OFFICE OF AUDITOR OF STATE

STATE OF IOWA

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NEWS RELEASE

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FOR RELEASE August 23, 2012

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

The District had total revenues of $19,242,490 for the year ended December 31, 2011, an 83% increase over the prior year. Revenues included water sales of $10,480,836 and system connection fees of $281,014. The increase in revenues was primarily due to an increase in water rates and gains of $1,187,184 from the sale of capital assets and $6,669,701 due to the forgiveness of debt by a creditor.

Expenses totaled $15,330,933 for the year ended December 31, 2011, a 23% decrease from the prior year. Expenses included $6,054,795 of interest expense, $3,426,990 of depreciation/amortization and $1,479,395 for salaries and wages. The decrease in expenses is due primarily to decreased operating expenses and recognition of losses on inventory, asset impairment and uncollectible TIF receivable in the prior year.

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/1133-0037-B000.pdf.

# # #

XENIA RURAL WATER DISTRICT

INDEPENDENT AUDITOR'S REPORTS
BASIC FINANCIAL STATEMENTS AND
OTHER INFORMATION
SCHEDULE OF FINDINGS

DECEMBER 31, 2011 and December 31, 2010

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Xenia Rural Water District

Officials

(Before April 2011)

Name	Title	Term Expires
Walt Tomenga	Chair	Apr 2011
Thomas Pierce	Vice Chair	Apr 2011
Frank Hayer	Treasurer	Apr 2013
David Larson	Secretary	Apr 2011
Marc DeLong	Director	(Resigned)
Jim Fevold	Director	Apr 2011
Greg Rinehart	Director	Apr 2012
Troy Wilson	Director	Apr 2013
Marc DeLong (Appointed)	Interim Executive Director	Indefinite
Greg Clay	Controller	Indefinite

(After April 2011)

Name	Title	Term Expires
Walt Tomenga	Chair	Apr 2013
Greg Rinehart	Vice Chair	Apr 2012
Steve Mestad	Treasurer	Apr 2014
Jean Bromert	Secretary	Apr 2014
Frank Hayer	Director	Apr 2013
Dan Lovett	Director	Apr 2013
Troy Wilson	Director	Apr 2013
Tamera Mason	General Manager	Indefinite
Greg Clay	Controller	(Resigned)
Gary Andrews (Appointed)	Interim Controller	Indefinite

Xenia Rural Water District

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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 years ended December 31, 2011 and 2010. 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 audits.

We conducted our audits 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 audits provide 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 $2,488,342 at December 31, 2011. The District is working to restructure its debt. However, there are significant uncertainties regarding the District's ability to continue its operations and to satisfy its obligations to its creditors on a timely basis. In addition, the District has been unable to renegotiate its borrowings from its parity lenders. Consequently, adjustments may be required to the recorded asset amounts and the classification of liabilities.

In our opinion, except for the adjustments, if any, that may be required to the recorded asset amounts and the 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, 2011 and 2010, 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 August 14, 2012 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.

U.S. generally accepted accounting principles require Management's Discussion and Analysis and the Schedule of Finding Progress for the Retiree Health Plan on pages 7 through 12 and 38 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board which considers it to be an essential part of the financial reporting for placing the basic financial statements in an appropriate operational, economic or historical context. We have applied certain limited procedures to the required supplementary information in accordance with U.S. generally accepted auditing standards, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the required supplementary information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

DAVID A. VAUDT, CPA	WARREN G. JENKINS, CPA
Auditor of State	Chief Deputy Auditor of State

August 14, 2012

MANAGEMENT'S DISCUSSION AND ANALYSIS

As financial management of the District, we offer readers of these financial statements 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.

FINANCIAL HIGHLIGHTS

- The District's net assets increased 430%, or $3,911,557, in 2011 and decreased 111%, or $9,323,872, in 2010 as a result of operations and other gains or losses in the respective years.
- Operating revenue increased 9.1%, or $937,757, in 2011. The increase in operating revenues resulted from a rate increase. Operating revenue in 2010 increased $1,205,015, or 13.2%, over 2009.
- Operating expenses decreased 5.8%, or $548,450, in 2011 because of factors such as lower salaries and wages, lower purchased water expenses and lower professional fee expenses. Operating expenses in 2010 increased $1,970,446, or 26.4%, over 2009, because of decreased capitalized salary and wages and continued professional fee expenses.

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 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 years.

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 operating activities, capital and related financing activities and investing activities.

The Notes to Financial Statements 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.

Required Supplementary Information further explains and supports the financial statements by presenting the Schedule of Funding Progress for the Retiree Health Plan.

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 2011 totaled $3,001,576. This compares to a deficit of $909,981 at the end of 2010. A summary of the District's net assets is presented below.

Net Assets			
	December 31,		
	2011	2010	2009
Current assets	$ 7,671,317	4,020,695	3,899,594
Noncurrent assets	1,346,532	1,760,875	3,799,592
Capital assets (net of accumulated depreciation/amortization)	126,728,850	134,034,721	140,498,914
Total assets	135,746,699	139,816,291	148,198,100
Current liabilities	10,159,659	16,181,921	13,252,299
Noncurrent liabilities	122,585,464	124,544,351	126,531,910
Total liabilities	132,745,123	140,726,272	139,784,209
Net assets:			
Invested in capital assets, net of related debt	-	-	2,552,945
Restricted	2,509	-	-
Unrestricted (deficit)	2,999,067	(909,981)	5,860,946
Total net assets	$ 3,001,576	(909,981)	8,413,891

Net assets increased $3,911,557 during the year ended December 31, 2011 and decreased $9,323,872 during the year ended December 31, 2010. The increase in net assets is primarily the result of a gain of $6,669,701 due to the forgiveness of project anticipation notes and $1,187,184 from a gain on the disposition of capital assets. Reasons for the decrease in net assets in 2010 were impairment losses on capital assets and holding losses on inventory.

Total liabilities of the District were $132,745,123 and $140,726,272 at December 31, 2011 and 2010, respectively. Noncurrent liabilities included in total liabilities were $122,585,464 and $124,544,351 at December 31, 2011 and 2010, respectively. Total liabilities decreased $7,981,149 in 2011 and increased $942,063 in 2010. The decrease in liabilities at December 31, 2011 was primarily the result of the project anticipation note debt forgiveness.

A significant portion of the District's total assets, 93% and 96%, were invested in capital assets at December 31, 2011 and 2010, respectively.

Statement of Revenues, Expenses and Changes in Net Assets

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

Changes in Net Assets			
	Year Ended December 31,		
	2011	2010	2009
Operating revenues	$ 11,284,396	10,346,639	9,141,624
Operating expenses	(8,881,982)	(9,430,432)	(7,459,986)
Operating income	2,402,414	916,207	1,681,638
Nonoperating revenue	7,958,094	195,314	1,313,651
Nonoperating expenses	(6,448,951)	(10,435,393)	(5,363,541)
Extraordinary loss	-	-	(2,003,324)
Change in net assets	$ 3,911,557	(9,323,872)	(4,371,576)

The Statement of Revenues, Expenses and Changes in Net Assets reflects an increase in net assets in 2011 and a decrease in both 2010 and 2009.

Year ended December 31, 2011:

The change in net assets in 2011 was a result of the following: 1) Total operating revenue increased 9.1% over the prior year because of water rate increases. The District's water revenue of $10,480,836 increased 10.0% over 2010. In May 2011, a water rate increase went into effect for all users. 2) Operating expenses decreased 5.5% from 2010. Decreases in operating expenses were from lower payroll, lower purchased water costs and lower professional fees. 3) Non-operating revenues increased 3,975% over 2010. The increase was a result of gains from the sale of capital assets and the forgiveness of debt. 4) Non-operating expenses decreased 38% from 2010. In 2010, the District recognized impairment losses of $2,304,905 on water and wastewater capital assets in Worth County because of a construction stoppage and the likely disposal of the assets. A loss of $576,483 was recognized in 2010 for the subsequent year's sale of land held as a prospective water treatment plant site. A holding loss of $1,215,819 occurred from a valuation adjustment of surplus inventory to the lower of cost or market. The market value was based on sales experience on inventory disposal in the subsequent year. A receivable of $254,989 for costs incurred on infrastructure projects to provide the Hartland Township Economic Development Renewal Area in Worth County with water and wastewater services were written off as uncollectible. Interest expense increased slightly to $6,054,795.

Year ended December 31, 2010:

The change in net assets in 2010 was a result of the following: 1) Total operating revenue increased 13% over the prior year because of water rate increases and additional usage by industrial customers. The District's water revenue of $9,531,751 increased 13% over 2009. 26% of the water revenue increase was a result of increased gallons purchased by industrial users and volumetric rate increases to users in the industrial user class. On May 15, 2010, a water rate increase of 22% went into effect for residential and commercial users. 2) Operating expenses increased 26% from 2009. Professional fees addressing the District's insolvency accounted for $687,360 of the $1,966,446 increase in operating expenses. Additional depreciation/amortization accounted for $478,675 of the increase. The increase in depreciation/amortization was a result of a full year of depreciation expense on over $20,000,000 of capital asset projects placed in service in 2009 being recognized in 2010 and the inclusion of depreciation expense for the remaining vehicles and equipment previously capitalized as capital asset project costs. Other increases in operating expenses were from payroll overhead no longer capitalized to capital assets and increased costs for purchased water. 3) Non-operating revenues decreased 89% from 2009. The decrease was a result of a lesser number of custom connection fees and a decrease of land generating rental income. Interest income increased 151% as the District increased investment balances. The rate of return earned on investments remained low. 4) Non-operating expenses increased 94% from 2009. The District recognized impairment losses of $2,304,905 on water and wastewater capital assets in Worth County because of a construction stoppage and the likely disposal of the assets. A loss of $576,483 was recognized in 2010 for the subsequent year's sale of land held as a prospective water treatment plant site. A holding loss of $1,215,819 occurred from a valuation adjustment of surplus inventory to the lower of cost or market. The market value was based on sales experience on inventory disposal in the subsequent year. A receivable of $254,989 for costs incurred on infrastructure projects to provide the Hartland Township Economic Development Renewal Area in Worth County with water and wastewater services were written off as uncollectible. Interest expense increased 17% to $6,033,527, net of interest capitalized on capital assets of $22,628.

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 employee payroll and payments to suppliers. Cash used by 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,		
	2011	2010	2009
Cash flows provided (used) by:			
Operating activities	$ 6,372,710	4,657,911	4,750,778
Capital and related financing activities	(2,663,709)	(5,138,985)	(10,465,407)
Investing activities	26,642	621,187	7,898,943
Net increase in cash	3,735,643	140,113	2,184,314
Cash beginning of year	2,437,407	2,297,294	112,980
Cash end of year	$ 6,173,050	2,437,407	2,297,294

CAPITAL ASSETS

The following summarizes capital assets:

	December 31,		
	2011	2010	2009
Nondepreciable assets	$ 2,124,389	3,643,774	5,456,325
Depreciable assets	144,794,350	150,203,865	152,344,395
Intangible assets	4,975,332	4,967,737	5,148,100
Accumulated depreciation/amortization	(25,165,221)	(24,780,655)	(22,449,906)
Total capital assets, net of accumulated depreciation/amortization	$ 126,728,850	134,034,721	140,498,914

Capital assets, net of accumulated depreciation/amortization, (including water lines, equipment and buildings) of the District were $126,728,850 and $134,034,721 at December 31, 2011 and 2010, respectively. This is a net decrease of $7,305,871 during the year ended December 31, 2011. Total capital assets decreased because of the disposal of surplus construction equipment.

Construction in progress included in nondepreciable capital assets was $8,431 and $633,239 at December 31, 2011 and 2010, respectively. The District has decided to discontinue development of a treatment plant in Dallas County, resulting in an impairment loss of $391,532. 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. Further details on capital assets are presented in Note 4 of the Notes to Financial Statements.

LONG TERM DEBT

The following summarizes outstanding long-term debt:

	December 31,		
	2011	2010	2009
Revenue notes	$ 45,632,446	45,635,253	45,377,746
Revenue bonds	80,136,560	81,400,160	82,608,760
Assured Guaranty Corporation	2,440,580	1,329,936	-
Project anticipation notes	1,468,168	9,029,817	9,289,817
Asset purchase agreement	76,426	76,426	77,579
Rural community 2000 loan	20,000	20,000	20,000
Total	$ 129,774,180	137,491,592	137,373,902

The District repaid no principal on previously issued USDA Rural Development water revenue bonds. $1,110,644 of the total principal payment of $1,285,000 on Water Revenue Bonds Series 2006 was paid by the bond insurer when the District did not have sufficient sinking or reserve funds for the payment. For further detail on long-term debt, see Note 7 of the Notes to Financial Statements.

In 2010, the District issued a $260,000 wastewater revenue capital loan note 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 proceeds of the note paid the balance due on the related anticipation note funding its construction.

Debt service coverage has been calculated based on the definitions of gross revenues, operating expenses and special charges as defined in the Water Revenue Bonds Series 2006 resolution. Debt service coverage on the scheduled water parity debt payments of the District was 51% at December 31, 2011 and 52% at December 31, 2010. 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.

In 2010, the District again used funds from the restricted cash, Series 2006 reserve to make debt service payments. The balance requirement for the restricted reserve is $5,225,300. At December 31, 2011 and 2010, the balance of the restricted cash, Series 2006 reserve was $0 and $0, respectively.

The USDA Rural Development bond resolution requires 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 7 of the Notes to Financial Statements.

In July 2011, CIFG Assurance North America, Inc. (CIFG NA), the bond insurer, and Assured Guaranty Corporation, the reinsurance company, reached a settlement where the Water Revenue Bonds, Series 2006 guarantee has been assumed by Assured Guaranty Corporation under the Quota Share Reinsurance Agreement dated January 21, 2009. Because of this guarantee, the long term and underlying ratings on the District's 2006 water revenue bonds were raised from 'D' to 'AA-'. The District's prior rating of 'D' was the result of the District not paying obligations in accordance with terms of the agreement. The District was unable to fully service its June 1, 2010 interest payment and, having exhausted the debt service reserve, filed a claim with the bond insurer for the remainder of the payment.

ECONOMIC OUTLOOK

The District believes there is substantial doubt about its ability to continue as a going concern. The District is not producing sufficient net revenues (gross revenues less on-going costs of operations and maintenance) to stay current on debt payments and to replenish its debt reserves. In this regard, the District did not achieve sufficient net revenues from the water system during 2011 or 2010 to meet sinking fund requirements and debt service reserve funds were exhausted to make partial payment of principal and interest on bonds. The bond insurer of the Water Revenue Bonds Series 2006 covered two payment shortfalls during 2010 and one payment shortfall in 2011 as described in Note 7 of the Notes to Financial Statements. Although the District realized an increase in net assets during 2011, the increase was largely the result of debt forgiveness by a creditor.

The District's Board of Directors approved a USDA requested debt work-out plan at its January 2012 meeting. This proposal also has been provided to its parity lenders for consideration. Although further member rate increases, as well as reduced costs by means of improved employee productivity and best practices related to material and supplies costs, are essential elements, further contributions by the ethanol plant owners to whom the District provides one-half of its delivered water, as well as debt restructure and relief from its creditors is critical to resolving the District's financial insolvency.

Additional going concern information is presented in Note 13 of the Notes to Financial Statements, including a description of the essential elements of the Board approved debt work-out plan.

OTHER INFORMATION

In addition to the basic financial statements and accompanying Notes to Financial Statements, this report presents other information, including the Schedule of Funding Progress for the Retiree Health Plan and the Schedule of Findings. This information can be found on pages 38 through 48.

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 Controller of the Xenia Rural Water District at (515) 676-2117 or 23998 141st Street, Bouton, Iowa 50039.

Basic Financial Statements

Xenia Rural Water District

Statement of Net Assets

December 31, 2011 and 2010

	December 31, 2011	December 31, 2010
Assets		
Current assets:		
Cash and cash equivalents	$ 6,173,050	2,437,407
Accounts receivable:		
Trade	1,365,652	1,429,440
Other	51,973	81,320
Prepaid expenses	80,642	72,528
Total current assets	7,671,317	4,020,695
Noncurrent assets:		
Inventory	626,913	1,016,044
Capital assets (net of accumulated depreciation/amortization)	126,728,850	134,034,721
Unamortized bond issuance costs	602,417	622,609
USDA Rural Development restricted cash reserve	61,453	61,430
Organizational costs (net of amortization)	55,749	60,792
Total noncurrent assets	128,075,382	135,795,596
Total assets	$ 135,746,699	139,816,291

Xenia Rural Water District

Statement of Net Assets

December 31, 2011 and 2010

	December 31, 2011	December 31, 2010
Liabilities		
Current liabilities:		
Accounts payable:		
Trade	$ 1,354,667	923,433
Construction	-	14,433
Accrued payroll taxes, IPERS contribution and sales tax	82,737	65,305
Accrued payroll	25,105	29,838
Accrued compensated absences	47,089	44,698
Customer deposits	69,124	75,710
Sewer payables	20,033	20,157
Accrued interest payable:		
USDA Rural Development revenue notes	1,002,787	1,355,683
Water revenue bonds, Series 2006	305,241	309,256
Other bonds and notes	56,160	392,167
Current portion of long-term debt	7,196,716	12,951,241
Total current liabilities	10,159,659	16,181,921
Noncurrent liabilities:		
Revenue notes payable	43,718,890	44,361,057
Revenue bonds payable	78,801,560	80,115,160
Asset purchase agreement payable	57,014	64,134
Net OPEB liability	8,000	4,000
Total noncurrent liabilities	122,585,464	124,544,351
Total liabilities	132,745,123	140,726,272
Net assets		
Restricted for sewer bond debt service	2,509	-
Unrestricted (deficit)	2,999,067	(909,981)
Total net assets	3,001,576	(909,981)
Total liabilities and net assets	$ 135,746,699	139,816,291

See notes to financial statements.

Xenia Rural Water District

Statement of Revenues, Expenses and
Changes in Net Assets

Years ended December 31, 2011 and 2010

	December 31, 2011	December 31, 2010
Operating revenues:		
Water sales:		
Residential	$ 7,112,457	6,353,379
Commercial	636,233	600,563
Industrial	2,500,221	2,399,377
Wholesale	231,925	178,432
Service charges	282,971	255,616
Contracted billing:		
Water	17,384	23,931
Wastewater	33,190	36,916
Connection fees:		
Water	208,494	206,479
Wastewater	-	6,536
Wastewater revenue	260,389	273,359
Lab fees	-	5,085
Miscellaneous	1,132	6,966
Total operating revenues	11,284,396	10,346,639
Operating expenses:		
Provision for depreciation/amortization:		
Wastewater systems	61,349	127,724
Other	3,365,641	3,272,858
Salaries and wages	1,479,395	1,582,779
Purchased water	1,077,596	1,221,142
Professional fees	577,962	1,085,403
Utilities	328,996	335,581
Chemicals	288,066	261,999
Payroll taxes	116,565	122,860
General insurance	192,413	218,912
Employee benefits	268,295	296,557
Repair	277,273	167,383
Wastewater operations	157,106	147,642
Fuel	180,307	141,189
Maintenance	190,815	132,729
Office expense	106,302	80,197
Postage and freight	31,341	50,714
Telephone	47,167	47,481
Vehicle repair and maintenance	18,302	35,923
Testing and lab	43,934	32,664
Amortization of bond costs	25,236	25,236
Licenses, dues and subscriptions	6,961	10,051

Xenia Rural Water District

Statement of Revenues, Expenses and
Changes in Net Assets

Years ended December 31, 2011 and 2010

	December 31, 2011	December 31, 2010
Operating expenses (continued):		
Miscellaneous	11,759	13,809
Bank fees and service charges	14,281	6,733
Continuing education	3,502	6,056
Mileage	1,886	2,667
Advertising and promotion	3,664	2,249
Directors' per diem	2,391	1,499
Meals and lodging	3,477	395
Total operating expenses	8,881,982	9,430,432
Operating income	2,402,414	916,207
Non-operating revenues (expenses):		
Grant revenue	2,023	-
Custom connection and relocation fees:		
Water	72,520	86,211
Wastewater	-	16,794
Interest income	2,816	4,466
Interest expense	(6,054,795)	(6,033,527)
Rental income	23,850	37,563
Holding loss on inventory	-	(1,215,819)
Loss on land sale	-	(576,483)
Gain on sale of capital assets	1,187,184	50,280
Gain on forgiveness of debt	6,669,701	-
Miscellaneous	(482)	-
Impairment loss	(391,532)	(2,304,905)
Uncollectible TIF receivable	-	(254,989)
Loss on disposal of inventory	(2,142)	(49,670)
Net non-operating revenues (expenses)	1,509,143	(10,240,079)
Change in net assets	3,911,557	(9,323,872)
Net assets beginning of year	(909,981)	8,413,891
Net assets (deficit) end of year	$ 3,001,576	(909,981)

See notes to financial statements.

Xenia Rural Water District

Statement of Cash Flows

Years ended December 31, 2011 and 2010

	December 31, 2011	December 31, 2010
Cash flows from operating activities:		
Cash received from customers	$ 11,381,097	10,158,422
Cash payments to employees for services	(1,892,611)	(2,066,010)
Cash payments to suppliers for goods and services	(3,115,776)	(3,434,501)
Net cash provided by operating activities	6,372,710	4,657,911
Cash flows from capital and related financing activities:		
FEMA public assistance grant received	15,175	-
Other grants received	2,023	2,435
Cash received from custom connection fees	72,520	80,000
Proceeds from bonds and other long-term debt	-	260,000
Proceeds from sale of assets	5,037,621	474,398
Proceeds from sale of excess inventory	325,126	-
Acquisition and construction of capital assets	(292,595)	(581,007)
Principal paid on bonds and notes	(1,054,466)	(263,646)
Interest paid on bonds and notes	(6,769,113)	(5,111,165)
Net cash used by capital and related financing activities	(2,678,884)	(5,138,985)
Cash flows from investing activities:		
Proceeds from sale of investments	-	579,197
Purchase of investments	(24)	(57)
Investment income	26,666	42,047
Net cash provided by investing activities	26,642	621,187
Net increase in cash and cash equivalents	3,720,468	140,113
Cash and cash equivalents beginning of year	2,437,407	2,297,294
Cash and cash equivalents end of year	$ 6,157,875	2,437,407

Xenia Rural Water District

Statement of Cash Flows

Years ended December 31, 2011 and 2010

	December 31, 2011	December 31, 2010
Reconciliation of operating income to net cash provided by operating activities:		
Operating income	$ 2,402,414	916,207
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation - wastewater systems	61,349	127,724
Depreciation - other	3,365,641	3,272,858
Amortization	25,236	25,236
Gain on forgiveness of debt	6,755	-
Loss on disposal of inventory	(2,888)	(49,670)
Changes in assets and liabilities:		
Accounts receivable	93,135	(190,640)
Prepaid expenses	(8,114)	(24,783)
Accounts payable	416,801	598,241
Accrued salaries and wages	(2,341)	(23,884)
Accrued payroll taxes, IPERS and sales tax	17,432	(158)
Other postemployment benefits	4,000	4,000
Customer deposits	(3,886)	3,504
Sewer payable	(124)	(324)
Membership refund liability	(2,700)	(400)
Total adjustments	3,970,296	3,741,704
Net cash provided by operating activities	$ 6,372,710	4,657,911
Non-cash capital and related financing activities:		
Holding loss on inventory	$ -	1,215,819
Loss on land sale	-	(576,484)
Impairment loss	(391,532)	(2,304,905)
Uncollectible TIF receivable	-	(254,989)
Principal forgiven on project anticipation notes	6,662,946	-
Principal paid by debt guarantor	1,110,644	1,230,000
Interest paid by debt guarantor	-	99,936
Total	$ 7,382,058	(590,623)

See notes to financial statements.

(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 have one vote at the annual meeting. The Directors are elected to staggered 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 filed for administrative dissolution, effective August 9, 2011.

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/amortization) 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/amortization 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.

In January 2011, the District changed from the units of production method to the straight line method for depreciating construction equipment. Capital assets of the District are depreciated/amortized 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
Intangibles, purchased capacity	40
Intangibles, software	3-5
Plant building	40
Office building and improvements	7-39
Equipment and tools	3-12
Transportation equipment	3-7
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, 2011 and 2010, interest costs of $0 and $22,628, 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, 2011 and 2010.

Inventory – Inventories are valued at the lower of cost (first-in, first-out) 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. Excess inventory held for sale is stated at estimated realizable value.

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 the water revenue bonds, series 2006 for the purpose of refunding 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 the water revenue bonds, series 2006 for the purpose of refunding 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 2011 and 2010 was $46,635 and $46,635, respectively. Estimated amortization expense for each of the ensuing years through December 31, 2016 is $46,635.

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, 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 have been reclassified to conform to current year presentations.

(2) Cash and Investments

The District's deposits in banks at December 31, 2011 and 2010 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.

In addition, the District had investments in the Iowa Public Agency Investment Trust which are valued at an amortized cost of $64,428 pursuant to rule 2a-7 under the Investment Company Act of 1940. The investment in the Iowa Public Agency Investment Trust is unrated for credit risk purposes.

(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 4.50% of their annual covered salary until July 1, 2011, at which time the contribution rate changed to 5.38% of their annual covered salary. The District was required to contribute 6.95% of annual covered payroll until July 1, 2011, at which time the contribution rate changed to 8.07% of annual covered payroll. Contribution requirements are established by state statute. The District's contributions to IPERS for the years ended December 31, 2011, 2010 and 2009 were $109,246, $105,941 and $181,859, respectively, equal to the required contributions for each year.

(4) Capital Assets

Capital assets activity for the years ended December 31, 2011 and 2010 was as follows:

	Year ended December 31, 2011				
	Balance Beginning of Year	Reclass-ifications	Increases	Decreases	Balance End of Year
Capital assets not being depreciated/amortized:					
Land	$ 3,010,535	-	132,555	(1,027,132)	2,115,958
Construction in progress	633,239	-	263,350	(888,158)	8,431
Total capital assets not being depreciated/amortized	3,643,774		395,905	(1,915,290)	2,124,389
Capital assets being depreciated/amortized:					
Office building and improvements	3,275,189	-	46,727	-	3,321,916
Office furniture and equipment	563,330	-	1,962	-	565,292
Plant building	618,339	-	-	-	618,339
Wells	62,982	-	104,182	-	167,164
Wastewater systems	1,988,334	-	-	(553,390)	1,434,944
Water lines	137,353,219	-	202,758	(1,929,103)	135,626,874
Intangibles, purchased capacity	4,728,209	-	-	-	4,728,209
Intangibles, software	239,528	-	7,595	-	247,123
Telemetry system	553,420	-	6,138	-	559,558
Equipment and tools	5,436,054	352,998	94,120	(3,382,909)	2,500,263
Transportation equipment	352,998	(352,998)	-	-	-
Total capital assets being depreciated/amortized	155,171,602	-	463,482	(5,865,402)	149,769,682
Less accumulated depreciation/amortization for:					
Office building and improvements	673,581	-	123,698	-	797,279
Office furniture and equipment	502,160	-	36,026	-	538,186
Plant building	430,410	-	15,537	-	445,947
Wells	44,094	-	1,574	-	45,668
Wastewater systems	137,975	-	61,349	(116,896)	82,428
Water lines	17,155,601	-	2,374,545	(375,653)	19,154,493
Intangibles, purchased capacity	1,550,262	-	121,059	-	1,671,321
Intangibles, software	212,741	-	20,142	-	232,883
Telemetry system	170,363	-	27,641	-	198,004
Equipment and tools	3,622,150	281,318	645,419	(2,549,875)	1,999,012
Transportation equipment	281,318	(281,318)	-	-	-
Total accumulated depreciation/amortization	24,780,655	-	3,426,990	(3,042,424)	25,165,221
Total capital assets being depreciated/amortized, net	130,390,947	-	(2,963,508)	(2,822,978)	124,604,461
Capital assets, net	$134,034,721	-	(2,567,603)	(4,738,268)	126,728,850

	Year ended December 31, 2010			
	Balance Beginning of Year	Increases	Decreases	Balance End of Year
Capital assets not being depreciated/amortized:				
Land	$ 3,661,158	-	(650,623)	3,010,535
Construction in progress	1,795,167	33,829	(1,195,757)	633,239
Total capital assets not being depreciated/amortized	5,456,325	33,829	(1,846,380)	3,643,774
Capital assets being depreciated/amortized:				
Office building and improvements	3,275,189	-	-	3,275,189
Office furniture and equipment	549,958	16,666	(3,294)	563,330
Plant building	618,339	-	-	618,339
Wells	62,982	-	-	62,982
Wastewater systems	2,980,028	4,206	(995,900)	1,988,334
Water lines	137,440,251	142,954	(229,986)	137,353,219
Intangibles, purchased capacity	4,728,209	-	-	4,728,209
Intangibles, software	419,891	1,615	(181,978)	239,528
Telemetry system	601,458	-	(48,038)	553,420
Equipment and tools	6,463,192	9,500	(1,036,638)	5,436,054
Transportation equipment	352,998	-	-	352,998
Total capital assets being depreciated/amortized	157,492,495	174,941	(2,495,834)	155,171,602
Less accumulated depreciation/amortization for:				
Office building and improvements	550,587	122,994	-	673,581
Office furniture and equipment	466,136	39,319	(3,295)	502,160
Plant building	413,741	16,669	-	430,410
Wells	42,519	1,575	-	44,094
Wastewater systems	154,113	127,714	(143,852)	137,975
Water lines	14,808,568	2,392,374	(45,341)	17,155,601
Intangibles, purchased capacity	1,429,203	121,059	-	1,550,262
Intangibles, software	204,783	77,863	(69,905)	212,741
Telemetry system	143,234	27,129	-	170,363
Equipment and tools	4,007,115	435,706	(820,671)	3,622,150
Transportation equipment	229,907	51,411	-	281,318
Total accumulated depreciation/amortization	22,449,906	3,413,813	(1,083,064)	24,780,655
Total capital assets being depreciated/amortized, net	135,042,589	(3,238,872)	(1,412,770)	130,390,947
Capital assets, net	$140,498,914	(3,205,043)	(3,259,150)	134,034,721

Depreciation/amortization charged to wastewater systems for 2011 and 2010 was $61,349 and $127,724, respectively. Depreciation/amortization charged to other operations for 2011 and 2010 was $3,365,641 and $3,272,858, respectively.

Depreciation/amortization capitalized as capital assets for 2011 and 2010 was $0 and $13,231, 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) Major Customers

Water sales revenue to three ethanol plants was $2,492,611 and $2,395,334 for the years ended December 31, 2011 and 2010, respectively. This represents 22% and 23% of total operating revenue for each year, respectively. The balance due from these customers and included in accounts receivable-trade was $203,894 and $184,771 at December 31, 2011 and 2010, respectively.

(7) Changes in Long Term Liabilities

A summary of changes in long-term liabilities for the years ended December 31, 2011 and 2010 is as follows:

	Year ended December 31, 2011				
	Balance Beginning of Year	Additions	Deletions	Balance End of Year	Due Within One Year
USDA Rural Development:					
Water revenue notes	$ 45,377,746	-	-	45,377,746	1,910,690
Wastewater revenue notes	257,507	-	(2,807)	254,700	2,866
Water revenue bonds, Series 2006	81,400,160	-	(1,263,600)	80,136,560	1,335,000
Assured Guaranty Corporation	1,329,936	1,110,644	-	2,440,580	2,440,580
Rural Community 2000 loan	20,000	-	-	20,000	20,000
Project anticipation notes	9,029,817	-	(7,561,649)	1,468,168	1,468,168
Asset purchase agreement	76,426	-	-	76,426	19,412
Net OPEB liability	4,000	4,000	-	8,000	-
Total	$ 137,495,592	1,114,644	(8,828,056)	129,782,180	7,196,716

	Year ended December 31, 2010				
	Balance Beginning of Year	Additions	Deletions	Balance End of Year	Due Within One Year
USDA Rural Development:					
Water revenue notes	$ 45,377,746	-	-	45,377,746	1,271,440
Wastewater revenue notes		260,000	(2,493)	257,507	2,756
Water revenue bonds, Series 2006	82,608,760	-	(1,208,600)	81,400,160	1,285,000
Assured Guaranty Corporation	-	1,329,936	-	1,329,936	1,329,936
Rural Community 2000 loan	20,000	-	-	20,000	20,000
Project anticipation notes	9,289,817	-	(260,000)	9,029,817	9,029,817
Asset purchase agreement	77,579	-	(1,153)	76,426	12,292
Net OPEB liability	-	4,000	-	4,000	-
Total	$ 137,373,902	1,593,936	(1,472,246)	137,495,592	12,951,241

USDA Rural Development Water Revenue Notes – The District has issued water revenue notes totaling $47,281,900 at December 31, 2011. The water revenue notes bear interest at rates ranging from 4.125% to 5.625% per annum. 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, 2011 and 2010, the debt service coverage ratios of the revenues to debt service were 51% and 52%, 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 to 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 principal and interest on the notes and has not deposited sufficient amounts to the sinking or improvement accounts as required. Additionally, the amount of surety bond insurance does not meet the minimum requirements of the note resolutions.

Details of the USDA Rural Development water revenue notes at December 31, 2011 and 2010 are as follows:

Loan Number	Issue Date	Interest Rates	Maturity Date	Monthly Payment	Amount Originally Issued	Note Balances December 31, 2011	2010
91-13	12/29/1993	5.250%	12/29/2033	$ 1,024	200,000	162,304	162,304
91-14	9/23/1994	5.625	9/23/2034	5,360	1,000,000	813,548	813,548
91-15	9/23/1994	5.375	9/23/2034	3,640	700,000	583,025	583,025
91-27	2/11/1999	4.500	2/1/2039	3,113	672,200	607,189	607,189
91-31	9/27/2001	4.750	9/27/2041	19,846	4,143,100	3,872,775	3,872,775
91-38	9/27/2001	4.750	9/27/2041	3,771	787,100	703,621	703,621
91-46	10/19/2001	4.750	9/27/2041	1,916	400,000	373,826	373,826
91-41	12/21/2001	4.750	9/27/2041	17,325	3,500,000	3,271,641	3,271,641
91-44	6/21/2002	4.750	6/21/2042	11,752	2,453,400	2,324,303	2,324,303
91-66	9/26/2003	4.250	1/1/2043	6,882	1,536,000	1,467,380	1,467,380
91-64	9/26/2003	4.250	1/1/2043	6,630	1,479,900	1,413,817	1,413,817
91-62	9/26/2003	4.250	1/1/2043	9,008	2,010,700	1,920,915	1,920,915
91-52	6/25/2004	4.375	1/1/2044	15,960	3,500,000	3,391,331	3,391,331
91-58	6/25/2004	4.250	1/1/2044	2,565	572,500	554,281	554,281
91-56	6/25/2004	4.375	1/1/2044	2,204	4,845,000	4,694,543	4,694,543
25-61	9/26/2005	4.125	9/26/2044	6,675	1,517,000	1,486,687	1,486,687
25-73	9/26/2005	4.125	9/26/2044	15,278	3,500,000	3,430,072	3,430,072
40-01	9/26/2005	4.125	9/26/2045	7,700	1,750,000	1,710,894	1,710,894
25-70	9/26/2005	4.125	9/26/2045	15,400	3,500,000	3,430,072	3,430,072
25-71	9/26/2005	4.125	9/26/2045	8,800	2,000,000	1,960,041	1,960,041
40-03	2/1/2006	4.125	2/1/2046	5,346	1,215,000	1,205,481	1,205,481
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	4,000,000
Total				$ 196,946	47,281,900	45,377,746	45,377,746

<u>USDA Rural Development Wastewater Revenue Note</u> – On January 8, 2010, the District issued a $260,000 wastewater revenue 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.

The District has pledged future wastewater customer receipts, net of specified operating disbursements, to repay the wastewater revenue note. The note is payable solely from wastewater customer net receipts and is payable through 2050. At December 31, 2011 and 2010, the debt service coverage ratios of the revenues to debt service were 173% and 230%, respectively.

The resolution providing for the issuance of the wastewater revenue note includes the following provisions:

(a) The note 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 wastewater revenue note sinking account for the purpose of making the note principal and interest payments when due.

(c) A wastewater reserve account shall be established. Monthly payments of $109 shall be deposited in the wastewater reserve account. 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 note 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 note resolution.

Details of the USDA Rural Development wastewater revenue note at December 31, 2011 and 2010 are as follows:

Loan Number	Issue Date	Interest Rate	Maturity Date	Monthly Payment	Amount Originally Issued	Note Balances December 31, 2011	2010
92-06	1/8/2010	4.00%	12/1/2049	$ 1,088	260,000	254,700	257,507

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 $80,775,000. At December 31, 2011 and 2010, the debt service coverage ratios of the revenues (excluding connection fees) to debt service were 51% and 52%, 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 principal and interest on the bonds and has not deposited sufficient amounts to the sinking and improvement accounts as required.

Assured Guaranty Corporation – In July 2011, CIFG Assurance North America, Inc. (CIFG NA), the bond insurer, and Assured Guaranty Corporation, the reinsurance company, reached a settlement where the water revenue bonds, series 2006 guarantee, including principal and interest payments of $1,329,936 made by CIFG NA in c010, has been assumed by Assured Guaranty Corporation under the Quota Share Reinsurance Agreement dated January 21, 2009. During 2011, Assured Guaranty Corporation paid the District's deficiency of $1,110,644 of principal payments on the water revenue bonds, series 2006. Total principal and interest of $2,440,580 paid by the reinsurance company continues to accrue interest at the stated rate of the bond. Accrued interest payable to Assured Guaranty Corporation was $49,250 and $3,741 at December 31, 2011 and 2010, respectively. The outstanding balances at December 31, 2011 and 2010, including accrued interest, were $2,489,830 and $1,333,677, respectively.

Rural Community 2000 Loan – The District obtained a $200,000 loan in 1993 from the Iowa Department of Economic Development (now the Iowa Economic Development Authority) under the Rural Community 2000 program. The loan is interest free and required annual principal payments of $20,000 through 2009. The District was in default for non-payment of the outstanding loan balance at December 31, 2011 and 2010. The outstanding balances at December 31, 2011 and 2010 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. The District has drawn $1,468,168. 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 and then to October 16, 2011. The District is working with the Iowa Finance Authority to extend the maturity date to October 1, 2025. The District made no principal or interest payments during 2011 or 2010. Iowa Finance Authority project anticipation notes outstanding at December 31, 2011 and 2010 are as follows:

				Note Balances	
	Interest	Maturity		December 31,	
Project	Rate	Date	Limit	2011	2010
Beaver Creek Treatment Plant	0.00%	10/16/2011	$ 917,000	917,000	917,000
North Service Area 3 Phase IIB	0.00	10/16/2011	175,000	175,000	175,000
Service Area 3, Phase II	0.00	10/16/2011	250,000	18,168	18,168
Winn/Worth	0.00	10/16/2011	358,000	358,000	358,000
Total			$ 1,700,000	1,468,168	1,468,168

In a prior year, 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 and wastewater revenue notes with the remainder of the project anticipation notes 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. Payments of $260,000 of principal and $592 of interest were made during the year ended December 31, 2010. During 2011, the District entered into a settlement agreement with Bank of America. The District paid Bank of America $1,550,000 to satisfy $7,561,649 of principal and $651,297 of interest on project anticipation notes and $6,755 of attorney fees. Project anticipation notes outstanding for Bank of America and F & M Bank at December 31, 2011 and 2010 are as follows:

	Interest			December 31,	
Lender	Rates	Maturity Date	Limit	2011	2010
F & M Bank	3.90%	1/1/2010	$ 260,000	-	-
Bank of America	3.70	6/1/2010	5,000,000	-	5,000,000
Bank of America	3.16	11/15/2010	5,000,000	-	2,561,649
Total				$ -	7,561,649

Asset Purchase Agreement – The District entered into an asset purchase agreement with Coats Utilities Company on November 5, 2007. As part of the 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. No principal and interest were paid during the year ended December 31, 2011. The balances outstanding at December 31, 2011 and 2010 were $76,426 and $76,426, respectively. The District was in default for insufficient payments of the outstanding loan balance at December 31, 2011.

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

	USDA Rural Development								
Year Ending	Water Revenue Notes			Wastewater Revenue Notes			Water Revenue Bonds, Series 2006		
December 31,	Principal	Interest	Total	Principal	Interest	Total	Principal	Interest	Total
2012	$ 1,910,690	2,945,370	4,856,060 #	2,866	10,190	13,056	1,335,000	3,662,888	4,997,888
2013	685,662	1,914,175	2,599,837	2,981	10,075	13,056	1,385,000	3,609,488	4,994,488
2014	716,145	1,883,739	2,599,884	3,100	9,956	13,056	1,440,000	3,554,088	4,994,088
2015	747,995	1,851,936	2,599,931	3,224	9,832	13,056	1,500,000	3,496,488	4,996,488
2016	781,268	1,818,713	2,599,981	3,353	9,703	13,056	1,560,000	3,436,488	4,996,488
2017-2021	4,460,029	8,540,704	13,000,733	18,885	46,395	65,280	8,880,000	14,481,417	23,361,417
2022-2026	5,546,338	7,456,011	13,002,349	22,978	42,302	65,280	11,045,000	13,931,219	24,976,219
2027-2031	6,899,365	6,104,988	13,004,353	27,956	37,324	65,280	13,735,000	9,243,955	22,978,955
2032-2036	8,066,420	4,463,846	12,530,266	34,013	31,267	65,280	17,425,000	7,812,269	25,237,269
2037-2041	9,450,876	2,562,487	12,013,363	41,382	23,898	65,280	22,470,000	3,268,625	25,738,625
2042-2046	5,471,718	706,710	6,178,428	50,347	14,933	65,280	-	-	-
2047-2051	641,240	59,399	700,639	43,615	4,199	47,814	-	-	-
Total	$ 45,377,746	40,308,078	85,685,824	254,700	250,074	504,774 *	80,775,000	66,496,924	147,271,924

Year Ending	Rural Community 2000 Loan			Project Anticipation Notes			Asset Purchase Agreement		
December 31,	Principal	Interest	Total	Principal	Interest	Total	Principal	Interest	Total
2012	$ 20,000	-	20,000	1,468,168	-	1,468,168	19,412	9,688 &	29,100
2013	-	-	-	-	-	-	7,483	2,681	10,164
2014	-	-	-	-	-	-	7,866	2,298	10,164
2015	-	-	-	-	-	-	8,269	1,895	10,164
2016	-	-	-	-	-	-	8,691	1,472	10,163
2017-2021	-	-	-	-	-	-	22,259	3,222	25,481
2022-2026	-	-	-	-	-	-	2,446	36	2,482
2027-2031	-	-	-	-	-	-	-	-	-
2032-2036	-	-	-	-	-	-	-	-	-
2037-2041	-	-	-	-	-	-	-	-	-
2042-2046	-	-	-	-	-	-	-	-	-
2047-2051	-	-	-	-	-	-	-	-	-
Total	$ 20,000	-	20,000	1,468,168	-	1,468,168	76,426	21,292	97,718

Year Ending	Total		
December 31,	Principal	Interest	Total
2012	$ 4,756,136	6,628,136	11,384,272
2013	2,081,126	5,536,419	7,617,545
2014	2,167,111	5,450,081	7,617,192
2015	2,259,488	5,360,151	7,619,639
2016	2,353,312	5,266,376	7,619,688
2017-2021	13,381,173	23,071,738	36,452,911
2022-2026	16,616,762	21,429,568	38,046,330
2027-2031	20,662,321	15,386,267	36,048,588
2032-2036	25,525,433	12,307,382	37,832,815
2037-2041	31,962,258	5,855,010	37,817,268
2042-2046	5,522,065	721,643	6,243,708
2047-2051	684,855	63,598	748,453
Total	$ 127,972,040	107,076,368	235,048,408

* - The unamortized discount at December 31, 2011 and 2010 totaled $638,440 and $659,840, respectively.

\# - Includes unpaid water revenue note principal of $1,271,399 and interest of $1,002,787 at December 31, 2011.

& - Includes unpaid principal of $12,293 and interest of $6,343 at December 31, 2011.

(8) 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 $4,336 and $14,146 for the years ended December 31, 2011 and 2010, respectively. The District passed a resolution in August 2011 to terminate its lease with Pitney Bowes Global Financial Services due to the District's financial situation.

The District leased 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 lease was to expire in 2017. The lease with the employee was terminated as of December 31, 2011. The District is attempting to sign a new lease. A schedule of future annual lease payments for the Conservation Reserve Program is not prepared as the District does not qualify to receive the payment and does not have a qualifying tenant as of December 31, 2011. The District's investment in property subject to the operating lease was $568,986 at December 31, 2011 and 2010.

The District leased land to farm tenants during 2011 and 2010 with rent payments totaling $8,750 and $20,900, respectively. The lease terms were from April through November, 2011 and 2010, respectively, at which time the leases automatically terminated.

(9) Related Party Transactions

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 $15,100 and $15,663 for 2011 and 2010, respectively. Rental income receivable was $0 and $15,663 at December 31, 2011 and 2010, respectively. The lease with the employee was terminated, effective December 31, 2011.

(10) Discretely Presented 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. The Corporation had no activity during 2011 and the Corporation filed for administrative dissolution in August 2011.

(11) 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, 2011 and 2010 was $47,089 and $44,698, respectively. This liability has been computed based on rates of pay in effect at December 31, 2011 and December 31, 2010, respectively.

(12) Subsequent Events

On January 26, 2012, the District's Board of Directors approved an updated version of the debt work-out plan. The updated document addresses a request by the USDA and Assured Guaranty to provide a written debt work-out plan that is acceptable to all parties. To date, the District and its creditors have been unable to formally agree to a final debt work-out plan. A summary description of the debt work-out proposal is described in Note 13 of the Notes to Financial Statements.

On July 11, 2012 Assured Guaranty Corporation filed a lawsuit against the District seeking the appointment of a receiver or, in the alternative, a writ of mandamus to enforce and compel the District to raise rates and take other specified actions.

(13) Going Concern

The District has been delinquent on monthly USDA Rural Development water revenue note principal and interest payments since October 1, 2009, except for partial payment of interest totaling $2,351,139 during 2011. The USDA notified the District in late 2009 it must enter into a formal debt workout agreement to resolve its payment deficiencies. If an agreement cannot be reached, or the agreement is unable to correct the deficiency, other servicing actions, such as debt re-amortization 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 water revenue bonds, series 2006 during the year. Without sufficient net water revenues, the District cannot pay principal and interest coming due on the bonds from the sinking account. Related debt reserve accounts are depleted and the bond insurer paid claims for the District's deficiency applicable to principal due on the bonds as described in Note 7 of the Notes to Financial Statements.

Assured Guaranty Corporation (Assured), 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 engaged by the outside counsel representing Assured. The consultant's report, issued in early 2010, concluded the District would still not meet its financial obligations in 2010 and thereafter with the recommended water rate structure. Assured previously reserved rights under the series 2006 bond resolution, approved by the District's Board of Directors, to obtain a writ of mandamus, as well as petition a court to appoint a receiver, should timely resolution of the District's debt default not occur.

On January 26, 2012, the Board of Directors approved a debt work-out proposal to replace the previous debt work-out proposal which was approved on March 31, 2011. The plan's key elements include: 1) following the amortization schedule for the series 2006 bonds in 2012, 2) repayment of past series 2006 bond shortfall payments to Assured, 3) repayment of USDA loans over 40 years at 2.25% stated interest rate, 4) discontinue use of the Woodward treatment plant during 2012 and replace the Woodward source water with water from the Des Moines Water Works, Warren Rural Water District and from the District's plant in Stratford, Iowa, 5) a rate increase of 4.5% effective January 1, 2012 and 6) sale of at least one parcel of land owned by the District that is considered excess.

(14) Other Postemployment Benefits (OPEB)

Plan Description. The District operates a single-employer health benefit plan which provides medical/prescription drug benefits for retirees and their spouses. There are 30 active and no retired members in the plan. Retired participants must be age 55 or older at retirement.

The medical/prescription drug and dental benefits are provided through a medical and dental plan administered by Wellmark and Principal Financial Group, respectively. Retirees under age 65 would pay the same premium for the medical/prescription drug and dental benefits as active employees, which results in an implicit rate subsidy and an OPEB liability.

Funding Policy. The contribution requirements of plan members are established and may be amended by the District. The District currently finances the benefit plan on a pay-as-you-go basis.

Annual OPEB Cost and Net OPEB Obligation. The District's annual OPEB cost is calculated based on the annual required contribution (ARC) of the District, an amount determined using the alternate measurement method permitted by GASB Statement No. 45. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and amortize any unfunded actuarial liabilities over a period not to exceed 30 years.

The following table shows the components of the District's annual OPEB cost for the year ended December 31, 2011, the amount actually contributed to the plan and changes in the District's net OPEB obligation:

Annual required contribution	$ 4,000
Interest on net OPEB ogligation	-
Contribution made	-
Increase in net OPEB obligation	4,000
Net OPEB obligation beginning of year	4,000
Net OPEB obligation end of year	$ 8,000

For the year ended December 31, 2011, the District contributed $0 to the plan and there were no contributions from plan members eligible for benefits.

The District's annual OPEB cost, the percentage of annual OPEB cost contributed to the plan and the net OPEB obligation as of December 31, 2011 are summarized as follows:

Year Ended December 31,	Annual OPEB Cost	Percentage of Annual OPEB Cost Contributed	Net OPEB Obligation
2010	$ 4,000	0%	$ 4,000
2011	4,000	0	8,000

Funded Status and Funding Progress. As of December 31, 2011, the actuarial accrued liability was $14,884, with no actuarial value of assets, resulting in an unfunded actuarial accrued liability (UAAL) of $14,884. The covered payroll (annual payroll of active employees covered by the plan) was approximately $1,494,000 and the ratio of the UAAL to covered payroll was 1.0%. As of December 31, 2011, there were no trust fund assets.

The projection of future benefit payments for an ongoing plan involves estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality and the health care cost trend. Amounts determined regarding the funded status of the plan and the annual required contributions of the employer are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future. The Schedule of Funding Progress for the Retiree Health Plan, presented as Required Supplementary Information in the section following the Notes to Financial Statements, presents multiyear trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liabilities for benefits.

Methods and Assumptions. Projections of benefits for financial reporting purposes are based on the plan as understood by the employer and the plan members and include the types of benefits provided at the time of each valuation and the historical pattern of sharing of benefit costs between the employer and plan members to that point. The methods and assumptions used include techniques designed to reduce the effects of short-term volatility in actuarial accrued liabilities and the actuarial value of assets, consistent with the long-term perspective of the calculations.

As of the January 1, 2010 valuation date, a simplified version of the unit credit actuarial cost method was used. The assumptions include a 4.5% discount rate based on the District's funding policy. The projected annual medical trend rate is 10%. The ultimate medical trend rate is 5%. The medical trend rate is reduced 1% each year until reaching the 5% ultimate trend rate.

Mortality rates are from the 2004 United States Live Tables. Annual retirement and termination probabilities were developed from the assumption active plan members were assumed to retire at age 62, or the first subsequent year in which the member would qualify for normal benefits under IPERS.

Projected claim costs of the medical plan are range from $352 to $1,079 per month for retirees less than age 65. The UAAL is being amortized as a level percentage of projected payroll expense on an open basis over 30 years.

(15) Impairment Loss

Management of the District computed an impairment loss for water system assets in accordance with GASB Statement No. 42, Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries.

The District has incurred costs of $391,532 for construction of a water treatment plant in Dallas County. The District has stopped construction on those assets and an impairment loss of $391,532 has been recorded for the year ended December 31, 2011.

The impairment loss on assets has been recorded as a non-operating loss in the Statement of Revenues, Expenses and Changes in Net Assets. A corresponding reduction in capital assets has been recorded at December 31, 2011.

Other Information

Xenia Rural Water District

Schedule of Funding Progress for the
Retiree Health Plan
(In Thousands)

Year Ended December 31,	Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) (b)	Unfunded AAL (UAAL) (b-a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ((b-a)/c)
2010	January 1, 2010	-	$ 15	15	0.00%	$ 1,428	1.05%
2011	January 1, 2010	-	15	15	0.00	1,494	1.00

See Note 14 in the accompanying Notes to Financial Statements for the plan description, funding policy, annual OPEB cost, net OPEB obligation, funded status and funding progress.

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David A. Vaudt, CPA
Auditor of State

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 years ended December 31, 2011 and 2010, and have issued our report thereon dated August 14, 2012. 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

Management of the Xenia Rural Water District is responsible for establishing and maintaining effective 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 an opinion on the financial statements, but not for the purpose of expressing an 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 was not designed to identify all deficiencies in and internal control over financial reporting that might be significant deficiencies or material weaknesses and, therefore, there can be no assurance all deficiencies, significant deficiencies or material weaknesses have been identified. However, as described in the accompanying Schedule of Findings, we identified deficiencies in internal control over financial reporting we consider to be material weaknesses and other deficiencies we consider to be significant deficiencies.

A deficiency in internal control 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 and correct misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility a material misstatement of the Xenia Rural Water District's financial statements will not be prevented or detected and corrected on a timely basis. We consider the deficiencies described in the accompanying Schedule of Findings as items (A) and (B) to be material weaknesses.

A significant deficiency is a deficiency, or a combination of deficiencies, in internal control which is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider the deficiencies described in the accompanying Schedule of Findings as items (C) through (H) to be significant deficiencies.

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 instances of non-compliance required to be reported under Government Auditing Standards which are described in item (1) in the accompanying Schedule of Findings. We also noted certain immaterial instances of non-compliance or other matters which are described in the accompanying Schedule of Findings.

Comments involving statutory and other legal matters about the District's operations for the year ended December 31, 2011 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. 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 and 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

August 14, 2012

Findings Related to the Financial Statements:

INTERNAL CONTROL DEFICIENCIES:

(A) Adjusting Journal Entries – Standard and nonstandard journal entries are entered into the accounting system during the year by District personnel and the Controller. The Controller reviews standard and nonstandard journal entries entered by the accounting staff. The independent review of journal entries entered by the Controller does not specify which entries were reviewed.

Recommendation – The District should develop procedures to ensure all standard and nonstandard journal entries are reviewed and approved by an independent person. The independent review should be evidenced by the reviewer's initials or signature, documentation of specific entries reviewed and the date of the review.

Response – The District will develop and implement documented review procedures for the approval of adjusting journal entries.

Conclusion – Response accepted.

(B) Segregation of Duties - One important aspect of the internal control structure is the segregation of duties among employees to prevent an individual employee from handling duties which are incompatible. The initial receipt collection is done by an employee who has the ability to post collections and make adjustments to customer accounts.

Additionally, the employee responsible for reconciling is able to post adjustments to the customer accounts receivable ledger and has access to original customer checks electronically deposited with the bank.

Recommendation – The District should review its operating procedures to obtain the maximum internal control possible under the circumstances, including utilizing members of the Board of Directors.

Response – The District will review its internal control policies and implement measures to maximize internal control effectiveness.

Conclusion – Response accepted.

(C) Timesheets – Certain salaried and contract employees do not submit timesheets for review and approval.

Recommendation – Timesheets should be prepared by all employees and submitted for approval. The timesheets should be signed by the employee and reviewed and signed by the employee's immediate supervisor. The timesheet should support all hours worked and leave taken.

Response – The District believes it has sufficient controls in place for salaried and contract employees. The salaried employees are all at the management level and are generally on site. Email communication and calendar, accessible by staff, are used to confirm when managers are not available during work hours. Leave for sick and vacation time are currently documented for all employees. Contract employees are generally subordinate positions and their hours are kept with daily timesheets.

Conclusion – Response acknowledged. Timesheets should be prepared and signed by all employees and reviewed and signed by the employee's immediate supervisor.

(D) Payroll and Tax Reports – The District did not file the employer's quarterly federal tax return, Iowa quarterly employer's contribution and payroll reports for workers compensation and Iowa sales tax reports in a timely manner.

Recommendation – The District should ensure required reports are filed timely.

Response – The District has assigned responsibilities for filing reports, making payments and confirming payments to help ensure they are done on a timely basis.

Conclusion – Response accepted.

(E) Cost Benefit Analysis – The District requires the completion of a cost benefit analysis for all projects with an anticipated cost exceeding $5,000. The cost benefit analysis is to be reviewed by the Finance Committee. The District did not complete required cost benefit analyses during the year.

Recommendation - The District should complete required cost benefit analyses as required or seek to have the provisions changed or repealed. At a minimum, further clarification of the definition of "project" and the required elements of a cost benefit analysis should be completed.

Response – The District's Board will address this issue, refine the language and adjust the financial threshold required for a cost benefit analysis to be performed.

Conclusion – Response accepted.

(F) Payroll – Annual gross salaries were not approved or documented in the District's Board minutes.

Recommendation – Annual gross salaries for all employees should be approved by the District's Board and documented in the minutes record.

Response – The District's Board approves the annual gross salaries as part of the annual budget and will continue to do so. The Board approves the General Manager's salary, while all other salaries are approved by the General Manager.

Conclusion – Response acknowledged. The individual salaries of all employees should be approved by the District's Board and documented in the minutes record.

(G) Capital Assets – The District changed from the units of production to the straight line method for calculating depreciation on construction equipment. However, the District's policy requires construction equipment purchased after December 31, 2006 be depreciated using current year units of production over the estimated total units of production.

The District's capital asset policy does not adequately address procedures to add assets to the capital asset record. Several assets with inadequate descriptions to identify the specific asset were identified and certain assets were made up of several items with different descriptions and useful lives. Additionally, several assets below the capitalization threshold of $1,000 were added to the capital asset record.

Recommendation – The District should revise the written capital asset policy to include procedures for recording assets in the capital asset record, assigning descriptions and useful lives and appropriate depreciation methods.

Response – The District will amend the capital asset policy and document and follow agreed upon depreciation methods.

Conclusion – Response accepted.

(H) Financial Transaction Policy – The District's Board has delegated significant financial authority to the Board Chair, Board Treasurer, District General Manager and Human Resources and Administration Manager. Authority includes making any purchase less than $75,000 as long as two signatures are obtained. Also, authority of the Board Chair includes unlimited borrowing on behalf of the District.

The District purchased three pickup trucks at a cost of approximately $73,000. However there was no evidence of the required cost benefit analysis being completed prior to the purchase. District management decided to utilize one truck and place the other two in storage.

Recommendation – The District should review its financial transaction policy to ensure proper Board involvement, including ensuring the required cost benefit analysis is performed and approved prior to significant purchases. Also, the Board may wish to reconsider the authority granted the Board Chair for unlimited borrowing on behalf of the District.

Response – The District's Board will review the financial transaction policy and make amendments where it is deemed necessary.

Conclusion – Response accepted.

INSTANCES OF NON-COMPLIANCE:

(1) Long Term Notes, Bonds and Loans – Instances of non-compliance with the water revenue note and bond resolutions were noted, as follows:

The District is in default on approximately $45 million of USDA water revenue notes at December 31, 2011. The District also requested Assured Guaranty Corporation, the bond reinsurer for the water revenue bonds, series 2006 to make partial required debt payments. This appears to violate provisions of the water revenue note and bond 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 and bonds.

The District did not meet the minimum balance requirements or make adequate transfers to the water reserve, sinking and improvement accounts.

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

The District did not complete and submit the Tax Arbitrage Return within 30 days of December 31, 2010 and remit 90% of the calculated obligation, if any, to the U.S. Treasury within 60 days after December 31, 2010.

Also, the District is in default on other outstanding loans and notes, including those held by Coats Utilities Company and the Iowa Economic Development Authority.

Recommendation – The District should review the note and bond provisions and comply with the requirements. Also, 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 is working with USDA and Assured Guaranty to reach a debt workout agreement that complies with provisions and provides rates that are sufficient to meet operating and debt repayment obligations. The District is negotiating with USDA and Assured Guaranty on a timeframe to replenish funds that allows the District to meet operating and debt repayment obligations. The District maintains a surety bond to the extent available in the market. The District is working on finalizing the calculation for the arbitrage rebate.

Conclusion – Response acknowledged.

Xenia Rural Water District

Schedule of Findings

Year ended December 31, 2011

Other Findings Related to Required Statutory Reporting:

(1) 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. These disbursements are detailed as follows:

Paid to	Purpose	Amount
Wells Fargo Corporate Card	Late charges	$ 156
Iowa Department of Revenue	Penalty and interest	2,081
Internal Revenue Service	Penalty	386
Iowa Workforce Development	Penalty and interest	1,725

According to the opinion, it is possible for such disbursements to meet the test of serving a public purpose under certain circumstances, although such items will certainly be subject to a deserved close scrutiny. The line to be drawn between a proper and an improper purpose is very thin.

Recommendation – The District should ensure all disbursements are paid timely and all reports are filed timely to avoid late charges, penalties and interest.

Response – The District has assigned responsibilities for filing reports, making payments and confirming payments to help ensure they are made on a timely basis.

Conclusion - Response accepted.

(2) Travel Expense – No expenditures of District money for travel expenses of spouses of District officials or employees were noted.

(3) Board Minutes – No transactions were found that we believe should have been approved in the Board minutes but were not, except as follows:

The Board of Directors went into closed session numerous times during the year ended December 31, 2011. However, the minutes did not reference a specific code exemption as required by Chapter 21.5 of the Code of Iowa.

Recommendation - Closed sessions should be held in compliance with Chapter 21.5 of the Code of Iowa and reference a specific code exemption as required.

Response – The District's Board will reference specific code exemptions authorizing closed sessions in the future.

Conclusion – Response accepted.

(4) Deposits and Investments – Deposits and investments were in compliance with Chapter 12B and Chapter 12C of the Code of Iowa and the District's investment policy.

(5) Wastewater Revenue Notes and Water Revenue Bonds – Instances of non-compliance with the wastewater revenue note and water revenue bond resolutions were noted, as follows:

While the District maintains surety bond coverage for employee theft, the amount of coverage 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 District has been denied the coverage level required under the bond resolution requirements. A policy is maintained to the extent that the markets will insure the District.

Conclusion – Response acknowledged.

(6) Electronic Check Retention – Chapter 554D.114 of the Code of Iowa allows the District to retain cancelled checks in an electronic format and requires retention in this manner to include an image of both the front and back of each cancelled check. The District retains electronic images of the front of cancelled checks, but not the back of cancelled checks.

Recommendation – The District should retain an image of both the front and back of each cancelled check as required.

Response – The District has requested copies of both front and back of each cancelled check.

Conclusion – Response accepted.

(7) Other Information Required by the Bond Resolution

Insurance – The following insurance policies were in force at December 31, 2011:

Insurer	Description	Amount	Expiration Date
EMC Insurance Companies	Property:		
	Blanket: Buildings and personal property	$ 35,563,661	5/1/12
	Extra expense	75,000	5/1/12
	Contractors equipment	730,386	5/1/12
	Leased contractors equipment	300,000	5/1/12
	Miscellaneous property - Radios and GPS	78,850	5/1/12
	Data processing - equipment and software	132,500	5/1/12
	Off-site tools and equipment:		
	Per installation site	300,000	5/1/12
	Property temporarily off premises	20,000	5/1/12
	Property in transit	40,000	5/1/12
EMC Insurance Companies	General liability coverage:		
	General aggregate	2,000,000	5/1/12
	Products general liability	2,000,000	5/1/12
	Personal and/or advertising	1,000,000	5/1/12
	Each occurrence	1,000,000	5/1/12
	Fire damage	100,000	5/1/12
	Medical expense	5,000	5/1/12
EMC Insurance Companies	Automobile coverage:		
	Liability	1,000,000	5/1/12
	Medical payments	1,000	5/1/12
	Uninsured motorists	100,000	5/1/12
	Underinsured motorists	100,000	5/1/12
Liberty Mutual Workers Comp Group	Workers' compensation:		
	Employee liability limit	1,000,000	5/1/12
EMC Insurance Companies	Commercial umbrella:		
	Policy aggregate	5,000,000	5/1/12
EMC Insurance Companies	Public officials errors and omissions:		
	Each loss	1,000,000	5/1/12
	Aggregate	1,000,000	5/1/12
EMC Insurance Companies	Fidelity coverage:		
	Per loss - Employee dishonesty	1,000,000	5/1/12
	Per loss deductible	10,000	5/1/12
EMC Insurance Companies	Employee benefit liability:		
	Each loss from administrative errors	1,000,000	5/1/12
	Aggregate	2,000,000	5/1/12

Xenia Rural Water District

Schedule of Findings

Year ended December 31, 2011

Water Rates – The following water rates were in effect at December 31, 2011:

	Gallons	Rate
RESIDENTIAL/COMMERCIAL		
Rural 5/8" meter (non-franchise users):		
Minimum	0-1,000	$50.40
Steps	per 1,000 after minimum	$10.00 to $4.20
Franchise 5/8" meter:		
Minimum	0-1,000	$20.10 to $44.30
Steps	per 1,000 after minimum	$10.00 to $4.20
City of Boone contracted rate:		
Minimum	0-1,000	$10.30
Steps	per 1,000 after minimum	$10.00 to $4.20
3/4" meter:		
Minimum	0-1,000	$100.80
Steps	per 1,000 after minimum	$10.00 to $4.20
1" meter:		
Minimum	0-1,000	$76.50 to $151.20
Steps	per 1,000 after minimum	$10.00 to $4.20
1 1/2" meter:		
Minimum	0-1,000	$178.00 to $252.00
Steps	per 1,000 after minimum	$4.20
2" meter:		
Minimum	0-1,000	$175.20 to $403.20
Steps	per 1,000 after minimum	$4.20 to $4.90
6" meter:		
Minimum	0-16,000	$403.20
Steps	per 1,000 after minimum	$4.20
INDUSTRIAL	fixed cost	$14,631.00 to $67,228.00
	per 1,000 after minimum	$3.24 to $1.67
WHOLESALE	no minimum/per 1,000 charge	$6.25 to $1.80

Statistical Information

Water Customers served at December 31, 2011:

Description	Number
Residential	9,178
Commercial	261
Industrial	4
Wholesale	4
Total	9,447

Xenia Rural Water District

Staff

This audit was performed by:

Ernest H. Ruben, Jr., CPA, Manager
Brett M. Zeller, Senior Auditor
Philip A. Rethwisch, Assistant Auditor
Ryan A. Yeager, CPA, Assistant Auditor

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Deputy Auditor of State