



ricci&company llc

Certified Public Accountants

**PAA-KO COMMUNITIES SEWER
ASSOCIATION**

FINANCIAL STATEMENTS

DECEMBER 31, 2011

A vertical decorative strip on the left side of the page features a dark brown background with large, semi-transparent numbers and mathematical symbols (plus, minus, multiplication, division) in shades of gold and brown, arranged in a scattered pattern.

PAA-KO COMMUNITIES SEWER ASSOCIATION

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PAA-KO COMMUNITIES SEWER ASSOCIATION

Official Roster

Board of Directors

<u>Name</u>	<u>Title</u>
Ken Lundy, Sr.	President
Patrick Hall	Vice President
W. Bruce Franks	Treasurer
Josh Hyatt	Secretary
Nick Thompson	Member

Independent Auditor's Report

Mr. Hector H. Balderas
New Mexico State Auditor and
Board of Directors
Paa-Ko Communities Sewer Association
Sandia Park, New Mexico

We have audited the accompanying financial statements of the business-type activities of the Paa-Ko Communities Sewer Association (Paa-Ko or the Association), as of and for the years ended December 31, 2011 and 2010, which collectively comprise the Association's basic financial statements as listed in the table of contents. We also have audited the accompanying budgetary comparisons for the year ended December 31, 2011 presented as supplementary information as listed in the table of contents. These financial statements and budgetary comparisons are the responsibility of Paa-Ko's management. Our responsibility is to express opinions 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 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 consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the agency's internal control over financial reporting. Accordingly, we express no such opinion. 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 that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the business-type activities of the Association, as of December 31, 2011 and 2010, and the respective changes in financial position and cash flows thereof for the years then ended and the budgetary comparison for the year ended December 31, 2011 in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated May 11, 2012 on our consideration of Paa-Ko'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 controls 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 audits.

Mr. Hector H. Balderas
New Mexico State Auditor and
Board of Directors
Paa-Ko Communities Sewer Association
Sandia Park, New Mexico

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 4 through 6 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Our audits were conducted for the purpose of forming an opinion on the basic financial statements and the budgetary comparison statement. The additional schedules listed as "other supplemental information" in the table of contents are presented for purposes of additional analysis and are not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

Ricci & Company LLC

Albuquerque, New Mexico
May 11, 2012

**PAA-KO COMMUNITIES SEWER ASSOCIATION
MANAGEMENT'S DISCUSSION AND ANALYSIS
December 31, 2011**

OVERVIEW OF THE FINANCIAL STATEMENTS

The management of the Association offers readers of the Association's financial statements this narrative overview and analysis of the financial position of the Association as of December 31, 2011 and the results of its operations for the year then ended. Data as of December 31, 2010 has been provided for comparative purposes.

Governmental Accounting Standards Board (GASB) Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – For State and Local Governments*, was adopted by the Association as of January 1, 2006.

BASIC FINANCIAL STATEMENTS

The Association is considered a local public body pursuant to statutes and legal rulings but does not employ fund accounting and therefore this format is not presented. The Association is reporting using the business-type activities (BTA) format pursuant to GASB 34 reporting model for the fiscal years ending December 31, 2011 and 2010.

The basic financial statements include statements of net assets, which report the Association's assets, liabilities and net assets (equity), statements of revenues, expenses, and changes in net assets, and statements of cash flows. The statement of net assets is presented as of December 31, 2011 and 2010 while the latter two statements cover the years then ended.

CONDENSED COMPARATIVE FINANCIAL INFORMATION

The Association's assets, liabilities and net assets can be summarized as follows as of December 31, 2011 and 2010:

	2011	2010
Current assets	\$ 456,715	409,335
Noncurrent assets	<u>4,161,361</u>	<u>4,405,814</u>
Total assets	<u>\$ 4,618,076</u>	<u>4,815,149</u>
Current liabilities	\$ 85,100	84,617
Noncurrent liabilities	<u>1,247,623</u>	<u>1,310,684</u>
Total liabilities	<u>1,332,723</u>	<u>1,395,301</u>
Members' net assets	<u>3,285,353</u>	<u>3,419,848</u>
Total liabilities and unrestricted net assets	<u>\$ 4,618,076</u>	<u>4,815,149</u>

**PAA-KO COMMUNITIES SEWER ASSOCIATION
MANAGEMENT'S DISCUSSION AND ANALYSIS
December 31, 2011**

The Association's revenues and expenses can be summarized as follows for the years ended December 31, 2011 and 2010:

	2011	2010
Operating revenues	\$ 333,534	342,088
Interest income	<u>3,129</u>	<u>2,984</u>
Total revenues	336,663	345,072
Operating expenses	431,211	452,701
Nonoperating expenses	<u>39,947</u>	<u>41,762</u>
Change in net assets	<u>\$ (134,495)</u>	<u>(149,391)</u>

ANALYSIS OF FINANCIAL POSITION AND RESULTS OF OPERATIONS

Current assets increased by \$47,380 from the prior year mainly due to lower operating and nonoperating expenses for 2011. Fewer septic tanks were pumped in 2011 as this was an "off year" for pumping. Current liabilities also were up slightly by about \$483.

The net decrease in non-current assets is due to the current year's depreciation provision. The decrease in non-current liabilities was the result of the Association paying its scheduled loan payments.

Operating revenues for 2011 were \$8,554 less than in 2010 mainly as a result of Hook-up fee revenue being down by \$8,500.

Expenses for 2011 are down from those for 2010. Septic tank pumping as well as electric expense in 2011 was less than in 2010. As mentioned above, on our three year septic tank pumping cycle, 2011 was a year when fewer tanks are pumped than in the other two years of the three year cycle.

**PAA-KO COMMUNITIES SEWER ASSOCIATION
MANAGEMENT'S DISCUSSION AND ANALYSIS
December 31, 2011**

BUDGETARY ANALYSIS

The budgetary basis is cash basis.

	Original Budget	Final Budget	Actual	Positive (Negative) Variance
Revenues	\$ 349,612	349,612	336,663	(12,949)
Expenses	315,800	315,800	287,930	27,870
Excess of revenues over expenses	<u>\$ 33,812</u>	<u>33,812</u>	<u>48,733</u>	<u>14,921</u>

There was no significant difference between the final budget revenues and actual budget results except that sewer hookup fees were less than budgeted by \$11,200.

The differences in final budget expenses and actual budget results were related to decreases in several expense areas (electric, insurance, septic tank pumping, lift station pumping, professional fees and property taxes). We were also under budget as we did not expend funds for driveway gravel.

CAPITAL ASSET ACTIVITY

There were no capital assets purchased during 2011. Current depreciation in the amount of \$244,453 was recorded.

DEBT ACTIVITY

There were principal payments totaling \$61,225 made as scheduled in 2011.

CONTACTING THE ASSOCIATION'S FINANCIAL MANAGEMENT

This financial report is designed to provide a more understandable and useful overview of the Association and its finances, and to demonstrate the Authority's prudent use of the money it receives. If you have any questions about this report or need additional financial information, contact:

The Paa-Ko Communities Sewer Association
1717 Louisiana NE, Suite 111
Albuquerque, NM 87110

BASIC FINANCIAL STATEMENTS

PAA-KO COMMUNITIES SEWER ASSOCIATION
STATEMENTS OF NET ASSETS - PROPRIETARY FUND
December 31, 2011 and 2010

ASSETS

	2011	2010
Current Assets		
Cash and cash equivalents	\$ 272,981	225,139
Certificates of deposit	165,564	165,000
Accounts receivable	15,236	16,296
Prepaid insurance	2,934	2,900
Total current assets	<u>456,715</u>	<u>409,335</u>
Property and Equipment		
Wastewater treatment plant	3,199,163	3,199,163
Wastewater collection system	2,642,632	2,642,632
Wetland treatment facilities	-	590,746
Total, at cost	<u>5,841,795</u>	<u>6,432,541</u>
Accumulated depreciation	(1,680,434)	(2,026,727)
Net property and equipment	<u>4,161,361</u>	<u>4,405,814</u>
Total assets	<u>\$ 4,618,076</u>	<u>4,815,149</u>

LIABILITIES

	2011	2010
Current Liabilities		
Accounts payable	\$ 205	531
Current maturities of long-term debt	63,061	61,225
Accrued interest payable	21,834	22,861
Total current liabilities	<u>85,100</u>	<u>84,617</u>
Noncurrent Liabilities		
Notes payable	1,241,551	1,304,612
Estimated closure costs payable	6,072	6,072
Total noncurrent liabilities	<u>1,247,623</u>	<u>1,310,684</u>
Total liabilities	<u>1,332,723</u>	<u>1,395,301</u>

Commitments

NET ASSETS

Members' Net Assets		
Invested in capital assets, net of related debt	2,856,749	3,039,977
Unrestricted	428,604	379,871
Total members' net assets	<u>\$ 3,285,353</u>	<u>3,419,848</u>

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

**PAA-KO COMMUNITIES SEWER ASSOCIATION
STATEMENTS OF REVENUES, EXPENSES AND
CHANGES IN NET ASSETS - PROPRIETARY FUND
For the Years Ended December 31, 2011 and 2010**

	2011	2010
Operating Revenues		
Members' assessments	\$ 323,627	322,788
Sewer hookup fees	8,000	16,500
Sewer transfer fees	1,907	2,800
	<hr/>	<hr/>
Total revenues	333,534	342,088
	<hr/>	<hr/>
Operating Expenses		
Depreciation and amortization	244,453	244,320
Maintenance fees	127,842	132,012
Utilities and telephone	23,487	30,530
Septic pumping	6,343	19,376
Professional fees	16,043	16,803
Insurance	5,921	5,991
Repairs and maintenance	5,880	2,058
Office supplies	600	966
Licenses and permits	642	390
Postage	-	255
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Total operating expenses	431,211	452,701
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Operating deficit	(97,677)	(110,613)
	<hr/>	<hr/>
Nonoperating Revenues and (Expenses)		
Interest income	3,129	2,984
Interest expense	(39,947)	(41,762)
	<hr/>	<hr/>
Total nonoperating expenses	(36,818)	(38,778)
	<hr/>	<hr/>
Deficit before contributions and transfers	(134,495)	(149,391)
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Contributions and transfers	-	-
	<hr/>	<hr/>
Change in net assets	(134,495)	(149,391)
	<hr/>	<hr/>
Members' net assets, beginning of year	3,419,848	3,569,239
	<hr/>	<hr/>
Members' net assets, end of year	\$ 3,285,353	3,419,848
	<hr/>	<hr/>

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

PAA-KO COMMUNITIES SEWER ASSOCIATION
STATEMENTS OF CASH FLOWS
For the Years Ended December 31, 2011 and 2010

	2011	2010
Cash Flows From Operating Activities		
Cash received from members	\$ 334,594	337,519
Cash paid to suppliers	(187,118)	(208,593)
Interest paid	(40,974)	(42,759)
	<u>106,502</u>	<u>86,167</u>
Net cash provided by operating activities	<u>106,502</u>	<u>86,167</u>
Cash Flows From Investing Activities		
Additions to plant and equipment	-	(5,575)
Interest received	2,565	2,984
	<u>2,565</u>	<u>2,984</u>
Net cash provided (used) by investing activities	<u>2,565</u>	<u>(2,591)</u>
Cash Flows From Capital Financing Activities		
Principal payments on notes payable	(61,225)	(59,441)
	<u>(61,225)</u>	<u>(59,441)</u>
Net cash used by financing activities	<u>(61,225)</u>	<u>(59,441)</u>
Net increase in cash and cash equivalents	47,842	24,135
Cash and cash equivalents, beginning of year	<u>225,139</u>	<u>201,004</u>
Cash and cash equivalents, end of year	<u>\$ 272,981</u>	<u>225,139</u>
Reconciliation of Operating Income (Deficit) to Net Cash Provided by Operating Activities		
Operating deficit	\$ (97,677)	(110,613)
Adjustments to reconcile changes in net assets to net cash provided by operating activities		
Depreciation and amortization	244,453	244,320
Interest paid	(40,974)	(42,759)
Changes in assets and liabilities		
Other assets	(34)	(115)
Receivables	1,060	(4,569)
Accounts and estimated closure costs payable	(326)	(97)
Total adjustments	<u>204,179</u>	<u>196,780</u>
Net cash provided by operating activities	<u>\$ 106,502</u>	<u>86,167</u>

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

**PAA-KO COMMUNITIES SEWER ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
December 31, 2011 and 2010**

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Financial Reporting Entity. Paa-Ko Communities Sewer Association (Paa-Ko or the Association) is a not-for-profit sewer association formed to provide sewer service to its members-owned and operated sewer utility system and to develop adequate and sanitary sewer works, including the construction of sewage treatment facilities and other necessary improvements and expansion of its sewer system. The Association services only the Paa-Ko Communities, which are located in Sandia Park, New Mexico. The Association operates facilities located in Sandia Park. The Association has the authority to borrow money, to act as an agent or representative of any members, and to convey, assign, and transfer, all of its property and contractual rights to another association or other legal entity that is capable and willing to meet the purposes for which the Association is formed.

On February 13, 2004, the Paa-Ko Communities Sewer Cooperative, Inc., a cooperative association organized on September 1, 1993, acting under the authority granted by the provisions of the Sanitary Projects Act, Sections 3-29-1 through 3-29-19, New Mexico Statutes 1978 (Sanitary Projects Act), reorganized the cooperative association as an association under the Sanitary Projects Act under the new name of Paa-Ko Communities Sewer Association.

All persons who are bona fide owners of land in the service area of the Association, and who evidence their present or future need and desire for wastewater collection and treatment services provided by the Association shall be members. Each member is entitled to only one vote, regardless of the number of lots the member owns. Members owning the same lot will jointly have one vote. Membership is not transferable and terminates upon the conveyance of the last property owned by the member.

There are no component units of the Association as defined in governmental accounting principles.

Basic Financial Statements - GASB Statement No. 34. The financial statements of the Association have been prepared in conformity with accounting principles generally accepted in the United States of America (US GAAP) as applied to governmental units. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles.

In June 1999, the GASB unanimously approved Statement No. 34, *Basic Financial Statements-Management's Discussion and Analysis-For State and Local Governments*. This Statement provides for the most significant change in financial reporting in over twenty years.

Per Attorney General Opinion 06-02, the Attorney General of the State of New Mexico ruled that mutual domestic water associations are local public bodies considered governmental nonprofit organizations and, as such, are subject to certain state statutes and should present financial statements in a government format. The Association has a responsibility to abide by the following:

**PAA-KO COMMUNITIES SEWER ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
December 31, 2011 and 2010**

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

- Open Meeting Act
- Inspection of Public Records Act
- Procurement Code
- Per Diem and Mileage Act
- Section 6-6 NMSA 1978

As of January 1, 2006, the Association implemented the provisions of GASB No. 34, *Basic Financial Statements-Management's Discussion and Analysis-For State and Local Governments*. There was no financial impact to the Association from adopting GASB No. 34.

Basis of Presentation. The Association is considered a special purpose government engaged in a single business-type activity and presents only financial statements required for enterprise funds. These financial statements and corresponding required supplementary information consist of:

- Statement of Net Assets
- Statement of Revenues, Expenses and Changes in Net Assets
- Statement of Cash Flows
- Notes to Financial Statements
- Management's Discussion and Analysis
- Information Required by the State Auditor Rules

Basis of Accounting and Measurement Focus - Enterprise Fund. The accompanying financial statements have been prepared on the accrual basis of accounting. The economic resource measurement focus is used for all assets (both financial and capital), liabilities, revenues, expenses, gains and losses. Revenues are recorded when earned and expenses are recorded when incurred regardless of the timing of the related cash flows. The Association has elected not to apply FASB pronouncements issued after November 30, 1989. The proprietary fund consists of one enterprise fund and as such does not employ any internal service funds.

The fund distinguishes operating revenues and expenditures in the enterprise fund from nonoperating items. Operating revenues and expenditures generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. The principal operating revenues of the fund are members' assessments, hookup fees, and sewer transfer fees. Operating expenditures include administrative expenditures required to manage and operate the fund. All revenues and expenditures not meeting this definition are reported as non-operating revenues and expenditures.

PAA-KO COMMUNITIES SEWER ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
December 31, 2011 and 2010

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

New Accounting Standards Affecting the Association. The Association has adopted GASB Statement No 49, *Accounting and Financial Reporting for Pollution Remediation Obligations*, as of the year ending December 31, 2007. It has accrued an estimated remediation liability in connection with its old plant. The balance at December 31, 2011 and 2010 was \$6,072.

Cash and Cash Equivalents. The Association maintains its cash in various bank deposit accounts in order to maximize FDIC insurance coverage. The Association has not experienced any losses in such accounts and believes it is not exposed to any significant credit risk.

For the purposes of the statements of cash flows, the Association considers all highly liquid investments purchased with an original maturity of three months or less to be cash equivalents.

In accordance with Section 6-10-17, NMSA, 1978 Compilation, the Association is required to obtain collateral in an amount equal to one-half of the deposited public money in excess of \$250,000.

Receivables. Receivables represent amounts due for member assessments. The Association considers these amounts to be fully collectible; accordingly, no allowance is deemed necessary. When receivables are determined to be uncollectible, they are charged to operations when that determination is made. Member assessments are billed in January of each year, and reminder notices are sent throughout the year for delinquent accounts. At year end, the Association files liens on large outstanding balances. No interest or late fees are currently being charged on outstanding balances that have liens filed; however, a \$100 lien release fee is charged as applicable.

Capital Assets. Capital assets are tangible assets that are used in operations and that have initial useful lives that extend beyond a single reporting period. Capital assets are reported at historical cost. Capital assets are depreciated using the straight-line method over their estimated useful lives, which range from ten to twenty-five years. The Association capitalizes new asset additions greater than \$5,000. The Association does not own or lease any vehicles or equipment. Useful lives of capital assets are included in the following table:

Asset Class	Useful Life
Wastewater treatment plant	10 - 24
Wastewater collection system	25
Wetland treatment facilities	10

Repairs and maintenance expenses are charged to operations when incurred and major betterments and replacements are capitalized.

PAA-KO COMMUNITIES SEWER ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
December 31, 2011 and 2010

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Components of Net Assets. Net assets are reported as restricted when constraints placed on net assets use are externally imposed by creditors, grantors, contributors or laws or regulations of other governments or imposed by law through constitutional provisions or enabling legislation. The Association has no restricted net assets at December 31, 2011 and 2010.

The Association has significant assets invested in capital assets, net of related debt as reported on the statement of net assets - proprietary fund for 2011 and 2010. They consist principally of sewer facilities and the corresponding debt thereon. Capital assets are defined as those that are tangible or intangible assets that are used in operations and have a useful life extending beyond one reporting period.

Classification of Revenues. The Association has classified its revenues for the enterprise fund as either operating or nonoperating according to the following criteria:

Operating Revenues: Operating revenues include activities that have characteristics of exchange transactions, such as (1) annual association member fees, (2) sewer hook-up fees, and (3) transfer fees for changes in home ownership.

Nonoperating Revenues: Nonoperating revenues include activities that have the characteristics of non-exchange transactions such as investment income and revenue sources that are defined as nonoperating revenues by GASB Statement No. 9, *Reporting Cash Flows Proprietary and Nonexpendable Trust Funds and Governmental Entities that use Proprietary Fund Accounting*, and GASB Statement No. 34.

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

Budgetary Basis. The Association budgets on a cash basis. Depreciation is not budgeted. The Board of Directors is responsible for authorizing the Association's budget. The Association is statutorily required to submit a budget to the Department of Finance and Administration for approval. The Association was in compliance with these requirements for 2011 and 2010. The Association treats aggregate cash receipts disbursements as one fund. The level of budgetary control is at the fund level.

Reclassifications. Certain reclassifications of information have been made to the prior year financial statements so as to conform to the presentation for the current year.

Subsequent Events. Subsequent events were evaluated through May 11, 2012, which is the date the financial statements were available to be issued.

**PAA-KO COMMUNITIES SEWER ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
December 31, 2011 and 2010**

NOTE 2. CASH AND CASH EQUIVALENTS

Custodial credit risk is the risk that in the event of a bank failure the Association's deposits may not be returned to it. The Association has implemented a deposit policy to utilize multiple deposit accounts with different banks so as to maximize the protection of the FDIC insurance coverage. As of December 31, 2011, the bank balances were not exposed to custodial credit risk.

Credit risk, securities custodial risk, and interest rate rise disclosures do not apply.

NOTE 3. RELATED PARTY TRANSACTIONS

Member assessments of \$51,188 and \$54,075 were paid by Mountain Ranch Limited Partnership (Partnership) during 2011 and 2010, respectively, for developed lots still owned by the Partnership.

The majority of the officers of the Association's Board of Directors are employees of Roger Cox and Associates, Inc. or its affiliates. The Association paid Roger Cox and Associates, Inc. \$7,062 and \$7,050 during 2011 and 2010, respectively, for bookkeeping services. These amounts are included in professional fees on the accompanying statements of revenues, expenses and changes in net assets. Roger Cox and Associates, Inc. is currently providing secretarial and clerical assistance to the Association at no charge.

Treated wastewater is disposed of on the Paa-Ko Golf Course, which is owned by Paa-Ko Golf Venture, LLC, a member of the Association. Paa-Ko Golf Venture, LLC has paid for the pumping equipment, transmission line, and storage ponds necessary to move the treated wastewater to the golf course. Operating expenses associated with transporting the treated wastewater to the golf course is the responsibility of Paa-Ko Golf Venture, LLC.

Transfer and Subsidy Agreement

During 2004, the Partnership transferred ownership of the wastewater collection system, wetland treatment facilities, and the related wetland real estate to the Association. During 2007, the Association completed construction of the sewage treatment plant that replaced the existing wetland sewage treatment system that services Paa-Ko Communities.

Billing services are provided by Paa-Ko Homeowner's Association who bills and collects member assessments and transfers them intact to the Association. Lot owners are required to be members of both the Homeowner's Association and the Sewer Association.

The Partnership is obligated to pay all design, construction and related costs, but not annual operation and maintenance costs, required to provide wastewater collection and/or treatment service to portions of the Association's service area not developed as of September 2004.

**PAA-KO COMMUNITIES SEWER ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
December 31, 2011 and 2010**

NOTE 3. RELATED PARTY TRANSACTIONS (CONTINUED)

The Partnership agreed to reimburse the Association, for each of five years commencing January 1, 2005, in the amount that the Association's annual costs and expenses, including but not limited to debt service and facility operation and maintenance costs, exceed the sum of the Association's total collected dues and other assessments for that year, plus any remaining surplus of collections over expenses for years prior to January 1, 2005. Such subsidies, if any, are due to the Association within three months after the end of the year for which the subsidy is owed.

The agreement is secured by a mortgage on one undeveloped lot owned by the Partnership.

NOTE 4. PROPERTY AND EQUIPMENT

Construction on a new wastewater treatment plant was completed in December 2007. The Wetlands Treatment Facilities is fully depreciated as of January 31, 2007. The Wetlands also consists of certain land transferred at no cost to the Association, not zoned for any alternative purpose and listed at no value by county records. The Wetlands was decommissioned upon completion of the new wastewater treatment facility, and the process was substantially complete in 2010.

The roll forward of capital assets for the year ending December 31, 2011 is as follows:

	Balance 2010	Additions	Deletions	Balance 2011
Nondepreciable				
Wetlands land	\$ -	-	-	-
Depreciable				
Treatment plant	3,199,163	-	-	3,199,163
Wastewater collection system	2,642,632	-	-	2,642,632
Wetlands treatment facilities	590,746	-	(590,746)	-
Total	<u>6,432,541</u>	-	<u>(590,746)</u>	<u>5,841,795</u>
Accumulated depreciation				
Treatment plant	(480,504)	(156,851)	-	(637,355)
Collection system	(955,477)	(87,602)	-	(1,043,079)
Wetlands	<u>(590,746)</u>	-	<u>590,746</u>	<u>-</u>
Total	<u>(2,026,727)</u>	<u>(244,453)</u>	-	<u>(1,680,434)</u>
Net capital assets	<u>\$ 4,405,814</u>	<u>(244,453)</u>	-	<u>4,161,361</u>

Depreciation expense for years ended December 31, 2011 and 2010 was \$244,453 and \$244,320, respectively.

**PAA-KO COMMUNITIES SEWER ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
December 31, 2011 and 2010**

NOTE 5. COMMITMENTS

Agreements

The Association entered into an agreement with New Mexico American Water, a New Mexico corporation, to provide certain operations and maintenance services in connection with the management, operations and maintenance of the wastewater system beginning November 1, 2010 and ending October 31, 2013. The Association is required to pay a monthly service fee of \$11,208, adjusted annually based on the change in the annual Consumer Price Index (CPI).

The Association has also entered into an agreement with Souder, Miller & Associates, a New Mexico corporation, to provide engineering services in connection with the operation of the wastewater system beginning December 14, 2010. The Association is required to pay a monthly service fee of \$1,390 plus gross receipts tax. The agreement has a term of two years.

Legal Proceedings

From time to time, the Association is involved in claims and legal actions arising from the ordinary course of business and member relations. In the opinion of management, the ultimate disposition of the various claims and legal actions will not have a material adverse effect on the Association's financial statements. The Association carries standard insurance for risk purposes.

Discharge Permit

The Association's discharge permit was renewed in 2007. The State of New Mexico Environment Department has the authority to fine the Association for the expiration of the discharge permit.

**PAA-KO COMMUNITIES SEWER ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
December 31, 2011 and 2010**

NOTE 6. DEBT

The Association has the following debt in connection with construction of new facilities:

Debt Description	December 31, 2010	Payments	December 31, 2011	Amount Due Within One Year
Loan #RIP 2004-11 with New Mexico Environment Department (NMED); 3% interest rate per annum; payment begins after final warrant for a period of 20 years at \$33,895/year; option to pay all interest upon completion of construction, uncollateralized	\$ 446,268	(20,507)	425,761	21,122
Loan #RIP 2005-04 with New Mexico Environment Department (NMED); 3% interest rate per annum; payment begins after final warrant for a period of 20 years at \$33,805/year; option to pay all interest upon completion of construction, uncollateralized	445,082	(20,453)	424,629	21,066
Loan #RIP 2006-01 with New Mexico Environment Department (NMED); 3% interest rate per annum; payment begins after final warrant for a period of 20 years at \$34,499/year; option to pay all interest upon completion of construction, uncollateralized	474,487	(20,265)	454,222	20,873
Total	<u>\$ 1,365,837</u>	<u>(61,225)</u>	<u>1,304,612</u>	<u>63,061</u>

As stated in the loan agreements with New Mexico Environment Department, the Association has the option to include accrued interest in the loan amounts and amortized over 20 years for any interim draw downs made prior to construction being completed. As of December 31, 2011 and 2010, accrued interest on loan amounts is:

Loan Number	2011	2010
Loan #RIP 2004-11	\$ 8,233	9,720
Loan #RIP 2005-04	5,965	5,926
Loan #RIP 2006-01	7,636	7,215
Total accrued interest	<u>\$ 21,834</u>	<u>22,861</u>

**PAA-KO COMMUNITIES SEWER ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
December 31, 2011 and 2010**

NOTE 6. DEBT (CONTINUED)

As of December 31, 2011, the Association has drawn down the entire amount of available loan funds. The debt service requirements would be as follows for all currently outstanding loans:

Years ending December 31,	Principal	Interest	Total
2012	\$ 63,061	39,139	102,200
2013	64,953	37,247	102,200
2014	66,902	35,298	102,200
2015	68,909	33,291	102,200
2016	70,975	31,225	102,200
2017-2021	388,127	122,873	511,000
2022-2026	449,943	61,057	511,000
2027-2028	131,742	4,958	136,700
	<u>\$ 1,304,612</u>	<u>365,088</u>	<u>1,669,700</u>

The wetlands sewage treatment system was replaced by a sewage treatment plant near the end of 2007. Per federal and state regulations, if facilities are closed or discharge of wastewater ceases, Paa-Ko shall take steps as defined by New Mexico Environment Department to remediate wetland cells. These steps include the following:

- Remove all lines leading to the wetlands cells so that a discharge can no longer occur;
- Drain and/or evaporate all liquids and dispose of any plant material in accordance with all regulations;
- Dispose of any sludge in accordance with all regulations;
- Perforate or remove wetland liners and fill the cells with dirt to match the surrounding topography in such a way for proper drainage preventing any ponding; and
- Notify NMED within 30 days of the closure.

Paa-Ko is liable for closure and post closure costs. The remaining post closure costs are expected to be minimal and are currently estimated to approximate \$6,000. No additional accrued expenses have been recorded since 2008 as management believes the original estimate is sufficient.

SUPPLEMENTARY INFORMATION

PAA-KO COMMUNITIES SEWER ASSOCIATION
SCHEDULE OF REVENUES AND EXPENSES - BUDGET AND ACTUAL
For the Year Ended December 31, 2011

	Original Budget	Final Budget	Actual	Positive (Negative) Variance
Revenues				
Members' assessments	\$ 324,490	324,490	323,627	(863)
Sewer hookup fees	19,200	19,200	8,000	(11,200)
Sewer transfer fees	2,600	2,600	1,907	(693)
Interest income	3,322	3,322	3,129	(193)
Total revenues	349,612	349,612	336,663	(12,949)
Budgeted cash balance	-	-	-	-
Total revenues and budgeted cash balance	\$ 349,612	349,612	336,663	(12,949)
Expenses				
Operations and maintenance contract	117,200	117,200	117,152	48
Debt service principal and interest	102,200	102,200	101,172	1,028
Electric and gas plant	27,000	27,000	20,119	6,881
Accounting and audit fees	17,000	17,000	15,890	1,110
Engineering services: monthly monitoring	9,000	9,000	9,067	(67)
Septic tank pumping	8,700	8,700	6,343	2,357
Insurance	8,000	8,000	5,921	2,079
Repairs (non-capital)	6,500	6,500	5,880	620
Property tax	3,500	3,500	-	3,500
Telephone	3,000	3,000	2,811	189
Tank pumping - plant and lift stations	2,700	2,700	-	2,700
Professional fees	2,500	2,500	153	2,347
Driveway gravel	2,500	2,500	-	2,500
Testing and analysis	1,500	1,500	1,537	(37)
Bad debt	1,100	1,100	-	1,100
Water	1,000	1,000	557	443
Postage and delivery	1,000	1,000	-	1,000
Office supplies and miscellaneous	1,000	1,000	600	400
License, permits and fees	400	400	642	(242)
Administration fees	-	-	86	(86)
Total expenses	315,800	315,800	287,930	27,870
	\$ 33,812	33,812	48,733	14,921
Revenues, budgetary basis			\$ 336,663	
Interest income			(3,129)	
Total revenues, GAAP basis			<u>\$ 333,534</u>	
Expenses, budgetary basis			\$ 287,930	
Debt service principal and interest			(101,172)	
Depreciation			244,453	
Total expenses, GAAP basis			<u>\$ 431,211</u>	

OTHER SUPPLEMENTARY INFORMATION

**PAA-KO COMMUNITIES SEWER ASSOCIATION
SCHEDULE OF INDIVIDUAL DEPOSIT ACCOUNTS AND PLEDGED COLLATERAL
December 31, 2011**

Account	Bank Balance	Book Balance
Compass Bank		
General checking account	\$ 25,066	\$ 23,426
Association savings account	31,048	31,048
	<hr/>	<hr/>
Total Compass Bank	56,114	54,474
First Community Bank		
Certificate of deposit	90,000	90,000
NM Bank & Trust		
Certificate of deposit	75,000	75,564
Main Bank		
Money market account	218,507	218,507
	<hr/>	<hr/>
Total	439,621	<u><u>\$ 438,545</u></u>
FDIC coverage	<hr/>	439,621
Total uninsured public funds	<hr/>	<u><u>\$ -</u></u>
Collateral requirements - 50% (Section 6-10-17)	\$ -	-
Amounts of pledged collateral -	Maturity	
pledged inventory Compass Bank	Date	CUSIP
	Description	
	1/25/2034	31393VGC3
	FNMA	<hr/>
		130,772
Total over uncollateralized		<u><u>\$ 130,772</u></u>

OTHER REPORT

**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***

Mr. Hector H. Balderas
New Mexico State Auditor and
Board of Directors
Paa-Ko Communities Sewer Association
Sandia Park, New Mexico

We have audited the financial statements of the business-type activities and related budgetary comparison presented as supplemental information of the Paa-Ko Communities Sewer Association (Paa-Ko or the Association) as of and for the year ended December 31, 2011, and have issued our report thereon dated May 11, 2012. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

Management of the Association is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered the Association's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Association's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Association's internal control over financial reporting.

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

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

Mr. Hector H. Balderas
New Mexico State Auditor and
Board of Directors
Paa-Ko Communities Sewer Association

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*.

We noted certain other matters that are required to be reported pursuant to Government Auditing Standards paragraph 5.14 and 5.16, and pursuant to Section 12-6-5, NMSA 1978, which is described in the accompanying schedule of findings and responses as finding 2010-01.

The Association's response to the finding identified in our audit is described in the accompanying schedule of findings and responses. We did not audit the Association's response and, accordingly, we express no opinion on it.

This report is intended solely for the information and use of management, others within the Association, the State Auditor, the New Mexico Legislature, and the Department of Finance and Administration, and is not intended to be and should not be used by anyone other than these specified parties.

Ricci & Company LLC

Albuquerque, New Mexico
May 11, 2012

STATE COMPLIANCE SECTION

**PAA-KO COMMUNITIES SEWER ASSOCIATION
SUMMARY FINDINGS AND RESPONSES
For the Years Ended December 31, 2011 and 2010**

PRIOR YEAR – FINANCIAL STATEMENT FINDING

FINDING	STATUS
2010-01 Late Submission of Report	Resolved

CURRENT YEAR – FINANCIAL STATEMENT FINDING

None

**PAA-KO COMMUNITIES SEWER ASSOCIATION
EXIT CONFERENCE
For the Year Ended December 31, 2011**

An exit conference was held on May 11, 2012 to discuss the annual financial report. Attending were the following:

Representing the PAA-Ko Community Sewer Association:

Ken Lundy	President
W. Bruce Franks	Treasurer

Representing the Independent Auditor:

Herman Chavez, CPA

Note: Management is responsible for the context of the report, even though the financial statements were prepared substantially by the independent auditor.