

AUDIT REPORT

MAYES COUNTY RURAL WATER DISTRICT #2
MAYES COUNTY, OKLAHOMA

DECEMBER 31, 2015

KERSHAW CPA & ASSOCIATES, PC

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MAYES COUNTY RURAL WATER DISTRICT #2
DECEMBER 31, 2015

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MAYES COUNTY RURAL WATER DISTRICT #2
DECEMBER 31, 2015

BOARD OF DIRECTORS

<u>NAME</u>	<u>POSITION</u>
CHARLES COBLENTZ	CHAIRMAN
J.B. HALL	VICE CHAIRMAN
MIKE SOUTHERN	SECRETARY
E.J. CHUPP	MEMBER
JOHN G. COBB	MEMBER
JOHN HARDIN	MEMBER
JOHNNY DIACON	MEMBER
OTTO DEACON	MEMBER
ED YODER	MEMBER

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INDEPENDENT AUDITOR'S REPORT

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

Report on the Financial Statements

We have audited the accompanying financial statements of Mayes County Rural Water District #2, as of and for the fiscal year ended December 31, 2015, as listed in the table of contents and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of the financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

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 involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used, and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the Mayes County Rural Water District #2, Mayes County, as of December 31, 2015, and the respective changes in financial position and, where applicable, cash flows thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Management has omitted the Management's Discussion and Analysis that 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 who considers it to be an essential part of 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.

Supplementary and Other Information

The introductory and the other supplementary information sections listed in the accompanying table of contents are presented for the purpose of additional analysis and are 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 or provide any assurance on it.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated February 11, 2016, on our consideration of the Mayes County Rural Water District #2'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 the results of that testing, and not to provide

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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* in considering Mayes County Rural Water District #2's internal control over financial reporting and compliance.

Kershaw CPA & Associates, P.C.

Kershaw, CPA & Associates, PC

February 11, 2016

**MAYES COUNTY RURAL WATER DISTRICT #2
STATEMENT OF NET POSITION
DECEMBER 31, 2015**

<u>ASSETS</u>	<u>2015</u>	<u>Memo Only 2014</u>
<u>Current Assets:</u>		
Petty Cash	\$ 801	\$ 829
Checking Account - BOC - Revenue	53,286	61,828
RCB - Merchant Account	98,871	44,825
Checking Account - BOC - Deposit Refunds	239	282
Accounts receivable	106,658	153,099
Prepaid Insurance	11,563	11,125
Inventory	39,276	32,053
Total Current Assets	<u>310,693</u>	<u>304,040</u>
<u>Restricted Assets:</u>		
BOK - Debt Service Fund	62,055	31,480
BOK - Debt Service Reserve Fund	346,480	346,480
Certificates of Deposit - Reserved for Capital Construction	403,752	502,746
Total Restricted Assets	<u>812,287</u>	<u>880,707</u>
<u>Capital Assets:</u>		
Land	22,107	22,107
Buildings	104,774	104,774
Water Distribution System & Equipment	10,582,622	10,316,397
Less: Accumulated Depreciation	(4,651,856)	(4,362,334)
Total Fixed Assets	<u>6,057,647</u>	<u>6,080,944</u>
<u>Other Assets</u>		
Deposits	1,144	1,144
Deferred Charges	51,687	54,349
Total Other Assets	<u>52,831</u>	<u>55,493</u>
TOTAL ASSETS	<u>\$ 7,233,458</u>	<u>\$ 7,321,184</u>
<u>LIABILITIES & NET POSITION</u>		
<u>Current Liabilities:</u>		
Accounts Payable	\$ 52,015	\$ 55,389
Meter Deposits	69,490	66,220
Accrued Payroll Tax & Related	7,134	615
Accrued Interest Payable	9,270	9,996
Current Portion of Long-Term Debt	97,700	92,600
Total Current Liabilities	<u>235,609</u>	<u>224,820</u>
<u>Long-Term Liabilities:</u>		
Note Payable - OWRB	2,162,000	2,269,600
Less: Current Portion of Long-Term Debt	(97,700)	(92,600)
Total Long-Term Debt	<u>2,064,300</u>	<u>2,177,000</u>
TOTAL LIABILITIES	<u>2,299,909</u>	<u>2,401,820</u>
<u>NET POSITION:</u>		
Net investment in capital assets	3,895,647	3,811,344
Restricted for debt service	812,287	880,707
Unrestricted	225,616	227,313
TOTAL NET POSITION	<u>4,933,549</u>	<u>4,919,364</u>
TOTAL LIABILITIES AND NET POSITION	<u>\$ 7,233,458</u>	<u>\$ 7,321,184</u>

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

EXHIBIT B

**MAYES COUNTY RURAL WATER DISTRICT #2
STATEMENT OF REVENUES, EXPENSES & CHANGES IN NET POSITION
FOR THE TWELVE MONTHS ENDED DECEMBER 31, 2015**

	<u>2015</u>	<u>Memo Only 2014</u>
<u>Operating Revenues:</u>		
Water sales	\$ 1,200,616	\$ 1,164,716
Misc Customer Fees	59,458	51,351
Total Operating Revenues	<u>1,260,074</u>	<u>1,216,067</u>
<u>Operating Expenses:</u>		
Water Purchases & Testing	562,809	500,328
Salaries	212,058	203,483
Retirement Benefit	18,150	14,464
Medical and Disability Benefit	38,545	33,424
Payroll Taxes and Related	4,038	3,953
Insurance	21,144	17,996
Uniforms	3,169	2,692
Line, Pump Station, & Meter Materials	24,840	30,367
Dues & Licenses	9,591	7,631
Repairs and Maintenance	6,197	5,536
Fuel and Lubricants	9,257	14,598
Small Tools	1,557	1,951
Utilities and Telephone	27,604	25,633
Professional Fees	35,417	56,881
Bank Charges	9,148	8,050
Office Supply and Postage	18,795	12,977
Misc. Expense	2,915	8,008
Depreciation Expense	289,522	286,838
Amortization Expense	2,662	2,662
Total Operating Expenses	<u>1,297,418</u>	<u>1,237,472</u>
Net Operating Income (Loss)	<u>(37,344)</u>	<u>(21,404)</u>
<u>Non-operating Income (Expense):</u>		
Interest Income	4,553	6,386
Interest Expense	(33,450)	(30,326)
Membership Fees	83,529	84,772
Miscellaneous Income	-	1,416
Total Non-operating Income (Expense)	<u>54,632</u>	<u>62,248</u>
Change in Net Position	17,288	40,844
Capital Contributions	-	-
Total Net Position, Beginning of Year	4,919,364	4,864,647
Total Net Position, Prior Year Adjustment	<u>(3,103)</u>	<u>13,873</u>
Total Net Position, End of Year	<u>\$ 4,933,549</u>	<u>\$ 4,919,364</u>

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

EXHIBIT C

**MAYES COUNTY RURAL WATER DISTRICT #2
STATEMENT OF CASH FLOWS
FOR THE TWELVE MONTHS ENDED DECEMBER 31, 2015**

	<u>2015</u>	<u>Memo Only 2014</u>
<u>Cash Flows from Operating Activities:</u>		
Cash Receipts from Customers	\$ 1,309,785	\$ 1,165,159
Payments to Suppliers for Goods & Services	(1,012,853)	(942,292)
Net Cash Provided (Used) by Operating Activities	<u>296,932</u>	<u>222,867</u>
<u>Cash Flows from Capital & Related Financing Activities:</u>		
Additions to Capital Assets	(266,225)	(327,998)
Membership Fees	83,529	84,772
Misc. Income	-	1,416
Principal paid on long-term debt	(107,600)	(111,050)
Interest paid on Debt	(34,176)	(27,342)
Net Cash Provided (Used) by Capital & Related Financing Activities	<u>(324,472)</u>	<u>(380,202)</u>
<u>Cash Flows from Investing Activities:</u>		
Interest Income	4,553	6,386
Net Cash Provided (Used) by Investing Activities	<u>4,553</u>	<u>6,386</u>
Net Increase (Decrease) in Cash and Cash Equivalents	(22,987)	(150,949)
Cash & Cash Equivalents, Beginning of Year	988,470	1,139,428
Cash & Cash Equivalents, Prior Year Adjustment	-	(10)
Cash & Cash Equivalents, End of Year	<u>\$ 965,483</u>	<u>\$ 988,470</u>
<u>Reconciliation of operating income (loss) to net cash provided operating activities:</u>		
Operating Income (Loss)	\$ (37,344)	\$ (21,404)
Adjustments to reconcile operating income (loss) to net cash provided (used) by operating activities		
Depreciation & Amortization	292,184	289,500
(Increase)Decrease in Accounts Receivable	46,441	(51,599)
(Increase)Decrease in Prepaid Insurance	(439)	1
(Increase)Decrease in Inventory	(7,223)	6,925
Increase(Decrease) in Accounts Payable	(3,374)	(1,890)
Increase(Decrease) in Accrued expenses	3,416	644
Increase(Decrease) in Customer Deposits	3,270	690
Net Cash Provided (Used) by Operating Activities	<u>\$ 296,932</u>	<u>\$ 222,867</u>
Supplemental Information:		
Unrestricted Cash and Cash Equivalents	\$ 153,196	\$ 107,763
Certificates of Deposit & Savings - Reserved for Improvements	403,752	502,746
Restricted Cash & Cash Equivalents - BOK Reserve & Debt Ser	408,535	377,960
Total Cash & Cash Equivalents	<u>\$ 965,483</u>	<u>\$ 988,470</u>

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

MAYES COUNTY RURAL WATER DISTRICT #2
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2015

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accounting policies employed by Mayes County Rural Water District #2 (the District) are consistent with accounting principles generally accepted in the United States of America. Significant polices are described below.

In June 1999, the GASB issued Statement No. 34, Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments. The statement established a new reporting model for governments that is substantially different from prior reporting standards. The District adopted the new reporting model December 31, 2004, which includes the following segments:

Management's Discussion & Analysis - provides introductory information on basic financial statements and an analytical overview of the District's financial activities. For the year ended December 31, 2015, management has not presented the Management's Discussion and Analysis as required by the Governmental Accounting Standards Board (GASB) and GASB has determined it necessary to supplement, although not required to be part of, the basic financial statements.

Fund financial statements - provide information about the District's proprietary fund. The proprietary fund utilizes 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. The proprietary fund utilizes an "economic resources" measurement focus. The accounting objectives of this measurement focus are the determination of net income, financial position and cash flows. All assets and liabilities (whether current or non-current) associated with their activities are reported. Proprietary fund equity is classified as net position.

A. Reporting Entity:

Mayes County Rural Water District #2 was incorporated under the Rural Water District Act of Oklahoma, for the purpose of acquiring water rights, and to build and acquire pipelines and other facilities and to operate the same for the purpose of furnishing water to serve the needs of owners and occupants of land located within the District.

The membership consists of approximately 2,850 users, each entitled to one vote. The Board of Directors consists of 9 members serving 3-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.

MAYES COUNTY RURAL WATER DISTRICT #2
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2015

B. Basis of Presentation and Accounting:

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.

The financial statements are presented on the accrual basis of accounting in accordance with U. S. Generally Accepted Accounting Principles. Under the accrual basis of accounting, revenues are recognized when earned and expenditures are recorded when the liability is incurred.

C. Cash and Cash Equivalents:

For purposes of the statement of cash flows, the District considers all highly liquid debt instruments purchased with a maturity of three months or less to be cash equivalents.

D. Accounts Receivable

Accounts receivable consists primarily of charges for water sales. Management has not established a provision for uncollectible accounts. Such amounts are written off the month in which management determines they are uncollectible.

E. Inventory

Inventory consists primarily of distribution repair supplies and is counted annually. The inventory is valued at the lower of cost or market on a first-in-first-out basis, but not in excess of market.

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

MAYES COUNTY RURAL WATER DISTRICT #2
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2015

G. Capitalization Policy:

Purchases of capital items in excess of \$150.00 that increase the capacity or operation efficiency or extend the useful life of any asset are capitalized. Repairs and maintenance are expensed as incurred.

H. Equity Classification:

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

1. Net investment in capital assets – 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 and adjusted for any deferred inflows and outflows of resources attributable to capital assets and related debt.
2. Restricted – Consists of restricted assets reduced by liabilities and deferred inflows or resources related to those assets, with restriction constraints placed on the use either by (a) external groups such as creditors, grantors, contributors, or laws and regulations of other governments; or (b) law through constitutional provisions or enabling legislation.
3. Unrestricted - Net amount of assets, deferred outflows of resources, liabilities, and deferred inflows of resources that are not included in the determination of net investment in capital assets or the restricted component of net position.

It is the District's policy to first use restricted net resources prior to the use of unrestricted net resources when an expense is incurred for purposes for which both restricted and unrestricted net resources are available.

I. 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.

J. Income Taxes:

The District is exempt from federal and state income tax.

MAYES COUNTY RURAL WATER DISTRICT #2
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2015

K. Estimates:

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

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 is in compliance with the reserve requirement of the loan agreement.

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.

NOTE 3 - CUSTODIAL CREDIT RISK RELATED TO DEPOSITS

Custodial Credit Risk

At December 31, 2015, the District held deposits of approximately \$965,483 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:

MAYES COUNTY RURAL WATER DISTRICT #2
 NOTES TO FINANCIAL STATEMENTS
 DECEMBER 31, 2015

- 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 District has the following credit risk: 100% in Certificates of Deposit (\$403,752).

NOTE 4 - ACCOUNTS RECEIVABLE

The following is an aged schedule of accounts receivable as of December 31, 2015:

Current	1-30 Days	31-60 Days	Over 60 Days	Prepayments	Total
\$ 99,160	\$ 11,660	\$ 2,784	\$ 13,932	\$ (20,878)	\$ 106,658

NOTE 5 - RESTRICTED ASSETS

The terms of the loan agreement with the Oklahoma Water Resources Board (OWRB) require that the District maintain funds for the use of servicing debt in the amount of 125% of the total annual payment. The deposits with the Bank of Oklahoma (BOK) trust account is sufficient to fulfill this requirement. Management has elected to restrict the use of cash deposited in certificates of deposit to be used for capital improvements. There is no other legal restriction on the certificates of deposit.

NOTE 6 - CAPITAL ASSETS

Capital asset activity, for the fiscal year ended December 31, 2015, was as follows:

MAYES COUNTY RURAL WATER DISTRICT #2
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2015

	Balance at December 31, 2014	Additions	Deductions	Balance at December 31, 2015
Land	\$ 22,107	\$ -	\$ -	\$ 22,107
Buildings	104,774	-	-	104,774
Distribution System	9,527,548	175,267	-	9,702,815
Meter Reading System	404,110	89,127	-	493,237
Computers and Accessories	2,926	1,350	-	4,276
Furniture and Fixtures	26,095	481	-	26,575
Tools and Equipment	355,719	-	-	355,719
Subtotal	10,443,279	266,225	-	10,709,503
Less: Accum. Depr.	(4,362,334)	(289,522)	-	(4,651,856)
Total Capital Assets (Net of Depreciation)	<u>\$ 6,080,944</u>	<u>\$ (23,297)</u>	<u>\$ -</u>	<u>\$ 6,057,647</u>

NOTE 7 - LONG-TERM DEBT

On May 26, 2005, Mayes County Rural Water District #2 borrowed \$4,050,000 from the Oklahoma Water Resources Boards. Loan issuance costs of \$78,307 paid out of loan funds are carried as a deferred charge on the balance sheet and will be amortized over the life of the loan. Substantially all capital assets, accounts receivable, and assignment of revenues are pledged as security for the OWRB note. The note bears interest at an initial rate of 3.27% from May 26, 2005 through September 30, 2005 and after that date until maturity the interest rate may be adjusted periodically not exceeding applicable statutory limits. This note will mature on April 1, 2035. Payments are made by the 15th day of each month to the trustee bank, Bank of Oklahoma, and placed into a restricted debt service account. A debt service reserve account as part of the loan agreement must maintain a minimum balance of 125% of the maximum annual amount required for debt service. Earnings from debt service and debt service reserve accounts are placed into the debt service reserve fund. Semi-annual note payments are made each March 15th, and September 15th, from the debt service account.

Additional information: The District board of trustees voted in September 2013 to make a one million dollar principal reduction payment on this note and to pay an additional \$30,000 principal payment twice yearly. However, during the fiscal year ending December 31, 2015, only one additional payment of \$15,000 was made and a second payment of \$15,000 was still in transit.

Changes in Long-Term Debt

The following is a summary of changes in long-term debt for the year ended December 31, 2015:

MAYES COUNTY RURAL WATER DISTRICT #2
 NOTES TO FINANCIAL STATEMENTS
 DECEMBER 31, 2015

	Balance at December 31, 2014	Additions	Deductions	Balance at December 31, 2015
Notes Payable	\$ 2,269,600	\$ -	\$ (107,600)	\$ 2,162,000
Total Long-Term Debt	\$ 2,269,600	\$ -	\$ (107,600)	\$ 2,162,000

Debt Services Requirements to Maturity

The annual debt service requirements to maturity, including principal only (variable interest rate), for long-term debt, as of December 31, 2015, are as follows:

Long-Term Notes Payable:

Year Ending June 30,	Principal
2016	\$ 97,700
2017	103,200
2018	108,900
2019	115,000
2020	121,400
2021-2025	716,700
2026-2030	899,100
Total	\$ 2,162,000

NOTE 8 - FUND EQUITY

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

1. Net investment in capital assets
2. Restricted
3. Unrestricted

Restricted amounts are described in Note 5 above.

NOTE 9 - AMORTIZATION OF DEFERRED CHARGES

Issuance costs related to the OWRB loan of \$4,050,000 were \$78,307.17. This amount was paid out of loan funds and is carried on the balance sheet as a deferred charge less accumulated amortization expense, which is calculated and charged off over the life of the loan. The current year amortization expense is \$2,662.00.

NOTE 10 - CONTINGENCIES

Litigation

According to the District's management, there is no pending litigation.

MAYES COUNTY RURAL WATER DISTRICT #2
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2015

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 11 - ECONOMIC DEPENDENCE

Mayes County Rural Water District #2 is dependent upon the Oklahoma Ordnance Works Authority (OOWA) for the District's water supply.

NOTE 12 - EMPLOYEE RETIREMENT PLAN

The District maintains an elective SEP retirement plan for employees. The employees are allowed to contribute up to 7.65% of their wages (which is withheld from their payroll) and the District matches up to this amount. The District paid \$18,150.21 into the retirement plan in 2014. The plan is maintained by the Legend Group.

NOTE 13 - SUBSEQUENT EVENTS

The District did not have any subsequent events through February 11, 2016, which is the date the financial statements were issued, for events requiring recording or disclosure in the financial statements for the year ending December 31, 2015.

NOTE 14 - PRIOR YEAR ADJUSTMENT

Prior year adjustments were made to payroll tax liabilities that totaled \$3,102.68.

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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
Mayes County Rural Water District #2
Mayes County, Oklahoma

We have audited, in accordance with the 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, the financial statements of the Mayes County Rural Water District #2, as of and for the year ended December 31, 2015, and the related notes to the financial statements, and have issued our report thereon dated February 11, 2016. Management has omitted the MD&A required by accounting principles generally accepted in the United States of America.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Mayes County Rural Water District #2's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances 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 Mayes County Rural Water District #2's internal control. Accordingly, we do not express an opinion on the effectiveness of Mayes County Rural Water District #2's internal control.

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. 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.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified. We did identify certain deficiencies in internal control

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described in the accompanying Schedule of Findings that we consider to be significant deficiencies. Those deficiencies are listed as Item 15-01.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Mayes 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*.

Mayes County Rural Water District #2's Response to Findings

Mayes County Rural Water District #2's responses to the findings identified in our audit are described in the accompanying Schedule of Findings. Mayes County Rural Water District #2's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

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

February 11, 2016

MAYES COUNTY RURAL WATER DISTRICT #2
SCHEDULE OF FINDINGS
DECEMBER 31, 2015

Item 15-01: 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 a few individuals, who are 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: Some compensating controls have been implemented by the Board and management plays a large role in oversight of the billing, collection and reconciliation function.