

12005

**BDW WATER SYSTEM ASSOCIATION
CROSBY, NORTH DAKOTA**

AUDITED FINANCIAL STATEMENTS

FOR THE YEARS ENDED DECEMBER 31, 2013 AND 2012

TABLE OF CONTENTS

	Page
INDEPENDENT AUDITOR'S REPORT	1
FINANCIAL STATEMENTS	
Statements of Net Position - Modified Cash Basis	3
Statements of Revenues, Expenses and Changes in Net Position - Modified Cash Basis	4
Statements of Cash Flows - Modified Cash Basis	5
Notes to the Financial Statements	6
SUPPLEMENTARY INFORMATION	
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	14
Schedule of Findings and Responses	16



CERTIFIED PUBLIC ACCOUNTANTS
AND CONSULTANTS

INDEPENDENT AUDITOR'S REPORT

To the Board of Directors
BDW Water System Association
Crosby, North Dakota

Report on the Financial Statements

We have audited the accompanying modified cash basis financial statements of the business-type activities of BDW Water System Association as of and for the years ended December 31, 2013 and 2012, and the related notes to the financial statements, which collectively comprise BDW Water System Association's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with the modified cash basis of accounting described in Note 1; this includes determining that the modified cash basis of accounting is an acceptable basis for the preparation of the financial statements in the circumstances. Management is also responsible for the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

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

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

BRADY, MARTZ & ASSOCIATES, P.C.
24 West Central P.O. Box 848
Minot, ND 58702-0848 (701) 852-0196 Fax (701) 839-5452
www.bradymartz.com

McGLADREY ALLIANCE



Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the modified cash basis financial position of the business-type activities of BDW Water System Association as of December 31, 2013 and 2012, and their changes in modified cash basis financial position and their cash flows thereof for the years then ended in conformity with the modified cash basis of accounting described in Note 1.

Basis of Accounting

We draw attention to Note 1 of the financial statements which describes the basis of accounting. The financial statements are prepared on the modified cash basis of accounting, which is a basis of accounting other than government accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

Other Reporting Required by Government Auditing Standards

In accordance with *Governmental Auditing Standards*, we have also issued our report dated December 22, 2014 on our consideration of BDW Water System Association's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing and not to provide an opinion on 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* in considering BDW Water System Association's internal control over financial reporting and compliance.

Brady, Martz

BRADY, MARTZ & ASSOCIATES, P. C.
Minot, North Dakota

December 22, 2014

BDW WATER SYSTEM ASSOCIATION
STATEMENTS OF NET POSITION – MODIFIED CASH BASIS
DECEMBER 31, 2013 AND 2012

ASSETS		2013	2012
Current assets			
Cash and cash equivalents		\$ 12,848	\$ 624
Cash held in escrow		220,643	-
Capital assets			
Construction in process		-	3,682,978
Capital assets, net of accumulated depreciation		<u>3,773,215</u>	<u>-</u>
Total assets		<u>4,006,706</u>	<u>3,683,602</u>
DEFERRED INFLOWS OF RESOURCES			
Grant proceeds held in escrow		<u>220,643</u>	<u>-</u>
NET POSITION			
Net position			
Net investment in capital assets		3,773,215	3,682,978
Unrestricted		<u>12,848</u>	<u>624</u>
Total net position		<u>\$ 3,786,063</u>	<u>\$ 3,683,602</u>

SEE NOTES TO THE FINANCIAL STATEMENTS

BDW WATER SYSTEM ASSOCIATION
STATEMENTS OF REVENUES, EXPENSES
AND CHANGES IN NET POSITION – MODIFIED CASH BASIS
FOR THE YEARS ENDED DECEMBER 31, 2013 AND 2012

	<u>2013</u>	<u>2012</u>
Operating revenue		
Water sales	\$ 157,389	\$ -
Total operating revenue	<u>157,389</u>	<u>-</u>
Operating expenses		
Cost of water sold	186,706	-
Administration expenses	13,401	18,596
Other operating expenses	11,698	6,785
Depreciation expense	31,708	-
Total operating expenses	<u>243,513</u>	<u>25,381</u>
Operating loss	<u>(86,124)</u>	<u>(25,381)</u>
Non-operating revenue		
Interest	<u>23</u>	<u>8</u>
Capital contributions and grants		
DWSRF funding	95,402	231,961
State grants and funding	93,160	49,995
Total capital contributions and grants	<u>188,562</u>	<u>281,956</u>
Change in net position	102,461	256,583
Net position - January 1	<u>3,683,602</u>	<u>3,427,019</u>
Net position - December 31	<u>\$ 3,786,063</u>	<u>\$ 3,683,602</u>

SEE NOTES TO THE FINANCIAL STATEMENTS

BDW WATER SYSTEM ASSOCIATION
STATEMENTS OF CASH FLOWS – MODIFIED CASH BASIS
FOR THE YEARS ENDED DECEMBER 31, 2013 AND 2012

	2013	2012
Cash flows from operating activities		
Receipts from customers	\$ 157,389	\$ -
Payments to suppliers	(211,805)	(25,381)
Net cash used by operating activities	<u>(54,416)</u>	<u>(25,381)</u>
Cash flows from capital and related financing activities		
Capital contribution and grant proceeds	93,160	49,995
Grant proceeds held in escrow	220,643	-
Purchase of property and equipment	(121,945)	(263,147)
Proceeds from long-term borrowings	95,402	231,961
Net cash provided by capital and related financing activities	<u>287,260</u>	<u>18,809</u>
Cash flows from investing activities		
Interest income	23	8
Net cash provided by investing activities	<u>23</u>	<u>8</u>
Net change in cash and cash equivalents	<u>232,867</u>	<u>(6,564)</u>
Cash and cash equivalents at beginning of year	624	7,188
Cash and cash equivalents at end of year	<u>\$ 233,491</u>	<u>\$ 624</u>
Reconciliation of operating income to net cash provided by operating activities		
Cash and cash equivalents	\$ 12,848	\$ 624
Cash held in escrow	220,643	-
Total cash and cash equivalents	<u>\$ 233,491</u>	<u>\$ 624</u>
Reconciliation of operating income to net cash used by operating activities		
Operating loss	\$ (86,124)	\$ (25,381)
Adjustments to reconcile operating loss to net cash provided by operating activities:		
Depreciation	31,708	-
Net cash used by operating activities	<u>\$ (54,416)</u>	<u>\$ (25,381)</u>
Supplemental schedule of noncash investing and financing activities		
Debt forgiveness	(95,402)	(231,961)

SEE NOTES TO THE FINANCIAL STATEMENTS

BDW WATER SYSTEM ASSOCIATION
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEARS ENDED DECEMBER 31, 2013 AND 2012

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

This summary of significant accounting policies of BDW Water System Association is presented to assist in understanding the Association's financial statements.

The Association reports as a business-type activity, as defined by the Governmental Accounting Standards Board (GASB). Business-type activities are those that are financed in whole or in part by fees charged to external parties for goods or services. In 2009, the Financial Accounting Standards Board (FASB) established the FASB Accounting Standards Codification as a single source of authoritative accounting principles recognized by the FASB in preparation of financial statements in conformity with generally accepted accounting principles. The Codification supersedes existing non-grandfathered non-SEC accounting and reporting standards. In the financial statements, Financial Accounting Standards Board (FASB) pronouncement and Accounting Principles Board (APB) opinions issued on or before November 30, 1989, have been applied, to the extent they are applicable, unless those pronouncement conflict with or contradict GASB pronouncement, in which case GASB prevails.

Nature of Operations and History

BDW Water System Association is organized as a nonprofit organization under North Dakota Century Code 54-40.3. Its purpose is to 1) provide for the exploration of an underground water source that may be used for distribution to Crosby, Noonan, Fortuna and Columbus and the surrounding areas for municipal, industrial, and domestic uses; 2) investigate the feasibility of constructing, maintaining, and operating a water supply system for Crosby, Noonan, Fortuna and Columbus and the surrounding areas that will utilize the Crosby, Noonan, Fortuna and Columbus aquifer for the above-stated purposes; and 3) construct, maintain, and operate a water district system for Crosby, Noonan, Fortuna, and Columbus and the surrounding areas, for municipal, industrial, and domestic uses.

Reporting Entity

Component units are legally separate organizations for which the Association is financially accountable. The Association is financially accountable for an organization if the Association appoints a voting majority of an organization's governing body and (1) the Association is able to significantly influence the programs or services performed or provided by the organization; or (2) the Association is legally entitled to or can otherwise access the organization's resources. Component units may also include organizations that are fiscally dependent on the Association. Fiscal dependence can include the Association's approval of the budget and issuance of debt.

Based on the above criteria, the Association has no component units included in its report.

BDW WATER SYSTEM ASSOCIATION
NOTES TO THE FINANCIAL STATEMENTS - CONTINUED
FOR THE YEARS ENDED DECEMBER 31, 2013 AND 2012

Basis of Accounting

Basis of accounting determines when transactions are recorded in the financial records and reported in the financial statements. The accompanying financial statements have been presented using the modified cash basis of accounting. This basis recognizes assets, deferred outflows of resources, liabilities, deferred inflows of resources, net position, revenues, and expenditures/expenses when they result from cash transactions with a provision for depreciation. This basis is a comprehensive basis of accounting differs other than accounting principles generally accepted in the United States of America (GAAP).

As a result of the use of the modified cash basis of accounting, certain assets and their related revenues (such as accounts receivable and revenue for billed or provided services not yet collected) and certain liabilities and their related expenses (such as accounts payable and expenses for good or services received but not yet paid, and accrued expenses and liabilities) are not recorded in these financial statements.

If the Association utilized the basis of accounting recognized as generally accepted, the statements would be prepared on the accrual basis of accounting.

The Association's activities are accounted for similar to those often found in the private sector using the flow of economic resources measurement focus. The accounting objectives of this measurement focus are the determination of net income, financial position, and cash flows. All assets, liabilities, net position, revenues and expenses are accounted for through a single business-type activity. Current assets include cash and amounts convertible to cash during the next normal operating cycle or one year. Current liabilities include those obligations to be liquidated with current assets. Equity is classified as net position.

Business-type activities distinguish operating from nonoperating revenues and expenses. Operating revenues and expenses are those that generally result from providing service and producing and delivering goods and/or services. It also includes all revenue and expenses not related to capital and related financing, noncapital financing, or investing activities. Revenue from water sales, hookups, memberships, penalties and sales of supplies are reported as operating revenue. Interest income is reported as nonoperating revenue. All expenses related to operating the Association are reported as operating expenses. Interest expense and financing costs are reported as nonoperating.

Cash and Cash Equivalents

For purpose of the statement of cash flows, the Association considers all highly liquid debt instruments purchased with a maturity of three months or less to be cash equivalents, except for certificates of deposits which are considered cash equivalents regardless of their term since there is no loss of principal for early withdrawal, and reserve funds which are considered noncash equivalents regardless of the maturity terms.

BDW WATER SYSTEM ASSOCIATION
NOTES TO THE FINANCIAL STATEMENTS - CONTINUED
FOR THE YEARS ENDED DECEMBER 31, 2013 AND 2012

Investment Policy

The Association does not have a formal investment policy. State statutes authorize local governments to invest in:

(1) Bonds, treasury bills and notes, or other securities that are a direct obligation insured or guaranteed by, the treasury of the United States, or its agencies, instrumentalities or organizations created by an act of Congress.

(2) Securities sold under agreements to repurchase written by a financial institution in which the underlying securities for the agreement to repurchase are of the type listed above.

(3) Certificates of deposit fully insured by the federal deposit insurance corporation.

(4) Obligations of the State.

Capital Assets

Capital assets are recorded at historical costs less accumulated depreciation. A portion of the cost of the capital assets is charged against earnings each year as depreciation expense. Depreciation is computed on the straight-line basis, over the estimated useful life of the asset. The Association established a capitalization threshold of \$5,000. The cost of normal maintenance and repairs that do not add to the value of the assets or materially extend asset lives are not capitalized.

The Association has established the following useful lives:

Buildings and Infrastructure	15 to 40 years
Vehicles	10 years

Net Position

Net position represents the difference between (a) assets and deferred outflows of resources and (b) liabilities and deferred inflows of resources in the Association's financial statements. Net investment in capital assets consists of capital assets, net of accumulated depreciation, reduced by the outstanding balances of any long-term debt attributable to the acquisition, construction, or improvement of those assets. Restricted Net Position consists of restricted assets reduced by liabilities and deferred inflows of resources related to those assets. Unrestricted Net Position is the net amount of assets, deferred outflows of resources, liabilities, and deferred inflows of resources that are not included in the determination of net investment in capital assets or the restricted component of net position.

BDW WATER SYSTEM ASSOCIATION
NOTES TO THE FINANCIAL STATEMENTS - CONTINUED
FOR THE YEARS ENDED DECEMBER 31, 2013 AND 2012

Net Position Flow Assumption

Sometimes, the government will fund capital outlays for particular purposes for both restricted (e.g., restricted bond or grant proceeds) and unrestricted resources. In order to calculate the amounts to report as restricted – net position and unrestricted – net position in the financial statements, a flow assumption must be made about the order in which the resources are considered to be applied. It is the government's policy to consider restricted – net position to have been depleted before unrestricted – net position is applied.

Deferred Outflows/Inflows of Resources

In addition to assets, the statement of net position will sometimes report a separate section for deferred outflows of resources. This separate financial element, *deferred outflows of resources*, represents a consumption of net position that applies to future period(s) and so will not be recognized as an outflow of resource (expense/expenditure) until then. The Association has no items that qualify for reporting in this category.

In addition to liabilities, the statement of net position will sometimes report a separate section for deferred inflows of resources. This separate financial element, *deferred inflows of resources*, represents an acquisition of net position that applies to future period(s) and so will not be recognized as an inflow of resources (revenue) until that time. The Association has one item that qualifies in this category for the year ended December 31, 2013. See Note 5 for a description.

For the year ended December 31, 2013, the Association implemented GASB Statement No. 65, *Items Previously Reported as Assets and Liabilities*. This statement establishes accounting and financial reporting standards that reclassify, as deferred outflows of resources or deferred inflows of resources, certain items that were previously reported as assets and liabilities and recognizes, as outflows of resources or inflows of resources, certain items that were previously reported as assets and liabilities.

Use of Estimates

The preparation of financial statements in conformity with the other comprehensive basis of accounting (OCBOA) used by the Association requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent asset 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 these estimates.

NOTE 2 CUSTODIAL CREDIT RISK

The Association maintains cash deposits at a financial institution. The amount on deposit was insured by the FDIC up to \$250,000. At December 31, 2013 and 2012, the entire balance was fully covered by the FDIC.

BDW WATER SYSTEM ASSOCIATION
NOTES TO THE FINANCIAL STATEMENTS - CONTINUED
FOR THE YEARS ENDED DECEMBER 31, 2013 AND 2012

NOTE 3 CAPITAL ASSETS

The following is a summary of changes in capital assets for the years ended December 31, 2013 and 2012:

	Balance 1/1/13	Additions	Disposals	Balance 12/31/13
Capital assets, not being depreciated				
Construction in progress	\$ 3,682,978	\$ 121,945	\$ (3,804,923)	\$ -
Total capital assets, not being depreciated	<u>3,682,978</u>	<u>121,945</u>	<u>(3,804,923)</u>	<u>-</u>
Capital assets being depreciated				
Buildings and infrastructure	-	3,804,923	-	3,804,923
Total capital assets, being depreciated	<u>-</u>	<u>3,804,923</u>	<u>-</u>	<u>3,804,923</u>
Less accumulated depreciation				
Buildings and infrastructure	-	31,708	-	31,708
Total accumulated depreciation	<u>-</u>	<u>31,708</u>	<u>-</u>	<u>31,708</u>
Total capital assets being depreciated, net	<u>-</u>	<u>3,773,215</u>	<u>-</u>	<u>3,773,215</u>
Net capital assets	<u>\$ 3,682,978</u>	<u>\$ 3,895,160</u>	<u>\$ (3,804,923)</u>	<u>\$ 3,773,215</u>
	Balance 1/1/12	Additions	Disposals	Balance 12/31/12
Capital assets, not being depreciated				
Construction in progress	3,419,831	\$ 263,147	\$ -	3,682,978
Total capital assets, not being depreciated	<u>3,419,831</u>	<u>263,147</u>	<u>-</u>	<u>3,682,978</u>
Net capital assets	<u>\$ 3,419,831</u>	<u>\$ 263,147</u>	<u>\$ -</u>	<u>\$ 3,682,978</u>

NOTE 4 DWSRF FUNDING

DWSRF funding of \$95,402 and \$231,961 was received during the years ended December 31, 2013 and 2012, respectively. This funding was issued as debt proceeds with an automatic debt forgiveness of the entire amount. Therefore, the entity does not have outstanding debt as of December 31, 2013 and 2012. At December 31, 2013, the entity had a deferred inflow of resources in relation to DWSRF funding that had been transferred to an escrow account on behalf of the entity at December 31, 2013. These funds were not recognized as revenue as the funding related to reimbursement for expenditures was not yet approved by the funding source. Revenue will be recognized in the year in which the matching expenses were incurred, approved, and paid.

BDW WATER SYSTEM ASSOCIATION
NOTES TO THE FINANCIAL STATEMENTS - CONTINUED
FOR THE YEARS ENDED DECEMBER 31, 2013 AND 2012

NOTE 5 RISK MANAGEMENT

BDW Water System Association is exposed to various risks relating to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters.

The State Bonding Fund currently provides the Association with blanket fidelity bond coverage in the amount of \$675,000 for its employees. The State Bonding Fund does not currently charge any premium for this coverage. Settled claims resulting from this risk have not exceeded insurance coverage in any of the past three fiscal years.

NOTE 6 COMMITMENTS

The Association has entered into a contract for the construction and expansion of its infrastructure. The Association will use capital grants to pay for the project. As of December 31, 2013, the Association had incurred approximately \$3,805,000 in capitalized costs. Estimated costs to complete the project were approximately \$395,316. The final payments to the contractor were paid in April and November of 2014. No amounts remained outstanding as of the date of these financial statements.

NOTE 7 CONTINGENCIES

The Association received financial assistance from federal and state agencies in the form of grants. The expenditure of funds received under these programs generally requires compliance with items and conditions specified in the grant agreements and are subject to audit by the grantor agencies. Any disallowed claims resulting from such audits could become a liability of the general fund or other applicable funds. The Association's management believes it has complied in all material respects with all applicable grant provisions. In the opinion of management, any possible disallowed claims would not have a material adverse effect on the overall financial position of the Association as of December 31, 2013 and 2012.

NOTE 8 JOINTLY GOVERNED ORGANIZATIONS

WAWSA was formed to own, finance, construct, and operate the Western Area Water Supply Project. The project is a comprehensive water supply project largely utilizing the Missouri River water treated at the Williston Regional Water Treatment Plant and distributed to meet the municipal, rural and industrial water needs for all or part of McKenzie, Williams, Divide, Burke, and Mountrail counties. The project is financed by a series of loans issued by the State of North Dakota. The Association holds two of eleven seats on the board of WAWSA.

BDW WATER SYSTEM ASSOCIATION
NOTES TO THE FINANCIAL STATEMENTS - CONTINUED
FOR THE YEARS ENDED DECEMBER 31, 2013 AND 2012

During 2012, BDW Water System Association entered into the following agreements with WAWSA:

Access and Use Agreement: This agreement sets forth the terms and conditions on which the Member will permit WAWSA to access and use identified infrastructure owned by the BDW. This includes infrastructure identified under sub-agreements with the cities of Crosby and Fortuna. The Association will be responsible for all repairs and maintenance of the access infrastructure identified in the agreement. The Association will have the authority and responsibility for the general management and operation of the identified infrastructure, establishing and implementing purchasing and administrative policies, ensuring compliance with applicable legal requirements, budgeting and accounting procedures, programs and other operational matters. The Association retains ownership of the infrastructure unless a purchase option is exercised. As consideration of this agreement, the Association is also entitled to reimbursement for costs identified in the agreement and in accordance with an approved budget. The Association bears the risk of loss to the infrastructure. The term of the agreement continues until the earlier of: (i) repayment of all WAWSA debt or ii) 99 years after the effective date of the agreement.

Water Supply Agreement: Under this agreement, BDW commits to purchasing water from WAWSA. Subject to a minimum monthly quantity, peak instantaneous flow, and minimum pressure limitation set forth in the agreement, WAWSA agrees to provide, pump, transmit and deliver treated water to the Association. The Association will pay for the water using an agreed-upon base rate plus supplemental rate as outlined in the agreement, which is subject to change. The agreement remains in effect until all of WAWSA's debt is repaid.

Under the above agreement, the Association purchased water from WAWSA during 2013 for a total of \$186,706.

NOTE 9 NEW ACCOUNTING PRONOUNCEMENTS

GASB Statement No. 69, *Government Combinations and Disposals of Government Operations*, establishes accounting and financial reporting standards related to government combinations and disposals of government operations. The requirements of this Statement are effective for government combinations and disposals of government operations occurring in financial reporting periods beginning after December 15, 2013, and should be applied on a prospective basis. Earlier application is encouraged.

BDW WATER SYSTEM ASSOCIATION
NOTES TO THE FINANCIAL STATEMENTS - CONTINUED
FOR THE YEARS ENDED DECEMBER 31, 2013 AND 2012

GASB Statement No. 70, *Accounting and Financial Reporting for Nonexchange Financial Guarantees*, requires a government that extends a nonexchange financial guarantee to recognize a liability when qualitative factors and historical data, if any, indicate that it is more likely than not that the government will be required to make a payment on the guarantee. This Statement also requires a government that has issued an obligation guaranteed in a nonexchange transaction to report the obligation until legally released as an obligor. Or a government that is required to repay a guarantor for making a payment on a guaranteed obligation or legally assuming the guaranteed obligation to continue to recognize a liability until legally released as an obligor. This Statement also provides additional guidance for intra-entity nonexchange financial guarantees involving blended component units. The provisions of this Statement are effective for reporting periods beginning after June 15, 2013. Earlier application is encouraged. Except for disclosures related to cumulative amounts paid or received in relation to a nonexchange financial guarantee, the provisions of this Statement are required to be applied retroactively. Disclosures related to cumulative amounts paid or received in relation to a nonexchange financial guarantee may be applied prospectively.

Management has not determined the effects these pronouncements will have on the Association's financial statements.

NOTE 10 SUBSEQUENT EVENTS

No significant events occurred subsequent to the Association year end. Subsequent events have been evaluated through December 22, 2014, which is the date these financial statements were available to be issued.



CERTIFIED PUBLIC ACCOUNTANTS
AND CONSULTANTS

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 Board of Directors
BDW Water System Association
Minot, North Dakota

We have audited, in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller of the United States, the financial statements of the business-type activities of BDW Water System Association as of and for the years ended December 31, 2013 and 2012, and the related notes to the financial statements, which collectively comprise BDW Water System Association's basic financial statements, and have issued our report thereon dated December 22, 2014.

Internal Control over Financial Reporting

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

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. However, as described in the accompanying schedule of findings and responses, we identified certain deficiencies in internal control that we consider a material weakness and significant deficiencies.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiency described in the accompanying schedule of findings and responses as 2013-003 to be a material weakness.

A *significant deficiency* is a deficiency, or combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider the deficiencies described in the accompanying schedule of findings and responses as items 2013-001 and 2013-002 to be significant deficiencies.

Compliance and Other Matters

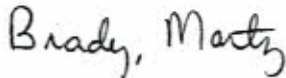
As part of obtaining reasonable assurance about whether the Association's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

BDW Water System Association's Response to Findings

BDW Water System Association's response to the findings identified in our audit is described in the accompanying schedule of findings and responses. The Association's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.



BRADY, MARTZ & ASSOCIATES, P.C.
Minot, North Dakota

December 22, 2014

BDW WATER SYSTEM ASSOCIATION
SCHEDULE OF FINDINGS AND RESPONSES
DECEMBER 31, 2013 AND 2012

I. Findings Relating to Financial Statements

2013-001 *Financial Statement Preparation – Significant Deficiency*

Criteria:	An appropriate system of internal control requires the Association to determine that financial statements are properly stated in compliance with the modified cash basis of accounting (OCBOA). This requires the Association's personnel to maintain knowledge of current accounting principles and required financial statement disclosures.
Condition/Context:	The Association's personnel prepare periodic financial information for internal use that meets the needs of management and the board. However, the Association does not have internal resources to prepare full-disclosure financial statements for external reporting.
Effect:	An appropriate system of internal controls is not present to make a determination that financial statements and the related disclosures are fairly stated in compliance with the modified cash basis of accounting (OCBOA).
Cause:	The Association's internal controls have not been designed to address the specific training needs that are required of its personnel to obtain and maintain knowledge of current accounting principles and required financial statement disclosures.
Recommendation:	We recommend that the Association reviews its current training system to determine if it is cost effective for the Association to obtain this knowledge internally. As a compensating control the Association should establish an internal control policy to document the annual review of the financial statements and schedules and to review a financial statement disclosure checklist.

Views of Responsible Officials and Corrective Actions:

The Association has reviewed their current system and due to the small size of the Association, it is not cost effective for the Association to properly address this significant deficiency

BDW WATER SYSTEM ASSOCIATION
SCHEDULE OF FINDINGS AND RESPONSES - CONTINUED
DECEMBER 31, 2013 AND 2012

2013-002 *Segregation of Duties – Significant Deficiency*

Criteria: Generally, an appropriate system of internal control has the proper separation of duties between authorization, custody, record keeping, and reconciliation functions.

Condition/Context: The billing and collection functions of the Association do not provide for an adequate segregation of duties.

Cause: The Association has a limited number of staff available due to the size of the organization.

Effect: Under the current system, one individual has the ability to enter receipts, prepare and post payments, and reconcile the Association's bank accounts.

Recommendation: While the Association does have some monitoring controls in place, we recommend that the Association review its current process to determine if the monitoring controls can be expanded and if any segregation controls can be economically implemented.

View of responsible officials and corrective actions:

The Board will review the accounting functions and will strive to improve in areas that are economically feasible.

2013-003: *Adjusting Journal Entries – Material Weakness*

Criteria: The Association is required to maintain internal controls at a level where underlying support for general ledger accounts can be developed and a determination can be made that the general ledger accounts are properly reflected on the modified cash basis of accounting.

Condition: During our audit, adjusting entries to the financial statements were proposed in order to bring the financial statements into compliance with the modified cash basis of accounting.

Cause: The entity's internal controls have not been designed to address the specific training needs that are required to maintain the general ledger accounts on a modified cash basis.

Effect: An appropriate system of internal controls is not present to make a determination that the general ledger accounts are properly adjusted in compliance with the modified cash basis of accounting prior to the audit.

BDW WATER SYSTEM ASSOCIATION
SCHEDULE OF FINDINGS AND RESPONSES - CONTINUED
DECEMBER 31, 2013 AND 2012

Recommendation: Accounting personnel will need to determine the proper balance in each general ledger account prior to the audit. We recommend that the entity reviews its current training system to determine if it is cost effective for the entity to obtain this knowledge internally.

Views of responsible officials and planned corrective action:

The Association will review the current year adjustments and determine if it is cost beneficial for personnel of the Association to identify the adjustments prior to the start of future audits.

II. Schedule of Prior Year Findings

Findings 2013-001, 2013-002, and 2013-003 are repeat findings from the December 31, 2011 issued financial statements.