

***Broad River Water Authority
Spindale, North Carolina***



FINANCIAL STATEMENTS

For the Year Ended June 30, 2012

Broad River Water Authority

Spindale, North Carolina

BOARD MEMBERS

Sally Leshner - Chairman
Jim Goode - Vice-Chairman
Rob Bole – Treasurer
Maria Hunnicutt – Secretary/Manager

Don Baynard
Mickey Bland
Stan Clements
Susan Crowe
Tommy Hardin

Broad River Water Authority

TABLE OF CONTENTS

	<u>Page(s)</u>
FINANCIAL SECTION	
Independent Auditors' Report	1 - 2
Management's Discussion and Analysis	3 - 8
Basic Financial Statements	
Statement of Net Assets	9
Statement of Revenue, Expenses and Changes in Fund Net Assets	10
Statement of Cash Flows	11
Notes to the Financial Statements	12 - 21
Individual Fund Financial Statements	
Statement of Revenues and Expenses - Budget and Actual	22
Compliance	
Report on Compliance and on Internal Control over Financial Reporting Based on an Audit of Financial Statements Performed in Accordance with <u>Government Auditing Standards</u>	23 - 24

BURLESON & EARLEY, P.A.

CERTIFIED PUBLIC ACCOUNTANTS

INDEPENDENT AUDITORS' REPORT

To the Board of Directors
Broad River Water Authority
Spindale, North Carolina

We have audited the accompanying statement of net assets of the Broad River Water Authority as of and for the year ended June 30, 2012, and the related statement of revenues, expenses and changes in net assets and cash flows for the year then ended. These financial statements are the responsibility of the Broad River Water Authority management. Our responsibility is to express an opinion 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. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Broad River Water Authority as of June 30, 2012 and the results of its operations and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated November 8, 2012 on our consideration of the Broad River Water Authority'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* and should be considered in assessing the results of our audit.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 3 through 8 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.

Our audit was performed for the purpose of forming an opinion on the financial statements that collectively comprise the basic financial statements of the Broad River Water Authority. The schedule of revenue and expenditures – budget to actual is presented for purposes of additional analysis and is not a required part of the financial statements. The accompanying schedule of revenue and expenditures – budget to actual is the responsibility of management and was derived from and relate directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied by us in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements themselves, 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 statements and, accordingly, we do not express an opinion or provide any assurance on them.

Burleson & Earley, P.A.
Certified Public Accountants
November 8, 2012

MANAGEMENT'S DISCUSSION AND ANALYSIS

As management of Broad River Water Authority, we offer readers of the Authority's financial statements this narrative overview and analysis of the financial activities of the Authority for the fiscal year ended June 30, 2012. We encourage readers to read the information presented here in conjunction with the financial information contained in the various sections of this audit report.

FINANCIAL HIGHLIGHTS

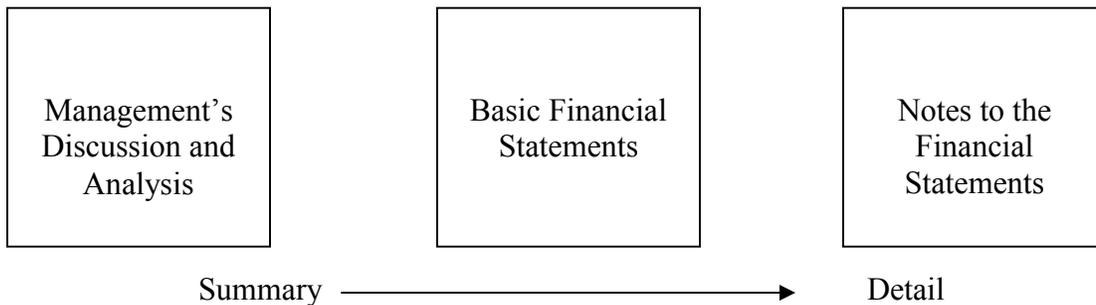
- The assets of Broad River Water Authority exceeded its liabilities at the close of the fiscal year by \$11,872,842 (*net assets*).
- The Authority's total net assets increased by \$2,103,111, primarily due to increased operating revenues.

OVERVIEW OF THE FINANCIAL STATEMENTS

This discussion and analysis are intended to serve as an introduction to the Authority's basic financial statements. The audited financial statements of the Authority consist of two components: 1) basic financial statements and 2) notes to the financial statements (see Figure 1). In addition to the basic financial statements, this report contains other supplemental information that will enhance the reader's understanding of the financial condition of Broad River Water Authority.

Required Components of Annual Financial Report

Figure 1



The Basic Financial Statements are prepared using the full accrual basis of accounting. They consist of 3 statements. The first is the Statement of Net Assets. Assets and liabilities are classified between current and long-term. This statement provides a summary of the Authority's investments in assets and obligations to creditors. Liquidity and financial flexibility can be evaluated using the information contained in this statement.

The next statement is the Statement of Revenues, Expenses, and Changes in Net Assets. This statement is used in evaluating whether the Authority has recovered all of its costs through revenues. Its information is used in determining credit worthiness.

The final required statement is the Statement of Cash Flows. This statement reports cash inflows and outflows in the following categories: operating, investing, and financing activities. Based on this data, the user can determine the sources of cash, and the change in cash.

The Notes to the Financial Statements provide more detail information and should be read in conjunction with the statements.

FINANCIAL POSITION SUMMARY

<u>At June 30</u>	<u>2012</u>	<u>2011</u>	<u>\$ Change</u>	<u>% Change</u>
Assets				
Current Assets	\$ 6,206,153	\$ 5,328,950	\$ 877,203	16%
Restricted Assets	170,142	332,784	(162,642)	-49%
Capital Assets	33,648,862	33,778,214	(129,352)	0%
Other Assets	2,164,626	1,884,717	279,909	15%
	<u>\$ 42,189,783</u>	<u>\$ 41,324,665</u>	<u>\$ 865,118</u>	<u>-18%</u>
Liabilities				
Current Liabilities	\$ 2,048,909	\$ 2,097,651	\$ (48,742)	-2%
Long-term Liabilities	28,268,032	29,792,275	(1,524,243)	-5%
Total Liabilities	<u>30,316,941</u>	<u>31,889,926</u>	<u>\$ (1,572,985)</u>	<u>-7%</u>
Net Assets				
Invested in Capital Assets, Net of Related Debt	3,814,459	2,379,684	1,434,775	60%
Restricted for Debt Retirement	170,142	332,784	(162,642)	-49%
Unrestricted	7,888,241	6,722,271	1,165,970	17%
Total Net Assets	<u>11,872,842</u>	<u>9,434,739</u>	<u>2,438,103</u>	<u>28%</u>
	<u>\$ 42,189,783</u>	<u>\$ 41,324,665</u>	<u>\$ 865,118</u>	<u>21%</u>

Net assets may serve over time as a useful indicator of the Authority’s financial position. The Authority’s net assets exceeded liabilities by \$11,872,842 at June 30, 2012, a \$2,103,111 increase from June 30, 2011. One portion of net assets reflects the Authority’s investment in capital assets (e.g. water distribution infrastructure, equipment and vehicles), less any related debt still outstanding that was issued to acquire those items. The Authority uses these capital assets to provide services to customers; consequently, these assets are not available for future spending. Although the Authority’s investment in its capital assets is reported net of the outstanding related debt, the resources needed to repay that debt must be provided by the sources, since the capital assets cannot be used to liquidate these liabilities.

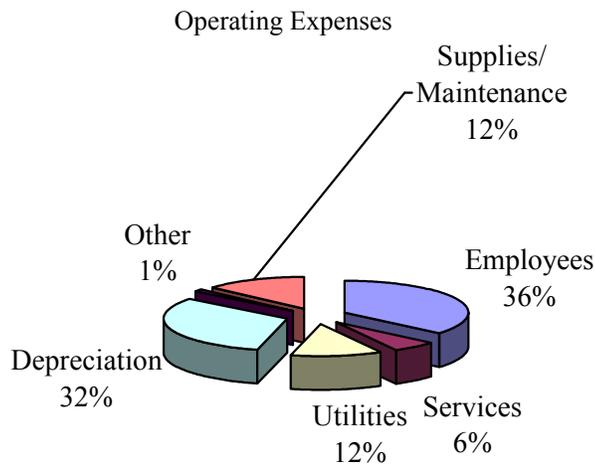
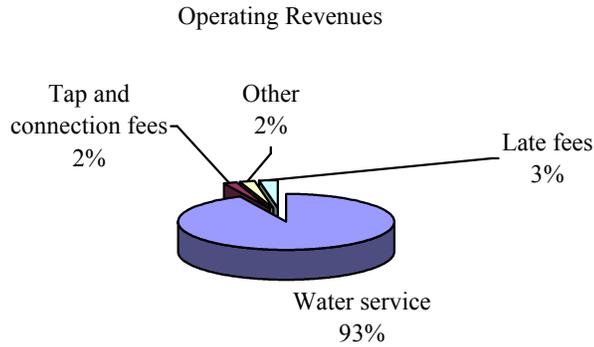
Several particular aspects of the Authority’s financial operations positively influenced total net assets:

- Capital contributions of \$563,444 for the expansions to the Plantation Drive lines; and renovations for the water treatment plant.
- Increased revenues from the sale of water to Polk County and Inman-Campobello Water District.

SUMMARY OF OPERATIONS AND CHANGES IN NET ASSETS

<u>For the Fiscal Year Ended June 30</u>	<u>2012</u>	<u>2011</u>	<u>\$ Change</u>	<u>% Change</u>
Operating Revenues	\$ 6,384,861	\$ 6,206,441	\$ 178,420	3%
Operating Expenses	3,354,695	3,244,626	110,069	3%
Operating Income Before Nonoperating Revenues and Expenses	3,030,166	2,961,815	68,351	2%
Nonoperating Revenues and Expenses, net	(1,490,499)	(1,692,031)	201,532	12%
Capital Contributions	563,444	972,141	(408,697)	-42%
Increase in Net Assets	<u>\$ 2,103,111</u>	<u>\$ 2,241,925</u>	<u>\$ (138,814)</u>	<u>-6%</u>

The daily operations of the Authority are funded through the collection of water revenues. The customer base includes a mixture of single and multi-family residential, commercial, institutional, and industrial.



SUMMARY OF CASH FLOW ACTIVITIES

The following shows a summary of the major sources and uses of cash and cash equivalents. Cash equivalents are considered cash-on-hand, bank deposits and highly liquid investments with an original maturity of three months or less.

<u>For the Fiscal Year Ended June 30</u>	<u>2012</u>	<u>2011</u>	<u>\$ Change</u>	<u>% Change</u>
Cash Flows from Operating Activities	\$ 4,023,400	\$ 3,784,214	\$ 239,186	6%
Cash Flows from Capital and Related Financing Activities	(3,562,034)	(7,833,994)	4,271,960	-55%
Cash Flows from Investment Activities	302	5,884	(5,582)	-95%
Net Increase (Decrease) in Cash and Cash Equivalents	461,667	(4,043,896)	4,505,564	111%
Cash and Cash Equivalents, beginning of year	4,541,022	8,584,919	(4,043,897)	-47%
Cash and Cash Equivalents, end of year	<u>\$ 5,002,689</u>	<u>\$ 4,541,022</u>	<u>\$ 461,667</u>	<u>10%</u>

CAPITAL ASSET AND DEBT ADMINISTRATION

Capital Assets

During fiscal year 2012, the Authority expended approximately \$933,000 on capital activities. This included approximately \$550,000 for line extensions, \$218,000 for the water plant expansion and the balance for renovations at the administrative office, vehicles and equipment.

Acquisitions are funded using a variety of techniques, including State reimbursements, county grants, revenue bond issuances and operating revenues.

SUMMARY OF CAPITAL ASSETS

	<u>2012</u>	<u>2011</u>	<u>\$ Change</u>	<u>% Change</u>
Land	\$ 453,907	\$ 447,107	\$ 6,800	2%
Construction in progress	56,593	66,636	(10,043)	-15%
Building and improvements	21,673,766	21,426,112	247,654	1%
System lines	20,444,879	19,894,813	550,066	3%
Vehicles	270,346	311,303	(40,957)	-13%
Equipment	625,891	549,639	76,252	14%
	<u>43,525,382</u>	<u>42,695,610</u>	<u>829,772</u>	<u>2%</u>
Accumulated depreciation	<u>(9,876,520)</u>	<u>(8,917,396)</u>	<u>(959,124)</u>	<u>11%</u>
Capital assets, net	<u>\$ 33,648,862</u>	<u>\$ 33,778,214</u>	<u>\$ (129,352)</u>	<u>0%</u>

Long-term Debt

As of June 30, 2012, the Authority had total debt outstanding of \$29,829,404.

SUMMARY OF OUTSTANDING DEBT

	<u>2012</u>	<u>2011</u>
Water system revenue bonds	\$ 29,393,614	\$ 30,934,071
Add: unamortized premium	435,790	357,821
Net debt	<u>\$ 29,829,404</u>	<u>\$ 31,291,892</u>

ECONOMIC FACTORS AND NEXT YEAR’S BUDGETS AND RATES

Since the Authority’s inception in December 2000, its major challenge has been to manage the impact of a transition in the customer base. For the 2001 calendar year, the “top ten” customers were all industrial based, with a heavy emphasis in the textile industry. These “top ten” customers accounted for over 50% of water consumption and nearly 40% of water sales revenue. However, due to national industrial trends and changes in trade laws, the water usage by the Authority’s industrial customers dropped 90% in a 10-year period. This equated to a decrease of industrial sales in 2001 of \$1.28 million to sales in 2011 of \$361,000.

To mitigate the trend of industrial loss, the Authority initiated an aggressive program to expand waterlines to County residents and businesses in need of public water. Partnerships with the North Carolina Rural Economic Development Center, Rutherford County, and the Town of Ruth have generated over \$4.6 million in direct grants for waterline expansion over the last 11 years. These funds, along with over \$2.6 million of the Authority’s funds, allowed for the construction of more than 78 miles of waterline, and the growth of our customer base by nearly 1,000 accounts (19% growth).

In 2000, the average production of the water treatment plant was 5 MGD. In 2008, annual production dipped to an average of 2.74 MGD. Having excess capacity presented an opportunity for the Authority to partner with a major bulk resale customer. An agreement was reached in July 2008 for the Authority to sell bulk finished water to Inman-Campobello Water District (ICWD) through Polk County. ICWD is based in Spartanburg County, SC, with a primarily residential customer base of over 12,000 connections. Polk County, which neighbors Rutherford County, had no water customers at the time of the agreement, but planned to slowly build a system. The agreement allowed the Authority to sell a minimum of 2.0 MGD and a maximum of 4.0 MGD to Polk County/ ICWD for a period of 15 years. Water sales began December 31, 2008. Since that time, Polk County/ ICWD has purchased an average of 2.6 MGD, and generated total revenue of \$4.7 million.

The most effective and immediate means to increase revenue when consumption has decreased is the use of the rate structure and imposing rate increases. The Authority chose a rate-setting philosophy with a high minimum charge and reasonable declining block volume rates. This strategy seeks to provide a minimum revenue stream that is less subject to sudden volume changes resulting from an industry closing or weather patterns. While steady rate increases have been implemented by the Authority, the average water bill (assuming usage of 5,000 gallons) is currently \$44.53. This is comparable with other local utilities (Cleveland, Rutherford, and Polk Counties) which have “outside” rates for water customers. In addition, future rate increases can be determined and justified through a financial model that was created for the Authority in 2007 and updated yearly. The model accounts for changes in

revenues and expenses, capital improvement needs, reserve funds, and the ability to meet bond covenants.

The success of the Authority's growth, strategies, and partnerships are evident in the data below. The customer base has expanded, consumption/production has rebounded and revenues have diversified and greatly increased.

TREND SHOWING REDUCED RELIANCE ON INDUSTRIAL CUSTOMERS AND INCREASED CONTRIBUTION OF RESALE/ BULK CUSTOMERS

<u>Type of Customer</u> Year	<u>Number of Accounts</u>		<u>Consumption (millions of gals.)</u>		<u>Water Sales Revenue (\$ 000)</u>	
	2002 ⁽¹⁾	FY 2012	2002	FY 2012	2002	FY 2012
Residential	4,956	5,835	282	278	\$ 1,677	\$ 2,749
Commercial/ Other	524	616	114	99	\$ 518	\$ 744
Industrial	39	33	871	74	\$ 1,433	\$ 343
Resale/ Bulk	1	2 ⁽²⁾	283	1,349	\$ 407	\$ 1,947
Totals	5,521	6,486	1,550	1,800	\$ 4,036	\$ 5,948

⁽¹⁾ Calendar year 2002 is the first year of complete available data for BRWA. Duke Power maintained operations in calendar yr 2000.

⁽²⁾ Resale accounts: Grassy Pond Water Company represents 3,850 accounts, all residential/ commercial; and Polk/ ICWD represents 12,000 accounts, 95% residential/commercial.

With stable revenues and higher production requirements, the Authority has been able to increase their focus towards modernizing and replacing aging infrastructure. The Water Treatment Plant, which was originally built 1982, underwent a \$7 million rehabilitation in FY 2011. The goal of the modernization project was to allow the WTP to reliably produce 8 MGD and implement new process equipment that was hydraulically capable of handling flows up to 12 MGD. Unused contingency funds from this project were used in FY 2012 to update the lab/ control room of the WTP and to renovate the building to include additional bathrooms, storage space, and a training facility.

We also completed a successful new waterline installation project in the Cleghorn Community. This project involved 14,700 linear feet of waterline in an area served by community and private wells. 33 residential customers were immediately connected to our system, and the project was partially funded by Rutherford County.

REQUESTS FOR INFORMATION

This report is designed to provide an overview of the Authority's finances for those with an interest in this area. Questions concerning any of the information found in this report, or requests for additional information, should be directed to the Authority Manager, Broad River Water Authority, PO Box 37, Spindale, NC 28160.

BASIC FINANCIAL STATEMENTS

Broad River Water Authority
Statement of Net Assets

At June 30	2012
Assets	
Current assets:	
Unrestricted assets:	
Cash and cash equivalents	\$ 4,832,547
Customer accounts receivable - net	1,139,885
Grants receivable	182,137
Other receivables - net	51,584
Total unrestricted assets	6,206,153
Restricted assets:	
Cash and cash equivalents	170,142
Total current assets	6,376,295
Noncurrent assets:	
Capital assets:	
Land and other non-depreciable assets	510,501
Capital assets, net of depreciation	33,138,361
Total capital assets	33,648,862
Other assets:	
Other assets, net	2,164,626
Total noncurrent assets	35,813,488
	\$ 42,189,783
Liabilities and net assets	
Current liabilities:	
Payable from unrestricted assets:	
Current portion long term debt	\$ 1,605,022
Accounts payable	213,753
Accrued salaries and related payables	20,660
Customer deposits and overpayments	102,363
Accrued interest	107,111
Total current liabilities	2,048,909
Noncurrent liabilities:	
Accrued vacation payable	43,650
Noncurrent portion long term debt	28,224,382
Total noncurrent liabilities	28,268,032
Net assets:	
Invested in capital assets, net of related debt	3,814,459
Restricted for debt retirement	170,142
Unrestricted	7,888,241
Total net assets	11,872,842
	\$ 42,189,783

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

Broad River Water Authority
Statement of Revenues, Expenses and Changes in Fund Net Assets

For the Fiscal Year Ended June 30	2012
Operating revenue:	
Water service	\$ 5,948,284
Tap and connection fees	118,416
Water testing fees	6,850
Late fees	169,588
Other operating	141,723
Total revenue	6,384,861
 Operating expenses:	
Salaries and employee benefits	1,209,407
Professional services	68,984
Departmental supplies and expenses	343,408
Telephone	18,821
Travel and training	8,423
Repairs and maintenance	39,750
Vehicle maintenance	60,238
Licenses and franchise fees	5,366
Utilities	381,707
Contracted services	127,333
Depreciation	1,062,657
Other operating	28,602
Total expenses	3,354,696
Operating income	3,030,165
 Nonoperating revenues (expenses):	
Investment earnings	302
Interest on bond indebtedness	(1,409,764)
Amortization of bond costs	(81,036)
Total nonoperating revenues (expenses)	(1,490,498)
Income before capital contributions	1,539,667
Capital contributions	563,444
Change in net assets	2,103,111
Total net assets, beginning of year, as restated	9,769,731
Total net assets, end of year	\$11,872,842

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

Broad River Water Authority
Statement of Cash Flows

For the Fiscal Year Ended June 30	2012
Cash flows from operating activities:	
Cash received from customers	\$ 6,309,954
Cash paid for goods and services	(1,078,380)
Cash paid to employees for services	(1,208,175)
Net cash provided by operating activities	4,023,399
 Cash flows from capital and related financing activities:	
Acquisition and construction of capital assets	(1,034,944)
Capital contributions	381,307
Interest payments on debt maturities	(1,367,940)
Principal payments on debt maturities	(1,540,457)
Net cash used by capital and financing activities	(3,562,034)
 Cash flows from investing activities:	
Interest on investments	302
Net increase in cash and cash equivalents	461,667
Cash and cash equivalents, beginning of year	4,541,022
Cash and cash equivalents, end of year	\$ 5,002,689
 Reconciliation of operating income to net cash provided by operating activities:	
Operating income	\$ 3,030,165
Adjustments to reconcile operating income to net cash provided by operating activities:	
Depreciation	1,062,657
Changes in assets and liabilities:	
(Increase) decrease in accounts receivable	(70,757)
Increase (decrease) in accounts payable	4,252
Increase (decrease) in customer deposits	(4,150)
Increase (decrease) in accrued salaries and related payable:	1,232
Total adjustments	993,234
Net cash provided by operating activities	\$ 4,023,399

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

Broad River Water Authority
Notes to Financial Statements
For the Year Ended June 30, 2012

Note 1 - Summary of Significant Accounting Policies

The accounting policies of the Broad River Water Authority conform to accounting principles generally accepted in the United States of America as applicable to governments. The following is a summary of the more significant accounting policies:

A. Reporting Entity

The Broad River Water Authority (Authority) is a public body and a body politic and corporate created under the authority of Chapter 162A-1 of the General Statutes of North Carolina. The Certificate of Incorporation for the Authority was issued by the Secretary of State on August 3, 1999, under the name of Spindale-Rutherfordton Water Authority. On April 20, 2000, a Certificate of Name Change was issued by the Secretary of State changing the name of the Authority to Broad River Water Authority.

The Authority was formed by resolution of the political subdivisions of the Town of Spindale and the Town of Rutherfordton. Subsequently, the County of Rutherford and the Town of Ruth joined the Authority pursuant to Certificates of Joinder issued by the Secretary of State on December 30, 1999, and March 10, 2000, respectively. The business and affairs of the corporation are managed by the members of the Authority who determine the policies and activities of the corporation within the confined of the stated purposes of the corporation as allowed and provided by Chapter 162A, Article I, of the North Carolina Statutes. The Authority consists of eight (8) members. The Town of Spindale, the Town of Rutherfordton, the Town of Ruth, and the County of Rutherford each appoint two (2) members of the Authority.

B. Purpose

The Authority was organized to acquire and operate water systems serving Rutherford County from Duke Energy Corporation.

C. Basis of Presentation

Fund financial statements provide information about the Authority's funds. Statements for the proprietary fund category are presented.

Proprietary Funds include the following fund type:

Enterprise Funds – Enterprise Funds account for those operations (a) that are financed and operated in a manner similar to private business enterprises where the intent of the governing body is that costs (expenses, including depreciation) of providing goods or services to the general public on a continuing basis be financed or recovered primarily through use charges; or (b) where the governing body has decided that the periodic determination of revenues earned, expenses incurred, and/or net income is appropriate for capital maintenance, public policy, management control, accountability, or other purposes. The Authority has one Enterprise Fund for water operations.

D. Measurement of Focus and Basis of Accounting

The proprietary fund financial statements are reported using the economic resources measurement focus. These statements are reported using the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded at the time liabilities are incurred, regardless of when the related cash flows take place. Non exchange transactions, in which the Authority gives (or receives) value without directly receiving (or giving) equal value in exchange, include capital contributions.

As permitted by U.S. generally accepted accounting principles, the Authority has elected to apply only applicable FASB Statements and Interpretations issued before November 30, 1989 that do not contradict GASB pronouncements in its accounting and reporting practices for its proprietary operations.

E. Budgetary Data

The Authority's budgets are adopted as required by the North Carolina General Statutes. An annual operating budget is adopted for the enterprise fund. All annual appropriations lapse at the fiscal-year end. Project ordinances are adopted for the Capital Improvements Fund. All budgets are prepared using the modified accrual basis of accounting. Expenditures may not legally exceed appropriations at the departmental level for all annually budgeted funds and at the object level for the multi-year funds. All amendments must be approved by the governing board. During the year, several amendments to the original budget were necessary, the effects of which were not material. The budget ordinance must be adopted by July 1 of the fiscal year or the governing board must adopt an interim budget that covers that time until the annual ordinance can be adopted.

F. Estimates

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

G. Assets, Liabilities, and Fund Equity

1. Deposits and Investments

All deposits of the Authority are made in board-designated official depositories and are secured as required by State law (G.S. 159-31). The Authority may designate, as an official depository, any bank or savings association whose principal office is located in North Carolina. Also, the Authority may establish time deposit accounts such as NOW and SuperNOW accounts, money market accounts, and certificates of deposits.

State law [G.S. 159-30 (c)] authorizes the Authority to invest in obligations of the United States or obligations fully guaranteed both as to principal and interest by the United States; obligations of the State of North Carolina; bonds and notes of any North Carolina local government or public authority; obligations of certain non-guaranteed federal agencies; certain high quality issues of commercial paper and bankers' acceptances; and the North Carolina Capital Management Trust (NCCMT).

The Authority's investments with a maturity of more than one year at acquisition and non-money market investments are reported at fair value as determined by quoted

market prices. The securities of the NCCMT Cash Portfolio, a SEC-registered (2a7) money market mutual fund, are valued at fair value, which is the NCCMT's share price. The NCCMT Term Portfolio's securities are valued at fair value. Money market investments that have a remaining maturity at the time of purchase of one year or less are reported at amortized cost. Non-participating interest earnings and investment contracts are reported at cost.

2. Cash and Cash Equivalents

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

3. Accounts Receivable

The amounts shown on the balance sheet for receivables is net of an allowance for doubtful accounts. This amount is estimated by analyzing the accounts receivable aging and the percentage of receivables that were written off in previous years.

Unbilled revenue represents revenues that were earned in the year ended June 30, 2012, but not billed in that year.

Other receivables represent the sales tax refund due from the North Carolina Department of Revenue for the sales tax paid during the fiscal year ended June 30, 2012.

4. Capital Assets

The Authority's capital assets are recorded at original cost at the time of acquisition and depreciated over the useful lives, ranging from 5 – 100 years, on a straight line basis. When an asset is disposed of, the cost of the asset and the related accumulated depreciation are removed from the books. Any gain or loss on disposition is reflected in the earnings for the period.

5. Other Assets

The Authority's other assets are comprised of the bond issue costs related to the remaining outstanding balance of the original 2000 bond issue, the subsequent advanced refunding issue in 2005, the 2008 bond issue and the 2010 bond issue. Additionally, the amount of the deferred interest costs associated with the 2005 advanced refunding issue is a component of the other assets. The issue costs associated with the 2000 issue are being amortized over 71 months, the 2005 bond costs and the deferred interest are being amortized over 240 months and the 2008 and 2010 bond costs are being amortized over 180 months.

6. Compensated Absences

The Authority allows its full time employees to accumulate up to thirty days earned vacation and such leave is fully vested when earned. Accumulated earned vacation at June 30, 2012 was \$43,650. Accumulated vacation is accounted for on a LIFO basis, assuming that employees are taking leave time as it is earned. The current portion of the accumulated vacation pay is not considered to be material and therefore, no provision for this has been made in the accompanying financial statements.

Employees can accumulate an unlimited amount of sick leave. Sick leave may be used in the determination of length of service for retirement benefit purposes. Since the Authority has no obligation for accumulated sick leave until it is taken, no accrual for sick leave has been made.

7. Net Assets

Net assets in proprietary fund financial statements are classified as invested in capital assets, net of related debt; restricted; and unrestricted. Restricted net assets represent constraints on resources that are either externally imposed by creditors, grantors, contributors, or laws or regulations of other governments or imposed by law through state statute.

Note 2 - Detailed Notes on All Funds

A. Assets

1. Deposits and Investments

All of the Authority's deposits are either insured or collateralized by using the Pooling method. Under the Pooling Method, which is a collateral pool, all uninsured deposits are collateralized with securities held by the State Treasurer's agent in the name of the State

Treasurer. Since the State Treasurer is acting in a fiduciary capacity for the Authority, These deposits are considered to be held by the Authority's agents in their names. The amount of the pledged collateral is based on an approved averaging method for non-interest bearing deposits and the actual current balance for interest-bearing deposits. Depositories using the Pooling Method report to the State Treasurer the adequacy of their pooled collateral covering uninsured deposits. The State Treasurer does not confirm this information with the Authority or escrow agent. Because of the inability to measure the exact amounts of collateral pledged for the Authority under the Pooling Method, the potential exists for under-collateralization, and this risk may increase in periods of high cash flows. However, the State Treasurer of North Carolina enforces strict standards of financial stability for each depository that collateralizes public deposits under the Pooling Method. The Authority does not have a deposit policy for custodial credit risk.

At June 30, 2012, the Authority's deposits had a carrying amount of \$5,001,649 and a bank balance of \$5,012,335. Of the bank balance, \$250,000 was covered by Federal Depository Insurance and \$4,762,335 was covered by collateral held under the Pooling Method.

At June 30, 2012, the Authority had \$170,142 invested with the North Carolina Capital Management Trust's Cash Portfolio which carried a credit rating of AAAM by Standard and Poor's. The Authority has no policy regarding credit risk.

At June 30, 2012, the Authority had \$1,040 in petty cash.

2. Accounts Receivable

The accounts receivable consists of the following at June 30, 2012:

Customers billed	\$1,050,064
Unbilled revenues	296,148
Less: allowance for doubtful accounts	<u>(206,327)</u>
Total accounts receivable	<u>\$ 1,139,885</u>

3. Capital Assets

The capital assets of the Broad River Water Authority at June 30, 2012 consist of the following:

	<u>Beginning</u> <u>Balances</u>	<u>Increases</u>	<u>Decreases</u>	<u>Ending</u> <u>Balance</u>
Business-type activities:				
Capital assets not being depreciated:				
Construction in progress	\$ 66,637	\$ 56,593	\$ (66,636)	\$ 56,594
Land	447,107	6,800		453,907
Total capital assets not being depreciated	<u>513,744</u>	<u>63,393</u>	<u>(66,636)</u>	<u>510,501</u>
Capital assets being depreciated:				
Building and improvements	21,426,112	247,652		21,673,764
System lines	19,894,814	550,064		20,444,878
Vehicles	311,303	62,577	(103,531)	477,411
Computer Equipment	112,499			112,499
Equipment	437,140	76,251		513,391
Total capital assets being depreciated	<u>42,181,868</u>	<u>936,544</u>	<u>(103,531)</u>	<u>43,221,943</u>
Less accumulated depreciation for:				
Building and improvements	6,135,681	741,352		6,877,033
System lines	2,087,196	259,847		2,347,043
Vehicles	208,830	34,282	(103,531)	346,643
Computer Equipment	112,499			112,499
Equipment	373,188	27,176		400,364
Total accumulated depreciation	<u>8,917,394</u>	<u>1,062,657</u>	<u>(103,531)</u>	<u>10,083,582</u>
Total capital assets being depreciated, net	<u>33,264,474</u>			<u>33,138,361</u>
Business-type activities capital assets, net	<u>\$ 33,778,218</u>			<u>\$ 33,648,862</u>

4. Restricted Assets

The Water System Revenue Bonds call for certain funds to be placed into a Reserve Fund. These funds are restricted to payment of certain items approved in the Bond agreement. Any interest earned by these funds is also restricted. At June 30, 2012, the restricted cash balance was \$170,142.

5. Other Assets

Other assets consist of the following at June 30, 2012:

Issue costs associated with remaining 2000 bonds	\$ 252,946
Issue costs associated with 2005 advance refunding bonds	1,494,015
Issue costs associated with the 2008 bond issue	37,950
Issue costs associated with the 2010 bond issue	<u>57,077</u>
	1,841,988
Less: accumulated amortization	<u>(791,528)</u>
	1,050,460
Deferred interest on 2005 advanced refunding	<u>1,114,166</u>
Total other assets	<u>\$ 2,164,626</u>

B. Liabilities

1. Local Governmental Employees' Retirement System

Employees' Retirement System (LGERS), a cost-sharing multiple-employer defined benefit pension plan administered by the State of North Carolina. LGERS provides retirement and disability benefits to plan members and beneficiaries. Article 3 of G.S. Chapter 128 assigns the authority to establish and amend benefit provisions to the North Carolina General Assembly. The Local Governmental Employees' Retirement System is included in the Comprehensive Annual Financial Report (CAFR) for the State of North Carolina. The State's CAFR includes financial statements and required supplementary information for LGERS. That report may be obtained by writing to the Office of the State Controller, 1410 Mail Service Center, Raleigh, North Carolina 27699-1410, or by calling (919) 981-5454.

Funding Policy. Plan members are required to contribute six percent of their annual covered salary. The Authority is required to contribute at an actuarially determined rate. For the Authority, the current rate for employees is 7.13% of annual covered payroll. The contribution requirements of members and of the Authority are established and may be amended by the North Carolina General Assembly. The Authority's contributions to LGERS for the years ended June 30, 2012, 2011 and 2010 were \$64,836, \$60,858, and \$48,653, respectively. The contributions made by the Authority equaled the required contributions for each year.

Supplemental Retirement Income Plan

On July 1, 2001, the Authority elected to participate in the Supplemental Retirement Income Plan of North Carolina, a 401(k) Plan. Employee contributions to the plan are voluntary. The Authority contributes amounts equal to 5% of each employee's gross annual salary. Contributions are remitted bi-weekly. Such contributions vest immediately. Authority contributions to the plan totaled \$45,414, \$45,332 and \$47,431 for the years ended June 30, 2012, 2011 and 2010, respectively.

2. Long Term Obligations

Water System Revenue Bonds

On December 1, 2000, the Authority issued Water System Revenue Bonds – Series 2000 in the amount of \$30,440,000. These bonds were issued to finance the purchase of the water system from Duke Energy.

On July 1, 2005, the Authority refunded and defeased the 2000 series bonds by placing the proceeds of new bonds in an irrevocable trust with an escrow agent to provide for all future debt service payments on the 2000 Series bonds. Accordingly, the trust account assets and the liability for the defeased bonds are not included in the Authority’s financial statements. At June 30, 2012, \$22,955,000 of the 2000 Series bonds are considered to be defeased. These bonds are recorded including an unamortized premium of \$435,790.

On October 21, 2008, the Authority issued the 2008 series bonds. The proceeds of these bonds were used in the construction of the waterline expansion to the Inman-Campobello Water District. The principal amount of this issue was \$2,000,000.

On January 11, 2010, the Authority issued the 2010 series bonds. The proceeds of these bonds are being used for the water plant expansion. The principal amount of this issue was \$6,000,000. At June 30, 2012, the cash balance from this issue is \$170,142 and is presented as restricted in these financial statements.

At June 30, 2012, the following amounts are outstanding for these bond issues:

Series 2005	\$22,310,000
Series 2008	1,654,866
Series 2010	<u>5,428,747</u>
	<u>\$29,393,614</u>

The future payments of the bonds for the years ending June 30th are as follows:

<u>Year</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2013	\$ 1,605,022	\$ 1,344,987	\$ 2,950,009
2014	1,667,039	1,283,041	2,950,080
2015	1,732,784	1,218,252	2,951,036
2016	1,814,493	1,133,544	2,948,037
2017	1,907,210	1,044,827	2,952,037
2018-2022	11,005,516	3,732,666	14,738,182
2023-2026	<u>9,661,550</u>	<u>999,819</u>	<u>10,661,369</u>
	<u>\$29,393,614</u>	<u>\$10,757,136</u>	<u>\$40,150,750</u>

The Authority is in compliance with the covenants as to rates, fees, rentals and charges of the Bond Order, authorizing the issuance of the Water and Sewer Revenue Bonds, Series 2000, 2005 and 2008. The 2000 and 2005 Bond Orders require the debt service coverage ratio to be no less than 120%, while the 2008 and 2010 Bond Orders require the ratio to be no less than 125%.

The debt service coverage ratio calculation for the year ended June 30, 2012, is as follows:

Operating revenues	\$6,384,861
Operating expenses*	<u>2,292,038</u>
Operating income	4,092,823
Nonoperating revenues (expenses)**	<u>302</u>
Income available for debt service	4,093,125
Debt service, principal and interest paid (Revenue bonds only)	2,950,221
Debt service coverage ratio	139%

* Per rate covenants, this does not include the depreciation expense of \$1,062,657.

** Per rate covenants, this does not include revenue bond interest paid of \$1,409,764 and bond cost amortization of \$81,036.

The Authority has pledged future water and sewer customer revenues, net of specified operating expenses, to repay \$29,393,614 in water and sewer system revenue bonds issued in 2000 and defeased in 2005 and new bonds issued in 2008 and 2010. The bonds are payable solely from water and sewer customer net revenues and are payable through 2026. Annual principal and interest payments on the bonds are expected to require approximately 46 percent of net revenues. The total principal and interest remaining to be paid on the bonds is \$40,150,750. Principal and interest paid for the current year and total customer net revenues were \$2,950,221 and \$4,092,823, respectively.

Long-Term Obligation Activity

The following is a summary of changes in the Authority's long-term obligations for the year ended June 30, 2012.

	June 30, 2011	Additions	Retirements	June 30, 2012	Current Portion
Water System Revenue Bonds					
Series 2005	\$ 23,440,000	\$ -	\$ 1,130,000	\$ 22,310,000	\$ 1,170,000
Series 2008	1,774,239	-	\$ 119,373	1,654,866	123,920
Series 2010	5,719,832	-	\$ 291,084	5,428,748	311,102
Unamortized bond premium	469,205	-	\$ 33,415	435,790	-
Accrued vacation	43,650	-	-	43,650	-
	<u>\$ 31,446,926</u>	<u>\$ -</u>	<u>\$ 1,573,872</u>	<u>\$ 29,873,054</u>	<u>\$ 1,605,022</u>

Accrued vacation is accounted for on the LIFO basis, assuming that employees are taking leave time as it is earned.

3. Risk Management

The Authority is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. The Authority participates in two self-funded risk financing pools administered by the North Carolina League of Municipalities. Through these pools, the Authority obtains general liability of \$3 million per occurrence, auto liability coverage of \$2 million per occurrence, property coverage up to the total insurance values of the property policy, workers' compensation coverage up to statutory limits, and employee health from United Health Care coverage with no lifetime limit and in-network providers. The pools are reinsured through commercial companies for single occurrence claims against general liability, auto liability and property in excess of \$500,000 and \$300,000 up to statutory limits for workers' compensation. The property liability pool has an aggregate limit for the total property losses in a single year, with the reinsurance limit based upon a percentage of the total insurance values. The Authority does not carry flood insurance.

The Authority carries commercial coverage for all other risks of loss. There have been no significant reductions in insurance coverage in the prior year, and settled claims have not exceeded coverage in any of the past fiscal years.

In accordance with G.S. 159-29, the Authority's employees that have access to \$100 or more at any given time of the Authority's funds are performance bonded through a commercial surety bond. Coverage in the amount of \$50,000 has been secured to provide against employee theft, forgery or alteration, inside and outside the premises – theft of money and securities. Additional coverage in the amount of \$25,000 is in place for computer fraud, funds transfer fraud and money orders. The finance officer is individually bonded for \$50,000.

4. Sale of Finished Water Agreement

On July 7, 2008, the Authority entered into an agreement with Polk County (Polk) and the Inman-Campobello Water District (ICWD) to furnish water to both systems. As part of this agreement, the Authority constructed a new water line which allows for the Polk system to connect to the Authority's system. The ICWD system will obtain its water through connections to the Polk system. The cost of the new waterline was \$3,123,970 and was funded through the issuance of the 2008 series Revenue Bonds and capital contributions from both ICWD and Rutherford County. Under the terms of the agreement, the Authority will furnish to Polk/ICWD a maximum of 4 million gallons per day for the first two years of the agreement and 4.1 million gallons per day for years three to fifteen.

5. Construction Commitments

At June 30, 2012, the Authority has outstanding obligations related to a construction project totaling \$327,450.

Note 3 - Stewardship, Compliance, and Accountability

Excess of Expenditures over Appropriations

Actual expenditures exceeded budget appropriations in several of the operating expense line items. These line item overages were managed with positive variances in other expense areas. In the future, the Authority board will review these variances and make the necessary budget amendments.

Note 4 – Prior Period Adjustment

Prior Period Restatement

An error in the calculation of bond cost and discount amortization was discovered that required restatement of beginning net assets. These adjustments have been applied to the prior year balances as presented in these financial statements as follows:

	<u>Total</u>
Overstatement of bond amortization	\$ 161,605
Overstatement of discount amortization	<u>173,387</u>
Total overstatement in prior years	<u>\$ 334,992</u>
Beginning net assets, as originally presented	\$ 9,434,739
Net reduction in amortization costs previously deducted	<u>334,992</u>
Beginning net assets, as restated	<u>\$ 9,769,731</u>

INDIVIDUAL FUND FINANCIAL STATEMENTS SECTION

Broad River Water Authority
Schedule of Revenues and Expenditures - Budget and Actual (Non-GAAP)
For the Fiscal Year Ended June 30, 2012

	Final Budget	Actual	Variance Favorable (Unfavorable)
Operating revenue:			
Water service	\$ 5,800,000	\$ 5,948,284	\$ 148,284
Tap and connection fees	110,150	118,416	8,266
Water testing fees	4,500	6,850	2,350
Late fees	145,000	169,588	24,588
Other operating	239,000	141,723	(97,277)
Total operating revenue	6,298,650	6,384,861	86,211
Non-operating revenue:			
Capital contributions	489,900	563,444	73,544
Interest earned	200	302	102
Total non-operating revenue	490,100	563,746	73,646
Total revenue	6,788,750	6,948,607	159,857
Operating expenses:			
Salaries and employee benefits	1,233,500	1,209,407	24,093
Professional services	74,200	68,984	5,216
Departmental supplies and expenses	388,000	343,408	44,592
Telephone	16,500	18,821	(2,321)
Travel and training	6,000	8,423	(2,423)
Repairs and maintenance	30,000	39,750	(9,750)
Vehicle maintenance	65,000	60,238	4,762
Licenses and franchise fees	5,000	5,366	(366)
Utilities	430,000	381,707	48,293
Contracted services	138,600	127,333	11,267
Principal retirement	1,540,500	1,540,457	43
Interest expense	1,367,900	1,409,764	(41,864)
Capital outlay	1,286,500	933,305	353,195
Other operating	22,000	28,602	(6,602)
Total operating expenses	6,603,700	6,175,565	428,135
Other financing sources/(uses):			
Addition to fund balance	(185,050)		185,050
	(185,050)	-	185,050
Revenues over expenses and other financing uses	\$ -	\$ 773,042	\$ 773,042

Reconciliation from budgetary basis (modified accrual basis) to full accrual net income (2012):

Revenues over expenses	\$ 773,042
Reconciling items:	
Depreciation expense	(1,062,657)
Amortization expense	(81,036)
Acquisition of property and equipment	933,305
Debt service principal payments	1,540,457
Change in net assets	\$ 2,103,111

Compliance

BURLESON & EARLEY, P.A.

CERTIFIED PUBLIC ACCOUNTANTS

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*

INDEPENDENT AUDITORS' REPORT

To the Board of Directors
Broad River Water Authority
Spindale, North Carolina

We have audited the accompanying financial statements of the Broad River Water Authority, as of and for the year ended June 30, 2012, which collectively comprise the Broad River Water Authority's basic financial statements, and have issued our report thereon dated November 8, 2012. 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.

Internal Control Over Financial Reporting

Management of the Broad River Water Authority is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered the Broad River Water Authority's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Town's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Town's internal control over financial reporting.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A material weakness is a deficiency, or combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the Authority's financial statements will not be prevented, or detected and corrected on a timely basis.

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

POST OFFICE BOX 2125 ♦ CANDLER, NC 28715
902 SAND HILL ROAD ♦ ASHEVILLE, NC 28806
TELEPHONE: (828) 251-2846 ♦ FAX: (828) 251-1144

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Broad River Water Authority'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*.

We noted certain matters that we reported to management of the Broad River Water Authority, in a separate letter dated November 8, 2012.

This report is intended solely for the information and use of management, others within the entity, and the governing council and is not intended to be and should not be used by anyone other than these specified parties.

Burleson & Earley, P.A.
Certified Public Accountants
November 8, 2012