

ANNUAL FINANCIAL REPORT

Board of Directors
Rural Water District No. 5
Sequoyah County
Gore, Oklahoma

I have audited the accompanying financial statements of the Board of Directors of Rural Water District No. 5, Sequoyah County, Oklahoma, for the year ended December 31, 2011, which collectively represent the financial statements of Rural Water District No. 5's management. My responsibility is to express an opinion on the financial statements based on my audit.

**RURAL WATER DISTRICT NO. 5
SEQUOYAH COUNTY, OKLAHOMA
GORE, OKLAHOMA
ANNUAL FINANCIAL REPORT
DECEMBER 31, 2011**

My audit was conducted in accordance with the standards of the American Institute of Certified Public Accountants (AICPA) for a general audit of financial statements. These standards require me to plan and perform the audit to be reasonably assured of detecting material misstatements. Inherent limitations of an audit include the fact that the financial statements are prepared by management and I am not permitted to audit the underlying records. My audit also included an examination of the internal control system of the District. My audit was limited to the financial statements and does not constitute an audit of the internal control system. My audit was also limited to the financial statements and does not constitute an audit of the internal control system. My audit was also limited to the financial statements and does not constitute an audit of the internal control system.

In my opinion, the financial statements referred to above present fairly the financial position of Rural Water District No. 5 as of December 31, 2011, and the changes in financial position and cash flows for the year ended December 31, 2011, in accordance with accounting principles generally accepted in the United States of America.

Rural Water District No. 5 has not presented Management's Discussion and Analysis with the accompanying financial statements. Management's Discussion and Analysis is not required to be part of the financial statements.

I have audited the financial statements of Rural Water District No. 5, Sequoyah County, Oklahoma, for the year ended December 31, 2011, in accordance with the standards of the American Institute of Certified Public Accountants (AICPA) for a general audit of financial statements. These standards require me to plan and perform the audit to be reasonably assured of detecting material misstatements. Inherent limitations of an audit include the fact that the financial statements are prepared by management and I am not permitted to audit the underlying records. My audit also included an examination of the internal control system of the District. My audit was limited to the financial statements and does not constitute an audit of the internal control system. My audit was also limited to the financial statements and does not constitute an audit of the internal control system.

**RALPH OSBORN
CERTIFIED PUBLIC ACCOUNTANT
500 SOUTH CHESTNUT
P.O. BOX 1015
BRISTOW, OK 74010-1015**

Ralph Osborn

Sequoyah County
Gore, Oklahoma
December 31, 2011

RURAL WATER DISTRICT NO. 5
 SEQUOYAH COUNTY, OKLAHOMA
 GORE, OKLAHOMA
 STATEMENT OF NET ASSETS
 DECEMBER 31, 2011

ASSETS

Current assets:

Cash and cash equivalents	\$ 78,502
Accounts receivable, net	27,074
Grants receivable	40,750
Prepaid expense	6,860
Interest receivable	<u>50</u>

Total current assets 153,236

Restricted assets:

Restricted cash and cash equivalents	<u>44,664</u>
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Total restricted assets 44,664

Non-current assets:

Capital assets:

Land	14,448
Other capital assets, net of accumulated depreciation	<u>967,753</u>

Total non-current assets 982,201

Total assets 1,180,101

LIABILITIES

Current liabilities:

Accounts payable	17,571
Payroll liabilities	1,783
Accrued Interest Payable	431
Notes payable, current	<u>25,632</u>

Total current liabilities 45,417

Non-current liabilities:

Notes payable, non-current	<u>367,243</u>
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Total non-current liabilities 367,243

Total liabilities 412,660

NET ASSETS

Nonspendable	589,326
Reserved for debt service	44,664
Unassigned	<u>133,451</u>

Net assets \$ 767,441

See accompanying notes to financial statements.

RURAL WATER DISTRICT NO. 5
 SEQUOYAH COUNTY, OKLAHOMA
 GORE, OKLAHOMA
 STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN FUND NET ASSETS
 FOR THE YEAR ENDED DECEMBER 31, 2011

OPERATING REVENUES

Water Sales	\$ 342,625
Membership	27,000
Penalties	15,152
Connect Fees	<u>2,775</u>
Total operating revenues	<u>387,552</u>

OPERATING EXPENSES

Personal services	106,389
Payroll taxes	8,160
Employee benefits	2,231
Supplies	27,885
Testing	1,236
Fuel	9,735
Insurance and bonds	22,696
Legal and professional	7,025
Contract labor	15,597
Repairs and maintenance	36,400
Office and postage	12,908
Water purchases	30,157
Telephone and utilities	22,908
Bonds and permits	7,039
Depreciation	<u>45,832</u>
Total operating expenses	<u>356,198</u>
Operating income (loss)	<u>31,354</u>

NON-OPERATING REVENUE (EXPENSES)

Grants	159,080
Investment income	763
Interest on notes payable and fiscal fees	<u>(19,354)</u>
Total non-operating revenue (expenses)	<u>140,489</u>
Net income (loss)	171,843
Total net assets, beginning	<u>595,598</u>
Total net assets, ending	<u>\$ 767,441</u>

See accompanying notes to financial statements.

RURAL WATER DISTRICT NO. 5
 SEQUOYAH COUNTY, OKLAHOMA
 GORE, OKLAHOMA
 STATEMENT OF CASH FLOWS
 FOR THE YEAR ENDED DECEMBER 31, 2011

Cash flows from operating activities	
Cash received from customers	\$ 379,574
Cash paid to employees	(117,056)
Cash payments to suppliers for goods and services	<u>(175,041)</u>
Net cash provided (used) by operating activities	<u>87,477</u>
Cash flows from capital and related financing activities	
Acquisition of fixed assets	(158,743)
CDBG Grant passed through Sequoyah County	118,330
Interest paid on notes payable and fiscal fees	(19,936)
Principal paid on notes payable	<u>(38,864)</u>
Net cash (used) by capital and related financing activities	<u>(99,213)</u>
Cash flows from investing activities	
Receipt of interest and dividends	<u>763</u>
Net cash provided (used) by investing activities	<u>763</u>
Net increase in cash and cash equivalents	(10,973)
Cash and cash equivalents, beginning	<u>134,139</u>
Cash and cash equivalents, ending	<u>\$ 123,166</u>
Reconciliation of operating income (loss) to net cash provided by (used) by operating activities	
Operating income (loss)	\$ 31,354
Depreciation	45,832
(Increase)/Decrease in Current Assets	
Accounts receivables, net	(7,978)
Prepaid expenses	4,937
Increase/(Decrease) in Current Liabilities	
Accounts payable	13,608
Payroll liabilities	<u>(276)</u>
Net cash provided by operating activities	<u>\$ 87,477</u>

See accompanying notes to financial statements.

RURAL WATER DISTRICT NO. 5
SEQUOYAH COUNTY, OKLAHOMA
GORE, OKLAHOMA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2011

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Rural Water District No. 5, Sequoyah County, Oklahoma (the "District") was organized on May 5, 1977 by the Sequoyah County Board of County Commissioners under the provisions of the Rural Water District Act (Title 82, O.S. Supp 1972, Sections 1324.1 to 1324.26) for the purpose of providing a water works system including all physical facilities, improvements and services necessary for executing that purpose in Sequoyah County. Since the District is a political subdivision of the State of Oklahoma, under Title 82, it is exempt from Federal and State income taxes.

The membership consists of approximately 607 benefit unit holders, each entitled to one vote. Subscribers to benefit units pay a \$1,500 subscription fee, which is non refundable, and entitles the holder to one line from the District's water system. The Board of Directors consists of 5 members serving 3 year terms. The vacant Board seats are filled at the annual meeting, and the Board of Directors elects a Chairman, Vice-Chairman, Secretary, and Treasurer.

Government-Wide and Fund 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, 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.

RURAL WATER DISTRICT NO. 5
SEQUOYAH COUNTY, OKLAHOMA
GORE, OKLAHOMA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2011

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

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 District did not report any investments at December 31, 2011.

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 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 with one-half year depreciation in the year acquired and one-half in the year of disposal. 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	20 - 50 years
Water and sewer system	30 - 50 years
Machinery, and equipment	5 - 10 years
Improvements	10 - 20 years

Compensated Absences

At December 31, 2011, it is not believed that accrued benefits, if any, are significant and would not be materially affect the financial statements.

Reserves and Designations

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

RURAL WATER DISTRICT NO. 5
SEQUOYAH COUNTY, OKLAHOMA
GORE, OKLAHOMA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2011

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.

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 December 31, 2011, 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 \$123,166 at December 31, 2011. The bank balance of the deposits at December 31, 2011 was approximately \$127,209.

Credit Risk

Fixed-income securities are subject to credit risk. However, the District did not have fixed income securities at December 31, 2011.

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 December 31, 2011, the District's deposits consisted of demand deposits and certificates of deposit with a maturity of 12 months or less.

RURAL WATER DISTRICT NO. 5
 SEQUOYAH COUNTY, OKLAHOMA
 GORE, OKLAHOMA
 NOTES TO FINANCIAL STATEMENTS
 DECEMBER 31, 2011

NOTE C - RESTRICTED ASSETS

USDA RURAL DEVELOPMENT

The District has reported as restricted assets cash held by a trustee bank for use in relation to the note payable listed in Note E. The cash reported in the Statement of Net Assets is restricted as indicated. This cash is not available for other purposes.

The Loan Resolution Security Agreements with the USDA Rural Development requires a reserve fund to be funded at 10% of the monthly installment until the balance is equal to the annual installment amount (\$3,722 X 12 = \$44,664). At December 31, 2011, the total balance in the debt service reserve accounts at Lakeside State Bank, Chelsea, Oklahoma was \$42,840.

Debt Service Reserve Account	\$ 47,106
Less: Excess Funds	(2,442)
Net Required Reserve	<u>\$ 44,664</u>

NOTE D - CAPITAL ASSETS

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

	Beginning Balance	Additions	Retirements	Ending Balance
Buildings & Improvements	\$ 73,095	\$ -	\$ -	\$ 73,095
Land	14,448	-	-	14,448
Equipment	82,593	-	-	82,593
Construction in Progress	-	158,743	-	158,743
Water Distribution System	1,430,498	-	-	1,430,498
Total Capital Assets	\$ 1,600,634	\$ 158,743	\$ -	\$ 1,759,377
Depreciation	(731,344)	(45,832)	-	(777,176)
Total Net Capital Assets	<u>\$ 869,290</u>	<u>\$ 112,911</u>	<u>\$ -</u>	<u>\$ 902,201</u>

REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE
AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN
ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS

To the Board of Directors
Rural Water District No. 5
Sequoyah County
Gore, Oklahoma

I have audited the financial statements of the business-type activities of Rural Water District No. 5 as of and for the year ended December 31, 2011, which collectively comprise Rural Water District No. 5's basic financial statements and have issued my report thereon dated March 15, 2012 which did not include Management's Discussion and Analysis. 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.

Internal Control Over Financial Reporting

In planning and performing my audit, I considered Rural Water District No. 5's internal control over financial reporting as a basis for designing my auditing procedures 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 No. 5's internal control over financial reporting. Accordingly, I do not express an opinion of the effectiveness of Rural Water District No. 5'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.

My consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies, or material weaknesses. However, as discussed below, I identified certain deficiencies in internal control over financial reporting that I consider to be significant deficiencies. 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 the lack of segregation of duties to be a significant deficiency.