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**MAYES COUNTY
RURAL WATER DISTRICT NO. 3**

FINANCIAL STATEMENTS
AND
INDEPENDENT AUDITOR'S REPORT
FOR THE YEAR ENDED JUNE 30, 2011

MAYES COUNTY RURAL WATER DISTRICT #3

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WINGARD, RAGSDALE & LANGLEY

CERTIFIED PUBLIC ACCOUNTANTS, PLLC

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INDEPENDENT AUDITOR'S REPORT

Honorable Chairman and Board of Directors
Mayes County Rural Water District No. 3
Disney, Ok 74340

We have audited the statement of net assets, statement of revenues, expenses and changes in net assets and statement of cash flows, which collectively comprise the basic financial statements of the Mayes County Rural Water District #3 as of June 30, 2011. These financial statements are the responsibility of the Mayes County Rural Water District No. 3'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 Mayes County Rural Water District No. 3 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.

Sincerely,



WINGARD, RAGSDALE & LANGLEY

CERTIFIED PUBLIC ACCOUNTANTS, PLLC

PRYOR, OKLAHOMA

September 1, 2011

MAYES COUNTY RURAL WATER DISTRICT NO. 3
STATEMENT OF NET ASSETS
 JUNE 30,

Assets	<u>2011</u>
Current Assets	
Cash and cash equivalents	\$ 243,816
Accounts Receivable	41,262
Inventory	<u>13,724</u>
Total Current Assets	<u>298,802</u>
Noncurrent Assets:	
Restricted Investments	101,164
Capital Assets (net)	3,185,548
Loan Costs, net	<u>28,751</u>
Total Restricted Assets	<u>3,315,463</u>
Total Assets	<u><u>3,614,265</u></u>
Liabilities and Net Assets	
Current Liabilities	
Accounts Payable	13,083
Current Notes Payable	59,300
Accrued Interest Payable	<u>6,069</u>
Total Current Liabilities	<u>78,452</u>
Long Term Liabilities	
Long Term Notes Payable	1,600,377
Customer Deposits	<u>46,305</u>
Total Current Liabilities	<u>1,646,682</u>
Net Assets	
Invested in capital assets, net of related debt	1,519,802
Restricted	101,164
Unrestricted	<u>268,165</u>
Total Net Assets	<u>1,889,131</u>
Total Liabilities and Net Assets	<u><u>\$ 3,614,265</u></u>

The accompanying notes are an integral part of these financial statements.

MAYES COUNTY RURAL WATER DISTRICT NO. 3
STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS
 JUNE 30,

	<u>2011</u>
Support and Revenue	
Water Income	\$ 455,031
Water Tap Income	<u>21,250</u>
Total Support and Revenue	<u>476,281</u>
Expenses	
Water Purchases	5,896
Depreciation	93,241
Salaries	172,738
Chemicals	9,673
Maintenance	32,518
Operating Supplies	4,172
Office Expense	12,636
Utilities	32,945
Directors Expense	4,380
Professional Fees	5,659
Vehicle Expense	8,681
Miscellaneous	1,419
Insurance	13,991
Payroll Taxes	14,133
Lab Testing	9,745
Bad Debt	1,071
Employee pension Plan	21,726
Employee Health Insurance	<u>9,625</u>
Total Expenses	<u>454,249</u>
Non-Operating Revenue (Expense)	
Interest Expense	(25,369)
Late Charges	6,922
Interest Income	1,407
Miscellaneous	<u>6,371</u>
Total Support and Revenue	<u>(10,669)</u>
Increase (Decrease) in Net Assets	11,363
Net Assets, beginning of year	<u>1,877,768</u>
Net Assets, end of year	<u><u>\$ 1,889,131</u></u>

The accompanying notes are an integral part of these financial statements.

MAYES COUNTY RURAL WATER DISTRICT NO. 3
STATEMENT OF CASH FLOWS
 June 30,

	<u>2011</u>
Cash flows from operating activities	
Changes in net assets	\$ 11,363
Adjustments to reconcile change in net assets to net cash used operating activities:	
Depreciation and amortization expense	93,169
Change in operating assets/liabilities	
(Increase) of receivables	(1,697)
(Increase) decrease in inventory	(3,224)
(Decrease) in accounts payable and accrued expenses	<u>(158,293)</u>
Net cash provided by (used in) operating activities	<u>(58,681)</u>
Cash flows from investing activities	
Purchase of property and equipment	(299,568)
Loan Costs Incurred	1,166
Customer Deposits	<u>255</u>
Net cash used in investing activities	<u>(298,147)</u>
Cash flows from financing activities	
Borrowings under long-term debt	354,925
Borrowings under current notes payable	59,300
Payments of notes payable	(39,950)
Payments on line-of-credit	<u>-</u>
Net cash provided by financing activities	<u>374,275</u>
Net increase in cash	17,447
Cash and cash equivalents, beginning of year	327,533
Cash and cash equivalents, end of year	<u>\$ 344,980</u>

The accompanying notes are an integral part of these financial statements.

Note 1 - Nature of Organization

The Mayes County Rural Water District No. 3 is a non-profit governmental organization. Its purpose is to process and provide for the use and benefit of its members a water processing and distribution system, including physical facilities necessary for its operations and maintenance. The District was organized by the Board of County Commissioners of Mayes County, Oklahoma. District members fall within territorial boundaries within Delaware and Mayes County as assigned by the Board of County Commissioners of Mayes County, Oklahoma.

Note 2 - Summary of Significant Accounting Policies

Basis of 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. The activities are financed primarily by user charges and the measurement of financial activity focuses on net income measurement similar to the private sector.

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

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

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

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make certain estimates and assumptions that effect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the balance sheet date, and reported revenues and expenses during the reporting period. Estimates are used to determine depreciation expense, the allowance for doubtful accounts and certain claims and judgment liabilities, among other amounts. Actual results may differ from those estimates.

The District adopts annual operations and capital budgets. Budgets are adopted on a basis consistent with accounting principles generally accepted in the United States of America. The current operating budget details the District's plans to earn and expend funds for charges incurred for operation, maintenance, certain interest and general functions, and other charges for the fiscal year. The capital budget details the plan to receive and expend cash basis capital contribution fees, special assessments, grants, borrowings and certain revenues for capital projects.

Note 2 - Summary of Significant Accounting Policies (continued)

All unexpensed and unencumbered appropriations in the operating budget lapse at the end of the fiscal year. No appropriation for a capital project in the capital budget lapses until the purpose for which the appropriation was made has been accomplished or abandoned.

The Board of Directors adopts a budget at the meeting prior to the beginning of the new fiscal year. Actual revenues and expenditures are monitored and compared with the budget during the year. Significant variations from budgeted amounts are researched and the board is informed of the results.

Cash and Cash Equivalents - Cash and cash equivalents, for purposes of the statement of cash flows, include restricted and unrestricted cash on hand or on deposit, interest in State Treasurer's Pool, certificates of deposit, repurchase agreements and investments with a maturity of three months or less.

Investments are reported at their fair market value. The District is permitted to invest in certificates of deposit and United States general obligations. Banks must guarantee all District funds they hold with specified securities the bank owns for cumulative amounts exceeding the \$250,000 FDIC guarantee.

Restricted Assets - Restricted assets represent cash, investments and receivables maintained in accordance with bond resolutions, loan agreements, grant awards, and other resolutions and formal actions of the District or by agreement for the purpose of funding certain debt service payments, depreciation and contingency activities, and improvements and extensions to the water system.

Receivables and Payables - Customer receivables represent service fees earned, but not yet collected. Service billings at the end of the year are made and the revenues recorded through year-end.

Inventories - Inventories consist of construction materials, repair parts, and chemicals. Materials and supplies are stated at cost.

Capital Assets - Property, plant and equipment in service and construction in progress are recorded at cost, if purchased or constructed. Assets acquired through contributions from developers or other customers are capitalized at their estimated fair market value, if applicable or at engineers' fair market value or cost to construct at the date of contribution. Internal engineering costs are capitalized to the extent of direct support and contribution to construct and expansion projects. Costs of studies that directly result in specific construction projects are capitalized.

Maintenance and repairs, which do not significantly extend the value or life of property, plant and equipment, are expensed as incurred.

Interest costs are capitalized on the construction of qualified assets, whether or not borrowings exist for such projects, to the extent of amounts funded by debt or operating results. Interest is not capitalized on project costs funded by contributed capital, such as grants and gifts. Interest costs of tax-exempt borrowings are capitalized net of related investment earnings or the proceeds.

Note 2 - Summary of Significant Accounting Policies (continued)

Assets are depreciated on the straight-line method. Depreciation is calculated using the following estimated useful lives:

	<u>Years</u>
Land and Buildings	10 - 30
Water System	10 - 75
Furniture and Fixtures	5-10
Equipment	3-10
Vehicles	10

Long Term Obligations - Long-term obligations are reported at face value, net of applicable premiums and discounts.

Revenues and Rate Structure - Revenues from water services are recognized on the accrual basis and as earned. Services are supplied to customers under a rate structure designed to produce revenues sufficient to provide for operating and maintenance costs, capital outlay, debt service, reserves and debt service coverage.

Capital Contributions - Contributions are recognized in the Statement of Revenues, Expenses and changes in Net Assets when earned. Contributions include tap fees, capital grants, and other supplemental support by federal, state and local grants in support of system improvements.

Net Assets - Net assets comprise the various net earnings from operating and non-operating revenues, expenses and contributions of capital. Net assets are classified in the following three components: invested in capital assets, net of related liabilities; Restricted for capital activity and debt service; and unrestricted net assets. Invested in capital assets, net of related debt, consists of all capital assets, net of accumulated depreciation and reduced by outstanding debt that is attributable to acquisition, construction and improvement of those assets; debt related to unspent proceeds or other restricted cash and investments is excluded from determination. Restricted for capital activity and debt service consists of net assets for which constraints are placed by external parties, such as lenders, grantors, contributors, laws, regulations, legislation, including self-imposed legal mandates, less any related liabilities. Unrestricted consists of all other assets not included in the above categories.

Note 3 - Deposits and Investments

Deposits include demand deposits and certificates of deposit in financial institutions. All bank balances are covered by federal depository insurance or by collateral held by the bank and pledged to the District.

MAYES COUNTY RURAL WATER DISTRICT NO. 3
 NOTES TO FINANCIAL STATEMENT
 June 30, 2011

Note 7 - Long-Term Debt

Note 1

The Oklahoma Water Resources Board provided the MAYES COUNTY RURAL WATER DISTRICT NO. 3 with a note in the amount of \$ 465,000.00 on June 17, 1998. This note requires quarterly principal and interest payments on February 15, May 15, August 15, and November 15. Monthly payments are made to the loan trustee, The Bank of New York Trust Company, N.A. The monthly payments are invested in securities by the trustee. Quarterly, the monthly payments and earnings are used by the trustee to make the principal and interest payments. The note also required an amount be kept in reserve of \$ 41,840. This is to be used to make principal and interest payments in case the District is not able to make such payments. As of June 30, 2011, the balance on this note is \$344,200.

Note 2

The Oklahoma Water Resources Board provided the MAYES COUNTY RURAL WATER DISTRICT NO. 3 a note in the amount of \$845,000.00 on December 17, 2003. This note requires quarterly principal and interest payments on March 15, June 15, September 15, and December 15. Monthly payments are made to the loan trustee, The Bank of New York Trust Company, NA. The monthly payments are invested in securities by the trustee. Quarterly, the monthly payments and earnings are used by the trustee to make the principal and interest payments. The note also required an amount be kept in reserve of \$57,832.00. This is to be used to make principal and interest payments in case the District is not able to make such payments. As of June 30, 2011, the balance on this note is \$721,100.

Note 3

The Oklahoma Water Resources Board provided the MAYES COUNTY RURAL WATER DISTRICT NO. 3 with a \$900,000 note on December 15, 2009 to expand its water system. This note requires semi-annual interest only payments until the construction is complete and will require semi-annual principal and interest payments on March 15 and September 15 of each year starting no later than March 15, 2011. The rate of interest currently charged on this variable rate loan is 3.06%. As of June 30, 2011 the balance on this is \$594,377.

Principal payments on the notes are required as follows:

	<u>Note 1</u> <u>2011</u>	<u>Note 2</u> <u>2011</u>	<u>Note 3</u> <u>2011</u>
Year 1	9,500	13,800	36,000
Year 2	13,700	19,300	36,000
Year 3	14,700	20,400	36,000
Year 4	15,900	21,500	36,000
Year 5	17,300	22,700	36,000
Thereafter	273,100	623,400	414,377

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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*

Honorable Chairman and Board of Directors
Mayes County Rural Water District No. 3
Disney, Ok 74340

We have audited the statement of net assets, statement of revenues, expenses and changes in net assets and statement of cash flows, which collectively comprise the basic financial statements of the Mayes County Rural Water District #3 as of June 30, 2011. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

INTERNAL CONTROL OVER FINANCIAL REPORTING

In planning and performing our audit, we considered the Mayes County Rural Water District #3's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Mayes County Rural Water District #3's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Mayes County Rural Water District #3's internal control over financial reporting.

A control deficiency 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 misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the Mayes County Rural Water District #3's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the Mayes County Rural Water District #3's financial statements that is more than inconsequential will not be prevented or detected by the Mayes County Rural Water District #3's internal control.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the Mayes County Rural Water District #3's internal control. We consider items 2011-1 reported on the Schedule of Findings and Responses to be a material weakness in internal control.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses.

COMPLIANCE AND OTHER MATTERS

As part of obtaining reasonable assurance about whether the Mayes County Rural Water District #3'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*.

This report is intended solely for the information and use of management, the Board of Directors, other within the entity, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses.



WINGARD, RAGSDALE & LANGLEY

CERTIFIED PUBLIC ACCOUNTANTS, PLLC

SEPTEMBER 1, 2011

WINGARD, RAGSDALE & LANGLEY

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SCHEDULE OF FINDINGS AND RESPONSES

2011-1 Cash Receipts:

REPEAT FINDING FROM 2010 AUDIT

Criteria or specific requirement: Segregation of certain duties is necessary to maintain the integrity of reported financial information.

Condition: Inherent in small entities, segregation of certain accounting duties is limited due to the limited number of staff. As such, alternative methods of maintaining the “check and balance” feature of segregated accounting procedures may require alternative solutions to meet those needs.

Context: Observations and inquiries revealed that the cash receipts accounting cycle involves receipt of cash payments from customers. The same person is responsible for the custody, recording, and reconciling of these amounts. Although the amounts are immaterial on a daily basis, over time, these amounts become material to the financial statements. No reconciliation of these, or any revenue amounts, is reviewed by someone independent of these procedures. Without reviewing the operational results in comparison to cash receipts there is an opportunity for fraud.

Effect: Revenues could be embezzled. When the same individual has responsibilities

Cause: There is no monitoring control over cash receipts.

Recommendation: Reconciliation of the cash receipts process should be reviewed by someone outside of the recording and reconciling functions. By reviewing the monthly bank reconciliations and billing register reports, discrepancies in reported amounts would be identified, before a material error or fraud could occur.

Views of responsible officials and planned corrective actions:

There has been no action by management to change operating policies or procedures with respect to these findings as presented in the 2009 audit engagement.