

RURAL WATER DISTRICT NO. 3
Washington County, Oklahoma

FINANCIAL STATEMENTS
For the Year Ended December 31, 2016

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RURAL WATER DISTRICT NO. 3
Washington County, Oklahoma

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INDEPENDENT AUDITOR'S REPORT

Board of Directors
Rural Water District No. 3
Washington County, Oklahoma

Report on the Financial Statements

We have audited the accompanying financial statements of the business-type activities of Washington County Rural Water District No. 3 as of and for the years ended December 31, 2016 and 2015, and the related notes to the financial statements, which collectively comprise Washington County Rural Water District No. 3'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 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

Our responsibility is to express opinions on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. 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 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 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, we 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.

Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the business-type activities of Washington County Rural Water District No. 3 as of December 31, 2016 and 2015, and the respective changes in financial position and, where applicable, cash flows thereof for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and budgetary comparison information on pages 3 through 8, and page 23, be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated April 24, 2017, on our consideration of Washington County Rural Water District No. 3'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 our testing of internal control over financial reporting and 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 Washington County Rural Water District No. 3's, internal control over financial reporting and compliance.



Bruce G. Luttrell, CPA, PC

April 24, 2017

MANAGEMENT'S DISCUSSION AND ANALYSIS

**Washington County Rural Water District No. 3
Management's Discussion and Analysis Report
For Fiscal Year 2016
(Ended December 31, 2016)**

Introduction

The purpose for this report is to present, from the District Manager's perspective, an assessment of the financial activities and performance of Washington County Rural Water District No. 3 (hereinafter referred to as the "District") for the audited year. The primary goal of this report is to address the critical question "Is the District as a whole better or worse off as a result of the year's activities?" It is also the goal of this report to present the findings from the audit and other critical operations information in an easy-to-read format for interpretation by the non-accountant.

The information included herein should be read in conjunction with the financial statements prepared by the District's Auditor. Also note that the currency amounts presented herein have been rounded to the nearest dollar.

Financial Highlights

- The amount of water sold in FY '16 (704,334,019 gallons) increased by approximately 9.5 percent when compared to the previous year (sold 643,253,088 gallons in FY '15).
- Revenues from the sale of water accounted for 67.3 percent of all revenues. The total revenue from water sales increased by approximately 9 percent when compared to FY '15.
- The District increased new infrastructure by approximately \$ 2,881,000 during the year. \$ 1,767,641.60 of that was provided by infrastructure contributed to the District through new housing developments.
- The District did not improve its position with regard to total liabilities by increasing their value by \$ 134,455 when compared to FY '15. Total equity increased by approximately \$ 1,926,000.
- The District as a whole is much better off as a result of the year's activities.

Overview of Financial Statements

The financial statements prepared for the FY '16 audit were used to develop this report. A brief description of each statement and their purpose follows:

Statements of Financial Position [Balance Sheet] - The purpose for the "Statements of Financial Position" is to present a summary of the District's net assets. In simple terms this statement shows what we own (assets) minus what we owe (liabilities). When we compare this years Statement of Financial Position to previous years we look at how our net worth (i.e., net assets) is increasing or decreasing. This is one indicator of how the District's financial position is improving or deteriorating.

Statements of Activities - The "Statements of Activities" presents the results of the business activities over the course of the fiscal year and information as to how the net assets changed during the year without regard to when cash was received or paid.

Statements of Cash Flows - The "Statements of Cash Flows" presents changes in cash and cash equivalents (i.e., Accounts Payable and Receivable), resulting from operational, financing and investing activities. This statement shows how the District's cash on hand changed from the beginning to the end of the year.

Condensed Financial Statements

Condensed Statement of Financial Position

	12/31/16	12/31/15	Dollar Change	Percent Change
Current and Other Assets	\$ 5,556,381	\$ 5,221,474	\$ 334,907	6.4
Capital Assets	\$33,045,319	\$31,307,381	\$ 1,737,938	5.6
Total Assets	\$38,601,700	\$36,528,855	\$ 2,072,845	5.7
Current Liabilities	\$ 630,139	\$ 606,796	\$ 23,343	3.8
Long-Term Liabilities	\$17,770,991	\$17,648,333	\$ 122,658	0.7
Total Liabilities	\$18,401,130	\$18,255,129	\$ 146,001	0.8
Net Assets invested in capital assets, net of related debt	\$14,876,798	\$13,273,315	\$ 1,603,483	12.1
Restricted for debt service	\$ 727,028	\$ 330,174	\$ 396,854	120.2
Unrestricted net assets	\$ 4,596,744	\$4,670,237	\$ <73,493>	<1.6>
Total Net Assets	\$20,200,570	\$18,273,726	\$ 1,926,844	10.5

Condensed Statement of Activities

	12/31/16	12/31/15	Dollar Change	Percent Change
Operating Revenues	\$ 5,065,949	\$ 4,699,991	\$ 365,958	7.8
Non-operating Revenues	\$ 2,123,038	\$ 1,232,969	\$ 890,069	72.2
Total Revenues	\$ 7,188,987	\$ 5,932,960	\$ 1,256,027	21.2
Depreciation Expense	\$ 1,163,172	\$ 1,112,026	\$ 51,146	4.6
Other Operating Expenses	\$ 4,098,971	\$ 3,764,221	\$ 334,750	8.9
Total Expenses	\$ 5,262,143	\$ 4,867,247	\$ 394,896	8.1
Change in Net Assets	\$ 1,926,844	\$ 1,056,713	\$ 870,131	82.3
Beginning Net Assets	\$18,273,726	\$17,217,013	\$ 1,056,713	6.1
Ending Net Assets	\$20,200,570	\$18,273,726	\$ 1,926,844	10.5

Analytical Overview

Sources of Income - The District's primary sources of income are from the sale of water services. Other sources of income include interest on investments; membership fees; and collection fees. The District has no taxing power.

Growth - During the year 351 new benefit units (i.e., water meters) were sold compared to a total of 314 sold in FY '15. The District sold 704,334,019 gallons of water, which represents an approximate increase of 9.5 percent over FY '15 likely the result of a drier year in FY '15. The increase in year-over-year benefit unit sales is likely the result of a improving housing market compared to the previous year.

Statements of Net Position:

Total Net Position - The *Statement of Net Position* shows that the District's total net position actually increased by \$ 1,926,844 when compared with FY '15. This increase represents 10.5 % in our total net position. Although current assets (i.e., cash) increased by \$ 334,907, the District's fixed assets (i.e., land, equipment and infrastructure) actually increased by \$ 1,737,938 and the District's investments stayed the same.

On the 2 nd page of the *Statement of Net Position* we see that the District did not improve its position with regard to total (i.e., current and long term) liabilities by increasing their value by \$ 146,001 when compared to FY '15. This increase occurred primarily in the category of long term liabilities. Total equity increased by approximately \$ 1,926,844.

Statement of Revenues, Expenditures and Changes in Net Position:

Reviewing the *Statement of Revenues, Expenditures and Changes in Net Position* we can see that the District's change in net position was \$ 1,926,844. This compares favorably to the net change in net position of \$ 1,056,713 experienced in FY '15.

Revenues – The District's total operating revenues for FY '16 were \$ 5,065,949. This represents an increase of approximately \$ 365,958 or 7.8 percent over FY '15. Approximately 67.3 percent of our revenues (i.e., \$ 4,837,880) were derived from sale of water services.

Approximately 4.9 percent of revenues (\$ 351,500) came from membership fees. Revenues from these items were up 11.9 percent over FY '15.

Expenses - The District's total operating expenses were \$ 5,262,143. Excluding depreciation and amortization the total operating expenses are reduced to \$ 4,098,971. This represents an approximate increase of \$ 334,750 or 8.9 percent over FY '15.

Statement of Cash Flows:

As shown in the *Statement of Cash Flows* the District had a net increase in cash at the end of the year of \$ 275,417.

Annual Budget

As required by the District's By-Laws, an Annual Budget was prepared by the District Manager for FY '16. The basis for the budget included a thorough examination of the actual results from the last several years. The budget also included certain anticipated expenses that were related to budgeted capital projects. The FY '16 Annual Budget was reviewed and approved by the Board during the Board meeting held on March 14, 2016.

Debt Administration:

The remaining balance for all promissory notes (i.e., loans) at the beginning of the year was \$ 18,034,066. Another \$ 555,562 was drawn on the OWRBB loan, and all scheduled loan and interest payments through December 31, 2016 were made on time. The District increased its principal on outstanding loans by \$ 134,455. The balance remaining on all outstanding loans is \$ 18,168,521. The sinking fund for the District's loans is fully funded.

Highlights of Other Critical Information:

- In Fiscal Year 2016 the District has continued to meet the new and more stringent water quality regulations. This includes monthly testing for Total Organic Carbons (TOC's) and quarterly testing for Trihalomethanes (THM's) and Haloacetic Acids (HAA's). The District is pleased to report that our water quality complied with all the regulations.
- In Fiscal Year 2016 the District started sampling for the EPA required Long Term 2 Surface Water Treatment Rule.
- In Fiscal Year 2016 the District started sampling for the EPA required Total Coliform Rule.
- Caney River Raw Water Supply Project
 - Legal action filed by the Contractor against the District is in progress.
 - The District completed a bank stabilization project on the upstream east bank of the Caney River. Additional rip-rap was also installed along the west bank to improve conditions.
- Water Treatment Plant (WTP) Expansion Project – The one (1) warranty period ended in September 2016 for the new expansion. Several warranty items were addressed at the end of the warranty period. Additional investigations continued on potential grounding issues.
- Discharge Permit – The District began electronic filing of the monthly discharge monitoring report per ODEQ requirements.
- Legal Action by Design Engineer of WTP Expansion Project – Formal legal action continued against the District in 2016 by the design engineer for additional fees.
- Overflow modifications were designed and completed on the Hogue Tower in 2016.
- Water Resources Master Planning – We continue work on a new master plan for the District.
- Oologah Raw Water Line – The District worked with AEP/PSO towards finalizing the easement agreement with AEP/PSO Oologah Power Station.
- 6-Inch Water Line Extension along NS 3954 Road – The District completed construction on approximately one-half mile of new 6-inch water line along NS 3954 Road north of 186th Street North. This water line replaced an existing 2-inch water line.

Conclusions – The District as a whole has a better financial position than a year ago. The value of our total liabilities increased while the value of our total equity increased. Our total debt service was increased by \$ 146,001. We ended the year with more cash and investments (\$ 275,417) than we started with.

Looking Forward – As we look forward to Fiscal Year 2017 we anticipate our growth to be the same or slightly greater than that which was experienced in FY '16. We also anticipate progress on the following major capital projects:

- Water Treatment Plant (WTP) Expansion Project – We anticipate all warranty work to be completed in the first quarter of 2017.
- Caney River Raw Water Supply Project: We anticipate progress on the lawsuit for this project.
- Water Resources Master Plan – We anticipate completing the master plan in 2017. This master plan will identify future capital needs with emphasis on priority.
- Future Water Lines – The District is planning:
 - To continue to work with AEP/PSO to complete the balance of work remaining on this project (i.e., easement).
 - To develop plans for the construction of new 24-inch water line.
 - The District will work with the ODOT on the following:
 - To complete water line relocation plans for approximately three (3) miles of water line along State Highway 20 between US Highway 75 and Mingo.
 - To complete construction for relocation of certain water lines along Highway 11.
 - To develop water line relocation plans for existing water lines at Bevan Creek along Memorial north of Vera.
 - The District will work with Tulsa County to prepare water line relocation plans for existing infrastructure in the intersection of 86th Street North and Sheridan. Construction of the relocation work is anticipated to begin in the fourth quarter of 2017.
 - The District will work with Owasso on the following:
 - Water line relocations in the intersection of 116th Street North and 129th East Avenue.
 - Water line relocations in the intersection of 106th Street North and 145th East Avenue.
 - Water line relocations along 116th Street North between 129th East Avenue and Garnett.
 - The District will work with Developers on the following:
 - To relocate existing 12 and 24-inch water lines located along 129th East Avenue between 126th Street North and 116th Street North. Water line relocations are associated with Morrow Place Phase I and the Estates at Morrow Place developments.
 - To relocate and increase size of existing water lines along 106th Street North near the new Abbott Farms development.
- Water Quality Regulations
 - Long Term 2 Surface Water Treatment Rule (LT2) – Testing will continue for the second phase of the LT2 regulations in the 2017.

FINANCIAL STATEMENTS

**RURAL WATER DISTRICT NO. 3
WASHINGTON COUNTY, OKLAHOMA**

**STATEMENTS OF NET POSITION
DECEMBER 31, 2016 AND 2015**

	<u>2016</u>	<u>2015</u>
ASSETS		
Current assets:		
Cash	\$ 827,716	\$ 949,153
Investments	3,150,000	3,150,000
Restricted cash & investments (Note 7)	727,028	330,174
Accounts receivable	499,066	451,184
Accrued interest receivable	481	493
Inventory	284,558	286,523
Prepaid insurance	67,532	53,947
Total current assets	<u>5,556,381</u>	<u>5,221,474</u>
Noncurrent assets:		
Other assets:		
Capital assets:		
Building & land	307,638	307,638
Machinery & tools	375,659	363,546
Automotive equipment	340,778	340,778
Furniture & fixtures	116,212	116,212
Lab equipment	40,706	40,706
Water treatment & distribution system	45,094,501	42,225,259
Less accumulated depreciation	<u>(13,230,175)</u>	<u>(12,086,758)</u>
Total capital assets	<u>33,045,319</u>	<u>31,307,381</u>
Total Assets	<u>\$ 38,601,700</u>	<u>\$ 36,528,855</u>

The accompanying notes to the financial

	<u>2016</u>	<u>2015</u>
LIABILITIES		
Current liabilities:		
Accounts payable	\$ 88,246	\$ 79,143
Accrued interest payable	144,363	141,920
Current portion of long-term debt (Note 2)	397,530	385,733
Total current liabilities	<u>630,139</u>	<u>606,796</u>
Noncurrent liabilities:		
Notes payable (Note 2)	18,168,521	18,034,066
Less: current portion	<u>(397,530)</u>	<u>(385,733)</u>
Total noncurrent liabilities	<u>17,770,991</u>	<u>17,648,333</u>
Total Liabilities	<u>18,401,130</u>	<u>18,255,129</u>
NET POSITION		
Invested in capital assets, net of related debt	14,876,798	13,273,315
Restricted for debt service	727,028	330,174
Unrestricted	<u>4,596,744</u>	<u>4,670,237</u>
Total Net Position	<u>\$ 20,200,570</u>	<u>\$ 18,273,726</u>

statements are an integral part of this statement.

**RURAL WATER DISTRICT NO. 3
WASHINGTON COUNTY, OKLAHOMA**

**STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN FUND NET POSITION
FOR THE YEARS ENDED DECEMBER 31, 2016 AND 2015**

	<u>2016</u>	<u>2015</u>
Operating revenues:		
Water sales (net of adjustments)	\$ 4,837,880	\$ 4,437,790
Penalties, fees, service charges and miscellaneous	228,069	262,201
Total operating revenues	<u>5,065,949</u>	<u>4,699,991</u>
Operating expenses:		
Salaries, wages & contract labor	856,709	860,909
Payroll taxes	67,534	66,085
Employee benefits	247,705	221,763
Utilities	362,748	345,963
Telephone	13,367	13,642
Equipment expense	19,336	30,733
Depreciation	1,163,172	1,112,026
Interest expense	673,024	675,276
Vehicle expense	34,429	49,212
Building, vehicle & other insurance	135,090	100,760
Plant repair & maintenance	118,324	135,249
Chemicals	666,215	534,600
Travel, entertainment & miscellaneous	39,250	36,717
Licenses & fees	33,445	34,056
Plant supplies	371,194	275,479
Water purchased	8,169	14,065
Office expense & postage	79,177	107,107
Professional fees	373,255	262,605
Total operating expenses	<u>5,262,143</u>	<u>4,876,247</u>
Net operating income	<u>(196,194)</u>	<u>(176,256)</u>
Nonoperating revenue (expense)		
New benefit units	351,500	314,000
Contribution of developments	1,767,642	906,234
Interest income	14,384	13,235
Gain on sale of assets	(9,988)	-
Trustee fee	(500)	(500)
Total nonoperating revenue (expense)	<u>2,123,038</u>	<u>1,232,969</u>
Change in net position	1,926,844	1,056,713
Net position beginning of year	<u>18,273,726</u>	<u>17,217,013</u>
Net position end of year	<u><u>\$ 20,200,570</u></u>	<u><u>\$ 18,273,726</u></u>

The accompanying notes to the financial statements are an integral part of this statement.

**RURAL WATER DISTRICT NO. 3
WASHINGTON COUNTY, OKLAHOMA**

**STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2016 AND 2015**

	2016	2015
Cash flows from operating activities:		
Receipts from customers	\$ 5,018,067	\$ 4,656,129
Payments to suppliers	(3,251,003)	(2,807,516)
Payments to employees	(848,030)	(829,936)
Net cash provided (used) by operating activities	<u>919,034</u>	<u>1,018,677</u>
Cash flows from noncapital financing activities:		
Transfers from (to) investments	-	-
Transfers from (to) restricted cash and investments	(396,854)	(10,501)
Trustee fee	(500)	(500)
Net cash provided (used) by noncapital financing activities	<u>(397,354)</u>	<u>(11,001)</u>
Cash flows from capital and related financing activities:		
New benefit units	351,500	314,000
Purchase of capital assets	(1,113,713)	(1,045,208)
Principal paid on capital debt	(421,107)	(542,797)
Issue new capital debt	555,562	476,238
Sales and trade assets	(29,743)	-
Net cash provided (used) by capital and related financing activities	<u>(657,501)</u>	<u>(797,767)</u>
Cash flows from investing activities:		
Interest income	<u>14,384</u>	<u>13,235</u>
Net increase (decrease) in cash and cash equivalents	(121,437)	223,144
Cash balance beginning of year	<u>949,153</u>	<u>726,009</u>
Cash balance end of year	<u><u>\$ 827,716</u></u>	<u><u>\$ 949,153</u></u>
Reconciliation of operating income (loss) to net cash provided (used) by operating activities:		
Operating income (loss)	\$ (196,194)	\$ (176,256)
Adjustments to reconcile operating income to net cash provided (used) by operating activities:		
Cash flows reported in other categories:		
Depreciation expense	1,163,172	1,112,026
Amortization	-	-
Change in assets and liabilities:		
Accounts receivable	(47,882)	(43,862)
Accrued interest receivable	12	15
Inventory	1,965	133,103
Prepaid insurance	(13,585)	(2,141)
Accounts payable	9,103	(98)
Accrued interest payable	2,443	(4,110)
Net cash provided by operating activities	<u><u>\$ 919,034</u></u>	<u><u>\$ 1,018,677</u></u>

The accompanying notes to the financial statements are an integral part of this statement.

NOTES TO BASIC FINANCIAL STATEMENTS

RURAL WATER DISTRICT NO. 3
Washington County, Oklahoma

NOTES TO THE FINANCIAL STATEMENTS
For the Year Ended December 31, 2016

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Washington County Rural Water District Number 3 (the District) complies with accounting principles generally accepted in the United States of America (GAAP) as applicable to governmental units. The Governmental Accounting Standards Board (GASB) is responsible for establishing GAAP for state and local governments through its pronouncements (Statements and Interpretations.) The accounting and reporting framework and the more significant accounting policies established in GAAP and used by the District are discussed below.

A. REPORTING ENTITY

The District was organized in 1965, under 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 Washington, Osage, Tulsa and Rogers counties. 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 10,000 benefit unit holders, each entitled to one vote. Subscribers to benefit units pay a \$ 1,000 subscription fee (\$ 750 prior to May 2005), which is non-refundable, and entitles the holder to one line from the District's water system. The Board of Directors consist of 7 members serving 3 year terms. The vacant Board seats are filled at the annual meeting in April, and following, the Board of Directors meet and elect a Chairman, Vice-Chairman, Secretary and Treasurer.

B. BASIS OF ACCOUNTING

The District's policy is to prepare its financial statements on the accrual basis of accounting; consequently, revenue and the related assets are recognized when earned, and expenditures are recognized when the obligation is incurred.

C. INVENTORY

During the year ended December 31, 1998, the District instituted a perpetual inventory system for supplies. The supplies on hand at year end are valued at the lower of cost or market, on a first-in, first-out basis, and included in the December 31, 2016 and 2015, financial statements at \$ 284,558 and \$ 286,523, respectively.

D. FIXED ASSETS

All fixed assets are recorded at their original acquisition cost. Depreciation is provided in the financial statements utilizing the following estimated useful lives:

RURAL WATER DISTRICT NO. 3
Washington County, Oklahoma

NOTES TO THE FINANCIAL STATEMENTS
For the Year Ended December 31, 2016

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

	<u>Years</u>
Office Building	40
Water Plant & System	40
Furniture, Fixtures & Equipment	10
Machinery & Tools	10-15
Automotive	5
Office Equipment	5-15

A summary of the fixed asset accounts for the year ended December 31, 2016, is as follows:

	<u>Beginning</u> <u>Balance</u>	<u>Additions</u>	<u>Rtmts</u>	<u>Transfers</u>	<u>Ending</u> <u>Balance</u>
Building & Land	\$ 307,638				\$ 307,638
Machinery & Tools	363,546	77,956	65,843		375,659
Automotive	340,778				340,778
Furniture, Fixtures & Equipment	116,212				116,212
Lab Equipment	40,706				40,706
Water Treatment & Distribution System	<u>42,225,259</u>	<u>2,869,242</u>			<u>45,094,501</u>
Total	<u>\$ 43,394,139</u>	<u>2,947,198</u>	<u>65,843</u>	<u>-</u>	<u>\$ 46,275,494</u>

E. DEPOSITS AND INVESTMENTS

Custodial Credit Risk - Custodial credit risk related to deposits exists when the District holds deposits that are uninsured and uncollateralized with securities held by the pledging financial institution, or by its trust department or agent but not in the District's name, or collateralized without a written or approved collateral agreement. Exposure to custodial credit risk related to investments exists when the District holds investments that are uninsured and unregistered, with securities held by the counterparty or by its trust department or agent but not in the District's name. The District's policy for custodial credit risk is to secure its uninsured deposits with collateral. As of December 31, 2016, \$ 4,254,497 of the District's bank balances was exposed to custodial credit risk as follows:

Collateralized with securities held by the banks' trust department but not in the District's name	\$ 4,254,497
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Investment Credit Risk - The District has no investment policy that limits its investments choices other than the limitation of state law as follows:

RURAL WATER DISTRICT NO. 3
Washington County, Oklahoma

NOTES TO THE FINANCIAL STATEMENTS
For the Year Ended December 31, 2016

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

- a) Direct obligations of the U.S. Government, its agencies or 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 deposit or savings accounts that are either insured or secured with acceptable collateral with in-state financial institutions, and fully insured certificates of deposit or savings accounts in out-of-state financial institutions.
- c) With certain limitation, negotiable certificates of deposit, prime bankers acceptances, prime commercial paper, and repurchase agreements with certain limitations.
- d) County, municipal, or school district tax-supported debt obligation, bond or revenue anticipation notes, money judgments, or bond or revenue anticipation notes of public trusts whose beneficiary is a county, a 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.
- e) Money market funds regulated by the Securities and Exchange Commission and in which investments consist of the investments mentioned in the previous paragraphs a,b,c, and d.

Investment Interest Rate Risk – the District does not have a formal investment policy that limits investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates.

Concentration of Credit Risk – The District places no limit on the amount it may invest in any one issuer. Since the District has all investments in certificates of deposit, there is no concentration of investment credit risk exposure.

The deposits and investments held at December 31, 2016, are as follows:

Type	Maturity (Months)	Credit Rating	Market Value	Cost
Cash Deposits	N/A	N/A	1,554,744	1,554,744
Investments				
Certificates of Deposit	12	N/A	<u>3,150,000</u>	<u>3,150,000</u>
Total Deposits and Investments			<u>4,704,744</u>	<u>4,704,744</u>

RURAL WATER DISTRICT NO. 3
Washington County, Oklahoma

NOTES TO THE FINANCIAL STATEMENTS
For the Year Ended December 31, 2016

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

F. STATEMENT OF CASH FLOWS

For purposes of the Statement of Cash Flows, the District considers demand accounts, subject to withdrawal by check, and cash on hand, as cash or cash equivalents.

G. COMPENSATED ABSENCES

Employees must complete one (1) year of continuous service before earning two (2) weeks of vacation time per calendar year. Employees who have completed two (2) years through five (5) years of continuous service will earn three (3) weeks of vacation time per calendar year. Beginning in the sixth (6) year of continuous service, employees will earn four (4) weeks of vacation time per calendar year. Beginning in the twentieth (20) year of continuous service, employees will earn five (5) weeks of vacation time per calendar year. Vacation time is computed on a calendar year basis.

Vacation pay is vested, and thus paid upon retirement or separation (with two weeks' notice.) Vacation time is to be taken during the calendar year. Employees are required to utilize at least one-half of earned vacation time. The remaining vacation time will be paid at year end, and does not carry over to the next year without Board approval. The vacation accrued at December 31, 2016, was paid the first week of 2017.

All full- time employees are eligible for sick leave, after six months service, accrued at four hours per month (6 days per year.) Employees may accrue a maximum of 120 days of sick leave. Sick leave is not vested, and is thus lost upon separation.

H. ACCOUNTS RECEIVABLE

Accounts receivable at December 31, 2016 and 2015, represent charges for services provided to customers. The District utilizes the direct charge-off method of recognition of bad debts. Uncollectible accounts are an insignificant amount each year, thus there is no reserve for uncollectible accounts at December 31, 2016 and 2015.

I. INVESTMENTS

Investments classified in the financial statements, consist entirely of certificates of deposit whose original maturity term exceeds three months. Investments are carried at cost, which approximated fair value.

J. USE OF ESTIMATES

The preparation of financial statements in conformity with generally accepted accounting principles

RURAL WATER DISTRICT NO. 3
Washington County, Oklahoma

NOTES TO THE FINANCIAL STATEMENTS
For the Year Ended December 31, 2016

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period (such as estimated useful lives in determining depreciation expense.) Accordingly, actual results could differ from those estimates.

K. CASH AND CASH EQUIVALENTS

For the purpose of financial reporting, “cash and cash equivalents” include all demand and savings accounts and certificates of deposit or short-term investments with an original maturity of three months or less.

L. EQUITY CLASSIFICATION

Net position is displayed in three components:

- a. *Invested in capital assets, net of related debt* – consists of capital assets including restricted capital assets, net of accumulated depreciation and reduced by the outstanding balances of any bonds, mortgages, notes, or other borrowings that are attributable to the acquisition, construction, or improvements of those assets.
- b. *Restricted fund balance* – consists of net assets with constraints placed on the use either by an external group such as creditors, grantors, contributors, or laws and regulation of other governments, or by law through constitutional provisions or enabling legislation.
- c. *Unrestricted fund balance* – all other net assets that do not meet the definition of “restricted” or “invested in capital assets, net of related debt.”

The District applies restricted resources first when expenditures are incurred for purposes for which either restricted or unrestricted (committed, assigned, and unassigned) amounts are available. Similarly, within unrestricted fund balance, committed amounts are reduced first followed by assigned, and then unassigned amounts when expenditures are incurred for purposes for which amounts in any of the unrestricted fund balance classifications could be used.

M. BUDGETARY DATA

In accordance with the by-laws of the District, the Board of Directors prepare a budget, under the accrual basis of accounting.

NOTE 2: LONG-TERM DEBT

A. RURAL DEVELOPMENT LOANS

RURAL WATER DISTRICT NO. 3
Washington County, Oklahoma

NOTES TO THE FINANCIAL STATEMENTS
For the Year Ended December 31, 2016

NOTE 2: LONG-TERM DEBT (continued)

During a previous year, the District entered into a loan agreement with the Rural Utilities Service division of the USDA for \$ 4,800,000. The loan bears interest at 3.75 %, and requires monthly payments of \$ 19,344, beginning December 17, 2010, through November 17, 2050 (forty years.) The proceeds of the loan was utilized to acquire and construct water system improvements, namely the Caney River project. The total cost of the project was approximately \$ 6,300,000, thus the District provided the balance of the funds for the project (\$ 1,500,000.) The total balance outstanding under the loan as of December 31, 2016 and 2015, was \$ 4,286,239 and \$ 4,356,208, respectively.

This loan requires that a reserve be established in the amount of \$ 1,934.40 per month, until a balance of \$ 232,128 is maintained. During the year ended December 31, 2011, the District funded the reserve in full. The balance in the reserve account at December 31, 2016 and 2015, was \$ 238,372 and \$ 237,308, respectively.

During the year ended December 31, 2000, the District entered into two separate loan agreements with the Rural Economic and Community Development division of the USDA for \$ 724,200 and \$ 329,000. The loans bear interest at 5.5 %, and require monthly payments of \$ 3,737 and \$ 1,698, respectively, beginning November 4, 2000, through October 4, 2040. The proceeds of the loans were utilized to renovate and upgrade the existing north water treatment plant. The total cost of the project was approximately \$ 1,746,000. Thus, the District provided the balance of the funds for the project (approximately \$ 692,000.) The total balance outstanding under the loans as of December 31, 2016 and 2015, was approximately \$ 667,310 and \$ 694,998, respectively.

Each of the loans require that a reserve be established in the amount of \$ 373.70 per month for the \$ 724,200 loan, until a balance of \$ 44,844 is maintained, and in the amount of \$ 169.80 per month for the \$ 329,000 loan, until a balance of \$ 20,376 is maintained. As of December 31, 2016 and 2015, the balances in the reserve accounts were \$ 66,988 and \$ 66,689, respectively.

B. OKLAHOMA WATER RESOURCES BOARD LOAN

On December 14, 2009, the District entered into a Drinking Water SRF (State Revolving Fund) promissory note, and a Trust Indenture, with the Oklahoma Water Resources Board, for \$ 17,394,645, to fund the expansion of the north water treatment plant. The total cost of the project was estimated at \$ 17,832,782. Part of the funding (\$ 2,000,000) was from a grant from the EPA (Environmental Protection Agency) to the OWRB, under the Clean Water State Revolving Fund – American Recovery and Reinvestment Act of 2009 (ARRA.) In accordance with the agreement with the Oklahoma Water Resources Board, the \$ 2,000,000 funded through the American Recovery and Reinvestment Act of 2009, was forgiven, pending compliance with

RURAL WATER DISTRICT NO. 3
Washington County, Oklahoma

NOTES TO THE FINANCIAL STATEMENTS
For the Year Ended December 31, 2016

NOTE 2: LONG-TERM DEBT (continued)

all ARRA regulations. During the current year, the final \$ 555,562 was drawn under the loan agreement, and expended, and principal of \$ 323,449 was paid on the loan.

The loan requires monthly payments into a debt service fund, to be held by a trustee, who will make semi-annual payments of principal and interest to the Oklahoma Water Resources Board on March 15 and September 15, beginning no later than March 15, 2012. The loan carries interest at 2.99 %, and an administrative fee of 0.5 %, and will be payable in 360 months from the date of completion. Interest and the administrative fee began March 15, 2010. The balance outstanding under the loan at December 31, 2016 and 2015, was \$ 13,214,972 and \$ 12,982,859, respectively.

The loan is secured by the revenue derived from the operation of the system, on parity with the security interest securing the District's existing debt. OWRB has also taken a security interest in virtually all of the District's assets.

The District's schedule of rates or charges for the services of the system shall be sufficient to provide funds which, together with other revenues pledged under the loan, will provide net revenues available for debt service equal to at least 125 % of the maximum annual amount required for debt service on all obligations of the District. The District was in compliance with this requirement during the years ending December 31, 2016 and 2015.

C. CHANGES IN LONG-TERM DEBT

The following is a summary of changes in Long-term debt for the year ended December 31, 2016.

Loan	Jan. 1, 2016	Additions	Reductions	Dec. 31, 2016	Amount Due Within One Year
RECD Loan – 724,200	564,626		14,145	550,481	14,939
RECD Loan – 329,000	130,373		13,544	116,829	14,509
RUS Loan	4,356,208		69,969	4,286,239	69,550
OWRB Loan	<u>12,982,859</u>	<u>555,562</u>	<u>323,449</u>	<u>13,214,972</u>	<u>298,532</u>
Total	<u>18,034,066</u>	<u>555,562</u>	<u>421,107</u>	<u>18,168,521</u>	<u>397,530</u>

D. DEBT SERVICE REQUIREMENTS

The annual debt service requirements to maturity, including principal and interest, for the long-term debt as of December 31, 2016, is as follows:

RURAL WATER DISTRICT NO. 3
Washington County, Oklahoma

NOTES TO THE FINANCIAL STATEMENTS
For the Year Ended December 31, 2016

NOTE 2: LONG-TERM DEBT (continued)

For the Year Ended December 31,	\$ 724,200 RECD Loan		\$ 329,000 RECD Loan		\$ 4,800,000 RUS Loan		OWRB Loan	
	Prin	Int	Prin	Int	Prin	Int	Prin	Int
2017	14,939	29,906	14,509	5,867	72,209	159,920	336,331	464,601
2018	15,781	29,063	15,328	5,048	74,970	157,160	348,338	452,594
2019	16,671	28,173	16,192	4,184	77,836	154,294	360,773	440,159
2020	17,612	27,232	17,106	3,270	80,812	151,318	372,450	428,482
2021	18,605	26,239	18,071	2,305	83,901	148,228	386,947	413,985
2022-2026	110,003	114,217	35,623	1,549	470,147	690,500	2,150,940	1,853,722
2027-2031	144,731	79,489	-	-	567,161	593,487	2,563,423	1,441,239
2032-2036	190,424	33,796	-	-	684,192	476,455	3,054,597	950,065
2037-2041	21,715	347	-	-	825,373	335,275	3,641,173	363,489
2042-2046	-	-	-	-	995,686	164,962	-	-
2047-2051	-	-	-	-	353,952	11,261	-	-
Totals	\$ 550,481	368,462	116,829	22,223	4,286,239	3,042,860	13,214,972	6,808,336

NOTE 3: WATER PURCHASE CONTRACT

The District purchases water from Lake Oologah (an impoundment of the Verdigris River) the Skiatook Reservoir (an impoundment of Hominy Creek) and the City of Tulsa. In connection therewith, the District has contracts with the United States Corps of Engineers and the City of Tulsa, and permits to appropriate stream water, from the Verdigris River, Hominy Creek and the Caney River, with the Oklahoma Water Resources Board.

NOTE 4: INVESTMENTS

Investments as of December 31, 2016, are summarized as follows:

	<u>Cost</u>	<u>Fair Value</u>	<u>Carrying Value</u>
Unrestricted:			
Certificates of Deposit	\$ 3,150,000	3,150,000	3,150,000
	<u>\$ 3,150,000</u>	<u>3,150,000</u>	<u>3,150,000</u>

NOTE 5: FAIR VALUES OF FINANCIAL INSTRUMENTS

The following methods and assumptions were used by the Corporation in estimating its fair value disclosures for financial instruments.

RURAL WATER DISTRICT NO. 3
Washington County, Oklahoma

NOTES TO THE FINANCIAL STATEMENTS
For the Year Ended December 31, 2016

NOTE 5: FAIR VALUES OF FINANCIAL INSTRUMENTS (continued)

Cash, restricted cash, and notes payable: The carrying amounts reported in the statement of financial position approximate fair values because of the short term maturities of those instruments.

Investments: The fair values of investments are based on quoted market prices for those or similar investments.

The estimated fair values of the District's financial instruments at December 31, 2016, none of which are held for trading purposes, are as follows:

	<u>Carrying Amount</u>	<u>Fair Value</u>
Financial assets:		
Cash	\$ 827,716	\$ 827,716
Investments	3,150,000	3,150,000
Restricted Cash & Investments	727,028	727,028
Accounts Receivable	499,066	499,066
Financial liabilities:		
Notes Payable	18,168,521	18,168,521

NOTE 6: RETIREMENT PLAN

The District participates in a governmental Section 457 salary reduction plan. The plan is managed by Pension Solutions. All full time employees are eligible to participate. The District contributes 4 % of each employee's gross salary, monthly, to the plan. Employees are eligible to contribute a percentage of their compensation up to a maximum amount allowed by the plan, and if they contribute at least 2 %, then the District matches that up to 2 %. All District contributions become fully vested after 1 year of service.

NOTE 7: RESTRICTED NET ASSETS

Net assets were restricted for debt service at December 31, 2016 and 2015, as follows:

	<u>2016</u>	<u>2015</u>
RECD Reserve	\$ 46,061	\$ 45,856
RECD Reserve	20,926	20,833
RUS Reserve – Caney River	238,372	237,308
North Treatment Plant Project Fund	152	151
North Treatment Plant Construction Fund	187,625	1,525
North Treatment Plant Debt Service Fund	200,247	-
Interest Reserve	33,645	24,501
	<u>\$ 727,028</u>	<u>\$ 330,174</u>

RURAL WATER DISTRICT NO. 3
Washington County, Oklahoma

NOTES TO THE FINANCIAL STATEMENTS
For the Year Ended December 31, 2016

NOTE 7: RESTRICTED NET ASSETS (continued)

The RECD Reserves are maintained by the District, in separate interest bearing accounts, as discussed in Note 2.A. The North Treatment Plant Project Fund, the North Treatment Plant Construction Fund, and the Interest Reserve are held in separate interest bearing accounts at a local bank.

NOTE 8: LITIGATION

The District is a party to various legal proceedings that normally occur in the course of operations. The financial statements do not include accruals or provisions for loss contingencies that may result from these proceedings. While the outcome of the above noted proceedings cannot be predicted, due to the insurance coverage maintained by the District, the District feels that any settlement or judgment not covered by insurance would not have a material adverse effect on the financial condition of the District.

NOTE 9: SUBSEQUENT EVENTS

Subsequent events have been evaluated through April 24, 2017, which is the date the financial statements were available to be issued.

REQUIRED SUPPLEMENTARY INFORMATION

**RURAL WATER DISTRICT NO. 3
WASHINGTON COUNTY, OKLAHOMA**

**BUDGETARY COMPARISON SCHEDULE
FOR THE YEAR ENDED DECEMBER 31, 2016**

- UNAUDITED -

	Budgeted Amounts		Actual	Variance with
	Original	Final	Amounts	Final Budget Favorable (Unfavorable)
Beginning Budgetary Balance	\$ 3,780,499	\$ 3,780,499	\$ 3,878,090	\$ 97,591
Operating Revenues:				
Water sales	4,556,700	4,556,700	4,852,880	296,180
Memberships	340,000	340,000	351,500	11,500
Penalties, fees, service charges & misc	128,850	128,850	149,493	20,643
Total operating revenues	5,025,550	5,025,550	5,353,873	328,323
Operating Expenses:				
Salaries	881,815	881,815	851,956	29,859
Contract labor	23,000	23,000	4,753	18,247
Payroll taxes	68,500	68,500	67,534	966
Retirement	47,000	47,000	42,963	4,037
Automobile	115,000	115,000	34,429	80,571
Equipment expense	68,000	68,000	19,336	48,664
Chemicals	650,000	650,000	666,215	(16,215)
Subscriptions / License / Fees	45,000	45,000	35,838	9,162
Education	10,000	10,000	8,874	1,126
Supplies	375,000	375,000	371,194	3,806
Office expense	79,000	79,000	37,088	41,912
Postage	51,500	51,500	42,089	9,411
Professional fees	188,000	188,000	373,255	(185,255)
Line Extensions	120,000	120,000	23,941	96,059
Repair & maintenance	120,000	120,000	118,324	1,676
Telephone	14,000	14,000	13,367	633
Utilities	355,000	355,000	362,748	(7,748)
Travel	8,000	8,000	10,957	(2,957)
Uniforms	3,500	3,500	995	2,505
Water Purchased	25,000	25,000	8,169	16,831
Insurance	370,000	370,000	339,468	30,532
Taxes	50	50	50	-
Refunds	16,000	16,000	14,239	1,761
Total operating expenses	3,633,365	3,633,365	3,447,782	185,583
Non-operating (income) expenses:				
Caney River project	10,000	10,000	459,467	(449,467)
Caney River loan payments	232,128	232,128	232,128	-
N. Plant loan payments	800,932	800,932	892,977	(92,045)
FmHA loan payments	65,220	65,220	65,220	-
N. Plant upgrade	30,300	30,300	43,646	(13,346)
Miscellaneous income	(90,000)	(90,000)	(68,588)	(21,412)
Interest income	(15,000)	(15,000)	(14,384)	(616)
Total non-operating (income) expenses	1,033,580	1,033,580	1,610,466	(576,886)
Total Expenses	4,666,945	4,666,945	5,058,248	(391,303)
Ending Budgetary Balance	\$ 4,139,104	\$ 4,139,104	\$ 4,173,715	\$ 34,611

RURAL WATER DISTRICT NO. 3
Washington County, Oklahoma

NOTES TO BUDGETARY COMPARISON SCHEDULE
For the Year Ended December 31, 2016

Budgetary Information

In accordance with the by-laws of the District, the Board of Directors shall prepare an estimated budget for the coming year.

Basis of Accounting

The budget is prepared on the same accrual basis of accounting as applied to the basic financial statements. Revenues and the related assets are recognized when earned, and expenditures are recognized when the obligation is incurred.

OTHER SUPPLEMENTARY INFORMATION

**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 No. 3
Washington County, Oklahoma

We 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 Washington County Rural Water District No. 3 as of and for the years ended December 31, 2016 and 2015, and the related notes to the financial statements, which collectively comprise Washington County Rural Water District No. 3's basic financial statements and have issued our report thereon dated April 24, 2017.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered Washington County Rural Water District No. 3's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of Washington County Rural Water District No. 3's internal control. Accordingly, we do not express an opinion on the effectiveness of Washington County Rural Water District No. 3'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 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.

Our consideration of internal control 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 Washington County Rural Water District No. 3's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

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 entity'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 entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.



Bruce G. Luttrell, CPA, PC

April 24, 2017