



**OFFICE OF AUDITOR OF STATE**  
**STATE OF IOWA**

David A. Vaudt, CPA  
Auditor of State

State Capitol Building  
Des Moines, Iowa 50319-0004

Telephone (515) 281-5834 Facsimile (515) 242-6134

**NEWS RELEASE**

FOR RELEASE

July 14, 2010

Contact: Andy Nielsen  
515/281-5834

Auditor of State David A. Vaudt today released an audit report on the Xenia Rural Water District.

The District had total revenues of \$10,455,275 for the year ended December 31, 2009, a 9% increase over the prior year. Revenues included water sales of \$8,426,455 and system connection fees of \$578,143. The increase in revenues was due to an increase in water rates and the addition of industrial customers.

Expenses totaled \$12,823,527 for the year ended December 31, 2009, a 24% increase over the prior year. Expenses included \$5,172,851 for interest expense, \$2,795,199 for depreciation and \$1,324,296 for salaries and wages. The increase in expenses is due primarily to increased interest expense and depreciation.

A copy of the audit report is available for review at the Xenia Rural Water District, in the Office of Auditor of State and on the Auditor of State's web site at <http://auditor.iowa.gov/reports/index.html>.

###



**XENIA RURAL WATER DISTRICT**

**INDEPENDENT AUDITOR'S REPORTS**  
**BASIC FINANCIAL STATEMENTS AND**  
**SUPPLEMENTARY INFORMATION**  
**SCHEDULE OF FINDINGS AND QUESTIONED COSTS**

**DECEMBER 31, 2009 and DECEMBER 31, 2008**

## Table of Contents

		<u>Page</u>
Officials		3
Independent Auditor's Report		5-6
Management's Discussion and Analysis		7-12
Basic Financial Statements:	<u>Exhibit</u>	
Statement of Net Assets	A	14-15
Statement of Revenues, Expenses and Changes in Net Assets	B	16-17
Statement of Cash Flows	C	18-19
Notes to Financial Statements		20-34
Other Supplementary Information:	<u>Schedule</u>	
Schedule of Expenditures of Federal Awards	1	36
Independent Auditor's Report on Internal Control over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with <u>Government Auditing Standards</u>		37-38
Independent Auditor's Report on Compliance with Requirements Applicable to Each Major Program and on Internal Control over Compliance in Accordance with OMB Circular A-133		41-42
Schedule of Findings and Questioned Costs		43-51
Staff		52

**Xenia Rural Water District**

**Officials**

<u>Name</u>	<u>Title</u>	<u>Term Expires</u>
Thomas Pierce	Chair	Apr 2011
Dennis Powers	Vice Chair	Apr 2010
Greg Rinehart	Treasurer	Apr 2012
Larry Herron	Secretary	(Resigned)
David Larson (Appointed April 2009)	Secretary	Apr 2011
Brian Sansgaard	Director	Apr 2010
Stacy Young	Director	Apr 2010
Jim Fevold	Director	Apr 2011
Marc Delong	Director	Apr 2012

**Xenia Rural Water District**



**OFFICE OF AUDITOR OF STATE**  
**STATE OF IOWA**

David A. Vaudt, CPA  
Auditor of State

State Capitol Building  
Des Moines, Iowa 50319-0004

Telephone (515) 281-5834 Facsimile (515) 242-6134

Independent Auditor's Report

To the Members of the  
Xenia Rural Water District:

We have audited the accompanying basic financial statements of the Xenia Rural Water District as of and for the year ended December 31, 2009. These financial statements are the responsibility of the District's management. Our responsibility is to express an opinion on these financial statements based on our audit. The financial statements of the Xenia Rural Water District as of and for the year ended December 31, 2008 were audited by other auditors whose report dated June 30, 2009 expressed an unqualified opinion on those financial statements. The auditor's report included an explanatory paragraph regarding conditions which raised substantial doubt about the District's ability to continue as a going concern.

We conducted our audit in accordance with U.S. generally accepted auditing standards 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 examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe our audit provides a reasonable basis for our opinion.

Adverse economic conditions have limited the ability of the District to obtain customers in amounts sufficient to service its long-term debt. As a result, the District's current liabilities exceed current assets by \$9,352,705 at December 31, 2009. The District is currently investigating potential buyers for its facilities. However, there are significant uncertainties regarding the District's ability to continue its operations and to satisfy its creditors on a timely basis. In addition, the District has been unable to renegotiate its borrowings from its lenders. Consequently, adjustments may be required to the recorded asset amounts and classification of liabilities.

In our opinion, except for the adjustments, if any, that may be required to the recorded asset amounts and classification of liabilities discussed in the preceding paragraph, the financial statements referred to above present fairly, in all material respects, the financial position of the Xenia Rural Water District at December 31, 2009 and 2008, and the changes in its financial position and its cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

The accompanying financial statements have been prepared assuming the District will continue as a going concern. The conditions described in the third paragraph of this report raise substantial doubt about the District's ability to continue as a going concern. The financial statements do not include any adjustments which might result from the outcome of this uncertainty.

In accordance with Government Auditing Standards, we have also issued our report dated June 2, 2010 on our consideration of the Xenia Rural Water District's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with Government Auditing Standards and should be considered in assessing the results of our audit.

Management's Discussion and Analysis on pages 7 through 12 is not a required part of the basic financial statements, but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information for the year ended December 31, 2009. We did not audit the information and express no opinion on it. Management declined to present Management's Discussion and Analysis for the year ended December 31, 2008.

Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise the Xenia Rural Water District's basic financial statements. Other supplementary information included in Schedule 1, the Schedule of Expenditures of Federal Awards, required by U.S. Office of Management and Budget (OMB) Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations, is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in our audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.



DAVID A. VAUDT, CPA  
Auditor of State



WARREN G. JENKINS, CPA  
Chief Deputy Auditor of State

June 2, 2010

---

## **MANAGEMENT'S DISCUSSION AND ANALYSIS**

---

As financial management of the District, we offer readers of this financial statement an overview and analysis of the financial activities of the District. This narrative is designed to assist readers in focusing on significant financial issues, identifying changes in the District's financial position and identifying individual issues or concerns.

Management's Discussion and Analysis (MD&A) is designed to focus on the current year's activities, resulting changes and currently known facts. It should be read in conjunction with the financial statements which begin on page 14. Due to the way the District previously recognized grant revenue, legal defeasance of refunded capital loan notes and errors in depreciating purchased capacity, the net assets for December 31, 2008 and 2007 were restated. Therefore, comparative information is not available for 2007 financial statements and, accordingly, MD&A for the year ended December 31, 2008 has not been presented.

### **FINANCIAL HIGHLIGHTS**

- ◆ The District's net assets decreased 34.2%, or \$4,371,576, in 2009 and 2.9%, or \$403,473, in 2008 as a result of operations in the respective years.
- ◆ Operating revenue increased 20.9%, or \$1,581,326, in 2009. The increase in operating revenues resulted from a rate increase and usage increases in 2009.
- ◆ Operating expenses increased 36.2%, or \$1,982,288, in 2009 because of factors such as additional depreciation expense on water lines and improvements and the higher cost and quantity of purchased water. The completion of capital improvement projects resulted in an increase in operational labor.

### **USING THIS ANNUAL REPORT**

The financial statements included in this financial report provide information about the activities and performance of the District using accounting methods similar to those used by private sector businesses. These statements combine the District's current financial resources with capital assets and long-term obligations.

Management's Discussion and Analysis introduces the basic financial statements and provides an analytical overview of the District's financial activities.

The Statement of Net Assets presents information on the District's assets and liabilities, with the difference between the two reported as net assets. Over time, changes in net assets may serve as a useful indicator of whether the financial position of the District is improving or deteriorating.

The Statement of Revenues, Expenses and Changes in Net Assets presents information showing how the District's net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the changes occurs, regardless of the timing of the related cash flows. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods.

The Statement of Cash Flows provides information about the District's sources and uses of cash receipts and cash payments. The sources and uses of cash are organized by operations, capital and related financing and investing activities.

The notes provide additional information essential to a full understanding of the data provided in the District's financial statements. The Notes to Financial Statements are a required part of the basic financial statements.

## FINANCIAL ANALYSIS

### *Statement of Net Assets*

As noted earlier, net assets may serve over time as a useful indicator of the District's financial position. The District's net assets at the end of fiscal year 2009 totaled \$8,413,891. This compares to \$12,785,467 at the end of calendar year 2008. A summary of the District's net assets is presented below.

	Net Assets	
	December 31,	
	2009	2008 (as restated)
Current assets	\$ 3,899,594	1,977,970
Noncurrent assets	3,799,592	12,528,258
Capital assets (net of accumulated depreciation)	140,498,914	140,984,587
Total assets	<u>148,198,100</u>	<u>155,490,815</u>
Current liabilities	13,252,299	4,526,565
Noncurrent liabilities	126,531,910	138,178,783
Total liabilities	<u>139,784,209</u>	<u>142,705,348</u>
Net assets:		
Invested in capital assets, net of related debt	2,552,945	-
Restricted	-	5,061,924
Unrestricted	5,860,946	7,723,543
Total net assets	<u>\$ 8,413,891</u>	<u>12,785,467</u>

Assets of the District exceeded liabilities for the year ended December 31, 2009 by \$8,413,891 (net assets). Net assets decreased \$4,371,576 and \$403,473 for the years ended December 31, 2009 and 2008, respectively.

Total liabilities of the District were \$139,784,209 and \$142,705,348 at December 31, 2009 and 2008. Noncurrent liabilities included in total liabilities were \$126,531,910 and \$138,178,783 at December 31, 2009 and 2008, respectively. Total liabilities and noncurrent liabilities decreased \$2,921,139 and \$11,646,873.

A significant portion of the District's assets, 95% and 91%, were invested in capital assets at December 31, 2009 and 2008, respectively.

### *Statement of Revenues, Expenses and Changes in Net Assets*

The following Condensed Statement of Revenues, Expenses and Changes in Net Assets summarize the District's operating results for the years ended December 31, 2009 and 2008.

Changes in Net Assets		
	Year Ended December 31,	
	2009	2008 (as restated)
Operating revenues	\$ 9,141,624	7,560,298
Operating expenses	(7,459,986)	(5,477,698)
Operating income	1,681,638	2,082,600
Nonoperating revenue	1,313,651	2,364,301
Nonoperating expenses	(5,363,541)	(4,850,374)
Extraordinary loss	(2,003,324)	-
Decrease in net assets	<u>\$ (4,371,576)</u>	<u>(403,473)</u>

The Statement of Revenues, Expenses and Changes in Net Assets reflects a decrease in the net assets at the end of the years ended December 31, 2009 and 2008.

The change in net assets in 2009 was a result of the following: 1) Total operating revenue increased 21% over the prior year because of additional usage by industrial customers and water rate increases. The District's water revenue of \$8,426,455 increased 19% over 2008. 13% of the water revenue increase was a result of increased sales to an industrial user for an ethanol production plant which began production during 2008 and volumetric rate increases to users in the industrial user class. On March 1, 2009, a water rate increase of 6% went into effect for residential and commercial users. Standard connection fees increased 87% over the prior year because of an increase in the fee charged to connect new water users to the system. 2) Operating expenses increased 36% from 2008. 38% of the \$1,982,288 increase in operating expenses was from additional depreciation expense on the water lines and improvements placed in service during 2009. Other increases in operating expenses were from additional costs for professional fees to address the District's insolvency, payroll overhead no longer capitalized to capital assets and increased quantities of purchased water at a higher cost. 3) Non-operating revenues decreased 44% from 2008. The decrease was a result of no new large connection fees compared to the 2008 fees from an ethanol production plant, a farm expo event and an urban renewal area. Additional connection fee revenue was earned in 2009 from the urban renewal area. FEMA public assistance revenue of \$563,123 was earned for repairs and improvements of flood damage. Gain on forgiveness of debt of \$295,152 was recognized when an agreement on an outstanding engineering account balance was settled. The District recognized operating grant revenues of \$41,240 for utility management organization services and the Rural Community Development Initiative. Interest income decreased 99% as the District's water reserve accounts decreased and a lower rate of return was earned on investments. 4) Non-operating expenses increased 11% from 2008. Interest expense increased 20% to \$5,172,851, net of interest capitalized on capital assets of \$899,607. 5) An extraordinary loss on abandoned projects of \$2,003,324 occurred when capital asset projects in progress were determined to be nonviable. Abandoned projects included costs from planning, design and initial development of water treatment facilities, expansion of water lines and wastewater systems.

The 2008 financial statements were restated to correct errors in reporting capital grant revenue, depreciation expense of purchased capacity in water treatment facilities of others and legal defeasance of refunded capital loan notes. The restatements decreased the beginning net assets in 2009 and 2008 \$1,696,446 and \$812,594, respectively. Further detail on Restatements is presented in Note 14 of Notes to Financial Statements.

#### *Statement of Cash Flows*

The Statement of Cash Flows presents information related to cash inflows and outflows, summarized by operating, capital and related financing and investing activities. Cash provided by operating activities includes cash received from customers for water sales and sewer use reduced by payments to employees and to suppliers. Cash used from capital and related financing

activities includes principal and interest paid on bonds and notes and the purchase of capital assets. Cash provided by investing activities includes sales of money market securities and interest income.

The following summarize the cash flows:

	Year ended December 31,	
	2009	2008 (as restated)
Cash flows provided (used) by:		
Operating activities	\$ 4,750,778	4,042,890
Capital and related financing activities	(10,465,407)	(22,440,822)
Investing activities	7,898,943	17,598,063
Net increase (decrease) in cash	2,184,314	(799,869)
Cash beginning of year	112,980	912,849
Cash end of year	\$ 2,297,294	112,980

## CAPITAL ASSETS

The following summarizes capital assets at December 31, 2009 and 2008:

	Capital Assets	
	December 31,	
	2009	2008 (as restated)
Nondepreciable assets	\$ 5,456,325	23,475,193
Depreciable assets	157,492,495	139,158,214
Accumulated depreciation	(22,449,906)	(21,648,820)
Total capital assets, net of depreciation	\$ 140,498,914	140,984,587

Capital assets net of accumulated depreciation (including water lines, equipment and buildings) of the District were \$140,498,914 and \$140,984,587 at December 31, 2009 and 2008, respectively. This is a net decrease of \$485,673 during the year ended December 31, 2009. Total capital assets decreased because the disposal of excess water line construction equipment and depreciation exceeded the addition of capitalized costs of improvements and extensions to the rural water system.

During the year ended December 31, 2009, the I-80 transmission and Dallas County transmission water line projects were completed and the District further wound down its in-house construction division. Construction in progress included in nondepreciable capital assets was \$1,795,167 and \$19,957,045 at December 31, 2009 and 2008, respectively. Planning, design and infrastructure improvements in Worth County and the site testing and development of a future water treatment plant site in Dallas County comprise the capital assets remaining in construction in progress at December 31, 2009. Further details on capital assets is presented in Note 4 of the Notes to Financial Statements.

## LONG TERM DEBT

The following summarizes outstanding debt at December 31:

	Outstanding Debt	
	December 31,	
	2009	2008 (as restated)
Revenue notes payable	\$ 45,377,746	41,769,492
Revenue bonds payable	82,608,760	82,912,412
Project anticipation notes payable	9,289,817	15,641,626
Asset purchase agreement payable	77,579	84,074
Rural community 2000 loan	20,000	20,000
Total noncurrent liabilities	<u>\$ 137,373,902</u>	<u>140,427,604</u>

During the year, the District borrowed and repaid \$500,000 on a line of credit. USDA Rural Development loaned the District \$4,000,000 to take out an anticipation note for miscellaneous capital in 2006 and \$260,000 to take out an anticipation note for the construction of a wastewater system for Bouton, Iowa. The District abandoned the North Service Area 4 Phase 1 water distribution project and returned \$2,438,351 of a \$5,000,000 anticipation note to Bank of America. The District borrowed \$86,542 from the Iowa Finance Authority to pay for planning and design costs of a water treatment plant. The District repaid \$391,746 of principal on previously issued USDA Rural Development long-term water revenue bonds and \$325,000 of principal on Water Revenue Bonds Series 2006. For further detail on long-term debt, see Note 6 of the Notes to Financial Statements.

Debt service coverage has been calculated based on the definitions of gross revenues, operating expenses and special charges as defined in the resolution of Water Revenue Bonds Series 2006. Debt service coverage of the District was 61% at December 31, 2009 and 62% at December 31, 2008, as restated. Covenants of the Series 2006 bonds state net revenues during each fiscal year will be sufficient to pay debt service and deposits into the required funds, but not less than 100% of the debt service payments on the bonds and parity obligations.

The District used funds from the restricted cash, Series 2006 reserve to make debt service payments in 2009, 2008 and 2007. The balance requirement for the restricted reserve is \$5,225,300. At December 31, 2009 and 2008, the balance of restricted cash, Series 2006 reserve was \$579,197 and \$4,636,870, respectively. The District repaid \$314,400 plus earned interest of \$100,289 to the restricted reserve during 2008 before drawing on the reserve fund again.

The USDA Rural Development bond resolutions require amounts to be deposited monthly into a reserve account until a balance of one-tenth of one full year's principal and interest payment is on reserve. The District did not meet the monthly reserve deposit requirements. Further detail on Reserves and Debt Service is presented in Note 6 of the Notes to Financial Statements.

On August 20, 2009, Standard & Poor's Corporation downgraded the rating and underlying rating assigned the Series 2006 bonds to 'BB' from 'BBB'. The rationale for the downgrade was the District's deteriorating financial position and use of debt service reserves to cover water debt payments. The rating outlook is developing, which means the rating may be raised or lowered in the intermediate term.

## **ECONOMIC OUTLOOK**

The District has indicators there may be substantial doubt about its ability to continue as going concern. Debt service coverage indicates the District is not producing sufficient cash to cover its debt payments. The District did not achieve sufficient revenues from the water system to meet sinking fund requirements. Debt service reserve funds were used to meet principal and interest payments on bonds. Continued decreases in net assets indicates deteriorating financial position. Further detail on Going Concern is presented in Note 12 of Notes to Financial Statements.

Subsequent to the date of these financial statements, the District implemented water rate increases to residential, commercial and industrial water users. The water rate increases will not provide sufficient revenue to meet the District's debt service requirements. The rate increases for the residential and commercial water users were part of a proposal made by the Board of Director's to sell the District's assets to a new entity managed by the Des Moines Water Works. An agent for the bond insurer of the Water Revenue Bonds, Series 2006 acknowledged the rate increase was lower than the increase recommended by a consultant retained by the agent's counsel.

The June 1, 2010 interest payment on the Water Revenue Bonds, Series 2006 was paid from the remaining funds in restricted cash, Series 2006 reserve and certain other cash and cash equivalents. The amount transferred was \$69,250 less than the debt payment due. The paying agent for the Series 2006 bonds has submitted a claim to the bond insurer for the shortfall.

At June 1, 2010, the District is in default on the payment of a Bank of America note.

## **OTHER INFORMATION**

In addition to the basic financial statements and accompanying Notes to Financial Statements, this report presents other information, including the Schedule of Expenditures of Federal Awards and the Schedule of Findings and Questioned Costs. This information can be found on pages 36 to 51.

## **CONTACTING THE DISTRICT'S FINANCIAL MANAGEMENT**

This report is designed to present our customers and creditors with a general overview of the District's finances and operating activities. If you have any questions or require additional information, please contact the Comptroller of the Xenia Rural Water District at (515) 676-2117 or 23998 141<sup>st</sup> Street, Bouton, Iowa 50039.

## **Basic Financial Statements**

**Exhibit A**

Xenia Rural Water District  
Statement of Net Assets  
December 31, 2009 and 2008

	December 31,	
	2009	2008 (as restated)
<b>Assets</b>		
Current assets:		
Cash and cash equivalents	\$ 2,297,294	112,980
Cash restricted for construction	-	177,725
Grants receivable	2,435	20,390
Accounts receivable:		
Trade	1,138,799	1,026,107
Other	413,303	543,494
Accrued interest receivable	18	20,295
Prepaid expenses	47,745	76,979
Total current assets	<u>3,899,594</u>	<u>1,977,970</u>
Noncurrent assets:		
Inventory	2,450,385	3,509,442
Capital assets (net of accumulated depreciation)	140,498,914	140,984,587
Unamortized bond issuance costs	642,802	662,945
Restricted cash:		
Capital projects	-	2,520,622
USDA Rural Development reserve	61,373	1,127,501
Series 2006 reserve	579,197	4,636,870
Organizational costs (net of amortization)	65,835	70,878
Total noncurrent assets	<u>144,298,506</u>	<u>153,512,845</u>
<b>Total Assets</b>	<u>\$ 148,198,100</u>	<u>155,490,815</u>

Xenia Rural Water District  
Statement of Net Assets  
December 31, 2009 and 2008

	December 31,	
	2009	2008 (as restated)
<b>Liabilities</b>		
Current liabilities:		
Accounts payable:		
Trade	\$ 325,192	129,615
Construction	572,067	1,000,812
Accrued payroll taxes, IPERS contribution and sales tax	65,463	75,581
Accrued payroll	28,631	160,515
Accrued compensated absences	69,789	148,974
Customer deposits	72,606	35,616
Sewer payables	20,481	17,297
Accrued interest payable:		
USDA Rural Development	823,235	193,010
Series 2006 bonds	313,049	314,822
Other bonds and notes	119,794	201,502
Current portion of long-term debt	10,841,992	2,248,821
Total current liabilities	13,252,299	4,526,565
Noncurrent liabilities:		
Revenue notes payable	44,822,244	41,253,396
Revenue bonds payable	81,378,760	82,587,412
Project anticipation notes payable	260,000	14,260,000
Asset purchase agreement payable	70,906	77,975
Total noncurrent liabilities	126,531,910	138,178,783
<b>Total liabilities</b>	<b>139,784,209</b>	<b>142,705,348</b>
<b>Net assets</b>		
Invested in capital assets, net of related debt	2,552,945	-
Restricted for debt service	-	5,061,924
Unrestricted	5,860,946	7,723,543
Total net assets	8,413,891	12,785,467
<b>Total liabilities and net assets</b>	<b>\$ 148,198,100</b>	<b>155,490,815</b>

See notes to financial statements.

**Exhibit B**

## Xenia Rural Water District

Statement of Revenues, Expenses and  
Changes in Net Assets

Years ended December 31, 2009 and 2008

	December 31,	
	2009	2008 (as restated)
Operating revenues:		
Water sales:		
Residential	\$ 5,786,257	5,385,718
Commercial	361,500	316,532
Industrial	2,107,796	1,191,341
Wholesale	170,902	164,269
Service charges:		
Water	217,732	216,449
Wastewater	108	470
Connection fees:		
Water	194,011	115,080
Wastewater	30,086	5,000
Wastewater revenue	224,096	64,124
Trash and recycle revenue	2,138	2,106
Lab fees	2,179	14,412
Miscellaneous	44,819	84,797
Total operating revenue	<u>9,141,624</u>	<u>7,560,298</u>
Operating expenses:		
Depreciation:		
Wastewater systems	126,708	27,147
Other	2,795,199	2,145,929
Salaries and wages	1,324,296	974,542
Purchased water	1,014,852	783,925
Professional fees	398,043	45,846
Utilities	295,966	219,698
Chemicals	274,638	222,121
Repairs	181,955	161,406
Payroll taxes and IPERS	176,728	128,359
Employee benefits	162,501	151,370
Wastewater operations	113,486	18,455
General insurance	112,745	59,158
Maintenance	88,613	96,431
Fuel	87,200	105,969
Office expense	61,729	54,398
Postage and freight	56,324	63,547
Amortization	25,187	25,960
Testing and lab expense	33,688	28,231
Telephone	28,690	18,337
Bank fees and service charges	23,181	14,088
Licenses, dues and subscriptions	22,346	35,779

Xenia Rural Water District  
Statement of Revenues, Expenses and  
Changes in Net Assets  
Years ended December 31, 2009 and 2008

	December 31,	
	2009	2008 (as restated)
Operating expenses (continued):		
Vehicle repair and maintenance	9,460	15,125
Continuing education	7,748	6,972
Directors' per diem	6,138	21,677
Meals and lodging	2,170	4,917
Advertising and promotion	2,023	22,442
Mileage	1,583	1,302
Miscellaneous	26,789	24,567
Total operating expenses	7,459,986	5,477,698
Operating income	1,681,638	2,082,600
Non-operating revenues (expenses):		
Grant revenue	41,240	348,533
FEMA public assistance grant	563,123	-
Custom connection fees:		
Water	148,026	1,669,878
Wastewater	206,020	153,023
Interest income	1,782	141,745
Interest expense	(5,172,851)	(4,311,827)
Rental income	47,250	28,900
Holding loss on inventory	(190,690)	(538,547)
Gain on disposal of equipment	11,058	22,222
Gain on forgiveness of debt	295,152	-
Net non-operating revenues (expenses)	(4,049,890)	(2,486,073)
Extraordinary item:		
Loss on abandoned projects	(2,003,324)	-
Change in net assets	(4,371,576)	(403,473)
Net assets beginning of year, as restated	12,785,467	13,188,940
Net assets end of year	\$ 8,413,891	12,785,467

See notes to financial statements.

Xenia Rural Water District

Statement of Cash Flows

Years ended December 31, 2009 and 2008

	December 31,	
	2009	2008 (as restated)
Cash flows from operating activities:		
Cash received from customers	\$ 8,958,188	7,359,072
Cash payments to employees for services	(1,928,165)	(1,230,807)
Cash payments to suppliers for goods and services	<u>(2,279,245)</u>	<u>(2,085,375)</u>
Net cash provided by operating activities	<u>4,750,778</u>	<u>4,042,890</u>
Cash flows from capital and related financing activities:		
Grants received	59,195	43,188
Capital grants received	-	396,000
FEMA public assistance grant	504,017	-
Cash received from custom connection fees	647,453	1,461,110
Proceeds from bonds and notes	4,586,543	10,417,589
Proceeds from sale of assets	1,884,805	226,106
Acquisition and construction of capital assets	(5,881,068)	(29,392,517)
Principal paid on bonds and notes	(7,640,246)	(751,261)
Interest paid on bonds and notes	<u>(4,626,106)</u>	<u>(4,841,037)</u>
Net cash used by capital and related financing activities	<u>(10,465,407)</u>	<u>(22,440,822)</u>
Cash flows from investing activities:		
Proceeds from sales of investments	8,166,270	23,393,413
Purchases of investments	(344,120)	(6,345,208)
Investment income	<u>76,793</u>	<u>549,858</u>
Net cash provided by investing activities	<u>7,898,943</u>	<u>17,598,063</u>
Net increase (decrease) in cash and cash equivalents	2,184,314	(799,869)
Cash and cash equivalents beginning of year	<u>112,980</u>	<u>912,849</u>
Cash and cash equivalents end of year	<u>\$ 2,297,294</u>	<u>112,980</u>

Xenia Rural Water District

Statement of Cash Flows

Years ended December 31, 2009 and 2008

	December 31,	
	2009	2008 (as restated)
<b>Reconciliation of operating income to net cash provided by operating activities:</b>		
Operating income	\$ 1,681,638	2,082,600
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation - wastewater systems	126,708	27,147
Depreciation - other	2,795,199	2,145,929
Amortization	25,187	25,960
Gain on forgiveness of debt	295,152	-
Changes in assets and liabilities:		
Accounts receivable	(216,902)	(203,663)
Prepaid expenses	29,234	(16,195)
Accounts payable	196,942	(52,867)
Accrued salaries and wages	(211,069)	20,567
Accrued payroll taxes, IPERS and sales tax	(10,118)	12,922
Employee fund	(1,367)	(200)
Customer deposits	5,790	366
Sewer payable	3,184	324
Membership refund liability	31,200	-
Total adjustments	<u>3,069,140</u>	<u>1,960,290</u>
Net cash provided by operating activities	<u>\$ 4,750,778</u>	<u>4,042,890</u>
Non-cash capital activities:		
Holding loss on construction material inventory	<u>\$ 190,690</u>	<u>538,547</u>

See notes to financial statements.

Xenia Rural Water District  
Notes to Financial Statements  
December 31, 2009 and 2008

**(1) Summary of Significant Accounting Policies**

The Xenia Rural Water District was formed in 1992 pursuant to the provisions of Chapter 357A.2 of the Code of Iowa. The purpose of the District is to establish, develop, construct, operate and maintain water distribution and wastewater treatment systems for resident members throughout its territory in rural central and north-central Iowa. The district extends credit to customers served, all of whom are located in the State of Iowa.

The governing body of the District is composed of up to nine members, all of whom shall be participating members of the District. The directors are elected by the participating members who each has one vote at the annual meeting. The directors are elected to staggering terms so no more than three directors are elected in any year. Directors hold office for a term of three years and until a successor is elected and has qualified.

The District's financial statements are prepared in conformity with U.S. generally accepted accounting principles as prescribed by the Governmental Accounting Standards Board.

A. Reporting Entity

For financial reporting purposes, the Xenia Rural Water District has included all funds, organizations, agencies, boards, districts and authorities. The District has also considered all potential component units for which it is financially accountable and other organizations for which the nature and significance of their relationship with the District are such that exclusion would cause the District's financial statements to be misleading or incomplete. The Governmental Accounting Standards Board has set forth criteria to be considered in determining financial accountability. These criteria include appointing a voting majority of an organization's governing body and (1) the ability of the District to impose its will on that organization or (2) the potential for the organization to provide specific benefits to or impose specific financial burdens on the District.

These financial statements present the Xenia Rural Water District (the primary government) and its component unit. The component unit discussed below is included in the District's reporting entity because of the significance of its operations or financial relationship with the District.

Blended Component Unit

The Xenia Economic Development Corporation is legally separate from the District but is so intertwined with the District it is, in substance, part of the District. The Xenia Economic Development Corporation was organized under Chapter 504A of the Code of Iowa as a non-profit corporation. The boards for the District and the Corporation are the same. The Corporation receives grants to promote and develop projects for the District. The financial transactions have been discretely presented in Note 9 of the Notes to Financial Statements.

B. Basis of Presentation

The accounts of the District are organized as an Enterprise Fund. Enterprise Funds are used to account for operations (a) financed and operated in a manner similar to private business enterprises, where the intent of the governing body is the costs (expenses, including depreciation) of providing goods or 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 periodic determination of revenues earned, expenses incurred, and/or net income is appropriate for capital maintenance, public policy, management control, accountability or other purposes.

C. Measurement Focus and Basis of Accounting

The financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

The District applies all applicable GASB pronouncements, as well as the following pronouncements issued on or before November 30, 1989, unless these pronouncements conflict with or contradict GASB pronouncements: Financial Accounting Standards Board Statements and Interpretations, Accounting Principles Board Opinions and Accounting Research Bulletins of the Committee on Accounting Procedure.

The District distinguishes operating revenues from non-operating revenues. Operating revenues generally result from providing services and producing and delivering goods in connection with the District's principal ongoing operations. All revenues not meeting this definition are reported as non-operating revenues.

D. Assets, Liabilities and Net Investments

The following accounting policies are followed in preparing the Statement of Net Assets:

Cash and Cash Equivalents – The District considers all short-term investments that are highly liquid to be cash equivalents. Cash equivalents are readily convertible to known amounts of cash and, at the day of purchase, have a maturity date no longer than three months.

Restricted Cash – Funds set aside for payment of debt issuances are classified as restricted.

Capital Assets – Capital assets are accounted for at historical cost. The cost of repair and maintenance is charged to expense while the cost of renewals or substantial betterments is capitalized. The cost and accumulated depreciation of assets disposed of are deleted, with any gain or loss recorded in current operations.

Reportable capital assets are defined by the District as assets with initial, individual costs in excess of \$1,000 and estimated useful lives in excess of two years.

Capital assets of the District are depreciated using either the straight line or the units of production method, depending on classification. Construction equipment purchased after December 31, 2006 is depreciated using current year units of production over the estimated total units of production. With the exception of construction equipment purchased after December 31, 2006 capital assets are depreciated using the straight line method over the following estimated useful lives:

Asset Class	Estimated Useful lives (In Years)
Water system and wells	60
Wastewater systems	15-60
Purchased capacity	40
Plant building	40
Office building and improvements	7-39
Equipment and tools	3-12
Transportation equipment	5
Office furniture and equipment	3-7

Interest is capitalized on qualified assets. The amount of interest capitalized is calculated using the weighted average cost of interest on outstanding debt multiplied by the construction expenditures for the project until completion of the project. During the years ended December 31, 2009 and 2008, interest costs of \$899,607 and \$1,571,589, respectively, were capitalized.

Compensated Absences – District employees accumulate a limited amount of earned but unused vacation hours for subsequent use or for payment upon termination, death or retirement. The District’s liability for accumulated vacation has been computed based on rates of pay in effect at December 31, 2009 and 2008.

Inventory – Inventories are valued at the lower of cost (first-in, first-out) method or market. Inventories consist of parts for the assembly and repair of new and existing water systems. When inventory is used for capital projects, it is included as a cost of the related project.

Accounts Receivable – The District recognizes bad debt expense on the direct write-off method.

E. Organizational Costs and Bond Issuance Costs

Organizational expenses of the District are amortized on the straight-line method over forty years.

Underwriter’s costs incurred on Water Revenue Bonds, Series 2006 for the purpose of refunding currently outstanding obligations are amortized on the straight-line method over the life of the bonds. Underwriter’s costs incurred for the purpose of funding capital projects are treated as a cost of the project, and capitalized as a capital asset when the project was started, based on the project budget.

Bond discounts incurred on Water Revenue Bonds, Series 2006 for the purpose of refunding currently outstanding obligations are amortized on the straight-line method over the life of the bonds. Bond discounts incurred for the purpose of funding capital projects are treated as a cost of the project and capitalized as a capital asset when the project was started, based on the project budget.

Amortization charged to operations and interest expense for 2009 and 2008 was \$46,635 and \$79,118, respectively. Estimated amortization expense for each of the ensuing years through December 31, 2014 is \$46,636.

Amortization capitalized as capital assets for 2009 and 2008 was \$0 and \$402,521, respectively.

#### F. Use of Estimates

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

#### G. Reclassifications

Certain prior year amounts for the year ended December 31, 2008 were reclassified to conform to current year reporting requirements.

### **(2) Cash and Investments**

The District's deposits in banks at December 31, 2009 and 2008 were entirely covered by federal depository insurance or by the State Sinking Fund in accordance with Chapter 12C of the Code of Iowa. This chapter provides for additional assessments against depositories to insure there will be no loss of public funds.

The District is authorized by statute to invest public funds in obligations of the United States government, its agencies and instrumentalities; certificates of deposit or other evidences of deposit at federally insured depository institutions approved by the District; prime eligible bankers acceptances; certain high rated commercial paper; perfected repurchase agreements; certain registered open-end management investment companies; certain joint investment trusts; and warrants or improvement certificates of a drainage district.

The District had no investments meeting the disclosure requirements of Governmental Accounting Standards Board Statement No. 3, as amended by Statement No. 40.

### **(3) Pension and Retirement Benefits**

The District contributes to the Iowa Public Employees Retirement System (IPERS), which is a cost-sharing multiple-employer defined benefit pension plan administered by the State of Iowa. IPERS provides retirement and death benefits established by state statute to plan members and beneficiaries. IPERS issues a publicly available financial report that includes financial statements and required supplementary information. The report may be obtained by writing to IPERS, P.O. Box 9117, Des Moines, Iowa, 50306-9117.

Plan members were required to contribute 3.90% of their annual covered salary until July 1, 2008 and 4.10% of their annual covered salary until July 1, 2009, at which time, the contribution rate changed to 4.30% of their annual covered salary. The District was required to contribute 6.05% of annual covered payroll until July 1, 2008 and 6.35% of annual covered payroll until July 1, 2009, at which time the contribution rate changed to 6.65% of annual covered payroll. Contribution requirements are established by state statute. The District's contributions to IPERS for the years ended December 31, 2009, 2008 and 2007 were \$181,859, \$304,738 and \$240,609, respectively, equal to the required contributions for each year.

#### (4) Capital Assets

Capital assets activity for the years ended December 31, 2009 and 2008 was as follows:

	Year ended December 31, 2009			Balance End of Year
	Balance Beginning of Year (as restated)	Increases	Decreases	
Capital assets not being depreciated:				
Land	\$ 3,518,148	143,010	-	3,661,158
Construction in progress	19,957,045	3,812,210	(21,974,088)	1,795,167
Total capital assets not being depreciated	23,475,193	3,955,220	(21,974,088)	5,456,325
Capital assets being depreciated:				
Office building and improvements	2,140,319	1,140,173	(5,303)	3,275,189
Office furniture and equipment	701,960	96,097	-	798,057
Plant building	616,436	1,903	-	618,339
Wells	62,982	-	-	62,982
Wastewater systems	2,922,360	57,668	-	2,980,028
Water lines	116,055,817	21,427,533	(43,099)	137,440,251
Purchased capacity	4,728,209	-	-	4,728,209
Telemetry system	484,757	116,701	-	601,458
Equipment and tools	10,988,827	3,957	(4,357,800)	6,634,984
Transportation equipment	456,547	27,611	(131,160)	352,998
Total capital assets being depreciated	139,158,214	22,871,643	(4,537,362)	157,492,495
Less accumulated depreciation for:				
Office building and improvements	464,416	86,186	(15)	550,587
Office furniture and equipment	517,664	71,058	-	588,722
Plant building	397,071	16,670	-	413,741
Wells	40,945	1,574	-	42,519
Wastewater systems	27,259	126,854	-	154,113
Water lines	12,630,990	2,180,609	(3,031)	14,808,568
Purchased capacity	1,308,144	121,059	-	1,429,203
Telemetry system	119,156	24,078	-	143,234
Equipment and tools	5,841,484	741,502	(2,493,674)	4,089,312
Transportation equipment	301,691	59,376	(131,160)	229,907
Total accumulated depreciation	21,648,820	3,428,966	(2,627,880)	22,449,906
Total capital assets being depreciated, net	117,509,394	19,442,677	(1,909,482)	135,042,589
Capital assets, net	\$ 140,984,587	23,397,897	(23,883,570)	140,498,914

	Year ended December 31, 2008			Balance Beginning of Year (as restated)
	Balance Beginning of Year (as restated)	Increases	Decreases	
Capital assets not being depreciated:				
Land	\$ 1,669,604	1,848,544	-	3,518,148
Construction in progress	9,566,857	34,605,589	(24,215,401)	19,957,045
Total capital assets not being depreciated	11,236,461	36,454,133	(24,215,401)	23,475,193
Capital assets being depreciated:				
Office building and improvements	2,135,016	21,696	(16,393)	2,140,319
Office furniture and equipment	633,706	68,254	-	701,960
Plant building	616,436	-	-	616,436
Wells	62,982	-	-	62,982
Wastewater systems	20,000	2,902,360	-	2,922,360
Water lines	101,230,626	14,825,191	-	116,055,817
Purchased capacity	4,728,209	-	-	4,728,209
Telemetry system	316,501	168,256	-	484,757
Equipment and tools	9,327,808	1,913,454	(252,435)	10,988,827
Transportation equipment	380,116	76,431	-	456,547
Total capital assets being depreciated	119,451,400	19,975,642	(268,828)	139,158,214
Less accumulated depreciation for:				
Office building and improvements	392,204	72,713	(501)	464,416
Office furniture and equipment	434,028	83,636	-	517,664
Plant building	379,964	17,107	-	397,071
Wells	39,370	1,575	-	40,945
Wastewater systems	111	27,148	-	27,259
Water lines	10,841,535	1,789,455	-	12,630,990
Purchased capacity	1,187,085	121,059	-	1,308,144
Telemetry system	103,148	16,008	-	119,156
Equipment and tools	4,904,004	1,182,141	(244,661)	5,841,484
Transportation equipment	245,804	55,887	-	301,691
Total accumulated depreciation	18,527,253	3,366,729	(245,162)	21,648,820
Total capital assets being depreciated, net	100,924,147	16,608,913	(23,666)	117,509,394
Capital assets, net	\$ 112,160,608	53,063,046	(24,239,067)	140,984,587

Depreciation charged to wastewater systems for 2009 and 2008 was \$126,708 and \$27,147, respectively. Depreciation charged to other operations for 2009 and 2008 was \$2,795,199 and \$2,145,929, respectively.

Depreciation capitalized as capital assets for 2009 and 2008 was \$507,059 and \$1,193,653, respectively.

## (5) Risk Management

The District is exposed to various risks of loss related to torts; theft, damage to and destruction of assets; errors and omissions; injuries to employees; and natural disasters. These risks are covered by the purchase of commercial insurance. Settled claims from these risks have not exceeded commercial insurance coverage in any of the past three fiscal years. The District assumes liability for any deductibles and claims in excess of coverage limitations.

**(6) Changes in Long Term Liabilities**

A summary of changes in long-term liabilities for the years ended December 31, 2009 and 2008 is as follows:

	Year ended December 31, 2009				
	Balance Beginning of Year (as restated)	Additions	Deletions	Balance End of Year	Due Within One Year
USDA Rural Development water revenue notes	\$ 41,769,492	4,000,000	(391,746)	45,377,746	555,503
Water revenue bonds, Series 2006	82,912,412	-	(303,652)	82,608,760	1,230,000
Rural Community 2000 loan	20,000	-	-	20,000	20,000
Project anticipation notes	15,641,626	86,542	(6,438,351)	9,289,817	9,029,817
Loan agreement	-	500,000	(500,000)	-	-
Asset purchase agreement	84,074	-	(6,495)	77,579	6,672
<b>Total</b>	<b>\$ 140,427,604</b>	<b>4,586,542</b>	<b>(7,640,244)</b>	<b>137,373,902</b>	<b>10,841,992</b>

  

	Year ended December 31, 2008				
	Balance Beginning of Year (as restated)	Additions	Deletions	Balance End of Year (as restated)	Due Within One Year
USDA Rural Development water revenue notes	\$ 42,245,355	-	(475,863)	41,769,492	516,096
Water revenue bonds, Series 2006	83,141,064	-	(228,652)	82,912,412	325,000
Rural Community 2000 loan	40,000	-	(20,000)	20,000	20,000
Project anticipation notes	5,224,037	10,417,589	-	15,641,626	1,381,626
Asset purchase agreement	89,472	-	(5,398)	84,074	6,099
<b>Total</b>	<b>\$ 130,739,928</b>	<b>10,417,589</b>	<b>(729,913)</b>	<b>140,427,604</b>	<b>2,248,821</b>

USDA Rural Development Water Revenue Notes – The District has issued water revenue notes totaling \$47,281,900 at December 31, 2009. The water revenue notes bear interest at rates ranging from 4.125% to 5.625% per annum. On January 30, 2009, the District issued \$4,000,000 of USDA Rural Development water revenue notes with an interest rate of 4.250% for miscellaneous construction projects.

The District has pledged future water customer receipts, net of specified operating disbursements, to repay the water revenue notes. The notes are payable solely from water customer net receipts and are payable through 2049. At December 31, 2009 and 2008, the debt service coverage ratios of the revenues to debt service were 61% and 62%, respectively.

The resolutions providing for the issuance of the water revenue notes include the following provisions:

- (a) The notes will only be redeemed from the future earnings of the enterprise activity and the note holder holds a lien on the future earnings of the funds.
- (b) Sufficient monthly transfers shall be made to a water revenue note sinking account for the purpose of making the note principal and interest payments when due.
- (c) A water reserve account shall be established. Annually, there shall be deposited in the water reserve account an amount equal to 10 percent of the water reserve account requirement. This account is restricted for the purpose of paying principal and interest when funds in the sinking account are inadequate.
- (d) An improvement account shall be established for the purpose of paying principal and interest when there is insufficient money in the sinking and reserve accounts and extraordinary maintenance and repairs, as needed.

- (e) User rates or charges to consumers shall be sufficient in each year for the payment of the proper and reasonable expenses of operation and maintenance of the system, for the payment of principal and interest on the notes and for the establishment of adequate reserves.
- (f) At all times, persons handling money will be bonded for the faithful performance of their duties. The amount will not be less than the maximum amount of principal and interest coming due in any fiscal year on all obligations of the District.

The District has not maintained the required balance in the water reserve account. In addition, the District has not maintained user rates at a sufficient level for payment of expenses for operation and maintenance of the system and for payment of principal and interest on the notes and has not established sinking or improvement accounts as required. Additionally, the amount of surety bond insurance does not meet the minimum requirements of the note resolution.

Details of the USDA Rural Development water revenue notes at December 31, 2009 and 2008 are as follows:

Loan No.	Issue Date	Interest Rate	Maturity Date	Monthly Payment	Amount Originally Issued	Note Balances	
						2009	2008
91-13	12/29/1993	5.250%	12/29/2033	\$ 1,024	200,000	162,304	165,063
91-14	9/23/1994	5.625	9/23/2034	5,360	1,000,000	813,548	827,118
91-15	9/23/1994	5.375	9/23/2034	3,640	700,000	583,025	592,059
91-27	2/11/1999	4.500	2/1/2039	3,113	672,200	607,189	614,557
91-31	9/27/2001	4.750	9/27/2041	19,846	4,143,100	3,872,775	3,912,514
91-38	9/27/2001	4.750	9/27/2041	3,771	787,100	703,621	712,300
91-46	10/19/2001	4.750	9/27/2041	1,916	400,000	373,826	377,665
91-41	12/21/2001	4.750	9/27/2041	17,325	3,500,000	3,271,641	3,305,217
91-44	6/21/2002	4.750	6/21/2042	11,752	2,453,400	2,324,303	2,346,751
91-66	9/26/2003	4.250	1/1/2043	6,882	1,536,000	1,467,380	1,482,241
91-64	9/26/2003	4.250	1/1/2043	6,630	1,479,900	1,413,817	1,428,129
91-62	9/26/2003	4.250	1/1/2043	9,008	2,010,700	1,920,915	1,940,360
91-52	6/25/2004	4.375	1/1/2044	15,960	3,500,000	3,391,331	3,423,018
91-58	6/25/2004	4.250	1/1/2044	2,565	572,500	554,281	559,589
91-56	6/25/2004	4.375	1/1/2044	2,204	4,845,000	4,694,543	4,738,415
25-61	9/26/2005	4.125	9/26/2044	6,675	1,517,000	1,486,687	1,500,490
25-73	9/26/2005	4.125	9/26/2044	15,278	3,500,000	3,430,072	3,461,914
40-01	9/26/2005	4.125	9/26/2045	7,700	1,750,000	1,710,894	1,726,941
25-70	9/26/2005	4.125	9/26/2045	15,400	3,500,000	3,430,072	3,461,914
25-71	9/26/2005	4.125	9/26/2045	8,800	2,000,000	1,960,041	1,978,237
40-03	2/1/2006	4.125	2/1/2046	5,346	1,215,000	1,205,481	1,215,000
40-05	12/20/2007	4.375	12/20/2047	8,831	2,000,000	2,000,000	2,000,000
40-04	1/30/2009	4.250	1/30/2049	17,920	4,000,000	4,000,000	-
Total				\$ 196,946	47,281,900	45,377,746	41,769,492

Water Revenue Bonds – The District has pledged future water customer receipts, net of specified operating disbursements, to repay \$83,865,000 of water revenue bonds issued in November 2006. Proceeds from the bonds provided financing to refund certain outstanding USDA Rural Development water revenue notes, lease purchase obligation agreements and water revenue capital loan notes and for the costs of improvements and extension to the District’s water system. The bonds are payable solely from water customer net receipts and are payable through 2041. The total principal remaining to be paid on the bonds is \$83,290,000. At December 31, 2009 and 2008, as restated, the debt service coverage ratios of the revenues (excluding connection fees) to debt service were 64% and 62%, respectively.

The resolution providing for the issuance of the water revenue bonds includes the following provisions:

- (a) The bonds will only be redeemed from the future earnings of the enterprise activity and the bond holder holds a lien on the future earnings of the funds.
- (b) Sufficient monthly transfers shall be made to a water revenue bond sinking account for the purpose of making the bond principal and interest payments when due.
- (c) A water reserve account shall be established. This account is restricted for the purpose of paying principal and interest when funds in the sinking account are inadequate.
- (d) An improvement account shall be established for the purpose of paying principal and interest when there is insufficient money in the sinking and reserve accounts and extraordinary maintenance and repairs, as needed.
- (e) User rates or charges to consumers shall be sufficient in each year for the payment of the proper and reasonable expenses of operation and maintenance of the system, for the payment of principal and interest on the bonds and for the establishment of adequate reserves.
- (f) At all times, persons handling money will be bonded for the faithful performance of their duties. The amount will not be less than the maximum amount of principal and interest coming due in any fiscal year on all obligations of the District.

The amount of surety bond insurance does not meet the minimum requirements of the bond resolution and the District has not maintained the required balance in the water reserve account. In addition, the District has not maintained user rates at a sufficient level for payment of expenses for operation and maintenance of the system and for payment of principal and interest on the bonds and has not established sinking or improvement accounts as required.

#### Rural Community 2000 Loan

The District obtained a \$200,000 loan in 1993 from the Iowa Department of Economic Development under the Rural Community 2000 program. The loan is interest free and requires annual principal payments of \$20,000 through the year 2009. The District was in default for non-payment of the outstanding loan balance at December 31, 2009. The outstanding balances at December 31, 2009 and 2008 were \$20,000 and \$20,000, respectively.

#### Project Anticipation Notes

In 2006, the District entered into a State Revolving Fund loan and disbursement agreement with the Iowa Finance Authority, the Iowa Department of Natural Resources and Wells Fargo Bank Iowa, N.A. (Trustee for the issuance of planning and design loans.) The notes were issued pursuant to the provisions of Chapter 384.24A of the Code of Iowa to pay the costs of planning, designing and constructing improvements and extensions to the water system. The funds were drawn by the District from the Trustee upon request to reimburse the District for costs as they were incurred. At December 31, 2009, the District had drawn \$1,468,168. In 2009, the District decided not to move forward with the projects and received approval from the Iowa Finance Authority to extend the maturity date from October 16, 2009 to October 16, 2010. The District made no principal or interest payments during 2009. Iowa Finance Authority project anticipation notes outstanding at December 31, 2009 and 2008 are as follows:

Project	Interest		Limit	Note Balances	
	Rate	Maturity Date		2009	2008
Beaver Creek Treatment Plant	0.00%	10/16/2010	\$ 917,000	917,000	830,459
North Service Area 3 Phase IIB	0.00	10/16/2010	175,000	175,000	175,000
Service Area 3, Phase II	0.00	10/16/2010	250,000	18,168	18,168
Winn/Worth	0.00	10/16/2010	358,000	358,000	357,999
Total			\$ 1,700,000	1,468,168	1,381,626

In 2008 and 2007, the District entered into project anticipation loan notes to finance construction of new projects. As security, the District committed to retire the project anticipation notes through proceeds from the issuance of additional USDA water revenue notes and the remainder of the project anticipation notes will be payable from other unrestricted assets. In 2009, the maturity date of the F & M Bank note was extended from October 1, 2009 to January 1, 2010. During 2008, a Bank of America project anticipation note was amended to extend the term 12 months and lower the interest rate from 4.08% to 3.83% per annum. Payments of \$6,438,351 of principal and \$437,457 of interest were made during the year ended December 31, 2009. Project anticipation notes outstanding for Bank of America and F & M Bank notes at December 31, 2009 and 2008 are as follows:

Lender	Interest		Limit	Note Balances	
	Rate	Maturity Date		2009	2008
F & M Bank	3.90%	1/1/2010	\$ 260,000	260,000	260,000
Bank of America	3.83	2/1/2009	4,000,000	-	4,000,000
Bank of America	3.70	6/1/2010	5,000,000	5,000,000	5,000,000
Bank of America	3.16	11/15/2010	5,000,000	2,561,649	5,000,000
Total				\$ 7,821,649	14,260,000

#### Loan Agreement

The District opened a line of credit with Ames Community Bank on January 26, 2009. The open end credit line expired on December 31, 2009. Under the terms of the loan agreement, the District could borrow up to \$500,000 at a variable interest rate equal to the Wall Street Journal U.S. Prime Rate with a limit of not less than 5.0%. The loan was secured by equipment and tools. Funds from these borrowings could be used for construction projects. During the year ended December 31, 2009, the District borrowed \$500,000. \$500,000 of principal and \$14,072 of interest were paid during the year ended December 31, 2009. The line of credit was completely repaid at December 31, 2009.

#### Asset Purchase Agreement

The District entered into an asset purchase agreement with Coats Utilities Company on November 5, 2007. As part of this agreement, the District assumed Capmark Loans #01-03244-01 and #01-03244-03 from Coats Utilities Company for the assets collateralizing the loans. Capmark Loan #01-03244-01 bears interest at 5.0% per annum and requires monthly principal and interest payments of \$470, with a maturity date of May 6, 2017. Capmark loan #01-03244-03 bears interest at 5.0% per annum and requires monthly principal and interest payments of \$377, with a maturity date of May 11, 2022. \$6,495 of principal and \$4,516 of interest were paid during the year ended December 31, 2009. The balances outstanding at December 31, 2009 and 2008 were \$77,579 and \$84,074, respectively.

#### Debt Defeasance

In a prior year, the District defeased certain capital loan notes by placing the proceeds of new bonds in an irrevocable trust to provide for all future debt service payments on the notes. Accordingly, the trust account assets and the liability for the defeased notes are not included in the District's financial statements. As of December 31, 2009, notes totaling \$2,040,000 were considered defeased.

A summary of the annual principal and interest payments to maturity is as follows:

Year ending December 31,	USDA Rural Development Water Revenue Notes			Water Revenue Bonds, Series 2006		
	Principal	Interest	Total	Principal	Interest	Total
2010	\$ 555,503	1,998,249	2,553,752	1,230,000	3,756,585	4,986,585
2011	580,257	1,973,495	2,553,752	1,285,000	3,711,075	4,996,075
2012	633,240	1,947,632	2,580,872	1,335,000	3,662,888	4,997,888
2013	679,339	1,919,453	2,598,792	1,385,000	3,609,488	4,994,488
2014	709,540	1,889,252	2,598,792	1,440,000	3,554,088	4,994,088
2015-2019	4,050,190	8,943,770	12,993,960	8,155,000	16,820,988	24,975,988
2020-2024	5,035,974	7,957,986	12,993,960	10,130,000	14,848,156	24,978,156
2025-2029	6,263,581	6,730,379	12,993,960	12,575,000	12,398,256	24,973,256
2030-2034	7,579,195	5,206,448	12,785,643	15,715,000	9,293,456	25,008,456
2035-2039	8,906,953	3,429,977	12,336,930	20,345,000	5,239,575	25,584,575
2040-2044	8,418,169	1,407,448	9,825,617	9,695,000	680,450	10,375,450
2045-2049	1,965,805	180,802	2,146,607	-	-	-
Total	\$ 45,377,746	43,584,891	88,962,637 *	83,290,000	77,575,005	160,865,005

Year ending December 31,	Project Anticipation Notes			Rural Communities 2000 Loan		
	Principal	Interest	Total	Principal	Interest	Total
2010	\$ 9,289,817 ^	148,107	9,437,924	20,000	-	20,000
2011	-	-	-	-	-	-
2012	-	-	-	-	-	-
2013	-	-	-	-	-	-
2014	-	-	-	-	-	-
2015-2019	-	-	-	-	-	-
2020-2024	-	-	-	-	-	-
2025-2029	-	-	-	-	-	-
2030-2034	-	-	-	-	-	-
2035-2039	-	-	-	-	-	-
2040-2044	-	-	-	-	-	-
2045-2049	-	-	-	-	-	-
Total	\$ 9,289,817	148,107	9,437,924	20,000	-	20,000

Year ending December 31,	Asset Purchase Agreement			Total		
	Principal	Interest	Total	Principal	Interest	Total
2010	\$ 6,672	3,492	10,164	11,101,992	5,906,433	17,008,425
2011	6,773	3,392	10,164	1,872,030	5,687,962	7,559,991
2012	7,119	3,045	10,164	1,975,359	5,613,565	7,588,924
2013	7,483	2,681	10,164	2,071,822	5,531,622	7,603,444
2014	7,866	2,298	10,164	2,157,406	5,445,637	7,603,044
2015-2019	30,858	5,903	36,761	12,236,048	25,770,661	38,006,709
2020-2024	10,807	723	11,530	15,176,781	22,806,865	37,983,646
2025-2029	-	-	-	18,838,581	19,128,635	37,967,216
2030-2034	-	-	-	23,294,195	14,499,904	37,794,099
2035-2039	-	-	-	29,251,953	8,669,552	37,921,505
2040-2044	-	-	-	18,113,169	2,087,898	20,201,067
2045-2049	-	-	-	1,965,805	180,802	-
Total	\$ 77,579	21,533	99,111	138,055,142	121,329,535	259,384,677

\* - The unamortized discount at December 31, 2009 and 2008 totaled \$681,240 and \$702,588, respectively.

^ - The principal balance includes \$260,000 classified as noncurrent in the Statement of Net Assets, as permitted by U.S. generally accepted accounting principles.

**(7) Leases**

The District leases mailing equipment from Pitney Bowes Global Financial Services. The cost of leases expensed to operations and included in office expense was \$10,250 and \$10,418 for the years ended December 31, 2009 and 2008, respectively.

The following is a schedule by years of future minimum rental payments required under operating leases which have partial or remaining non cancelable lease terms in excess of one year as of December 31, 2009:

Year ending December 31,	Total Minimum Lease Payments
2010	\$ 7,425
2011	6,861
2012	3,440
2013	2,685
Total	<u>\$ 20,411</u>

The District leases land to an employee under an operating lease. The land is enrolled in the United States Department of Agriculture Farm Service Agency Conservation Reserve Program. The future annual lease payments are calculated by multiplying the Conservation Reserve Program annual contract payment by 79.25%. The lease expires in 2017. The District's investment in property subject to the operating lease is \$907,667 at December 31, 2009 and 2008.

The following is a schedule by years of minimum future rentals on non-cancelable operating leases as of December 31, 2009:

Year ending December 31,	Total Estimated Rental Receipts
2010	\$ 15,832
2011	15,832
2012	15,832
2013	15,042
2014	15,042
2015 - 2024	40,635
Total	<u>\$ 118,215</u>

The District has entered into a lease agreement with RTK of Iowa exchanging the use of water towers as base stations for use of the GPS network. The lease expires in 2013 and the tenant has an option to renew the agreement for an additional five year period.

The District leased land to farm tenants during 2009 totaling \$20,900. The lease terms were April 15, 2009 through November 30, 2009, at which time the leases automatically terminated.

**(8) Related Party Transactions**

The former Executive Director is a limited shareholder and was a Board Member with a bank maintaining operating and construction accounts for the District. The former Executive Director terminated employment with the District on June 5, 2009. The balance of cash accounts at the bank was \$2,222,121 and \$230,711 at December 31, 2009 and 2008, respectively.

The former Executive Director was also a Board Member of RTK of Iowa.

The Board President owns a company which provided grass mowing services to a portion of the District's facilities in 2008. Fees for these services totaled \$0 and \$11,328 for 2009 and 2008, respectively. No balance was payable to this company at December 31, 2009 and 2008.

A Board Member owns a rental house used by the District to house construction workers. Rental payments for this house totaled \$0 and \$1,600 for 2009 and 2008, respectively. No balance was payable for rental fees at December 31, 2009 and 2008.

An employee of the District pays rent for land and the periodic use of equipment used to maintain the land to the standards of the USDA Farm Service Agency Conservation Reserve Program. Rent payments received by the District for land and equipment totaled \$26,350 and \$28,900 for 2009 and 2008, respectively. There was no receivable for rent at December 31, 2009 and 2008.

**(9) Discrete Component Unit**

During 2003, the Xenia Economic Development Corporation was formed as a component unit of the District. The Xenia Economic Development Corporation was organized as a not-for-profit corporation for the purpose of obtaining grant funding.

The Xenia Economic Development Corporation was named as a sub-recipient of a Rural Community Development Initiative grant in 2006. The \$63,000 grant from Iowa Rural Water Association was awarded to train local officials and to provide assistance in the development of housing and business in rural communities. The Rural Community Development Initiative grant is a service type grant, and revenues from this grant are realized as services are performed. The District is compensated by the Xenia Economic Development Corporation for the services performed for this grant.

Condensed statements of net assets:

	2009	2008
Assets:		
Cash	\$ 2,517	2,545
Grant receivable	-	26,022
Organizational fees	500	500
Total	<u>\$ 3,017</u>	<u>29,067</u>
Liabilities and Net Assets:		
Accounts payable	\$ 2,434	19,497
Deferred grant revenue	-	9,004
Unrestricted net assets	583	566
Total	<u>\$ 3,017</u>	<u>29,067</u>

Condensed statement of revenues, expenses and changes in net assets:

	2009	2008
Operating revenues (expenses):		
Service grant revenue	\$ 7,888	33,673
Contract labor	(7,888)	(33,673)
Operating income	-	-
Other revenues	17	65
Change in net assets	17	65
Net assets beginning of year	566	501
Net assets end of year	<u>\$ 583</u>	<u>566</u>

**(10) Compensated Absences**

District employees accumulate a limited amount of earned but unused vacation leave hours for subsequent use or for payment upon termination, retirement or death. These accumulations are not recognized as expenses by the District until used or paid. The District's liability for earned vacation payable to employees at December 30, 2009 and 2008 was \$69,789 and \$148,974, respectively. This liability has been computed based on rates in effect at December 31, 2009 and December 31, 2008, respectively.

**(11) Subsequent Events**

On January 8, 2010, the District issued a \$260,000 Wastewater Revenue Capital Loan Note, Series 2010 for the purpose of paying the construction costs of a community-wide sanitary sewer collection and treatment system to serve the residents of Bouton. The note proceeds paid the outstanding principal of the \$260,000 project anticipation note from F & M Bank. The Series 2010 note bears interest at 4.00% per annum with monthly principal and interest payments of \$1,088. The note matures on January 8, 2050.

On January 25, 2010, the District approved a rate increase ranging from 25% to 44% of the volumetric rate component of each of the three ethanol plant customers. With this rate increase, industrial water sales revenues are projected to increase 12% to 13% in 2010.

On March 22, 2010, the District approved a 22% rate increase for residential and commercial water users. This rate increase is part of a proposal made by the Board of Directors to sell the District's assets to a new entity managed by the Des Moines Water Works. On April 16, 2010, Assured Guaranty Corporation, acting as agent for the bond insurer of the Water Revenue Bonds, Series 2006, acknowledged the rate increase was lower than the increase recommended by a consultant which serves public infrastructure organizations retained by counsel for Assured Guaranty Corporation.

The June 1, 2010, interest payment on the Water Revenue Bonds, Series 2006 was paid from the remaining funds in restricted cash – Series 2006 reserve and certain other cash and cash equivalents. The amount transferred was \$69,250 less than the debt payment due. The paying agent for the Series 2006 bonds has submitted a claim to the bond insurer for the shortfall.

At June 1, 2010 the District is in default on the payment of a Bank of America note.

**(12) Going Concern**

The District is past due on monthly principal and interest payments on the USDA Rural Development water revenue notes since October 1, 2009. The USDA notified the District it will ask the District to enter into a formal workout agreement. If an agreement cannot be reached or the agreement is unable to correct the deficiency, other servicing actions, such as reamortization or rescheduling, transfer and assumption, sale, receivership or foreclosure, may be considered.

The net revenues of the District did not meet the debt service coverage ratio requirement of not less than 100% of the principal and interest payments on the bonds and other parity obligations during the year. Without sufficient water revenues, the District will not be able to pay principal and interest coming due on the bonds and parity obligations from the sinking account. The reserve account is not sufficient to meet the current maturities of the bonds and parity obligations. In addition to the parity obligations, the District has \$9,029,817 of project anticipation notes maturing on various dates in 2010.

Subsequent to December 31, 2009, Assured Guaranty Corp., acting as an agent for the bond insurer of the Water Revenue Bonds, Series 2006, requested the District implement water rate increases to a level recommended by a consultant which serves public infrastructure organizations. The consultant's report concludes the District would still not meet its financial obligations in 2010 and thereafter with the recommended water rate structure.

The Board of Directors recommended the sale of the District's assets to a new entity managed by the Des Moines Water Works. The terms of the sale would require debt relief from the District's lenders. The District believes the increase in water rates required to address the District's insolvency, without significant debt relief, would likely cause substantial membership loss, which could lead to the collapse of the District.

The District also plans to dispose of water line construction equipment with a remaining book value of approximately \$1,300,000. The District plans to dispose of excess construction material inventory and further reduce its labor expenses.

**(13) Litigation**

The District is a party to pending eminent domain litigation and a threatened trespass action stemming from the District's alleged actions during the installation of a waterline. The District and plaintiffs have agreed upon a settlement of \$8,000, though plaintiffs' counsel has not prepared a settlement agreement or dismissal.

The District is party to pending litigation for nonpayment for the construction of a water tower. The plaintiff is seeking to enforce a mechanic's lien. The balance due of \$166,550 is included in accounts payable – construction at December 31, 2009.

The bond insurer of the water revenue bonds, Series 2006, has threatened an action seeking a writ of mandamus requiring the Board to implement a water rate increase sufficient to comply with net revenue pledges and covenants of the bonds. The Board approved a 22% water rate increase on March 22, 2010. A writ of mandamus could result in further rate increases.

**(14) Restatements**

The beginning net assets for 2009 and 2008 have been restated to correct an error in reporting capital grant revenue. Grant revenue is to be recognized when all applicable eligibility requirements are met. The District previously recognized grant revenues when the grant was awarded. The total effect of this restatement is to decrease previously reported net assets \$1,219,000 at January 1, 2008.

The beginning net assets for 2009 and 2008 have also been restated to correct an error in reporting the depreciation of purchased capacity in other treatment facilities. In 2001, the District changed the useful life of purchased capacity in other treatment facilities to 60 years. The useful life of these purchased capacities is a maximum of 40 years according to the purchased capacity agreements. The total effect of this restatement is to decrease previously reported net assets and capital assets by \$400,213 at January 1, 2008.

The beginning net assets for 2009 and 2008 have been restated to correct an error in reporting capital loan notes after legal defeasance of water revenue capital loan notes series 1998, series 2002A and fixed rate capital loan notes, Series 2000 upon the issuance of the water revenue bonds, Series 2006. The effect of the restatement was to decrease the restricted cash – refunding escrow by \$2,241,205 and underwriter's cost on water revenue bonds – net of amortization by \$34,436 in 2008. The restatement decreased capital loan notes by \$2,185,000, accrued interest payable - bonds and notes by \$13,408 and net assets by \$77,233 in 2008.

The restatements increased (decreased) net assets and capital assets as follows:

	Year ended Dec 31, 2007	Year ended Dec 31, 2008	Dec 31, 2008 Capital Assets
Beginning balances, as previously reported	\$ 14,001,534	14,481,913	141,384,800
Correct grant revenues recognized before earned	(305,278)	(1,219,000)	-
Correct purchased capacity depreciation	(367,498)	(400,213)	(400,213)
Correct reporting for capital loan notes legally defeased	(139,818)	(77,233)	-
Beginning balances, as restated	<u>\$ 13,188,940</u>	<u>12,785,467</u>	<u>140,984,587</u>

**Other Supplementary Information**

**Schedule 1**

Xenia Rural Water District  
Schedule of Expenditures of Federal Awards  
Year ended December 31, 2009

Grantor/Program	CFDA Number	Agency or Pass-through Number	Program Expenditures
Indirect:			
U.S. Department of Agriculture: Iowa Rural Water Association: Rural Community Development Initiative	10.446		\$ 16,130
U.S. Department of Homeland Security: Iowa Department of Public Defense: Iowa Homeland Security and Emergency Management Division: Disaster Grants-Public Assistance (Presidentially Declared Disasters)	97.036	FEMA-IA-DR1763	<u>492,877</u>
Total indirect			<u>\$ 509,007</u>

**Basis of Presentation** – The Schedule of Expenditures of Federal Awards includes the federal grant activity of the Xenia Rural Water District and is presented on the accrual basis of accounting. The information on this schedule is presented in accordance with the requirements of OMB Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations. Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of, the basic financial statements.

See accompanying independent auditor's report.



**OFFICE OF AUDITOR OF STATE**  
**STATE OF IOWA**

David A. Vaudt, CPA  
Auditor of State

State Capitol Building  
Des Moines, Iowa 50319-0004

Telephone (515) 281-5834 Facsimile (515) 242-6134

Independent Auditor's Report on Internal Control  
over Financial Reporting and on Compliance and Other Matters  
Based on an Audit of Financial Statements Performed in Accordance with  
Government Auditing Standards

To the Members of the  
Xenia Rural Water District:

We have audited the accompanying financial statements of the Xenia Rural Water District as of and for the year ended December 31, 2009, and have issued our report thereon dated June 2, 2010. We conducted our audit in accordance with U.S. generally accepted auditing standards 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

In planning and performing our audit, we considered the Xenia Rural Water District's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing our opinion on the effectiveness of the Xenia Rural Water District's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Xenia Rural Water District'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 would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed below, we identified deficiencies in internal control over financial reporting that we consider to be significant deficiencies, including a material weakness.

A control deficiency exists when the design or operation of the control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the Xenia Rural Water District's ability to initiate, authorize, record, process or report financial data reliably in accordance with U.S. generally accepted accounting principles such that there is more than a remote likelihood a misstatement of the Xenia Rural Water District's financial statements that is more than inconsequential will not be prevented or detected by the Xenia Rural Water District's internal control. We consider the deficiencies in internal control described in the accompanying Schedule of Findings and Questioned Costs to be a significant deficiencies in internal control over financial reporting.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood a material misstatement of the financial statements will not be prevented or detected by the Xenia Rural Water District's internal control.

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, we believe the significant deficiency described as item (A) is a material weakness.

#### Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Xenia Rural Water District's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters, non-compliance 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 non-compliance or other matters required to be reported under Government Auditing Standards. However, we noted an immaterial instance of non-compliance that is described in the accompanying Schedule of Findings and Questioned Costs.

Comments involving statutory and other legal matters about the District's operations for the year ended December 31, 2009 are based exclusively on knowledge obtained from procedures performed during our audit of the financial statements of the District. Since our audit was based on tests and samples, not all transactions that might have had an impact on the comments were necessarily audited. The comments involving statutory and other legal matters are not intended to constitute legal interpretations of those statutes.

The Xenia Rural Water District's responses to the findings identified in our audit are described in the accompanying Schedule of Findings and Questioned Costs. While we have expressed our conclusions on the District's responses, we did not audit the Xenia Rural Water District's responses and, accordingly, we express no opinion on them.

This report, a public record by law, is intended solely for the information and use of the members and customers of the Xenia Rural Water District and other parties to whom the District may report, including federal awarding agencies and pass-through entities. This report is not intended to be and should not be used by anyone other than these specified parties.

We would like to acknowledge the many courtesies and assistance extended to us by personnel of the Xenia Rural Water District during the course of our audit. Should you have any questions concerning any of the above matters, we shall be pleased to discuss them with you at your convenience.



DAVID A. VAUDT, CPA  
Auditor of State



WARREN G. JENKINS, CPA  
Chief Deputy Auditor of State

June 2, 2010

**Independent Auditor's Report on Compliance with Requirements Applicable  
to Each Major Program and on Internal Control over Compliance  
in Accordance with OMB Circular A-133**

**Xenia Rural Water District**



**OFFICE OF AUDITOR OF STATE**  
**STATE OF IOWA**

David A. Vaudt, CPA  
Auditor of State

State Capitol Building  
Des Moines, Iowa 50319-0004

Telephone (515) 281-5834 Facsimile (515) 242-6134

Independent Auditor's Report on Compliance with Requirements  
Applicable to Each Major Program and on Internal Control over Compliance  
in Accordance with OMB Circular A-133

To the Members of the  
Xenia Rural Water District:

Compliance

We have audited the compliance of the Xenia Rural Water District with the types of compliance requirements described in U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement that are applicable to its major federal program for the year ended December 31, 2009. The Xenia Rural Water District's major federal program is identified in Part I of the accompanying Schedule of Findings and Questioned Costs. Compliance with the requirements of laws, regulations, contracts and grant agreements applicable to its major federal program is the responsibility of the Xenia Rural Water District's management. Our responsibility is to express an opinion on the Xenia Rural Water District's compliance based on our audit.

We conducted our audit of compliance in accordance with U.S. generally accepted auditing standards, the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States, and OMB Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether non-compliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the Xenia Rural Water District's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on the Xenia Rural Water District's compliance with those requirements.

In our opinion, the Xenia Rural Water District complied, in all material respects, with the requirements referred to above that are applicable to its major federal program for the year ended December 31, 2009.

Internal Control Over Compliance

The management of the Xenia Rural Water District is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts and grant agreements applicable to federal programs. In planning and performing our audit, we considered the Xenia Rural Water District's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the Xenia Rural Water District's internal control over compliance.

A control deficiency in the District's internal control over compliance 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 noncompliance with a type of compliance requirement of a federal program on a timely basis. A significant deficiency is a control deficiency, or a combination of control deficiencies, that adversely affects the District's ability to administer a federal program such that there is more than a remote likelihood noncompliance with a type of compliance requirement of a federal program that is more than inconsequential will not be prevented or detected by the District's internal control.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood material noncompliance with a type of compliance requirement of a federal program will not be prevented or detected by the District's internal control.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the District's internal control that might be significant deficiencies or material weaknesses as defined above. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses as defined above.

This report, a public record by law, is intended solely for the information and use of the members and customers of the Xenia Rural Water District and other parties to whom the Xenia Rural Water District may report, including federal awarding agencies and pass-through entities. This report is not intended to be and should not be used by anyone other than these specified parties.



DAVID A. VAUDT, CPA  
Auditor of State



WARREN G. JENKINS, CPA  
Chief Deputy Auditor of State

June 2, 2010

Xenia Rural Water District  
Schedule of Findings and Questioned Costs  
Year ended December 31, 2009

**Part I: Summary of the Independent Auditor's Results:**

- (a) A qualified opinion was issued on the financial statements due to significant uncertainties regarding the District's ability to continue its operations and to satisfy its creditors on timely basis.
- (b) Significant deficiencies in internal control over financial reporting were disclosed by the audit of the financial statements, including a material weakness.
- (c) The audit did not disclose any non-compliance which is material to the financial statements.
- (d) No material weaknesses in internal control over the major program were noted.
- (e) An unqualified opinion was issued on compliance with requirements applicable to the major program.
- (f) The audit did not disclose audit findings which were required to be reported in accordance with Office of Management and Budget Circular A-133, Section .510(a).
- (g) The major program was CFDA Number 97.036 – Disaster Grants – Public Assistance (Presidentially Declared Disasters).
- (h) The dollar threshold used to distinguish between Type A and Type B programs was \$300,000.
- (i) The Xenia Rural Water District did not qualify as a low-risk auditee.

Xenia Rural Water District  
Schedule of Findings and Questioned Costs  
Year ended December 31, 2009

**Part II: Findings Related to the Financial Statements:**

**SIGNIFICANT DEFICIENCIES:**

II-A-09 Financial Reporting – During the audit we identified trust assets and debt liabilities recorded in the District’s financial statements for debt legally defeased. Also, material amounts of capital asset depreciation had not been recorded. Additionally, grant receivables recorded in a prior year should not have been recorded and are no longer expected to be realized. Adjustments were subsequently made by the District to properly record these amounts in the financial statements. We also identified a component unit which should be blended with the Districts financial statements instead of being discretely presented.

Recommendation – The District should implement procedures to help ensure all amounts are properly recorded and presented in the District’s financial statements. Also, potential component units should be evaluated according to criteria established by the Governmental Accounting Standards Board and properly presented.

Response – The District will implement procedures to help ensure amounts are properly recorded and presented in the financial statements including consulting with the Office of Auditor of State and other Certified Public Accountants. The presentation of the component unit will be further evaluated.

Conclusions – Response accepted.

II-B-09 Capital Assets – The District does not have a written capital asset policy.

Recommendation – The District should adopt a written capital asset policy. The policy, at a minimum, should establish capitalization thresholds for the various asset classes, identify appropriate useful lives for calculating depreciation and require proper authorization for deletions.

Response – On March 22, 2010, the District adopted a written asset capitalization policy.

Conclusion – Response accepted

**INSTANCES OF NON-COMPLIANCE:**

No matters were noted.

Xenia Rural Water District  
Schedule of Findings and Questioned Costs  
Year ended December 31, 2009

**Part III: Findings and Questioned Costs For Federal Awards:**

**INSTANCES OF NON-COMPLIANCE:**

No matters were reported.

**SIGNIFICANT DEFICIENCIES:**

No material weaknesses in internal control over the major program were noted.

Xenia Rural Water District  
Schedule of Findings and Questioned Costs  
Year ended December 31, 2009

**Part IV: Other Findings Related to Required Statutory Reporting:**

IV-A-09 Questionable Disbursements – Certain disbursements we believe may not meet the requirements of public purpose as defined in an Attorney General’s Opinion dated April 25, 1979 since the public benefits to be derived have not been clearly documented were noted.

The District purchased debit cards totaling \$4,429 in December 2009 as a holiday bonus for employees.

Recommendation – The District should determine and document the public purpose served by these disbursements before authorizing any further payments. If this practice is continued, the District should establish written policies and procedures, including the requirement for proper documentation.

Response – The District will gain an understanding of certain disbursements defined by the Attorney General’s Opinion and establish policies and procedures on proper documentation. The District will document the public purpose served by the disbursements prior to authorizing any further payments.

Each employee of the District, on December 16, 2009, received additional compensation of \$100 after payroll taxes as a holiday bonus. The payments were disbursed in the form of debit cards. The minutes of the meeting at which the board approved this disbursement do not state the reason for this disbursement. However, when approving this disbursement, the board discussed that a holiday bonus would help improve staff morale, which was poor given the District’s financial condition and the lack of job security perceived by employees.

Conclusion – Response accepted.

IV-B-09 Travel Expense – No expenditures of District money for travel expenses of spouses of District officials or employees were noted.

IV-C-09 Bond Coverage – Surety bond coverage of District officials and employees is in accordance with statutory provisions. The amount of coverage should be reviewed annually to ensure the coverage is adequate for current operations.

IV-D-09 Board Minutes – No transactions were found that we believe should have been approved in the Board minutes but were not.

IV-E-09 Deposits and Investments – Except as noted below, no instances of non-compliance with the deposit and investment provisions of Chapter 12B and Chapter 12C of Code of Iowa were noted.

The District has not adopted a written investment policy which includes all the requirements of Chapter 12B.10B of the Code of Iowa

Recommendation – The District should ensure compliance with Chapters 12B and 12C of the Code of Iowa. Additionally, the District should adopt a written investment policy that complies with the provisions of Chapter 12B.10B of the Code of Iowa.

Xenia Rural Water District  
Schedule of Findings and Questioned Costs  
Year ended December 31, 2009

Response – The District will gain a better understanding of the requirements of Chapters 12B and 12C of the Code of Iowa and adopt an investment policy to ensure compliance with those requirements.

Conclusion – Response accepted.

IV-F-09 Official Depositories – A resolution naming official depositories was not located.

Recommendation – The District should adopt a depository resolution which establishes maximum deposit amounts for each bank and ensure the official depositories adequately secure all uninsured deposits as required by Chapter 12C.2 of the Code of Iowa.

Response – The District will adopt a depository resolution as required by Chapter 12C.2 of the Code of Iowa.

Conclusion – Response accepted.

IV-G-09 Bank Loan – On January 26, 2009, the District entered into a line of credit loan agreement and subsequently borrowed and repaid \$500,000 against the line of credit. The District did not publish notice and hold a public hearing before entering into the loan agreement.

Recommendation – Chapter 357A.11 of the Code of Iowa requires the District to follow Chapter 384.24A, which states, “The governing body shall follow substantially the same authorization procedure required for the issuance of general obligation bonds issued for the same purpose to authorize a loan agreement made payable from the debt service fund.” Pursuant to Chapter 384.25 of the Code of Iowa, the District should have published notice of and held a public hearing prior to entering into the loan agreement. In the future, the District should comply with the requirements of Chapters 357A, 384.24A and 384.25 of the Code of Iowa before entering into loan agreements.

Response – The District will comply with the requirements of Chapter 357A and Sections 384.24 and 384.25 of the Code of Iowa before entering into loan agreements.

Conclusion – Response accepted.

IV-H-09 Revenue Notes and Bonds – Instances of non-compliance with the revenue note and bond resolutions were noted, as follows:

The District is in default on the USDA water revenue notes at December 31, 2009. This appears to violate provisions of the water revenue note resolutions which state the District shall maintain user rates at a sufficient level for payment of expenses for operation and maintenance of the system and for payment of principal and interest on the notes.

The District did not meet the minimum balance requirements in the water reserve accounts.

Xenia Rural Water District

Schedule of Findings and Questioned Costs

Year ended December 31, 2009

The District has not established the required sinking and improvement accounts and therefore has not made required deposits.

While the District maintains surety bond coverage for employee theft, the amount does not meet the note and bond resolution requirements.

Recommendation – The District should review the note and bond provisions and comply with the requirements.

Response – The Board of Directors believes the District’s financial condition cannot be resolved by rate increases and changes in operations alone. On March 22, 2010, the District adopted a 22% rate increase for its residential and commercial water users. This rate increase is part of a proposal made by the Board of Directors to sell the District’s assets to a new entity managed by the Des Moines Water Works. The rate increase will not result in sufficient revenues to make the required principal and interest payments.

The District paid principal and interest payments on USDA RD notes and Series 2006 bonds from the water reserve accounts and was not able to restore the minimum balance requirements of the water reserve accounts.

The District will review the note and bond provisions for the establishment of the sinking and improvement funds and comply with the requirements to the extent sufficient revenues exist to make the required fund deposits.

The District will request increased coverage limits from its insurer.

Conclusion – Response accepted.

IV-I-09 Financial Condition – The District is in default on approximately \$45 million of outstanding USDA revenue bonds and has not made a monthly payment since September 2009. Additionally, the District used \$4,083,610 of debt service reserve series 2006 funds in order to meet the semi-annual interest and annual principal payment on the Wells Fargo Series 2006 water revenue bonds. The amount remaining in the debt service reserve series 2006 reserve fund at December 31, 2009 is \$579,197.

Recommendation – The District should raise rates, when possible, to generate sufficient funds to make required principal and interest payments and consult legal counsel to resolve these matters.

Response – The District has engaged legal counsel concerning default on the principal and interest on USDA Rural Development water revenue notes and Series 2006 water revenue bonds.

On March 22, 2010, the District adopted a 22% rate increase for its residential and commercial water users. This rate increase is part of a proposal made by the Board of Directors to sell the District’s assets to a new entity managed by the Des Moines Water Works. The rate increase will not result in sufficient revenues to make the required principal and interest payments.

Conclusion – Response acknowledged.

Xenia Rural Water District

Schedule of Findings and Questioned Costs

Year ended December 31, 2009

IV-J-09 CRP Agreement – The District has entered into a lease agreement with an employee for land owned by the District. The land has been put into the United States Department of Agriculture (USDA) Conservation Reserve Program (CRP). Under the agreement, the amount of rent paid by the employee to the District is based on the annual amount of the CRP payments, which was approximately 80% of the total CRP payment during fiscal year 2009. At the time of this agreement, the District was eligible to participate in CRP, but the State of Iowa and all political subdivisions were considered one entity for payment determinations, which effectively limited the number of governmental entities which received CRP payments. It is not clear whether the District would have received CRP payments in the absence of the lease agreement.

Recommendation – The District should discuss the details of the lease agreement between the District and the employee with the USDA to ensure compliance with CRP requirements.

Response – The District will discuss the lease arrangement with the USDA to ensure continued compliance with CRP requirements.

Conclusion – Response accepted.

Xenia Rural Water District  
Schedule of Findings and Questioned Costs  
Year ended December 31, 2009

IV-K-09 Other Information Required by the Bond Resolution

Insurance – The following insurance policies were in force at December 31, 2009:

Insurer	Description	Amount	Expiration Date
EMC Insurance Companies	Property:		
	Blanket: Buildings and personal property	\$ 28,187,745	5/1/10
	Extra expense	75,000	5/1/10
	Contractors equipment	4,821,207	5/1/10
	Leased contractors equipment	300,000	5/1/10
	Miscellaneous property - Radios and GPS	92,140	5/1/10
	Data processing - equipment and software	132,500	5/1/10
	Off-site tools and equipment:		
	Per installation site	300,000	5/1/10
	Property temporarily off premises	20,000	5/1/10
	Property in transit	40,000	5/1/10
EMC Insurance Companies	General liability coverage:		
	General aggregate	2,000,000	5/1/10
	Products general liability	2,000,000	5/1/10
	Personal and/or advertising	1,000,000	5/1/10
	Each occurrence	1,000,000	5/1/10
	Fire damage	100,000	5/1/10
Medical expense	5,000	5/1/10	
EMC Insurance Companies	Automobile coverage:		
	Liability	500,000	5/1/10
	Medical payments	1,000	5/1/10
	Uninsured motorists	100,000	5/1/10
Underinsured motorists	100,000	5/1/10	
Chartis Specialty Workers Comp Group	Workers' compensation: Employee liability limit	1,000,000	5/1/10
EMC Insurance Companies	Commercial umbrella:		
	Policy aggregate	5,000,000	5/1/10
EMC Insurance Companies	Public Officials Errors and Omissions:		
	Each loss	1,000,000	5/1/10
Aggregate	1,000,000	5/1/10	
EMC Insurance Companies	Fidelity coverage:		
	Per loss - Employee Dishonesty	1,000,000	5/1/10
	Per loss deductible	10,000	5/1/10
EMC Insurance Companies	Employee benefit liability:		
	Each loss from administrative errors	1,000,000	5/1/10
Aggregate	2,000,000	5/1/10	

Xenia Rural Water District  
 Schedule of Findings and Questioned Costs  
 Year ended December 31, 2009

Water Rates – The following water rates were in force at December 31, 2009:

	<u>Gallons</u>	<u>Rate</u>
Water rates in effect at December 31, 2009:		
Rural 5/8" meter (non-franchise users)		
Minimum	0-2,000	\$34.06 to \$39.38
Steps	per 1,000 after minimum	\$10.00 to \$3.24
Franchise 5/8" meter		
Minimum	0-2,000	\$11.68 to \$34.60
Steps	per 1,000 after minimum	\$7.78 to \$3.24
Water rates in effect at December 31, 2008:		
Rural 5/8" meter (non-franchise users)		
Minimum	0-2,000	\$32.13 to \$37.15
Steps	per 1,000 after minimum	\$10.00 to \$3.06
Franchise 5/8" meter		
Minimum	0-2,000	\$11.02 to \$32.64
Steps	per 1,000 after minimum	\$7.34 to \$3.06

For 3/4" meters, the minimum charge and included gallons is two times those of the 5/8" meter.  
 For 1" meters, the minimum charge and included gallons is three times those of the 5/8" meter.  
 For 1 1/2" meters, the minimum charge and included gallons is five times those of the 5/8" meter.  
 For 2" meters, the minimum charge and included gallons is eight times those of the 5/8" meter.

Statistical Information

<u>Description</u>	<u>Amount</u>
Water customers served at December 31, 2009	9,392

---

Xenia Rural Water District

Staff

This audit was performed by:

Ernest H. Ruben, Jr., CPA, Manager  
Brett M. Zeller, Staff Auditor  
Lori M. Dinville, Staff Auditor

A handwritten signature in black ink that reads "Andrew E. Nielsen". The signature is written in a cursive style with a large initial "A" and "N".

Andrew E. Nielsen, CPA  
Deputy Auditor of State