

RURAL WATER DISTRICT NUMBER 2
OKFUSKEE COUNTY
OKEMAH, OKLAHOMA
ANNUAL FINANCIAL REPORT
NOVEMBER 30, 2016

RALPH OSBORN
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INDEPENDENT AUDITORS' REPORT

Board of Directors
Rural Water District Number 2
Okfuskee County
Okemah, Oklahoma

I have audited the accompanying modified cash basis financial statements of Rural Water District Number 2, Okfuskee County, Okemah, Oklahoma as of and for the year ended November 30, 2016, and the related notes to the financial statements, which collectively comprise Rural Water District Number 2, Okfuskee County'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 the modified cash basis of accounting described in Note A; this includes determining that the modified cash basis of accounting is an acceptable basis for the presentation of the financial statements in the circumstances. Management is also responsible for the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statement that are free from material misstatement, whether due to error or fraud.

Auditor's Responsibility

My responsibility is to express an opinion on these financial statements based on our 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 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.

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

Opinion

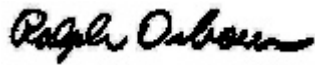
In my opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position - modified cash basis of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of Rural Water District Number 2, Okfuskee County as of November 30, 2016, and the respective changes in financial position - modified cash basis, thereof for the year then ended in accordance with the basis of accounting as described in Note A.

Basis of Accounting

I draw attention to Note A of the financial statements, which describes the basis of accounting. The financial statements are prepared on the modified cash basis of accounting, which is a basis of accounting other than accounting principles generally accepted in the United States of America. My opinion is not modified with respect to that matter.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, I have also issued my report dated February 9, 2017, on my consideration of Rural Water District Number 2, Okfuskee County'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* in considering *Rural Water District Number 2, Okfuskee County's* internal control over financial reporting and compliance.



Ralph Osborn
Certified Public Accountant
Bristow, Oklahoma
February 9, 2017

RURAL WATER DISTRICT NUMBER 2
OKFUSKEE COUNTY, OKLAHOMA
STATEMENT OF NET ASSETS - MODIFIED CASH BASIS
NOVEMBER 30, 2016

ASSETS

Current assets:	
Cash and cash equivalents	\$ 275,639
Investments	177,233
Restricted assets:	
Investments	546,767
Reserve certificates	<u>45,000</u>
Total current assets	<u>1,044,639</u>
Non-current assets:	
Capital assets:	
Land	2,000
Other capital assets, net of accumulated depreciation	<u>924,769</u>
Total non-current assets	<u>926,769</u>
Total assets	<u>1,971,408</u>

LIABILITIES

Current liabilities:	
Utility deposits	40,486
Notes payable, current	9,812
Lease payable, current	<u>22,680</u>
Total current liabilities	<u>72,978</u>
Non-current liabilities:	
Notes payable, non-current	151,936
Lease payable, non-current	<u>99,146</u>
Total non-current liabilities	<u>251,082</u>
Total liabilities	<u>324,060</u>

NET ASSETS

Invested in capital assets, net related debt	643,195
Restricted for insurance reserves	45,000
Reserved for capital projects	546,767
Unassigned	<u>412,386</u>
Net assets	<u>\$ 1,647,348</u>

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

RURAL WATER DISTRICT NUMBER 2
OKFUSKEE COUNTY, OKLAHOMA
STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN FUND NET ASSETS
MODIFIED CASH BASIS
FOR THE YEAR ENDED NOVEMBER 30, 2016

OPERATING REVENUES

Charges for services:

Water charges	\$ 471,430
New connections	26,917
Other	<u>675</u>

Total operating revenues	<u>499,022</u>
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OPERATING EXPENSES

Personal services	115,544
Water purchases	239,900
Contract labor	40,931
Insurance	14,072
Repairs and maintenance	62,531
Office expense	16,458
Professional services	12,167
Other	443
Telephone and utilities	18,965
Depreciation	<u>72,112</u>

Total operating expenses	<u>593,123</u>
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Operating income (loss)	<u>(94,101)</u>
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NON-OPERATING REVENUE (EXPENSES)

Investment income	12,895
Interest on notes payable	(13,491)
Reimbursement income/ODOT	32,259
Insurance rebate	2,181
Reimbursement income/FEMA	96,859
Project expense	<u>(93,848)</u>

Total non-operating revenue (expenses)	<u>36,855</u>
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Net income (loss)	(57,246)
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Total net assets, beginning	<u>1,704,594</u>
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Total net assets, ending	<u>\$ 1,647,348</u>
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The accompanying notes are an integral part of these financial statements.

RURAL WATER DISTRICT NUMBER 2
OKFUSKEE COUNTY, OKLAHOMA
STATEMENT OF CASH FLOWS-MODIFIED CASH BASIS
FOR THE YEAR ENDED NOVEMBER 30, 2016

Cash flows from operating activities	
Cash received from customers	\$ 501,364
Cash payments to employees	(115,544)
Cash payments to suppliers for goods and services	<u>(405,467)</u>
Net cash provided (used) by operating activities	<u>(19,647)</u>
Cash flows from capital and related financing activities	
Acquisition of fixed assets	-
Interest paid on notes payable and fiscal fees	(8,340)
Interest paid on lease purchases	(5,151)
Principal paid on notes payable	(9,312)
Principal paid on lease payable	(21,896)
Reimbursement income/ODOT	32,259
Insurance rebate	2,181
Reimbursement income/FEMA	96,859
Project expense	<u>(93,848)</u>
Net cash provided by capital and related financing activities	<u>(7,248)</u>
Cash flows from investing activities	
Transfer (to)/from investments	200,000
Interest revenue	<u>12,895</u>
Net cash provided (used) by investing activities	<u>212,895</u>
Net increase/(decrease) in cash and cash equivalents	186,000
Cash and cash equivalents, beginning	<u>89,639</u>
Cash and cash equivalents, ending	<u>\$ 275,639</u>
Reconciliation of operating income (loss)	
to net cash provided by (used) by operating activities	
Operating income (loss)	\$ (94,101)
Adjustments to reconcile operating income to	
net cash used by operating activities:	
Depreciation	72,112
Changes in assets and liabilities:	
Increase/(decrease) in utility deposits	<u>2,342</u>
Net cash provided by operating activities	<u>\$ (19,647)</u>

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

RURAL WATER DISTRICT NUMBER 2
OKFUSKEE COUNTY, OKLAHOMA
NOTES TO FINANCIAL STATEMENTS
NOVEMBER 30, 2016

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Rural Water District Number 2 (the "District") was created February 26, 1969 by the Board of County Commissioners of Okfuskee County, Oklahoma under the provisions of the Rural Water District Act (Title 82 Oklahoma Statutes 1961, Sections 1301 to 1321). The District is managed by a six member Board of Directors and Chairman. Members of the board are elected by the membership of the District at its annual meeting. Membership in the District is attained by paying membership dues and receiving services from the District. The activities of the District constitute the entire reporting entity. There are no other component or oversight units. The District is a political subdivision of the state of Oklahoma.

Financial Statements

The District is a special purpose governmental entity engaged only in business type activities. The District prepares financial statements required for enterprise funds.

Measurement Focus and Basis of Accounting

Measurement focus is a term used to describe "how" transactions are recorded within the various financial statements. Basis of accounting refers to "when" transactions are recorded regardless of the measurement focus applied.

Measurement Focus

In the financial statements business-like activities are presented using the economic resources measurement focus, within the limitations of the modified cash basis of accounting. The accounting objectives of this measurement focus are the determination of operating income, changes in net assets (or cost recovery), financial position, and cash flows. All assets and liabilities (whether current or non-current, financial, or non-financial) associated with their activities are reported. Fund equity is classified as net assets.

Basis of Accounting

In the financial statements, business-like activities are presented using a modified cash basis of accounting. This basis recognizes assets, liabilities, net assets/fund equity, revenues, and expenditures/expenses when they result from cash transactions with a provision for depreciation. This basis is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America.

RURAL WATER DISTRICT NUMBER 2
OKFUSKEE COUNTY, OKLAHOMA
NOTES TO FINANCIAL STATEMENTS
NOVEMBER 30, 2016

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Basis of Accounting (Continued)

As a result of the use of this modified cash basis of accounting, certain assets and their related revenues (such as accounts receivable and revenue for billed or provided services not yet collected) and certain liabilities and their related expenses (such as accounts payable and expenses for goods or services received but not yet paid, and accrued expenses and liabilities) are *not recorded* in these financial statements. If the Authority utilized the basis of accounting recognized as generally accepted, the financial statements would use the accrual basis of accounting.

FUND TYPES AND MAJOR FUNDS

The District reports all activity within a single 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 investments reported in the financial statements consist of Certificates of Deposits.

Capital Assets, Depreciation, and Amortization

The District's property, plant, equipment, and infrastructure with useful lives of more than one year are stated at historical cost or at estimated historical cost for those items not previously reported. The District maintains infrastructure assets records consistent with all other capital assets. Donated assets are stated at fair value on the date donated. The District generally capitalizes assets with a cost of \$2,500 or more as purchase and construction outlay 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:

Buildings	5-60
Improvements, other than buildings	2-50
Mobile equipment	3-40
Furniture, machinery, and equipment	3-30
Utility system	5-60

RURAL WATER DISTRICT NUMBER 2
OKFUSKEE COUNTY, OKLAHOMA
NOTES TO FINANCIAL STATEMENTS
NOVEMBER 30, 2016

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Compensated Absences

Full-time, permanent employees are granted personal leave in varying amounts to specified maximums depending on tenure with the District. The District does not record a liability for accrued compensated absences. Using the modified cash basis the amount paid for compensated absences is expensed as paid.

Reserves and Designations

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

Use of Estimates

The preparation of financial statements in conformity with the modified cash basis 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.

NOTE B - CASH 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 November 30, 2016, all of the Districts 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 \$1,044,639 at November 30, 2016. The bank balance of the deposits at November 30, 2016 was approximately \$1,053,210.

Credit Risk

Fixed-income securities are subject to credit risk. However, the District did not have fixed income securities at November 30, 2016.

RURAL WATER DISTRICT NUMBER 2
OKFUSKEE COUNTY, OKLAHOMA
NOTES TO FINANCIAL STATEMENTS
NOVEMBER 30, 2016

NOTE B - CASH AND INVESTMENTS (Continued)

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 November 30, 2016, the District's deposits consisted of demand deposits and certificates of deposit with a maturity of 12 months or less.

NOTE C - RESERVE CERTIFICATES

The District has purchased reserve certificates totaling \$45,000 from the Oklahoma Rural Water Association Assurance Group (the Group). These certificates are on deposit in the self-insurance reserves of the Group under the Agreement Establishing the Oklahoma Rural Water Association Assurance Group entered into pursuant to the Oklahoma Interlocal Cooperation Act. The District has insurance coverage other than the self-insurance of the group. Reserve certificates may be surrendered and the deposit refunded subject to certain time and notice requirements. The certificates accrue interest at a fluctuating rate on the basis of a 360-day year at the Treasury rate plus two percent per annum. The balance in the self-insurance reserve certificates is considered reserved net assets.

NOTE D - RESTRICTED INVESTMENTS

The District reports restricted investments for use as a depreciation reserve. These investments are to be used for expense related to replacing the water system.

NOTE E - CAPITAL ASSETS

Changes in capital assets.

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

	CAPITAL ASSETS, DEPRECIATED				Capital Assets Not Depreciated Land
	Buildings	Infrastructure & Improvements Other Than Buildings	Furniture, Machinery, And Equipment	Totals	
PRIMARY GOVERNMENT					
Business-type activities					
Balance, June 30, 2015	\$ 24,518	\$ 2,990,626	\$ 76,198	\$ 3,091,342	\$ 2,000
Increases	-	-	-	-	-
Decreases	-	-	-	-	-
Balance, June 30, 2016	<u>24,518</u>	<u>2,990,626</u>	<u>76,198</u>	<u>3,091,342</u>	<u>2,000</u>
Accumulated Depreciation					
Balance, June 30, 2015	14,003	2,031,607	48,851	2,094,461	
Increases	568	68,361	3,183	72,112	
Decreases	-	-	-	-	
Balance, June 30, 2016	<u>14,571</u>	<u>2,099,968</u>	<u>52,034</u>	<u>2,166,573</u>	
Business-type activities					
Capital Assets, Net	<u>\$ 9,947</u>	<u>\$ 890,658</u>	<u>\$ 24,164</u>	<u>\$ 924,769</u>	<u>\$ 2,000</u>

RURAL WATER DISTRICT NUMBER 2
OKFUSKEE COUNTY, OKLAHOMA
NOTES TO FINANCIAL STATEMENTS
NOVEMBER 30, 2016

NOTE F - NOTES PAYABLE PROPRIETARY FUND

The District has incurred debt for the expansion of the water system. On May 18, 1989, the District signed a Promissory Note with the Farmers Home Administration, United States Department of Agriculture for a loan in the principal amount of \$299,500. Interest payments were made May 18, 1990 and May 18, 1991. Beginning June 18, 1991, payments in the amount of \$1,471 became payable monthly. The loan is for a term of forty years at 5% interest. The balance due on the loan at November 30, 2016 was \$161,748.

The annual debt service requirements for the note is \$17,652 including principal and interest. The District has reserve funds sufficient to equal the annual debt service requirement.

Following is the anticipated annual debt service amounts:

<u>Year Ended November 30</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2017	\$ 9,812	\$ 7,840	\$ 17,652
2018	10,314	7,338	17,652
2019	10,842	6,810	17,652
2020	11,396	6,256	17,652
2021	11,979	5,673	17,652
2022-2026	69,742	18,518	88,260
2027-2029	37,663	2,618	40,281
Total	<u>\$ 161,748</u>	<u>\$ 55,053</u>	<u>\$ 216,801</u>

NOTE G - LEASE OBLIGATIONS

The District has entered into a lease agreement as lessee for financing the acquisition of equipment. The lease agreement qualifies as a capital lease for accounting purposes since title transfers at the end of the lease term and it has been recorded at the present value of the future minimum lease payments.

The schedule of the future minimum lease payments under the capital lease and the present value of the net minimum lease payments at November 30, is as follows:

<u>Year ending November 30</u>	<u>Radio Meters</u>	<u>Total</u>
2017	\$ 27,046	\$ 27,046
2018	27,046	27,046
2019	27,046	27,046
2020	27,046	27,046
2021	27,046	27,046
Total minimum lease payments	135,230	135,230
Less: Amount representing interest	13,404	13,404
Present value of future minimum lease payments	<u>\$ 121,826</u>	<u>\$ 121,826</u>

RURAL WATER DISTRICT NUMBER 2
OKFUSKEE COUNTY, OKLAHOMA
NOTES TO FINANCIAL STATEMENTS
NOVEMBER 30, 2016

NOTE H- PENSION OBLIGATIONS

The District established a Savings Incentive Match Plan for Employees of Small Employers (SIMPLE) plan under Section 408 (p) of the Internal Revenue Code effective January 1, 2000. All employees are eligible to participate. All contributions made under this SIMPLE plan are fully vested and nonforfeitable.

An eligible employee may make a salary reduction election to have his or her compensation for each pay period reduced by a percentage. The total amount of the reduction in the employee's compensation cannot exceed \$10,000 for any calendar year. For each calendar year, the District will contribute a matching contribution to each eligible employee's SIMPLE IRA equal to the employee's salary reduction contribution up to a limit of 3% of the employee's compensation for the calendar year. The District paid \$2,040 to employee plans during the current fiscal year on salary of \$103,381.

NOTE I - 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; injuries to employees; and natural disasters. The District carries commercial insurance for risk of loss, including workers' compensation. Settled claims resulting from these risks have not exceeded commercial insurance coverage in any of the past three fiscal years.

NOTE J - CONTRACTS

The District purchases water for resale from the Okemah Utilities Authority, Okemah, Oklahoma, under the terms of an Amended Water Purchase Contract dated December 3, 1985. The contract runs until November 1, 2025. The price paid by the District is determined based on costs incurred by the Authority in producing the water purchased. The contract contains terms defining the costs to be considered.

Note K - SUBSEQUENT EVENTS

Management has evaluated subsequent events through February 9, 2017, the date on which the financial statements were available to be issued. The Authority does not believe there are any events requiring disclosure.

INDEPENDENT AUDITOR'S 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

Board of Directors
Rural Water District Number 2
Okfuskee County
Okemah, 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 modified cash basis financial statements of the business-type activities of Rural Water District Number 2, Okfuskee County, Oklahoma, as of and for the year ended November 30, 2016, and the related notes to the financial statements, which collectively comprise Rural Water District Number 2, Okfuskee County's basic financial statements and have issued my report thereon dated February 9, 2017.

Internal Control Over Financial Reporting

In planning and performing my audit, I considered Rural Water District Number 2, Okfuskee County'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 Rural Water District Number 2, Okfuskee County's internal control. Accordingly, I do not express an opinion of the effectiveness of Rural Water District Number 2, Okfuskee County'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.

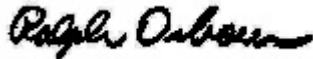
Compliance and Other Matters

As part of obtaining reasonable assurance about whether Rural Water District Number 2, Okfuskee County, Okemah, 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
February 9, 2017