

AUDIT REPORT
CHEROKEE COUNTY RURAL WATER DISTRICT NO. 2
FOR THE YEAR ENDED DECEMBER 31, 2018

AUDITED BY
ALAN CHAPMAN
CERTIFIED PUBLIC ACCOUNTANT
104 S. Muskogee Ave.
TAHLEQUAH, OKLAHOMA

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INDEPENDENT AUDITOR'S REPORT

Board of Directors

Cherokee County Rural Water District No. 2

Report on the Financial Statements

I have audited the accompanying financial statements of the business-type activities of the Cherokee County Rural Water District No.2 (the District), as of and for the year ended December 31, 2018, which collectively comprise the District's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements. Management is also responsible for 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 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. Those standards require that I 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 judgment, 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 District'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.

I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my audit opinion.

Opinions

In my opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the business-type activities of Cherokee County Rural Water District No. 2. as of December 31, 2018, 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

The District has omitted the Management's Discussion and Analysis that 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 who consider it to be an essential part of financial reporting for placing the basic financial statements in the appropriate operational, economic, or historical context. Our opinion on the basic financial statements is not affected by this missing information.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, I have also issued my report dated May 13, 2019, on my consideration of Cherokee County Rural Water District No. 2's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of my testing of internal control over financial reporting or on compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering Cherokee County Rural Water District No. 2's internal control over financial reporting and compliance.

May 13, 2019

A handwritten signature in cursive script that reads "ALAN CHAPMAN".

Alan Chapman, CPA

CHEROKEE COUNTY RURAL WATER DISTRICT NO. 2
STATEMENT OF NET POSITION
DECEMBER 31, 2018

ASSETS

CURRENT ASSETS

CASH IN BANK	\$ 128,694
CERTIFICATE OF DEPOSIT	115,781
ACCOUNTS RECEIVABLE	34,032
PREPAID INSURANCE	<u>10,596</u>

TOTAL CURRENT ASSETS 289,103

NONCURRENT ASSETS

RESTRICTED CASH DEBT SERVICE FUND	53,513
CAPITAL ASSETS, NET	<u>1,980,285</u>

TOTAL NONCURRENT ASSETS 2,033,798

TOTAL ASSETS \$ 2,322,901

LIABILITIES

ACCOUNTS PAYABLE	\$ 13,704
NOTES PAYABLE - CURRENT PORTION	35,057
NOTES PAYABLE - LONG TERM PORTION	522,342
ACCRUED INTEREST	2,734
ACCRUED BENEFITS VAC/SICK	<u>17,343</u>

TOTAL LIABILITIES 591,179

NET POSITION

INVESTED IN CAPITAL ASSETS, NET OF RELATED DEBT	1,422,886
RESTRICTED FOR DEBT RESERVE	53,513
UNRESTRICTED	<u>255,323</u>

TOTAL NET POSITION 1,731,722

TOTAL LIABILITIES AND NET POSITION \$ 2,322,901

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

CHEROKEE COUNTY RURAL WATER DISTRICT NO. 2
STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET POSITION
FOR THE YEAR ENDED DECEMBER 31, 2018

OPERATING REVENUES

WATER SALES AND OTHER SALES \$ 445,293

OPERATING EXPENSES

SALARIES	128,929
EMPLOYEE BENEFITS	1,659
ACCOUNTING & BILLING	18,509
PROFESSIONAL FEES	4,398
BAD DEBTS	10,932
BANK CHARGES	1,503
POSTAGE/ SHIPPING	3,197
INSURANCE	36,892
TAXES	10,490
RETIREMENT	6,295
OFFICE EXPENSE	3,774
AUTOMOBILE EXPENSE	17,808
DUES & SUB & FEE	1,623
TELEPHONE EXPENSE	7,316
WATER PURCHASED AND STORAGE RIGHTS AND FEES	80,176
DEQ REGULATORY FEE AND WATER TESTING FEES	13,637
EMPLOYEE TRAINING, LICENSES PERMITS ETC	1,896
REPAIRS & MAINTENANCE	9,679
FIELD SUPPLIES	48,669
CHEMICALS	24,211
EQUIPMENT RENTAL	252
UTILITIES	26,291
DEPRECIATION EXPENSE	108,980
OTHER MISCELLANEOUS	<u>850</u>
TOTAL EXPENSES FROM OPERATIONS	<u>567,966</u>

OPERATING INCOME (LOSS) (122,672)

NON OPERATING REVENUE (EXPENSE)

INTEREST INCOME	\$ 5,516
MISCELLANEOUS INCOME	13,903
MEMBERSHIP/CONNECT	21,434
CHEROKEE NATION DONATION	35,087
EXPENSE- INTEREST	<u>(17,929)</u>

TOTAL NON-OPERATING REVENUE (EXPENSE) 58,011

CHANGE IN NET POSITION (64,661)

NET POSITION, BEGINNING OF YEAR 1,796,383

NET POSITION, END OF YEAR **\$ 1,731,722**

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

CHEROKEE COUNTY RURAL WATER DISTRICT NO. 2
STATEMENT OF CASH FLOWS FOR THE YEAR ENDED
DECEMBER 31, 2018

CASH FLOW FROM OPERATING ACTIVITIES

RECEIPTS FROM CUSTOMERS	\$ 447,490
PAYMENTS TO VENDORS	(688,720)
NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES	<u>(241,230)</u>

CASH FLOWS FROM INVESTING ACTIVITIES

INTEREST REVENUE	5,516
CAPITAL ASSETS PURCHASED	(179,652)
CHEROKEE NATION DONATION	35,087
MISCELLANEOUS INCOME	13,903
MEMBERSHIP FEES	21,434
NET CASH PROVIDED BY (USED IN) INVESTING ACTIVITIES	<u>(103,712)</u>

CASH FLOWS FROM FINANCING ACTIVITIES

INTEREST PAYMENTS ON NOTES	(17,929)
PRINCIPAL PAYMENTS ON NOTES	(30,664)
NET CASH PROVIDED BY (USED IN) FINANCING ACTIVITIES	<u>(48,593)</u>

NET INCREASE (DECREASE) IN CASH	<u>(393,535)</u>
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CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	<u>691,523</u>
CASH AND CASH EQUIVALENTS AT END OF YEAR	<u>\$ 297,988</u>

RECONCILIATION OF OPERATING INCOME (LOSS) TO NET CASH PROVIDED BY OPERATING ACTIVITIES:

OPERATING INCOME (LOSS)	\$ (122,672)
DEPRECIATION	108,980
(INCREASE) DECREASE IN ACCOUNTS & GRANTS RECEIVABLE	2,197
(INCREASE) DECREASE IN PREPAID EXPENSES	(1,262)
INCREASE (DECREASE) IN PAYABLES	<u>(228,473)</u>
NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES	<u>\$ (241,230)</u>

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

NOTES TO THE FINANCIAL STATEMENTS

CHEROKEE COUNTY RURAL WATER DISTRICT NO. 2
P.O. BOX 190
HULBERT, OK 74441

NOTES TO THE FINANCIAL STATEMENTS
DECEMBER 31, 2018

I. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Cherokee County Rural Water District No. 2 was incorporated under the Rural Water District Act of Oklahoma, for the purpose of acquiring water rights, and to build and acquire pipelines and other facilities and to operate the same for the purpose for furnishing water to serve the need of owners and occupants of land located within the district. The District is exempt from federal and state income tax.

The membership consists of approximately 630 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, and following, the Board of Directors meet and elect a chairman, Vice-chairman, and secretary-treasurer.

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

A. Reporting Entity

The District complies with GASB Statement No 14, "The Financial Reporting Entity." This statement establishes standards for defining and reporting on the financial reporting entity. It defines component units as legally separate organizations for which the elected officials of the primary government are financially accountable and together organizations for which the nature and significance of their relationship with primary government are such that exclusion would cause the reporting entity's financial statements to be misleading or incomplete.

The District considered all potential component units in determining what organizations should be included in the financial statements. Based on these criteria, there are no component units to include in the District's financial statements.

B. Measurement Focus and Basis of Accounting and Basis of Presentation- Fund Accounting

The District's fund is enterprise fund. Enterprise funds are proprietary funds used to account for business-like activities provided to the general public. These activities are finance primarily by user charges and the measurements of financial activity focuses on net income measurement similar to the private sector.

**CHEROKEE COUNTY RURAL WATER DISTRICT NO. 2
P.O. BOX 190
HULBERT, OK 74441**

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

B. Measurement Focus and Basis of Accounting and Basis of Presentation- Fund Accounting (Continued)

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 statement of activities presents increases (e.g. revenues) and decreases (e.g. expenses) in net total assets. Depreciation expense is provide 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 recoded at the time liabilities are incurred. In compliance with the Governmental Accounting Standards Board (GASB) Statement No. 34 "Basic Financial Statement- and Management's Discussion and Analysis-for State and Local Governments which requires the classification of net assets into three components- invested in capital assets, net of related debt, restricted; and unrestricted.

C. Assets, Liabilities, and Net Assets

1. Deposits and investments

Oklahoma statutes authorize the District to invest in certificates of deposit, repurchase agreements, passbooks, banker's 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 investment is expressly prohibited by law.

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

CHEROKEE COUNTY RURAL WATER DISTRICT NO. 2
P.O. BOX 190
HULBERT, OK 74441

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

C. Assets, Liabilities, and Net Assets (Continued)

Custodial Credit Risk

At December, 31, 2018 the District held deposits of approximately \$297,988 at financial institutions. The District's cash deposits, including interest-bearing certificates of deposit, are not 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

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 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 saving 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 agreement with certain limitations.
- d. County, municipal or school district tax supported debt obligations, bond or revenue anticipation notes, money judgment or bond or revenue anticipation notes of public trusts whose beneficiary is 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.

CHEROKEE COUNTY RURAL WATER DISTRICT NO. 2
P.O. BOX 190
HULBERT, OK 74441

1. SUMMARY OF SIGNIFICAN ACCOUNTING POLICIES (Continued)

C. Assets, Liabilities, and Net Assets (Continued)

f. Money market funds regulated by the SEC and in which investments consist of the investments mentioned in the previous paragraphs (a-f.).

The investments held at December 31, 2018 are as follows:

Type	Weighted Average Maturity (Months)	Credit Rating	Market Value	Cost
Investments Cert. Cert. of Deposit	6	N/A	<u>\$ 115,781</u>	<u>\$ 115,781</u>
Total Investments			<u>\$ 115,781</u>	<u>\$ 115,781</u>

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 Certificates of Deposit (\$ 115,781).

2. Fair Value of Financial Instruments

The District's financial statements include cash and investments. The District's estimates of fair values of its financial instruments recoded in the accompanying balance sheet. the carrying amount of these financial instruments approximates fair value because of the short maturity of these instrument.

3. Estimates

The Preparation of financial statements in conformity with U.S. 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 statement and the reported amounts of revenues and expense during the reporting period. Accordingly, actual results could differ from those estimates.

CHEROKEE COUNTY RURAL WATER DISTRICT NO. 2
P.O. BOX 190
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1. SUMMARY OF SIGNIFICAN ACCOUNTING POLICIES (Continued)

C. Assets, Liabilities, and Net Assets (Continued)

4. Inventory

The District does not maintain an inventory of materials and supplies. These items are purchased when needed and expensed in that period.

5. Accounts Receivable

Accounts Receivable consist primarily of charges for water sales. Management has not establish a provision for uncollectable accounts. Such amount are written off the month in which management determines they are uncollectible.

6. Restricted Assets

The terms of the loan agreement with the Rural Development require that the Company maintain funds for the use of servicing debt in the amount of 125% of the total annual payment. The balance in the restricted cash account is sufficient to fulfill this requirement.

7. Capital Assets

The water storage and delivery system and furniture and equipment are recorded at cost. Donated Capital assets are Reported and estimated fair market value at the date of donation.

The cost of normal maintenance and repairs that do not add to the value of the assets or materially extend asset lives are not capitalized.

All reported assets are depreciated on the straight-line basis over their estimated useful lives ranging from five to fifty years.

Assets purchased with a value of \$500 or more that benefit more that one period will be depreciated.

CHEROKEE COUNTY RURAL WATER DISTRICT NO. 2
P.O. BOX 190
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1. SUMMARY OF SIGNIFICAN ACCOUNTING POLICIES (Continued)

C. Assets, Liabilities, and Net Assets (Continued)

8. Equity Classifications

Equity is classified as net assets and displayed in three components:

- a. Invested in capital assets, net of related debt- Consisted of capital assets including restricted capital assets, net of accumulated depreciation and reduce by the outstanding balances of any mortgages, notes, or other borrowings that are attributable to the acquisitions, construction, or improvement of those assets.
- b. Restricted net assets-Consists of net assets with constraints place on the use either by (1) external groups such as creditors, grantor, contributor, or laws or regulations of their governments; or (2) law through constitutional provisions or enabling legislation, or (3) elected restrictions by management concerning cash to be used for capital improvements.
- c. Unrestricted net assets- All other net assets that do not meet the definition of "restricted" or "invested in capital assets, net of related debt".

II. Detailed Notes Concerning the Funds

B. Accounts Receivable

Following is and aged schedule of accounts receivable as of December 31, 2018:

<u>Current</u>	<u>1-30 Days</u>	<u>31-60 Days</u>	<u>Over 60 Days</u>	<u>Prepayments</u>	<u>Total</u>
27,854	8,366	1,204	811	(4,203)	34,032

**CHEROKEE COUNTY RURAL WATER DISTRICT NO. 2
P.O. BOX 190
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II. Detailed Notes Concerning the Funds (Continued)

C. Changes in Capital Assets

Capital assets activity for the year was as follows:

	BEG. OF YEAR	ADDITIONS	DELETIONS	END OF YEAR
CAPITAL ASSETS				
DISTRIBUTION SYSTEM	2,860,621	178,453		3,039,074
BUILDINGS	289,319	-		289,319
LAND	44,741	-		44,741
MACHINERY & EQUIPMENT	159,376	1,199		160,575
AUTOMOBILES	74,104	-		74,104
OFFICE FURNITURE & EQUIP	<u>3,348</u>	<u>-</u>		<u>3,348</u>
 TOTAL CAPITAL ASSETS	 <u>3,431,509</u>	 <u>179,652</u>		 <u>3,611,161</u>
 LESS: ACCUMULATED DEPRECIATION	 <u>(1,521,896)</u>	 <u>108,980</u>		 <u>1,630,876</u>
 NET BOOK VALUE	 <u>\$1,909,613</u>	 <u>70,672</u>		 <u>\$1,980,285</u>

CHEROKEE COUNTY RURAL WATER DISTRICT NO. 2
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II. Detailed Notes Concerning the Funds (Continued)

D. Long-Term Debt

The District executed a note payable with the Oklahoma Water Resources Board (OWRB) during year 2002 to expand its treatment facility in the principal amount of \$645,000, with a maturity date of 09/15/2032. The Note is secured by all net profit and assets of the District. The note has a forty year term and bears interest at a variable rate that is reset twice annually on April 1 and October 1 of each year. As is indicated in the Trust Agreement, the Bank of Oklahoma, acting as "Trustee" for the borrower, receives monthly loan payments from the District on or before the 15th of every month . The "Trustee" will submit the semi annual payment on the District's behalf to the OWRB. The OWRB determines the amount of the semi-annual payments and notifies the District and the "Trustee" of the required payment amounts in April and October of each year. A debt service reserve account as part of the loan agreement must maintain a minimum balance of 125% of the maximum annual amount required for debt service. Debt principal service requirements on the note are as follows:

Year Ended Dec. 31,	Amount
2019	21,000
2020	22,100
2021	23,400
2022	24,700
2023	26,100
2024	27,600
2025	29,000
2026	30,700
2027	32,400
2028	34,200
2029	36,100
2030	38,100
2031	40,300
2032	<u>42,500</u>
Totals	<u>\$ 428,200</u>

CHEROKEE COUNTY RURAL WATER DISTRICT NO. 2
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II. Detailed Notes Concerning the Funds (Continued)

The District executed a note payable with the Bank of Cherokee County in April of 2017 in the amount of \$150,000.00 for a shop building. The note will be amortized over a period of one hundred twenty (120) months and bears interest at 2.95%. The first payment was due on 04/22/2017 and the final payment will be due on 03/22/2027.

Year Ended Dec. 31,	Amount
2019	14,146
2020	14,557
2021	14,970
2022	15,379
23-27	<u>70,147</u>
Totals	<u>\$ 139,961</u>

III. Other Information

A. Risk Management

The District is exposed to various risk of loss related to torts: theft of, damage to, and destruction of assets: errors and omissions: injuries to employees and natural disaster. The District purchases commercial insurance to cover these risks, including general and auto liability, property damage, and public officials liability. There were no significant reductions in insurance coverage from the prior year. settled claims from these risks have not exceeded commercial insurance coverage in any of the past three fiscal years.

B. Arbitrage Agreement

The District should monitor their obligation related to the arbitrage agreement signed when they obtained their loan from the OWRB. The arbitrage calculations are normally due every five years.

C. Subsequent Events

Management has evaluated subsequent events though May 13, 2019, which is the date the financial statements were available to be issued and have determined that not additional information needs to be added to the financial statements.

GOVERNMENTAL AUDITING STANDARDS

**INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER
FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED
ON AN AUDIT OF COMBINED FINANCIAL STATEMENTS PERFORMED
IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS**

To the Board of Directors
Cherokee County Rural Water District No. 2

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 accompanying financial statements of the Cherokee County Rural Water District No. 2, as of and for the year ended December 31, 2018 and the related notes to the financial statements, which collectively comprise the District's basic financial statements and have issued my report thereon dated May 13, 2019.

Internal Control Over Financial Reporting

Management of the District is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit of the financial statements, I considered the District's internal control over financial reporting in order to determine our auditing procedures that are appropriate 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 District's No. 2 internal control. Accordingly, I do not express an opinion on the effectiveness of the District's internal control over financial reporting.

My consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. However, as described in the accompanying schedule of findings and responses, I identified a significant deficiency in the internal controls that we do not consider to be material weakness.

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 District'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. I consider this deficiency described in the accompanying schedule of findings and responses as item 20-1, not to be a material weakness.

Report on Compliance (continued)

Compliance

As part of obtaining reasonable assurance about whether the District's financial statements are free of material misstatement, I performed tests of its compliance with certain provisions of laws, regulations, contracts, and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of my audit and, accordingly, I do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

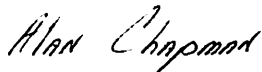
District's Response to Findings

The Cherokee County Rural Water District No. 2's response to the findings identified in our audit is described in the accompanying schedule of findings and questioned costs. The District's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

Purpose of this 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 District's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the District's internal control or on compliance. Accordingly, this communication is not suitable for any other purpose.

May 13, 2019



Alan Chapman, CPA

CHEROKEE COUNTY RURAL WATER DISTRICT NO. 2
P.O. BOX 190
HULBERT, OK 74441

SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED DECEMBER 31, 2018

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

Condition: Management is responsible for the preparation and fair presentation of the financial statement in accordance with applicable financial reporting. Accordingly, the District's ability to prepare financial statements in accordance with (GAAP). The Size of the District's accounting and administrative staff preclude certain internal controls that would be preferred if the office staff were large enough to provide optimum segregation of duties. This situation dictates that the Board remain involved in the financial affairs of the organization to provide oversight and independent review functions.

Recommendation: I recommend that the district consider designing and implementing sufficient internal controls over financial reporting by obtaining the necessary knowledge, expertise and continuing education to prepare financial statements in accordance with generally accepted accounting principles without assistance from 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 expand their knowledge and understanding of the presentation and disclosure of the financial statements.