INDEPENDENT AUDITORS’ REPORT

To The Honorable Members of the Board of Directors
Rural Sewer District No. 1, Rogers County, Oklahoma
Verdigris, Oklahoma

I have audited the accompanying financial statements of the business-type activities of Rural Sewer District No. 1, Rogers County, Oklahoma, Verdigris, Oklahoma as of and for the year ended June 30, 2013, and the related notes to the financial statements, which collectively comprise Rural Sewer District No. 1's basic financial statements.

Management’s Responsibility for the Financial Statements

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

Auditor’s Responsibility

My responsibility is to express opinions on these financial statements based on our audit. I conducted my audit in accordance with the auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

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

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

Opinion

In my opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the business-type activities of Rural Sewer District No. 1 as of June 30, 2013, and the respective changes in financial position and cash flows thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.
Other Matters

Rural Sewer District No. 1 has not presented Management’s Discussion and Analysis that the Governmental Accounting Standards Board has determined is necessary to supplement, although not required to be part of, the basic financial statement.

In accordance with *Government Auditing Standards*, I have also issued my report dated September 19, 2013, on my consideration of Rural Sewer District No. 1's internal control over financial reporting and 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 accordance with *Government Auditing Standards* and should be considered in assessing the results of my audit.

Ralph Osborn
Certified Public Accountant
Bristow, Oklahoma
September 19, 2013
### ASSETS

Current assets:
- Cash and cash equivalents $146,112  
- Investments 2,178  
- Prepaid Expenses 6,690  
- Accounts Receivable 275  

Restricted assets:
- Investments Rural Development 48,408  
- Held in trust Revenue Bonds 161,453  

Total current assets 365,116

Non-current assets:
- Deferred debt expense, net 17,414  

Capital assets:
- Land 46,325  
- Capital assets, net of accumulated depreciation 1,622,580  

Total non-current assets 1,686,319

Total assets 2,051,435

### LIABILITIES

Current liabilities:
- Accounts payable 8,547  
- Accrued interest 8,422  
- Notes payable, current 70,225  

Total current liabilities 87,194

Non-current liabilities:
- Notes payable, non-current 1,208,368  

Total non-current liabilities 1,208,368

Total liabilities 1,295,562

### NET ASSETS

- Nonspendable 397,722  
- Restricted for debt service 209,861  
- Unassigned 148,290  

Net assets of business-type activities $755,873

See accompanying notes to financial statements.
RURAL SEWER DISTRICT NO. 1
ROGERS COUNTY, OKLAHOMA
VERDIGRIS, OKLAHOMA
STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS
FOR THE YEAR ENDED JUNE 30, 2013

OPERATING REVENUES
Charges for services:
  Wastewater charges $ 431,585
  Membership benefit units 31,350
  Developer’s agreement fees 26,400
  Rent 7,150

  Total operating revenues 496,485

OPERATING EXPENSES
  Contract management fees 86,700
  Contract operator fees 36,000
  Vehicle expense 3,007
  Repair and maintenance 55,771
  Professional fees 35,978
  Insurance 7,417
  License and permits 2,443
  Office 12,663
  Miscellaneous 113
  Utilities and telephone 44,887
  Depreciation 126,776

  Total operating expenses 411,755

  Operating income (loss) 84,730

NON-OPERATING REVENUE (EXPENSES)
  Amortization of debt issue cost (1,700)
  Investment earnings 4,319
  Interest on notes payable and fees (65,572)

  Total non-operating revenue (expenses) (62,953)

Change in net assets 21,777

Total net assets, beginning 734,096

Total net assets, ending $ 755,873

See accompanying notes to financial statements.
Cash flows from operating activities
  Cash received from customers $495,738
  Cash payments to suppliers for goods and services (283,234)

Net cash provided (used) by operating activities 212,504

Cash flows from capital and related financing activities
  Interest paid on notes payable and fiscal fees (65,572)
  Principal paid on notes payable (70,242)

Net cash used for capital and related financing activities (135,814)

Cash flows from investing activities
  Transfer to investments (60)
  Investment earnings 4,319

Net cash provided by investing activities 4,259

Net decrease in cash and cash equivalents 80,949

Cash and cash equivalents, beginning 226,616

Cash and cash equivalents, ending $307,565

Reconciliation of operating income (loss) to net cash provided by (used) by operating activities
  Operating income (loss) $84,730
  Adjustments to reconcile operating income to net cash used by operating activities:
    Depreciation 126,776
  Changes in assets and liabilities:
    Increase in accrued receivables (747)
    Increase in prepaid expense (420)
    Increase in accounts payable 2,165

Net cash provided by operating activities $212,504

See accompanying notes to financial statements.
NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Rural Sewer District No. 1 (the "District") was created by the Board of County Commissioners of Rogers County, Oklahoma, Oklahoma under the provisions of the Rural Water Districts Act (Title 82, Oklahoma Statutes 1961, Sections 1301 to 1321). The District is managed by the five member Board of Directors. Members of the board are elected by the membership of the District at annual meetings. Membership in the District is attained by purchasing membership benefit units and receiving services from the District. The activities of the District constitute the entire reporting entity. There are no other component or oversight units.

Measurement Focus, Basis of Accounting and Financial Statement Presentation

The financial statements of the District are prepared in accordance with generally accepted accounting principles (GAAP). The District’s reporting entity applies all relevant Governmental Accounting Standards Board (GASB) pronouncements and applicable Financial Accounting Standards (FASB) pronouncements and Accounting Principles Board (APB) opinions issued on or before November 30, 1989, unless they conflict with GASB pronouncements. The District’s reporting entity does not apply FASB pronouncements or APB opinions issued after November 30, 1989.

The financial statements report using the economic resources measurement focus and the accrual basis of accounting. Reimbursements are reported as reductions to expenses. Revenues are recorded when earned and expenses recorded when a liability is incurred, regardless of the timing of related cash flows.

Operating income reported in financial statements include revenues and expenses related to the primary, continuing operations of the District. Principal operating revenues 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.

FUND TYPES AND MAJOR FUNDS

The District is reported as a single enterprise fund.

Investments

The District follows Governmental Accounting Standards Board (GASB) Statement No. 31, "Accounting and Financial Reporting for Certain Investments and for External Investment Pools," which requires marketable securities to be carried at fair value. The District considers highly liquid investments with a maturity of three months or less when purchased to be cash equivalents. The District’s investments consist of a certificate of deposit.
Inventories and Prepaids

Inventories consist of expendable supplies held for consumption stated on a first-in, first-out basis. They are reported at cost which is recorded as an expenditure at the time individual inventory items are used. The District has not maintained inventory records, however, the value of inventory on hand at June 30, 2013 is not believed to be material.

Prepaids record payments to vendors that benefit future reporting periods and are also reported on the consumption basis.

Capital Assets, Depreciation, and Amortization

The District’s property, plant, and equipment, with useful lives of more than one year are stated at historical cost and comprehensively reported in the financial statements. Donated assets are stated at fair value on the date donated. The District generally capitalizes assets with cost of $2,500 or more as purchase and construction outlays occur. The cost of normal maintenance and repairs that do not add to the assets value or materially extend useful lives are not capitalized. Capital assets are depreciated using the straight-line method. When capital assets are disposed, the cost and applicable accumulated depreciation are moved from the respective accounts, and the resulting gain or loss is recorded in operations.

Estimated useful lives, in years, for depreciable assets are as follow:

<table>
<thead>
<tr>
<th>Asset Type</th>
<th>Useful Life (Years)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Buildings</td>
<td>5-60</td>
</tr>
<tr>
<td>Improvements, other than buildings</td>
<td>2-50</td>
</tr>
<tr>
<td>Mobile equipment</td>
<td>3-40</td>
</tr>
<tr>
<td>Furniture, machinery, and equipment</td>
<td>3-30</td>
</tr>
<tr>
<td>Utility system</td>
<td>5-50</td>
</tr>
</tbody>
</table>

Reserves and Designations

Reserves represent those portions of net assets not available for expenditure or legally segregated for a specific future use. Designated net assets represent tentative plans for future use of financial resources.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.
RURAL SEWER DISTRICT NO. 1
ROGERS COUNTY, OKLAHOMA
VERDIGRIS, OKLAHOMA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2013

NOTE B - DEPOSITS WITH FINANCIAL INSTITUTIONS AND INVESTMENTS

Custodial Credit Risk
Custodial credit risk is the risk that in the event of failure of counterparty, the District will not be able to recover the value of its deposits or investments. Deposits are exposed to custodial credit risk if they are uninsured and uncollateralized. Investment securities are exposed to custodial credit risk if they are uninsured, are not registered in the name of the District, and are held by counterparty or the counterparty’s trust department but not in the name of the District. The District’s policy requires that all deposits and investments in excess of amounts covered by federal deposit insurance be fully collateralized by the entity holding the deposits or investments. As of June 30, 2013, all of the District's deposits and investments were either covered by federal deposit insurance or were fully collateralized.

Deposits
The District had deposits at financial institutions with a carrying amount of approximately $358,151 at June 30, 2013. The bank balance of the deposits at June 30, 2013 was approximately $364,026.

Credit Risk
Fixed-income securities are subject to credit risk. However, the District did not have fixed income securities at June 30, 2013.

Interest Rate Risk
Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. The Board of Directors monitor’s the investment performance on an ongoing basis to limit the District’s interest rate risk. As of June 30, 2013, the District’s deposits consisted of demand deposits and certificates of deposit with a maturity of 12 months or less.

Note C - ACCOUNTS RECEIVABLE
The District records the total due on accounts owed for services unpaid at June 30. Any uncollectible amounts are written-off as they become uncollectible. The District believes any amount of uncollected receivables will not be material.

Note D - RESTRICTED ASSETS
The District has restricted certain assets held in accounts of a trustee bank obtained as a result of the issue of its revenue bonds. The accounts are to be used for a debt reserve and a sinking fund for use in paying debt principal and interest. Amounts are as follows:

<table>
<thead>
<tr>
<th>Investments Rural Development</th>
<th>48,408</th>
</tr>
</thead>
<tbody>
<tr>
<td>Held in trust Revenue Bonds</td>
<td>161,453</td>
</tr>
<tr>
<td>Total</td>
<td>$ 209,861</td>
</tr>
</tbody>
</table>

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Note E - PREPAID EXPENSE

The District records insurance premiums paid for future periods as prepaid expense.

Note F - CAPITAL ASSETS

The following table provides a summary of changes in capital assets:

<table>
<thead>
<tr>
<th>CAPITAL ASSETS, DEPRECIATED</th>
<th>Furniture, Improvements Buildings</th>
<th>Other Than Buildings $ 2,647,853</th>
<th>Machinery, And Equipment $ 250,381</th>
<th>Totals $ 3,224,757</th>
<th>Land $ 46,325</th>
</tr>
</thead>
<tbody>
<tr>
<td>Balance, June 30, 2012</td>
<td>$ 326,523</td>
<td>$ 2,647,853</td>
<td>$ 250,381</td>
<td>$ 3,224,757</td>
<td>$ 46,325</td>
</tr>
<tr>
<td>Increases</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Decreases</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Balance, June 30, 2013</td>
<td>326,523</td>
<td>2,647,853</td>
<td>250,381</td>
<td>3,224,757</td>
<td></td>
</tr>
<tr>
<td>Accumulated Depreciation</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Balance, June 30, 2012</td>
<td>5,126</td>
<td>1,322,028</td>
<td>148,247</td>
<td>1,475,401</td>
<td></td>
</tr>
<tr>
<td>Increase</td>
<td>8,395</td>
<td>101,711</td>
<td>16,670</td>
<td>126,776</td>
<td></td>
</tr>
<tr>
<td>Decreases</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Balance, June 30, 2013</td>
<td>13,521</td>
<td>1,423,739</td>
<td>164,917</td>
<td>1,602,177</td>
<td></td>
</tr>
<tr>
<td>Capital Assets, Net</td>
<td>$ 313,002</td>
<td>$ 1,224,114</td>
<td>$ 85,464</td>
<td>$ 1,622,580</td>
<td>$ 46,325</td>
</tr>
</tbody>
</table>

Note G - DEFERRED DEBT EXPENSE

The Verdigris Public Works Authority (the Authority), Verdigris, Oklahoma issued its Capital Improvement Revenue Bonds, Series 2003, dated October 1, 2003, in the amount of $490,000. The purpose of the bond issue was to provide funds for constructing office facilities to be leased to the District and to provide improvements to the District’s sewer system. The District signed a guaranty agreement for the bonds on September 1, 2003. Payments of debt service requirements are made directly from the District to the trustee bank. The District, based on the use of the funds and the guarantee, has reported the bond issue as a note payable.

The bond issue had costs relating to the issuance of the bonds totaling $19,288 and a bond discount of $14,700. These costs are being amortized over the 20 year life of the bond issue. The District recorded $1,700 amortization cost during the current period. Net deferred debt expense at June 30, 2013 was $17,414.
Note H - NOTES PAYABLE

The District has incurred indebtedness for the expansion of system facilities. The following is a summary of note payable transactions for the year ended June 30, 2013.

<table>
<thead>
<tr>
<th>Payable at</th>
<th>Balance at</th>
</tr>
</thead>
<tbody>
<tr>
<td>July 1, 2012</td>
<td>Addition</td>
</tr>
<tr>
<td>Rural Development</td>
<td>$614,617</td>
</tr>
<tr>
<td>Water Resources Board</td>
<td>354,218</td>
</tr>
<tr>
<td>Revenue Bonds</td>
<td>380,000</td>
</tr>
<tr>
<td>TOTAL</td>
<td>$1,348,835</td>
</tr>
</tbody>
</table>

A brief description of the outstanding notes payable at June 30, 2013 is set forth below:

**Outstanding**
- Rural Development loan number 9201, dated February 9, 1994, original loan amount of $781,700, interest rate of 5.375%, term of 40 years, monthly installments of $4,034 until February 2034: $598,862
- Oklahoma Water Resources Board loan dated June 13, 2001, original loan amount of $630,000, interest rate 3.2%, principal payments vary, matures in September 2021: 319,731
- Revenue bonds through The Verdigris Public Works Authority dated October 1, 2003 in the amount of $490,000, interest rate 4% to 6.25%, principal payable annually until October 2023: 360,000

Total: $1,278,593

Less current portion: 70,225

Net non-current portion: $1,208,368

The annual debt service requirement including principal and interest, is as follows:

<table>
<thead>
<tr>
<th>Year Ended</th>
<th>Principal</th>
<th>Interest</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>June 30</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2014</td>
<td>$70,225</td>
<td>$63,061</td>
<td>$133,086</td>
</tr>
<tr>
<td>2015</td>
<td>72,239</td>
<td>60,129</td>
<td>132,368</td>
</tr>
<tr>
<td>2016</td>
<td>74,318</td>
<td>57,135</td>
<td>131,453</td>
</tr>
<tr>
<td>2017</td>
<td>81,529</td>
<td>54,020</td>
<td>135,549</td>
</tr>
<tr>
<td>2018</td>
<td>83,813</td>
<td>50,562</td>
<td>134,375</td>
</tr>
<tr>
<td>2019-2023</td>
<td>421,317</td>
<td>203,403</td>
<td>624,720</td>
</tr>
<tr>
<td>2024-2028</td>
<td>248,339</td>
<td>92,763</td>
<td>341,102</td>
</tr>
<tr>
<td>2029-2033</td>
<td>207,035</td>
<td>35,005</td>
<td>242,040</td>
</tr>
<tr>
<td>2034</td>
<td>19,778</td>
<td>392</td>
<td>20,170</td>
</tr>
<tr>
<td>Total</td>
<td>$1,278,593</td>
<td>$616,470</td>
<td>$1,894,863</td>
</tr>
</tbody>
</table>

The District has a loan reserve for the Rural Development loan in the amount of $48,408. This amount equals the annual payment required on the note.
Note I - DEBT SERVICE COVERAGE

The Oklahoma Water Resource Board loan requires the District maintain a schedule of charges, fees, and rates sufficient to produce annual net revenues not less than 1.25 times annual debt service requirements after payment of all operating and maintenance expense.

Ratio of net revenue to debt service follows:

<table>
<thead>
<tr>
<th>Operating Revenue</th>
<th>$496,485</th>
</tr>
</thead>
<tbody>
<tr>
<td>Operating Expenses</td>
<td>(284,979)</td>
</tr>
<tr>
<td>Revenue Available For Debt Service</td>
<td>$211,506</td>
</tr>
<tr>
<td>Annual Debt Service</td>
<td>$135,814</td>
</tr>
<tr>
<td>Coverage Ratio</td>
<td>1.55 to 1</td>
</tr>
</tbody>
</table>

Note J - EMPLOYEE BENEFITS

The District operates through contracted services. It does not have employees.

Note K - RISK MANAGEMENT

The District is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; and natural disasters. The District carries commercial insurance for risk of loss. Settled claims resulting from these risks have not exceeded commercial insurance coverage in any of the past three fiscal years.

Note L - LITIGATION

The District is party to various legal proceedings which normally occur in governmental operations. These legal proceedings are not likely to have a material adverse impact on the District. The District retains legal council for legal proceedings. The District may also be represented by attorneys retained by its insurance carrier.

Note M - FEDERAL AND STATE GRANTS

In the normal course of operations, the District receives grant funds from various federal and state agencies. The grant programs are subject to audit by agents of the granting authorities the purpose of which is to ensure compliance with conditions precedent to the granting of the funds. Any liability for reimbursement which may arise as the result of these audits is not believed to be material.

Note N - SUBSEQUENT EVENTS

Management has evaluated subsequent events through September 19, 2013, the date on which the financial statements were available to be issued. The Authority does not believe there are any events requiring disclosure.
To the Board of Directors
Rural Sewer District No. 1
Verdigris, Oklahoma

I have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards issued by the Comptroller General of the United States, the financial statements of the business-type activities of Rural Sewer District No. 1, Rogers County, Oklahoma, Verdigris, Oklahoma, as of and for the year ended June 30, 2013, and the related notes to the financial statements, which collectively comprise Rural Sewer District No. 1’s basic financial statements and have issued my report thereon dated September 19, 2013 which did not include Management’s Discussion and Analysis.

Internal Control Over Financial Reporting

In planning and performing my audit, I considered Rural Sewer District No. 1's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing my opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of Creek County Educational Facilities Authority’s internal control. Accordingly, I do not express an opinion of the effectiveness of Rural Sewer District No. 1's internal control.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A material weakness is a deficiency, or 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. 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.

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 that might be material weaknesses or, significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.
Compliance and Other Matters

As part of obtaining reasonable assurance about whether Rural Sewer District No. 1, Rogers County, Oklahoma, Verdigris, Oklahoma’s financial statements are free of material misstatement, I 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 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.

Purpose of the Report

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

Sincerely,

Ralph Osborn
Certified Public Accountant
Bristow, Oklahoma
September 19, 2013