

AUDIT REPORT

ATOKA COUNTY RURAL WATER DISTRICT #2 ATOKA, OKLAHOMA

JUNE 30, 2012



KERSHAW CPA & ASSOCIATES, PC

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ATOKA COUNTY RURAL WATER DISTRICT #2
ATOKA, OKLAHOMA
JUNE 30, 2012

TABLE OF CONTENTS

	<u>PAGE</u>
INTRODUCTORY SECTION:	
BOARD OF DIRECTORS	3
FINANCIAL SECTION:	
INDEPENDENT AUDITOR'S REPORT	4-5
BASIC FINANCIAL STATEMENTS:	
EXHIBIT A STATEMENT OF NET ASSETS	6
EXHIBIT B STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS	7
EXHIBIT C STATEMENT OF CASH FLOWS	8
NOTES TO THE FINANCIAL STATEMENTS	9-16
REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH <i>GOVERNMENT AUDITING STANDARDS</i>	17-18
SCHEDULE OF FINDINGS	19

ATOKA COUNTY RURAL WATER DISTRICT #2
ATOKA, OKLAHOMA
JUNE 30, 2012

BOARD OF DIRECTORS

<u>NAME</u>	<u>POSITION</u>
DAVID BLACKBURN	CHAIRMAN
THOMAS SMOOT	VICE-CHAIRMAN
MERRITT TAYLOR	TREASURER
ROGER MCININCH	SECRETARY
MONTY BIRDSONG	MEMBER
DUANE CRAWFORD	MEMBER
GEORGE BICKNELL	MEMBER

MANAGER

MARTY COATES

Unaudited

KERSHAW CPA & ASSOCIATES, PC

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INDEPENDENT AUDITOR'S REPORT

To the Board of Directors
Atoka County Rural Water District #2
Atoka, Oklahoma

We have audited the accompanying financial statements of the Atoka County Rural Water District #2, as of and for the fiscal year ended June 30, 2012, as listed in the table of contents. These financial statements are the responsibility of the Atoka County Rural Water District #2'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, and in accordance with Oklahoma Statutes. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Atoka County Rural Water District #2, Atoka, Oklahoma, as of June 30, 2012, and the changes in financial position thereof for the year then ended in conformity with U.S. Generally Accepted Accounting Principles.

In accordance with Government Auditing Standards, we have also issued our report dated October 24, 2012, on our consideration of the Atoka County Rural Water District #2'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 compliance with Government Auditing Standards and should be considered in assessing the results of our audit.

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Atoka County Rural Water District #2 has implemented the general provisions of the Governmental Accounting Standards Board (GASB) Statement No. 34. However 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.

The introductory section listed in the accompanying table of contents is presented for the purpose of additional analysis and is not a required part of the basic financial statements of the District. Such additional information has not been subjected to the auditing procedures applied in our audit of the basic financial statements, and accordingly, we do not express an opinion thereon.

Kershaw CPA & Associates, P.C.
Kershaw CPA & Associates, PC

October 24, 2012

ATOKA COUNTY RURAL WATER DISTRICT #2
ATOKA, OKLAHOMA
STATEMENT OF NET ASSETS
JUNE 30, 2012

	Total 2012	Total (Memo Only) 2011
<u>ASSETS</u>		
<u>Current Assets:</u>		
Cash and Cash Equivalents (Note 5)	\$ 169,807	\$ 141,458
Accounts Receivable - Trade	23,714	22,819
Prepaid Insurance	5,729	5,231
Total Current Assets	199,250	169,507
<u>Restricted Assets:</u>		
Reserve Account	9,793	6,426
Sewer Project Account	-	-
Water Security Deposit Account	26,927	25,769
Total Restricted Assets	36,720	32,195
<u>Capital Assets:</u>		
Land	7,620	7,620
Equipment	14,572	14,572
Water Distribution Facilities	519,876	519,876
Sewer Lagoon	17,728	17,728
System Improvements	1,168,867	1,166,617
Less: Accumulated Depreciation	(440,063)	(395,864)
Total Capital Assets	1,288,601	1,330,549
TOTAL ASSETS	\$ 1,524,571	\$ 1,532,251
<u>LIABILITIES</u>		
<u>Current Liabilities:</u>		
Accounts Payable	\$ 7,410	\$ 7,520
Interest Payable	23,308	1,486
Security Deposits	20,050	17,725
Current Portion of Long-Term Debt	-	7,857
Total Current Liabilities	50,768	34,588
<u>Long-Term Liabilities:</u>		
Notes Payable	647,292	648,640
Less: Current Portion	-	(7,857)
TOTAL LIABILITIES	698,060	675,372
<u>NET ASSETS</u>		
Invested in capital assets, net of related debt	641,308	681,909
Restricted for debt service	36,720	32,195
Unrestricted	148,482	142,775
TOTAL NET ASSETS	826,511	856,879
TOTAL LIABILITIES & NET ASSETS	\$ 1,524,571	\$ 1,532,251

See Accountant's Audit Report & Notes Which Accompany These Financial Statements

ATOKA COUNTY RURAL WATER DISTRICT #2
 ATOKA, OKLAHOMA
 STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS
 FOR THE FISCAL YEAR ENDED JUNE 30, 2012

	Total June 30, 2012	Total (Memo Only) June 30, 2011
<u>Operating Revenues:</u>		
Water Sales	\$ 144,684	\$ 137,144
Sewer Sales	32,826	34,776
Penalties	4,844	4,551
Benefit Units and Hook-Up Fees	2,530	2,155
Miscellaneous Income	2,062	3,224
Total Operating Revenues	186,946	181,850
<u>Operating Expenses:</u>		
Salaries	43,590	41,842
Payroll Taxes	3,691	4,012
Retirement Expense	5,670	5,784
Water Purchases	67,195	56,991
Repairs/Maintenance and Operating Supplies	16,788	19,789
Utilities	4,219	4,529
Legal & Accounting	1,885	7,858
Office Supplies & Postage	5,295	5,470
Bank Charges	8	10
Dues & Fees	-	-
Professional Services	-	440
Insurance and Bonds	7,060	5,766
Travel	1,989	1,738
Licenses & Permits	1,087	991
Office Rental	4,800	4,800
Contract Labor	800	580
Returned Checks	-	194
Miscellaneous	681	653
Depreciation	44,199	14,977
Total Operating Expenses	208,956	176,423
Operating Income (Loss)	(22,010)	5,427
<u>Non-Operating Revenues (Expenses):</u>		
Interest Income	408	1,318
Interest Expense	(26,066)	(26,044)
Total Non-operating Revenues (Expenses)	(25,658)	(24,727)
Net Income (Loss) Before Contributions	(47,668)	(19,300)
Capital Contributions	17,300	45,055
Change in Net Assets	(30,368)	25,755
Total Net Assets - Beginning	856,879	831,124
Total Net Assets - Prior Year Adjustment	-	-
Total Net Assets - Ending	\$ 826,511	\$ 856,879

See Accountant's Audit Report & Notes Which Accompany These Financial Statements

ATOKA COUNTY RURAL WATER DISTRICT #2
ATOKA, OKLAHOMA
STATEMENT OF CASH FLOWS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

	<u>6/30/12</u>	<u>Memorandum Only 6/30/11</u>
<u>Net Cash Flows from Operating Activities:</u>		
Cash Receipts from Customers	\$ 186,051	\$ 182,061
Payments to Suppliers for Goods & Services	(121,777)	(118,754)
Payments to Employees & Laborers	(43,590)	(41,842)
Receipts of Customer Utility Deposits, Net of Refunds	2,325	(2,350)
Net Cash Provided (Used) by Operating Activities	<u>23,009</u>	<u>19,115</u>
<u>Net Cash Flows from Capital & Related Financing Activities:</u>		
Additions to Capital Assets	(2,250)	(66,570)
Capital Contributions - Grants	17,300	45,055
Loan Proceeds	-	-
Proceeds from sale of Capital Assets	-	-
Principal paid on Debt	(1,348)	(7,563)
Interest paid on Debt	(4,244)	(25,989)
Net Cash Provided (Used) by Capital & Related Financing Activities	<u>9,458</u>	<u>(55,067)</u>
Net Cash Flows from Investing Activities:		
Non-Operating Income	-	-
Interest Income	408	1,318
Net Cash Provided (Used) by Investing Activities	<u>408</u>	<u>1,318</u>
Net Increase (Decrease) in Cash and Cash Equivalents	32,875	(34,635)
Cash & Cash Equivalents, Beginning of Year	173,652	208,287
Cash & Cash Equivalents, Prior Year Adjustment	-	-
Cash & Cash Equivalents, End of Year	<u>\$ 206,527</u>	<u>\$ 173,652</u>
<u>Reconciliation of operating income (loss) to net cash provided operating activities:</u>		
Operating Income (Loss)	\$ (22,010)	\$ 5,427
Adjustments to reconcile operating income (loss) to net cash provided (used) by operating activities		
Depreciation	44,199	14,977
(Increase)Decrease in Accounts Receivable-Trade	(895)	211
(Increase)Decrease in Prepaid Insurance	(499)	(2,227)
Increase(Decrease) in Accounts Payable	(111)	3,077
Increase(Decrease) in Security Deposits	2,325	(2,350)
Net Cash Provided (Used) by Operating Activities	<u>\$ 23,009</u>	<u>\$ 19,115</u>

See Accountant's Audit Report & Notes Which Accompany These Financial Statements

ATOKA COUNTY RURAL WATER DISTRICT #2
ATOKA, OKLAHOMA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization

Rural Water District No. 2, Atoka County, Oklahoma, was formed in 1966, pursuant to the Oklahoma Rural Water, Sewer, and Solid Waste Management District Act. The District operates as a nontaxable government entity to serve residents of a portion of rural Atoka County in Atoka, Oklahoma.

Accounting

In June 1999, the Governmental Accounting Standards Board (GASB) unanimously approved Statement No. 34, Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments. Certain of the significant changes in the Statement include the following:

1. For the first time the financial statement should include:
 - a. A Management Discussion and Analysis (MD&A) section providing analysis of the District's overall financial position and results of operations. However, the District has chosen not to present the required MD&A for the current year.
 - b. Financial statements prepared using full accrual accounting for all of the District's activities, except for including the General capital assets or infrastructure (lines, pump stations, etc.).
2. A change in the fund financial statements to focus on major funds.

These and other changes are reflected in the accompanying financial statements (including the notes to the financial statements). The District has elected to implement the general provisions of the Statement and report infrastructure acquired after July 1, 2003 as provided by GASB standards.

Basis of Presentation

The accounts of the District are organized on the basis of proprietary fund type, specifically an enterprise fund. The activities of this fund are accounted for with a separate set of self-balancing accounts that comprise the District's assets, liabilities, net assets, revenues and expenses. Enterprise Funds account for activities (1) that are financed with debt that is secured solely by a pledge of the net revenues from fees and charges of the activity; or (2) that are required by laws or regulations that the activity's costs of providing services, including capital costs (such as depreciation or debt service), be recovered with fees and charges, rather than with taxes or similar revenues; or (3) that the

ATOKA COUNTY RURAL WATER DISTRICT #2
ATOKA, OKLAHOMA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012

pricing policies of the activity establish fees and charges designed to recover its costs, including capital costs (such as depreciation or debt service).

Basis of Accounting

The proprietary fund type is accounted for on a flow of economic resources measurement focus. With this measurement focus, all assets and all liabilities associated with the operation of this fund are included on the balance sheet. Fund equity consists of contributed capital and retained earnings. Proprietary fund type operating statements present increases (e.g. revenues) and decreases (e.g. expenses) in net total assets. The accrual basis of accounting is utilized by the proprietary fund type. Under this basis of accounting revenues are recognized when earned and expenses are recognized when the related liability is incurred.

Budgetary Data

The District is required by Article 8 of its By-laws to prepare an annual budget.

Property and Equipment

Water distribution facilities and equipment purchased or constructed by the District are stated at cost. Depreciation is computed on the straight-line method based on the estimated useful lives of the assets ranging from five to forty years.

Construction in progress is recorded at cost. No depreciation is recognized until construction contracts are complete and the applicable facilities become operational.

System improvements in excess of \$1,000.00 and equipment in excess of \$80.00 that increase the capacity or operation efficiency or extend the useful life of any asset are capitalized. Repairs and maintenance are expensed as incurred.

Equity Classification

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

1. 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 bonds, mortgages, notes, or other borrowings that are attributable to the acquisition, construction, or improvements of those assets.
2. Restricted net assets—Consists of net assets with constraints placed on the use either by (a) external groups such as creditors, grantors,

ATOKA COUNTY RURAL WATER DISTRICT #2
ATOKA, OKLAHOMA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012

- contributors, or laws and regulations of other governments; or (b) law through constitutional provisions or enabling legislation.
3. Unrestricted net assets—All other net assets that do not meet the definition of “restricted” or “invested in capital assets, net of related debt.”

Revenues, expenditures & expenses

Operating revenues and expenses for proprietary funds result from providing services and producing and delivering goods and/or services. They also include all revenues and expenses not related to capital and related financing, noncapital financing, or investing activities.

Memorandum Only

The “Memorandum Only” captions above the total columns mean that totals are presented for overview information purposes only.

NOTE 2 - STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY

As a local government unit, the District is subject to various federal, state, and local laws and contractual regulations. In accordance with Government Auditing Standards, the auditor has issued a report on his consideration of the District’s internal control over financial reporting and tested its compliance with certain provisions of laws, regulations, contracts and grants. That report is an integral part of an audit performed in compliance with Government Auditing Standards and should be read in conjunction with this report in considering the results of the audit.

Finance-related Legal & Contractual Provisions

The District has complied with all of the covenants of the loan agreements.

Deficit Fund Balance or Retained Earnings

As indicated in the financial statements, there are no fund balance or retained earnings deficits for the District for this fiscal year.

ATOKA COUNTY RURAL WATER DISTRICT #2
ATOKA, OKLAHOMA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012

NOTE 3 - AGED ACCOUNTS RECEIVABLE - TRADE

CURRENT	\$ 18,282.75
30-60 DAYS	2,352.52
60-90 DAYS	1,408.93
90-120 DAYS	1,079.67
OVER 120 DAYS	<u>590.03</u>
Total Accounts Receivable	<u>\$ 23,713.90</u>

NOTE 4 - ACCUMULATED UNPAID VACATION BENEFITS

Accumulated unpaid vacation benefits have not been shown as a liability in the financial statements. The District's position is that any accrued benefits are not significant and would not materially affect the financial statements.

NOTE 5 - CASH AND INVESTMENTS

Custodial Credit Risk

At June 30, 2012, the District held deposits of approximately \$206,527 at financial institutions. The District's cash deposits, including interest-bearing certificates of deposit are 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

ATOKA COUNTY RURAL WATER DISTRICT #2
 ATOKA, OKLAHOMA
 NOTES TO FINANCIAL STATEMENTS
 JUNE 30, 2012

- 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 District has collateral pledges with AmeriState Bank totaling \$100,000.00.

The following is a breakdown of the Cash & Cash Equivalents figure shown in the Statement of Net Assets:

Cash & Cash Equivalents:	
Operating Fund	\$ 50,515.64
Savings Accounts	78,327.81
Special Projects	9,743.18
Certificate of Deposit	31,008.20
Petty Cash	212.02
Total	\$ 169,806.85

NOTE 6 - RESTRICTED ASSETS

Restrictions on restricted assets are as follows:

Security Deposits	-Use is Restricted to deposit and refund water meter security deposits
Reserve Account	-Restricted by USDA RD loan covenants
Sewer Project Account	-Restricted for Sewer Project

The loan agreement with the United States Department of Agriculture Rural Development (USDA) requires the District to set aside into a Reserve Account an accumulated amount equal to the sum of the annual installments (\$26,004 and \$7,548), after which deposits may be suspended, except to replace withdrawals. The District cannot withdraw funds from the reserve account without USDA approval. As of June 30, 2012, the District was required to have at least \$9,786.00 set aside in the reserve account; as of that date

ATOKA COUNTY RURAL WATER DISTRICT #2
 ATOKA, OKLAHOMA
 NOTES TO FINANCIAL STATEMENTS
 JUNE 30, 2012

the account balance for the reserve account was \$9,793.26, which complies with the covenants of the loan agreements.

NOTE 7 - CAPITAL ASSETS

Capital asset activity, for the fiscal year ended June 30, 2012, was as follows:

	Balance at June 30, 2011	Additions	Deductions	Balance at June 30, 2012
Land	\$ 7,620	\$ -	\$ -	\$ 7,620
Equipment	14,572	-	-	14,572
Water Distribution Facilities	519,876	-	-	519,876
Sewer Lagoon	17,728	-	-	17,728
System Improvements	1,166,617	2,250	-	1,168,867
Subtotal	1,726,413	2,250	-	1,728,663
Less: Accum. Depr.	(395,864)	(29,222)	-	(425,086)
Total Capital Assets (Net of Depreciation)	<u>\$ 1,330,549</u>	<u>\$ (26,972)</u>	<u>\$ -</u>	<u>\$ 1,303,578</u>

The current year capital asset additions included the water and sewer system improvement project final engineering fees.

NOTE 8 - LONG-TERM DEBT

The District has a note payable with an original balance of \$481,500, to the United States Department of Agriculture Rural Development (USDA), payable in monthly installments of \$2,167 until maturity, including interest at 4.50%. The final payment is scheduled for July 10, 2049. The note is secured by the water and sewer system.

The District has a note payable with an original balance of \$186,400, to the United States Department of Agriculture Rural Development (USDA), payable in monthly installments of \$629 until maturity, including interest at 2.625%. The final payment is scheduled for July 10, 2049. The note is secured by the water and sewer system.

Changes in Long-Term Debt

The following is a summary of changes in long-term debt for the year ended June 30, 2012:

	Balance 6/30/2011	Additions	Deductions	Balance 6/30/2012
USDA RD #93-01	\$ 469,583	\$ -	\$ (862)	\$ 468,722
USDA RD #93-03	179,057	-	(486)	178,571
	<u>\$ 648,640</u>	<u>\$ -</u>	<u>\$ (1,348)</u>	<u>\$ 647,292</u>

On August 5, 2011, the District entered into an 18-month moratorium to postpone loan payments for the USDA loans. The moratorium was due to a tornado in the area. The

ATOKA COUNTY RURAL WATER DISTRICT #2
ATOKA, OKLAHOMA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012

moratorium will expire on April 4, 2013. USDA Rural Development has not yet determined whether or not payments will continue with the current amortization schedule or if a new revised amortization schedule will be used for repayment. Therefore, amortization information and current year maturities are not available at this time.

NOTE 9 - FUND EQUITY

As described in Note 1 above, equity is classified as net assets and displayed in three components:

1. Invested in capital assets, net of related debt
2. Restricted net assets
3. Unrestricted net assets

Restricted assets are described in Note 6 above.

NOTE 10 - ESTIMATES

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that could affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

NOTE 11 - CONTINGENCIES

Litigation

The District currently has no pending litigation.

Federally Assisted Programs

In the normal course of operations, the District participates in various federal or state/loan programs from year to year. The grant/loan programs are often subject to additional audits by agents of the granting or loaning agency, the purpose of which is to ensure compliance with the specific conditions of the grant or loan. Any liability of reimbursement that may arise as a result of these audits cannot be reasonably determined at this time, although it is believed the amount, if any, would not be material.

NOTE 12 - ECONOMIC DEPENDENCY - WATER CONTRACT

The District has a contract to purchase all of its water from the City of Atoka.

ATOKA COUNTY RURAL WATER DISTRICT #2
ATOKA, OKLAHOMA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012

NOTE 13 - RETIREMENT PLAN

During the fiscal year 2003, the District joined the Oklahoma Public Employees Retirement (OPERS). The District follows the OPERS Code H percentages for retirement contributions as follows: employees contribute 6.5% of gross wages and the District contributes 7.0%. Retirement plan contributions by the District for 2012 were \$5,670.00.

NOTE 14 - SUBSEQUENT EVENTS

The District did not have any subsequent events through the date the financial statements were issued, for events requiring recording or disclosure in the financial statements for the year ending 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*

To the Board of Directors
Atoka County Rural Water District #2
Atoka, Oklahoma

We have audited the financial statements of the Atoka County Rural Water District #2, as of June 30, 2012 and have issued our report thereon dated October 24, 2012. The Atoka County Rural Water District #2 has implemented the general provisions of the Governmental Accounting Standards Board (GASB) Statement No. 34, except that the District did not present the required MD&A. We conducted our audit in accordance with U.S. generally accepted auditing standards, the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States, and in accordance with Oklahoma Statutes.

Internal Control Over Financial Reporting

Management of Atoka County Rural Water District #2 is responsible for establishing and maintaining internal control over financial reporting. In planning and performing our audit, we considered the Atoka County Rural Water District #2's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Atoka County Rural Water District #2's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Atoka County Rural Water District #2'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 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 weakness, as defined above. However, we identified certain deficiencies in internal control over financial reporting, described in the accompanying Schedule of Findings that we consider to be significant deficiencies in internal control over

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financial reporting. Those deficiencies are listed as Item 12-01. 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.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Atoka County Rural Water District #2's financial statements are free of material misstatement, we performed tests of 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 findings identified in our audit is described in the accompanying Schedule of Findings. 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 the board of directors and management of the Atoka County Rural Water District #2 and is not intended to be and should not be used by anyone other than these specified parties.

Kershaw CPA & Associates, P.C.

Kershaw CPA & Associates, PC

October 24, 2012

ATOKA COUNTY RURAL WATER DISTRICT #2
ATOKA, OKLAHOMA
SCHEDULE OF FINDINGS
FOR THE YEAR ENDED JUNE 30, 2012

INTERNAL CONTROL FINDINGS:

Item 12-01: Segregation of Duties

Criteria: A good system of internal control requires a proper segregation of duties to prevent one person from being in a position to authorize, execute, and record the same transaction.

Condition: Due to the size of the District's major areas of internal control, that would be prevalent in a larger District, such segregation of duties is not available for this size operation. Duties are concentrated in the hands of the District Clerk, who is responsible for all phases of the accounting functions. Because of this lack of division of responsibility, internal control is determined to be weak, and in some instances, non-existent.

Cause/Effect: Due to the limited number of personnel, a breach of internal controls could occur and not be detected in the normal course of operations.

Recommendation: The Board should continue to be actively involved in the operations of the organization.

Response: The Board continues to be actively involved in the operations of the organization.