

SOUTH LOGAN WATER ASSOCIATION, INC.
FINANCIAL STATEMENTS
FOR THE YEARS ENDED DECEMBER 31, 2016 AND 2015

**SOUTH LOGAN WATER ASSOCIATION, INC.
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INDEPENDENT AUDITORS' REPORT

Commissioners
South Logan Water Association, Inc.
Adairville, Kentucky

Report on the Financial Statements

We have audited the accompanying financial statements of South Logan Water Association, Inc. (a nonprofit organization), which comprise the statements of financial position as of December 31, 2016 and 2015, and the related statements of activities and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with 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.

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits 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 opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of South Logan Water Association, Inc. as of December 31, 2016 and 2015, and the changes in its net assets and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated March 27, 2017, on our consideration of South Logan Water Association, Inc.'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 South Logan Water Association, Inc.'s internal control over financial reporting and compliance.

Respectfully submitted,

Buckles, Travis & Hart, PLLC

Buckles, Travis & Hart, PLLC
Certified Public Accountants
Leitchfield, Kentucky
March 27, 2017

SOUTH LOGAN WATER ASSOCIATION, INC.
STATEMENTS OF FINANCIAL POSITION
DECEMBER 31, 2016 AND 2015

	DECEMBER 31,	
	2016	2015
ASSETS		
CURRENT ASSETS		
Cash	\$ 242,139	\$ 262,719
Restricted cash	492,708	571,627
Accounts receivable (net of allowance of \$45,290 for 2016 and \$43,305 for 2015)	130,625	121,916
Inventory	73,512	54,923
Prepaid expenses	4,123	5,291
TOTAL CURRENT ASSETS	943,107	1,016,476
 UTILITY PLANT, net	 4,957,679	 5,006,286
 OTHER ASSETS	 45	 45
TOTAL ASSETS	\$ 5,900,831	\$ 6,022,807
 LIABILITIES AND NET ASSETS		
CURRENT LIABILITIES		
Accounts payable	\$ 64,917	\$ 51,112
Current portion of long-term debt	53,862	51,797
Customer deposits	104,032	101,793
Accrued liabilities	6,107	7,090
Accrued interest	52,096	53,233
Unearned revenue	933	0
TOTAL CURRENT LIABILITIES	281,947	265,025
 LONG-TERM DEBT, net of current portion	 2,505,066	 2,560,730
TOTAL LIABILITIES	2,787,013	2,825,755
 NET ASSETS		
Contributions in aid of construction	2,174,894	2,163,499
Net assets	938,924	1,033,553
TOTAL NET ASSETS	3,113,818	3,197,052
TOTAL LIABILITIES AND NET ASSETS	\$ 5,900,831	\$ 6,022,807

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

SOUTH LOGAN WATER ASSOCIATION, INC.
STATEMENTS OF ACTIVITIES
FOR THE YEARS ENDED DECEMBER 31, 2016 AND 2015

	DECEMBER 31,	
	2016	2015
UNRESTRICTED REVENUES, GAINS AND OTHER SUPPORT		
Water service	\$1,181,461	\$1,181,975
Late charges	17,250	16,915
Other	18,805	12,202
TOTAL UNRESTRICTED REVENUES, GAINS AND OTHER SUPPORT	1,217,516	1,211,092
OPERATING EXPENSES		
Purchased water	607,321	589,608
Payroll	190,095	177,889
Payroll taxes	15,824	15,022
Directors fees	2,600	3,000
Retirement expense	550	909
Transmission and distribution	86,565	43,541
Repairs and maintenance	13,404	13,134
Vehicle expense	14,305	20,701
Contractual services	1,617	1,570
Utilities and telephone	18,383	16,348
Professional fees	10,998	8,050
Insurance	28,051	28,187
Taxes and licenses	1,207	2,908
Office supplies	42,499	37,439
Water tests	4,711	3,772
Depreciation	159,708	157,170
Bad debt	2,005	4,823
Miscellaneous	7,589	4,399
Advertising	1,323	2,821
TOTAL OPERATING EXPENSES	1,208,755	1,131,291
INCOME (LOSS) FROM OPERATIONS	8,761	79,801
NON-OPERATING GAINS (LOSSES)		
Interest income	1,281	1,286
Gain (loss) on sale of assets	0	10,000
PSC taxes	(2,351)	(2,272)
Interest expense	(95,818)	(97,678)
Line relocation revenue	169,187	0
Line relocation expense	(175,689)	0
TOTAL NON-OPERATING GAINS (LOSSES)	(103,390)	(88,664)
EXCESS OF REVENUES OVER EXPENSES AND INCREASE (DECREASE) IN UNRESTRICTED NET ASSETS	\$ (94,629)	\$ (8,863)

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

**SOUTH LOGAN WATER ASSOCIATION, INC.
STATEMENTS OF CHANGES IN NET ASSETS
FOR THE YEARS ENDED DECEMBER 31, 2016 AND 2015**

	<u>NET ASSETS</u>	<u>CONTRIBUTIONS IN AID OF CONSTRUCTION</u>	<u>TOTAL</u>
BALANCE, JANUARY 1, 2015	\$ 1,042,416	\$ 2,169,764	\$ 3,212,180
Net income	(8,863)	0	(8,863)
Capital contributions-KIA and Rural			
Development grants	0	46,080	46,080
Depreciation on assets acquired by grant	0	(61,195)	(61,195)
Capital contributions-Tap on fees	0	8,850	8,850
BALANCE, DECEMBER 31, 2015	1,033,553	2,163,499	3,197,052
Net income	(94,629)	0	(94,629)
Capital contributions-KIA and Rural			
Development grants	0	58,696	58,696
Depreciation on assets acquired by grant	0	(66,301)	(66,301)
Capital contributions-Tap on fees	0	19,000	19,000
BALANCE, DECEMBER 31, 2016	<u>\$ 938,924</u>	<u>\$ 2,174,894</u>	<u>\$ 3,113,818</u>

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

**SOUTH LOGAN WATER ASSOCIATION, INC.
STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2016 AND 2015**

	DECEMBER 31, 2016	2015
CASH FLOWS FROM OPERATING ACTIVITIES		
Operating income (loss)	\$ (94,629)	\$ (8,863)
Adjustments to reconcile net operating income (loss) to net cash provided (used) by operating activities:		
Depreciation expense	159,708	157,170
(Gain) loss on sale of assets	0	(10,000)
(Increase) decrease in restricted cash	78,919	10,198
Net (increase) decrease in accounts receivable	(8,709)	(3,263)
Net (increase) decrease in inventory	(18,589)	9,257
Net (increase) decrease in prepaid expenses	1,168	(84)
Net increase (decrease) in accounts payable	13,805	45,312
Net increase (decrease) in customer deposits	2,239	2,694
Net increase (decrease) in accrued interest	(1,137)	(846)
Net increase (decrease) in accrued liabilities	(983)	(3,648)
Net increase (decrease) in unearned revenue	933	0
NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES	132,725	197,927
CASH FLOWS FROM FINANCING ACTIVITIES		
Payments on long-term debt	(53,599)	(33,729)
Acquisition of utility plant	(177,402)	(72,217)
Proceeds from sale of assets	0	10,000
Contributions in aid of construction from customers and grants	77,696	54,930
Miscellaneous receipts (payments)	0	(1)
NET CASH PROVIDED (USED) BY FINANCING ACTIVITIES	(153,305)	(41,017)
CASH FLOWS FROM INVESTING ACTIVITIES		
NET CASH PROVIDED (USED) BY INVESTING ACTIVITIES	0	0
NET INCREASE (DECREASE) IN CASH	(20,580)	156,910
BALANCES-BEGINNING OF YEAR	262,719	105,809
BALANCES-END OF YEAR	\$ 242,139	\$ 262,719
SUPPLEMENTAL DISCLOSURE		
Interest paid	\$ 96,955	\$ 99,719

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

SOUTH LOGAN WATER ASSOCIATION, INC.
NOTES TO THE FINANCIAL STATEMENTS
DECEMBER 31, 2016 AND 2015

NOTE A – DESCRIPTION OF SIGNIFICANT ACCOUNTING POLICIES

1. Nature of Operations

The South Logan Water Association, Inc. (the “Association”) was chartered on October 6, 1971. It is a distributor of water under the authority of the Public Service Commission of Kentucky. The Association provides water service to customers in a sector of Logan County, Kentucky.

2. Basis of Presentation

The accompanying financial statements of the Association are presented on the accrual basis of accounting.

3. Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities 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. Actual results could differ from those estimates.

4. Accounts Receivable and Other Receivables

Customer accounts receivable and other receivables are stated at the amount billed to customers. The Association’s operating revenues are recognized on the basis of cycle billings rendered monthly. Accounts receivable are due on the 20th of each month. Accounts unpaid 10 days after the due date are considered delinquent and service is disconnected. An allowance is established for delinquent receivables and they are written off when deemed uncollectible. New service is denied until all outstanding balances have been settled.

5. Inventory

Inventory consists of operating supplies and is stated at the lower of cost or market. Cost is determined by the first-in, first-out method.

6. Utility Plant

Expenditures for utility plant with an original cost of \$500 or more are capitalized at cost, while maintenance and repairs are charged to operations when incurred. Depreciation is recorded on the straight-line method over the estimated useful lives of the assets. Interest costs for fixed asset construction are capitalized.

SOUTH LOGAN WATER ASSOCIATION, INC.
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2016 AND 2015

NOTE A – DESCRIPTION OF SIGNIFICANT ACCOUNTING POLICIES (CONCLUDED)

7. Contributions in Aid of Construction

Beginning January 1, 1997, the Association changed its method of accounting for tap on fees. Prior to 1997, tap on fees were recorded as other revenue. Effective January 1, 1997, tap on fees are recorded as contributions in aid of construction. The cumulative effect on retained earnings at the beginning of 1997 is undeterminable.

Federal and state capital grants and construction contributions are recorded as capital contributions when received.

8. Income Taxes

The Association may qualify for an exemption from federal income tax under the Internal Revenue Code as a not-for-profit organization. The Association has not filed for an exempt status with the Internal Revenue Service. See Note D.

9. Concentrations of Credit Risk

At year-end, the carrying amount of the Association's cash and investments was \$734,847 and the bank balance was \$740,706. Of the total bank balance, \$250,000 was covered by federal depository insurance and the remaining balance of \$490,706 would require collateralization. As of December 31, 2016, \$691,284 was pledged with securities held by the pledging banks' trust department but not in the Association's name.

10. Cash and Cash Equivalents

The Association has defined cash and cash equivalents to include all highly liquid investments (including restricted assets) with a maturity of three months or less when purchased to be cash equivalents.

11. Impairment of Long-Lived Assets

The Association reviews its property for impairment whenever events or changes in circumstances indicate that the carrying value of an asset may not be recoverable. For assets held and used, if the undiscounted cash flows estimated to be generated by those assets are less than the carrying amounts of the asset, an impairment loss has occurred. The amount of the impairment loss is equal to the excess of the asset's carrying value over its estimated fair value. No impairment loss has been recognized during the years ended December 31, 2016 and 2015.

**SOUTH LOGAN WATER ASSOCIATION, INC.
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2016 AND 2015**

NOTE B – RESTRICTED CASH

Restricted cash consists of the following at December 31, 2016 and 2015:

	<u>2016</u>	<u>2015</u>
System improvement project construction funds	\$ 159,905	\$ 261,503
Customer deposits	139,866	136,325
Debt service-Bonds	50,512	49,130
Cash reserves-Bonds	130,925	124,669
Short-lived assets	11,500	0
	<u>\$ 492,708</u>	<u>\$ 571,627</u>

The Association’s bond agreements require certain debt and capital reserves. Capital project funds are restricted for the expansion project. Customer deposits are refundable after service has been terminated.

NOTE C – UTILITY PLANT

A summary of utility plant activity at December 31, 2016 and 2015 is as follows:

	<u>2016</u>	<u>2015</u>
Land and land improvements	\$ 36,719	\$ 36,719
Pumping equipment	44,627	44,627
Distribution reservoirs and standpipes	630,077	630,077
Transmission and distribution mains	6,358,345	6,221,216
Services	42,701	42,701
Meters and installations	631,287	718,182
Hydrants	68,328	68,328
Communication equipment	19,341	19,341
Vehicles	180,695	180,695
Building and improvements	94,685	94,685
Office equipment	39,076	37,176
Construction in progress	0	0
	<u>8,145,881</u>	<u>8,093,747</u>
Less: Accumulated depreciation	<u>(3,188,202)</u>	<u>(3,087,461)</u>
Utility Plant, Net	<u>\$4,957,679</u>	<u>\$5,006,286</u>

NOTE D – CONTINGENCY

The Association has been operating as a tax exempt, not-for-profit organization since its inception. However, no formal application has been made with the Internal Revenue Service to receive official tax exempt status. No provision has been made in the accompanying financial statements to reflect any uncertainty of this status, including potential income taxes.

SOUTH LOGAN WATER ASSOCIATION, INC.
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2016 AND 2015

NOTE E – LONG-TERM DEBT

Current year long-term debt activity is as follows:

<u>Description</u>	<u>Beginning Balance</u>	<u>Increases</u>	<u>Decreases</u>	<u>Ending Balance</u>	<u>Due Within One Year</u>
Note payable – FmHA, payable in annual installments of principal and interest of \$24,655, interest at 5.00%, maturing May 2033, secured by assignment and pledge of revenue	\$ 258,336	\$ 0	\$ 11,738	\$ 246,598	\$ 10,765
Note payable – FmHA, payable in annual installments of \$33,594, interest at 4.875%, maturing February 2038, secured by assignment and pledge of revenue	457,057	0	11,312	445,745	11,794
Note payable – Rural Development, payable in annual installments of principal and interest, interest at 4.125%, maturing September 2045, secured by substantially all assets and revenues of the Association	697,134	0	12,249	684,885	12,500
Note payable – Rural Development, payable in annual installments of \$51,300 principal and interest, interest at 2.75%, maturing September 2053, secured by assignment and pledge of revenue	1,200,000	0	18,300	1,181,700	18,803
	<u>\$ 2,612,527</u>	<u>\$ 0</u>	<u>\$ 53,599</u>	<u>\$ 2,558,928</u>	<u>\$ 53,862</u>

Annual debt service requirements to maturity are as follows:

<u>Year</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2017	\$ 53,862	\$ 96,486	\$ 150,348
2018	55,992	94,340	150,332
2019	58,691	92,084	150,775
2020	60,964	89,754	150,718
2021	63,311	87,309	150,620
2022-2026	356,650	396,191	752,841
2027-2031	435,311	317,576	752,887
2032-2036	423,768	223,161	646,929
2037-2041	386,282	140,870	527,152
2042-2046	341,604	76,127	417,731
2047-2051	224,151	32,349	256,500
2052-2053	98,342	4,258	102,600
	<u>\$ 2,558,928</u>	<u>\$ 1,650,505</u>	<u>\$ 4,209,433</u>

SOUTH LOGAN WATER ASSOCIATION, INC.
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2016 AND 2015

NOTE F – RISK MANAGEMENT

The Association is exposed to various risks of loss related torts; theft of, damage to and destruction of assets; errors and omissions; injuries to employees; and natural disasters.

The Association carries insurance for all risks of loss, including worker's compensation, general liability and property loss insurance. Settled claims resulting from these risks have not exceeded insurance coverage in any of the past three years.

NOTE G – WATER AGREEMENT

The Association has entered into a water purchase contract with the Logan-Todd Regional Water Commission, whereas the contract requires the Commission to provide water to the Association and the rates the Association will be charged for the expected water usage are defined therein. The contract will extend for a term of 50 years beginning January 1, 2003. The agreement may be renewed or extended for such term or terms as may be agreed by the Commission and the Association. Under terms of the agreement, the Association may not produce or resell water to any other water system or water seller, nor may the Association add any customer to its system that would increase average daily water demand or peak water demand within the Association by over 25% without prior written approval from the Commission. The agreement was originally signed to begin from the earlier date of initial availability of water for delivery by the Commission or January 1, 2003. The Association began purchasing water from the Commission in April 2003; therefore, the Commission is the sole provider of water to the Association. The agreement does require the Association to purchase minimum levels of water from the Commission. If minimum levels are not met, the Commission may charge the Association for shortages.

NOTE H – FAIR VALUE OF FINANCIAL INSTRUMENTS

The following methods and assumptions were used by the Association in estimating the fair value of its financial instruments:

Cash and cash equivalents – The carrying amount reported in the statement of financial position approximates fair value because of the short maturity of those instruments.

Accounts payable and accrued expenses – The carrying value amount reported in the statement of financial position approximates its fair value.

Long-term debt – Fair value of the Association's debt is based on current traded value.

**SOUTH LOGAN WATER ASSOCIATION, INC.
NOTES TO THE FINANCIAL STATEMENTS (CONCLUDED)
DECEMBER 31, 2016 AND 2015**

NOTE I – RETIREMENT PLAN

The Association began a SIMPLE IRA retirement plan in 2007 that covers all employees who meet the eligibility requirements. The Association's contributions to the plan have been determined by the Board of Commissioners. Contributions to the plan were \$550 and \$909 for 2016 and 2015, respectively.

NOTE J – SUBSEQUENT EVENTS

South Logan Water Association, Inc.'s management has evaluated and considered the need to recognize or disclose subsequent events through March 27, 2017, which represents the date that these financial statements were available to be issued. Subsequent events past this date, as they pertain to the fiscal year ended December 31, 2016, have not been evaluated by management.

NOTE K – RELATED PARTY TRANSACTIONS

During the year ended December 31, 2015, the Association sold a surplus truck for \$10,000 to a company whose principal is the spouse of the Association's former general manager.

A substantial amount of the Association's insurance is purchased through a local agency, the principal of which is a commissioner. The total payments to the agency or to represented companies were \$1,127 and \$16,691 for the years ended December 31, 2016 and 2015, respectively.

NOTE L – LITIGATION

A claim was assessed against the Association during 2014, for alleged home damages suffered due to high water pressure in the Association's water main lines. An Agreed Order of Dismissal was entered by Logan Circuit Court during the current year.

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INDEPENDENT AUDITORS' 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

Commissioners
South Logan Water Association, Inc.
Adairville, Kentucky

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 South Logan Water Association, Inc. (a nonprofit organization), which comprise the statement of financial position as of December 31, 2016, and the related statements of activities and cash flows for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated March 27, 2017.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered South Logan Water Association, Inc.'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 statements, but not for the purpose of expressing an opinion on the effectiveness of South Logan Water Association, Inc.'s internal control. Accordingly, we do not express an opinion on the effectiveness of South Logan Water Association, Inc.'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 the 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. We did identify certain deficiencies in internal control, described in the accompanying schedule of findings and responses as 2016-001 and 2016-002, that we consider to be significant deficiencies.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether South Logan Water Association, Inc.'s financial statements are 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*.

South Logan Water Association, Inc.'s Response to Findings

South Logan Water Association, Inc.'s response to the findings identified in our audit is described in the accompanying schedule of findings and responses. South Logan Water Association, Inc.'s response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the organization'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 organization's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Respectfully submitted,

Buckles, Travis & Hart, PLLC

Buckles, Travis & Hart, PLLC
Certified Public Accountants
Leitchfield, Kentucky
March 27, 2017

**SOUTH LOGAN WATER ASSOCIATION, INC.
SCHEDULE OF FINDINGS AND RESPONSES
FOR THE YEAR ENDED DECEMBER 31, 2016**

SIGNIFICANT DEFICIENCIES

<u>Reference Number</u>	<u>Finding</u>
2016-001	<p>Condition: Accounting personnel responsible for the accounting and reporting function lacks the professional training and professional experience to apply generally accepted accounting principles in preparing the Association's financial statements.</p> <p>Criteria: Deficiencies in the design of controls include the above mentioned condition.</p> <p>Effect: The Association is unable to prepare and present properly adjusted financial statements with full note disclosures throughout the fiscal year and at year-end.</p> <p>Cause: Budgetary constraints limit hiring individuals possessing the required technical knowledge.</p> <p>Recommendation: The Association should consider obtaining the professional training and expertise to apply generally accepted accounting principles in preparing the Association's financial statements.</p> <p>Response: The Association concurs with the recommendation; however, it is not feasible to obtain the training and expertise at this time.</p>
2016-002	<p>Condition: Due to the small staff size, the Association's bookkeeping lacks adequate segregation of duties. Two of its employees perform essentially all accounting functions, including maintenance of journals, ledgers, check preparation, and cash receipts and disbursements.</p> <p>Criteria: Segregation of duties is an essential element of proper internal control.</p> <p>Effect: Significant controls over transaction processing were absent.</p> <p>Cause: Budgetary constraints limit hiring the number of employees sufficient to permit assignment of accounting functions to various individuals.</p> <p>Recommendation: The Association should continue its efforts to distribute the accounting procedures over as many different individuals as practical, also considering realignment of duties.</p> <p>Response: The Association believes that there will always be a risk involved in a small business with limited personnel. Policy whereby employees check each other could possibly be restricted and monitored more extensively, but they also feel that they have enough backup to prevent fraud or theft where deposits are concerned. The Association has implemented measures for the bank statements and reconciliations to be reviewed by the treasurer.</p>