

RURAL WATER DISTRICT NO. 3

Rooks County, Kansas

FINANCIAL STATEMENTS AND INDEPENDENT AUDITOR'S REPORT

December 31, 2012

RURAL WATER DISTRICT NO. 3

For the Year Ended December 31, 2012

BOARD OF DIRECTORS

James Ochampaugh – Chairman

Don Benoit – Vice-Chairman

Roger Comeau – Secretary/Treasurer

Jimmy Jackson

Norma Braun

Darren Rubottom

RURAL WATER DISTRICT NO. 3
Rooks County, Kansas
December 31, 2012

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INDEPENDENT AUDITOR'S REPORT

Board of Directors
Rural Water District No. 3
2335 Highway 183
Plainville, KS 67663

We have audited the accompanying summary statement of regulatory basis receipts, expenditures, and unencumbered cash balances of Rural Water District No. 3, Rooks County, Kansas as of and for the year ended December 31, 2012 and the related notes to the financial statement.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of this financial statement in accordance with the Kansas Municipal Audit and Accounting Guide as described in Note 1 to meet the financial reporting requirements of the State of Kansas. Management is also responsible for the design, implementation and maintenance of internal control relevant to the preparation and fair presentation of the financial statement that is free from material misstatement, whether due fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on the financial statement 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, and the Kansas Municipal Audit and Accounting Guide. Those standards require we plan and perform the audit to obtain reasonable assurance about whether the financial statement is free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statement. The procedures selected depend on auditor's judgment, including the assessment of the risks of material misstatement of the financial statement, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the District's preparation and fair presentation of the financial statement 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 District's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies use and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statement.

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

Basis for Adverse Opinion on U.S. Generally Accepted Accounting Principles

As described in Note 1 of the financial statement, the financial statement is prepared by the District to meet requirements of the State of Kansas on the basis of the financial reporting provisions of the Kansas Municipal Audit and Accounting Guide, which is a basis of accounting other than accounting principles generally accepted in the United States of America.

The effects on the financial statement of the variances between the regulatory basis of accounting described in Note 1 and accounting principles generally accepted in the United States of America, although not reasonably determinable, are presumed to be material.

Adverse Opinion on U.S. Generally Accepted Accounting Principles

In our opinion, because of the significance of the matter discussed in the “Basis for Adverse Opinion on U.S. Generally Accepted Accounting Principles” paragraph, the financial statement referred to above does not present fairly, in conformity with accounting principles generally accepted in the United States of America, the financial position of Rural Water District No. 3, Rooks County, Kansas, as of December 31, 2012, or changes in financial position and cash flows thereof for the year then ended.

Opinion on Regulatory Basis of Accounting

In our opinion, the financial statement referred to above presents fairly, in all material respects, the aggregate cash and unencumbered cash balance of the Rural Water District No. 3, Rooks County, Kansas as of December 31, 2012, and the aggregate receipts and expenditures for the year then ended in accordance with the financial reporting provisions of the Kansas Municipal Audit and Accounting Guide described in Note 1.

Report on Supplementary Information

Our audit was conducted for the purpose of forming an opinion on the fund summary statement of regulatory basis receipts, expenditures, and unencumbered cash balances (basic financial statement) as a whole. The individual fund schedules of regulatory receipts and expenditures (Schedule 1 as listed in the table of contents) are presented for analysis and are not a required part of the basic financial statement, however are required to be presented under the provisions of the Kansas Municipal Audit and Accounting Guide. The schedule of changes in capital assets (Schedule 2 as listed in the table of contents) are presented for analysis and are not a required part of the basic financial statement. The schedule of expenditures of federal awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is also not a required part of the financial statement. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statement. The information has been subjected to the auditing procedures applied in the audit of the basic financial statement and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statement or to the basic financial statement itself, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the basic financial statement as a whole, on the basis of accounting described in Note 1.

The 2011 actual column presented in the individual fund schedules of regulatory basis receipts and expenditures (Schedule 1 as listed in the table of contents) are presented for comparative analysis and are not a required part of the 2011 basic financial statement upon which we rendered an unqualified opinion dated October 29, 2012. The 2011 basic financial statement and our accompanying report are not presented herein, but are available in electronic form from the web site of the Kansas Department of Administration, Office of Management Analysis and Standards at the following link <http://da.ks.gov/ar/muniserv/>. Such 2011 comparative information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the 2011 basic financial statement. The 2011 comparative information was subjected to the auditing procedures applied in the audit of the 2011 basic financial statement and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the 2011 basic financial statement itself, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the 2011 comparative information is fairly stated in all material respects in relation to the 2011 basic financial statement as a whole, on the basis of accounting described in Note 1.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated August 6, 2013, on our consideration of Rural Water District No. 3, Rooks County, Kansas'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 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 No. 3, Rooks County, Kansas's internal control over financial reporting and compliance.

Mapes & Miller LLP

Certified Public Accountants

August 6, 2013
Stockton, Kansas

RURAL WATER DISTRICT NO. 3
Rooks County, Kansas

Statement 1

SUMMARY STATEMENT OF RECEIPTS, EXPENDITURES, AND UNENCUMBERED CASH
Regulatory Basis
For The Year Ended December 31, 2012

FUNDS	Beginning Unencumbered Cash Balance	Prior Year Cancelled Encumbrances	Receipts	Expenditures	Ending Unencumbered Cash Balance	Add Encumbrances and Accounts Payable	Ending Cash Balance
Governmental Type Funds:							
Capital Projects Fund:							
Water Improvement Fund	\$ (1,146,081) *	\$ 113,300	\$ 1,916,919	\$ 920,877	\$ (36,739) *	\$ 37,811	\$ 1,072
Business Fund:							
Water Utility Fund	400,853	-	386,777	295,012	492,618	21,329	513,947
Total Reporting Entity	<u>\$ (745,228)</u>	<u>\$ 113,300</u>	<u>\$ 2,303,696</u>	<u>\$ 1,215,889</u>	<u>\$ 455,879</u>	<u>\$ 59,140</u>	<u>\$ 515,019</u>

COMPOSITION OF CASH:

Stockton National Bank	
Stockton, Kansas	
Checking Account	\$ 274,695
Money Market Account	98,014
Money Market Account	36,709
Total Stockton National Bank	<u>409,418</u>
Midwest Community Bank	
Plainville, Kansas	
Super NOW Checking	1,072
Certificates of Deposit	104,529
Total Midwest Community Bank	<u>105,601</u>
Total Reporting Entity	<u>\$ 515,019</u>

* See Note 6, (Cash Basis Exceptions)

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

RURAL WATER DISTRICT NO.3
Rooks County, Kansas
NOTES TO THE FINANCIAL STATEMENT
For the Year Ended December 31, 2012

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Financial Reporting Entity

The District was incorporated on September 21, 1976. Rural Water District No. 3 was formed as a public body under the provisions of K.S.A. 82a-613 et seq and is exempt from federal and state income taxes. The purpose of the District is to acquire water and water rights, to build and acquire pipelines and other facilities; to operate the same for the purpose of furnishing water for domestic, garden, livestock and other purposes to owners and occupants of land located within the District, and to others as authorized by the by-laws.

Regulatory Basis Fund Types

General Fund – the chief operating fund. Used to account for all resources except those required to be accounted for in another fund.

Special Purpose Fund – used to account for the proceeds of specific tax levies and other specific revenue sources (other than Capital Project and tax levies for long-term debt) that are intended for specific purposes.

Bond and Interest Fund – used to account for the accumulation of resources, including tax levies, transfers from other funds and payment of general long-term debt.

Capital Project Fund – used to account for the debt proceeds and other financial resources to be used for the acquisition or construction of major capital facilities or equipment.

Business Fund – funds financed in whole or in part by fees charged to users of the goods or services (i.e. enterprise and internal serviced fund, etc.).

Trust Fund – funds used to report assets held in trust for the benefit of the municipal financial reporting entity (i.e. pension funds, investment trust funds, private purpose trust funds which benefit the municipal reporting entity, scholarship funds, etc.).

Agency Fund – funds used to report assets held by the municipal reporting entity in a purely custodial capacity (payroll clearing fund, county treasurer tax collection accounts, etc.).

Regulatory Basis of Accounting and Departure from Accounting Principles Generally Accepted in the United States of America

The Kansas Municipal Audit and Accounting Guide (KMAAG) regulatory basis of accounting involves the recognition of cash, cash equivalents, marketable investments, and certain accounts payable and encumbrance obligations to arrive at a net unencumbered cash and investments balance on a regulatory basis for each fund, and the reporting of changes in unencumbered cash and investments of a fund resulting from the difference in regulatory basis revenues and regulatory basis expenditures for the fiscal year. All recognized assets and liabilities are measured and reported at cost, unless they have been permanently impaired and have no future cash value or represent no future obligation against cash. The KMAAG regulatory basis does not recognize capital assets, long-term debt, accrued receivables and payables, or any other assets, liabilities or deferred inflows or outflows, other than those mentioned above.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Cont.)

Regulatory Basis of Accounting and Departure from Accounting Principles Generally Accepted in the United States of America (Cont.)

The District has approved a resolution that is in compliance with K.S.A. 75-1120a(c), waiving the requirement for application of generally accepted accounting principles and allowing the District to use the regulatory basis of accounting.

2. RESTRICTED CASH

Under the terms of a loan resolution security agreement between the District and USDA Farmers Home Administration the following business fund cash is restricted for specific purposes:

	<u>2012</u>	<u>2011</u>
Cash Restricted for Reserve	\$104,529	\$ 59,400
Cash Available for Operations	<u>409,418</u>	<u>348,367</u>
Total Cash	<u>\$513,947</u>	<u>\$407,767</u>

3. DEPOSITS AND INVESTMENTS

K.S.A. 9-1401 establishes the depositories which may be used by the District. The statute requires banks eligible to hold the District's funds have a main or branch bank in the county in which the District is located or in an adjoining county if such institution has been designated as an official depository, and the banks provide an acceptable rate of return on funds. In addition, K.S.A. 9-1402 requires the banks to pledge securities for deposits in excess of FDIC coverage. The District has no other policies that would further limit interest rate risk.

K.S.A. 12-1675 limits the District's investment of idle funds to time deposits, open accounts, and certificates of deposit with allowable financial institutions; U.S. government securities; temporary notes; no-fund warrants; repurchase agreements; and the Kansas Municipal Investment Pool. The District has no investment policy that would further limit its investment choices.

Concentration of credit risk. State statutes place no limit on the amount the District may invest in any one issuer as long as the investments are adequately secured under K.S.A. 9-1402 and 9-1405.

Custodial credit risk – deposits. Custodial credit risk is the risk that in the event of a bank failure, the District's deposits may not be returned to it. State statutes require the District's deposits in financial institutions to be entirely covered by federal depository insurance or by collateral held under a joint custody receipt issued by a bank within the State of Kansas, the Federal Reserve Bank of Kansas City, or the Federal Home Loan Bank of Topeka, except during designated "peak periods" when required coverage is 50%. All deposits were legally secured as of December 31, 2012.

At December 31, 2012, the District's carrying amount of deposits was \$515,019 and the bank balance was \$515,303. The bank balance was held by two banks resulting in a concentration of credit risk. Of the bank balance, \$355,600 was covered by federal depository insurance, \$159,703 was collateralized with securities held by the pledging financial institutions' agents in the District's name.

Custodial credit risk – investments. For an investment, this is the risk that, in the event of the failure of the issuer or counterparty, the District will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. State statutes require investments to be adequately secured.

4. COMPENSATED ABSENCES

The District provides two weeks of vacation and two weeks sick leave per year to the Operations Manager. No accrued benefits are paid upon termination.

5. LOAN AND RESERVE REQUIREMENTS

As shown in Note 11, on July 14, 2009 and April 17, 2012 the District entered into promissory note agreements with USDA Farmers Home Administration to borrow \$1,153,000 and \$942,000, respectively for the cost of construction of a water supply system and improvements. These agreements are secured by a real estate mortgage of the water system assets and operations.

Provisions of the loan agreements make the following requirements:

As required by the July 14, 2009 agreement each month the District shall transfer \$495 into a Reserve Account until such account accumulated to \$59,400. As shown in Note 2, this requirement has been met.

As required by the April 17, 2012 agreement each month the District shall transfer \$495 into a Reserve Account until such account accumulated to \$59,345. As shown in Note 2, \$45,129 of this requirement has been met.

6. STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY

Compliance with Kansas Statutes

K.S.A. 10-1113 states that expenditures are to be made in compliance with the cash basis law which requires that no indebtedness be created for a fund in excess of available monies in that fund. The fund with a negative cash balance was as follows:

Water Improvement Fund

The fund mentioned above is a capital project fund where the expenditures are incurred by the District and then reimbursed by a USDA Rural Development loan and grant. K.S.A. 12-1664 allows the District to temporarily finance the project from current funds until the federal funds are received.

7. CAPITAL PROJECTS

	Project Authorization	Cash Disbursements and Accounts Payable To Date
Water Improvement Project	<u>\$ 1,905,000</u>	<u>\$ 1,882,098</u>

8. RISK MANAGEMENT

Rural Water District No. 3 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 disaster. The District continues to carry insurance coverage to cover these risks. The District has had no significant reduction in insurance coverage from prior years. Settled claims resulting from these risks have not exceeded commercial insurance coverage for each of the past three years

9. SUBSEQUENT EVENTS

Management has evaluated the effects of the financial statements of subsequent events occurring through August 6, 2013 which is the date of which the financial statements were available to be issued.

10. LONG-TERM DEBT

Changes in long-term debt for the District for the year ended December 31, 2012, were as follows:

Issue	Interest Rates	Date of Issue	Amount of Issue	Date of Final Maturity	Balance Beginning of Year	Additions	Reductions/ Payments	Balance End of Year	Interest Paid
Loan Agreements									
High Plains Farm Credit	4.240%	06/01/11	900,000	08/01/12	\$ 701,644	\$ 191,639	\$ 893,283	\$ -	\$ 18,890
Farmers Home Administration	4.125%	07/14/09	1,153,000	07/14/49	1,122,963	-	12,865	1,110,098	46,079
Farmers Home Administration	2.750%	04/17/12	942,000	04/17/52	-	942,000	8,680	933,320	17,248
Total Loan Agreements					<u>\$ 1,824,607</u>	<u>\$ 1,133,639</u>	<u>\$ 914,828</u>	<u>\$ 2,043,418</u>	<u>\$ 82,217</u>

Current maturities of long-term debt and interest for the next five years and in five year increments through maturity are as follows:

	2013	2014	2015	2016	2017	2018-2022	2023-2027
PRINCIPAL							
Loan Agreements	\$ 26,768	\$ 27,703	\$ 28,673	\$ 29,678	\$ 30,720	\$ 170,611	\$ 203,023
INTEREST							
Loan Agreements	71,068	70,133	69,163	68,158	67,116	318,569	286,157
Total Principal & Interest	<u>\$ 97,836</u>	<u>\$ 489,180</u>	<u>\$ 489,180</u>				
	2028-2032	2033-2037	2038-2042	2043-2047	2048-2052	Total	
PRINCIPAL							
Loan Agreements	\$ 241,875	\$ 288,495	\$ 344,495	\$ 411,834	\$ 239,543	\$ 2,043,418	
INTEREST							
Loan Agreements	247,305	200,685	144,685	77,346	12,493	1,632,878	
Total Principal & Interest	<u>\$ 489,180</u>	<u>\$ 489,180</u>	<u>\$ 489,180</u>	<u>\$ 489,180</u>	<u>\$ 252,036</u>	<u>\$ 3,676,296</u>	

RURAL WATER DISTRICT NO. 3
REGULATORY-REQUIRED
SUPPLEMENTARY INFORMATION
FOR THE YEAR ENDED DECEMBER 31, 2012

RURAL WATER DISTRICT NO. 3
Rooks County, Kansas
CAPITAL PROJECT FUND
SCHEDULE OF RECEIPTS AND EXPENDITURES

Schedule 1-1

Regulatory Basis
For The Year Ended December 31, 2012
(With Comparative Amounts for the Prior Year Ended December 31, 2011)

WATER IMPROVEMENT FUND

	2012	2011
Cash Receipts:		
Miscellaneous Income	\$ 58	\$ 67
Interest Income	5	12
Loan Proceeds	191,639	701,644
USDA Grant Proceeds	783,217	-
USDA Loan Proceeds	942,000	-
Total Cash Receipts	1,916,919	701,723
Expenditures:		
Construction Costs	6,874	1,524,459
Engineering Fees	-	322,324
Legal Fees	1,815	400
Publications	-	621
Wire Fee	15	
Interim Financing Interest Expense	18,890	-
Interim Financing Principal Payment	893,283	-
Total Expenditures	920,877	1,847,804
Cash Receipts Over (Under) Expenditures	996,042	(1,146,081)
Unencumbered Cash, Beginning	(1,146,081)	-
Cancelled Prior Year Encumbrances	113,300	-
Unencumbered Cash, Ending	\$ (36,739)	\$ (1,146,081)

RURAL WATER DISTRICT NO. 3
Rooks County, Kansas
BUSINESS FUND
SCHEDULE OF RECEIPTS AND EXPENDITURES
Regulatory Basis
For The Year Ended December 31, 2012
(With Comparative Amounts for the Prior Year Ended December 31, 2011)

Schedule 1-2

WATER UTILITY FUND

	2012	2011
Cash Receipts:		
Operating Receipts		
Water Sales	\$ 224,503	\$ 172,083
Monthly Meter Fees	112,398	104,478
Late Charges and Other Revenue	8,285	5,569
Back Flow Preventer and Flow Control Charges	220	275
Other Income	11,425	4,348
Total Operating Receipts	356,831	286,753
Non-Operating Income		
Interest Income	1,946	3,485
Member Investments	28,000	20,000
Total Non-Operating Receipts	29,946	23,485
Total Cash Receipts	386,777	310,238
Expenditures:		
Operator/Manager Salary	46,957	44,367
Secretary/Bookkeeper Salary	17,629	17,702
Director's Fees	9,705	9,908
Payroll Taxes	5,104	5,196
Auditing and Accounting	25,924	505
Bank Charges	-	8
Legal Fees	180	684
Lab Fees	3,772	399
Utilities	22,381	19,646
Operating Supplies, Maintenance and Repairs	41,518	18,446
Telephone and Internet	2,362	2,321
Postage	1,189	1,303
Office Supplies	2,972	2,638
Insurance	8,261	8,646
Vehicle Expense	12,682	12,888
Licenses, Dues and Subscriptions	323	262
Meeting Expense	1,778	1,348
Miscellaneous	1,254	745
USDA Interest Expense	63,328	46,598
USDA Loan Principal Payments	21,545	12,346
Zurich Project Expense		
Engineering Fees	-	22,000
Legal Fees	-	1,633
Easements	-	1,653
Miscellaneous	2,468	-
Capital Asset Purchases	3,680	4,010
Total Expenditures	295,012	235,252
Cash Receipts Over (Under) Expenditures	91,765	74,986
Unencumbered Cash, Beginning	400,853	267,191
Cancelled Prior Year Encumbrances	-	58,676
Unencumbered Cash, Ending	\$ 492,618	\$ 400,853

SUPPLEMENTARY INFORMATION
FOR THE YEAR ENDED DECEMBER 31, 2012

RURAL WATER DISTRICT NO. 3
Rooks County, Kansas

Schedule 2

SCHEDULE OF CHANGES IN CAPITAL ASSETS
December 31, 2012

	Capital Assets 1/1/2012	Additions	Deductions	Capital Assets 12/31/2012
Equipment and Tools	\$ 104	\$ -	\$ -	\$ 104
Pumps, Treatment Equipment and Facilities	364,678	139,412	-	504,090
Wells	38,712	22,736	-	61,448
Transmission Lines and Storage Facilities	3,622,859	1,361,459	-	4,984,318
Easements	64,256	-	-	64,256
Office Equipment and Furniture	7,141	-	-	7,141
Vehicles	23,351	-	-	23,351
Buildings	255,705	307,934	-	563,639
Construction in Progress	1,934,287	-	1,934,287	-
Total Capital Assets	6,311,093	1,831,541	1,934,287	6,208,347
Less: Accumulated Depreciation	2,052,245	135,855	-	2,188,100
Net Capital Assets	<u>\$ 4,258,848</u>			<u>\$ 4,020,247</u>

Capital assets are recorded above at cost and are being depreciated over their estimated useful lives by use of the straight-line method. The following table reflects depreciation expense for 2012:

	Estimated Useful Life	
Equipment and Tools	10 years	\$ -
Pumps, Treatment Equipment and Facilities	10 years	5,169
Wells	30 years	820
Transmission Lines and Storage Facilities	36-40 years	119,934
Office Equipment and Furniture	5-10 years	100
Vehicles	5 years	390
Buildings	39 years	9,442
Total Depreciation		<u>\$ 135,855</u>

SINGLE AUDIT SECTION



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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
2335 Highway 183
Plainville, KS 67663

We have audited, in accordance with the auditing standards generally accepted in the United States of America, the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, and the Kansas Municipal Audit and Accounting Guide, the accompanying summary statement of regulatory basis receipts, expenditures, and unencumbered cash balances of Rural Water District No. 3, Rooks County, Kansas, as of and for the year ended December 31, 2012, and the related notes to the financial statement, and have issued our report thereon dated August 6, 2013.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statement, we considered Rural Water District No. 3, Rooks County, Kansas'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 opinion on the financial statement, but not for the purpose of expressing an opinion on the effectiveness of Rural Water District No. 3, Rooks County, Kansas's internal control. Accordingly, we do not express an opinion on the effectiveness of Rural Water District No. 3, Rooks County, Kansas'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.

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 and therefore, material weaknesses or significant deficiencies may exist that were not identified. 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. We did identify certain deficiencies in internal control, described in the accompanying schedule of findings and questioned costs that we consider to be significant deficiencies. 2012-1.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Rural Water District No. 3, Rooks County, Kansas's financial statement is free from 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*.

Rural Water District No. 3's Response to Findings

Rural Water District No. 3's response to the findings identified in our audit is described in the accompanying schedule of findings and questioned costs. Rural Water District No. 3's response was not subjected to the auditing procedures applied in the audit of the financial statement and, accordingly, we express no opinion on it.

Purpose of this Report

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

Mapes & Miller LLP

Certified Public Accountants

August 6, 2013
Stockton, Kansas



MAPES & MILLER LLP

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INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE FOR EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE REQUIRED BY CIRCULAR A-133

Board of Directors
Rural Water District No. 3
2335 Highway 183
Plainville, KS 67663

Report on Compliance for Each Major Federal Program

We have audited Rural Water District No. 3, Rooks County, Kansas's compliance with the types of compliance requirements described in the *OMB Circular A-133 Compliance Supplement* that could have a direct and material effect on each of Rural Water District No. 3, Rooks County, Kansas's major federal programs for the year ended December 31, 2012. Rural Water District No. 3, Rooks County, Kansas's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs.

Management's Responsibility

Management is responsible for compliance with the requirements of laws, regulations, contracts, and grants applicable to its major federal programs.

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for each of Rural Water District No. 3, Rooks County, Kansas's major federal programs based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about Rural Water District No. 3, Rooks County, Kansas's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

We believe that our audit provides a reasonable basis for our opinion on compliance for each major federal program. However, our audit does not provide a legal determination on Rural Water District No. 3, Rooks County, Kansas's compliance.

Opinion on Each Major Federal Program

In our opinion, Rural Water District No. 3, Rooks County, Kansas complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended December 31, 2012.

Report on Internal Control Over Compliance

Management of Rural Water District No. 3, Rooks County, Kansas is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered Rural Water District No. 3, Rooks County, Kansas's internal control over compliance with the types of requirements that could have a direct and material effect on a major federal program to determine the auditing procedures that are appropriate for the purpose of expressing an opinion on compliance for each major federal program and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of Rural Water District No. 3, Rooks County, Kansas's internal control over compliance.

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. A *material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. A *significant deficiency in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance

Our consideration of internal control over compliance 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. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of OMB Circular A-133. Accordingly, this report is not suitable for any other purpose.

Mapes & Miller LLP

Certified Public Accountants

Stockton, Kansas
August 6, 2013

RURAL WATER DISTRICT NO. 3
Rooks County, Kansas

Schedule 3

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
For the Year Ended December 31, 2012

Federal Grantor/Pass-Through Grantor/ Program Title	Federal CFDA Number	Federal Expenditures
U.S. Department of Agriculture Water and Waste Disposal Systems for Rural Communities - ARRA	10.781	\$ 1,066,874
Total Expenditures of Federal Awards		<u>\$ 1,066,874</u>

NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
For the Year Ended December 31, 2012

BASIS OF PRESENTATION

The accompanying Schedule of Expenditures of Federal Awards includes the federal loan and grant activity of the Rural Water District No. 3, Rooks County, Kansas and is presented on the cash basis of accounting. Therefore, amounts presented in this schedule may differ from amounts presented in, or use in the presentation of the basic financial statements.

**RURAL WATER DISTRICT NO. 3
Rooks County, Kansas**

Schedule 4

**SCHEDULE OF FINDINGS AND QUESTIONED COSTS
For the Year Ended December 31, 2012**

SECTION 1 – SUMMARY OF AUDITORS’ RESULTS

FINANCIAL STATEMENTS

Type of auditors’ report issued:

In accordance with the regulatory basis of accounting described in Note 1 to the financial statements.

Unqualified

Internal control over financial reporting:

- Material weaknesses identified? __ Yes x No
- Significant deficiencies identified that are not considered to be material weaknesses? x Yes __ No
- Noncompliance material to financial statements noted? __ Yes x No

FEDERAL AWARDS

Internal control over major programs:

- Material weaknesses identified? __ Yes x No
- Significant deficiencies identified that are not considered to be material weaknesses? __ Yes x No

Type of auditors’ report issued on compliance for major programs:

Unqualified

Any audit findings disclosed that are required to be reported in accordance with section 510(a) of OMB *Circular A-133*?

__ Yes x No

Identification of major programs:

<u>CFDA NUMBER</u>	<u>NAME OF FEDERAL PROGRAM</u>
10.781	Water and Waste Disposal Systems for Rural Communities - ARRA

Dollar threshold used to distinguish between type A and type B programs:

\$300,000

Auditee qualified as low-risk auditee?

__ Yes x No

RURAL WATER DISTRICT NO. 3
Rooks County, Kansas

Schedule 4
(Cont.)

SCHEDULE OF FINDINGS AND QUESTIONED COSTS
For the Year Ended December 31, 2012

SECTION II – FINANCIAL STATEMENT FINDINGS

2012-1 Segregation of Duties

Condition: The same employee performs some accounting duties and procedures that should be segregated.

Criteria: Segregation of duties should be maintained to strengthen internal control over accounting and compliance functions.

Cause: Because the entity is small, management does not feel it is feasible to hire more staff.

Effect: Lack of segregation of duties increases the risk of errors and noncompliance occurring and not being detected in a timely manner.

Recommendations: Duties of key financial and compliance personnel should be evaluated to determine if duties could be segregated.

Views of Responsible Officials and Planned Corrective Actions: We concur with the recommendation. However, the size of the entity does not make it practical to have sufficient number of employees to achieve the optimum level of internal control.

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

Questioned
Costs

Department of Agriculture - CFDA No. 10.781 Water and Waste Disposal Systems For
Rural Communities - ARRA - For the Year Ended December 31, 2012

1. Internal Control Findings

None found.

2. Compliance Findings

None found.

RURAL WATER DISTRICT NO. 3
Rooks County, Kansas

Schedule 4
(Cont.)

SCHEDULE OF FINDINGS AND QUESTIONED COSTS
For the Year Ended December 31, 2012

SECTION IV – SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS

Department of Agriculture - CFDA No. 10.781 Water and Waste Disposal Systems For Rural Communities - ARRA

2011-1 Segregation of Duties

Condition: The same employee performs some accounting duties and procedures that should be segregated.

Recommendations: Duties of key financial and compliance personnel should be evaluated to determine if duties could be segregated.

Current Status: The size of the entity does not make it practical to have sufficient number of employees to achieve the optimum level of internal control.

2011-2 Financial Statement Preparation

Condition: Management does not have the qualifications and training necessary to prepare the financial statements which would include the related footnote disclosures.

Recommendations: Management would need to attend training classes and annual continuing education classes to gain an understanding on proper and complete preparation of the financial statements and footnote disclosures and to be aware of all of the current accounting standards by purchasing annual accounting subscriptions.

Current Status: Management, through the completion of disclosure checklists and having successive years of single audits and regulatory basis audits, feels it could prepare the financial statements and note disclosures.

2011-3 Segregation of Duties

Condition: The same employee performs some accounting duties and procedures that should be segregated.

Recommendations: Duties of key financial and compliance personnel should be evaluated to determine if duties could be segregated.

Current Status: USDA Rural Development, the Districts' engineer and the Districts' board of directors were all involved with the approval of all expenditures to be paid out of the federal program. This involvement by the mentioned parties overcomes the segregation of duties finding for the federal award.