

**EARNHART HILL REGIONAL WATER
AND SEWER DISTRICT**

PICKAWAY COUNTY, OHIO

FINANCIAL STATEMENTS

* * * * *

December 31, 2003 and 2002

BALESTRA, HARR & SCHERER, CPAS, INC.

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**Auditor of State
Betty Montgomery**

Board of Trustees
Earnhart Hill Regional Water and Sewer District

We have reviewed the Independent Auditor's Report of the Earnhart Hill Regional Water and Sewer District, Pickaway County, prepared by Balestra, Harr & Scherer CPAs, Inc., for the audit period January 1, 2003 through December 31, 2003. Based upon this review, we have accepted these reports in lieu of the audit required by Section 117.11, Revised Code. The Auditor of State did not audit the accompanying financial statements and, accordingly, we are unable to express, and do not express an opinion on them.

Our review was made in reference to the applicable sections of legislative criteria, as reflected by the Ohio Constitution, and the Revised Code, policies, procedures and guidelines of the Auditor of State, regulations and grant requirements. The Earnhart Hill Regional Water and Sewer District is responsible for compliance with these laws and regulations.

Betty Montgomery

BETTY MONTGOMERY
Auditor of State

June 14, 2004

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EARNHART HILL REGIONAL WATER AND SEWER DISTRICT

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INDEPENDENT AUDITOR'S REPORT

We have audited the financial statements of the Earnhart Hill Regional Water and Sewer District (the "District"), as of December 31, 2003 and 2002, and for the years then ended as listed in the table of contents. These financial statements are the responsibility of the District's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with 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 general-purpose financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Earnhart Hill Regional Water and Sewer District, as of December 31, 2003 and 2002, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued a report dated April 14, 2004 on our consideration of the District's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grants. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is not a required part of the general-purpose financial statements. Such information has been subjected to the auditing procedures applied in the audit of the general-purpose financial statements, and, in our opinion, is fairly stated, in all material respects, in relation to the general-purpose financial statements taken as a whole.

Balestra, Harr & Scherer CPAs

Balestra, Harr & Scherer CPAs
April 14, 2004

EARNHART HILL REGIONAL WATER AND SEWER DISTRICT

BALANCE SHEETS

As of December 31, 2003 and 2002

	<u>2003</u>	<u>2002</u>
ASSETS		
CURRENT ASSETS		
Cash	\$ 796,696	\$ 925,689
Accounts receivable	182,751	131,295
Inventories	65,945	39,447
Prepaid expenses	25,808	16,440
TOTAL CURRENT ASSETS	<u>1,071,200</u>	<u>1,112,871</u>
RESTRICTED ASSETS		
Cash - Phase IV construction loan	0	2,332,667
Cash - debt service reserve	204,312	156,836
TOTAL RESTRICTED ASSETS	<u>204,312</u>	<u>2,489,503</u>
PROPERTY, PLANT AND EQUIPMENT		
Land	452,494	182,564
Buildings	1,014,310	997,610
Treatment facilities	2,605,783	1,935,488
Transmission and storage	9,896,108	4,774,661
Vehicles	202,485	185,869
Furniture and equipment	463,191	456,054
Construction in progress	0	2,381,020
	<u>14,634,371</u>	<u>10,913,266</u>
Less: Accumulated depreciation	<u>(2,818,390)</u>	<u>(2,568,139)</u>
NET PROPERTY, PLANT AND EQUIPMENT	<u>11,815,981</u>	<u>8,345,127</u>
TOTAL ASSETS	<u>\$ 13,091,493</u>	<u>\$ 11,947,501</u>

LIABILITIES AND FUND EQUITY	2003	2002
CURRENT LIABILITIES		
Accounts payable	\$ 39,102	\$ 203,005
Customer deposits	9,340	8,630
Insurance and taxes payable	10,158	11,372
Current portion of long term debt	138,165	84,264
Accrued payroll	14,216	14,216
Compensated absences payable	0	4,100
Interim notes payable	0	3,600,000
Intergovernmental payable	30,181	0
Retainage payable	77,059	64,040
Accrued interest payable	11,443	33,943
TOTAL CURRENT LIABILITIES	329,664	4,023,570
LONG-TERM LIABILITIES		
Notes payable	1,184,671	1,208,155
Revenue bonds payable	5,559,705	2,093,287
TOTAL LONG-TERM LIABILITIES	6,744,376	3,301,442
FUND EQUITY		
Contributed capital	564,166	564,166
Retained earnings	5,453,287	4,058,323
TOTAL FUND EQUITY	6,017,453	4,622,489
 TOTAL LIABILITIES AND FUND EQUITY	 \$ 13,091,493	 \$ 11,947,501

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

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EARNHART HILL REGIONAL WATER AND SEWER DISTRICT

STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN FUND EQUITY

For the Years Ended December 31, 2003 and 2002

	2003	2002
OPERATING REVENUES		
Service charges	\$ 1,571,031	\$ 1,366,512
Other	0	40,698
TOTAL OPERATING REVENUES	1,571,031	1,407,210
OPERATING EXPENSES		
Treatment expense	74,940	91,256
Power	78,126	75,461
Distribution	280,343	280,746
Customer accounting	136,196	132,584
Transportation	33,963	21,883
Fringe benefits	150,532	143,997
Depreciation and amortization	288,400	324,469
Administrative and general	171,385	188,650
TOTAL OPERATING EXPENSES	1,213,885	1,259,046
Operating income	357,146	148,164
OTHER INCOME (EXPENSE)		
Capacity charges	69,900	70,631
Tap fee revenue	44,100	27,641
Interest income	28,208	28,658
Capital Grant	1,074,113	0
Main Extensions	27,112	27,003
Gain on sale of assets	850	0
Interest expense	(225,591)	(217,522)
Rental income	19,126	20,105
Net other income (expenses)	1,037,818	(43,484)
NET INCOME	1,394,964	104,680
Retained earnings, beginning of year	4,058,323	3,953,643
Retained earnings, end of year	\$ 5,453,287	\$ 4,058,323
Contributed capital, beginning of year	\$ 564,166	\$ 564,166
Contributed capital, end of year	564,166	564,166
Total fund equity, end of year	\$ 6,017,453	\$ 4,622,489

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

EARNHART HILL REGIONAL WATER AND SEWER DISTRICT

STATEMENTS OF CASH FLOWS

For the Years Ended December 31, 2003 and 2002

	2003	2002
CASH FLOWS FROM OPERATING ACTIVITIES		
Cash received from customers	\$ 1,519,965	\$ 1,362,346
Cash paid for employee salaries and benefits	(436,885)	(545,421)
Cash payments to suppliers for goods and services	(663,892)	(432,157)
Cash received from other receipts	0	40,698
Net cash provided by operating activities	419,188	425,466
 CASH FLOWS FROM NON-CAPITAL AND RELATED FINANCING ACTIVITIES		
Deposits received	710	830
 CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Tap fees	44,100	27,641
Capacity charges	69,900	70,631
Main extensions	27,112	27,003
Rental income	19,126	20,105
Revenue bond principal payments	(80,717)	(58,517)
Revenue bond interest payments	(161,034)	(134,707)
Note principal payments	(22,443)	(22,910)
Note interest payments	(64,557)	(64,090)
Interim note principal payments	(3,600,000)	0
Cash received for sale of assets	850	0
Proceeds from short term bond anticipation note	0	3,600,000
Proceeds from USDA note	3,600,000	0
Proceeds from capital grant	1,074,113	0
Capital outlay	(3,768,740)	(1,980,531)
Net cash used by capital and related financing activities	(2,862,290)	1,484,625
 CASH FLOWS FROM INVESTING ACTIVITIES		
Interest on cash and investments	28,208	28,658
Net increase (decrease) in cash and cash equivalents	(2,414,184)	1,939,579
Cash and cash equivalents, beginning of year	3,415,192	1,475,613
Cash and cash equivalents, end of year	\$ 1,001,008	\$ 3,415,192

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

EARNHART HILL REGIONAL WATER AND SEWER DISTRICT

STATEMENTS OF CASH FLOWS - Continued

For the Years Ended December 31, 2003 and 2002

	<u>2003</u>	<u>2002</u>
RECONCILIATION OF OPERATING INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES:		
Operating income	\$ 357,146	\$ 148,164
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation and amortization	288,400	324,469
Changes in assets and liabilities:		
Decrease (increase) in accounts receivable	(51,456)	(4,166)
Decrease (increase) in inventories	(26,498)	(1,580)
Decrease (increase) in prepaid expenses	(9,368)	(2,215)
Increase (decrease) in accounts payable (trade only)	(163,903)	(50,683)
Increase (decrease) in insurance and taxes payable	(1,214)	3,649
Increase (decrease) in accrued payroll	0	7,442
Increase (decrease) in intergovernmental payable	30,181	0
Increase (decrease) in compensated absences payable	(4,100)	386
Total adjustments	<u>62,042</u>	<u>277,302</u>
Net cash provided by operating activities	<u>\$ 419,188</u>	<u>\$ 425,466</u>

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

EARNHART HILL REGIONAL WATER AND SEWER DISTRICT

NOTES TO FINANCIAL STATEMENTS

December 31, 2003 and 2002

NATURE OF ORGANIZATION AND REPORTING ENTITY

Earnhart Hill Regional Water and Sewer District (the District) was founded for the purpose of providing water and wastewater services to those areas in south central Ohio not served by other water companies. As of February 1, 1997, the previous company (Earnhart Hill Water District, Inc.) was declared by the Court to be a duly organized regional water and sewer district, a political subdivision of the state of Ohio organized pursuant to Chapter 6119 of the Ohio Revised Code. The Court approved the Plan to the Operation of the District which provided that the District would accept a transfer of the assets, and assume all of the liabilities of the Company as a part of its organization.

Reporting Entity

The reporting entity is comprised of the primary government, component units and other organizations that are included to ensure that the financial statements of the District are not misleading. The primary government consists of all funds, departments, boards and agencies that are not legally separate from the District. For Earnhart Hill Regional Water and Sewer District, there are no other boards and agencies other than the District.

Component units are legally separate organizations for which the District is financially accountable. The District is financially accountable for an organization if the District appoints a voting majority of the organization's governing board and (1) the District is able to significantly influence the programs or services performed or provided by the organization; or (2) the District is legally entitled to or can otherwise access the organization's resources; the District is legally obligated or has otherwise assumed the responsibility to finance the deficits of, or provide financial support to, the organization; or the District is obligated for the debt of the organization. Component units may also include organizations for which the District approves the budget, the issuance of debt or levying of taxes. The District has no component units.

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The significant accounting policies followed in the preparation of these financial statements conform to generally accepted accounting principles for local governmental units as prescribed in the statements issued by the Governmental Accounting Standards Board (GASB) and other recognized authoritative sources. Under the guidelines of GASB Statement No. 20, the District has elected not to apply Financial Accounting Standards Board Statements and Interpretations issued after November 30, 1989 to its proprietary activities. The adoption of this approach to accounting for proprietary activities by the District required no change from prior years. A summary of the significant accounting policies consistently applied in preparation of the accompanying financial statements is as follows:

1. Basis of Presentation - Fund Accounting

The accounts of the District are organized on the basis of funds, each of which is considered a separate accounting entity. The District has created a single type of fund and a single fund within that fund type. The fund is accounted for by a separate set of self-balancing accounts that comprise its assets, liabilities, fund equity, revenues, and expenses. This fund accounts for the governmental resources allocated to it for the purpose of carrying on specific activities in accordance with laws, regulations or other restrictions.

EARNHART HILL REGIONAL WATER AND SEWER DISTRICT

NOTES TO FINANCIAL STATEMENTS – Continued

December 31, 2003 and 2002

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – Continued

The fund type that the District uses is described below:

Proprietary Fund Type - This fund type accounts for operations that are organized to be self-supporting through user charges. The fund included in this category used by the District is the Enterprise Fund.

Enterprise Fund - This fund is established to account for operations that are financed and operated in a manner similar to private business enterprises where the intent is that costs of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges.

2. **Basis of Accounting**

The accounting records are maintained on the accrual basis of accounting for financial reporting purposes.

3. **Budgetary Process**

The Ohio Revised Code requires that each fund be budgeted annually. The District has adopted a budget and adopted and passed annual appropriations for the years ended December 31, 2003 and 2002.

Appropriations - Budgetary expenditures (that is, disbursements and encumbrances) may not exceed appropriations at the fund level of control, and appropriations may not exceed estimated resources. The District must annually approve appropriation measures and subsequent amendments. Appropriations lapse at year-end.

Estimated Resources - Estimated resources include estimates of cash to be received (budgeted receipts) plus unencumbered cash as of January 1.

Encumbrances - The Ohio Revised Code requires the District to reserve (encumber) appropriations when commitments are made.

4. **Revenue Recognition**

Revenues for service fees are recorded in the period the service is provided. Revenue for tap fees are recorded when the taps have been installed and the customer is using the service. All other revenue is recognized when earned.

5. **Accounts Receivable**

Accounts receivable are presented at their net realizable value. Uncollectible account balances are certified to the County Auditor after administrative collection efforts have been exhausted.

6. **Restricted Assets**

As explained in the CURRENT AND LONG-TERM DEBT FOOTNOTE, a restricted account was established for the required reserve for the Water System Revenue Bonds and is recorded as a restricted asset in the accompanying financial statements.

EARNHART HILL REGIONAL WATER AND SEWER DISTRICT

NOTES TO FINANCIAL STATEMENTS – Continued

December 31, 2003 and 2002

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – Continued

7. **Property, Plant, Equipment and Planning Costs**

Property, plant, equipment and planning costs are presented at cost and are depreciated over the estimated useful lives of the assets from 5 to 50 years, depending upon the type of asset. In addition, interest costs incurred during the construction of the water and sewer system are capitalized and included in property, plant and equipment. Once construction is complete and a project is operational, depreciation begins on all planning costs, construction costs, and capitalized interest over the estimated useful life of the assets.

Depreciation is computed using the straight-line method for financial reporting purposes. Repairs and maintenance costs are charged to operations when incurred. Improvements and additions are capitalized.

8. **Cash and Cash Equivalents**

For purposes of the statement of cash flows, the District does not have any investments; so all cash balances are included in the statement of cash flows.

9. **Interest Expense**

Interest expense represents the interest portion of loan payments to the United States Department of Agriculture, Rural Development, as well as amounts paid and accrued for the loans obtained through The Savings Bank of Circleville, Ohio.

10. **Interest Income**

Interest income represents earnings from all of the District's bank accounts.

11. **Inventory of Supplies**

Inventories are stated at the lower of cost or market. For all funds, cost is determined on a first-in, first-out basis. The costs of inventory items are recorded as expenses when used.

12. **Prepaid Expenses**

Payments made to vendors for services that will benefit periods beyond December 31, 2003 and 2002, are recorded as prepaid items by using the consumption method. A current asset for the prepaid amount is recorded at the time of the purchase and an expense is reported in the year in which services are consumed.

13. **Compensated Absences**

The District uses the provisions of GASB Statement No. 16, "Accounting for Compensated Absences." Vacation benefits are accrued as a liability as the benefits are earned if the employees' rights to receive compensation are attributable to services already rendered and it is probable that the employer will compensate the employees for the benefits through paid time off or some other means. Sick leave benefits are not accrued as a liability as employees receive no payment for accrued sick leave upon termination or retirement.

14. **Intergovernmental Payable**

The District bills and collects sewer fees and penalties for Scippo Sewer District and Circleville Sewer and Pickaway County Sewer. Intergovernmental payable represents those amounts collected on behalf of those districts but not yet paid as of December 31, 2003.

EARNHART HILL REGIONAL WATER AND SEWER DISTRICT

NOTES TO FINANCIAL STATEMENTS – Continued

December 31, 2003 and 2002

CONTRIBUTED CAPITAL

Prior to the implementation of GASB Statement No. 33, certain payments received by the District to construct capital improvements in prior years have been reported as contributed capital in the accompanying financial statements. There were no changes to contributed capital during fiscal years 2003 and 2002.

DEFINED BENEFIT RETIREMENT PLAN

All Earnhart Hill Regional Water and Sewer District full-time employees participate in the Public Employees Retirement System of Ohio (PERS), a cost-sharing multiple-employer public employee retirement system created by the State of Ohio. PERS provides retirement and disability benefits, annual cost of living adjustments, and death benefits to plan members and beneficiaries. Authority to establish and amend benefits is provided by state statute per Chapter 145 of the Ohio Revised Code. The Public Employees Retirement System issues a stand-alone financial report. Interested parties may obtain a copy by making a written request to 277 East Town Street, Columbus, Ohio 43215-4642 or by calling (614) 466-2085 or 1-800-222-PERS (7377).

The Ohio Revised Code provides statutory authority for employee and employer contributions. The 2003 employer contribution rate was 13.55% of covered payroll for employees. The 2003 member contribution rates were 8.5%, for members in classifications other than law enforcement and public safety. The District's contributions to PERS for the years ended December 31, 2003 and 2002 were \$94,492 and \$86,667, respectively. These contributions were equal to the required contributions for fiscal years 2003 and 2002. The unpaid amount of \$7,479 for the year ended December 31, 2003 was reported as a liability as of December 31, 2003.

CURRENT AND LONG-TERM DEBT – PLANNING AND CONSTRUCTION LOANS

Current and long-term debt at December 31, 2002 are as follows:

Loan #	Payable To	Interest Rate	First Payment	Principal Term	Principal Due in 2004	Principal Due after 2004
91-01	Rural Development	5.00%	10/1/1998	10 yrs.	\$ 23,683	\$ 105,887
93-02	Rural Development	5.00%	10/1/1998	16 yrs.	17,398	224,857
91-03	Rural Development	5.75%	10/1/1998	29 yrs.	4,647	218,647
91-04	Rural Development	6.625%	10/1/1998	33 yrs.	17,278	1,351,289
91-05	Rural Development	5.75%	10/1/1998	33 yrs.	1,938	127,663
91-06	Rural Development	4.25%	10/1/2003	30 yrs.	49,743	3,531,357
44972	The Savings Bank	5.29%	7/1/1999	30 yrs.	14,502	728,767
44973	The Savings Bank	5.29%	7/1/1999	30 yrs.	8,976	455,909
					<u>\$ 138,165</u>	<u>\$ 6,744,376</u>

During fiscal year 2003 the District refinanced \$3,600,000 short-term bond anticipation notes issued in the prior year by a loan through Rural Development. The loan was used to cover the cost of waterline construction. The new Rural Development loan is shown above as loan number 91-06.

EARNHART HILL REGIONAL WATER AND SEWER DISTRICT

NOTES TO FINANCIAL STATEMENTS – Continued

December 31, 2003 and 2002

CURRENT AND LONG-TERM DEBT – PLANNING AND CONSTRUCTION LOANS - Continued

The debt listed with the United States Department of Agriculture – Rural Development is water system revenue bonds. The District is required to maintain a cash balance reserve to meet revenue bond requirements. This cash balance is reported as a restricted asset in the accompanying financial statements. The debt listed above with the Savings Bank is a long-term loan. Principal and interest payments for all of the above listed debt are due on the 1st day of each month. Interest is calculated at the rates reflected above and payable for the terms described above. Future principal and interest payments on all debt are as follows:

Year	Savings Bank			Water System Revenue Bond		
	Principal	Interest	Total	Principal	Interest	Total
2004	23,478	63,522	87,000	114,687	266,025	380,712
2005	24,932	62,068	87,000	107,024	273,688	380,712
2006	26,283	60,717	87,000	112,578	268,134	380,712
2007	27,708	59,292	87,000	118,010	262,702	380,712
2008	29,044	57,956	87,000	122,578	256,464	379,042
2009-2013	171,380	263,620	435,000	558,202	1,197,158	1,755,360
2014-2018	223,159	211,841	435,000	585,276	1,046,711	1,631,987
2019-2023	290,584	144,416	435,000	732,689	876,932	1,609,621
2024-2028	378,373	56,627	435,000	926,775	654,357	1,581,132
2029-2033	13,213	96	0	886,637	396,629	1,283,266
2034-2038	0	0	0	724,677	228,387	953,064
2039-2042	0	0	0	685,254	63,539	748,793
Totals	\$1,208,154	\$980,155	\$0	\$5,674,387	\$5,790,726	\$11,465,113

DEPOSITS WITH FINANCIAL INSTITUTIONS – LEGAL REQUIREMENTS

Active deposits are public deposits necessary to meet current demands on the Treasury. Such monies must be maintained either as cash in the District Treasury, in commercial accounts payable or withdrawable on demand, including negotiable order of withdrawal (NOW) accounts, or in money market deposit accounts.

Inactive deposits are public deposits that the Board of Trustees has identified as not required for use within the current two-year period of designation of depositories. Inactive deposits must either be evidenced by certificates of deposit maturing not later than the end of the current period of designation of depositories, or by savings or deposit accounts including, but not limited to, passbook accounts.

Interim deposits represent interim monies that are not needed for immediate use but which will be needed before the end of the current period of designation of depositories. Interim deposits must be evidenced by time certificates of deposit maturing not more than one year from the date of deposit, or by savings or deposit accounts including passbook accounts. Interim monies can be deposited or invested in the following securities:

EARNHART HILL REGIONAL WATER AND SEWER DISTRICT

NOTES TO FINANCIAL STATEMENTS – Continued

December 31, 2003 and 2002

DEPOSITS WITH FINANCIAL INSTITUTIONS – LEGAL REQUIREMENTS – Continued

1. Notes, bills, bonds, or any other obligation or security issued by the United States Treasury or any other obligation guaranteed as to principal and interest by the United States;
2. Bonds, notes, debentures, or any other obligations or securities issued by any federal government agency or instrumentality, including but not limited to, the Federal National Mortgage Association, Federal Home Loan Bank, Federal Farm Credit Bank, Federal Home Loan Mortgage Corporation, Government National Mortgage Association, and Student Loan Marketing Association. All federal agency securities shall be direct issuances of federal government agencies or instrumentalities;
3. Written repurchase agreements in the securities listed above, provided that the market value of the securities subject to the repurchase agreement must exceed the principal value of the agreement by at least two percent and be marked to market daily, and that the term of the agreement must not exceed thirty days;
4. Bonds and other obligations of the State of Ohio;
5. No-load money market mutual funds consisting exclusively of obligations described in items (1) and (2) of this footnote and repurchase agreements secured by such obligations, provided that investments in securities described in this division are made only through eligible institutions;
6. The State Treasurer's investment pool (STAR Ohio);
7. Certain bankers' acceptances and commercial paper notes for a period not to exceed one hundred eighty days in an amount not to exceed twenty-five percent of the interim monies available for investment at any one time.
8. Under limited circumstances, corporate debt interests rated in either of the two highest rating classifications by at least two nationally recognized rating agencies.

Investments in stripped principal or interest obligations, reverse repurchase agreements and derivatives are prohibited. The issuance of taxable notes for the purpose of arbitrage, the use of leverage and short selling are also prohibited. An investment must mature within five years from the date of purchase unless matched to a specific obligation or debt of the District, and must be purchased with the expectation that it will be held to maturity. Investments may only be made through specified dealers and institutions. Payment for investments may be made only upon delivery of the securities representing the investments to the Treasurer or, if the securities are not represented by a certificate, upon receipt of confirmation of transfer from the custodian. The District held no investments during fiscal years 2003 and 2002.

EARNHART HILL REGIONAL WATER AND SEWER DISTRICT

NOTES TO FINANCIAL STATEMENTS – Continued

December 31, 2003 and 2002

DEPOSITS WITH FINANCIAL INSTITUTIONS – LEGAL REQUIREMENTS – Continued

Protection of the District's deposits is provided by the Federal Deposit Insurance Corporation (FDIC), by eligible securities pledged by the financial institution as security for repayment, by surety company bonds deposited with the Treasurer by the financial institution, or by a single collateral pool established by the financial institution to secure the repayment of all public monies deposited with the institution. The carrying amount of the District's deposits was \$1,001,008 and \$3,415,192 as of December 31, 2003 and 2002, respectively. The District's bank balance was \$1,089,219 and \$3,653,834 as of December 31, 2003 and 2002, respectively. Of the bank balances for each of the fiscal years ended, \$200,000 was covered by federal depository insurance. The remaining amounts were collateralized by specific investments held by a third party trustee in the name of the District.

POSTEMPLOYMENT BENEFITS

The Public Employees Retirement System of Ohio (PERS) provides postretirement health care coverage to age and service retirees with ten or more years of qualifying Ohio service credit and to primary survivor recipients of such retirants. Health care coverage for disability recipients and primary survivor recipients is available. The health care coverage provided by the retirement system is considered an Other Post Employment Benefit (OPEB) as described in GASB Statement No. 12. A portion of each employer's contribution to PERS is set-aside for the funding of post retirement health care. The Ohio Revised Code provides statutory authority for employer contributions. The employer rate for employees was 13.55% of covered payroll during fiscal years 2003 and 2002 and 5% and 4.3% were the portions used to fund health care for both years, while employee contribution rates were 8.5%. The Ohio Revised Code provides the statutory authority requiring public employers to fund postretirement health care through their contributions to PERS.

The assumptions and calculations below were based on the latest actuarial review performed as of December 31, 2002. An entry age normal actuarial cost method of valuation is used in determining the present value of OPEB. The difference between assumed and actual experience (actuarial gains and losses) becomes part of unfunded actuarial accrued liability.

All investments are carried at market value. For actuarial valuation purposes, a smoothed market approach is used. Under this approach assets are adjusted annually to reflect 25% of unrealized market appreciation or depreciation on investment assets. The investment assumption rate for 2002 was 8%. A compounded annual increase of 4% is the base portion of the individual pay increase assumption. This assumes no change in the number of active employees. Additionally, annual pay increases, over and above the 4% base increase, were assumed to range from 0.5% to 6.3%. Health care costs were assumed to increase 4% annually.

OPEB's are advance-funded on an actuarially determined basis. The number of active contributing participants was 364,881. The District contributions actually made to fund postemployment benefits during fiscal year 2003 were \$34,868. \$10.0 billion represents the actuarial value of the Retirement System's net assets available for OPEB at December 31, 2002 (the most recent data available). The actuarially accrued liability and the unfunded actuarial accrued liability, based on the actuarial cost method used, were \$18.7 billion and \$8.7 billion, respectively.

EARNHART HILL REGIONAL WATER AND SEWER DISTRICT

NOTES TO FINANCIAL STATEMENTS – Continued

December 31, 2003 and 2002

ACCOUNTS RECEIVABLE

Following are accounts receivable balances presented by aging classifications as of December 31:

	<u>2003</u>	<u>2002</u>
Current receivables (0-30 days)	\$ 157,193	\$ 108,570
Delinquent receivables (31-60 days)	12,070	13,999
Delinquent receivables (over 60 days)	13,488	8,726
Total accounts receivables	<u>\$ 182,751</u>	<u>\$ 131,295</u>

RISK MANAGEMENT

The District is exposed to various risks of loss related to torts, theft or damage to, and destruction of assets, errors and omissions, injuries to employees and natural disasters. During 2003 and 2002 the District contracted with Rinehart-Walters-Danner & Associates and the Ohio Plan for liability, property, and related insurance.

Coverages provided by the program are as follows:

General Liability	\$3,000,000 per occurrence and \$5,000,000 aggregate
Public Officials	\$3,000,000 per occurrence and \$5,000,000 aggregate
Automobile	\$3,000,000
Property, Boiler and Machinery	\$7,877,149
Inland Marine	\$140,540
Electronic Media	\$106,075
Faithful Performance and Employee Bond	\$500,000

There have been no claims that exceed commercial insurance coverage during the past three years. There have been no significant changes in coverage from the prior year. United Health Care provides health insurance.

Workers' compensation benefits are provided through the State Bureau of Workers' Compensation.

EARNHART HILL REGIONAL WATER AND SEWER DISTRICT

NOTES TO FINANCIAL STATEMENTS – Continued

December 31, 2003 and 2002

OHIO REVISED CODE 5705 COMPLIANCE

Budgetary activity for the years ended December 31, 2003 and 2002, follows:

	<u>Budgeted vs. Actual Receipts</u>	
	<u>2003</u>	<u>2002</u>
Budgeted Receipts	\$ 2,871,600	\$ 1,562,600
Actual Receipts	<u>2,834,440</u>	<u>1,581,248</u>
Variance	\$ 37,160	\$ 18,648

	<u>Budgeted vs. Actual Budgetary Basis Expenditures</u>	
	<u>2003</u>	<u>2002</u>
Appropriation Authority	\$ 1,481,680	\$ 1,983,500
Budgetary Expenditures	<u>1,439,476</u>	<u>1,365,993</u>
Variance	\$ 42,204	\$ 617,507

PENDING LITIGATION

The District's general legal counsel is Huffer and Huffer, LPA, Circleville, Ohio.

There was no material litigation pending or outstanding as of December 31, 2003 and 2002 that management believes might have a significant affect on the accompanying financial statements.

FEDERAL FINANCIAL ASSISTANCE

During fiscal years 2003 and 2002, the District had outstanding loans (CFDA # 10.760) with the United States Department of Agriculture – Rural Development. The outstanding loan balances were \$5,674,387 and \$2,155,108 as of December 31, 2003 and 2002, respectively. The District did expend \$3,401,057 (loan and grant monies) in federal financial assistance during fiscal year 2003 and \$1,273,056 in federal financial assistance during fiscal year 2002. The District believes that it complied with all requirements of the loan agreements during fiscal years presented.

**REPORT ON COMPLIANCE AND ON INTERNAL CONTROL
OVER FINANCIAL REPORTING BASED ON AN AUDIT OF
FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE
WITH *GOVERNMENT AUDITING STANDARDS***

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Ohio Society of Certified Public Accountants

REPORT ON COMPLIANCE AND ON INTERNAL CONTROL OVER FINANCIAL REPORTING BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*

We have audited the financial statements of Earnhart Hill Regional Water and Sewer District (the District), as of and for the years ended December 31, 2003 and 2002, and have issued our report thereon dated April 14, 2004. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Compliance

As part of obtaining reasonable assurance about whether the District's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*. However, we noted a certain immaterial instance of noncompliance that we have reported to management of the District in a separate letter dated April 14, 2004.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the District's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses. However, we noted other matters involving the internal control over financial reporting that do not require inclusion in this report, that we have reported to management of the District in a separate letter dated April 14, 2004.

This report is intended for the information and use of the audit committee, Board of Trustees, management, others within the District, and federal awarding agencies and pass through entities, and is not intended to be and should not be used by anyone other than these specified parties.

Balestra, Harr & Scherer CPAs

Balestra, Harr & Scherer CPAs
April 14, 2004

**REPORT ON COMPLIANCE WITH REQUIREMENTS APPLICABLE
TO EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER
COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133**

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REPORT ON COMPLIANCE WITH REQUIREMENTS APPLICABLE TO EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133

Compliance

We have audited the compliance of Earnhart Hill Regional Water and Sewer District with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement that are applicable to its major federal program for the year ended December 31, 2003. Earnhart Hill Regional Water and Sewer District's major federal program is identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to its major federal program is the responsibility of Earnhart Hill Regional Water and Sewer District's management. Our responsibility is to express an opinion on Earnhart Hill Regional Water and Sewer District's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, Audits of States, Local Governments and Non-Profit Organizations. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about Earnhart Hill Regional Water and Sewer District's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on Earnhart Hill Regional Water and Sewer District's compliance with those requirements.

In our opinion, Earnhart Hill Regional Water and Sewer District complied, in all material respects, with the requirements referred to above that are applicable to its major federal program for the year ended December 31, 2003.

Internal Control Over Compliance

The management of Earnhart Hill Regional Water and Sewer District is responsible for establishing and maintaining effective internal controls over compliance with requirements of laws, regulations, contracts and grants applicable to federal programs. In planning and performing our audit, we considered Earnhart Hill Regional Water and Sewer District's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133.

REPORT ON COMPLIANCE WITH REQUIREMENTS APPLICABLE
TO EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER
COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133
Page -2-

Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that noncompliance with applicable requirements of laws, regulations, contracts and grants that would be material in relation to a major federal program being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over compliance and its operation that we consider to be material weaknesses.

This report is intended solely for the information and use of the audit committee, Board of Directors, management, others within the organization, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than those specified parties.

Balestra, Harr & Scherer CPAs

Balestra, Harr & Scherer CPAs

April 14, 2004

EARNHART HILL REGIONAL WATER AND SEWER DISTRICT

SCHEDULE OF FEDERAL AWARDS EXPENDITURES

For the Year Ended December 31, 2003

U.S. Department of Agriculture

Rural Development	10.760	*	\$ 2,326,944
Rural Development Grant	10.760	^	1,074,113
Rural Development Loan	10.760	&	<u>5,674,387</u>
Total			<u>\$ 9,075,444</u>

* This amount represents expenditures on the new loan received from Rural Development.

^ This amount represents expenditures on the new grant received from Rural Development.

& This amount represents the loan balance outstanding at December 31, 2003. This amount was not received and/or expended during the audit period.

EARNHART HILL REGIONAL WATER AND SEWER DISTRICT

NOTES TO SCHEDULE OF FEDERAL AWARDS EXPENDITURES

For the Year Ended December 31, 2003

Note 1 - Basis of Presentation

The accompanying schedule of expenditures of federal awards includes the federal grant activity of Earnhart Hill Regional Water and Sewer District, and is presented on the cash basis of accounting. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of, the general-purpose financial statements.

EARNHART HILL REGIONAL WATER AND SEWER DISTRICT

SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS

For the Year Ended December 31, 2003

No matters were reported for the year ended December 31, 2002.

EARNHART HILL REGIONAL WATER AND SEWER DISTRICT

SUMMARY OF AUDITOR'S RESULTS

For the Year Ended December 31, 2003

SECTION I – SUMMARY OF AUDITOR'S RESULTS

Financial Statements

Type of auditor's report issued: Unqualified

Internal control over financial reporting:

- Material weakness(es) identified? YES NO
- Reportable condition(s) identified that are not considered to be material weaknesses? YES NO

Noncompliance material to financial statements noted? YES NO

Federal Awards

Internal control over major programs:

- Material weakness(es) identified? YES NO
- Reportable condition(s) identified that are not considered to be material weaknesses? YES NO

Type of auditor's report issued: Unqualified

Any audit findings disclosed required to be reported in accordance with section 510(a) of Circular A-133? YES NO

Identification of major programs

<u>CFDA Number(s)</u>	<u>Name of Federal Program or Cluster</u>
10.760	Rural Development

Dollar threshold used to distinguish between type A and type B programs? \$300,000

Auditee qualified as low-risk auditee? YES NO

SECTION II – FINANCIAL STATEMENT FINDINGS

No matters were reported for the year ended December 31, 2003

SECTIONS III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

No matters were reported for the year ended December 31, 2003

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Betty Montgomery**

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EARNHART HILL REGIONAL WATER AND SEWER DISTRICT

PICKAWAY COUNTY

CLERK'S CERTIFICATION

This is a true and correct copy of the report which is required to be filed in the Office of the Auditor of State pursuant to Section 117.26, Revised Code, and which is filed in Columbus, Ohio.

Susan Babbitt

CLERK OF THE BUREAU

**CERTIFIED
JUNE 29, 2004**