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State Auditor & Inspector

Rec: 016924

**LOVE COUNTY RURAL  
WATER DISTRICT NO. 2,**

Audit Report

Year Ended June 30, 2011

LOVE COUNTY RURAL WATER DISTRICT NO. 2  
June 30, 2011

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## INDEPENDENT AUDITOR'S REPORT

To the Board of Trustees  
Love County Rural Water District No. 2  
Thackerville, Oklahoma

We have audited accompanying financial statements of Love County Rural Water District No. 2 as of and for the year ended June 30, 2011, as listed in the table of contents. These financial statements are the responsibility of Love County Rural Water District No. 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. 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 Love County Rural Water District No. 2 as of June 30, 2011, and the changes in its net assets and cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Love County Rural Water District No. 2 has not presented management's discussion and analysis that accounting principles generally accepted in the United States of America have determined is necessary to supplement, although not required to be part of, the basic financial statements.

In accordance with *Government Auditing Standards*, we have also issued our report dated November 8, 2011, on our consideration of Love County Rural Water District No. 2's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grants agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.



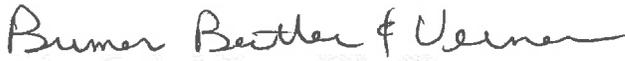
Brimer, Butler & Verner, CPAs, PC

November 8, 2011

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Love County Rural Water District No. 2's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, 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*.

This report is intended solely for the information and use of management and others within the entity, is not intended to be and should not be used by anyone other than these specified parties.



Brimer, Butler & Verner, CPAs, PC

November 8, 2011

RURAL WATER DISTRICT NO. 2, LOVE COUNTY

Schedule of Findings and Responses

Year ended June 30, 2011

2011-1 Interest expense and bond redemption was not posted to general ledger.

*Observation*

Transfers to the paying agent are made twice each year to pay interest and scheduled bond redemptions. The escrow account was not reconciled. Interest expense was not posted and the bonds outstanding were overstated.

*Recommendation*

Reconcile the escrow account.

*Management's Response*

The Board met and approved posting reconciling entries to escrow account and in the future will start reviewing the account to ensure principal and interest payments are posted as well as consulting with outside accountants.

RURAL WATER DISTRICT NO. 2, LOVE COUNTY

Schedule of Findings and Responses

Year ended June 30, 2011

2011-2 Capital assets are posted to expense.

*Observation*

The cost of purchasing a vehicle was posted to miscellaneous expense and the cost of telemetry was posted to machine hire and contract labor.

*Recommendation*

Develop capitalization policy.

*Management's Response*

The Board is working to develop and adopt a formal capitalization policy and conflict of interest policy.

**RURAL WATER DISTRICT No. 2, LOVE COUNTY**

**BALANCE SHEET**

June 30, 2011

**CURRENT ASSETS**

Cash - unrestricted	\$ 524,527
Accounts receivable net of allowance for bad debts	55,664
Grant receivable	178,760
Inventory	<u>16,750</u>

TOTAL CURRENT ASSETS 775,700

FIXED ASSETS, net of depreciation

657,695

**OTHER ASSETS**

Reserve cash accounts	212,298
Loan origination cost - net of amortization	<u>11,417</u>

223,715

\$ 1,657,110

**CURRENT LIABILITIES**

Accounts payable	\$ 12,994
Accrued interest payable	9,143
Current portion of long-term debt	20,000
Customer deposits	<u>8,082</u>

TOTAL CURRENT LIABILITIES 50,219

REVENUE BONDS PAYABLE, net of current portion

295,000

TOTAL LIABILITIES 345,219

**NET ASSETS**

Invested in capital assets, net of related debt	360,663
Unrestricted net assets	738,930
Restricted net assets	<u>212,298</u>

1,311,891

\$ 1,657,110

**RURAL WATER DISTRICT No. 2, LOVE COUNTY**  
**STATEMENT OF REVENUE, EXPENSES AND CHANGES IN NET ASSETS**  
 June 30, 2011

REVENUE

Water sales and related revenues	\$ 480,003
Grant income	249,999
Interest income	2,523
Rental income	3,000
	<u>735,525</u>

OPERATING EXPENSES

Salaries and benefits	129,504
Depreciation and amortization	35,917
Utilities and telephone	33,720
Insurance	37,347
Repairs and maintenance	4,536
Office and printing	6,412
Professional fees	21,493
Supplies	605
Gas, oil and mileage	3,213
Machine hire and contract labor	7,518
Water testing	5,025
Returned checks	335
Wire and bank fees	930
Interest expense	18,285
Miscellaneous other expense	6,207
	<u>311,048</u>

	NET INCOME	424,477
NET ASSETS BEGINNING OF THE YEAR		<u>887,414</u>
	NET ASSETS END OF THE YEAR	<u>\$ 1,311,891</u>

**RURAL WATER DISTRICT No. 2, LOVE COUNTY**

**STATEMENT OF CASH FLOWS**

Year ended June 30, 2011

**Cash flow from Operating Activities:**

Cash received from customers	\$ 478,821
Rents received	3,000
Grant funds received	71,240
Interest received	<u>2,523</u>
	555,583

Cash paid for good and services	75,533
Cash paid for employees and contractors	191,013
Interest paid	<u>18,845</u>
	<u>285,390</u>
Net cash provided (used) by operating activities	<u>270,192</u>

**Cash flows from capital and related financing activities:**

Principal paid on bonds	(20,000)
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**Cash flows from non-capital financing activities**

Transfers to restricted accounts	(80,323)
Interest earned on restricted account	(1,180)
Decrease in tenant deposits	(2,400)
Transfers from restricted accounts	<u>69,818</u>
	(14,085)

**Cash flows from investing activities:**

Cash paid for property and equipment	<u>(116,707)</u>
Net cash provided (used) by investing activities	<u>(116,707)</u>
Net Increase (Decrease) in Cash	119,401

Cash at the Beginning of the Year	<u>405,126</u>
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Cash at the End of the Year	<u>\$ 524,527</u>
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**Reconciliation of operating income (loss) to net cash**

**Provided by operating activities:**

Net income	\$ 424,477
Depreciation and amortization	35,917
(Increase) Decrease accounts receivable	(1,183)
(Increase) Decrease in inventory	(8,250)
(Increase) Decrease in Grant receivable	(178,760)
Increase (Decrease) accounts payable	<u>(2,010)</u>

Total adjustments	<u>(154,285)</u>
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Net cash provided (used) by operating activities	<u>\$ 270,192</u>
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LOVE COUNTY RURAL WATER DISTRICT NO.2  
NOTES TO THE FINANCIAL STATEMENTS  
June 30, 2011

**NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

*Organization and nature of operations*

Love County Rural Water District No. 2 (the “District”) is a body corporate and politic, without taxing power, established in the State of Oklahoma pursuant to Title 82, Oklahoma Statutes 1991, and an Order of the Board of County Commissioners of Love County, Oklahoma dated as of July 26, 1993. All assets and liabilities of Thackerville Water and Sewerage Company were transferred to the District. Its purpose is the construction, maintenance and operation of a water works within its district.

The basic financial statements of the Love County Rural Water District #2 have been prepared in conformity with generally accepted accounting principles as applied to government units. The Governmental Accounting Standards Board (GASB) is the accepted standard setting body for establishing governmental accounting and financial reporting principles. As allowed by the GASB, the District has elected not to apply to its proprietary activities Financial Accounting Standards Board Statements and Interpretation, Accounting Principles Board Opinions, and Accounting Research Bulletins of the Committee of Accounting Procedures issued after November 30, 1989.

The District is governed by a Board of Directors consisting of five members elected by the members of the District. The Board elects a Chairman.

*Basis of Presentation*

The District’s resources are allocated to and accounted for in these basic financial statements as an enterprise fund type of the proprietary fund group. The enterprise fund is used to account for operations that are financed and operated in a manner similar to private business enterprises, where the intent of the governing body is that the cost (expenses, including depreciation) of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges, or where the governing body has decided that periodic determination of revenues earned, expenses incurred, and/or net income is appropriate for capital maintenance, public policy, management control, accountability, or other policies. Net assets for the enterprise fund represent the amount available for future operations.

*Basis of accounting*

The accounting and financial reporting treatment applied to a fund is determined by its measurement focus. The enterprise 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. Net assets are segregated into amounts invested in capital assets, net of related debt, amounts restricted and amount unrestricted. Enterprise fund type operating statements present increases (i.e., revenues) and decreases (i.e., expenses) in net total assets.

The District uses the accrual basis of accounting. Under this method, revenues are recorded when earned and expenses are recorded at the time liabilities are incurred. Revenues are recognized when customers are billed.

*Accounts receivable*

The District uses the allowance method to account for uncollectible accounts receivable. Accounts receivable are presented net of an allowance for doubtful accounts of \$1,000.

LOVE COUNTY RURAL WATER DISTRICT NO.2  
NOTES TO THE FINANCIAL STATEMENTS  
June 30, 2011

*Cash and Cash Equivalents*

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

*Fair Value of Financial Instruments Approximates Carrying Amount*

The District's financial instruments are cash and cash equivalents, accounts receivable, accounts payable, and revenue bonds payable. The recorded values of cash and cash equivalents, accounts receivable, and payable approximate their fair values based on their short-term nature. The recorded values of bonds payable approximate their fair values, as interest approximates market rates.

*Operating and Nonoperating Revenues*

Operating income reported in proprietary fund financial statements includes revenues and expenses related to the primary, continuing operations of the fund. Principal operating revenues for proprietary funds are charges to customers for sales or services. Principal operating expenses are the cost of providing goods or services and include administrative expenses and depreciation of capital assets. Other revenues and expenses are classified as non-operating in the financial statements.

*Fixed Assets and Depreciation*

Fixed assets are stated at original cost. The costs of additions and replacements are capitalized. Replacements of minor items of property are charged to expense as incurred. Costs of property retired are eliminated from accounts, likewise such costs plus removal expense less salvage are charged to accumulated depreciation.

*Unamortized debt issue costs*

These costs are being amortized over the term of the related debt (19 years).

*Inventory*

Inventory consisting of meters, pumps, valves and other merchandise, held for replacement purposes, is stated at cost.

*Accounting estimates*

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

*Restricted and Unrestricted resources*

When both restricted and unrestricted resources are available for use, it is the District's policy to use restricted resources first, and then unrestricted resources as they are needed.

*Tenant Security Deposits*

Tenant security deposits are held in a segregated demand account in the name of the District.

LOVE COUNTY RURAL WATER DISTRICT NO.2  
 NOTES TO THE FINANCIAL STATEMENTS  
 June 30, 2011

**NOTE 2 – CASH AND INVESTMENTS**

All deposits are stated at cost, which approximates market value unless otherwise indicated. Funds are invested only in Certificates of Deposits in Oklahoma banks. Funds in excess of \$250,000 are collateralized by securities held by the pledging institution. As of June 30, 2011 the District had \$ 736,825 deposited in several financial institutions. Of those balances \$ 500,000 were insured by federal depository insurance and the remaining was collateralized by securities held on behalf of the District.

Custodial credit risk is the risk that in the event of a bank failure, the District's deposits may not be returned to it. GASB directs that deposits be disclosed as exposed to custodial credit risk if they are not covered by depository insurance and the deposits are as follow:

- A. Uncollateralized,
- B. Collateralized by securities held by pledging financial institution, or
- C. Collateralized by securities held by the pledging financial institution's trust department or agent but not in the district's name.

None of the District's aggregate bank balances, not covered by depository insurance, were exposed to custodial credit risk as described above at year end.

**NOTE 3 – LONG-TERM DEBT**

Description	Interest rate payable	Amount of Original issue	Amount outstanding 06/30/10	Issued current year	Retired Current year	Amount outstanding 06/30/11
Utility revenue Bonds						
Series 1998	5.00% - 5.70%	360,000	205,000	-	(20,000)	185,000
Utility revenue Bonds						
Series 2001	6.00%	<u>130,000</u>	<u>130,000</u>	-	-	<u>130,000</u>
Total bonded debt principal payable			335,000	-	(20,000)	315,000
Accrued interest			<u>9,703</u>	-	-	<u>9,143</u>
Total bond debt payable			<u>344,703</u>	-	<u>(20,000)</u>	<u>324,143</u>

As of June 30, 2011, long-term debt of the Love County Rural Water District No. 2 consisted of \$295,000 in utility system revenue bonds. The only security for the bonds is net revenue provided by the operation of the district's rural water system. The stated maturities of the bonds and interest rates are as follows:

July 1, 2013	\$ 40,000	5.60%
July 1, 2018	125,000	5.70%
July 1, 2023	<u>130,000</u>	6.00%
TOTAL	<u>\$ 295,000</u>	

LOVE COUNTY RURAL WATER DISTRICT NO.2  
 NOTES TO THE FINANCIAL STATEMENTS  
 June 30, 2011

The debt service requirements on the above bonds are as follows:

Due in fiscal year ending June 30,	Principal	Interest	Total
2012	20,000	17,165	37,165
2013	20,000	16,045	36,045
2014	25,000	14,925	39,925
2015	25,000	13,500	38,500
2016	25,000	12,075	37,075
2017- 2021	120,000	41,175	161,175
2021 - 2023	<u>60,000</u>	<u>5,100</u>	<u>65,100</u>
	<u>295,000</u>	<u>119,985</u>	<u>414,985</u>

Total interest charged to expense during the current year was \$18,285

**NOTE 4 – PROPERTY AND EQUIPMENT**

Fixed assets are depreciated on a straight-line basis over their estimated useful life. As of June 30, fixed assets consisted of the following:

	<u>June 30, 2010</u>	<u>Additions</u>	<u>Deletions</u>	<u>June 30, 2011</u>
Water systems	\$ 1,096,534		\$ -	\$ 1,096,534
Office furnitures and fixtures	8,214	-		8,214
Machinery and equipment	137,462	19,637		157,099
Land	30,057			30,057
Work in process - see Note No. 5	-	97,070	-	97,070
	<u>1,272,267</u>	<u>116,707</u>	<u>-</u>	<u>1,388,974</u>
Less accumulated depreciations	<u>(696,908)</u>	<u>(34,371)</u>	<u>-</u>	<u>(731,279)</u>
	-			-
Net book value	<u>\$ 575,359</u>	<u>\$ 82,336</u>	<u>\$ -</u>	<u>\$ 657,695</u>

Depreciation expense for the year ended June 30, 2011 was \$34,371.

**NOTE 5 – COMMUNITY DEVELOPMENT BLOCK GRANT**

The District received a Community Development Block Grant in the amount of \$249,999. The purpose is waterline replacement, purchase and install radio read meters with computer, telemetry/SCADA for well, standpipes, and booster station. The District's matching funds are equal to \$225,000.

**NOTE 6 – BOND ORIGATION COSTS**

Bond origination costs are amortized on the straight-line basis over the life of the bonds. Amortization expense for the year ended was \$1,547.

LOVE COUNTY RURAL WATER DISTRICT NO.2  
NOTES TO THE FINANCIAL STATEMENTS  
June 30, 2011

**NOTE 7 – CASH NOT AVAILABLE FOR USE IN OPERATIONS**

The District has classified as restricted certain cash and cash equivalents that are not available for use in operations. Cash restricted to maintain certain facilities, pay interest on and retire Utility Revenue Bonds outstanding:

Depreciation and replacement	\$	122,650
Series 2001 Bond reserve account		12,364
Series 1998 Bond reserve account		40,348
Principal and interest fund, including escrow		<u>36,935</u>
	\$	<u>212,298</u>

**NOTE 8 – RISK MANAGEMENT**

The District is exposed to various risks of loss related to limited torts; theft of, damage to and destruction of assets; errors and omissions and natural disasters for which the District carries commercial insurance. There have been no significant reductions in coverage from the prior year and settlements have not exceeded coverage in the past three years.

*Health Care Coverage*

During the year ended June 30, 2011, employees of the District were covered by health insurance under a plan sponsored by the State of Oklahoma.

*Workers' Compensation Coverage*

Workers' compensation insurance is purchased through Oklahoma Rural Water Association.