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AUDIT REPORT

RECEIPT #

16630

NOWATA COUNTY RURAL WATER AND SEWER DISTRICT #1
NOWATA COUNTY, OKLAHOMA

APRIL 30, 2011

KERSHAW CPA & ASSOCIATES, PC

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NOWATA COUNTY RURAL WATER AND SEWER DISTRICT #1
NOWATA COUNTY, OKLAHOMA
APRIL 30, 2011

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NOWATA COUNTY RURAL WATER AND SEWER DISTRICT #1
NOWATA COUNTY, OKLAHOMA
APRIL 30, 2011

BOARD OF DIRECTORS

<u>NAME</u>	<u>POSITION</u>	<u>TERM EXPIRATION</u>
WILLIAM HAYDEN	CHAIRMAN	JULY 2013
DON MEEKER	VICE-CHAIRMAN	JULY 2012
DAVID SEIGEL	SECRETARY	JULY 2012
STEVE BRINKER	MEMBER	JULY 2011
DUSTIN PERDUE	MEMBER	JULY 2013

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INDEPENDENT AUDITOR'S REPORT

To the Board of Directors
Nowata County Rural Water and Sewer District #1
Nowata County, Oklahoma

I have audited the accompanying financial statements of the Nowata County Rural Water and Sewer District #1, as of and for the fiscal year ended April 30, 2011, as listed in the table of contents. These financial statements are the responsibility of the Nowata County Rural Water and Sewer District #1's management. My responsibility is to express an opinion on these financial statements based on my audit.

I conducted my 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 I 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. I believe that my audit provides a reasonable basis for my opinion.

Because of the inadequacy of accounting records related to fixed assets prior to May 1, 1997, we were unable to form an opinion regarding the amounts at which property, plant and equipment and accumulated depreciation are recorded in the accompanying statement of net assets at April 30, 2011 (stated at \$1,090,068 and \$656,023, respectively) or the amount of depreciation expense for the year then ended (stated at \$29,831).

In my opinion, except for the effects, if any, on the financial statements of improper capital asset recordkeeping described in the preceding paragraph, the financial statements referred to above present fairly, in all material respects, the financial position of the Nowata County Rural Water and Sewer District #1, Nowata County, Oklahoma, as of April 30, 2011, 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, I have also issued my report dated August 18, 2011, on my consideration of the Nowata County Rural Water and Sewer District #1's internal control over financial reporting and on my 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 my audit.

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Nowata County Rural Water and Sewer District #1 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 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 my audit of the basic financial statements, and accordingly, I do not express an opinion thereon.



Robert E. Kershaw
Certified Public Accountant

August 18, 2011

EXHIBIT A

NOWATA COUNTY RURAL WATER AND SEWER DISTRICT #1
 NOWATA COUNTY, OKLAHOMA
 STATEMENT OF NET ASSETS
 APRIL 30, 2011

<u>ASSETS</u>	<u>2011</u>	<u>Memo Only 2010</u>
<u>Current Assets:</u>		
Cash and cash equivalents (Note 1)	\$ 122,562	\$ 113,755
Investments (Note 1)	56,728	56,141
Accounts Receivable (Note 1)	14,508	14,230
Interest Receivable	107	68
Accrued water sales	1,122	1,764
Prepaid Insurance	2,418	2,402
Total Current Assets	<u>197,445</u>	<u>188,360</u>
<u>Fixed Assets:</u>		
Land	22,012	22,012
Water Distribution System	1,068,056	1,051,177
Less: Accumulated Depreciation	<u>(656,023)</u>	<u>(626,201)</u>
Total Fixed Assets	<u>434,045</u>	<u>446,987</u>
<u>Other Assets:</u>		
Cash held in trust (Note 1)	21,877	22,113
Rural Development Reserve Account	-	-
Loan origination fees, net of accumulated amortization (Note 5)	<u>2,056</u>	<u>2,584</u>
Total Other Assets	<u>23,933</u>	<u>24,697</u>
TOTAL ASSETS	<u>\$ 655,423</u>	<u>\$ 660,044</u>
<u>LIABILITIES & NET ASSETS</u>		
<u>Current Liabilities:</u>		
Accounts Payable	\$ 8,020	\$ 8,853
Accrued water purchases	2,464	2,335
Accrued interest payable	316	361
Current Portion of Long-Term Debt	<u>9,600</u>	<u>8,900</u>
Total Current Liabilities	<u>20,400</u>	<u>20,449</u>
<u>Long-Term Liabilities:</u>		
Long-Term Debt	130,600	139,500
Less: Current Portion of Long-Term Debt	<u>(9,600)</u>	<u>(8,900)</u>
Total Long-Term Debt	<u>121,000</u>	<u>130,600</u>
TOTAL LIABILITIES	<u>141,400</u>	<u>151,049</u>
<u>NET ASSETS:</u>		
Invested in capital assets, net of related debt	303,445	307,487
Restricted for debt service	21,877	22,113
Unrestricted	<u>188,702</u>	<u>179,395</u>
TOTAL NET ASSETS	<u>514,024</u>	<u>508,995</u>
TOTAL LIABILITIES AND NET ASSETS	<u>\$ 655,423</u>	<u>\$ 660,044</u>

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

EXHIBIT B

**NOWATA COUNTY RURAL WATER AND SEWER DISTRICT #1
NOWATA COUNTY, OKLAHOMA
STATEMENT OF REVENUES, EXPENSES & CHANGES IN NET ASSETS
FOR THE TWELVE MONTHS ENDED APRIL 30, 2011**

	<u>2011</u>	<u>Memo Only 2010</u>
<u>Operating Revenue:</u>		
Water sales	\$ 108,435	\$ 104,041
Sewer sales	22,255	22,258
Other	4,838	4,107
Total Operating Revenue	<u>135,527</u>	<u>130,406</u>
<u>Operating Expenses:</u>		
Water purchases	41,784	38,110
Management fees	39,271	36,785
Utilities	5,870	5,476
Professional fees	2,450	790
Maintenance and repair	11,798	9,267
Insurance	2,025	2,152
Miscellaneous expense	2,526	4,518
Bad Debt Expense	-	75
Depreciation Expense	29,821	29,795
Amortization expense	528	528
Total Operating Expenses	<u>136,073</u>	<u>127,495</u>
Net Operating Income (Loss)	<u>(547)</u>	<u>2,911</u>
<u>Non-operating Income (Expense):</u>		
Interest Income	608	253
New units	7,000	2,460
Interest Expense	(2,032)	(2,796)
Total Non-operating Income (Expense)	<u>5,575</u>	<u>(83)</u>
Net Income (Loss)	5,029	2,828
Total Net Assets, Beginning of Year	508,995	506,167
Total Net Assets, Prior Year Adjustment	<u>-</u>	<u>-</u>
Total Net Assets, End of Year	<u>\$ 514,024</u>	<u>\$ 508,995</u>

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

NOWATA COUNTY RURAL WATER AND SEWER DISTRICT #1
 NOWATA COUNTY, OKLAHOMA
 STATEMENT OF CASH FLOWS
 FOR THE TWELVE MONTHS ENDED APRIL 30, 2011

	<u>2011</u>	<u>Memo Only 2010</u>
<u>Net Cash Flows from Operating Activities:</u>		
Cash Receipts from Customers	\$ 135,890	\$ 130,460
Payments to Suppliers for Goods & Services	(106,444)	(97,546)
Net Cash Provided (Used) by Operating Activities	<u>29,446</u>	<u>32,914</u>
<u>Net Cash Flows from Capital & Related Financing Activities:</u>		
Additions to Capital Assets	(16,879)	(5,957)
Proceeds from Sale of Capital Assets	-	-
Capital Contributions	-	-
Issuance of benefit units	7,000	2,460
Loan Proceeds	-	-
Principal paid on long-term debt	(8,900)	(8,200)
Interest paid on Debt	(2,077)	(3,093)
Net Cash Provided (Used) by Capital & Related Financing Activities	<u>(20,856)</u>	<u>(14,791)</u>
<u>Net Cash Flows from Investing Activities:</u>		
(Increase) Decrease in investments	(587)	(1,022)
(Increase) Decrease in trust fund cash accounts	236	1,194
Interest Income	569	642
Net Cash Provided (Used) by Investing Activities	<u>217</u>	<u>814</u>
Net Increase (Decrease) in Cash and Cash Equivalents	8,807	18,937
Cash & Cash Equivalents, Beginning of Year	113,755	94,818
Cash & Cash Equivalents, Prior Year Adjustment	-	-
Cash & Cash Equivalents, End of Year	<u>\$ 122,562</u>	<u>\$ 113,755</u>
<u>Reconciliation of operating income (loss) to net cash provided operating activities:</u>		
Operating Income (Loss)	\$ (547)	\$ 2,911
Adjustments to reconcile operating income (loss) to net cash provided (used) by operating activities		
Depreciation & Amortization	30,349	30,323
(Increase)Decrease in Accounts Receivable	(278)	(14,230)
(Increase)Decrease in Prepaid Insurance	(16)	(2,402)
(Increase)Decrease in Accrued water sales	641	(1,764)
(Increase)Decrease in Utility Deposit	-	-
Increase(Decrease) in Accounts Payable	(833)	8,853
Increase(Decrease) in Accrued Water Purchases	129	2,335
Net Cash Provided (Used) by Operating Activities	<u>\$ 29,446</u>	<u>\$ 26,026</u>

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

NOWATA COUNTY RURAL WATER AND SEWER DISTRICT #1
NOWATA COUNTY, OKLAHOMA
NOTES TO FINANCIAL STATEMENTS
APRIL 30, 2011

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accounting policies employed by Nowata County Rural Water and Sewer District #1 (the District) are consistent with accounting principles generally accepted in the United States of America. Significant policies 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. Nowata County Rural Water and Sewer District #1 began reporting during fiscal year ending 2004 under the new reporting model, 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.

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 assets.

A. Purpose:

Nowata County Rural Water and Sewer District #1 is a State of Oklahoma chartered public nonprofit water district. Its purpose is to maintain and operate a water distribution system to serve the needs of owners and occupants of land within the Water District.

B. Basis of Accounting:

The financial statements are presented on the accrual basis of accounting. Under the accrual basis of accounting, revenues are recognized when earned and expenditures are recorded when the liability is incurred.

C. Income Taxes:

Nowata County Rural Water and Sewer District #1 is exempt from federal income tax under section 501(c)(12) of the Internal Revenue Code.

NOWATA COUNTY RURAL WATER AND SEWER DISTRICT #1
NOWATA COUNTY, OKLAHOMA
NOTES TO FINANCIAL STATEMENTS
APRIL 30, 2011

D. 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.

E. Membership Benefit Units:

Members purchase benefit units for the right to obtain services from the Water District. Fees paid for benefit units are considered donations to the Water District and are nonrefundable. Benefit units sold are reflected as non-operating income in the period the services are established.

F. Cash and Cash Equivalents:

Cash and cash equivalents include amounts in demand deposits, money market funds, and certificates of deposit with and original maturity of three months or less.

G. Investments:

The District's investments are FDIC insured certificate of deposit of financial institutions. Investment totals at April 30, 2011 and April 30, 2010 were \$56,728 and \$56,141, respectively.

H. Cash Held in Trust:

Provisions of the loan payable to Oklahoma Water Resources Board require the District to set aside with a Trustee certain amounts for debt service and repair and replacement expenses. At April 30, 2011 and April 30, 2010, the District had \$21,877 and \$22,113, respectively on deposit with The Bank of New York Trust Company, N.A. as Trustee. These amounts were invested in U.S. Treasury Money Funds. The District makes payments monthly to the Trustee to service the semi-annual loan and interest payments. The amount of the payments is adjusted semi-annually to reflect changes in interest rates.

The cash restricted for loan with the Oklahoma Water Resources Board is designated as restricted retained earnings of \$21,877 and \$22,113 for the years ended April 30, 2011 and April 30, 2010, respectively.

I. Property and Equipment:

Property and equipment consisting of a water distribution system are stated at cost and depreciated over the estimated useful lives of the assets. Depreciation is computed using the straight-line method. A capitalization

NOWATA COUNTY RURAL WATER AND SEWER DISTRICT #1
NOWATA COUNTY, OKLAHOMA
NOTES TO FINANCIAL STATEMENTS
APRIL 30, 2011

policy was adopted in July 2005. This policy stated that purchases of capital items in excess of \$350 that increase the capacity or operation efficiency or extend the useful life of any asset are capitalized. Repairs and maintenance are expensed as incurred.

Useful life will be categorized as follows:

- A. 40 years - Meter sets and related equipment, road crossings, pipe in the ground that is not a repair or ordinary maintenance, and any new water line extensions.
- B. 15 years - Pump stations, buildings, tank painting and other structures
- C. 7 years - Motors, pumps, panel boxes, and other related items

J. Accounts Receivable:

The direct write-off method is used to account for uncollectible receivables. The balances at April 30, 2011 and 2010 are considered fully collectible.

K. 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, 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.”

L. 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.

M. Memorandum Totals

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

NOWATA COUNTY RURAL WATER AND SEWER DISTRICT #1
NOWATA COUNTY, OKLAHOMA
NOTES TO FINANCIAL STATEMENTS
APRIL 30, 2011

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

See Note 1(H) above.

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 - DEPOSITS AND INVESTMENTS

Custodial Credit Risk

At April 30, 2011, the District held deposits of approximately \$179,290 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

NOWATA COUNTY RURAL WATER AND SEWER DISTRICT #1
 NOWATA COUNTY, OKLAHOMA
 NOTES TO FINANCIAL STATEMENTS
 APRIL 30, 2011

- 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.).

Concentration of Investment Credit Risk

The District places no limit on the amount it may invest in any one issuer. The District has the following credit risk: 100% in certificate of deposit (\$56,728).

NOTE 4 - CAPITAL ASSETS

Capital asset activity, for the fiscal year ended April 30, 2011, was as follows:

	Balance at April 30, 2010	Additions	Deductions	Balance at April 30, 2011
Land	\$ 22,012	\$ -	\$ -	\$ 22,012
Water System	324,873	14,797	-	339,670
Extension	361,753	-	-	361,753
Water system equipment	6,861	-	-	6,861
Sewer system	357,691	2,082	-	359,773
Subtotal	1,073,189	16,879	-	1,090,068
Less: Accum. Depr.	(626,201)	(29,821)	-	(656,023)
Total Capital Assets (Net of Depreciation)	<u>\$ 446,987</u>	<u>\$ (12,943)</u>	<u>\$ -</u>	<u>\$ 434,045</u>

NOWATA COUNTY RURAL WATER AND SEWER DISTRICT #1
 NOWATA COUNTY, OKLAHOMA
 NOTES TO FINANCIAL STATEMENTS
 APRIL 30, 2011

NOTE 5 - LOAN ORIGINATION FEES

Loan origination fees were costs incurred in connection with the note issued by the Oklahoma Water Resources Board. These costs are being amortized over the remaining term of the note.

	<u>April 30, 2011</u>	<u>April 30, 2010</u>
Amortized asset:		
Loan origination costs	\$ 9,895	\$ 9,895
Accumulated amortization	(7,839)	(7,311)
Total	<u>\$ 2,056</u>	<u>\$ 2,584</u>

NOTE 6 - LONG-TERM DEBT

The District has a loan with Oklahoma Water Resources Board bearing interest based on the Board's Series 1994 A Bonds (1.450% at April 30, 2011), collateralized by the revenue and assets of the water and sewer system. The loan will mature in August 2020. This note is due in semi-annual installments of principal and interest.

Changes in Long-Term Debt

The following is a summary of changes in long-term debt for the year ended April 30, 2011:

	<u>Balance at April 30, 2010</u>	<u>Additions</u>	<u>Deductions</u>	<u>Balance at April 30, 2011</u>
Long-Term Note - OWRB	139,500	-	(8,900)	130,600
Total Long-Term Debt	<u>\$ 139,500</u>	<u>\$ -</u>	<u>\$ (8,900)</u>	<u>\$ 130,600</u>

Debt Services Requirements to Maturity

The annual debt service requirements to maturity, including principal and interest, for long-term debt, as of April 30, 2011, are as follows:

Long-Term Note - OWRB
 Year Ending April

<u>30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2012	\$ 9,600	\$ 1,894	\$ 11,494
2013	10,400	1,755	12,155
2014	11,200	1,604	12,804
2015	12,200	1,441	13,641
2016	13,200	1,264	14,464
2017-2021	74,000	1,073	75,073
Total	<u>\$ 130,600</u>	<u>\$ 9,031</u>	<u>\$ 139,631</u>

NOWATA COUNTY RURAL WATER AND SEWER DISTRICT #1
NOWATA COUNTY, OKLAHOMA
NOTES TO FINANCIAL STATEMENTS
APRIL 30, 2011

NOTE 7 - 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

NOTE 8 - CONTINGENCIES

Litigation

According to management there were no known contingent liabilities at April 30, 2011, which would have a material effect on the financial statements.

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 9 - ECONOMIC DEPENDENCE

Nowata County Rural Water and Sewer District #1 is dependent upon the City of Dewey, Oklahoma, for the District's water supply.

NOTE 10 - SUBSEQUENT EVENTS

The District did not have any subsequent events through August 18, 2011, which is the date the financial statements were issued, for events requiring recording or disclosure in the financial statements for the year ending April 30, 2011.

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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
Nowata County Rural Water and Sewer District #1
Nowata County, Oklahoma

I have audited the financial statements of the Nowata County Rural Water and Sewer District #1, as of April 30, 2011, and have issued my report thereon dated August 18, 2011, which was qualified because I was unable to form an opinion regarding the amount recorded in the accounting records for property, plant and equipment and accumulated depreciation acquired prior to May 1, 1997. Also, the District 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. Except as discussed in the preceding sentences, I conducted my 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

In planning and performing my audit, I considered the Nowata County Rural Water and Sewer District #1's internal control over financial reporting as a basis for designing my auditing procedures for the purpose of expressing my opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Nowata County Rural Water and Sewer District #1's internal control over financial reporting. Accordingly, I do not express an opinion on the effectiveness of the Nowata County Rural Water and Sewer District #1'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.

My 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. I did not identify

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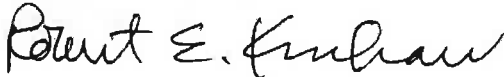
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any deficiencies in internal control over financial reporting that I consider to be material weakness, as defined above.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Nowata County Rural Water and Sewer District #1's financial statements are free of material misstatement, I 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 my audit, and accordingly I do not express such an opinion. The results of my 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 the board of directors and management of the Nowata County Rural Water and Sewer District #1, Nowata County, Oklahoma and is not intended to be and should not be used by anyone other than these specified parties.



Robert E. Kershaw, CPA

August 18, 2011

