

**Water and Sewer Fund of the  
City of Harrison, Arkansas**

**Audited Financial Statements  
December 31, 2012 and 2011**

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**WATER AND SEWER FUND OF THE CITY OF HARRISON, ARKANSAS**  
**AUDITED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2012 AND 2011**

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**WATER AND SEWER FUND OF THE CITY OF HARRISON, ARKANSAS  
MANAGEMENT'S DISCUSSION AND ANALYSIS  
FOR THE YEARS ENDED DECEMBER 31, 2012 AND 2011**

As management of the Water and Sewer Fund of the City of Harrison, Arkansas (the Utility), we offer readers of the City of Harrison, Arkansas's (the City) financial statements this overview and analysis of the financial activities of the Utility for the years ended December 31, 2012 and 2011. The Utility is a fund of the City and is accounted for separately as an enterprise fund.

Enterprise funds account for activities similar to those found in the private business sector, where the determination of net income is necessary or useful for sound financial administration. Enterprise funds are reported using the full accrual method of accounting in which all assets and all liabilities associated with the operation of these funds are included on the balance sheet. The focus of enterprise funds is on income measurement, which, together with the maintenance of equity, is an important financial indication.

The Utility provides water, sewer and sanitation services to residential, commercial and industrial customers in and around Harrison, Arkansas.

**Overview of the Financial Statements**

This annual report includes this Management's Discussion and Analysis report, the Basic Financial Statements and the Notes to Financial Statements.

The financial statements of the Utility report information of the Utility using accounting methods similar to those used by private sector companies. These statements offer short-term and long-term financial information about the Utility's activities. The Statement of Net Position includes all the Utility's assets and liabilities and provides information about the nature and amounts of investments in resources (assets) and obligations to the Utility's creditors (liabilities). It also provides the basis for evaluating the capital structure of the Utility and assessing the liquidity and financial flexibility of the Utility.

All of the current year's revenues and expenses are accounted for in the Statement of Revenues, Expenses and Changes in Net Position. This statement measures the success of the Utility's operations over the past year and can be used to determine whether the Utility has successfully recovered all its costs through its user fees and other charges, profitability and credit worthiness.

The Statement of Cash Flows reports cash receipts, cash payments, and net changes in cash resulting from operating, investing, and financing activities and provides answers to such questions as where did cash come from, what was cash used for, and what was the change in the cash balance during the reporting period.

The Notes to Financial Statements provide additional information that is essential to a full understanding of the data provided in the basic financial statements.

**Financial Highlights**

	<u>2012</u>	<u>2011</u>	<u>2010</u>	<u>2009</u>
Total Assets	\$ 20,889,079	\$ 19,624,426	\$ 18,681,564	\$ 18,291,596
Net Capital Assets	15,927,085	15,195,295	14,898,512	15,003,001
Total Liabilities	921,698	803,763	622,065	588,089
Net Position Invested in Capital Assets	15,927,085	15,195,295	14,898,512	15,003,001
Unrestricted Net Position	4,040,296	3,625,368	3,160,987	2,700,506
Total Net Position	19,967,381	18,820,663	18,059,499	17,703,507
Total Operating Revenues	5,698,989	5,710,683	5,463,028	4,924,599
Total Operating Expenses	5,874,390	5,752,804	5,685,224	5,224,132
Total Other Revenues	1,322,119	803,285	486,453	1,028,687
Increase (Decrease) in Net Position	1,146,718	761,164	264,257	729,154
Prior Period Adjustment	-	-	91,735	-

**Total Assets** - Total assets increased approximately \$1,264,000 from December 31, 2011 to 2012. This increase was due primarily to increases in cash and cash equivalents and net property, plant and equipment.

**Net Capital Assets** - Net capital assets increased approximately \$732,000 from December 31, 2011 to 2012. This increase was due to capital improvements of \$1,311,000, which were off-set by an increase in accumulated depreciation of \$580,000.

**Total Liabilities** - Total liabilities increased approximately \$118,000 from December 31, 2011 to 2012, due to increases in inter-fund accounts payable and accrued liabilities.

**Total Net Position** - Total net position increased approximately \$1,147,000 from December 31, 2011 to 2012, due to income from sales tax revenue (\$1,289,000) and interest income (\$33,000) offset by an operating loss (\$175,000) increases in operating and sales tax revenues.

**Total Operating Revenues** - Total operating revenues decreased approximately \$12,000 from December 31, 2011 to 2012. This decrease was due to a \$133,000 net decrease in water, sewer and other operating income offset by an increase in sanitation revenue of \$121,000.

**Total Operating Expenses** - Total operating expenses increased approximately \$121,000 from December 31, 2011 to 2012 due primarily to increases in water purchases of \$82,000, depreciation of \$11,000, and sanitation contracted services of \$66,000, which were offset by decreases in administrative and other expenses of \$38,000. Due to the reclassification of accounts between categories sanitation contracted services shows a decrease on the financial statements of \$41,000, and administrative and other expenses on the financial statements shows an increase of \$69,000.

**Total Other Income (Expense)** - Total other revenues increased approximately \$519,000 from December 31, 2011 to 2012 due primarily to an increase in infrastructure projects funded by the tax revenue of a 1/2 cent sales tax. The amount received each year is dependent upon the infrastructure projects scheduled for that year.

#### **Contacting the Utility's Financial Management**

The Utility's financial statements are designed to present users (citizens, taxpayers, customers, investors and creditors) with a general overview of the Utility's finances and to demonstrate the Utility's accountability. If you have questions about the report or need additional financial information, please contact Luke Feighert, Finance Director, at 114 S. Spring, Harrison, Arkansas 72602.

**PORTERFIELD KILLINGSWORTH CPA, PLLC**  
accountants • auditors • advisors

**INDEPENDENT AUDITORS' REPORT**

To the Honorable Mayor and Members of the City Council of the  
Water and Sewer Fund of the City of Harrison, Arkansas  
Harrison, Arkansas

We have audited the accompanying financial statements of the Water and Sewer Fund (the Utility), of City of Harrison, Arkansas, as of and for the years ended December 31, 2012 and 2011, and the related notes to the financial statements, as listed in the table of contents.

**Management's Responsibility for the Financial Statements**

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

**Auditor's Responsibility**

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

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

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

**Opinion**

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Water and Sewer Fund of City of Harrison, Arkansas, as of December 31, 2012 and 2011, and the 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.

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**Other Matters**

*Required Supplementary Information*

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis information on pages 1 and 2 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

*Other Information*

Our audit was conducted for the purpose of forming an opinion on the financial statements as a whole that comprise the Water and Sewer Fund of the City of Harrison, Arkansas's basic financial statements. The additional information on page 16 is presented for purposes of additional analysis and is not a required part of the basic financial statements.

Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied 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 basic financial statements or to the basic 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 as a whole.

**Other Reporting Required by *Government Auditing Standards***

In accordance with *Government Auditing Standards*, we have also issued our report dated July 1, 2013 on our consideration of the Utility'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 Utility's internal control over financial reporting and compliance.

*Porterfield Killingsworth CPA, PLLC*

Porterfield Killingsworth CPA, PLLC

Harrison, Arkansas  
July 1, 2013

**WATER AND SEWER FUND OF THE CITY OF HARRISON, ARKANSAS**  
**STATEMENTS OF NET POSITION**  
**AS OF DECEMBER 31, 2012 AND 2011**

<b>ASSETS</b>	<b>2012</b>	<b>2011</b>
<b>Current Assets</b>		
Cash and Cash Equivalents	\$ 3,703,932	\$ 3,254,625
Accounts Receivable, less allowance for doubtful accounts of \$10,000 in 2012 and 2011	617,961	646,407
Accounts Receivable - Inter-fund	101,997	-
Inventory	187,797	178,021
<b>Total Current Assets</b>	<b>4,611,687</b>	<b>4,079,053</b>
<b>Restricted Assets</b>		
Meter Deposits	350,307	350,078
<b>Net Restricted Assets</b>	<b>350,307</b>	<b>350,078</b>
<b>Property, Plant and Equipment, at Cost</b>		
Land	13,085	13,085
Property, Plant and Equipment, at Cost	28,824,204	27,512,808
Accumulated Depreciation	(12,910,204)	(12,330,598)
<b>Net Property, Plant and Equipment</b>	<b>15,927,085</b>	<b>15,195,295</b>
<b>Total Assets</b>	<b>\$ 20,889,079</b>	<b>\$ 19,624,426</b>
<b>LIABILITIES AND NET POSITION</b>		
<b>Current Liabilities</b>		
Accounts Payable - Trade	\$ 325,767	\$ 324,289
Accounts Payable - Inter-fund	84,402	-
Accrued Liabilities	83,005	56,574
Accrued Compensated Absences - Current Portion	31,196	29,243
<b>Total Current Liabilities</b>	<b>524,370</b>	<b>410,106</b>
<b>Liabilities Payable from Restricted Assets</b>		
Meter Deposits	350,307	350,078
<b>Total Liabilities Payable from Restricted Assets</b>	<b>350,307</b>	<b>350,078</b>
<b>Long-term Liabilities</b>		
Accrued Compensated Absences - Long-term Portion	47,021	43,579
<b>Total Long-term Liabilities</b>	<b>47,021</b>	<b>43,579</b>
<b>Total Liabilities</b>	<b>921,698</b>	<b>803,763</b>
<b>Net Position</b>		
Invested in Capital Assets	15,927,085	15,195,295
Unrestricted	4,040,296	3,625,368
<b>Total Net Position</b>	<b>19,967,381</b>	<b>18,820,663</b>
<b>Total Liabilities and Net Position</b>	<b>\$ 20,889,079</b>	<b>\$ 19,624,426</b>

See Accompanying Notes and Accountants' Report.

**WATER AND SEWER FUND OF THE CITY OF HARRISON, ARKANSAS  
STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET POSITION  
FOR THE YEARS ENDED DECEMBER 31, 2012 AND 2011**

	<u>2012</u>	<u>2011</u>
<b>Operating Revenues</b>		
Water	\$ 2,819,604	\$ 2,968,356
Sewer	1,720,751	1,792,733
Sanitation	1,063,259	942,191
Other Operating Income	95,375	7,403
<b>Total Operating Revenues</b>	<u>5,698,989</u>	<u>5,710,683</u>
<b>Operating Expenses</b>		
Water Purchases	1,548,559	1,465,722
Sanitation Contracted Service	900,505	942,191
Administrative and Other Expenses	2,845,720	2,776,730
Depreciation	579,606	568,161
<b>Total Operating Expenses</b>	<u>5,874,390</u>	<u>5,752,804</u>
<b>Operating Income (Loss)</b>	<u>(175,401)</u>	<u>(42,121)</u>
<b>Other Income (Expense)</b>		
Infrastructure Sales Tax Revenue	1,289,469	777,407
Interest Income	32,650	25,878
<b>Total Other Income (Expense)</b>	<u>1,322,119</u>	<u>803,285</u>
<b>Increase (Decrease) in Net Position</b>	1,146,718	761,164
<b>Net Position, Beginning of Year</b>	<u>18,820,663</u>	<u>18,059,499</u>
<b>Net Position, End of Year</b>	<u>\$ 19,967,381</u>	<u>\$ 18,820,663</u>

See Accompanying Notes and Accountants' Report.



**WATER AND SEWER FUND OF THE CITY OF HARRISON, ARKANSAS**  
**STATEMENTS OF CASH FLOWS**  
**FOR THE YEARS ENDED DECEMBER 31, 2012 AND 2011**

	<b>2012</b>	<b>2011</b>
<b>Cash Flows from Operating Activities</b>		
Cash Received from:		
Customers	\$ 5,692,060	\$ 5,703,949
Other Operating Activities	95,375	7,403
Cash Paid for:		
Water	(1,548,559)	(1,455,092)
Sanitation Contracted Service	(816,103)	(942,191)
Salaries, Wages and Related Benefits	(1,260,491)	(1,343,988)
Administrative and Other Expenses	(1,621,701)	(1,222,726)
<b>Net Cash Provided by (Used in) Operating Activities</b>	<b>540,581</b>	<b>747,355</b>
<b>Cash Flows from Noncapital Financing Activities</b>		
Infrastructure Sales Tax Revenue	1,187,472	777,407
<b>Net Cash Provided by (Used in) Noncapital Financing Activities</b>	<b>1,187,472</b>	<b>777,407</b>
<b>Cash Flows from Capital Financing Activities</b>		
Purchases of Property, Plant and Equipment	(1,311,396)	(864,944)
<b>Net Cash Provided by (Used in) Capital Financing Activities</b>	<b>(1,311,396)</b>	<b>(864,944)</b>
<b>Cash Flows from Investing Activities</b>		
Transfers (to) from Meter Deposits Restricted Assets	(229)	29,092
Increase (Decrease) in Meter Deposits Liability	229	(29,092)
Interest Income	32,650	25,878
<b>Net Cash Provided by (Used in) Investing Activities</b>	<b>32,650</b>	<b>25,878</b>
<b>Net Increase (Decrease) in Cash and Equivalents</b>	<b>449,307</b>	<b>685,696</b>
<b>Cash and Cash Equivalents, Beginning of Year</b>	<b>3,254,625</b>	<b>2,568,929</b>
<b>Cash and Cash Equivalents, End of Year</b>	<b>\$ 3,703,932</b>	<b>\$ 3,254,625</b>

**Reconciliation of Operating Income (Loss) to Net Cash Provided by (Used in) Operating Activities**

Operating Income (Loss)	\$ (175,401)	\$ (42,121)
Depreciation	579,606	568,161
Changes in Assets and Liabilities:		
Accounts Receivable	28,446	669
Inventory	(9,776)	9,856
Accounts Payable	1,478	132,906
Accounts Payable - Due to Other Funds	84,402	-
Accrued Liabilities	31,826	77,884
<b>Net Cash Provided by (Used in) Operating Activities</b>	<b>\$ 540,581</b>	<b>\$ 747,355</b>

**Supplementary Information**

<b>Cash Paid for Interest</b>	<b>\$ -</b>	<b>\$ -</b>
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See Accompanying Notes and Accountants' Report.

**WATER AND SEWER FUND OF THE CITY OF HARRISON, ARKANSAS**  
**NOTES TO FINANCIAL STATEMENTS**  
**DECEMBER 31, 2012 AND 2011**

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

**Nature of Business**

The Water and Sewer Fund of the City of Harrison, Arkansas (the Utility) is a component unit of the City of Harrison, Arkansas (the City). The Utility is primarily in the business of providing water, sewer and sanitation services to residential, commercial and industrial customers in and around Harrison, Arkansas.

**Reporting Entity**

For financial reporting purposes, in conformity with Governmental Accounting Standards Board (GASB), the Utility includes all funds over which the Utility's management exercises financial accountability.

**Fund Types**

The accounts of the Utility are organized on the basis of funds, each of which is considered a separate accounting entity. The operations of each fund are accounted for with a separate set of self-balancing accounts that comprise its Assets, Liabilities, Net Position, Revenues, and Expenditures.

The Utility's various funds are grouped in the financial statements as a single enterprise fund. Enterprise Funds are used to account for operations that (a) are financed and operated in a manner similar to private business enterprises, where the intent of the governing body is that the costs (expenses, including depreciation) of providing goods and services to the general public on a continuing basis be financed or recovered primarily through user charges; or (b) where the governing body has decided that periodic determination of revenues earned, expenses incurred and/or net income is appropriate for capital maintenance, public policy, management control, accountability, or other purposes.

**Basis of Accounting**

The accompanying financial statements have been prepared on the accrual basis of accounting. Under the accrual basis of accounting, revenues and expenses along with the related assets and liabilities are recorded in the period in which the transactions occur, regardless of when the related cash is received or disbursed.

**Budgets and Budgetary Accounting**

State law requires that the City Council, before the end of each fiscal year, make appropriations, by ordinance, for the expenditures of City government for the following year. The City Council may make appropriation amendments at any time during the current fiscal year. Appropriations lapse at the end of each year. Under certain conditions, the budget may be amended subsequent to year-end.

The Utility prepared the annual budget using the regulatory basis of accounting.

**Cash and Cash Equivalents**

For purposes of the statements of cash flows, the Utility considers all highly liquid investments with a maturity of three months or less to be cash equivalents.

**Investments**

The Utility maintains various cash and investment accounts. The Utility's investment policy states that the Utility will be limited to the purchase of certificates of deposit and Government securities including only direct U.S. Treasury obligations; treasury bills, notes and bonds. Certificates of deposit will be purchased directly from approved banks to enable management the opportunity to evaluate the financial condition of the specific bank.

**WATER AND SEWER FUND OF THE CITY OF HARRISON, ARKANSAS**  
**NOTES TO FINANCIAL STATEMENTS**  
**DECEMBER 31, 2012 AND 2011**

**NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, Continued**

**Interest Rate Risk**

Interest rate risk is the risk that changes in the market interest rates will adversely affect the fair value of an investment. Generally, the longer the maturity of an investment, the greater the sensitivity of its fair value to changes in market interest rates. According to the Utility's investment policy, all investments are monitored for changes in the effective yield. At December 31, 2012 and 2011, all interest bearing accounts are short-term in nature.

**Custodial Credit Risk**

For an investment, custodial credit risk is the risk that, in the event of the failure of the counterparty, the Utility will not be able to recover the value of the investments or collateral securities that are in the possession of the outside party. The Utility has established a policy in which deposits and restricted assets are to be secured by collateral, reduced by the amount of insurance provided by the Federal Deposit Insurance Corporation (FDIC).

**Accounts Receivable**

Accounts receivable primarily consist of credit extended to users in the normal course of business. Customers are required to pay a meter deposit when service commences. At the time service is terminated, these deposits may be applied to any outstanding receivable from the customer. The Utility uses the allowance method to account for uncollectible accounts receivable. In circumstances where management is aware of a specific user's inability to meet financial obligations, a specific reserve is recorded to reduce the receivable to the amount expected to be collected. In addition, the Utility has established a general reserve based upon historical customer performance. Management also performs ongoing credit evaluations of its accounts and those which are considered uncollectible are reserved for through the allowance account. The policy for determining when receivables are past due or delinquent is based on how recently payments have been received. Amounts are written off at the point when collection attempts have been exhausted. Management uses significant judgment in estimating uncollectible amounts. In estimating uncollectible amounts, management considers factors such as current overall economic conditions, industry-specific economic conditions, historical customer performance and anticipated customer performance. While management believes the Utility's processes effectively address its exposure to doubtful accounts, changes in economic, industry or specific customer conditions may require adjustment to the allowance recorded by the Utility.

**Inventory**

Inventory consists of various materials held for use to repair and maintain existing operations. Inventory is valued at average cost, which approximates the first-in, first-out method.

**Inter-Fund Receivables, Payables and Transfers**

Inter-fund receivables and payables result from lending and borrowing arrangements between the Utility and other funds of the City and are referred to as advances to and from other funds.

**Property, Plant and Equipment**

Property, Plant and Equipment is stated at historical cost. Contributed items are stated at estimated fair market value on the date of contribution. Depreciation is calculated using the straight-line method over the estimated useful lives of the depreciable assets. Assets with an initial value or cost greater than or equal to \$2,500 and an estimated useful life greater than one year are capitalized under the Utility's capitalization policy; capital expenditures not meeting this criteria are expensed as incurred. Significant betterments, which increase the useful lives of capital assets, are capitalized and depreciated over the remaining useful life.

**WATER AND SEWER FUND OF THE CITY OF HARRISON, ARKANSAS**  
**NOTES TO FINANCIAL STATEMENTS**  
**DECEMBER 31, 2012 AND 2011**

**NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, Continued**

**Long-Lived Assets**

Impairment of capital assets is a significant and unexpected decline, which is based on triggering events or changes in circumstances that were not anticipated when the capital assets was placed in service. Based on management's assessment, no triggering events or changes in circumstances occurred during the years ended December 31, 2012 or 2011.

**Restricted Assets**

The Utility designated certain funds to be maintained for customer meter deposits. These deposits are held until the customer discontinues the Utility's services.

**Net Position Classifications**

Net Position is classified and presented as follows:

Net Position Invested in Capital Assets, Net of Related Debt consists of capital assets, including restricted capital assets, net of accumulated depreciation and reduced by the outstanding balances of any bonds or other borrowing that is attributable to the acquisition, construction, or improvement of those assets.

Restricted Net Position consists of net assets with constraints placed on the use either by external groups such as creditors, grantors, contributors, or laws or regulations of other governments, or by law through constitutional provision or enabling legislation.

Unrestricted Net Position consists of all other fund equity balances that do not meet the definition of "restricted" or "invested in capital assets, net of related debt."

**Revenue Recognition**

The Utility recognizes revenue when earned, based upon customer usage or when the service is provided. Water, sewer and sanitation revenues are billed to the residents in monthly cycles.

**Classification of Revenues**

Operating revenues generally consist of charges for water, sewer and sanitation usage and other fees billed to customers. Non-operating revenues consist of interest income, sales tax and miscellaneous income.

**Advertising**

The Utility follows the policy of charging the costs of advertising to expense as incurred. Advertising expense for the years ended December 31, 2012 and 2011 was \$0 and \$0, respectively.

**Restricted Resources**

Under the terms of grant agreements, the Utility funds certain infrastructure improvements by a combination of specific improvement-reimbursement grants and general revenues. Thus, when infrastructure improvements are incurred, there may be both restricted and unrestricted net position available to finance these improvements. It is the Utility's policy to first apply improvement-reimbursement grant resources to such improvements and then general revenues.

**WATER AND SEWER FUND OF THE CITY OF HARRISON, ARKANSAS**  
**NOTES TO FINANCIAL STATEMENTS**  
**DECEMBER 31, 2012 AND 2011**

**NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, Continued**

**Compensated Absences**

The Utility has a policy whereby employees can accumulate unused sick and vacation leave and comp time. Sick leave is to be used for periods of illness and can be accrued up to 60 days if the employee has been employed longer than 5 years. Upon termination or retirement, the Utility will pay all accrued vacation days. The Utility has accrued the separation portion of this liability as accrued compensated absences, which totaled \$78,217 and \$72,822 at December 31, 2012 and 2011, respectively.

**Income Taxes**

Income of the Utility is derived from the exercise of essential governmental functions and accrues to the Utility, a component unit of the City of Harrison, Arkansas. It is, therefore, not subject to income taxes and, accordingly, no provision for income taxes has been made in the accompanying financial statements.

**Estimates**

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

**NOTE 2 - FINANCIAL INSTRUMENTS WITH RISK OF ACCOUNTING LOSS**

Financial instruments that could potentially subject the Utility to a risk of accounting loss are carried at fair market value and include restricted and unrestricted Cash and Cash Equivalents and excludes petty cash as follows:

	<u>Bank Balance</u>	<u>Carrying Balance</u>
Insured (FDIC)	\$ -	\$ -
Collateralized by pledged securities	4,064,635	4,053,539
Other assets held in trust	-	-
Uninsured or Uncollaterallized	-	-
Total	<u>\$ 4,064,635</u>	<u>\$ 4,053,539</u>

The Utility, a component unit of the City of Harrison, Arkansas, maintains cash and certificates of deposit in one commercial bank under the City's federal identification number. The total cash balance under the City's federal identification number is insured by the FDIC up to \$250,000. The City participates in a pledged collateral program whereby the bank pledges collateral for balances in excess of the FDIC limit. The Utility believes there is no significant risk with respect to these deposits.

**NOTE 3 - ACCOUNTS RECEIVABLE**

Receivables at December 31, 2012 and 2011 consisted of the following:

	<u>2012</u>	<u>2011</u>
Accounts Receivable – Trade	\$ 626,652	\$ 645,355
Less Allowance for Doubtful Accounts	(10,000)	(10,000)
Net Accounts Receivable – Trade	616,652	635,355
Accounts Receivable – Construction	1,309	11,052
Total Accounts Receivable	<u>\$ 617,961</u>	<u>\$ 646,407</u>

**WATER AND SEWER FUND OF THE CITY OF HARRISON, ARKANSAS**  
**NOTES TO FINANCIAL STATEMENTS**  
**DECEMBER 31, 2012 AND 2011**

**NOTE 4 - PROPERTY, PLANT AND EQUIPMENT**

The following is a summary of property, plant and equipment:

	Estimated Useful Life (in Years)	Balance 12/31/11	Additions	Disposals	Balance 12/31/12
Land	N/A	\$ 13,085	\$ -	\$ -	\$ 13,085
Water Plant	10 - 50	9,125,537	955,488	-	10,081,025
Sewer Plant	50	14,521,877	333,981	-	14,855,858
Machinery and Equipment	5 - 10	1,884,357	4,158	-	1,888,515
Transportation Equipment	5 - 10	948,090	17,769	-	965,859
Furniture, Fixtures and Office Equipment	5 - 15	316,082	-	-	316,082
Water Lines	50	<u>716,865</u>	<u>-</u>	<u>-</u>	<u>716,865</u>
Total Property, Plant and Equipment, at Cost		27,525,893	1,311,396	-	28,837,289
Less Accumulated Depreciation		<u>(12,330,598)</u>	<u>(579,606)</u>	<u>-</u>	<u>(12,910,204)</u>
Net Property, Plant and Equipment		<u>\$ 15,195,295</u>	<u>\$ 731,790</u>	<u>\$ -</u>	<u>\$ 15,927,085</u>

	Estimated Useful Life (in Years)	Balance 12/31/10	Additions	Disposals	Balance 12/31/11
Land	N/A	\$ 13,085	\$ -	\$ -	\$ 13,085
Water Plant	10 - 50	8,438,618	686,919	-	9,125,537
Sewer Plant	50	14,362,752	159,125	-	14,521,877
Machinery and Equipment	5 - 10	1,865,458	18,899	-	1,884,357
Transportation Equipment	5 - 10	948,090	-	-	948,090
Furniture, Fixtures and Office Equipment	5 - 15	316,082	-	-	316,082
Water Lines	50	<u>716,865</u>	<u>-</u>	<u>-</u>	<u>716,865</u>
Total Property, Plant and Equipment, at Cost		26,660,950	864,943	-	27,525,893
Less Accumulated Depreciation		<u>(11,762,437)</u>	<u>(568,161)</u>	<u>-</u>	<u>(12,330,598)</u>
Net Property, Plant and Equipment		<u>\$ 14,898,513</u>	<u>\$ 296,782</u>	<u>\$ -</u>	<u>\$ 15,195,295</u>

Depreciation expense for the years ended December 31, 2012 and 2011 was \$579,606 and \$568,161, respectively.

**NOTE 5 - ARKANSAS PUBLIC EMPLOYEES RETIREMENT SYSTEM PLAN DESCRIPTION**

The City, which includes the Utility, 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. APERS issues a publicly available financial report that includes financial statements and required supplementary information for APERS. That report may be obtained by writing to the Arkansas Public Employees Retirement System, One Union National Plaza, 124 W. Capitol Ave., Little Rock, Arkansas 72201 or by calling 1-800-682-7377.

**WATER AND SEWER FUND OF THE CITY OF HARRISON, ARKANSAS**  
**NOTES TO FINANCIAL STATEMENTS**  
**DECEMBER 31, 2012 AND 2011**

**NOTE 5 - ARKANSAS PUBLIC EMPLOYEES RETIREMENT SYSTEM PLAN DESCRIPTION,**  
*Continued*

**Funding Policy**

APERS has contributory and noncontributory plans. Contributory members are required to contribute 5% of their salary. Each participating employer is required 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 14.24% from July 1, 2012 and 13.47% from July 1, 2011 of annual covered payroll. The Utility's contributions to APERS were \$142,815 and \$136,918 for the years ending December 31, 2012 and 2011, respectively.

**NOTE 6 - RELATED PARTY TRANSACTIONS**

The Utility reimburses the City for its portion of expenses paid directly by the City's general fund. These reimbursements are paid monthly and consist of an accounting fee for administrative, billing and record keeping services, and a maintenance fee for repairs and upkeep of the water and sewer fund fixed assets, along with certain safety fees. During the years ended December 31, 2012 and 2011 the reimbursements were approximately \$362,000 and \$353,000, respectively.

**NOTE 7 - COMMITMENTS AND CONTINGENCIES**

Effective January 1, 1999, the Utility executed an agreement for the purchase of all water from the Carroll Boone Water District. This agreement may be amended by mutual agreement of the parties.

There are no significant minimum rental commitments under operating leases that have initial or remaining non-cancelable lease terms in excess of one year at December 31, 2012.

Effective January 1, 2013, the Utility executed a ten-year agreement for the collection and transfer of solid waste and recyclable materials with Inland Services. This agreement can not be modified or amended unless approved by the governing bodies of both parties and signed by the authorized representatives of the City and the contractor.

At December 31, 2012, there were no material outstanding unfilled contract commitments. At December 31, 2011, the Utility had unfulfilled contract commitments for construction, and repair and maintenance projects in various stages of completion of approximately \$48,000.

In the normal course of operations, the Utility receives grant funds from various federal and state agencies. The grant programs are subject to audit by the granting authority, the purpose of which is to ensure compliance with conditions precedent to the granting of funds. The City believes any liability for reimbursement, which may arise as a result of audits of grant funds, would not be material.

In January 2012 the Utility started the renewal process for its permit to operate a waste water treatment plant. During the renewal process it was discovered that Crooked Creek, which the treatment plant releases into, has an impaired status and the EPA is requiring the ADEQ to establish a total max daily limit (TMDL) for any impaired bodies of water. The Utility attended a Joint Congressional Hearing which granted a delay on the ADEQ's requirement to complete a TMDL on the creek pending the Utility completing a Use Attainability Analysis to modify the water quality criteria. The Utility estimates the total cost to modify the water quality criteria to range from \$150,000 to \$300,000. If the Utility is unsuccessful in their effort to modify the water quality criteria of Crooked Creek, the Utility may be required to make significant improvements and/or additions to the current sewer treatment plant.

**WATER AND SEWER FUND OF THE CITY OF HARRISON, ARKANSAS**  
**NOTES TO FINANCIAL STATEMENTS**  
**DECEMBER 31, 2012 AND 2011**

**NOTE 8 - RISK MANAGEMENT**

The Utility is exposed to various risks of loss from tort, theft of, damage to and destruction of assets, business interruption, errors and omissions, natural disasters, employee injuries and illnesses, and employee health, dental and accident benefits. Commercial insurance coverage is purchased for claims arising from such matters other than employee health and dental benefits and worker's compensation claims. Settled claims have not exceeded this commercial coverage in any of the three proceeding years.

The Utility has joined with other municipalities to form the Arkansas Municipal League Vehicle Insurance Program (the Pool), a public entity risk pool currently operating as a common risk management and insurance program for its members. The Utility pays an annual premium to the Pool for its vehicle insurance coverage. The Pool's governing agreement specifies that the Pool will be self-sustaining through member premiums and will reinsure through commercial carriers for claims in excess of specified stop loss amounts.

**NOTE 9 - WATER AND SEWER RATES**

In order to provide funding for system improvements, various water and sewer rates were established by ordinance in 2007. In May 2012, the rates were increased. The rates in effect for the year ended December 31, 2012 are as follows:

	<u>Water Rates</u>	<u>Sewer Rates</u>
First 1,500 gallons	\$9.72 minimum	\$7.66 minimum
Next 25,000 gallons	\$4.05 per 1,000 GA	\$4.56 per 1,000 GA
Next 250,000 gallons	\$3.65 per 1,000 GA	\$4.45 per 1,000 GA
Usage over 250,000 gallons	\$3.72 per 1,000 GA	\$4.52 per 1,000 GA

Billing rates for both "outside city" water and sewer rates are calculated at \$1.00 plus one hundred fifty percent (150%) of the above appropriate "inside city" rates.

**NOTE 10 - CONCENTRATIONS OF ECONOMIC AND CREDIT RISK**

The Utility's business activities are concentrated with customers located in and near the City of Harrison, Arkansas. All future revenue is associated within the above-mentioned geographic region.

The Utility purchases water from the Carroll Boone Water District. This is the Utility's only contracted source of water. In addition, the Utility contracts all of its solid waste with a single provider.

Financial instruments which potentially subject the Utility to concentrations of credit risk consist primarily of trade receivables with a variety of customers and cash and cash investments deposited with financial institutions.

Concentrations of credit risk with respect to accounts receivable are limited due to the Utility's customer base being made up of a large number of customers, thus spreading the trade credit risk. The Utility performs ongoing credit evaluations of its customers. Customer meter deposits are available to the Utility to apply to any amounts due upon termination of service.

The Utility, a component unit of the City of Harrison, Arkansas, maintains cash in one commercial bank under the City's federal identification number. The total cash balance under the City's federal identification number is insured by the FDIC up to \$250,000. However, the City participates in a pledged collateral program whereby the bank pledges collateral for balances in excess of the FDIC limit. The Utility believes there is no significant risk with respect to these deposits.



**WATER AND SEWER FUND OF THE CITY OF HARRISON, ARKANSAS  
NOTES TO FINANCIAL STATEMENTS  
DECEMBER 31, 2012 AND 2011**

**NOTE 11 - SUBSEQUENT EVENTS**

Management of the Utility has evaluated subsequent events through July 16, 2013, the date on which the financial statements were available to be issued.

**WATER AND SEWER FUND OF THE CITY OF HARRISON, ARKANSAS  
SCHEDULES OF ADMINISTRATIVE AND OTHER EXPENSES  
FOR THE YEARS ENDED DECEMBER 31, 2012 AND 2011**

	<u>2012</u>	<u>2011</u>
Accounting and Auditing	\$ 261,200	\$ 261,362
Billing Fee	28,183	-
Chemicals	66,381	65,365
Conservation	49,505	-
Contracted Services	79,572	75,601
Dues and Subscriptions	1,628	-
Fuel	96,473	98,906
Human Resources	6,276	-
Insurance	80,894	48,576
Maintenance Fund	65,872	63,668
Material and Supplies	64,864	87,075
Other Administrative Expenses	1,487	-
Payroll Taxes	74,902	92,369
Permits	33,577	31,653
Planning Costs	15,787	9,057
Postage	34,464	37,658
Regulatory Compliance	54,503	-
Repairs and Maintenance	390,223	323,709
Salaries, Wages and Related Benefits	1,292,317	1,421,872
Training and Travel	11,686	12,328
Utilities and Telephone	<u>135,926</u>	<u>147,531</u>
<b>Total Administrative and Other Expenses</b>	<u><u>\$ 2,845,720</u></u>	<u><u>\$ 2,776,730</u></u>

See Accountants' Report.

**PORTERFIELD KILLINGSWORTH CPA, PLLC**  
accountants•auditors•advisors

**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**

To the Honorable Mayor and Members of the City Council of the  
Water and Sewer Fund of the City of Harrison, Arkansas

We have audited the financial statements of Water and Sewer Fund of the City of Harrison, Arkansas (the Utility), a component unit of the City of Harrison, Arkansas, as of and for the year ended December 31, 2012, and have issued our report thereon dated July 1, 2013. 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 Utility is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered the Utility's internal control over financial reporting as a basis for designing 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 Utility's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Utility's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over financial reporting that might be significant deficiencies, or material weaknesses and therefore, there can be no assurance that all such deficiencies, significant deficiencies, or material weaknesses have been identified. However, as described in the accompanying schedule of findings and responses, we identified certain deficiencies in internal control over financial reporting that we consider to be material weaknesses.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiencies described in the accompanying schedule of findings and responses as items 2012-1, 2012-2, and 2012-3 to be material weaknesses.

**Compliance and Other Matters**

As part of obtaining reasonable assurance about whether the Utility'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 Utility in a separate letter dated July 1, 2013.

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**Water and Sewer Fund of the City of Harrison, Arkansas**

Page 2 of 2

This report is intended solely for the information and use of management, the Mayor, City Council, others within the entity, and federal and state awarding agencies of the Water and Sewer Fund of the City of Harrison, Arkansas, and is not intended to be and should not be used by anyone other than these specified parties.

*Porterfield Killingsworth CPA, PLLC*

**Porterfield Killingsworth CPA, PLLC**

Harrison, Arkansas

July 1, 2013

**WATER AND SEWER FUND OF THE CITY OF HARRISON, ARKANSAS  
SCHEDULE OF FINDINGS AND RESPONSES  
DECEMBER 31, 2012 AND 2011**

**CURRENT YEAR FINDINGS**

**Finding Number 2012-1 - Segregation of Duties**

**Finding:** Due to the small size and structure of the Utility's accounting and management staffs, there is an inadequate segregation of duties. Further, it is not economically feasible for the Utility to achieve a complete segregation of duties. However, there are opportunities and areas in which the level of segregation of duties can be improved in a cost effective manner.

**Recommendation:** We recommend that management review accounting, management and personnel procedures to identify areas in which duties may be further segregated in a cost effective manner and implement procedures designed to improve overall segregation of duties.

**Response:** With limited office personnel, proper segregation of duties is difficult to achieve though all areas of concern will be scrutinized to limit potential errors or fraud. The City of Harrison is continually updating internal policies and procedures and implementing cost effective changes to improve segregation of duties.

**Finding Number 2012-2 - Transaction Processing, Monthly Reconciliation and Closing Procedures**

**Finding:** The Utility's accounting and management staffs have established transaction processing, monthly reconciliation and closing procedures. Not all of these procedures are formalized in writing. Lack of formalized written procedures may result in reconciliation and closing procedures not being consistently and thoroughly applied, which may allow misstatements of financial records.

**Recommendation:** We recommend that management review and develop written procedures for all significant transaction processing, monthly reconciliation and closing processes.

**Response:** The City of Harrison is continuously updating procedures for transaction processing, monthly reconciliation and closing procedures and is currently working to formalize them in writing.

**Finding Number 2012-3 - Segregation of Duties to Information Technology**

**Finding:** While the Utility has segregated certain duties related to administrator rights to financial applications, the small size of the accounting and management staffs limits the effectiveness of the segregation, especially in the oversight of billing credits and adjustments. Lack of contemporaneous oversight and approval of billing credits and adjustments may lead to misstatements of financial information.

**Recommendation:** We recommend that management review the segregation of duties related to administrator rights to financial applications, especially in the oversight of billing credits and adjustments, in order to establish, to the level possible, contemporaneous oversight and approval of billing credits and adjustments.

**Response:** An essential part of constant upgrades to technology is oversight of the policies and procedures related to accounting and reporting applications, especially approval and input of billing credits and adjustments. The City of Harrison continues to monitor these procedures and will implement cost effective changes to improve segregation of duties to information technology.

**WATER AND SEWER FUND OF THE CITY OF HARRISON, ARKANSAS  
SCHEDULE OF FINDINGS AND RESPONSES  
DECEMBER 31, 2012 AND 2011**

**PRIOR YEAR FINDINGS**

**Finding Number 2011-1 - Segregation of Duties**

**Finding:** Due to the small size and structure of the Utility's accounting and management staffs, there is an inadequate segregation of duties. Further, it is not economically feasible for the Utility to achieve a complete segregation of duties. However, there are opportunities and areas in which the level of segregation of duties can be improved in a cost effective manner.

**Recommendation:** We recommend that management review accounting, management and personnel procedures to identify areas in which duties may be further segregated in a cost effective manner and implement procedures designed to improve overall segregation of duties.

**Response:** With limited office personnel, proper segregation of duties is difficult to achieve though all areas of concern will be scrutinized to limit potential errors or fraud. The City of Harrison is continually updating internal policies and procedures and implementing cost effective changes to improve segregation of duties.

**Finding Number 2011-2 - Transaction Processing, Monthly Reconciliation and Closing Procedures**

**Finding:** The Utility's accounting and management staffs have established transaction processing, monthly reconciliation and closing procedures. Not all of these procedures are formalized and in writing. Lack of formalized written procedures may result in reconciliation and closing procedures not being consistently and thoroughly applied, which may allow misstatements of financial records.

**Recommendation:** We recommend that management review and develop written procedures for all significant transaction processing, monthly reconciliation and closing processes.

**Response:** The City of Harrison is continuously updating procedures for transaction processing, monthly reconciliation and closing procedures and is currently working to formalize them in writing.

**Finding Number 2011-3 - Segregation of Duties to Information Technology**

**Finding:** While the Utility has segregated certain duties related to administrator rights to financial applications, the small size of the accounting and management staffs limits the effectiveness of the segregation, especially in the oversight of billing credits and adjustments. Lack of contemporaneous oversight and approval of billing credits and adjustments may lead to misstatements of financial information.

**Recommendation:** We recommend that management review the segregation of duties related to administrator rights to financial applications, especially in the oversight of billing credits and adjustments, in order to establish, to the level possible, contemporaneous oversight and approval of billing credits and adjustments.

**Response:** An essential part of constant upgrades to technology is oversight of the policies and procedures related to accounting and reporting applications, especially approval and input of billing credits and adjustments. The City of Harrison continues to monitor these procedures and will implement cost effective changes to improve segregation of duties to information technology.