

PAA-KO COMMUNITIES SEWER ASSOCIATION

FINANCIAL STATEMENTS

DECEMBER 31, 2013

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>
Patrick Hall	President
Derek Wartman	Vice President
Nick Thompson	Secretary
W. Bruce Franks	Treasurer
Thomas P. Dittman	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

Report on Financial Statements

We have audited the accompanying financial statements of the business-type activities of the Paa-Ko Communities Sewer Association (Association) as of and for the years ended December 31, 2013 and 2012, and the related notes to the financial statements, which collectively comprise the Association's basic financial statements as listed in the table of contents. We also have audited the accompanying budgetary comparison presented as supplementary information, as defined by the Government Accounting Standards Board, as of and for the year ended December 31, 2013, as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express opinions on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to 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 from material misstatement.

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

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

Opinions

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 Paa-Ko Communities Sewer Association as of December 31, 2013 and 2012, and the respective changes in financial position and cash flows thereof for the years then ended and the respective budgetary comparison for the year ended December 31, 2013 in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 5-7 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Association's basic financial statements. The Schedule of Individual Deposit Accounts and Pledged Collateral is presented for purposes of additional analysis and is not a required part of the basic financial statements.

The Schedule of Individual Deposit Accounts and Pledged Collateral required by 2.2.2.NMAC is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the Schedule of Individual Deposit Accounts and Pledged Collateral is fairly stated, in all material respects, in relation to the basic financial statements as a whole.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated May 27, 2014, on our consideration of the 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 internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Association's internal control over financial reporting and compliance.

Ricci & Company LLC

Albuquerque, New Mexico
May 27, 2014

**PAA-KO COMMUNITIES SEWER ASSOCIATION
MANAGEMENT'S DISCUSSION AND ANALYSIS
December 31, 2013**

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, 2013 and the results of its operations for the year then ended. Data as of December 31, 2012 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, 2013 and 2012.

The basic financial statements include statements of net position, which report the Association's assets, liabilities and net position (equity), statements of revenues, expenses, and changes in net position, and statements of cash flows. The statement of net position is presented as of December 31, 2013 and 2012 while the latter two statements cover the years then ended.

CONDENSED COMPARATIVE FINANCIAL INFORMATION

The Association's assets, liabilities and net position can be summarized as follows as of December 31, 2013 and 2012:

	2013	2012
Current assets	\$ 450,111	477,402
Noncurrent assets	<u>3,672,721</u>	<u>3,917,041</u>
Total assets	<u>4,122,832</u>	<u>4,394,443</u>
Current liabilities	91,050	89,365
Noncurrent liabilities	<u>1,115,768</u>	<u>1,182,670</u>
Total liabilities	<u>1,206,818</u>	<u>1,272,035</u>
Net investment in capital assets	2,496,123	2,675,490
Unrestricted	<u>419,891</u>	<u>446,918</u>
Total net position	<u>\$ 2,916,014</u>	<u>3,122,408</u>

**PAA-KO COMMUNITIES SEWER ASSOCIATION
MANAGEMENT'S DISCUSSION AND ANALYSIS
December 31, 2013**

The Association's revenues and expenses can be summarized as follows for the years ended December 31, 2013 and 2012:

	2013	2012
Operating revenues	\$ 347,167	346,562
Interest income	<u>1,790</u>	<u>2,090</u>
Total revenues	348,957	348,652
Operating expenses	519,194	473,517
Nonoperating expenses	<u>36,157</u>	<u>38,080</u>
Change in net position	<u>\$ (206,394)</u>	<u>(162,945)</u>

ANALYSIS OF FINANCIAL POSITION AND RESULTS OF OPERATIONS

Current assets decreased by \$27,291 from the prior year mainly due to increased operating expenses, particularly in repairs and maintenance. Current liabilities were up slightly by about \$1,685 due mainly to an increase in the current portion of long term debt to be paid in 2014.

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 2013 were only \$605 more than in 2012 which is expected because operations were fairly consistent.

Expenses for 2013 are up from those for 2012. Septic tank pumping as well as repairs and maintenance expense in 2013 was more than in 2012. On our three-year septic tank pumping cycle, 2013 was a year when many more tanks were pumped than in 2012. Repairs and maintenance expense was up in 2013 mainly due to various lift station repairs.

**PAA-KO COMMUNITIES SEWER ASSOCIATION
MANAGEMENT'S DISCUSSION AND ANALYSIS
December 31, 2013**

BUDGETARY ANALYSIS

The budgetary basis is cash basis.

	Original Budget	Final Budget	Actual	Positive (Negative) Variance
Revenues	\$ 350,931	350,931	348,957	(1,974)
Expenses	<u>369,800</u>	<u>369,800</u>	<u>375,984</u>	<u>(6,184)</u>
Excess of revenues over expenses	<u>\$ (18,869)</u>	<u>(18,869)</u>	<u>(27,027)</u>	<u>(8,158)</u>

There was no significant difference between the final budget revenues and actual budget results.

The differences in final budget expenses and actual budget results were related mainly to non-capital repairs which were more than budgeted by \$8,135.

CAPITAL ASSET ACTIVITY

There were no capital assets purchased during 2013. Current depreciation in the amount of \$244,320 was recorded.

DEBT ACTIVITY

There were principal payments totaling \$64,953 made as scheduled in 2013.

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 POSITION - PROPRIETARY FUND
December 31, 2013 and 2012**

ASSETS

	2013	2012
Current Assets		
Cash and cash equivalents	\$ 254,645	286,337
Certificates of deposit	166,302	165,846
Accounts receivable	24,888	21,823
New Mexico gross receipts tax overpayment	900	-
Prepaid insurance	3,376	3,396
Total current assets	<u>450,111</u>	<u>477,402</u>
Property and Equipment		
Wastewater treatment plant	3,199,163	3,199,163
Wastewater collection system	2,642,632	2,642,632
Total, at cost	<u>5,841,795</u>	<u>5,841,795</u>
Accumulated depreciation	(2,169,074)	(1,924,754)
Net property and equipment	<u>3,672,721</u>	<u>3,917,041</u>
Total assets	<u>4,122,832</u>	<u>4,394,443</u>

LIABILITIES

Current Liabilities		
Accounts payable	4,462	3,636
Current maturities of long-term debt	66,902	64,953
Accrued interest payable	19,686	20,776
Total current liabilities	<u>91,050</u>	<u>89,365</u>
Noncurrent Liabilities		
Notes payable	1,109,696	1,176,598
Estimated closure costs payable	6,072	6,072
Total noncurrent liabilities	<u>1,115,768</u>	<u>1,182,670</u>
Total liabilities	<u>1,206,818</u>	<u>1,272,035</u>

NET POSITION

Members' Net Position		
Net investment in capital assets	2,496,123	2,675,490
Unrestricted	419,891	446,918
Total members' net position	<u>\$ 2,916,014</u>	<u>3,122,408</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 POSITION - PROPRIETARY FUND
 For the Years Ended December 31, 2013 and 2012**

	2013	2012
Operating Revenues		
Members' assessments	\$ 322,318	325,462
Sewer hookup fees	22,000	18,500
Sewer transfer fees	2,849	2,600
	<hr/>	<hr/>
Total operating revenues	347,167	346,562
	<hr/>	<hr/>
Operating Expenses		
Depreciation and amortization	244,320	244,320
Maintenance fees	132,084	131,912
Septic pumping	43,938	34,172
Utilities and telephone	28,263	26,255
Professional fees	17,061	16,582
Repairs and maintenance	40,735	13,604
Insurance	6,899	5,993
Licenses and permits	5,126	334
Office supplies	657	308
Postage	111	37
	<hr/>	<hr/>
Total operating expenses	519,194	473,517
	<hr/>	<hr/>
Operating loss	(172,027)	(126,955)
	<hr/>	<hr/>
Nonoperating Revenues and (Expenses)		
Interest income	1,790	2,090
Interest expense	(36,157)	(38,080)
	<hr/>	<hr/>
Total nonoperating expenses	(34,367)	(35,990)
	<hr/>	<hr/>
Change in net position	(206,394)	(162,945)
	<hr/>	<hr/>
Members' net position, beginning of year	3,122,408	3,285,353
	<hr/>	<hr/>
Members' net position, end of year	\$ 2,916,014	3,122,408
	<hr/> <hr/>	<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, 2013 and 2012**

	2013	2012
Cash Flows From Operating Activities		
Cash received from members	\$ 344,102	339,975
Cash paid to suppliers	(274,928)	(226,228)
Interest paid	(37,247)	(39,138)
Net cash provided by operating activities	<u>31,927</u>	<u>74,609</u>
Cash Flows From Investing Activities		
Interest received	1,334	1,808
Net cash provided by investing activities	<u>1,334</u>	<u>1,808</u>
Cash Flows From Capital Financing Activities		
Principal payments on notes payable	(64,953)	(63,061)
Net cash used by capital financing activities	<u>(64,953)</u>	<u>(63,061)</u>
Net (decrease) increase in cash and cash equivalents	(31,692)	13,356
Cash and cash equivalents, beginning of year	<u>286,337</u>	<u>272,981</u>
Cash and cash equivalents, end of year	<u>\$ 254,645</u>	<u>286,337</u>
Reconciliation of Operating Loss to Net Cash Provided by Operating Activities		
Operating deficit	\$ (172,027)	(126,955)
Adjustments to reconcile changes in net position to net cash provided by operating activities		
Depreciation and amortization	244,320	244,320
Interest paid	(37,247)	(39,138)
Changes in assets and liabilities:		
Other assets	20	(462)
Receivables	(3,065)	(6,587)
Accounts and estimated closure costs payable	(74)	3,431
Total adjustments	<u>203,954</u>	<u>201,564</u>
Net cash provided by operating activities	<u>\$ 31,927</u>	<u>74,609</u>

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

**PAA-KO COMMUNITIES SEWER ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
December 31, 2013 and 2012**

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.

The Association is considered to be a special-purpose governmental entity in accordance with Governmental Accounting Standards Board Statement No. 14. The Association is not a component unit of a governmental entity nor does it have any component units.

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, 2013 and 2012**

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 Position
- Statement of Revenues, Expenses and Changes in Net Position
- 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 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, 2013 and 2012**

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

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. Late fees are currently being charged on outstanding balances and a \$125 lien release fee is charged as applicable. Late fees collected in 2013 and 2012 were insignificant.

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	7 - 24
Wastewater collection system	10 - 25

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

Components of Net Position. Net position is reported as restricted when constraints placed on net position 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 restrictions on net position at December 31, 2013 and 2012.

The Association has significant capital assets, net of related debt as reported on the statement of net position - proprietary fund for 2013 and 2012. 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.

PAA-KO COMMUNITIES SEWER ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
December 31, 2013 and 2012

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

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 2013 and 2012. The Association treats aggregate cash receipts disbursements as one fund. The level of budgetary control is at the fund level.

At December 31, 2013 the Association's actual expenditures exceeded budgeted expenditures at the legal level of compliance.

Subsequent Events. Subsequent events were evaluated through May 27, 2014, which is the date the financial statements were available to be issued.

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, 2013, the bank balances were not exposed to custodial credit risk.

The Association has funds in a money market account that is unrated as to its credit risk.

Securities custodial risk and interest rate risk disclosures do not apply.

**PAA-KO COMMUNITIES SEWER ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
December 31, 2013 and 2012**

NOTE 3. RELATED PARTY TRANSACTIONS

Member assessments of \$42,250 and \$47,250 were paid by Mountain Ranch Limited Partnership (Partnership) during 2013 and 2012, 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 \$7,038 during 2013 and 2012, respectively, for bookkeeping services. These amounts are included in professional fees on the accompanying statements of revenues, expenses and changes in net position. Roger Cox and Associates, Inc. provide administrative 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.

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.

NOTE 4. PROPERTY AND EQUIPMENT

The roll forward of capital assets for the year ending December 31, 2013 is as follows:

	Balance 2012	Additions	Deletions	Balance 2013
Depreciable				
Treatment plant	\$ 3,199,163	-	-	3,199,163
Wastewater collection system	2,642,632	-	-	2,642,632
Total	5,841,795	-	-	5,841,795
Accumulated depreciation				
Treatment plant	(794,206)	(154,733)	-	(948,939)
Collection system	(1,130,548)	(89,587)	-	(1,220,135)
Total	(1,924,754)	(244,320)	-	(2,169,074)
Net capital assets	\$ 3,917,041	(244,320)	-	3,672,721

Depreciation expense for years ended December 31, 2013 and 2012 was \$244,320.

**PAA-KO COMMUNITIES SEWER ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
December 31, 2013 and 2012**

NOTE 5. DEBT

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

Debt Description	December 31, 2012	Payments	December 31, 2013	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	\$ 404,639	(21,756)	382,883	22,409
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	403,563	(21,698)	381,865	22,349
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	433,349	(21,499)	411,850	22,144
Total	<u>\$ 1,241,551</u>	<u>(64,953)</u>	<u>1,176,598</u>	<u>66,902</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 amortize over 20 years for any interim drawdowns made prior to construction being completed. As of December 31, 2013 and 2012, accrued interest on loan amounts is:

Loan Number	2013	2012
Loan #RIP 2004-11	\$ 8,308	7,823
Loan #RIP 2005-04	5,053	5,669
Loan #RIP 2006-01	<u>6,325</u>	<u>7,284</u>
Total accrued interest	<u>\$ 19,686</u>	<u>20,776</u>

**PAA-KO COMMUNITIES SEWER ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
December 31, 2013 and 2012**

NOTE 5. DEBT (CONTINUED)

As of December 31, 2013, 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
2014	\$ 66,902	35,298	102,200
2015	68,909	33,291	102,200
2016	70,976	31,224	102,200
2017	73,106	29,094	102,200
2018	75,299	26,901	102,200
2019-2023	411,761	99,239	511,000
2024-2028	409,645	33,655	443,300
	<u>\$ 1,176,598</u>	<u>288,702</u>	<u>1,465,300</u>

NOTE 6. WETLANDS AND POST CLOSURE COSTS

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, based on engineering estimates, are expected to be minimal and are currently estimated to be \$6,072. No additional accrued expenses have been recorded since 2008 as management believes the original estimate is sufficient.

**PAA-KO COMMUNITIES SEWER ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
December 31, 2013 and 2012**

NOTE 7. COMMITMENTS

Agreements

The Association entered into an agreement with New Mexico American Water, now known as EPCOR Water, to provide certain operations and maintenance services in connection with the management, operations and maintenance of the wastewater system beginning November 1, 2013 and ending October 31, 2014. The Association is required to pay a monthly service fee of \$10,274, adjusted annually based on the change in the annual Consumer Price Index (CPI).

The Association has also entered into an agreement with Martin/Martin, Inc. to provide engineering services in connection with the operation of the wastewater system beginning December 7, 2012. The Association is required to pay a monthly service fee based on \$800 for onsite visits and \$480 for offsite operations monitoring, which is anticipated to be \$7,680 per annum. The agreement has a term of three 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.

SUPPLEMENTARY INFORMATION

PAA-KO COMMUNITIES SEWER ASSOCIATION
SCHEDULE OF REVENUES AND EXPENSES - BUDGET AND ACTUAL
For the Year Ended December 31, 2013

	Original Budget	Final Budget	Actual	Positive (Negative) Variance
Revenues				
Members' assessments	\$ 324,440	324,440	322,318	(2,122)
Sewer hookup fees	22,400	22,400	22,000	(400)
Sewer transfer fees	2,000	2,000	2,849	849
Interest income	2,091	2,091	1,790	(301)
Total revenues	350,931	350,931	348,957	(1,974)
Budgeted cash balance	18,869	18,869	37,500	18,631
Total revenues and budgeted cash balance	\$ 369,800	369,800	386,457	16,657
Expenses				
Operations and maintenance contract	120,700	120,700	123,818	(3,118)
Debt service principal and interest	102,200	102,200	101,110	1,090
Septic tank pumping	39,200	39,200	42,624	(3,424)
Electric and gas plant	27,000	27,000	25,113	1,887
Accounting and audit fees	17,000	17,000	16,736	264
Repairs (non-capital)	32,600	32,600	40,735	(8,135)
Engineering services: monthly monitoring	9,000	9,000	6,677	2,323
Insurance	8,000	8,000	6,899	1,101
Telephone	3,000	3,000	2,890	110
Tank pumping - plant and lift stations	2,700	2,700	1,314	1,386
Professional fees	2,500	2,500	325	2,175
Testing and analysis	1,500	1,500	1,589	(89)
Bad debt	1,000	1,000	-	1,000
Water	1,000	1,000	260	740
Postage and delivery	1,000	1,000	111	889
Office supplies and miscellaneous	1,000	1,000	657	343
License, permits and fees	400	400	5,126	(4,726)
Administration fees	-	-	-	-
Total expenses	369,800	369,800	375,984	(6,184)
	\$ -	-	10,473	10,473
Revenues, budgetary basis			\$ 386,457	
Interest income			(1,790)	
Transfer from savings			(37,500)	
Total revenues, GAAP basis			<u>\$ 347,167</u>	
Expenses, budgetary basis			\$ 375,984	
Debt service principal and interest			(101,110)	
Depreciation			244,320	
Total expenses, GAAP basis			<u>\$ 519,194</u>	

OTHER SUPPLEMENTARY INFORMATION

**PAA-KO COMMUNITIES SEWER ASSOCIATION
SCHEDULE OF INDIVIDUAL DEPOSIT ACCOUNTS AND PLEDGED COLLATERAL
December 31, 2013**

Account	Bank Balance	Book Balance
Compass Bank		
General checking account	\$ 28,282	\$ 6,030
Association savings account	28,769	28,769
	<hr/>	<hr/>
Total Compass Bank	57,051	34,799
US Bank		
Certificate of deposit	90,000	90,000
NM Bank & Trust		
Certificate of deposit	76,302	76,302
Main Bank		
Money market account	219,846	219,846
	<hr/>	<hr/>
Total	443,199	<u><u>\$ 420,947</u></u>
FDIC coverage	<hr/>	<hr/>
	443,199	
Total uninsured public funds	<hr/>	<hr/>
	\$ -	
Collateral requirements - 50% (Section 6-10-17)	\$ -	
Amounts of pledged collateral -	Maturity	
pledged inventory Compass Bank	Date	CUSIP
	Description	
	1/25/2034	31393VGC3
	FNMA	85,739
		<hr/>
Total over uncollateralized		<u><u>\$ 85,739</u></u>

OTHER REPORT

Ricci & Company LLC

CERTIFIED PUBLIC ACCOUNTANTS
6200 UPTOWN BLVD. NE - SUITE 400
ALBUQUERQUE, NM 87110

**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***

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, in accordance with the 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, the financial statements of the business-type activities of the Paa-Ko Communities Sewer Association (Association), as of and for the years ended December 31, 2013 and 2012, and the related notes to the financial statements, which collectively comprise the Association's basic financial statements, and the respective budgetary comparison of the Association presented as supplemental information, and have issued our report thereon dated May 27, 2014.

Internal Control over Financial Reporting

In planning and performing our audit of the financial statements, we considered the 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 opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Association's internal control. Accordingly, we do not express an opinion on the effectiveness of the Association's internal control.

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. *A significant deficiency* is a deficiency, or a 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.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or, significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

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 instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* and which are described in the accompanying schedule of findings and responses as items 2013-001.

The Association's Response to Findings

The Association's responses to the findings identified in our audit are described in the accompanying schedule of findings and responses. The Association's responses were not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on them.

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.

Ricci & Company LLC

Albuquerque, New Mexico
May 27, 2014

STATE COMPLIANCE SECTION

**PAA-KO COMMUNITIES SEWER ASSOCIATION
SCHEDULE OF FINDINGS AND RESPONSES
For the Years Ended December 31, 2013 and 2012**

A. PRIOR YEAR – FINANCIAL STATEMENT FINDING

None

B. FINDINGS – COMPLIANCE AND OTHER MATTERS

2013-001 Budget Deficits - Other

CRITERIA

The authority by which the Association can expend funds is with the Association's Board and the Department of Finance Administration approved budget (NMSA 1978, Section 6-6-6).

CONDITION

Expenditures in excess of budgeted amounts were as follows:

Business Type Activities	\$6,194
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CAUSE

Actual expenditures exceeded the budgeted amounts and a corresponding year end budget adjustment was not made.

EFFECT

The Association is in violation of applicable laws, regulations and policies established by the State and Department of Finance and Administration.

RECOMMENDATION

We recommend that management implement procedures to prevent budget over-expenditures.

MANAGEMENT RESPONSE

The Association incurred late year emergency repairs to a sewer lift station costing \$8,162 and repairs in the treatment plant computer as a result of a computer crash costing \$1,591. As the repairs were necessary due to health issues, they were immediately made. The Association had ample cash in its savings accounts (reserves) to cover the overage. The Association did disclose the additional transfers from savings to the operating account in excess of the budgeted transfers in its letter to DF&A of 12-24-13 which accompanied the 2014 budget proposal.

**PAA-KO COMMUNITIES SEWER ASSOCIATION
EXIT CONFERENCE
For the Year Ended December 31, 2013**

An exit conference was held on May 27, 2014 to discuss the annual financial report. Attending were the following:

Representing the PAA-Ko Community Sewer Association:

Patrick Hall	President
W. Bruce Franks	Treasurer

Representing the Independent Auditor:

Donna Peace, CPA, Principal
Colleen Gabaldon, Supervisor

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