

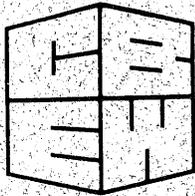
**RURAL WATER DISTRICT NO. 4  
PAWNEE COUNTY  
Pawnee, Oklahoma**

**BASIC FINANCIAL STATEMENTS  
June 30, 2012**

**RURAL WATER DISTRICT #4  
PAWNEE COUNTY  
Pawnee, Oklahoma**

**CONTENTS**

	<b>Page No.</b>
<b>Independent Auditor's Report</b>	1
<b>Basic Financial Statements:</b>	
Statement of Net Assets	2
Statement of Activities	3
Statement of Changes in Net Assets	4
Statement of Cash Flows	5
<b>Notes to the Financial Statements</b>	6-11
<b>Report Required by <i>Government Auditing Standards</i>:</b>	
Report on Internal Control over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with <i>Government Auditing Standards</i>	12-13
<b>Schedule of Findings and Responses</b>	14-15



**CBEW**  
**Professional**  
**Group, LLP**

Certified Public Accountants

DON K. ETHRIDGE, CPA  
WALTER H. WEBB, CPA  
JANE FRAZIER, CPA  
CHARLES E. CROOKS, CPA  
TRISHA J. RIEMAN, CPA

206 N. HARRISON ● P.O. BOX 790 ● CUSHING, OKLAHOMA 74023 ● 918-225-4216 ● FAX 918-225-4315

## INDEPENDENT AUDITOR'S REPORT

July 19, 2012

Board of Directors  
Rural Water District No. 4  
Pawnee County  
Pawnee, Oklahoma

We have audited the accompanying financial statements of Rural Water District No. 4, Pawnee County, Pawnee, Oklahoma (the District), as of and for the year ended June 30, 2012 and 2011, which collectively comprise the District's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the District's management. Our responsibility is to express opinions on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to the 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 audits provide a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Rural Water District No. 4, Pawnee County, Pawnee, Oklahoma as of June 30, 2012 and 2011, and the changes in financial position and cash flows thereof for the years then ended in conformity with accounting principals generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued a report dated July 19, 2012, on our consideration of the Rural Water District No. 4'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 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.

The District has not presented Management's Discussion and Analysis that governmental 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 (GASB), who considers it to be an essential part of the 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.

*CBEW Professional Group, LLP*

CBEW Professional Group, LLP  
Certified Public Accountants

**RURAL WATER DISTRICT NO. 4  
PAWNEE COUNTY  
Pawnee, Oklahoma**

**STATEMENT OF NET ASSETS  
June 30, 2012 and 2011**

	<u>June 30, 2012</u>	<u>June 30, 2011</u>
<b>Assets:</b>		
Cash and cash equivalents (Note 1)	\$ 142,023	\$ 88,072
Receivables (net of allowance for uncollectible)	15,146	20,043
Prepaid insurance	2,720	2,674
Temporarily restricted:		
Cash and cash equivalents (Note 2)	-	23,796
<b>Capital assets:</b>		
Water system, improvements and equipment, net of depreciation	<u>365,817</u>	<u>385,576</u>
<b>Total assets</b>	<u>\$ 525,706</u>	<u>\$ 520,161</u>
<b>Liabilities:</b>		
Accounts payable	\$ 418	\$ 1,203
Accrued water purchases	4,837	5,268
Payroll taxes payable	1,066	634
Interest payable	-	39
Notes payable (Note 3)	<u>-</u>	<u>16,758</u>
<b>Total liabilities</b>	<u>6,321</u>	<u>23,902</u>
<b>Net assets:</b>		
Invested in capital assets, net of related debt	365,817	368,818
Temporarily restricted (Note 2)	-	23,796
Unrestricted	<u>153,568</u>	<u>103,645</u>
<b>Total net assets</b>	<u>\$ 519,385</u>	<u>\$ 496,259</u>

The accompanying notes are an integral part of the basic financial statements.

**RURAL WATER DISTRICT NO. 4  
PAWNEE COUNTY  
Pawnee, Oklahoma**

**STATEMENT OF ACTIVITIES  
For the Years Ended June 30, 2012 and 2011**

	<b>June 30, 2012</b>	<b>June 30, 2011</b>
<b>Revenues:</b>		
Water sales	\$ 184,185	\$ 177,478
Membership income	4,000	4,125
Miscellaneous income	865	-
	<b>189,050</b>	<b>181,603</b>
<b>Expenses:</b>		
Accounting and legal	2,100	2,100
Advertising	70	160
Annual meeting	243	91
Contract services	1,740	11,820
Depreciation	19,759	19,759
Dues and subscriptions	476	514
Equipment rental	5,500	8,698
Insurance	3,946	3,753
Lab tests	252	240
Licenses and permits	-	-
Miscellaneous	-	307
Office supplies and postage	3,139	2,173
Payroll taxes	2,812	1,540
Repair and maintenance	-	-
Salaries	32,467	19,162
Supplies	7,554	14,451
Subcontractor labor	-	-
Telephone	414	410
Travel	3,600	3,600
Water purchases	82,362	63,558
	<b>166,434</b>	<b>152,336</b>
<b>Total expenses</b>		
	<b>22,616</b>	<b>29,267</b>
<b>Operating income (loss)</b>		
	<b>22,616</b>	<b>29,267</b>
<b>Other income and expense:</b>		
Interest income	746	565
Interest expense	(236)	(928)
Donation of capital assets	-	-
	<b>510</b>	<b>(363)</b>
<b>Total other income and expense</b>		
	<b>510</b>	<b>(363)</b>
<b>Net income (loss)</b>	<b>23,126</b>	<b>28,904</b>
<b>Net assets - beginning of year</b>	<b>496,259</b>	<b>467,355</b>
<b>Net assets - end of year</b>	<b>\$ 519,385</b>	<b>\$ 496,259</b>

The accompanying notes are an integral part of the basic financial statements.

**RURAL WATER DISTRICT NO. 4  
PAWNEE COUNTY  
Pawnee, Oklahoma**

**STATEMENT OF CHANGES IN NET ASSETS  
For the Years Ended June 30, 2012 and 2011**

	<u>Net Assets (Unrestricted)</u>	<u>Net Assets (Temporarily Restricted)</u>	<u>Total Net Assets</u>
<b>Balance - beginning of year 6-30-10</b>	\$ 443,559	\$ 23,796	\$ 467,355
Change in net assets	<u>28,904</u>	<u>-</u>	<u>28,904</u>
<b>Balance - end of year 6-30-11</b>	<u>\$ 472,463</u>	<u>\$ 23,796</u>	<u>\$ 496,259</u>
<b>Balance - beginning of year 6-30-11</b>	\$ 496,259	\$ 23,126	\$ 519,385
Change in net assets	<u>23,126</u>	<u>(23,126)</u>	<u>-</u>
<b>Balance - end of year 6-30-12</b>	<u>\$ 519,385</u>	<u>\$ -</u>	<u>\$ 519,385</u>

The accompanying notes are an integral part of the basic financial statements.

**RURAL WATER DISTRICT NO. 4  
PAWNEE COUNTY  
Pawnee, Oklahoma**

**STATEMENT OF CASH FLOWS  
For the Years Ended June 30, 2012 and 2011**

	<u>June 30, 2012</u>	<u>June 30, 2011</u>
<b>Cash flows from operating activities:</b>		
Cash received from customers	\$ 193,947	\$ 180,235
Cash payments to suppliers for goods and contractors and other services	<u>(147,505)</u>	<u>(132,392)</u>
<b>Net cash provided by operating activities</b>	<u>46,442</u>	<u>47,843</u>
<b>Cash flows from capital and related financing activities:</b>		
Acquisition & construction of capital assets	-	-
Principal paid on debt	(16,758)	(3,430)
Interest paid on debt	(275)	(951)
Release of cash from restriction	23,796	-
<b>Net cash used in capital and related financing activities</b>	<u>6,763</u>	<u>(4,381)</u>
<b>Cash flows from investing activities:</b>		
Interest income	746	565
<b>Net cash provided by investing activities</b>	<u>746</u>	<u>565</u>
<b>Net increase (decrease) in cash</b>	53,951	44,027
<b>Cash and cash equivalents at beginning of year</b>	<u>88,072</u>	<u>44,045</u>
<b>Cash and cash equivalents at end of year</b>	<u>\$ 142,023</u>	<u>\$ 88,072</u>
<b>Reconciliation of operation income to net cash provided by operating activities:</b>		
Operating income (loss)	\$ 22,616	\$ 29,267
<b>Adjustments to reconcile net income to net cash provided by operating activities:</b>		
Depreciation	19,759	19,759
Changes in assets and liabilities:		
(Increase) decrease in accounts receivable	4,897	(1,368)
(Increase) decrease in prepaid expenses	(46)	(119)
Increase (decrease) in accounts payable	(785)	103
Increase (decrease) in accrued water purchases	(431)	325
Increase (decrease) in payroll taxes payable	<u>432</u>	<u>(124)</u>
<b>Total adjustments</b>	<u>23,826</u>	<u>18,576</u>
<b>Net cash provided by operating activities</b>	<u>\$ 46,442</u>	<u>\$ 47,843</u>

The accompanying notes are an integral part of the basic financial statements.

**RURAL WATER DISTRICT NO. 4  
PAWNEE COUNTY  
Pawnee, Oklahoma**

**NOTES TO THE BASIC FINANCIAL STATEMENTS  
June 30, 2012 and 2011**

**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

Rural Water District No. 4, Pawnee County, Oklahoma (the District), was created under the provisions of Title 82, O.S. 1981, Sections 1324.1-1324.26 inclusive, for the purpose of providing water to the members it serves. Membership in the water district consists of water users who have paid the required membership and connection fees. The District is exempt from federal and state income taxes.

The membership consists of approximately 314 users, each entitled to one vote. The Board of Directors consists of 5 members serving 3-year terms. The vacant Board seats are elected at the annual meeting in July, and following, the Board of Directors meet and elect a chairman, vice-chairman, and secretary-treasurer. All Board members serve without pay.

The more significant of the government's accounting policies are described below.

**A. Reporting Entity**

Rural Water District No. 4 is an independent, self-contained reporting entity with no associated component units. It is operated in a manner similar to a private business enterprise where the cost (expenses, including depreciation) of providing water services is financed through user charges. The District purchases all of its water from Lone Chimney Water Association.

**B. Measurement Focus, Basis of Accounting and Basis of Presentation – Fund Accounting**

The accompanying financial statements have been prepared on the accrual basis of accounting in accordance with Generally Accepted Accounting Principles (GAAP) promulgated in the United States of America. The accounting and financial reporting treatment is accounted for on a flow of economic resources measurement focus. With this measurement focus, all assets and liabilities associated with the operation are included on the statement of net assets. The operating statements present increases (e.g., revenues) and decreases (e.g., expenses) in net total assets. Depreciation expense is provided for capital assets based upon estimated useful lives.

Financial activity is accounted for on the flow of economic resources measurement focus using the accrual basis of accounting. Under this method, revenues are recorded when earned and expenses are recorded at the time liabilities are incurred. In compliance with the Governmental Accounting Standards Board (GASB) Statement No. 29 the District has elected to only apply Financial Accounting Standards Board (FASB), Accounting Principles Board (APB) and Accounting Research Board (ARB) materials issued on or before November 30, 1989 that do not conflict with GASB.

**C. Assets, Liabilities and Equity**

**1. Deposits and Investments**

Oklahoma Statutes authorize the District to invest in certificates of deposit, repurchase agreements, passbooks, bankers' acceptances, and other available bank investments provided that all deposits are fully covered by approved securities pledged to secure those funds. In addition, the District can invest in direct debt securities of the United States unless such an investment is expressly prohibited by law.

All the bank deposits are held at one financial institution and are carried at cost. For purposes of statements of cash flows, the District considers cash and all highly liquid investments with an initial maturity of three months or less to be cash equivalents.

**RURAL WATER DISTRICT NO. 4  
PAWNEE COUNTY  
Pawnee, Oklahoma**

**NOTES TO THE BASIC FINANCIAL STATEMENTS  
June 30, 2012 and 2011**

**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

**C. Assets, Liabilities and Equity (Continued)**

**1. Deposits and Investments (Continued)**

*Custodial Credit Risk*

At June 30, 2012, the District held deposits of approximately \$142,023 at financial institutions. The District's cash deposits, including interest-bearing certificates of deposit, are entirely covered by Federal Depository Insurance (FDIC) or direct obligation of the U.S. Government insured or collateralized with securities held by the District or by its agent in the District's name.

*Investment Interest Rate Risk*

The District does not have a formal investment policy that limits investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates.

*Investment Credit Risk*

The District has no policy that limits its investment choices other than the limitation of state law as follows:

- a. Direct obligations of the U.S. Government, its agencies and instrumentalities to which the full faith and credit of the U.S. Government is pledged, or obligations to the payment of which the full faith and credit of the State is pledged.
- b. Certificates of deposits or savings accounts that are either insured or secured with acceptable collateral with in-state financial institutions, and fully 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 investments held at June 30, 2012 are as follows:

Type	Weighted Average Maturity (Months)	Credit Rating	Market Value	Cost
Investments				
Money Market	N/A	AAAm	\$ 142,023	\$ 142,023
Total investments			<u>\$ 142,023</u>	<u>\$ 142,023</u>

**RURAL WATER DISTRICT NO. 4  
PAWNEE COUNTY  
Pawnee, Oklahoma**

**NOTES TO THE BASIC FINANCIAL STATEMENTS  
June 30, 2012 and 2011**

**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

**C. Assets, Liabilities and Equity (Continued)**

**1. Deposits and Investments (Continued)**

*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 of credit risk: 100% in Money Market funds (\$142,023).

**2. Fair Value of Financial Instruments**

The District's financial instruments include cash and cash equivalents, accounts receivable, accounts payable and notes payable. The District's estimate of the fair value of all financial instruments does not differ materially from the aggregate carrying values of its financial instruments recorded in the accompanying statement of net assets. The carrying amount of these financial instruments approximates fair value because of the short maturity of these instruments.

**3. Estimates**

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Accordingly, actual results could differ from those estimates.

**4. Inventories**

Inventories consist primarily of water stored in lines for use in the distribution process. Inventory is expensed when purchased.

**5. Capital Assets**

Additions to the water storage delivery system and other equipment are recorded at cost or, if contributed property, at their estimated fair value at time of contribution. Repairs and maintenance are recorded as expenses; renewals and betterments are capitalized. The District maintains a capitalization threshold of \$500 and an estimated useful life in excess of two (2) years.

Depreciation has been calculated on each class of depreciable property using the straight-line method. Estimated useful lives are as follows:

Water system	40 years
Equipment	10 years
Office equipment	10 years

**6. Compensated Absences**

It is the District's policy to permit employees to accumulate earned but unused vacation time. Full-time employees are granted vacation and sick leave benefits in varying amounts to specified maximums depending on tenure. The District has not accrued compensated absences because the amount, if any, would not be material to the financial statements.

**RURAL WATER DISTRICT NO. 4  
PAWNEE COUNTY  
Pawnee, Oklahoma**

**NOTES TO THE BASIC FINANCIAL STATEMENTS  
June 30, 2012 and 2011**

**2. TEMPORARILY RESTRICTED ASSETS**

Under the terms of the various note indentures with Rural Development, the District is required to make monthly contributions into a reserve account until a minimum balance of \$23,796 has been reached. The funds are temporarily restricted and are to be used for repairing or replacing damaged assets caused by unforeseen catastrophes. With prior written approval from Rural Development, the reserve funds can also be used for making improvements to the water system or for debt service. After the payoff of the Rural Development note indenture, all money has been released from being temporarily restricted at the end of the year.

**3. LONG-TERM DEBT**

Long-term debt consists of one note with the United States Department of Agriculture, Rural Development (RD). The RD note was originally issued during November 1976. On September 14, 1984, the note was re-amortized to include the remaining unpaid principal and accrued interest. The total is now being amortized over the remaining life of the original note. The note is secured by the water works system including distribution lines, pump stations and reservoirs. These re-issued RD note is listed as follows:

Loan # 91-07 – Original amount of \$69,741, re-issued September 14, 1984, payable in monthly installments of \$365 for 33 years at 5% interest, maturing in January of 2016. The loan was paid off in the current year.

The following is a summary of long-term debt transactions during the year:

	Balance June 30, 2011	Additions	Reductions	Balance June 30, 2012
USDA Rural Dev. - 92-04	\$ 16,758	\$ -	\$ 16,758	\$ -
Total	\$ 16,758	\$ -	\$ 16,758	\$ -

**4. CAPITAL ASSETS**

The following is a summary of changes in property, plant and equipment.

	Balance June 30, 2011	Additions	Deletions	Balance June 30, 2012
Water system	\$ 766,606	\$ -	\$ -	\$ 766,606
Equipment	11,201	-	-	11,201
Office equipment	6,271	-	-	6,271
Total	784,078	-	-	784,078
Less accumulated depreciation	398,502	19,759	-	418,261
Net	\$ 385,576	\$ (19,759)	\$ -	\$ 365,817

**RURAL WATER DISTRICT NO. 4  
PAWNEE COUNTY  
Pawnee, Oklahoma**

**NOTES TO THE BASIC FINANCIAL STATEMENTS  
June 30, 2012 and 2011**

**4. CAPITAL ASSETS (Continued)**

	Balance June 30, 2010	Additions	Deletions	Balance June 30, 2011
Water system	\$ 766,606	\$ -	\$ -	\$ 766,606
Equipment	11,201	-	-	11,201
Office equipment	6,271	-	-	6,271
Total	<u>784,078</u>	<u>-</u>	<u>-</u>	<u>784,078</u>
Less accumulated depreciation	378,744	19,758	-	398,502
Net	<u>\$ 405,334</u>	<u>\$ (19,758)</u>	<u>\$ -</u>	<u>\$ 385,576</u>

**5. RISK MANAGEMENT**

Rural Water District No. 4 is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. The District continues to carry commercial insurance for these risks, including general and auto liability, property damage, and public officials liability. Settled claims resulting from these risks have not exceeded the commercial insurance coverage in any of the past three fiscal years.

**6. WATER PURCHASE COMMITMENT**

The governing board of Rural Water District No. 4, Pawnee County, Pawnee, Oklahoma, together with seven other cities and rural water districts located in Noble, Pawnee, and Payne Counties, Oklahoma, have jointly formed Lone Chimney Water Association. The purpose of the Association is to provide a water system for the benefit of its members and other users. The District has entered into various loan agreements with the United States Department of Agriculture, Rural Development and the Oklahoma Water Resources board to provide financing for the facility. Under the terms of the agreement regarding Rural Water District No. 4, each member has contracted to purchase a minimum amount of water from the Association during the 40-year term of the notes. In addition, each individual member is proportionately liable for any debts that exceed the assets of the Association to the extent of one and one-half times the percentage of ownership interest held by the entity pursuant to the agreement. The District is contingently liable for 12.4% of the obligations of the Association, which total approximately \$2,115,215 to Rural Development and \$573,851 to ORWB at year-end. The District's contingent share of Lone Chimney Water Association's debt is \$333,444.

At June 30, 2012, Rural Water District No. 4 was obligated to purchase a minimum of 20.4 million gallons of water annually, currently at a cost of \$58,080. The rates charged for the water can be adjusted every three years as necessary to provide sufficient revenues for the Association.

**RURAL WATER DISTRICT NO. 4  
PAWNEE COUNTY  
Pawnee, Oklahoma**

**NOTES TO THE BASIC FINANCIAL STATEMENTS  
June 30, 2012 and 2011**

**6. WATER PURCHASE COMMITMENT (Continued)**

Future purchase commitments at current rates are as follows:

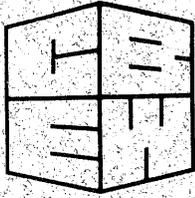
<u>June 30,</u>	<u>Amounts Due</u>
2013	\$ 58,080
2014	58,080
2015	58,080
2016	58,080
2017	58,080
2018-2022	290,400
2023-2027	290,400
2028-2032	290,400
Total	<u>\$ 1,161,600</u>

**7. SUBSEQUENT EVENTS**

Management has evaluated subsequent events through July 19, 2012, which is the date the financial statements were available to be issued and have determined that no additional information needs to be added to the financial statements.

**RURAL WATER DISTRICT NO. 4  
PAWNEE COUNTY  
Pawnee, Oklahoma**

**REPORT REQUIRED BY *GOVERNMENT AUDITING STANDARDS*  
June 30, 2012**



**CBEW**  
**Professional**  
**Group, LLP**

Certified Public Accountants

DON K. ETHRIDGE, CPA  
WALTER H. WEBB, CPA  
JANE FRAZIER, CPA  
CHARLES E. CROOKS, CPA  
TRISHA J. RIEMAN, CPA

206 N. HARRISON • P.O. BOX 790 • GUSHING, OKLAHOMA 74023 • 918-225-4216 • FAX 918-225-4315

**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**

July 19, 2012

Board of Directors  
Rural Water District No. 4  
Pawnee County  
Pawnee, Oklahoma

We have audited the basic financial statements of the Rural Water District No. 4, Pawnee County, Pawnee, Oklahoma (the District), as of and for the year ended June 30, 2012, and have issued our report thereon dated July 19, 2012. 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. The District did not present the Management's Discussion and Analysis required by the Governmental Accounting Standards Board.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the District's internal control over financial reporting as a basis for designing our audit procedures for the purpose of expressing our opinion on the basic financial statements, but not for the purpose of expressing an opinion on the effectiveness of the District's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the District'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 a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above. However, we identified certain deficiencies in internal control over financial reporting, described in the accompanying schedule of findings and questioned costs that we consider to be significant deficiencies in internal control over financial reporting. The finding reference numbers are 12-1 and 12-2. 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.

Rural Water District No. 4  
July 19, 2012

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the District'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*.

The District's response to the findings identified in our audit is described in the accompanying schedule of findings and responses. We did not audit the District's response and, according, we express no opinion on it.

This report is intended solely for the information and use of management, all applicable federal and state agencies, and is not intended to be and should not be used by anyone other than these specified parties.

*CBEW Professional Group, LLP*

CBEW Professional Group, LLP  
Certified Public Accountants

**RURAL WATER DISTRICT NO. 4  
PAWNEE COUNTY  
Pawnee, Oklahoma**

**SCHEDULE OF FINDINGS AND RESPONSES  
For the Year Ended June 30, 2012**

12-1. Internal Control – Segregation of Duties

Criteria: The segregation of duties and responsibilities between different individuals for custody of assets, recordkeeping for those assets and reconciliation of those asset accounts is an important control activity needed to adequately protect the district's assets and ensure accurate financial reporting.

Condition: Presently the same individual that receives utility service related cash payments is also responsible for service billing and adjustment, also balances the daily cash drawer, posts payments to subsidiary accounts receivable ledger and reconciles the monthly bank statements. In addition, only limited oversight is provided over this individual in the conduct of their daily functions. This finding was also noted in 2011.

Cause: The district's limited size and staffing resources have made it difficult for management to provide sufficient staffing to fully segregate incompatible duties in a cost-effective manner.

Effect or Potential Effect: Without sufficient segregation of duties, the risk significantly increases that errors and fraud related to utility billing and collection activities, including misappropriation of assets, could occur and not be detected within a timely basis.

Recommendation: We recommend that management and the board should consider a formal evaluation of their risks associated with this lack of duties segregation over utility cash and receivables. In response to the identified risks, consideration should be given to identifying and implementing controls that could help mitigate the risks associated with lack of segregation of duties, such as providing increased management oversight and an independent reconciliation of accounts. For example, the entity might consider soliciting the assistance of independent volunteer labor to perform certain functions including performing compensating procedures where applicable.

Responsible Official's Response: The district concurs with the recommendation, although, the cost to correct this condition might exceed the benefit, the district has made certain changes in procedures that will improve the overall lack of segregation of duties and has implemented compensating procedures as appropriate.

12-2. Internal Control – Financial Statements

Criteria: The District's management is responsible for internal controls over financial reporting. This includes controls over the fair and complete presentation of the District's annual financial statements in accordance with GAAP. The preparation of financial statements in accordance with GAAP requires internal controls over both (1) recording, processing and summarizing accounting data (i.e., maintaining internal books and records), and (2) reporting financial statements, including the related footnotes (i.e., external financial reporting). Professional standards clearly indicate that the external financial statement auditor cannot perform any part of management's control activities or be a component of the internal controls over financial reporting.

Condition: As is the case with many smaller and medium-sized entities, the District has relied on its independent external auditors to provide the needed expertise to assist in the preparation of the financial statements and footnotes as part of its controls over the external financial reporting process. Accordingly the District's ability to prepare financial statements in accordance with generally accepted accounting principles (GAAP) is based, in part, on its external auditors, who cannot by definition be considered a part of the District's internal controls. However, as required by professional standards the District has provided safeguards by designating a management level individual with suitable skill, knowledge and/or experience to oversee the services performed by our engagement, make all management decisions (e.g., determining or approving account classifications, adjusting journal entries, etc.) evaluate and monitor the performance and adequacy of the services, and take responsibility for the books, records and related financial statements. This finding was also noted in 2010.

**RURAL WATER DISTRICT NO. 4  
PAWNEE COUNTY  
Pawnee, Oklahoma**

**SCHEDULE OF FINDINGS AND RESPONSES  
For the Year Ended June 30, 2012**

Cause: Management has elected to use outside assistance from the external auditors to assist in meeting its responsibilities relative to preparing its annual financial statements. Although the District's management may lack certain expertise relative to preparing GAAP financial statements, professional standards do not require that the management or the individual possess the expertise to perform or re-perform all such services. The auditor has explained all proposed audit adjustments and their effect on the financial statements and the related note disclosures to management who has affirmed their understanding and agreement as required by professional standards.

Effect or Potential Effect: Although management has reviewed the financial statements drafted by the auditor and accepted full responsibility for them, the auditor could be placed in a questionable position regarding auditor independence as a result of potentially performing part of management's functions if management or its representative is unable to understand the nature of the services, evaluate its adequacy and accept responsibility for its results.

Recommendation: We recommend that the District consider designing and implementing further internal controls over financial reporting by obtaining additional expertise to process and summarize accounting data and prepare financial statements in accordance with generally accepted accounting principles without reliance on the external financial statement auditor. This could be achieved through employment of qualified accounting staff or the outsourcing of these control activities to a qualified accounting firm other than the external auditor.

Responsible Official's Response: The District concurs with the recommendation, and will strive to process and summarize accounting data and further understand the presentation and disclosure requirements of the financial statements.