

**OTIS
MUTUAL DOMESTIC WATER CONSUMERS
AND SEWAGE WORKS ASSOCIATION
AUDITED FINANCIAL STATEMENTS
AND SUPPLEMENTARY INFORMATION
JUNE 30, 2017**

INTRODUCTORY SECTION

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JUNE 30, 2017**

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**OTIS MUTUAL DOMESTIC WATER CONSUMERS AND SEWAGE WORKS ASSOCIATION
OFFICIAL ROSTER
JUNE 30, 2017**

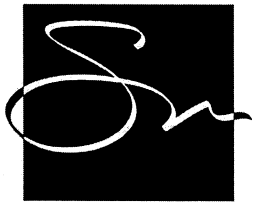
BOARD OF DIRECTORS

Name	Title
Jim Wilcox	President
Danny Bass	Vice-President
Jim Fry	Secretary-Treasurer
Rowdy Schenck	Director
Henry Vasquez	Director

ASSOCIATION OFFICIALS

Name	Title
Cutter Rogers	General Manager

FINANCIAL SECTION



SCOTT NORTHAM, CPA, PC
Certified Public Accountants

INDEPENDENT AUDITOR'S REPORT

Timothy Keller, New Mexico State Auditor, and
Board of Directors of
Otis Mutual Domestic Water Consumers
and Sewage Works Association
Otis, New Mexico

Report on the Financial Statements

We have audited the accompanying financial statements of the business-type activities for Otis Mutual Domestic Water Consumers and Sewage Works Association (Association) as of and for the year ended June 30, 2017, and the related notes to the financial statements, which comprise the 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 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 qualified audit opinions.

Basis for Qualified Opinions

Management has not adopted an internal control methodology sufficient enough to prevent or detect fraudulent activities by Association personnel. Accounting principles generally accepted in the United States of America require the Association to design, implement, and maintain an internal control system sufficient enough to provide for the preparation and fair presentation of financial statements to be free from material misstatement, whether due to fraud or error. The amount by which this departure affects the assets, liabilities, deferred inflows and outflows, net position, revenues or expenses of the Association has not been determined.

The Association did not properly reconcile and monitor unrestricted cash recorded within the general ledger with amounts reflected in the bank accounts. The accounting software does not reconcile with the amount reflected in the bank accounts. Proper reconciliation of the cash amounts is dependent on financial activity that occurs during the fiscal year. The effect of the proper reconciliation of cash, which affects assets, liabilities, deferred inflows and outflows, net position, revenues, or expenses, has not been determined.

Qualified Opinions

In our opinion, except for the effects of the matters described in the “Basis for Qualified Opinions” paragraphs, the financial statements referred to above present fairly, in all material respects, the financial position of the business-type activities for Otis Mutual Domestic Water Consumers and Sewage Works Association, and the changes in financial position thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

We draw attention to Note I of the financial statements which discloses the discovery of misappropriation of assets by an Association employee during the fiscal year and the resulting actions taken by the Association. Our opinion is modified with respect to this matter.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management’s discussion and analysis (MD&A) 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.

Management has elected to omit the MD&A which is required to be presented to supplement the basic financial statements by accounting principles generally accepted in the United States of America. Our opinion on the basic financial statements is not affected by this missing information.

Accounting principles generally accepted in the United States of America require that the Schedules of Required Supplementary Information for Pension Plans and related notes 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 inquires 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 the 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.

Supplementary Information

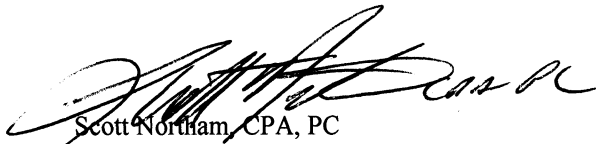
Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Otis Mutual Domestic Water Consumers and Sewage Works Association's basic financial statements. The budgetary comparison is presented for purposes of additional analysis and is not a required part of the basic financial statements.

The budgetary comparison 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, except for the effects of the matter described in the "Basis for Qualified Opinions" paragraphs above, based on our audit and the procedures performed as described above, the budgetary comparison 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 November 17, 2017, 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.



Scott Northam, CPA, PC
Ruidoso, New Mexico
November 17, 2017

OTIS MUTUAL DOMESTIC WATER CONSUMERS AND SEWAGE WORKS ASSOCIATION
STATEMENT OF NET POSITION
JUNE 30, 2017

ASSETS AND DEFERRED OUTFLOWS

CURRENT ASSETS

Unrestricted Cash and Cash Equivalents	\$ 15,770
Accounts Receivable	118,490
Inventory	<u>139,779</u>
TOTAL CURRENT ASSETS	<u>274,039</u>

NONCURRENT ASSETS

Restricted Cash and Cash Equivalents	
Debt Service Reserve - USDA RUS	74,420
Customer Deposits	95,915
Employee Theft Receivable	857,543
Capital Assets, Net	<u>4,779,055</u>
TOTAL NONCURRENT ASSETS	<u>5,806,933</u>
TOTAL ASSETS	<u>6,080,972</u>

DEFERRED OUTFLOWS

Deferred Outflows - PERA	<u>149,372</u>
TOTAL DEFERRED OUTFLOWS	<u>149,372</u>
TOTAL ASSETS AND DEFERRED OUTFLOWS	<u><u>\$ 6,230,344</u></u>

LIABILITIES, DEFERRED INFLOWS AND NET POSITION

LIABILITIES

CURRENT LIABILITIES

Accounts Payable	\$ 15,716
Accrued Wages	5,027
Accrued Payroll Tax Liabilities	4,351
Sales Tax Payable	12,506
Accrued Vacation, Current Portion	7,755
Long-Term Debt, Current Portion	20,893
TOTAL CURRENT LIABILITIES	<u>66,248</u>

NONCURRENT LIABILITIES

Customer Deposits	95,915
Accrued Vacation, Net of Current Portion	24,728
Long-Term Debt, Net of Current Portion	662,641
Long-Term PERA Payable	431,369

TOTAL NONCURRENT LIABILITIES 1,214,653

TOTAL LIABILITIES 1,280,901

DEFERRED INFLOWS

Deferred Inflows - PERA	<u>34,306</u>
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TOTAL DEFERRED INFLOWS 34,306

NET POSITION

Net Investment in Capital Assets	4,095,521
Restricted	
Debt Service	74,420
Unrestricted	<u>745,196</u>

TOTAL NET POSITION 4,915,137

TOTAL LIABILITIES, DEFERRED INFLOWS AND NET POSITION \$ 6,230,344

OTIS MUTUAL DOMESTIC WATER CONSUMERS AND SEWAGE WORKS ASSOCIATION
STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET POSITION
FOR THE YEAR ENDED JUNE 30, 2017

OPERATING REVENUES	
Water Sales and Charges for Service	\$ 1,224,464
Late Charges and Service Fees	17,993
Rental and Lease Income	7,704
	7,704
Total Operating Revenues	1,250,161
 OPERATING EXPENSES	
Wages and Salaries	344,676
Payroll Taxes	25,655
PERA Retirement	41,249
Other Employee Benefits	83,723
Advertising	1,027
Auto Expense	60,783
Travel	7,823
Training and Education	450
Dues and Subscriptions	923
Licenses, Fees, and Permits	16,975
Equipment Rental and Supplies	128,730
Insurance	34,933
Office and Administrative Expense	18,924
Postage and Shipping	10,002
Bank and Credit Card Fees	3,337
Professional Fees and Contracted Services	48,984
Repairs and Maintenance	87,981
Property and Other Taxes	1,730
Utilities	80,188
Water Purchases	19,178
Depreciation	77,720
	77,720
Total Operating Expenses	1,094,991
Operating Income	155,170
 NON-OPERATING REVENUE (EXPENSE)	
Interest Income	290
Memberships	26,000
Interest Expense	(22,454)
	(22,454)
Total Non-operating Income (Expense)	3,836
Income Before Capital Grants	159,006
 CAPITAL GRANTS	
State	77,983
	77,983
Total Capital Grants	77,983
CHANGE IN NET POSITION	236,989
NET POSITION, BEGINNING OF YEAR	4,678,148
NET POSITION, END OF YEAR	\$ 4,915,137

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

**OTIS MUTUAL DOMESTIC WATER CONSUMERS AND SEWAGE WORKS ASSOCIATION
STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED JUNE 30, 2017**

CASH FLOWS FROM OPERATING ACTIVITIES	
Receipts from Customers and Users	\$ 1,267,462
Payments to and on Behalf of Employees	(466,738)
Payments to Suppliers and Contractors	<u>(477,300)</u>
Net Cash Provided by Operating Activities	<u>323,424</u>
CASH FLOWS FROM INVESTING ACTIVITIES	
Interest Income	290
Capital Asset Purchases	<u>(46,846)</u>
Net Cash Used by Investing Activities	<u>(46,556)</u>
CASH FLOWS FROM NON-CAPITAL FINANCING ACTIVITIES	
Unauthorized Funds Expenditure	<u>(570,529)</u>
Net Cash Used by Non-Capital Financing Activities	<u>(570,529)</u>
CASH FLOWS FROM CAPITAL FINANCING ACTIVITIES	
Capital Grants	77,983
Memberships	26,000
Principal Payments on Notes Payable	(17,474)
Interest Expense	<u>(22,454)</u>
Net Cash Provided by Capital Financing Activities	<u>64,055</u>
NET CHANGE IN CASH	(229,606)
CASH AT BEGINNING OF YEAR	<u>415,711</u>
CASH AT END OF YEAR	<u><u>\$ 186,105</u></u>

Reconciliation of Operating Income to Net Cash Provided**by Operating Activities**

Operating Income	\$	155,170
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Adjustments to Reconcile Operating Income to Net Cash Provided by Operating Activities

Depreciation		77,720
Long-Term PERA Payable		117,336
Deferred Inflows		26,235
Deferred Outflows		(125,484)

Change in

Accounts Receivable		(6,365)
Inventory		44,941
Accounts Payable		(273)
Accrued Wages		(565)
Accrued Payroll Tax Liabilities		3,445
Sales Tax Payable		5,416
Accrued Vacation		7,598
Customer Deposits		18,250

Cash Provided by Operating Activities	\$	<u>323,424</u>
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Reconciliation to Statement of Net Position

Unrestricted	\$	15,770
Restricted - USDA RUS		74,420
Customer Deposits		95,915

Total Cash and Cash Equivalents	\$	<u>186,105</u>
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Supplemental Cash Flow Disclosures

Cash Paid for Interest	\$	22,454
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OTIS MUTUAL DOMESTIC WATER CONSUMERS AND SEWAGE WORKS ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2017

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization - Otis Mutual Domestic Water Consumers and Sewage Works Association (Association) is a Mutual Domestic Water Association established for the purpose of constructing, maintaining and operating a water and wastewater system for the members of the Association in the Otis community in southern Eddy County of New Mexico. The Board of Directors consists of five members elected by the membership. The Board shall appoint qualified personnel to guide and direct the operations of the Association, and to approve all major contracts, capital outlay, etc. involving the Association. The Association was initially incorporated as a co-operative association. The Board of Directors changed the organization type from a not-for-profit cooperative to a non-profit special-purpose government association under the Sanitary Projects Act (SPA), NMSA 3-29-1 through 3-29-20, effective July 1, 2005.

An Attorney General's (AG) opinion (90-30, dated December 27, 1990) concluded that entities created pursuant to the SPA are subject to the New Mexico Audit Act. Another AG opinion (68-38) states Mutual Domestic Water Associations (MDWAs) under the SPA Act are created for "one purpose only, and that is to establish and maintain a water system." Further it concluded MDWAs are not municipal corporations. HB 297, enacted during the 2009 legislative session, exempts MDWAs from being subject to ad valorem taxes.

Attorney General Opinion 06-02 determined that MDWAs created pursuant to the SPA are public bodies/political subdivisions, whose revenues are "public money" and they have statutory responsibilities to abide by, such as the Open Meetings Act, the Inspection of Public Records Act, the Procurement Code, and the Per Diem and Mileage Act. Since MDWAs have officially been determined to be governmental nonprofit organizations, their financial statements follow the format prescribed for special purpose government entities engaged only in business-type activities as described in GASB 34, paragraph 138

Under the guidelines of GASB 14, The Association is not considered a component unit or subdivision of a governmental entity, nor does it have any component units. This conclusion was reached because the Association was converted from a cooperative to an MDWA, pursuant to NMSA 3-29-20, by a vote of the Board of Directors rather than through legislative action or action by the entire membership; it does not have the ability to levy taxes but it does have the ability to set and change rates for service, and it is not required to file not-for-profit tax returns.

In June, 2009, the Board of Directors and the general membership approved a change in the bylaws which reclassifies how the Association records the \$5,200 initial membership purchase amount. Bona fide occupants and residents within and in the vicinity of the community of Otis, New Mexico may apply to become members by paying the \$5,200 non-refundable membership fee and be approved by the Board of Directors. The rights, privileges and obligations of the members are equal. No capital stock is authorized nor issued.

Basis of Presentation - The Association's basic financial statements are presented on the full accrual basis of accounting and conform to accounting principles generally accepted in the United States of America. The accounts of the Association are organized on the basis of one fund that is considered a separate accounting entity. All assets, liabilities and deferred outflows and inflows of resources associated with the operations are included on the statement of net position. Government resources are allocated to and accounted for in the fund based upon the purpose for which spending activities are controlled. In this report, the fund is presented in the financial statements as a proprietary fund.

OTIS MUTUAL DOMESTIC WATER CONSUMERS AND SEWAGE WORKS ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2017

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Cont.)

The proprietary fund is used to account for operations (a) that are financed and operated in a manner similar to private business enterprise - where the intent of the governing body is that the costs (expenses including depreciation) of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges; or (b) where the governing body has decided that periodic determination of revenues earned, expenses incurred, and/or net income is appropriate for capital maintenance, public policy, management control, accountability or other purposes.

The accounting and financial reporting treatment applied to the Association is determined by its measurement focus. The transactions of the Association are accounted for on the accrual basis flow of economic resources measurement focus. With this measurement focus, all net position (i.e., total assets and deferred outflows less total liabilities and deferred inflows) are segregated into net investment in capital assets, restricted, and unrestricted components. This basis of accounting recognizes revenues in the accounting period in which they are earned and become measurable and expenses in the accounting period in which they are incurred and become measurable. Revenue from grants, entitlements and donations are recognized in the fiscal year in which all eligibility requirements have been satisfied.

Deposits and Investments - For purposes of the statement of cash flows, the Association's cash and cash equivalents are considered to be cash on hand, demand deposits and short-term investments with original maturities of three months or less from the date of acquisition.

Restricted Cash - The Association restricts a compensating amount of cash equal to the amount of the customer deposits held on hand. These reserves are not required but are separated by management.

A separate Construction Account was established as required by the United States Department of Agriculture (USDA) into which the proceeds of the loan and grant proceeds from the USDA-RUS are deposited. Withdrawals from the Construction Account were and shall be made only on checks signed by the manager of the Association as authorized by the Board from time to time, and with prior concurrence of the USDA-RUS. When all construction costs have been paid in full, any balance remaining in the Construction Account may be applied on the loan or used for other authorized purposes that have been approved by the USDA-RUS and the Construction Account shall be closed.

Use of Restricted Cash - When the Association incurs an expense for which it may use either restricted or unrestricted assets, it uses the restricted assets first whenever they will have to be returned if they are not used.

Grants and Contributions - The Association receives grants as well as contributions in the course of operations. Revenues from grants and contributions (including contributions of capital assets) are recognized when all eligibility requirements, including time requirements, are met. Grants and contributions may be restricted for either specific operating purposes or for capital purposes. Amounts that are unrestricted or that are restricted to a specific operating purpose are reported as non-operating revenues. Amounts restricted to capital acquisitions are reported after non-operating revenues and expenses.

Receivables - Substantially all of the Association's outstanding receivables are due from its customers for water sales. Collateral is generally not required on receivables, but a deposit is required to activate new service.

Allowance for Doubtful Accounts - It is the opinion of management that no allowance for doubtful accounts was necessary as of June 30, 2017 because services will be disconnected should an account become delinquent.

**OTIS MUTUAL DOMESTIC WATER CONSUMERS AND SEWAGE WORKS ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2017**

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Cont.)

Concentration of Credit Risk - The Association grants credit without collateral to its customers for its services, but the customers are subject to service termination if the receivables are not settled within a specified time frame. The customer deposits held by the Association also help minimize the credit risk.

Inventory - Inventory includes water pipe, electronic water meters, pumps and supplies for future water system installation and repairs. Inventory is valued at the lower of cost or market on a first-in, first-out basis.

Property and Equipment - The Association's policy is to capitalize all expenditures for furniture, equipment and software in excess of \$5,000 and an estimated useful life in excess of one year. Such assets are recorded at historical cost or estimated historical cost if purchased or constructed. Items with a cost of less than \$5,000 are expensed in the year of acquisition, except for costs associated with the installation of new water lines, pumps and tanks, which are capitalized. Expenditures related to the routine repairs and maintenance of the existing water system are expensed in the current period.

Assets acquired under capital leases are amortized over the life of the respective leases or the service lives of the assets using the straight-line method and the amortization is included with depreciation expense. Renovations to the buildings, infrastructure and land improvements that significantly increase the value or extend the useful life of the structure are capitalized. Interest paid on loans for construction purposes is capitalized until the asset becomes available for use and amortized over the life of the related asset. Land owned by the Association is always capitalized. Water rights considered to have an indefinite life are not subject to amortization under GASB No. 51.

Assets of the Association are depreciated using the straight-line method over the following estimated useful lives:

Assets	Years
Leasehold Improvements	40
Water Lines, Pumps, and Tanks	20-40
Office and Maintenance Equipment	5-7
Vehicles	5

Analysis of Impairments - Management reviews long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Impairment is determined based on comparison of future cash flows to the recorded value of the assets. Impairment losses are measured based on the fair value of the impaired assets. No such impairment losses were recorded during the year ended June 30, 2017.

Customer Deposits - The Association requires a deposit to establish service for the customer. Deposits are not considered revenue for the Association unless or until the customer closes their account, at which time any remaining balance due on the account is deducted from the deposit and the customer is refunded the excess.

Net Position - Net position represents the difference between assets plus deferred outflows and liabilities plus deferred inflows. Net investment in capital assets consists of capital assets, net of accumulated depreciation, reduced by the outstanding balances of any borrowing used for the acquisition, construction or improvement of those assets, and adding back unspent proceeds. Net position is reported as restricted when there are limitations imposed on the use either through enabling legislation or through external restrictions imposed by creditors, grantors or laws or regulations of other governments. The remaining balance of the net position not falling into these categories is considered unrestricted for the Association's use.

OTIS MUTUAL DOMESTIC WATER CONSUMERS AND SEWAGE WORKS ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2017

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Cont.)

Operating and Non-operating Revenues - Revenues are classified as operating or non-operating according to the following criteria:

Operating revenue - include activities which have the characteristic of exchange transactions, such as charges for services and fees, net of any allowance for uncollectible amounts.

Non-operating revenues - include activities which have the characteristics of non-exchange transactions, such as capital grants and investment income.

Expenses - Expenses are classified as operating or non-operating according to the following criteria:

Operating expenses - include activities that have the characteristics of an exchange transaction such as employee salaries, benefits, and related expenses; maintenance, operations and contractual services; materials and supplies; office expenses; and depreciation expenses related to Association capital assets.

Non-operating expenses - include activities that have the characteristics of non-exchange transactions such as interest on capital asset-related debt and bond expenses that are defined as non-operating expenses by GASB Statement No. 9 - *Reporting Cash Flows of Proprietary and Non-expendable Trust Funds and Governmental Entities that Use Proprietary Fund Accounting*, and GASB Statement No. 34.

Advertising - Advertising costs are expensed as incurred during the fiscal year.

Budgetary Compliance - The Association's annual budget is not required to be presented to the New Mexico Department of Finance and Administration (DFA) for review, adjustment or approval as a special-purpose governmental organization organized under the SPA, however a budget is filed with the DFA in order to comply with the Colonias grant requirements.

Compensated Absences - The Association permits employees to accumulate earned but unused vacation and sick pay benefits. Vacation leave may be accumulated up to 80 hours. Upon termination, the Association will compensate an employee for unused accrued vacation leave up to a maximum of 80 hours. Accrued sick leave may be accrued and carried over, however sick leave is not paid out upon termination.

Use of Estimates - The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

Risk Management - The Association is exposed to various risks of loss from torts; theft of, damage to, and destruction of assets; business interruption; errors and omissions; employee injuries and illnesses; natural disasters; and employee health, dental, and accident benefits. Commercial insurance coverage is purchased for claims arising from such matters. Settled claims have not exceeded this commercial coverage in any preceding years.

Subsequent Events - GASB 56 requires reporting entities to disclose the date through which subsequent events have been evaluated and whether that date is the date the financial statements were issued or available to be issued. Management has evaluated subsequent events through the date of the auditor's report, which is the date the financial statements were available to be issued.

OTIS MUTUAL DOMESTIC WATER CONSUMERS AND SEWAGE WORKS ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2017

NOTE B - CASH AND CASH EQUIVALENTS

At June 30, 2017, the Association had cash and cash equivalents on deposit with local financial institutions, consisting of checking and money market accounts. Checking accounts which are required for debt service or for grant purposes are prohibited from accruing interest. Following is a schedule as of June 30, 2017, of the cash and cash equivalents.

	Bank Balance June 30, 2017	Outstanding Deposits	Outstanding Checks	Book Balance June 30, 2017
Western Commerce Bank				
Checking Account	\$ 88,698	\$ 35,315	\$ (25,382)	\$ 98,631
Money Market Account	12,215	-	-	12,215
Carlsbad National Bank				
Debt Service Reserve	74,420	-	-	74,420
USDA Construction Account	-	-	-	-
Short Lived Assets Account	<u>539</u>	<u>-</u>	<u>-</u>	<u>539</u>
Total Cash in Banks	<u>\$ 175,872</u>	<u>\$ 35,315</u>	<u>\$ (25,382)</u>	185,805
Cash on Hand				<u>300</u>
Total Cash on Books				<u>\$ 186,105</u>

As Reported in the Financial Statements:

Restricted Cash			
USDA-RUS account		\$ 74,420	
Customer Deposits		<u>95,915</u>	\$ 170,335
Unrestricted Cash			<u>15,770</u>
Total Cash on Books			<u>\$ 186,105</u>

In accordance with Section 6-10-17, NMSA 1978, deposits of public monies are required to be collateralized. Pledged collateral is required in amounts in aggregate equal to one half of the amount of uninsured public money in each account during the fiscal year. Securities which are obligations of the State of New Mexico, its agencies, institutions, counties, or municipalities or other subdivisions are accepted as security at par value; all other securities are accepted as security at market value. No security is required for the deposit of public money that is insured by the Federal Deposit Insurance Corporation.

	Western Commerce Bank	Carlsbad National Bank	Totals
Deposits:	\$ 100,913	\$ 74,959	\$ 175,872
Less FDIC Coverage	<u>(100,913)</u>	<u>(74,959)</u>	<u>(175,872)</u>
Uninsured Funds	-	-	-
Collateral Pledged by Bank	<u>267,534</u>	<u>-</u>	<u>267,534</u>
Uninsured and Uncollateralized	<u>\$ (267,534)</u>	<u>\$ -</u>	<u>\$ (267,534)</u>
50% Pledged Collateral Requirement per Statute	\$ -	\$ -	\$ -
Pledged Collateral	<u>267,534</u>	<u>-</u>	<u>267,534</u>
(Over) Under Collateralized	<u>\$ (267,534)</u>	<u>\$ -</u>	<u>\$ (267,534)</u>

OTIS MUTUAL DOMESTIC WATER CONSUMERS AND SEWAGE WORKS ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2017

NOTE B - CASH AND CASH EQUIVALENTS (Cont.)

Custodial Credit Risk - Deposits - Custodial credit risk is the risk that in the event of a bank failure, the Association's deposits may not be returned to them. The Association does not have a deposit policy for custodial credit risk other than state statutes. As of June 30, 2017, the Association did not have any cash deposits exposed to custodial credit risk before applying the pledged collateral.

Western National Bank Pledged Collateral*:	Maturity	Market Value	Par Value
GNMA # 80185	4/20/2028	\$ 23,355	\$ 22,489
SBAP Series 2009-20F	6/01/2029	182,126	167,757
FNMA #888129	2/01/2037	35,745	31,870
FHLMC #C00553	9/01/2027	10,527	9,306
FHLMC #420168	12/02/2029	<u>15,781</u>	<u>15,512</u>
Total Collateral Pledged		<u>\$ 267,534</u>	<u>\$ 246,934</u>

*All securities are held by Federal Home Loan Bank, Dallas, Texas

NOTE C - CAPITAL ASSETS

The majority of the assets of the Association are located on land not owned by the Association, but are constructed on private easements for the specific and registered use of the Association or within the public utility right-of-way associated with public roads. Depreciation expense for the fiscal year was approximately \$77,720.

Capital asset activity for the year ended June 30, 2017 was as follows:

	Balance June 30, 2016	Increases	Decreases	Balance June 30, 2017
Non-depreciable Capital Assets				
Construction in Progress	\$ 1,859,427	\$ 46,843	\$ -	\$ 1,906,270
Land and Water Rights	<u>2,229,476</u>	<u>3</u>	<u>-</u>	<u>2,229,479</u>
Total Non-depreciable Capital Assets	<u>4,088,903</u>	<u>46,846</u>	<u>-</u>	<u>4,135,749</u>
Depreciable Capital Assets				
Water System Lines	1,633,201	-	-	1,633,201
Water Wells and Tanks	1,160,045	-	-	1,160,045
Tools and Equipment	600,184	-	-	600,184
Building and Well House	<u>150,938</u>	<u>-</u>	<u>-</u>	<u>150,938</u>
Total Depreciable Capital Assets	<u>3,544,368</u>	<u>-</u>	<u>-</u>	<u>3,544,368</u>
Less Accumulated Depreciation				
Water System Lines	(1,358,883)	(11,621)	-	(1,370,504)
Water Wells and Tanks	(813,489)	(34,225)	-	(847,714)
Tools and Equipment	(521,372)	(26,502)	-	(547,874)
Building and Well House	<u>(129,598)</u>	<u>(5,372)</u>	<u>-</u>	<u>(134,970)</u>
Total Accumulated Depreciation	<u>(2,823,342)</u>	<u>(77,720)</u>	<u>-</u>	<u>(2,901,062)</u>
Total Depreciable Capital Assets, Net	<u>721,026</u>	<u>(77,720)</u>	<u>-</u>	<u>643,306</u>
Capital Assets, Net	<u>\$ 4,809,929</u>	<u>\$ (30,874)</u>	<u>\$ -</u>	<u>\$ 4,779,055</u>

OTIS MUTUAL DOMESTIC WATER CONSUMERS AND SEWAGE WORKS ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2017

NOTE D - COMPENSATED ABSENCES

Vacation and sick leave is earned by employees during the year based on time worked, is non-cumulative and considered to be a long-term liability. Vacation leave due, if any, is paid upon an employee's termination. Compensation for sick leave is limited to time off and is not monetarily compensated. The activity of the vacation leave due to employees as of June 30, 2017 is detailed below.

	Balance	Increases	Decreases	Balance	Payable
	June 30, 2016			June 30, 2017	Within One
					Year
Compensated Absences	<u>\$ 24,885</u>	<u>\$ 11,076</u>	<u>\$ (3,478)</u>	<u>\$ 32,483</u>	<u>\$ 7,755</u>

NOTE E - RELATED PARTY TRANSACTIONS

A current board member owns and operates an auto repair business located across the highway from the Association's office. As a convenience, the Association sometimes has vehicles serviced or repaired at the board member's business. Rates charged to the Association are at market rates charged to the general public and are comparable to rates charged by other auto repair businesses in the immediate area. Association members are notified of the relationship with the board member during the Association's annual meeting with the membership. Total amount paid to the board member for auto repair services for the year ended June 30, 2017 was approximately \$10,113.

Each board member maintains a utility account with the Association for water service. Monthly water usage is billed to the respective board members' accounts at the nominal approved rates and are subject to the same collections proceedings as other Association members.

NOTE F - LONG-TERM DEBT

The Association has the following long-term debt obligations as of June 30, 2017:

USDA - RUS 91-02 - The Association entered into an agreement with the United States Department of Agriculture's Rural Utilities Services on July 31, 2012, for water system improvements, which includes the acquisition of land right-of-way easements, engineering and design, water distribution system improvements, and equipment. The original amount of the note was \$397,000, bearing 3.50% interest. Principal and interest payments of \$1,541 are due monthly, with the note maturing in July, 2054. Net revenues from water sales have been pledged to the repayment of the principal and interest.

NMED - RIP 2012-03 - The Association entered into an agreement with the New Mexico Environment Department on February 28, 2012, for improvements to the water distribution system. The original amount of the note was approximately \$313,875, bearing 3.00% interest. Twenty principal and interest payments of approximately \$21,097 are due annually, with the note maturing in March, 2034. Net revenues from water sales have been pledged for the payment of the loan.

**OTIS MUTUAL DOMESTIC WATER CONSUMERS AND SEWAGE WORKS ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2017**

NOTE F - LONG-TERM DEBT (Cont.)

NMFA - CIF-2772 - The Association entered into an agreement with the New Mexico Finance Authority on November 15, 2013 for construction of line extensions and additional capacity for the Association. The original amount of the note was \$29,181 and is non-interest bearing. Principal payments of \$1,493 on the note are due annually on June 1. The note matures June, 2033. The Association has pledged net revenues from the water utility system to the payment of the loan.

The Association paid approximately \$22,454 in interest expense and finance charges, of which \$22,116 was attributed to long-term obligations. The remaining \$338 of nominal interest and finance charges paid was expensed when incurred.

Long-term debt activity for the year ended June 30, 2017 was as follows:

Obligation	Balance June 30, 2016	Increases	Decreases	Balance June 30, 2017	Due Within One Year	Interest Expense
USDA-RUS 91-02	\$ 385,464	\$ -	\$ (5,082)	\$ 380,382	\$ 5,143	\$ 13,411
NMED-RIP 2012-03	290,162	-	(12,392)	277,770	12,764	8,705
NMFA CIF-2772	<u>25,382</u>	<u>-</u>	<u>-</u>	<u>25,382</u>	<u>2,986</u>	<u>-</u>
Total Long-term Debt	<u>\$ 701,008</u>	<u>\$ -</u>	<u>\$ (17,474)</u>	<u>\$ 683,534</u>	<u>\$ 20,893</u>	<u>\$ 22,116</u>

Long-term debt service requirements to maturity are as follows:

Fiscal Year Ending June 30,	Principal	Interest	Total
2018	\$ 20,893	\$ 21,682	\$ 42,575
2019	19,966	21,116	41,082
2020	20,550	20,532	41,082
2021	21,152	19,930	41,082
2022	21,774	19,308	41,082
2023-2027	118,906	86,506	205,412
2028-2032	137,697	67,715	205,412
2033-2037	88,499	47,650	136,149
2038-2042	55,541	36,919	92,460
2043-2047	66,146	26,314	92,460
2048-2052	78,776	13,684	92,460
2053-2054	<u>33,634</u>	<u>1,412</u>	<u>35,046</u>
Totals	<u>\$ 683,534</u>	<u>\$ 382,768</u>	<u>\$ 1,066,302</u>

NOTE G - RETIREE HEALTH CARE ACT CONTRIBUTIONS

The Retiree Health Care Act (10-7C-1 to 10-7C-16, NMSA 1978) provides comprehensive care group health insurance for persons who have retired from certain public service in New Mexico. The Association has elected not to participate in the program.

OTIS MUTUAL DOMESTIC WATER CONSUMERS AND SEWAGE WORKS ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2017

NOTE H - PERA PENSION PLAN

Pensions - For purposes of measuring the net pension liability, deferred outflows of resources and deferred inflows of resources related to pensions, and pension expense, information about the fiduciary net position of the New Mexico Public Employees Retirement Association (PERA) and additions to/deductions from PERA's fiduciary net position have been determined on the same basis as they are reported by PERA, on the economic resources measurement focus and accrual basis of accounting. For this purpose, benefit payments (including refunds of employee contributions) are recognized when due and payable in accordance with the benefit terms. Investments are reported at fair value.

Plan Description - This fund has six divisions of members, including State General, State Police/Adult Correction Officers, Municipal General, Municipal Police/Detention Officers, Municipal Fire, and State Legislative Divisions, and offers 24 different types of coverage within the PERA plan. All assets accumulated may be used to pay benefits, including refunds of member contributions, to any of the plan members or beneficiaries, as defined by the terms of this plan.

Certain coverage plans are only applicable to a specific division. Eligibility for membership in the PERA Fund is set forth in the Public Employees Retirement Act (Chapter 10, Article 11, NMSA 1978). Except as provided for in the Volunteer Firefighters Retirement Act (10-11A-1 to 10-11A-7, NMSA 1978), the Judicial Retirement Act (10-12B-1 to 10-12B-19, NMSA 1978), the Magistrate Retirement Act (10-12C-1 to 10-12C-18, NMSA 1978), and the Educational Retirement Act (Chapter 22, Article 11, NMSA 1978), and the provisions of Sections 29-4-1 through 29-4-11, NMSA 1978 governing the State Police Pension Fund, each employee and elected official of every affiliated public employer is required to be a member in the PERA Fund. PERA issues a publicly available financial report and a comprehensive annual financial report that can be obtained at <http://saonm.org> using the Audit Report Search function for Agency 366-B.

Benefits Provided - For a description of the benefits provided and recent changes to the benefits see Note I in the PERA audited financial statements for the fiscal year ended June 30, 2016 available at:
[www.pera.state.nm.us/pdf/AuditFinancialStatements/366 Public Employees Retirement Association 2016.pdf](http://www.pera.state.nm.us/pdf/AuditFinancialStatements/366%20Public%20Employees%20Retirement%20Association%202016.pdf).

Contributions - The contribution requirements of defined benefit plan members and the Association are established in state statute under Chapter 10, Article 11, NMSA 1978. The contribution requirements may be amended by acts of the legislature. For the employer and employee contribution rates in effect for FY 16 for the various PERA coverage options, for both Tier I and Tier II, see the tables available in the note disclosures on pages 29 through 31 of the PERA FY16 annual audit report at [http://osanm.org/media/audits/366 Public Employees Retirement Association 2016.pdf](http://osanm.org/media/audits/366%20Public%20Employees%20Retirement%20Association%202016.pdf). The PERA coverage option that applies to the Association is the General Division. Statutorily required contributions to the pension plan from the Association were \$23,153 and employer paid member benefits that were "picked up" by the employer were \$0 for the year ended June 30, 2017.

Pension Liabilities, Pension Expense, and Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions - The PERA pension liability amounts, net pension liability amounts, and sensitivity information were based on an annual actuarial valuation performed as of June 30, 2015. The PERA pension liability amounts for each division were rolled forward from the valuation date to the Plan year ending June 30, 2015, using generally accepted actuarial principles. Therefore, the employer's portion was established as of the measurement date June 30, 2015.

The assets of the PERA fund are held in one trust, but there are six distinct membership groups (municipal general members, municipal police members, municipal fire members, state general members, state police members and legislative members) for whom separate contribution rates are determined each year pursuant to chapter 10, Article 11 NMSA 1978. Therefore, the calculations of the net pension liability, pension expense and deferred inflows and outflows were performed separately for each of the membership groups. The Association's proportion of the net pension liability for each membership group that the employer participates in is based on the employer contributing entity's percentage of that membership group's total employer contributions for the fiscal year ended June 30, 2016.

OTIS MUTUAL DOMESTIC WATER CONSUMERS AND SEWAGE WORKS ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2017

NOTE H - PERA PENSION PLAN (Cont.)

Only employer contributions for the pay period end dates that fell within the period of July 1, 2015 to June 30, 2016 were included in the total contributions for a specific employer. Regular and any adjustment contributions that applied to FY 2016 are included in the total contribution amounts. In the event that an employer is behind in reporting to PERA its required contributions, an estimate (receivable) was used to project the unremitted employer contributions. This allowed for fair and consistent measurement of the contributions with the total population. This methodology was used to maintain consistent measurement each year in determining the percentages to be allocated among all the participating employers.

PERA Fund Division – General - At June 30, 2017, the Association reported a liability of \$431,369 for its proportionate share of the net pension liability. At June 30, 2017, the Association's proportion was 0.0270%, which was slightly less than its 0.0308% proportion measured as of June 30, 2016.

For the year ended June 30, 2017, the Association recognized PERA Fund - General, pension expense of \$41,249. At June 30, 2017, the Association reported PERA Fund Division - General deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

	Deferred Outflows of Resources	Deferred Inflows of Resources
Changes in Assumption	\$ 25,295	\$ 72
Changes in Proportion	79,371	30,024
Differences Between Expected and Actual Experience	21,553	4,210
Contributions Subsequent to Measurement Date	<u>23,153</u>	<u>-</u>
Totals	<u>\$ 149,372</u>	<u>\$ 34,306</u>

For the General Division, \$23,153 is reported as deferred outflows of resources related to pensions resulting from Association contributions subsequent to the measurement date June 30, 2016 and will be recognized as a reduction of the net pension liability in the year ended June 30, 2018. Other amounts reported as deferred outflows of resources and deferred inflows of resources related to pensions will be recognized in pension expense as follows:

Year Ended	Net Amount
June 30,	
2018	\$ 16,872
2019	16,872
2020	38,962
2021	<u>19,207</u>
Totals	<u>\$ 91,913</u>

Actuarial Assumptions - As described above, the PERA Fund member group pension liabilities and net pension liabilities are based on actuarial valuations performed as of June 30, 2015 for each of the membership groups. Then each PERA Fund member group pension liability was rolled forward from the valuation date to the Plan year ending June 30, 2015 using generally accepted actuarial principles. There were no significant events or changes in benefit provisions that required an adjustment to the roll-forward liabilities as of June 30, 2015. These actuarial methods and assumptions were adopted by the Board for use in the June 30, 2015 actuarial valuation.

OTIS MUTUAL DOMESTIC WATER CONSUMERS AND SEWAGE WORKS ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2017

NOTE H - PERA PENSION PLAN (Cont.)

Actuarial Valuation Date	June 30, 2015
Actuarial Cost Method	Entry Age Normal
Amortization Method	Level Percentage of Pay, Open
Amortization Period	Solved for Based on Statutory Rates
Asset Valuation Method	Fair Value
Actuarial Assumptions:	
Investment Rate of Return	7.48% Annual Rate, Net of Investment Expense
Projected Benefit Payment	100 Years
Payroll Growth	2.75% Annual Rate for First 10 Years, then 3.25% Annual Rate
Projected Salary Increases	2.75% to 14.25% Annual Rate
Included Inflation at	2.75% Annual Rate for First 10 Years, then 3.25% Annual Rate
Mortality Assumption	RP-2000 Mortality Tables
Experience Study Dates	July 1, 2008 – June 30, 2013 (demographic) July 1, 2010 – June 30, 2015 (economic)

The long-term expected rate of return on pension plan investments was determined using a statistical analysis in which best-estimate ranges of expected future real rates of return (expected returns, net of pension plan investment expense and inflation) are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and by adding expected inflation. The target asset allocation and most recent best estimates of arithmetic real rates of return for each major asset class are summarized in the following table:

ALL FUNDS – Asset Class	Target Allocation	Long-Term Expected Real Rate of Return
Global Equity	43.5%	7.39 %
Risk Reduction & Mitigation	21.5	1.79
Credit Oriented Fixed Income	15.0	5.77
Real Assets to Include Real Estate Equity	<u>20.0</u>	7.35
Totals	<u>100.0%</u>	

Discount Rate - The discount rate used to measure the total pension liability was 7.25% for the first ten years (select period) then 7.75% for all other years (ultimate). The equivalent blended rate of 7.48% will be used to measure the total pension liability. The projection of cash flows used to determine the discount rate assumed that future contributions will be made in accordance with statutory rates. On this basis, the pension plan's fiduciary net position together with the expected future contributions are sufficient to provide all projected future benefit payments of current plan members as determined in accordance with GASB 67. Therefore, the 7.48% assumed long-term expected rate of return on pension plan investments was applied to all periods of projected benefit payments to determine the total pension liability.

Sensitivity of the Association's Proportionate Share of the Net Pension Liability to Changes in the Discount Rate - The following table shows the sensitivity of the net pension liability to changes in the discount rate. In particular, the table presents the Association's net pension liability in each PERA Fund Division in which the Association participates, under the current single rate assumption, as if it were calculated using a discount rate one percentage point lower (6.48%) or one percentage point higher (8.48%) than the single discount rate.

	1% Decrease (6.48%)	Current Discount Rate (7.48%)	1% Increase (8.48%)
Proportionate Share of Net Pension Liability	<u>\$ 643,133</u>	<u>\$ 431,369</u>	<u>\$ 255,722</u>

OTIS MUTUAL DOMESTIC WATER CONSUMERS AND SEWAGE WORKS ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2017

NOTE H - PERA PENSION PLAN (Cont.)

Pension Plan Fiduciary Net Position - Detailed information about the pension plan's fiduciary net position is available in the separately issued FY16 PERA financial report. The report is available at: www.pera.state.nm.us/publications.html.

Payables to the Pension Plan - At June 30, 2017, the Association had no outstanding contributions to the pension plan which is reported within current liabilities on the balance sheet.

NOTE I - COMMITMENTS, CONTINGENCIES, AND SUBSEQUENT EVENTS

NMED 14-1625-STB Water System Phase 6 Improvements Grant - The Association has received approval for a \$200,000 grant from the New Mexico Environment Department for engineering and professional services to design water distribution line connections to eliminate dead-end lines. Additional funding would be needed for construction. Approximately \$59,557 has been disbursed by NMED through the 2017 fiscal year for engineering costs on the project. The Association has until June 30, 2018 to spend the remaining \$140,443 before the remaining balance reverts back to the State.

NMED 15-0503-STB Water Mains Phase 6 Improvements Grant - The Association has received approval for a \$50,000 grant from the New Mexico Environment Department for engineering and professional services to design water distribution line connections to eliminate dead-end lines. Additional funding would be needed for construction. Approximately \$7,541 has been disbursed by NMED in the 2017 fiscal year for engineering costs on the project. The Association has until June 30, 2019 to spend the remaining \$42,459 before the remaining balance reverts back to the State.

NMFA 3513-CIF - Colonias Infrastructure Project - In October 2016, The Association entered into an agreement with the Colonias Infrastructure Board, NMFA, and the Rural Community Assistance Corporation (RCAC), a branch of the United States Department of Agriculture Rural Development, for continued improvements of the water system. The agreement calls for a 90/10 grant/loan total of \$497,153 with a grant amount of \$447,438 and a loan amount of \$49,715. The Association has yet to draw on the loan funds. Reversion date on this agreement is June 30, 2019.

Employee Theft - On April 18, 2017, an employee of the Association resigned and admitted to using the Association's credit card to misappropriate cash funds over a two-year period. Funds misappropriated include approximately \$12,087 in the 2015 fiscal year, \$274,927 in the 2016 fiscal year and \$570,529 in the 2017 fiscal year for an approximate loss amount of \$857,543 reported as Employee Theft Receivable on the statement of net position. The funds in question were from cash reserves the Association had accumulated over the years designated for upgrades and repairs to water towers and other infrastructure improvements, and did not affect or include Federal Colonias or Southeastern New Mexico Economic Development District funding.

The underlying documentation and information has been turned over to the Federal Bureau of Investigation, Office of the State Auditor and the District Attorney's office for review and appropriate action. The Association submitted a notice of claim to its insurance company for \$500,000, the maximum amount of policy coverage, which was received in September 2017.

REQUIRED SUPPLEMENTARY INFORMATION

**OTIS MUTUAL DOMESTIC WATER CONSUMERS AND SEWAGE WORKS ASSOCIATION
SCHEDULES OF PROPORTIONATE SHARE OF NET PENSION
LIABILITY AND REQUIRED CONTRIBUTIONS
LAST 10 FISCAL YEARS***

Actuarial Valuation Date	6/30/15	6/30/16	6/30/17
Schedules of Proportionate Share of Net Pension Liability			
Proportion of Net Pension Liability	0.0308%	0.0308%	0.0270%
Net Pension Liability	240,273	314,033	431,369
Annual Covered Payroll	291,263	289,005	239,925
NPL as Percentage of Covered Payroll	82.49%	108.66%	179.79%
Fiduciary Net Position as a Percentage of Total Pension Liability	81.29%	76.99%	69.18%

Schedules of Required Contributions			
Contractually Required Contributions	24,347	23,888	23,153
Contributions Made	24,347	23,888	23,153
Contributions as Percentage of Covered Payroll	8.36%	8.27%	9.65%

*The amounts presented above for trend analysis are determined as of June 30. These schedules are presented to illustrate the requirement to show information for 10 years. However, until a full 10-year trend is compiled, the Association will present information for those years for which information is available.

**OTIS MUTUAL DOMESTIC WATER CONSUMERS AND SEWAGE WORKS ASSOCIATION
NOTES TO REQUIRED SUPPLEMENTARY INFORMATION
YEAR ENDED JUNE 30, 2017**

Changes of Benefit Terms - The PERA Fund COLA and retirement eligibility benefits changes in recent years are described in Note 1 of the PERA FY16 audit available at:

http://www.pera.state.nm.us/pdf/AuditFinancialStatements/366_Public_Employees_Retirement_Association_2016.pdf.

Changes of Assumptions - The Public Employees Retirement Association (PERA) of New Mexico Annual Actuarial Valuation as of June 30, 2016 report is available at:

http://www.pera.state.nm.us/pdf/Investments/RetirementFundValuationReports/6-30-2016%20PERA%20Valuation%20Report_FINAL.pdf.

The summary of Key Findings for the PERA Fund (on page 2 of the report) states “based on a recent experience study for the five-year period ending June 30, 2015, the economic and demographic assumptions were updated for this valuation. The changes in assumptions resulted in a decrease of \$30.8 million to Fund liabilities and an increase of 0.13% to the funded ratio”.

For details about changes in the actuarial assumptions, see Appendix B on page 60 of the report.

SUPPLEMENTARY INFORMATION

OTIS MUTUAL DOMESTIC WATER CONSUMERS AND SEWAGE WORKS ASSOCIATION
SCHEDULE OF REVENUES, EXPENSES AND CHANGES IN
NET POSITION - BUDGET AND ACTUAL (NON-GAAP BASIS)
YEAR ENDED JUNE 30, 2017

	<u>Original Budget</u>	<u>Final Budget</u>	<u>Actual</u>	<u>Variance Favorable (Unfavorable)</u>
REVENUES				
Charges for Services	\$ 1,279,094	\$ 1,279,094	\$ 1,241,765	\$ (37,329)
Late Charges and Service Fees	-	-	17,993	17,993
Rental and Lease Income	-	-	7,704	7,704
Total Operating Revenues	<u>1,279,094</u>	<u>1,279,094</u>	<u>1,267,462</u>	<u>(11,632)</u>
EXPENDITURES				
Current				
Personnel Services	462,438	462,438	466,738	(4,300)
Utilities	104,280	104,280	99,366	4,914
Maintenance, Materials and Supplies	270,858	270,858	172,043	98,815
Other Expenditures	50,902	50,902	205,891	(154,989)
Depreciation	124,938	124,938	-	124,938
Capital Outlay	<u>-</u>	<u>-</u>	<u>46,846</u>	<u>(46,846)</u>
Total Operating Expenses	<u>1,013,416</u>	<u>1,013,416</u>	<u>990,884</u>	<u>22,532</u>
Operating Gain	<u>265,678</u>	<u>265,678</u>	<u>276,578</u>	<u>10,900</u>
NONOPERATING REVENUES (EXPENSES)				
Principal Payments on Debt	-	-	(17,474)	(17,474)
Interest Expense and Administrative Fees	-	-	(22,454)	(22,454)
Employee Theft Receivable	-	-	(570,529)	(570,529)
Capital Grants	-	-	77,983	77,983
Memberships	-	-	26,000	26,000
Interest Income	-	-	290	290
Total Nonoperating Revenues (Expenses)	<u>-</u>	<u>-</u>	<u>(506,184)</u>	<u>(506,184)</u>
Net Change in Net Position	<u>265,678</u>	<u>265,678</u>	<u>(229,606)</u>	<u>(495,284)</u>
Cash - Beginning of Year	<u>415,711</u>	<u>415,711</u>	<u>415,711</u>	<u>-</u>
Cash - End of Year	<u>\$ 681,389</u>	<u>\$ 681,389</u>	<u>\$ 186,105</u>	<u>\$ (495,284)</u>
Reconciliation to GAAP Basis				
Change in Net Position - Budget Basis			\$ (229,606)	
Capital Outlay			46,846	
Depreciation			(77,720)	
Principal Payments			17,474	
Net Changes in Deferred Inflows and Outflows			99,249	
Net Changes in Net Pension Liability			(117,336)	
Employee Theft Receivable			570,529	
Change in:				
Accounts Receivable			6,365	
Inventory			(44,941)	
Accounts Payable			273	
Accrued Wages			565	
Accrued Payroll Tax Liabilities			(3,445)	
Sales Tax Payable			(5,416)	
Accrued Vacation			(7,598)	
Customer Meter Deposits			(18,250)	
Change in Net Position - GAAP Basis			<u>\$ 236,989</u>	

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

INTERNAL CONTROL AND COMPLIANCE



SCOTT NORTHAM, CPA, PC
Certified Public Accountants

**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***

Timothy Keller, New Mexico State Auditor, and
Board of Directors of
Otis Mutual Domestic Water Consumers
and Sewage Works Association
Otis, New Mexico

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 General of the United States, the financial statements of the business-type activities of Otis Mutual Domestic Water Consumers and Sewage Works Association (Association) as of and for the year ended June 30, 2017, and the related notes to the financial statements, which comprise the Association's basic financial statements, and have issued our report thereon dated November 17, 2017. Our report opinion is qualified on such financial statements because management has not adopted an internal control methodology sufficient enough to prevent or detect fraudulent activities by Association personnel.

Internal Control over Financial Reporting

In planning and performing our audit of the financial statements, we considered the City of X, State Y'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 and therefore, material weaknesses or significant deficiencies may exist that were not identified. We did identify certain deficiencies in internal control, described in the accompanying schedule of findings and responses costs that we consider to be material weaknesses as items 2017-001 (2012-001) and 2017-002 (2016-001).

Compliance and Other Matters

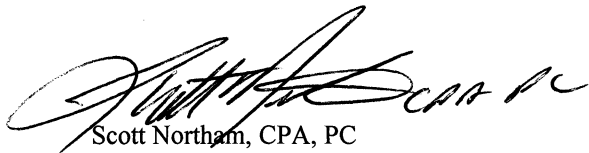
As part of obtaining reasonable assurance about whether the Association's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material 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 Section 12-6-5 NMSA 1978 which are described in the accompanying schedule of findings and responses as items 2017-003 (2016-004), 2017-004, 2017-005, 2017-006, and 2017-007.

Association's Responses 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 Association'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 Association's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.



Scott Northam, CPA, PC
Ruidoso, New Mexico
November 17, 2017

OTIS MUTUAL DOMESTIC WATER CONSUMERS AND SEWAGE WORKS ASSOCIATION
SCHEDULE OF FINDINGS AND RESPONSES
JUNE 30, 2017

2017-001 (2012-001) - Segregation of Duties (Revised and Repeated) – Material Weakness

CONDITION - The Association has a limited segregation of duties due to the limited amount of office personnel, resulting in the office staff being responsible for several incompatible duties and responsibilities without proper supervision.

PROGRESS ON RESOLVING PRIOR YEAR FINDING - During the prior and current fiscal years, the former office manager had unsupervised online access to the credit card account and checking and money market bank accounts. This deficiency in segregation of duties allowed the unauthorized access and misappropriation of assets of approximately \$857,543.

CRITERIA - Segregation of certain specific accounting and administrative functions among employees is critically needed to minimize concentration of internal controls and reduce the possibility of overriding of controls.

CAUSE - Personnel and budget limitations relegated the Association to consolidate some incompatible accounting and administrative functions without adequate oversight or supervision.

EFFECT - The lack of proper segregation of duties allowed the office manager to misappropriate a material amount of cash assets.

RECOMMENDATION - The Association should thoroughly analyze the responsibilities of the office employees and their access to liquid assets and review the controls in place to reduce the effect of the lack of segregation of duties.

MANAGEMENT RESPONSE AND PLANNED CORRECTIVE ACTION - The Association board members contracted with a local accounting firm in April 2017 to reconcile the bank statements to the accounting records, while restricting an office staff employee to make deposits and input and write checks for board members to sign. The online access to the bank accounts has been shuttered and the Association credit card cancelled.

2017-002 (2016-001) - Internal Control Deficiencies (Revised and Repeated) - Material Weakness

CONDITION - During our audits of the 2016 and 2017 fiscal years, we noted the following issues:

- The Association did not have effective procedures and policies in place to be able to analyze and review the financial operations and conditions of the Association at any given time.
- The Association lacked a process to review and reconcile financial statements on a monthly basis.
- The Association was not performing a secondary review of bank reconciliations being performed by the office manager.
- The Association lacked formal policies and procedures regarding online bank transfers and online bill payments.

PROGRESS ON RESOLVING PRIOR YEAR FINDING - As the incident with the office manager was discovered in April 2017, management did not have much opportunity to resolve the finding during the 2017 fiscal year. However, steps have been made to eliminate the identified weaknesses in the internal control system and implemented measures to strengthen monthly financial monitoring to prevent future incidents.

OTIS MUTUAL DOMESTIC WATER CONSUMERS AND SEWAGE WORKS ASSOCIATION
SCHEDULE OF FINDINGS AND RESPONSES
JUNE 30, 2017

2017-002 (2016-001) - Internal Control Deficiencies (Revised and Repeated) - Material Weakness (Cont.)

CRITERIA - *The Codification of Statements on Auditing Standards* (SAS AU) paragraph 110.03 states that the financial statements are the Board of Directors' responsibility. The Board is responsible for adopting sound accounting policies, and for establishing and maintaining internal control that will, among other things, initiate, authorize, record, process, and report transactions (as well as events and conditions) consistent with management's assertions embodied in the financial statements. The Association shall establish and maintain an internal control structure to provide management with reasonable assurance that assets are safe-guarded against loss from unauthorized use or disposition, and that transactions are executed in accordance with management's authorization and recorded properly to permit the preparation of financial statements in accordance with GAAP.

CAUSE - The Association did not have policies and procedures to ensure internal controls were in place and working properly or effectively.

EFFECT - The inadequate internal control structure allowed the office manager to circumvent controls and misappropriate a material amount of assets for an extended period.

RECOMMENDATIONS - The Association should begin preparing and independently reviewing formal bank reconciliations. The Association should also review financial statements that are prepared directly from the underlying accounting records on a monthly basis.

MANAGEMENT RESPONSE AND PLANNED CORRECTIVE ACTION – Tighter controls have been initiated by the Board as a result of the misappropriation within the business office. Monthly monitoring of the accounting records is performed by the local accounting firm and presented at monthly board meetings. The Association's attorney now attends the monthly board meetings. Although previous board meetings before the employee theft were publicly posted, virtually no members attended the meetings. Board meetings are now being held in the local community center to accommodate member attendance. This finding has been substantially resolved by November 2017.

2017-003 (2016-004) - Budgetary Completeness and Accuracy – Compliance (Repeated and Revised)

CONDITION - The Sanitary Projects Act exempts the Association from being required to submit an annual budget to the Department of Finance and Administration, but the Association is required to submit a simplified budget to the DFA as a condition of the UDSA-RUS Colonias Grant. The original budget summary submitted and approved by the DFA and adopted by the Association does not reconcile to the detailed information within the budget submission. The total budgeted expenses summary versus detail was understated by approximately \$122,726.

PROGRESS ON RESOLVING PRIOR YEAR FINDING - No progress was made on this finding over the prior fiscal year. The same former employee who prepared the FY16 budget spreadsheet also prepared the FY17 budget spreadsheet. The spreadsheet contained the same formula error from year to year with no corrections. The DFA approved the submitted budget without addressing the error in either year.

CRITERIA - Section 6-6-6 NMSA, 1978, requires local public bodies to adhere to the legally adopted budget. To ensure budgetary compliance to process for monitoring, the budget must include the correct budget amounts. Reconciliation of the legally adopted budget to actual revenues and expenses should be used to monitor the budget and is critical to ensuring budgetary compliance.

CAUSE - The Association did not place a priority on budgetary compliance since it normally does not have an annual requirement.

**OTIS MUTUAL DOMESTIC WATER CONSUMERS AND SEWAGE WORKS ASSOCIATION
SCHEDULE OF FINDINGS AND RESPONSES
JUNE 30, 2017**

2017-003 (2016-004) - Budgetary Completeness and Accuracy - Compliance (Repeated and Revised)

EFFECT - Not properly reporting budgetary information for grant purposes could put the current and future grant awards at risk.

MANAGEMENT RESPONSE AND PLANNED CORRECTIVE ACTION - The budget spreadsheet prepared by the new staff bookkeeper for the Fiscal 2018 budget removed the formula inconsistency and properly calculated ending budget line item amounts. The budget has been sent to DFA and has been approved for the 2018 fiscal year. The office bookkeeper is working on a more detailed budget presentation for the 2019 fiscal year. This finding should be resolved by July 2018.

2017-004 – Grant Management – Compliance

CONDITION - The Association employee coordinating the federal grants files resigned abruptly during the fiscal year. Other than an employee from the engineering vendor working on keeping the grant project files current, the Association does not have a sufficiently trained employee to assume the duties of grant coordinator.

CRITERIA - Federal grants require constant monitoring to ensure compliance to the contract.

CAUSE - The Association relied on one employee to monitor and coordinate the grant without adequate cross-training support or assistance.

EFFECT - The Association could not properly determine the status of the grant or loan obligations without assistance from the engineering consultant.

RECOMMENDATION - The Association should designate another office employee to be trained to handle the grant coordinator duties to reduce reliance on the engineer firm's staff.

MANAGEMENT'S RESPONSE AND PLANNED CORRECTIVE ACTION - The general manager is working with the office staff to determine which employee would be appointed to assume the grant file responsibilities. The decision should be made before the end of December 2017, which would substantially resolve this finding.

2017-005 – PERA Late Remittance – Compliance

CONDITION - A review of the twenty-six (26) PERA reports for the respective pay periods in the fiscal year noted five (5) reports were filed outside of the required filing period

CRITERIA - State Statute 10-11-126-A NMSA 1978 requires public employers to remit contributions in accordance with the procedures and schedules established by PERA. Per Section 2 of the PERA Employer Guide, contributions are due no later than the fifth business day after the payday applicable to the payroll period being reported. If an employer fails to make the required member deductions and employer contributions, the employer will be responsible for correcting the omission and responsible for any assessed interest charges.

CAUSE - Late filings were the result of office personnel turnover and inexperience of the replacement employee.

EFFECT - The Association is out of compliance with the PERA requirements and state statute.

**OTIS MUTUAL DOMESTIC WATER CONSUMERS AND SEWAGE WORKS ASSOCIATION
SCHEDULE OF FINDINGS AND RESPONSES
JUNE 30, 2017**

2017-005 – PERA Late Remittance - Compliance (Cont.)

RECOMMENDATION - The Association should provide additional training regarding PERA remittance and filing requirements with personnel.

MANAGEMENT RESPONSE AND PLANNED CORRECTIVE ACTION – In July 2017, the general manager requested the bookkeeper coordinate with the Association’s PERA analyst in order to receive training on PERA’s withholding and reporting and remittance requirements, so the Association can stay current on reporting and remittance. This finding has been substantially resolved in November 2017.

2017-006 – Gross Receipts Tax Form Late Remittance – Compliance

CONDITION - A review of the twelve CRS-1 reports for the respective pay periods in the fiscal year noted two reports were filed outside of the required filing period.

CRITERIA - State Statute 3.1.14 NMSA 1978 establishes filing requirements for gross receipts tax forms as the 25th day after the month the gross receipts were collected.

CAUSE - Late filings were the result of office personnel turnover and inexperience of the replacement employee.

EFFECT - The Association is out of compliance with the Taxation and Revenue Department and State Statute.

RECOMMENDATION – The Association should provide additional training regarding CRS remittance and filing requirements with personnel.

MANAGEMENT RESPONSE AND PLANNED CORRECTIVE ACTION – In July 2017, the general manager requested the bookkeeper coordinate with the Association’s assigned Taxation and Revenue analyst in order to receive training on gross receipts tax withholding and reporting and remittance requirements, so the Association can stay current on reporting and remittance. This has been substantially resolved in November 2017.

2017-007 - Late Submission of Audit Contract and IPA Recommendation - Compliance

CONDITION - Per 2.2.2.8(G)(6)(c) NMAC Audit Rule, the Association did not meet the deadline for submission of the agreed-upon procedures contract and recommendation by the deadline for the fiscal year ending 2017.

CRITERIA - 2.2.2.8(G)(6)(c) NMAC Audit Rule requires that the audit contract and IPA recommendation be submitted to the Office of the State Auditor by May 15th of each year for those agencies with a June 30 fiscal year end.

CAUSE - The audit contract was submitted on July 12, 2017 by the general manager and was approved by the State Auditor’s Office on July 26, 2017.

EFFECT - Late submission of the 2016 audit report was due to forced delays by the former office manager in an attempt to delay discovery of misappropriation of funds.

RECOMMENDATION - We recommend the Association coordinate with the IPA regarding timing of the audit and contract submission for the 2018 fiscal audit.

MANAGEMENT RESPONSE AND PLANNED CORRECTIVE ACTION - The Association’s board and general manager will work with the IPA for the 2018 contract to get the submission in on time. This finding should be resolved in May 2018.

**OTIS MUTUAL DOMESTIC WATER CONSUMERS AND SEWAGE WORKS ASSOCIATION
STATUS OF PRIOR YEAR FINDINGS
JUNE 30, 2017**

Finding	Status
2012-001 Segregation of Duties	Revised, Repeated
2016-001 Internal Control Deficiencies	Revised, Repeated
2016-002 Late Submission of Audit Report	Resolved
2016-003 Trial Balance Did Not Reconcile to Prior Year	Resolved
2016-004 Budgetary Compliance	Revised, Repeated

**OTIS MUTUAL DOMESTIC WATER CONSUMERS AND SEWAGE WORKS ASSOCIATION
EXIT CONFERENCE
JUNE 30, 2017**

The contents of this report were discussed with the Otis Mutual Domestic Water Consumers and Sewage Works Association (Association) representative on November 17, 2017. The following individuals were available for the conference:

Otis MDWC & SWA

James Wilcox, President

Scott Northam, CPA, PC

Scott Northam, CPA

The financial statements of Otis Mutual Domestic Water Consumers and Sewage Works Association were prepared by Scott Northam, CPA, PC, from original books and records provided by and with assistance from the management of the Association.

Although standards strongly emphasize the Association prepare its own financial statements, the consensus between Association management and the auditor was that it would be more time and cost efficient for the auditor to prepare the financial statements and the related notes. Accordingly, the Association designated a competent management-level individual to oversee the auditor's services, make all management decisions and perform all management functions. The Association reviewed, approved, and accepted responsibility for the accompanying financial statements and related notes and supplementary schedules, and for ensuring that the underlying accounting records adequately support the preparation of the financial statements in accordance with accounting principles generally accepted in the United States of America and that the records are current and in balance.