interest expense. This finding was also noted in 2011.

## **LONE CHIMNEY WATER ASSOCIATION**

### **SCHEDULE OF FINDINGS AND RESPONSES For the Year Ended June 30, 2012**

**Cause:** The government's accounting and financial reporting staff lacks the necessary expertise, 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 or Potential 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 in regards to the trial balances.

**Recommendation:** The government should consider designing and implementing sufficient internal controls over the completeness and accuracy of trial balances by obtaining the necessary 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.

**Responsible Official's Response:** The Association concurs with the recommendation, and will strive to prepare and post material adjusting journal entries to the financial statements.