

**CITY OF CAVE SPRINGS  
WATER AND SEWER DEPARTMENT  
Cave Springs, Arkansas  
FINANCIAL STATEMENTS  
and  
SUPPLEMENTARY INFORMATION  
For the Years Ended  
December 31, 2016 and 2015  
and  
INDEPENDENT AUDITOR'S REPORT**

**CITY OF CAVE SPRINGS WATER AND SEWER DEPARTMENT**  
**Cave Springs, Arkansas**  
**FINANCIAL STATEMENTS AND SUPPLEMENTARY INFORMATION**  
**For the Years Ended December 31, 2016 and 2015**

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# BERRY & ASSOCIATES, P.A.

## **Certified Public Accountants**

American Institute of CPAs

Arkansas Society of CPAs

Texas Society of CPAs

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### INDEPENDENT AUDITOR'S REPORT

**Honorable Travis Lee, Mayor  
and Members of the City Council  
City of Cave Springs Water and Sewer Department  
Cave Springs, Arkansas**

#### **Report on the Financial Statements**

We have audited the accompanying financial statements of the Water and Sewer Department of the City of Cave Springs, Arkansas, as of and for the years ended December 31, 2016 and 2015, 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.

#### **Auditor's Responsibility**

Our responsibility is to express opinions on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

An audit includes performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

#### **Opinion on the 2015 Financial Statements**

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the City of Cave Springs Water and Sewer Department as of December 31, 2015, and the respective changes in financial position, and cash flows thereof for the years then ended in accordance with accounting principles generally accepted in the United States of America.

#### **Basis for Qualified Opinion on 2016 Financial Statements**

Because of the inadequacy of accounting records for the year ended December 31, 2016, we were unable to obtain sufficient appropriate audit evidence regarding the amounts at which other transfers are recorded in the accompanying Statement of Revenues, Expenses, and Changes in Net Position at December 31, 2016 (stated at \$71,405).

Honorable Travis Lee, Mayor  
and Members of the City Council  
City of Cave Springs

**Qualified Opinion on the 2016 Financial Statements**

In our opinion, except for the possible effects of the matter discussed in the Basis for Qualified Opinion paragraph, the financial statements referred to in the first paragraph present fairly, in all material respects, the respective financial position of the City of Cave Springs Water and Sewer Department as of December 31, 2016, and the respective changes in financial position, and cash flows thereof for the year 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 June 21, 2018 on our consideration of the Water and Sewer Department of the City of Cave Springs, Arkansas'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 the Water and Sewer Department of the City of Cave Springs, Arkansas's internal control over financial reporting and compliance.

**Emphasis of Matter**

As discussed in Note 1, the financial statements present only the Water Department and do not purport to, and do not, present fairly the financial position of the City of Cave Springs, Arkansas, as of December 31, 2016 and 2015, the changes in its financial position, or, where applicable, its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.



BERRY & ASSOCIATES, P.A.  
Little Rock, Arkansas  
June 21, 2018

**CITY OF CAVE SPRINGS WATER AND SEWER DEPARTMENT  
STATEMENTS OF NET POSITION  
December 31, 2016 and 2015**

<b>ASSETS</b>		
	2016	2015
<b>CURRENT ASSETS</b>		
Cash and cash equivalents	\$ 607,458	\$ 756,402
Accounts receivable	110,488	82,061
Total current assets	717,946	838,463
<b>NON-CURRENT ASSETS</b>		
Restricted assets		
Cash and cash equivalents	1,048,575	959,116
Capital assets		
Capital assets, net of accumulated depreciation	11,247,926	11,471,767
Other assets		
Construction in progress	890,912	167,105
<b>TOTAL ASSETS</b>	\$ 13,905,359	\$ 13,436,451
<b>LIABILITIES AND NET POSITION</b>		
<b>CURRENT LIABILITIES</b>		
Accounts payable	\$ 32,346	\$ 139,390
Retainage payable	25,231	-
Sales tax payable	4,583	4,776
Current portion of long-term debt	60,900	77,300
Accrued interest payable	16,724	41,400
Total current liabilities	139,784	262,866
<b>CURRENT LIABILITIES PAYABLE FROM RESTRICTED ASSETS</b>		
Meter deposits	130,724	100,465
<b>NON-CURRENT LIABILITIES</b>		
Long-term debt, net of current portion	1,628,260	1,689,159
<b>TOTAL LIABILITIES</b>	1,898,768	2,052,490
<b>NET POSITION</b>		
Net investment in capital assets	10,399,217	9,841,409
Temporarily restricted	131,839	131,664
Unrestricted	1,475,535	1,410,888
Total net position	12,006,591	11,383,961
<b>TOTAL LIABILITIES AND NET POSITION</b>	\$ 13,905,359	\$ 13,436,451

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

**CITY OF CAVE SPRINGS WATER AND SEWER DEPARTMENT**  
**STATEMENTS OF REVENUES, EXPENSES, AND CHANGE IN NET POSITION**  
**For the Years Ended December 31, 2016 and 2015**

	<u>2016</u>	<u>2015</u>
<b>OPERATING REVENUES</b>		
Water revenue	\$ 711,407	\$ 821,009
Sewer revenue	497,291	225,095
Water & sewer tapping/connection fees	33,306	164,498
Pump package sales	-	76,118
Sewer tank sales	206,976	45,000
Penalties	17,636	12,727
Miscellaneous	<u>73,419</u>	<u>30,928</u>
Total operating revenues	<u>1,540,035</u>	<u>1,375,375</u>
<b>OPERATING EXPENSES</b>		
<b>Water:</b>		
Water purchases	137,281	142,489
Depreciation	74,893	65,924
Salaries & wages	228,472	118,897
Dues and subscriptions	8,176	7,222
Software fees	-	5,106
Bank fees	547	3,237
Office supplies	12,658	9,648
Professional fees	89,166	62,327
Repairs and maintenance	85,512	112,477
Fuel	9,039	2,857
Insurance	2,485	880
Miscellaneous	12,161	7,112
Taxes and licenses	-	115
Training	8,736	1,084
Travel	169	52
Utility permits and locates	1,866	4,498
Utilities	<u>62,711</u>	<u>14,068</u>
Total Water Expenses	<u>733,872</u>	<u>557,993</u>
<b>Sewer:</b>		
Depreciation	194,388	153,291
Office supplies	4,407	628
Professional fees	12,982	-
Repairs and maintenance	23,602	79,260
Sewer maintenance fees	91,935	69,465
Telephone & utilities	16,675	-
Travel	117	-
Sewer pumps	-	71,375
Sewer tanks	-	99,937
Miscellaneous	<u>7,873</u>	<u>-</u>
Total sewer expenses	<u>351,979</u>	<u>473,956</u>
Total operating expenses	<u>1,085,851</u>	<u>1,031,949</u>
<b>OPERATING INCOME</b>	<u>\$ 454,184</u>	<u>\$ 343,426</u>

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

**CITY OF CAVE SPRINGS WATER AND SEWER DEPARTMENT  
STATEMENTS OF REVENUES, EXPENSES, AND CHANGE IN NET POSITION, Continued  
For the Years Ended December 31, 2016 and 2015**

<b>NON-OPERATING REVENUE (EXPENSES)</b>	<u>2016</u>	<u>2015</u>
Interest income	\$ 1,152	\$ 1,272
Interest expense	(74,628)	(75,448)
Grant income	-	651,029
Other Income	<u>262,997</u>	<u>-</u>
Net non-operating income	<u>189,521</u>	<u>576,853</u>
<b>OTHER FINANCING SOURCES (USES)</b>		
Transfers (to) from other funds	(92,480)	27,289
Other transfers	<u>71,405</u>	<u>-</u>
Total other financing sources (uses)	<u>(21,075)</u>	<u>27,289</u>
<b>CHANGE IN NET POSITION</b>	622,630	947,568
<b>NET POSITION - BEGINNING OF YEAR</b>	<u>11,383,961</u>	<u>10,436,393</u>
<b>NET POSITION - END OF YEAR</b>	<u>\$ 12,006,591</u>	<u>\$ 11,383,961</u>

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

**CITY OF CAVE SPRINGS WATER AND SEWER DEPARTMENT  
STATEMENTS OF CASH FLOWS  
For the Years Ended December 31, 2016 and 2015**

	2016	2015
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>		
Cash received from customers	\$ 1,511,608	\$ 1,355,563
Cash payments to suppliers	(673,745)	(655,660)
Cash payments to employees	(194,572)	(118,897)
Net cash provided by operating activities	643,291	581,006
<b>CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES:</b>		
Grant proceeds	262,997	651,029
Loan proceeds	-	154,500
Purchases of capital assets	(45,439)	(900,872)
Costs paid on construction in progress	(723,807)	(167,105)
Principal payments on long-term debt	(77,299)	(30,845)
Interest payments on long-term debt	(99,303)	(51,648)
Net cash used by capital and related financing activities	(682,851)	(344,941)
<b>CASH FLOWS FROM NON-CAPITAL FINANCING ACTIVITIES:</b>		
Transfers (to) from to other funds	(92,480)	27,289
Other transfers	71,405	-
Net cash provided (used) by non-capital financing activities	(21,075)	27,289
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>		
Net activity of restricted cash	(89,461)	(261,058)
Interest received	1,152	1,272
Net cash used by investing activities	(88,309)	(259,786)
<b>NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS</b>	(148,944)	3,568
<b>CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR</b>	756,402	752,834
<b>CASH AND CASH EQUIVALENTS AT END OF YEAR</b>	\$ 607,458	\$ 756,402
<b>Reconciliation of operating income to net cash provided by operating activities:</b>		
Operating income	\$ 454,184	\$ 343,426
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation and amortization	269,281	219,215
(Increase) Decrease in:		
Accounts receivable	(28,427)	(19,812)
Increase (Decrease) in:		
Accounts payable	(107,044)	34,404
Retainage payable	25,231	(31,097)
Sales tax payable	(193)	1,570
Customer deposits	30,259	33,300
Net cash provided by operating activities	\$ 643,291	\$ 581,006

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



**CITY OF CAVE SPRINGS WATER AND SEWER DEPARTMENT**  
**NOTES TO FINANCIAL STATEMENTS**  
**December 31, 2016 and 2015**

**NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:**

**Organization**

The City of Cave Springs, Arkansas, Water and Sewer Department is an enterprise fund. Enterprise funds are proprietary funds used to account for business-like activities provided to the general public. These activities are financed primarily by user charges and the measurement of financial activity focuses on net income measurement similar to the private sector. The fund is used to record the revenues and expenses from the operation of the water and sewer system.

**Basis of Presentation and Accounting**

The accounts of the Department are organized on the basis of a proprietary fund type, specifically an enterprise fund. The activities of this fund are accounted for with a separate set of self-balancing accounts that comprise the Department's assets, liabilities, net position, revenues and expenses. Enterprise Funds account for activities (i) that are financed with debt that is secured solely by a pledge of the net revenues from fees and charges of the activity; or (ii) that are required by laws or regulations that the activity's costs of providing services, including capital costs (such as depreciation or debt service), be recovered with fees and charges, rather than with taxes or similar revenues; or (iii) that the pricing policies of the activity establish fees and charges designed to recover its costs, including capital costs (such as depreciation or debt service).

The accounting and financial reporting treatment applied to the Department is determined by its measurement focus. The transactions of the Department are accounted for on a flow of economic resources measurement focus. With this measurement focus, all assets and all liabilities associated with the operations are included on the statement of net position. Net position (i.e., total assets net of total liabilities) are segregated into net investment in capital assets, restricted for debt service; and unrestricted components.

**Estimates**

Management of the Department has made certain estimates and assumptions relating to the reporting of assets and liabilities and revenues and expenses to prepare these financial statements in conformity with generally accepted accounting principles. Actual results may differ from those estimates.

**Cash and Cash Equivalents**

The Department considers all highly liquid investments (including restricted cash and investments) with maturities of three months or less when purchased to be cash equivalents. Certificate of deposits are presented at fair value. Short-term investments generally mature or are otherwise available for withdrawal in less than one year.

**Allowance for Bad Debts**

The Department has elected to record bad debts using the direct write-off method. Generally accepted accounting principles require that the allowance method be used to recognize bad debts; however as of December 31, 2016 management had determined that no additional accounts needed to be written off. Bad debt expense for the year ended December 31, 2016 was \$0.

**Budgets and Budgetary Accounting**

Prior to the beginning of the new fiscal year, the Council Members adopt an annual budget for the Department. The budget of the Department is adopted under a basis consistent with GAAP, except that depreciation, certain capital expenses, and nonoperation income and expense items are not considered. All annual appropriations lapse at the fiscal year-end.

**CITY OF CAVE SPRINGS WATER AND SEWER DEPARTMENT  
 NOTES TO FINANCIAL STATEMENTS  
 December 31, 2016 and 2015**

**NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued):**

**Capital Assets**

The cost of additions and major replacements of retired units of property are capitalized. The Department defines capital assets as assets with an initial, individual cost of more than \$1,000 and an estimated useful life in excess of two years. Cost includes direct labor, outside services, materials and transportation, employee fringe benefits, overhead, and interest on funds borrowed to finance construction. The cost and accumulated depreciation of property sold or retired is deducted from capital assets and any profit or loss resulting from the disposal is credited or charged in the nonoperating section of the statements of revenues, expenses and changes in net position. The cost of current repairs, maintenance, and minor replacements is charged to expense. Construction in progress primarily relates to upgrades of existing facilities.

Depreciation has been provided over estimated useful lives of the assets using the straight-line method. The estimated useful lives are as follows:

Asset	Years
Water & Sewer System	25-40
Office Equipment	3-7
Equipment	5-15
Vehicles	5

**Long-Term Debt and Costs**

Long-term debt is reported at face value, net of applicable discounts and deferred loss on refunding. Costs related to the issuance of debt are deferred and amortized over the lives of the various debt issues. Losses occurring from advance refundings of debt are deferred and amortized as interest expense over the remaining life of the old bonds, or the life of the new bonds, whichever is shorter.

**Operating Revenues and Expenses**

Operating revenues and expenses consist of those revenues that result from the ongoing principal operations of the Department. Operating revenues consist primarily of charges for services. Nonoperating revenues and expenses consist of those revenues and expenses that are related to financing and investing type of activities and result from nonexchange transactions or ancillary activities. When an expense is incurred for purposes for which there are both restricted and unrestricted net position available, it is the Department’s policy to apply those expenses to restricted net position to the extent such are available and then to unrestricted net position.

**Equity Classification**

Net position comprises the various net earnings from operating income, nonoperating revenues and expenses, and capital contributions. Net position is classified in the following three components:

*Net Investment in Capital Assets*-This component of net position consists of capital assets, net of accumulated depreciation and reduced by the outstanding balances of any bonds, mortgages, notes or other borrowings that are attributable to the acquisition, construction or improvements of those assets. If there are significant unspent related debt proceeds at year-end, the portion of the debt attributable to the unspent proceeds is not included in the calculation of net investment in capital assets. Rather, that portion of debt is included in the same net position component as the unspent proceeds.

*Temporarily Restricted*- This component of net position consists of constraints imposed by creditors (such as through debt covenants), grantors, contributors, or laws or regulations of other governments or constraints imposed by law through constitutional provisions or enabling legislation.

*Unrestricted* - This component of net position consists of net position that does not meet the definition of “restricted.”

**Capitalized Interest**

Interest costs are capitalized when incurred on debt where proceeds were used to finance the construction of assets. Interest earned on proceeds of tax-exempt borrowing arrangements restricted to the acquisition of qualifying assets is offset against interest costs in determining the amount to be capitalized.

**CITY OF CAVE SPRINGS WATER AND SEWER DEPARTMENT**  
**NOTES TO FINANCIAL STATEMENTS**  
**December 31, 2016 and 2015**

**NOTE 2 – DEPOSITS WITH FINANCIAL INSTITUTIONS:**

All funds are deposited in approved banks. The deposited funds are insured by the Federal Deposit Insurance Corporation (“FDIC”) or collateralized by securities held by the banks in the Department’s name. The deposited funds were adequately insured at December 31, 2016.

**NOTE 3 – CAPITAL ASSETS:**

Capital asset activity for the years ended December 31, 2016 and 2015 was as follows:

	Balance 12/31/15	Additions	Retirements and transfers	Balance 12/31/16
Land & Easements	\$ 642,500	\$ -	\$ -	\$ 642,500
Sewer System	9,843,620	-	-	9,843,620
Water System	2,409,380	-	-	2,409,380
Equipment - Water	145,830	-	-	145,830
Equipment - Sewer	2,124	9,566	-	11,690
Office Equipment	3,029	-	-	3,029
Vehicles	68,991	35,873	-	104,864
	<u>13,115,474</u>	<u>\$ 45,439</u>	<u>\$ -</u>	<u>13,160,913</u>
Less Accumulated Depreciation	(1,643,707)			(1,912,987)
Total Net Capital Assets	<u>\$ 11,471,767</u>			<u>\$ 11,247,926</u>

	Balance 12/31/14	Additions	Retirements and transfers	Balance 12/31/15
Land & Easements	\$ 642,500	\$ -	\$ -	\$ 642,500
Sewer System	8,608,864	1,234,756	-	9,843,620
Water System	2,224,781	184,599	-	2,409,380
Equipment - Water	94,961	50,869	-	145,830
Equipment - Sewer	2,124	-	-	2,124
Office Equipment	3,029	-	-	3,029
Vehicles	14,291	54,700	-	68,991
	<u>11,590,550</u>	<u>\$ 1,524,924</u>	<u>\$ -</u>	<u>13,115,474</u>
Less Accumulated Depreciation	(1,424,492)			(1,643,707)
Total Net Capital Assets	<u>\$ 10,166,058</u>			<u>\$ 11,471,767</u>

**CITY OF CAVE SPRINGS WATER AND SEWER DEPARTMENT  
NOTES TO FINANCIAL STATEMENTS  
December 31, 2016 and 2015**

**NOTE 4 – LONG-TERM DEBT:**

Long-term debt consists of the following:

	<u>2016</u>	<u>2015</u>
Water System Revenue Bond, serviced by First Security Bank and payable to Arkansas Natural Resources Commission, due in annual installments of \$24,795, including interest at 5.0%, beginning December 2010 through December 2029. The bond is secured by revenues of the Department. (1)	\$ 232,913	\$ 257,363
Arkansas Natural Resources Commission loan, due in annual installments of \$42,449 including interest at 5.0%, beginning June 2013 through June 2032. The bond is secured by property and equipment revenues of the system. (2)	460,059	478,579
Arkansas Natural Resources Commission water revenue bond, due in semi- annual installments of \$15,515 including interest at 5.0%, beginning June 2004 through December 2033. The bond is secured by property and equipment revenues of the system. (3)	371,513	393,159
USDA Department of Rural Development loan, due in monthly installments of \$2,044 including interest at 3.75%, beginning June 2011 through December 2051. The bond is secured by property and equipment revenues of the system. (2)	476,326	482,858
Arkansas Natural Resources Commission loan, due in annual installments of \$10,786 including interest at 3.0%, beginning December 2016 through December 2034. The bond is secured by property and equipment revenues of the system. (2)	<u>148,349</u>	<u>154,500</u>
	1,689,160	1,766,459
Less Current Portion	<u>(60,900)</u>	<u>(77,300)</u>
Long-Term Debt, Net	<u>\$ 1,628,260</u>	<u>\$ 1,689,159</u>

- (1) The bond agreement with Arkansas Natural Resources Commission contains a provision which requires the Department to maintain their water rates at an amount sufficient to (1) pay all operation, repair and maintenance expenses, (2) leave a balance equal to the debt service requirements to which the system revenues are pledged, and (3) maintain a depreciation reserve that accumulates at a rate of 3% of revenues each month for the life of the bond. For the year ended December 31, 2016, the Department did not satisfy this requirement of the rate covenant.
- (2) This debt has no restrictive covenant.
- (3) The bond agreement with Arkansas Natural Resources Commission contains a provision which requires the Department to maintain their water rates at an amount sufficient to (1) pay all operation, repair and maintenance expenses, (2) leave a balance equal to the debt service requirements to which the system revenues are pledged, and (3) maintain a depreciation reserve that accumulates at a rate of \$120 a month for the life of the bond. For the year ended December 31, 2016, the Department did not satisfy this requirement of the rate covenant.

**CITY OF CAVE SPRINGS WATER AND SEWER DEPARTMENT  
NOTES TO FINANCIAL STATEMENTS  
December 31, 2016 and 2015**

**NOTE 4 – LONG-TERM DEBT (continued):**

The annual maturities of long-term debt at December 31, 2016, are as follows:

	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2017	\$ 61,000	\$ 72,660	\$ 133,660
2018	63,700	69,920	133,620
2019	66,500	67,055	133,555
2020	69,500	64,105	133,605
2021	72,700	60,924	133,624
2022-2026	415,600	252,340	667,940
2027-2031	467,900	150,728	618,628
2032-2036	193,800	65,658	259,458
2037-2041	77,300	45,357	122,657
2042-2046	93,200	29,440	122,640
2047-2051	107,960	10,245	118,205
	<u>\$ 1,689,160</u>	<u>\$ 888,431</u>	<u>\$ 2,577,591</u>

Long-term liability activity for the years ended December 31, 2016 and 2015 is as follows:

	<u>Balance</u>		<u>Balance</u>		<u>Due Within</u>
	<u>12/31/15</u>	<u>Additions</u>	<u>Retirements</u>	<u>12/31/16</u>	<u>One Year</u>
Long Term Debt					
Loans	\$ 894,721	\$ -	\$ (37,134)	\$ 857,587	\$ 26,200
Water Revenue Bonds	871,738	-	(40,165)	831,572	34,700
Total	<u>\$ 1,766,459</u>	<u>\$ -</u>	<u>\$ (77,299)</u>	<u>\$ 1,689,160</u>	<u>\$ 60,900</u>

	<u>Balance</u>		<u>Balance</u>		<u>Due Within</u>
	<u>12/31/14</u>	<u>Additions</u>	<u>Retirements</u>	<u>12/31/15</u>	<u>One Year</u>
Long Term Debt					
Loans	\$ 746,514	\$ 154,500	\$ (6,293)	\$ 894,721	\$ 37,200
Water Revenue Bonds	896,290	-	(24,552)	871,738	40,100
Total	<u>\$ 3,285,608</u>	<u>\$ 154,500</u>	<u>\$ (30,845)</u>	<u>\$ 1,766,459</u>	<u>\$ 77,300</u>

The Department has pledged future water customer revenues, net of specified operating expenses, to repay \$1,689,160 in revenue bonds. Proceeds from the bonds were used for building of the Department's water and sewer system. Principal and interest on the bonds are payable through 2051, solely from the water customer net revenues. Principal and interest paid in the year ended December 31, 2016 were \$77,299 and \$99,303, respectively. Principal and interest paid in the year ended December 31, 2015 were \$30,845 and \$51,648 respectively.

**CITY OF CAVE SPRINGS WATER AND SEWER DEPARTMENT  
NOTES TO FINANCIAL STATEMENTS  
December 31, 2016 and 2015**

**NOTE 5 – SUBSEQUENT EVENTS:**

Management has evaluated all the activities of the Department through June 21, 2018 (the date the financial statements were available to be issued) and concluded that no subsequent events have occurred that would require recognition in the financial statements or disclosure in the notes to the financial statements as of December 31, 2016.

**NOTE 6 – RESTRICTED ASSETS:**

Restricted assets consist of cash reserves restricted for specific use and cash deposits for meters by customers.

The following is a list of the restricted cash at December 31:

	2016	2015
Customer Meter Deposits	\$ 325,323	\$ 233,134
Construction Fund	591,413	594,318
Debt Service Reserves	131,839	131,664
	\$ 1,048,575	\$ 959,116

**NOTE 7 – RISK MANAGEMENT:**

The Department is exposed to various levels of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions, injuries to employees; and natural disasters. The Department carries property, vehicle insurance and workers compensation insurance.

There has been no significant reduction in the Department's insurance coverage from the previous year. In addition, there have been no settlements in excess of the Department's coverage in any of the prior three fiscal years.

**NOTE 8 – COMMITMENTS:**

The Department leases the right to discharge treated effluent from its sewage treatment facilities under a Drip Field operating lease. The 50-year lease term began February 11, 2008 and provides rents of \$15 for every connected residence and \$15 for every 208 gallons of commercial effluent discharged through the drip field irrigation system per month. Payment of the rent is subject to the collection of user fees charged to the system's customers by the Department. The lease requires the City of Cave Springs, Arkansas to provide \$1,000,000 of public liability insurance, and \$1,000,000 environmental insurance once volume reaches a certain level.

The Department started a construction project to extend and improve the water system during the year ended December 31, 2015. The Department has entered into contracts with an engineering firm for the oversight of water system rehabilitation project and has incurred costs of \$81,519 as of December 31, 2016. The Department has entered into contracts with a construction contractor for the amount of \$335,210. As of December 31, 2016 the Department has incurred costs of \$252,309 on these contracts.

**CITY OF CAVE SPRINGS WATER AND SEWER DEPARTMENT  
NOTES TO FINANCIAL STATEMENTS  
December 31, 2016 and 2015**

**NOTE 8 – COMMITMENTS (continued):**

The Department started a construction project to relocate a portion of the water system during the year ended December 31, 2015. The Department has entered into contracts with an engineering firm for the oversight of water system rehabilitation project and has incurred costs of \$52,468 as of December 31, 2016. The Department has entered into contracts with a construction contractor for the amount of \$248,702. As of December 31, 2016 the Department has incurred costs of \$242,352 on these contracts.

The Department is the recipient of a \$1,100,000 grant from the Arkansas Economic Development Commission, dated March 20, 2013. The Department has received proceeds of the grant of \$1,099,401 as of December 31, 2015.

**NOTE 9 – PENSION PLAN:**

**Plan Description.** The Department contributes to the Arkansas Public Employees Retirement System (APERS), a cost-sharing multiple-employer defined benefit pension plan that covers municipal employees whose municipalities have elected coverage under this System. APERS provides retirement and disability benefits, annual cost-of-living adjustments, and death benefits to plan members and beneficiaries. Benefit provisions are established by State law and can be amended only by the Arkansas General Assembly. The Arkansas Public Employees Retirement System issues a publicly available financial report that includes financial statements and required supplementary information for APERS. That report may be obtained by writing to Arkansas Public Employees Retirement System, One Union National Plaza, 124 W. Capitol, Little Rock, AR 72201 or by calling 1-800-682-7377.

**Funding Policy.** APERS has contributory and non-contributory plans. Contributory members are required by code to contribute 5% of their salary. Each participating employer is required by code to contribute at a rate established by the Board of Trustees of the system based on the annual actuarial valuation. The current employer rate is 14.76% for January 1 to June 30 and 14.50% for July 1 to December 31 of 2016 annual covered payroll. The Water and Sewer Department's contributions to APERS for the year ending December 31, 2016 were \$25,189, equal to the required contributions for the year.

**Implementation of GASB 68**

In June 2012, GASB issued Statement No. 68, Accounting and Financial Reporting for Pensions – an Amendment of GASB Statement No. 27, which became effective with fiscal year ending June 15, 2014. The Statement establishes standards for public pension plan obligations for participating employers. Under the new statement, a cost-sharing employer whose employees receive pensions through a trust will report in the financial statements a net pension liability, deferred outflows or inflows of resources related to pensions, and pension expense based on its proportionate share of the collective net pension liability of all employers in the plan. A net pension liability can be volatile due to changes in actuarial estimates and the actual investment return. These financial statements do not include the disclosure related to this accounting principal, but would be included in the government wide financial statements and not the individual fund financial statements.

# **BERRY & ASSOCIATES, P.A.**

## **Certified Public Accountants**

American Institute of CPAs

Arkansas Society of CPAs

Texas Society of CPAs

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### **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***

**Honorable Travis Lee, Mayor  
and Members of the City Council  
City of Cave Springs Water and Sewer Department  
Cave Springs, Arkansas**

We have audited, 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, the financial statements of the Water and Sewer Department of the City of Cave Springs, Arkansas, as of and for the year ended December 31, 2016, and the related notes to the financial statements, which collectively comprise the Water and Sewer Department of the City of Cave Springs, Arkansas's financial statements and have issued our report thereon dated June 21, 2018.

#### **Internal Control Over Financial Reporting**

In planning and performing our audit of the financial statements, we considered the Department's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Department's internal control. Accordingly, we do not express an opinion on the effectiveness of the Department's internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected in 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 as items 2016-001, 2016-002, 2016-003, and 2016-004 that we consider to be significant deficiencies.

#### **Compliance and Other Matters**

As part of obtaining reasonable assurance about whether the Department'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 instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* and which are described in the accompanying schedule of findings and responses as item 2016-005.



Honorable Travis Lee, Mayor  
and Members of the City Council  
City of Cave Springs  
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**Response to Findings**

The Water and Sewer Department of the City of Cave Springs, Arkansas' responses to the findings identified in our audit are described in the accompanying schedule of findings. The Department's responses were 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 entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.



Berry & Associates, P.A.  
Little Rock, Arkansas  
June 21, 2018

**CITY OF CAVE SPRINGS WATER AND SEWER DEPARTMENT  
SCHEDULE OF FINDINGS AND RESPONSES  
For the Year Ended December 31, 2016**

**2016-001 Internal Control – Segregation of Duties**

Criteria: The segregation of duties and responsibilities between different individuals for custody of assets, recordkeeping and those assets and reconciliation of those asset accounts is an important control activity needed to adequately protect the entity's assets and ensure accurate financial reporting.

Condition: Presently the same individual who is responsible for customer billing and adjustment, receives customer payments, and posts payments to subsidiary accounts receivable ledger. Also, the same individual who is responsible for general ledger activity, including posting and writing checks, also reconciles the bank statement. In addition, only limited oversight is provided over this individual in the conduct of their daily functions. This finding was also noted in 2015.

Cause: The Department's limited size and staffing resources have made it difficult for management to provide sufficient staffing to fully segregate incompatible duties in a cost-effective manner.

Effect or Potential Effect: Without sufficient segregation of duties, the risk significantly increases that errors and fraud related to utility billing and collection activities, including misappropriation of assets, could occur and not be detected within a timely basis.

Recommendation: We recommend that management of the Department should consider a formal evaluation of their risks associated with this lack of duty segregation over utility cash and receivables. In response to the identified risks, consideration should be given to identifying and implementing controls that could help mitigate the risks associated with lack of segregation of duties, such as providing increased management oversight. For example, the Department might consider soliciting the assistance of an independent volunteer to perform certain functions including to act as compensating procedures where applicable.

Responsible Official's Response: The Department concurs with the recommendation, although, the cost to correct this condition might exceed the benefit, the Department has made certain changes in procedures that will improve the overall lack of segregation of duties and has implemented compensating procedures as applicable.

**2016-002 Internal Control – Review and approval of adjustments to customer accounts**

Criteria: Adjustments to customer accounts should be approved by a party independent of the person who enters transactions to the accounts receivable subsidiary ledger.

Condition: Adjustments in aggregate reduced or credited the amounts billed to customer accounts. This finding was also noted in 2015.

Cause: The Department's limited size and staffing resources have made it difficult for management to provide sufficient oversight to properly supervise this necessary function.

Effect or Potential Effect: Without proper approval of adjustments posted to customer accounts by a party independent of the person recording transactions to the customer accounts receivable subsidiary ledger, the Department faces exposure to irregularities or unusual items that may require investigation on a timely basis.

Recommendation: We recommend that the management of the Department approve all monthly adjustments posted to the customer accounts receivable subsidiary ledger by someone other than the one who posts the original entry to the accounts receivable subsidiary ledger.

Responsible Official's Response: The Department concurs with the recommendation.

**CITY OF CAVE SPRINGS WATER AND SEWER DEPARTMENT  
SCHEDULE OF FINDINGS AND RESPONSES  
For the Year Ended December 31, 2016**

**2016-003 Internal Control – Inadequate Payroll Reimbursement**

Criteria: The Department is responsible for the proper recording and documentation of payroll transactions to enable management and City Council oversight of the recording process according to generally accepted accounting principles in the United States of America.

Condition: Transactions in the accounting records did not properly reflect the gross wages, employer payroll taxes, retirement expenses and health insurance costs for the respective employees of the Department. The Department recorded monthly payments payable to the general fund of the City of Cave Springs, but did not adequately account for the cost of the Departments' employees. A transfer in the amount of \$39,713 is reflected in the financial statements to account for the differences between the costs of the employees and the sum of the payments made to the City of Cave Springs general fund.

Cause: The Department did not properly record the respective transactions.

Effect or Potential Effect: Management was unable to adequately determine the costs of the Department's employees, thus not permitting the preparation of accurate and reliable financial statements.

Recommendation: We recommend that the Department properly record the costs and related employer expense of the Department's employees in the accounting records and reimburse the City of Cave Springs' general fund for these respective costs.

Responsible Official's Response: The Department concurs with the recommendation.

**2016-004 Internal Control – Inadequate Accounting Records**

Criteria: The Department is responsible for the proper recording and documentation of all financial activity, and maintaining segregated records for the water and sewer funds from other funds' activity.

Condition: The water and sewer fund accounts were not properly segregated from other funds. Several journal entries were made throughout the year to adjust bank account balances without supporting documentation. Many of the capitalized asset and long-term liability accounts were not recorded on the Department's accounting records.

Cause: The Department did not properly record transactions, carry forward capitalized assets and long-term debt, and segregate water and sewer activity.

Effect or Potential Effect: Management was unable to adequately segregate the activity of the Department thus not permitting the preparation of accurate and reliable financial statements.

Recommendation: We recommend that the Department properly segregate the Department's financial accounts in either a separate file or use proper classifications to ensure fund segregation in the accounting records. All transactions should be entered and bank accounts reconciled on a regular and consistent basis to ensure that all activity is properly recorded. Also, journal entries should be reduced to transactions that are in need of correction or necessary accruals. Capitalized assets and long-term debt should be maintained in the accounting records.

Responsible Official's Response: The Department concurs with the recommendation.

**CITY OF CAVE SPRINGS WATER AND SEWER DEPARTMENT  
SCHEDULE OF FINDINGS AND RESPONSES  
For the Year Ended December 31, 2016**

**2016-005 Compliance –Revenue Bond Agreements**

Criteria: The Department was not in compliance with the revenue bond agreements established by Arkansas Natural Resources Commission regarding depreciation cash reserve requirements, and the filing of annual audits with the Division of Legislative Audit as required by Arkansas Code 14-234-119 through 122.

Conditions: Revenue Bond 00824-WSSW-L with the Arkansas Natural Resources Commission requires a depreciation reserve to be accumulated at a rate of 3% of the gross revenue monthly while the bond is outstanding.

Revenue Bond 00105-WSSW-D with the Arkansas Natural Resources Commission requires a depreciation reserve to be accumulated at a rate of \$120 a month while the bond is outstanding.

Annual audit reports are required to be submitted to Arkansas Natural Resources Commission no later than 120 days following the period covered by the audit for obligation ANRC00105-WSSW-D, and obligation ANRC 00824-WSSW-L. All Annual audits are to be also filed with the Division of Legislative Audit as required by Arkansas Code 14-234-1198 through 122, in a timely manner, within one year of the period covered by the audit. This finding was also noted in 2015.

Cause: The Department has not maintained a depreciation cash reserve account adequate to be in compliance with the requirements set for in the revenue bond agreement. The Department has not filed timely annual audit reports with Arkansas Natural Resources Commission or Division of Legislative Audit.

Effect or Potential Effect: Non-compliance with the terms of the agreements may make the Department ineligible for further financial assistance from the state, and may be subject to an assessed penalty.

Recommendation: We recommend that the Department make the required monthly transfers to the depreciation cash reserve accounts and file future annual audit reports in a timely manner.

Responsible Official's Response: The Department concurs with the recommendation.