RURAL LORAIN COUNTY WATER AUTHORITY

Lorain County, Ohio

Regular Audit

January 1, 2005 through December 31, 2006

Fiscal Years Audited Under GAGAS: 2005 and 2006

BALESTRA, HARR & SCHERER, CPAS, INC.
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Mary Taylor, CPA
Auditor of State

Board of Trustees
Rural Lorain County Water Authority
42401 State Route 303
LaGrange, Ohio 44050

We have reviewed the *Independent Auditor's Report* of the Rural Lorain County Water Authority, Lorain County, prepared by Balestra, Harr & Scherer, CPAs, Inc., for the audit period January 1, 2005 to December 31, 2006. 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 Rural Lorain County Water Authority is responsible for compliance with these laws and regulations.

Mary Taylor

Mary Taylor, CPA
Auditor of State

October 24, 2007

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RURAL LORAIN COUNTY WATER AUTHORITY

TABLE OF CONTENTS

December 31, 2006 and 2005

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INDEPENDENT AUDITOR'S REPORT

To the Board of Directors
Rural Lorain County Water Authority
42401 State Route 303
LaGrange, Ohio 44050

We have audited the accompanying financial statements of the business-type activities of the Rural Lorain County Water Authority (the Authority), Lorain County, as of and for the years ended December 31, 2006 and December 31, 2005, which collectively comprise the Authority's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the Authority's management. 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 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 the significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

In our opinion the financial statements referred to above present fairly, in all material respects, the respective financial position of the business-type activities of the Authority, as of December 31, 2006 and December 31, 2005, and the respective changes in financial position and its cash flows thereof 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 our report dated July 20, 2007, on our consideration of the Authority's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

The management's discussion and analysis on pages 3 through 6 is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

As described in Note 9 to the basic financial statements, the Authority implemented Governmental Accounting Standards Board (GASB) Statement No. 40, *Deposit and Investment Risk Disclosures, an amendment of GASB Statement No.3,* GASB Statement No. 42, *Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries,* GASB Statement No. 46, *Net Assets Restricted by Enabling Legislation,* and GASB Statement No. 47, *Accounting for Termination Benefits.*

Balestra, Harr & Scherer

Balestra, Harr & Scherer, CPAs, Inc.

July 20, 2007

This discussion and analysis, along with the accompanying financial reports of Rural Lorain County Water Authority (RLCWA), is designed to provide our customers, bondholders, creditors and other interested parties with a general overview of the Authority and its financial activities.

FINANCIAL HIGHLIGHTS

The total assets of RLCWA exceeded liabilities by $22.7 and $21.1 million in 2006 and 2005, respectively.

The Authority's net assets increased by $1.6 million (7.8%) and $1.1 million (5.6%) in 2006 and 2005, respectively.

The Authority's Operating Revenues decreased by $18 thousand (.2%) and increased by $321 thousand (3.1%) with Operating Expenses decreasing $211 thousand (3.2%) and increasing $217 thousand (3.4%) in 2006 and 2005, respectively.

OVERVIEW OF BASIC FINANCIAL STATEMENTS

The Authority is a single fund using proprietary fund accounting, similar to private sector business. The Authority is described in Note 1, Summary of Significant Accounting Policies, on page thirteen (13). The Basic Financial Statements are presented using the accrual basis of accounting as further described in the above-mentioned note.

The **Statement of Net Assets** includes all of the Authority's Assets and Liabilities. This statement provides information about the nature and amounts of investments in resources (assets) owned by the Authority, and obligations owed by the Authority (liabilities) on December 31. The Authority's net assets (equity) are the difference between assets and liabilities.

The **Statement of Revenues, Expenses, and Changes in Net Assets** provides information on the Authority's operations over the past year and the revenue collected from user fees, charges and late fees, and other income. Revenues are reported when earned and expenses are reported when incurred.

The **Statement of Cash Flows** provides information about the Authority's cash receipts and cash disbursements from operations, investing and financing activities. The statement summarizes where the cash was provided, cash uses, and changes in the balances during the year.

SIGNIFICANT EVENTS AND EXPENDITURES DURING THE YEAR

The Authority has entered into an agreement with the Village of LaGrange to build a waterline north of Biggs Road and waive the tap fees for existing Village customers. The Village will turn over the entire area to the Authority as a RLCWA service area. LaGrange Village will serve this area with revenue sharing provisions in accord with the existing contract. This agreement will allow RLCWA to serve customers currently served by the Village of LaGrange. The Authority will waive the tap fees.

On April 11 the Authority issued $9,130,000 in Water Resource Revenue and Refunding Bonds for the purpose of refunding 1999 revenue bonds at a more favorable interest rate and to raise an additional $1,500,000 for capital improvements to the system.

The Ohio Division of Natural Resources (ODNR) has notified RLCWA that it does not object to the Authority providing water to residents of Ashland County. A moratorium had been in effect since November of 1995 regarding the sale of water to residents that were over the Continental Divide and not located in the Great Lakes Basin. After reviewing the project, ODNR pointed out that a diversion permit is not required, nor does the sale of water to Ashland County conflict with ODNR policies.

The Board approved construction projects for improvements to the existing lines in Pittsfield Township and existing lines in Wellington Township. The Board awarded the bid in the amount of $1,531,976 for the Ashland/Nankin water transmission main improvements project. The Board authorized the hiring of Arcadis Engineers, Inc. to proceed with the initial distribution system evaluation and sampling plan for the United States EPA disinfection byproduct rules as mandated by federal law. This project is a result of a required federal mandate, but will be paid for by RLCWA.

NET ASSETS

Table 1 summarizes the Net Assets of the Authority. Capital Assets are reported less accumulated depreciation. Invested in Capital, Net of Debt, are Capital Assets less outstanding debt that was used to acquire those assets.

Table 1

	2006	2005	Change Amount	%	2004	Change Amount	%
Current and Other Assets	$ 18,357,224	$ 16,641,318	$ 1,715,906	10.3%	$ 15,892,396	$ 748,922	4.7%
Capital Assets	31,450,380	30,491,197	959,183	3.1%	31,219,749	(728,552)	-2.3%
Total Assets	49,807,604	47,132,515	2,675,089	5.7%	47,112,145	20,370	0.0%
Long Term Liabilities	23,814,665	23,427,117	387,548	1.7%	24,744,405	(1,317,288)	-5.3%
Other Liabilities	3,252,316	2,602,353	649,963	25.0%	2,387,784	214,569	9.0%
Total Liabilities	27,066,981	26,029,470	1,037,511	4.0%	27,132,189	(1,102,719)	-4.1%
Invested in Capital Assets, Net of Related Debt	11,729,860	11,366,940	362,920	3.2%	10,951,064	415,876	3.8%
Restricted	4,468,935	4,134,016	336,919	8.2%	3,941,301	190,715	4.8%
Unrestricted	6,541,828	5,602,089	937,739	16.7%	5,087,591	516,498	10.2%
Total Net Assets	$ 22,740,623	$ 21,103,045	$ 1,637,578	7.8%	$ 19,979,956	$ 1,123,089	5.6%

The Authority's Net Assets increased $1.6 million (7.8%) and $1.1 million (5.6%) in 2006 and 2005, respectively. These increases are a result of excess revenues over expenses.

The Authority increased long term liabilities $387 thousand from issuance of 2006 Series Revenue Bonds. The Authority decreased long term liabilities $1.3 million from payment of long term notes for 2005.

STATEMENT OF REVENUES AND EXPENSES (CHANGES IN NET ASSETS)

Table 2 summarizes the changes in Revenues and Expenses and the resulting change in Net Assets.

Table 2

	2006	2005	Change Amount	%	2004	Change Amount	%
Operating Revenues	$ 10,562,343	$ 10,580,680	$ (18,337)	-0.2%	$ 10,259,383	$ 321,297	3.1%
Total Revenues	10,562,343	10,580,680	(18,337)	-0.2%	10,259,383	321,297	3.1%
Operating Expenses	6,304,940	6,515,985	(211,045)	-3.2%	6,298,798	217,187	3.4%
Maintenance Expenses	336,371	353,749	(17,378)	-4.9%	640,702	(286,953)	-44.8%
Depreciation Expenses	1,680,341	1,719,781	(39,440)	-2.3%	1,896,070	(176,289)	-9.3%
Total Expenses	8,321,652	8,589,515	(267,863)	-3.1%	8,835,570	(246,055)	-2.8%
Operating Income	2,240,691	1,991,165	249,526	12.5%	1,423,813	567,352	39.8%
Non-Operating Revenues	770,381	501,192	269,189	53.7%	412,807	88,385	21.4%
Non-Operating Expenses	(1,373,494)	(1,369,268)	(4,226)	0.3%	(1,289,004)	(80,264)	6.2%
Non-Operating Loss	(603,113)	(868,076)	264,963	54.0%	(876,197)	8,121	27.6%
Change in Net Assets	1,637,578	1,123,089	514,489	66.6%	547,616	575,473	67.5%
Beginning Net Assets	21,103,045	19,979,956	1,123,089	5.6%	19,432,340	547,616	2.8%
Ending Net Assets	$ 22,740,623	$ 21,103,045	$ 1,637,578	7.8%	$ 19,979,956	$ 1,123,089	5.6%

STATEMENT OF REVENUES AND EXPENSES (CHANGES IN NET ASSETS)(Continued)

Total Operating Revenues decreased $18 thousand (0.2%) and increased $321 thousand (3.1%) in 2006 and 2005, respectively. Investment income increased by $181 thousand (69.5%) and $96 thousand (58.3%) resulting in the majority of the increase of $269 thousand (53.7%) and $88 thousand (21.4%) in non-operating revenues for 2006 and 2005, respectively.

Operations and Maintenance Expenses, excluding depreciation, decreased $228 thousand (3.3%) and $70 thousand (1%) in 2006. Two retirements, one employee's voluntary termination, and the initial recording of the vacation and sick leave accrual of three employees in 2005 accounted for the majority of the decrease in operating and maintenance costs in 2006.

CAPITAL ASSETS

The Authority had $56.75 and $54.15million invested in Capital Assets (before depreciation) at the end of 2006 and 2005, respectively, as shown in Table 3. This amount is an increase of $2.60 million (4.8%) and $.8 million (1.5%) from the previous year.

Table 3

	2006	2005	Change Amount	%	2004 Restated	Change Amount	%
Land and Easements	$ 536,069	$ 531,911	$ 4,158	0.8%	$ 531,911	$ -	0.0%
Buildings	2,194,798	2,193,448	1,350	0.1%	2,184,959	8,489	0.4%
Tanks, Stations, and Lines	48,335,233	47,226,630	1,108,603	2.3%	46,697,668	528,962	1.1%
Meters and Replacements	1,444,824	1,405,768	39,056	2.8%	1,343,003	62,765	4.7%
Furniture and Fixtures	1,311,015	1,182,600	128,415	10.9%	954,244	228,356	23.9%
Machinery, Equipment, and Vehicles	1,736,849	1,579,165	157,684	10.0%	1,616,517	(37,352)	-2.3%
Construction in Progress	1,188,485	26,321	1,162,164	4415.3%	15,806	10,515	66.5%
Totals before Depreciation	56,747,273	54,145,843	2,601,430		53,344,108	801,735	
Accumulated Depreciation	(25,296,893)	(23,654,646)	(1,642,247)		(22,124,359)	(1,530,287)	
Total Capital Assets, Net	$ 31,450,380	$ 30,491,197	$ 959,183		$ 31,219,749	$ (728,552)	

The majority of the increase in capital assets from 2005 to 2006 was from the line extensions, line replacement and relocation, the geographical information system's (GIS) database equipment, software, computer hardware, computers, office equipment, four trucks, meter replacements, and tools.

The majority of the decrease in net capital assets from 2004 to 2005 was from increases in accumulated depreciation exceeding the increases in capital asset additions. See Note 1(F) of the financial statements for more details on the Authority's capital assets.

DEBT

Table 4 summarizes the Authority's long-term debt. The Authority issues long-term revenue bonds to finance much of its construction.

Table 4

	2006	2005	Change Amount	%	2004	Change Amount	%
Long-term debt							
1999 revenue bonds	$ 890,000	$ 8,510,000	$(7,620,000)	-89.5%	$ 8,770,000	$ (260,000)	-3.0%
2003 revenue bonds	12,145,000	13,100,000	(955,000)	-7.3%	14,040,000	(940,000)	-6.7%
2006 revenue bonds	9,110,000	-	9,110,000	100.0%	-	-	0.0%
Long Term Note Payable	-	-	-	0.0%	1,747,654	(1,747,654)	100.0%
Rural development	3,042,063	3,135,513	(93,450)	-3.0%	1,487,000	1,648,513	110.9%
Long-term debt	25,187,063	24,745,513	441,550	1.8%	26,044,654	(1,299,141)	-5.0%
Less: Current maturities	(1,372,398)	(1,318,396)	(54,002)	4.1%	(1,300,249)	(18,147)	1.4%
Net total long-term debt	$ 23,814,665	$ 23,427,117	$ 387,548	1.7%	$ 24,744,405	$(1,317,288)	-5.3%

See Note 4 of the financial statements for details of issuance and retirement of debt in 2006 and 2005.

The Bond Reserve Fund and Bond Fund were established for payment of bond service charges and cancellation or redemption of bonds. The Bond Reserve Fund had a balance of $2,408,981 and $2,394,243, and the Bond Fund had a balance of $2,059,954 and 1,739,773 at December 31, 2006 and 2005. See Note 2 of the financial statements for more details on the bond funds.

DEBT COVERAGE

Table 5 reflects the ability of the Authority to pay both interest and the current principal installments on its outstanding debt.

Table 5

	2006	2005	2004
Operating Revenues	$ 10,562,343	$ 10,580,680	$ 10,259,383
Non-Operating Revenue-Interest	440,481	259,927	164,186
Total Revenues	11,002,824	10,840,607	10,423,569
Less: Operations & Maintenance Expenses	(6,641,311)	(6,869,734)	(6,939,500)
Total Revenues Available for Debt	4,361,513	3,970,873	3,484,069
Total Debt Service Requirements	$ 2,499,760	$ 2,454,937	$ 2,437,517
Combined Coverage Ration-All Debt	1.74	1.62	1.43
Required Coverage Ratio			
Revenue Bonds - 1999, 2003, & 2006	1.20	1.20	1.20
Rural Development	1.00	1.00	1.00

The Authority is required to meet a revenue-to-debt ratio of 1.20 for its 1999, 2003, and 2006 revenue bonds and a 1.00 ratio for rural development bonds.

CONTACT INFORMATION

Questions regarding this report and requests for additional information should be forwarded to the General Manager of the Rural Lorain County Water Authority, 42401 Route 303, P.O. Box 567, LaGrange, Ohio 44050.

RURAL LORAIN COUNTY WATER AUTHORITY

STATEMENTS OF NET ASSETS

As of December 31, 2006 and 2005

	2006	2005
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents:		
General	$ 196,694	$ 174,023
Working capital	1,663,321	1,190,321
Capital improvements	1,350,678	1,850,679
Receivables:		
Trade (net of allowance for doubtful accounts of $3,000 in 2006 and $3,000 in 2005)	760,762	683,518
Other	26,821	24,364
Interest	31,094	23,193
Inventory	339,063	314,933
Prepaid expenses	59,571	55,933
Deferred debt issue costs	1,308,335	1,100,808
Total current assets	5,736,339	5,417,772
NONCURRENT ASSETS:		
Restricted cash and investments	7,154,342	5,602,290
Investment in Joint Venture	5,466,543	5,621,256
Total noncurrent assets	12,620,885	11,223,546
CAPITAL ASSETS, AT COST:	55,558,788	54,119,522
Less: Accumulated depreciation	25,296,893	23,654,646
	30,261,895	30,464,876
Current construction	1,188,485	26,321
	31,450,380	30,491,197
TOTAL ASSETS	$ 49,807,604	$ 47,132,515

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

RURAL LORAIN COUNTY WATER AUTHORITY

STATEMENTS OF NET ASSETS
(CONTINUED)

As of December 31, 2006 and 2005

	2006	2005
LIABILITIES AND NET ASSETS		
CURRENT LIABILITIES:		
Current portion of long-term debt	$ 1,372,398	$ 1,318,396
Accounts payable	869,264	395,377
Taxes payable	31,938	35,089
Compensation absences payable	385,486	404,374
Deposits	174,110	69,860
Accrued expenses:		
Retirement incentive plan	39,435	-
Wages	47,646	47,217
Interest	332,039	332,040
Total current liabilities	3,252,316	2,602,353
LONG-TERM DEBIT:		
Bonds and notes payable:		
2006 Series	9,110,000	-
2003 Series	12,145,000	13,100,000
1999 Series	890,000	8,510,000
Notes payable	1,582,063	1,661,513
USDA	1,460,000	1,474,000
	25,187,063	24,745,513
Less: Current portion	1,372,398	1,318,396
	23,814,665	23,427,117
Total liabilities	27,066,981	26,029,470
NET ASSETS:		
Invested in capital assets, net of related debt	11,729,860	11,366,940
Restricted for debt service	4,468,935	4,134,016
Unrestricted	6,541,828	5,602,089
TOTAL NET ASSETS	$ 22,740,623	$ 21,103,045

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

RURAL LORAIN COUNTY WATER AUTHORITY

STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS

For the Years Ended December 31, 2006 and 2005

	2006	2005
OPERATING REVENUE:		
Water Sales	$ 9,929,306	$ 9,941,889
Tap Fees	633,037	638,791
Total Operating Revenue	10,562,343	10,580,680
OPERATING EXPENSES:		
Wages:		
Board	84,637	84,681
Employees	1,271,122	1,489,718
O.P.E.R.S.	333,980	335,183
Payroll taxes	24,036	30,479
Insurance:		
Hospitalization	286,426	219,548
Life	4,678	3,999
General	86,039	77,352
Audit and professional fees	87,586	89,405
Legal fees	30,456	45,000
Engineering fees	21,460	4,131
Telephone	25,776	27,521
Depreciation expense	1,680,341	1,719,781
Utilities	32,945	35,522
Billing expense	24,102	20,571
Office equipment lease	14,994	15,232
Office supplies and expense	115,482	147,536
Clothing	17,128	18,313
Postage	78,313	72,387
Maintenance and repairs:		
Administration building and equipment	143,468	141,321
Vehicles	61,113	87,728
Water lines	64,385	82,527
Pump stations	26,605	19,387
Tanks	40,800	22,786
Travel and education expense	63,311	76,149
Gasoline	50,803	42,553
Water purchased	2,914,474	2,899,727
Distribution supplies	74,933	76,806
Electric pump stations and tanks	345,847	346,687
Tap installations	227,740	266,042
Communications equipment	16,197	6,172
Bond administration expense	-	4,500
Miscellaneous expense	72,475	80,771
Total Operating Expenses	8,321,652	8,589,515
INCOME FROM OPERATIONS	$ 2,240,691	$ 1,991,165

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

RURAL LORAIN COUNTY WATER AUTHORITY

STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS (CONTINUED)

For the Years Ended December 31, 2006 and 2005

	2006	2005
NON-OPERATING REVENUES:		
Penalty income	$ 122,304	$ 125,870
Miscellaneous	86,613	57,422
Miscellaneous subdivision income	43,710	35,000
Water line reimbursements	54,763	7,570
Discounts earned	163	536
Investment income	440,481	259,927
Unrealized gain (loss) on investments	22,347	(62,805)
Gain on disposal of assets	-	77,672
Total Other Income	770,381	501,192
NON-OPERATING EXPENSES:		
Interest expense	1,128,828	1,132,569
Change in Value of Investment in Joint Venture	154,713	154,714
Bad debts	1,131	3,301
Bond premium amortization	88,822	78,684
Total Other Expenses	1,373,494	1,369,268
CHANGES IN NET ASSETS	1,637,578	1,123,089
BEGINNING NET ASSETS	21,103,045	19,979,956
ENDING NET ASSETS	$ 22,740,623	$ 21,103,045

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

RURAL LORAIN COUNTY WATER AUTHORITY

STATEMENTS OF CASH FLOWS

Years Ended December 31, 2006 and 2005

	2006	2005
CASH FLOWS FROM OPERATING ACTIVITIES:		
Cash received from customers	$ 10,474,741	$ 10,571,871
Cash payments to suppliers for goods and services	(4,121,878)	(4,528,262)
Cash payments to employees and professional contractors for services and benefits	(2,248,719)	(2,274,279)
Net cash provided by operating activities	4,104,144	3,769,330
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES:		
Purchase of property and equipment and current construction	(2,639,524)	(993,533)
Proceeds from sale of equipment	-	79,975
Repayment of 1999 Series Bonds	(7,620,000)	(260,000)
Repayment of 2003 Series Bonds	(955,000)	(940,000)
Repayment of notes payable	(93,450)	(99,141)
Proceeds from issuance of 2006 Series Bonds	9,130,000	-
Repayment of 2006 Series Bonds	(20,000)	-
Interest paid on bonds	(1,128,829)	(1,126,824)
Net cash used in capital and related financing activities	(3,326,803)	(3,339,523)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Investment income	462,828	197,122
Net cash provided by investing activities	462,828	197,122
CASH FLOWS FROM NON-CAPITAL ACTIVITIES:		
Other non-operating activities	307,553	304,070
Net cash provided by non-capital activities	$ 307,553	$ 304,070
INCREASE IN CASH AND CASH EQUIVALENTS	$ 1,547,722	$ 930,999
CASH AND CASH EQUIVALENTS - Beginning of year	8,817,313	7,886,314
CASH AND CASH EQUIVALENTS - End of year	10,365,035	8,817,313

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

RURAL LORAIN COUNTY WATER AUTHORITY

STATEMENTS OF CASH FLOWS
(CONTINUED)

Years Ended December 31, 2006 and 2005

	2006	2005
CASH FLOWS FROM OPERATING ACTIVITIES:		
Income from operations	2,240,691	1,991,165
Adjustment to reconcile operating income to net cash provided by operating activities:		
Depreciation expense	1,680,341	1,719,781
Bond premium amortization	(88,822)	(78,684)
Gain on disposal of assets	-	(77,672)
Bad debts	(1,131)	(3,301)
Changes in assets and liabilities:		
(Increase) decrease in:		
Receivables	(87,602)	(8,809)
Inventory	(24,130)	(35,302)
Prepaid expenses	(3,638)	(4,480)
Deferred debt issue costs	(207,527)	75,955
Increase (decrease) in:		
Accounts payable	473,887	33,320
Taxes payable	(3,151)	7,645
Compensated absences payable	(18,888)	147,873
Advanced deposits	104,250	(1,175)
Accrued expenses	39,864	3,014
Net cash provided by operating activities	$ 4,104,144	$ 3,769,330

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

RURAL LORAIN COUNTY WATER AUTHORITY

NOTES TO FINANCIAL STATEMENTS

December 31, 2006 and 2005

1. Summary of Significant Accounting Policies:

The Rural Lorain County Water Authority, a regional water district, is a political subdivision of the State of Ohio created by order of the Lorain County Common Pleas Court. The Authority was declared by the Court, on August 23, 1973 to be a duly organized regional water district, a political subdivision of the state of Ohio organized pursuant to Chapter 6119 of the Ohio Revised Code. The Authority operates under a Board of Trustees, which consists of as many members as equals the total number of villages and townships within this regional water district. The following is a summary of significant accounting policies:

A. Introduction:

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 Authority has elected not to apply Financial Accounting Standards Board Statements (FASB) and Interpretations issued after November 30, 1989 to its proprietary activities. Proprietary funds apply FASB pronouncements and Accounting Principles Board (APB) opinions issued on or before November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements , in which case, GASB prevails. A summary of the significant accounting policies consistently applied in preparation of the accompanying financial statements is as follows:

B. Basis of Accounting:

The Rural Lorain County Water Authority prepares its financial statements on an accrual basis. By virtue of its by-laws, the Authority is required to make appropriations in accordance with budgetary policies.

C. Investments:

Investment procedures are restricted by the Provisions of the Ohio Revised Code. During 2006 and 2005, investments were limited to repurchase agreements, certificates of deposit, U.S. Government Income Funds, or U.S. Treasury Funds.

Except for nonparticipating investment contracts, investments are reported at fair value which is based on quoted market prices. Nonparticipating investment contracts such as repurchase agreements and nonnegotiable certificates of deposit are reported at cost.

D. Budgetary Process:

Budget - Thirty days before the end of each fiscal year a proposed budget of estimated revenues and expenditures for the succeeding fiscal year is submitted to the Board of Trustees by the General Manager. The Board may amend said budget as it deems proper. The Board of Trustees then approves the budget in its original or amended form.

Appropriations - After the budget is approved by the Board, the Board then makes appropriations of funds in accordance with said budget. Thereafter, the General Manager has the authority to authorize payment of any disbursement not to exceed $25,000, provided there are sufficient funds appropriated and remaining in the account of the fund from which payment will be made. The Board may, from time-to-time, amend or supplement said appropriation of funds and may also transfer any part of an unencumbered balance of an appropriation of any fund to any purpose or object for which the appropriation for the current fiscal year has proved insufficient. During the year, supplemental appropriations were authorized; however, none of these amendments are significant.

1. Summary of Significant Accounting Policies (Continued):

E. Inventory:

Inventory, which consists of raw materials, is stated at the lower of cost or market. In general, cost as applied to inventory valuation represents a moving average method whereby the cost per unit is recomputed after every addition to the inventory.

F. Capital Assets:

Capital assets including major renewals or betterments are capitalized and stated at cost. Depreciation is provided on the straight-line method based on the estimated useful lives of the various classes of assets.

The ranges of estimated useful lives used in computing depreciation are as follows:

Water Lines and Water Tanks	40 Years
Pump Stations	20 Years
Buildings and Building Improvements	4-20 Years
Machinery, Equipment, and Office Furniture	3-10 Years

Fully depreciated assets still in active use are included in the gross amount of capital assets, and the related allowance for depreciation is included as part of the total accumulated allowance for depreciation.

The Authority, by action of its Board, has adopted the policy of capitalizing meter replacement costs over a ten-year period with one-half year of depreciation being taken in the year of replacement. In 1992 and prior years, the Authority expensed all replacement meters at the time of installation.

Maintenance, repairs, and minor renewals are charged against earnings when incurred.

Depreciation expense for the years ended December 31, 2006 and 2005, was $1,680,341 and $1,719,781, respectively.

RURAL LORAIN COUNTY WATER AUTHORITY

NOTES TO FINANCIAL STATEMENTS

December 31, 2006 and 2005

1. Summary of Significant Accounting Policies (Continued):

F. Capital Assets (Continued):

A summary of changes in capital assets for the year ended December 31, 2006, is as follows:

	Balance December 31, 2005	Additions	Deletions	Balance December 31, 2006
Land and easements	$ 531,911	$ 4,158	$ -0-	$ 536,069
Buildings	2,193,448	1,350	-0-	2,194,798
Tanks, stations, and lines	47,226,630	1,108,603	-0-	48,335,233
Meters and replacements	1,405,768	39,056	-0-	1,444,824
Furniture and fixtures	1,182,600	166,509	(38,094)	1,311,015
Machinery, equipment, and vehicles	1,579,165	157,684	-0-	1,736,849
Current construction lines	26,321	1,162,164	-0-	1,188,485
	54,145,843	2,639,524	(38,094)	56,747,273
Less accumulated depreciation				
Buildings	(952,042)	(100,850)	-0-	(1,052,892)
Tanks, stations, and lines	(19,659,591)	(1,237,377)	-0-	(20,896,968)
Meters and replacements	(1,089,780)	(71,053)	-0-	(1,160,833)
Furniture and fixtures	(704,156)	(103,103)	38,094	(769,165)
Machinery, equipment, and vehicles	(1,249,077)	(167,958)	-0-	(1,417,035)
Total accumulated depreciation	(23,654,646)	(1,680,341)	38,094	(25,296,893)
Net capital assets	$ 30,491,197	$ 959,183	$ -0-	$ 31,450,380

A summary of changes in capital assets for the year ended December 31, 2005, is as follows:

	Balance December 31, 2004 as Restated	Additions	Deletions	Balance December 31, 2005
Land and easements	$ 531,911	$ -0-	$ -0-	$ 531,911
Buildings	2,184,959	8,489	-0-	2,193,448
Tanks, stations, and lines	46,697,668	528,962	-0-	47,226,630
Meters and replacements	1,343,003	62,765	-0-	1,405,768
Furniture and fixtures	954,244	228,356	-0-	1,182,600
Machinery, equipment, and vehicles	1,616,517	154,445	(191,797)	1,962,759
Current construction lines	15,806	10,515	-0-	26,321
	53,344,108	993,532	(191,797)	54,145,843
Less accumulated depreciation				
Buildings	(846,631)	(105,411)	-0-	(952,042)
Tanks, stations, and lines	(18,426,521)	(1,233,070)	-0-	(19,659,591)
Meters and replacements	(989,260)	(100,520)	-0-	(1,089,780)
Furniture and fixtures	(588,828)	(115,328)	-0-	(704,156)
Machinery, equipment, and vehicles	(1,273,119)	(165,452)	189,494	(1,249,077)
Total accumulated depreciation	(22,124,359)	(1,719,781)	189,494	(23,654,646)
Net capital assets	$ 31,219,749	$ (726,249)	$ (2,303)	$ 30,491,197

1. Summary of Significant Accounting Policies (Continued):

G. Prepaid Expenses:

Prepaid expenses are amortized over their economic useful lives.

H. Deferred Debt Issue Costs:

Bond issue costs are capitalized and amortized over the various terms of the 1993, 2003, and 2006 bonds using the straight-line method. Amortization expense for the years ended December 31, 2006 and 2005 was $88,822 and $78,684, respectively.

I. Tap Fees:

To receive service, customers are required to pay a tap fee that varies depending on when the deposit was made and the size of the meter. Fees are refundable in the event expansion does not occur in an area.

J. Compensated Absences Payable:

Employees are granted vacation benefits in varying amounts to specified maximums depending on tenure with the Authority. After one year of service, employees are entitled to all accrued vacation leave upon termination.

Sick leave accumulates to employees at a rate of 4.6 hours for every 80 hours of service. Upon retirement, employees are entitled to 100% of their accumulated sick leave balance at the rate of pay at time of retirement if an employee was hired before December 31, 2000. If an employee is hired on or after January 1, 2001, and retires, their accumulated sick leave is paid out at the rate of pay that it was accrued. In the event of the employee’s death, 100% of their accumulated sick leave balance would be paid to the employee’s life insurance beneficiary. The employees’ accumulating rights to receive compensation for future absences are contingent upon the absences being caused by future illnesses, years of service at retirement, or death. A liability for unused sick leave is not recorded in the financial statements unless the employee has accumulated sick leave after becoming eligible for retirement, which would be payable in its entirety. The unrecorded estimated unused sick leave for the years ended December 31, 2006 and 2005 was $423,009 and $406,805, respectively; the recorded estimated unused sick leave and vacation for the years ended December 31, 2006 and 2005 reflected in the compensated absences payable amount on page 8 was $385,486 and $404,374, respectively.

K. Statements of Cash Flows:

For the purposes of the Statements of Cash Flows, all liquid investments (including restricted assets) with a maturity of three months or less when purchased are considered cash equivalents. Because the Authority, at its option, can withdraw amounts within a three month time period on the 5-year Treasury Bills, the Treasury Bills are considered to be cash equivalents. Cash and cash equivalents as of December 31, 2006 and 2005, consist of:

	2006	2005
Cash:		
General	$ 196,694	$ 174,023
Working capital	1,663,321	1,190,321
Capital improvements	1,350,678	1,850,679
Restricted cash and investments	7,154,342	5,602,290
	$10,365,035	$8,817,313

1. Summary of Significant Accounting Policies (Continued):

L. Use of Estimates:

The process of preparing financial statements in conformity with generally accepted accounting principles requires the use of estimates and assumptions regarding certain types of assets, liabilities, revenues, and expenses. Such estimates primarily relate to unsettled transactions and events as of the date of the financial statements. Accordingly, upon settlement, actual results may differ from estimated amounts.

M. Receivables:

The Authority considers receivables to be collectible with an allowance for doubtful accounts that is based on past amounts of uncollectible accounts.

N. Net Assets:

The Authority has restricted net assets which are restricted for future debt service reqirements. None of the Authority's restricted net assets of $4,468,935 were restricted by enabling legislation.

2. Restricted Funds:

A. Revenue Fund:

This fund receives all revenues from operations, and it is maintained in the custody of the Authority, separate and distinct from all other funds of the Authority. With the exception of investment income on funds other than the Revenue Fund, all revenue shall be deposited in the Revenue Fund. Expenditures from this fund are limited to all reasonable and proper expenses of operating, repairing, and maintaining the system, excluding depreciation and capital replacements. Also, required payments are made into the remaining funds from this fund.

B. Bond Reserve Fund:

This fund shall be maintained in the custody of the Trustee as a trust fund and shall be used solely for the payment of bond service charges on the bonds, and to the extent provided herein, by purchase for cancellation or redemption of bonds. Payment shall be made by the Authority on or before the 20th of each month to fund this account until the balance exceeds one year's bond requirements. This fund was fully funded at the time bonds were issued.

C. Bond Fund:

This fund is maintained in the custody of the Trustee as a trust fund and is used solely for the payment of bond service charges provided herein, by purchase for cancellation or redemption of bonds. The Authority is required by bond agreement to make monthly payments to the fund for interest and redemption payments on or before the 20th of each month.

D. Replacement and Improvement Fund:

This fund is maintained in the custody of the Trustee as a trust fund separate and distinct from all other funds of the Authority. The monies held in the Replacement and Improvement Fund are transferred to the Bond Fund, to the extent necessary from time-to-time, after applying to that purpose any monies then in the System Reserve Fund, to permit the payment of all obligations payable from the Bond Fund without drawing on the Bond Reserve Fund and, otherwise, shall be used solely to replace obsolete or worn-out equipment or to make improvements to the system, or, with funds in the Bond Fund and Bond Reserve Fund and other funds made available by the Authority, to retire by purchase or by call all or part of the Bonds from time-to-time outstanding. The Authority may borrow from this fund for any improvements unless it is in default of its bonds obligations.

2. Restricted Funds (Continued):

E. Project Fund:

This fund is maintained in the custody of the Trustee as a separate account and monies in the fund will be used for expansion and capital additions to the water system. The fund had a balance of $1,101,611 and $-0- as of December 31, 2006 and 2005, respectively.

F. System Reserve Fund (Capital Improvements):

This fund is maintained in the custody of the Authority as a trust fund separate and distinct from all other funds of the Authority. The monies held in the System Reserve Fund shall be transferred to the Bond Fund, to the extent necessary from time-to-time, to permit the payment of all obligations payable from the Bond Fund without drawing upon the Replacement and Improvement Fund or Bond Reserve Fund, or may be transferred to the appropriate fund of the Authority to permit the payment of principal and interest on any general obligation bonds, or notes issued in anticipation thereof, issued by the Authority to pay costs of improvements to the system, and otherwise may be used for any other lawful system purpose, including without limitation, the retirement of outstanding bonds by call for redemption or by purchase for cancellation.

G. Employee Policy Fund:

This fund is maintained in the custody of the Authority as a separate account. Payments of $10,000 are made each month. Monies in this fund will be used for employees entitled to 100% of their accumulated sick leave balance after becoming eligible for retirement.

H. Restricted Cash and Investments:

	2006	2005
Bond reserve fund	$2,408,981	$2,394,243
Bond fund	2,059,954	1,739,773
Replacement and improvement fund	773,351	761,638
Project fund	1,101,611	0
Employee policy fund	810,445	706,636
	$7,154,342	$5,602,290

3. Equity in Pooled Cash and Investment:

Active deposits are public deposits necessary to meet current demands on the Treasury. Such monies must be maintained either as cash in the Authority 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 five-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:

3. Equity in Pooled Cash and Investment (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, its political subdivisions, or other units or agencies of this State or its political subdivisions;
5. Time certificates of deposit or savings or deposit accounts, including, but not limited to, passbook accounts;
6. 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;
7. The State Treasurer's investment pool (STAR Ohio);
8. Securities lending agreements in which the District lends securities and the eligible institution agrees to exchange either securities described in division (1) or (2), or cash, or both securities and cash, equal value for equal value;
9. High grade commercial paper in an amount not to exceed five percent of the District's total average portfolio; and
10. Bankers acceptances for a period not to exceed 270 days and in an amount not to exceed ten percent of the District's average portfolio.

Protection of the Authority'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 Authority 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.

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 Authority, 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 Authority or, if the securities are not represented by a certificate, upon receipt of confirmation of transfer from the custodian.

Deposits – Custodial credit risk for deposits is the risk that in the event of bank failure, the Authority will not be able to recover deposits or collateral securities that are in the possession of an outside party.

3. Equity in Pooled Cash and Investment (Continued):

Based on the criteria described in GASB Statement No. 40, "*Deposits and Investment Risk Disclosures*", as of December 31, 2006 and 2005, $300,000 and $300,000 of the Authority's bank balances of $4,061,163 and $3,956,500 were covered by federal depository insurance. The remaining balances were covered by specific securities held by the pledging financial institution's trust department in the Authority's name. Although all State statutory requirements for the deposit of money have been followed, non-compliance with federal requirements could potentially subject the Authority to a successful claim by the FDIC.

The Authority has no deposit policy for custodial risk beyond the requirements of State statute. Ohio law requires that deposits be either insured or be protected by eligible securities pledged to and deposited either with the Authority or a qualified trustee by the financial institution as security for repayment, or by a collateral pool of eligible securities deposited with a qualified trustee and pledged to secure the repayment of all public monies deposited in the financial institution whose market value at all times shall be at least one hundred five percent of the deposits being secured.

Investments – For an investment, custodial credit risk is the risk that, in the event of the failure of the counterparty, the Authority will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party.

As of December 31, 2006, the Authority had the following investments:

		% of	Maturities (in Years)	
Investment Type	Fair Value	Total	Less than 1	1-5
Federal Home Loan Banks	$ 203,543	3%	$ 101,373	$ 102,170
Federal Home Loan Mortgage Corporation Discount Notes	392,665	6%	392,665	-
Federal National Mortgage Association	96,650	2%	96,650	-
First American Treasury Obligation	80,493	1%	80,493	-
Federated Treasury Obligation Fund	3,967,671	63%	3,967,671	-
U.S. Treasury Funds, Bonds, and Notes	1,602,875	25%	1,602,875	-
	$6,343,897			

As of December 31, 2005, the Authority had the following investments:

		% of	Maturities (in Years)	
Investment Type	Fair Value	Total	Less than 1	1-5
Federal Home Loan Banks	$ 174,379	4%	$ 174,379	$ -
Federal Home Loan Mortgage Corporation Discount Notes	99,000	2%	99,000	-
Federal National Mortgage Association	462,765	9%	462,765	-
First American Treasury Obligation	25,494	1%	25,494	-
Federated Treasury Obligation Fund	1,739,773	36%	1,739,773	-
U.S. Treasury Funds, Bonds, and Notes	2,394,243	48%	2,394,243	-
	$4,895,654			

Interest Rate Risk – Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. It is the Authority's policy to hold instruments to maturity, limiting any investment to a maximum of five years. The targeted weighted average days to maturity for the overall Authority portfolio is not more than two years. In addition, Ohio law prescribes that all Authority investments mature within five years of purchase, unless the investment is matched to a specific obligation or debt of the Authority.

3. Equity in Pooled Cash and Investment (Continued):

Credit Risk – Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. As of December 31, 2006, the Authority's investment in U.S. instrumentalities (Federal National Mortgage Corporation, Federal Home Loan Bank) were all rated AAA by Standard and Poor's and Aaa by Moody's Investors Service. As of December 31, 2005, the Authority's investment in U.S. instrumentalities (Federal National Mortgage Corporation, Federal Home Loan Bank) were all rated AAA by Standard and Poor's and Aaa by Moody's Investors Service.

Custodial Credit Risk – Custodial credit risk is the risk that, in the event of the failure of a counterparty to a transaction, the Authority will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. Consistent with the requirements of State Law, it is the policy of the Authority to require full collateralization of all investments other than obligations of the U.S. Government, its agencies and instrumentalities. The Authority's investment in U.S. agencies with fair values totaling $692,858 has maturities of $590,688 in less than one year and $102,170 within two years for the year ended December 31, 2006. The Authority's investment in U.S. agencies with fair values totaling $736,144 has maturities of $736,144 in less than one year. U.S. agencies are held in the account of U.S. Bank ("Trustee"), at the Federal Reserve Bank of Boston, Massachusetts. The Authority's securities associated with the principal and interest payment of bond proceeds in the amount of $5,651,039 and $4,159,510, for 2006 and 2005, respectively, are held in the account of First Merit. Assets held by the Trustee as a custodial agent are considered legally separate from the other assets of the Trustee.

Concentration of Credit Risk – Concentration of credit risk is the risk of loss attributed to the magnitude of investment in a single issuer. The Authority's investment policy provides that investments be diversified to reduce the risk of loss from over concentration in a single issuer, but does not identity specific limits on the amounts that may be so invested. More than five percent of the Authority's investments are in Federal Home Loan Mortgage Corporation Notes, Federated Treasury Obligation Fund, and U.S. Treasury Funds.

4. Long-Term Debt:

A summary of long-term debt for the year ended December 31, 2006, is as follows:

Description	Balance December 31, 2005	Borrowed	Repaid	Balance December 31, 2006	Due Within One Year
$890,000 Water Resource Revenue Refunding Bonds, Series 1999 originally issued with interest rates ranging from 4.000% to 5.875% with final maturity dates ranging from 2000 to 2009.	$ 8,510,000	$ -	$ 7,620,000	$ 890,000	$ 285,000
A note payable in the amount of $1,582,063 is due to FirstMerit Bank, N.A. and Trust. The note requires annual principal and interest payments at the One-Year U.S. Treasury Security Index plus 2.12% with a maturity date of September 2019. The note is guaranteed by the United States Department of Agriculture (USDA).	1,661,513	-	79,450	1,582,063	77,398
A Water Resource Improvement Revenue Bond, Series 2003A in the amount of $1,460,000 is due to the USDA. The Bond requires annual principal and interest payments at an annual interest rate of 4.875% with a maturity date of October 2018.	1,474,000	-	14,000	1,460,000	15,000
A Water Resource Improvement Revenue Bond, Series 2003B in the amount of $12,145,000 is due to USDA. The Bond requires annual principal and interest payments with interest rates ranging from 1.5% to 4.4% with a final maturity date of October 2018.	13,100,000	-	955,000	12,145,000	975,000
A Water Resource Improvement Revenue Bond, Series 2006 in the amount of $9,110,000 is due to USDA. The Bond requires annual principal and interest payments with interest rates ranging from 3.75% to 5.00% with a final maturity date of October 2031.	-	9,130,000	20,000	9,110,000	20,000
	$ 24,745,513	$ 9,130,000	$ 8,688,450	$ 25,187,063	$ 1,372,398

4. Long-Term Debt (Continued):

A summary of long-term debt for the year ended December 31, 2005, is as follows:

Description	Balance December 31, 2004	Borrowed	Repaid	Balance December 31, 2005	Due Within One Year
$890,000 Water Resource Revenue Refunding Bonds, Series 1999 originally issued with interest rates ranging from 4.000% to 5.875% with final maturity dates ranging from 2000 to 2009.	$ 8,770,000	$ -	$ 260,000	$ 8,510,000	$ 270,000
A note payable in the amount of $1,582,063 is due to FirstMerit Bank, N.A. and Trust. The note requires annual principal and interest payments at the One-Year U.S. Treasury Security Index plus 2.12% with a maturity date of September 2019. The note is guaranteed by the United States Department of Agriculture (USDA).	1,747,654	-	86,141	1,661,513	79,396
A Water Resource Improvement Revenue Bond, Series 2003A in the amount of $1,460,000 is due to the USDA. The Bond requires annual principal and interest payments at an annual interest rate of 4.875% with a maturity date of October 2018.	1,487,000	-	13,000	1,474,000	14,000
A Water Resource Improvement Revenue Bond, Series 2003B in the amount of $12,145,000 is due to USDA. The Bond requires annual principal and interest payments with interest rates ranging from 1.5% to 4.4% with a final maturity date of October 2018.	14,040,000	-	940,000	13,100,000	955,000
	$ 26,044,654	$ -	$ 1,299,141	$ 24,745,513	$ 1,318,396

The annual debt service requirements to maturity, including principal and interest, for long-term debt as of December 31, 2006, are as follows:

Year Ending December 31,	Principal	Interest	Total
2007	$ 1,372,398	$ 1,127,362	$ 2,499,760
2008	1,481,812	1,031,565	2,513,377
2009	1,538,390	957,779	2,496,169
2010	1,595,440	898,602	2,494,042
2011	1,668,289	830,800	2,499,089
2012 to 2043	17,530,735	7,128,610	24,659,345
Total	$ 25,187,063	$ 11,974,719	$ 37,161,782

4. Long-Term Debt (Continued):

The 1999, 2003, and 2006 Series bonds and USDA bonds are payable from the revenues of the Authority after the payment of operating and maintenance costs. The bonds are secured by a pledge of the monies and securities on deposit in the Reserve Fund, the Replacement and Improvement Fund, and the System Reserve Fund. The bond indenture requires, among other provisions, that the Authority maintain the system in good operating condition and charge rates such that the necessary debt service payments can be made after operating and maintenance charges have been paid. In addition, the indenture requires the establishment of certain funds as discussed in Note 2.

The FirstMerit Bank N.A. note is payable from the revenues of the Authority after the payment of operating and maintenance costs. The note is guaranteed by the United States Department of Agriculture.

5. Insurance:

The Authority maintains comprehensive insurance coverage with private carriers for real property, building contents, and vehicles. Vehicle policies include liability coverage for bodily injury and property damage. Real property and contents are 90 percent coinsured. The Authority is exposed to various tasks of loss related to torts, theft, damage to or destruction of assets, errors and omissions, employee injuries, and natural disasters. Settled claims have not exceeded this commercial coverage in any of the past three years. There has not been a significant reduction of coverage from the prior year.

6. Retirement Commitments:

A. Defined Benefit Pension Plans:

The Ohio Public Employees Retirement System (OPERS) administers three separate pension plans as described below:

1. The Traditional Pension Plan (TP) – a cost-sharing multiple-employer defined benefit pension plan.
2. The Member-Directed Plan (MD) – a defined contribution plan in which the member invests both member and employer contributions (employer contributions vest over five years at 20% per year). Under the Member-Directed Plan members accumulate retirement assets equal to the value of member and (vested) employer contributions plus any investment earnings thereon.
3. The Combined Plan (CO) – a cost-sharing multiple-employer defined benefit pension plan. Under the Combined Plan employer contributions are invested by OPERS to provide a formula retirement benefit similar in nature to the Traditional Pension Plan benefit. Member contributions, the investment of which is self-directed by the members, accumulate retirement assets in a manner similar to the Member-Directed Plan.

OPERS provides retirement, disability, and survivor benefits as well as postretirement health care coverage to qualifying members of both the Traditional Pension and Combined Plans. Members of the Member-Directed Plan do not qualify for ancillary benefits.

Authority to establish and amend benefits is provided by state statute per Chapter 145 of the Ohio Revised Code.

The Ohio Public Employees Retirement System issues a stand-alone financial report. Interested parties may obtain a copy by making a written request to OPERS, 277 East Town Street, Columbus, Ohio 43215-4642 or by calling (614) 222-5601 or 1-800-222-7377.

The Ohio Revised Code provides statutory authority for employee and employer contributions. For 2006 and 2005, member and employer contribution rates were consistent across all three plans. Separate divisions for law enforcement and public safety exist only within the Traditional Pension Plan.

6. Retirement Commitments (Continued):

A. Defined Benefit Pension Plans (Continued):

The 2006 and 2005 member contribution rates were 9.0% and 8.5% for the Authority.

The 2006 and 2005 employer contribution rates for the Authority were 13.7% and 13.55% of covered payroll.

The Authority's contributions to OPERS for the years ended December 31, 2006, 2005, and 2004, were $333,980, $335,183 and $453,894, respectively. These contributions were equal to the required contributions for fiscal years 2006, 2005 and 2004.

B. Post-Employment Benefits:

Ohio Public Employees Retirement System (OPERS) administers three separate pension plans: The Traditional Pension Plan (TP) – a cost-sharing multiple-employer defined benefit pension plan; the Member-Directed Plan (MD) – a defined contribution plan; and the Combined Plan (CO) – a cost-sharing multiple-employer defined benefit pension plan that has elements of both a defined benefit and defined contribution plan.

OPERS provides retirement, disability, and survivor benefits as well as postretirement health care coverage to qualifying members of both the Traditional and the Combined Plans. Members of the Member-Directed Plan do not qualify for ancillary benefits, including post employment health care coverage.

In order to qualify for post-retirement health care coverage, age and service retirees under the Traditional Pension and Combined Plans must have 10 or more years of qualifying Ohio service credit. Health care coverage for disability benefit recipients and qualified survivor benefit recipients is available. The health care coverage provided by OPERS is considered to be an Other Post Employment Benefit (OPEB) as described in GASB Statement No. 12.

A portion of each employer's contribution to OPERS is set aside for the funding of post retirement health care. The Ohio Revised Code provides statutory authority for employer contributions. For local government employer units, the rate was 13.70% and 13.55% of covered payroll for both fiscal years 2006 and 2005; respectively. The portion of employer contributions allocated for healthcare was 4.5% and 4.0% for the years 2006 and 2005, respectively.

The Ohio Revised Code provides the statutory authority requiring public employers to fund postretirement health care through their contributions to OPERS, Summary of Assumptions:

Actuarial Review - The assumptions and calculations below were based on OPERS' latest Actuarial Reviews performed as of December 31, 2005.

Funding Method – An individual entry age 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.

Assets Valuation Method – 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 deprecation on investment assets annually, not to exceed a 12% corridor.

Investment Return – The investment assumption rate for 2005 was 6.50%.

Active Employee Total Payroll – An annual increase of 4.0%, compounded annually, 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 4.0% base increase, were assumed to range from 0.5% to 6.3%.

Health Care – Health care cost were assumed to increase at the projected wage inflation rate plus an additional factor ranging from 0.5% to 6% for the next 9 years. In subsequent years (10 and beyond) health care costs were assumed to increase at 4% (the projected wage inflation rate).

6. Retirement Commitments (Continued):

B. Post-Employment Benefits (Continued):

OPEB is advance-funded on an actuarially determined basis. The following disclosures are required:

1. The Traditional Pension and Combined Plans had 369,214 active contributing participants as of December 31, 2006. The number of active participants for both plans used in the December 31, 2005, actuarial valuation was 358,804.
2. The employer contributions that were used to fund post employment benefits were $24,991 for 2006 and $33,347 for 2005.
3. The amount of $11.1 billion represents the actuarial value of OPERS' net assets available for OPEB at December 31, 2005.
4. Based on the actuarial cost method used, the Actuarial Valuation as of December 31, 2005, reported the actuarial accrued liability and the unfunded actuarial accrued liability for OPEB at $31.3 billion and $20.2 billion, respectively.

OPERS Retirement Board adopts its Health Care Preservation Plan.

The Health Care Preservation Plan (HCPP) adopted by the OPERS Retirement Board on September 9, 2004, is effective on January 1, 2007. OPERS took additional actions to improve the solvency of the Health Care Fund in 2005 by creating a separate investment pool for health care assets. Member and employer contribution rates increased as of January 1, 2006 and January 1, 2007, which will allow additional funds to be allocated to the health care plan.

C. Retirement Incentive Plan:

The Authority adopted the Retirement Incentive Plan, which is adopted under guidelines of the Ohio Public Employees Retirement System. Participation in the Plan shall be available to five percent (5%) of employees of the Authority, per year, who are employed at their offices and are members of Ohio Public Employees Retirement System. Pursuant to the terms of the Plan, service credit for each participating employee shall be purchased by the Authority in an amount equal to the lesser of the following:

1. Five (5) years of service credit or
2. An amount of service credit equal to 1/5 of the total service of record credited to the participating employee in the OPERS, exclusive of the service credit purchased under this plan.

An employee of the Authority eligible to participate in the Plan shall meet the following criteria:

1. The employee is or will be eligible to retire under the Ohio Public Employees Retirement System of the Ohio Revised Code on or before the date of termination of the Plan.
2. The employee agrees to retire within 90 days after receiving notice from OPERS that service credit has been purchased for the employee pursuant to the Plan.
3. Employees with less than eighteen (18) months of service with the Authority shall have the right to elect to participate in this Plan only after all other eligible employees have been given the opportunity to elect to participate.

Retirement Incentive Plan payments for the years ended December 31, 2006 and 2005, was $102,471 and $-0-, respectively.

7. Leasing Arrangements:

The Authority leases two copiers under 48-month operating leases that began in January 2004 and April 2006, and expire in December 2006 and March 2010, respectively. These leases require rent in the amount of $322 and $437 per month plus charges for additional copies over 2,000 and 5,000, respectively.

The following is a schedule of future minimum rental payments required under the above operating leases as of December 31, 2006:

Year Ending December 31,	Amount
2007	$ 5,244
2008	5,244
2009	5,244
2010	1,311
	$17,043

Office equipment lease for the years ended December 31, 2006 and 2005, was $14,994 and $15,232, respectively.

8. Commitments:

A. Water Purchase Agreements:

The Authority's original and primary source of water (approximately 87.4%) has been the City of Avon Lake's water treatment plant located in northern Lorain County. On April 30, 1975, the Authority signed a long-term water purchase agreement with the City of Avon Lake with maximum amounts of water to be supplied per month.

The Authority purchases water from the Village of New London (approximately 10.7%) as a supplement to the water purchased from the City of Avon Lake. In addition to the Avon Lake agreement, the Authority signed a long-term water purchase agreement in 1996 with New London with maximum amounts of water to be supplied per month.

B. Water Supply Agreements:

The Authority has long-term agreements with various villages and municipalities to provide water in emergencies and at monthly bulk rates. The terms of the agreements vary with each municipality as to rate and period of time.

9. Changes in Accounting Principles:

For 2006, the District implemented GASB Statement No. 40, *Deposits and Investment Risk Disclosures,* GASB Statement No. 42, *Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries*, GASB Statement No. 46, *Net Assets Restricted by Enabling Legislation,* and GASB Statement No. 47, *Accounting for Termination Benefits*. GASB Statement No. 40 establishes the requirement of the disclosure of certain risks related to deposits and investments. GASB Statement No. 42 establishes accounting and financial reporting standards for impairment of capital assets. GASB Statement No. 46 requires that limitations on the use of net assets imposed by enabling legislation be reported as restricted net assets. GASB Statement No. 47 establishes accounting standards for termination benefits. The application of these new standards did not have a material effect on the financial statements, nor did their implementation require a restatement of prior year balances.

10. Investment in Joint Venture and Restatement of Net Assets:

The Authority is a member of the Medina-Lorain Water Consortium (the Consortium), which is a joint venture between the City of Avon Lake, the City of Medina, Medina County, and the Rural Lorain County Water Authority. The Consortium was created in 1999 for the purpose of construction, operation and maintenance of a water transmission line to serve members of the Consortium, and for the purpose of bulk water delivery from the City of Avon Lake. There is an ongoing financial responsibility for all parties for the maintenance and repair of the project. The Consortium is governed by representatives of the member parties. The City of Avon Lake serves as the fiscal agent for the Consortium. As of December 31, 2006 and 2005, the Authority's equity interest in the Consortium was $5,466,543 and $5,621,256, respectively. Financial information can be obtained from Joe Newlin, City of Avon Lake Finance Director, 150 Avon Beldon Road, Avon Lake, Ohio 44012.

The investment in joint venture was recorded as a capital asset in fiscal year 2004, therefore the capital assets and investment in joint venture of the Authority were misstated. The following reflects the adjustment for the reclassification of the investment:

	Enterprise Fund
Net Assets December 31, 2004	$ 19,979,956
Depreciable Capital Assets	(6,188,539)
Accumulated Depreciation	412,569
Investment in Joint Venture	5,775,970
Restated Net Assets December 31, 2004	$ 19,979,956

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Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based On an Audit of Financial Statements Performed in Accordance With *Government Auditing Standards*

To the Board of Directors
Rural Lorain County Water Authority
42401 State Route 303
Lagrange, Ohio 44050

We have audited the accompanying financial statements of the business-type activities of the Rural Lorain County Water Authority (the Authority), Lorain County, as of and for the years ended December 31, 2006 and 2005, which collectively comprise the Authority's basic financial statements as listed in the table of contents, and have issued our report thereon dated July 20, 2007, in which we indicated the Authority implemented Governmental Accounting Standards Board Statements No. 40, 42, 46 and 47. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

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

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed below, we identified a certain deficiency in internal control over financial reporting that we consider to be a significant deficiency.

A control deficiency 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 misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control over financial reporting. We consider the deficiency described in the accompanying schedule of findings and responses as item 2006-001 to be a significant deficiency in internal control over financial reporting.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the entity's internal control.

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, we do not believe that the significant deficiency described above is a material weakness.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Authority's basic financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed an instance of noncompliance that is required to be reported under *Government Auditing Standards* and which is described in the accompanying schedule of findings and responses as item 2006-002.

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

This report is intended solely for the information and use of the audit committee, management and the Board of Directors, and is not intended to be and should not be used by anyone other than these specified parties.

Balestra, Harr & Scherer

Balestra, Harr & Scherer, CPAs, Inc.

July 20, 2007

RURAL LORAIN COUNTY WATER AUTHORITY

SCHEDULE OF FINDINGS AND RESPONSES
FOR THE YEARS ENDED DECEMBER 31, 2006 AND 2005

FINDINGS RELATED TO THE FINANCIAL STATEMENTS REQUIRED TO BE REPORTED IN ACCORDANCE WITH GAGAS

FINDING NUMBER 2006-001

Significant Control Deficiency

The basic financial statements submitted by the Authority for audit required a number of audit corrections and modifications to the reporting format to properly comply with Governmental Accounting Standards Board (GASB) Statement Numbers 40, 42, 46, & 47 reporting requirements. An audit adjustment was also made to correctly report the Authority's investment in joint venture and to restate its capital assets accordingly. The Authority should make arrangements with its consultants to ensure that the format and content of the financial statements in future years incorporates the audit corrections and modifications made during this audit period, as well as, proper implementation of any new pronouncements for those years. Furthermore, the Authority should implement control procedures over year end reporting to ensure its compiled financial report is accurate and complete.

Client Response

We are in agreement on changes to be made to the financial statements based on GASB 34 in regards to basic financial statements including the management's discussion and analysis for state and local governments.

We are in agreement on the changes in the notes to the financial statements based on GASB 40 in regards to deposit and investments risk disclosures.

GASB 42 regarding accounting and financial reporting for the impairment of capital assets does not apply to Rural Lorain County Water Authority since the Authority has no capital assets that are impaired. If a disclosure is required, it will be made.

GASB 46 regarding net assets restricted by enabling legislation does not apply to Rural Lorain County Water Authority since there are no assets of the Authority that are restricted by enabling legislation. If a disclosure is required it will be made.

There is a disclosure for GASB 47 in the financial statements, Note 6c. If additional information is needed to make the note more accurate and relevant, the wording will be added.

FINDING NUMBER 2006-002

Noncompliance Citation

Ohio Revised Code Section 5705.41(D) states that no orders or contracts involving the expenditure of money are to be made unless there is a certificate of the fiscal officer that the amount required for the order or contract has been lawfully appropriated and is in the treasury or in the process of collection to the credit of an appropriate fund free from any previous encumbrances.

FINDINGS RELATED TO THE FINANCIAL STATEMENTS
REQUIRED TO BE REPORTED IN ACCORDANCE WITH GAGAS

FINDING NUMBER 2006-002 (Continued)

The statute provides the following exceptions to this basic requirement:

Then and Now Certificate: This exception provides that, if the fiscal officer can certify that both at the time that the contract or order was made and at the time that the certificate is completed, sufficient funds were available or in the process of collection, to the credit of a proper fund, properly appropriated and free from any previous encumbrance, the taxing authority can authorize the drawing of a warrant. The taxing authority has 30 days from the receipt of such certificate to approve payment by resolution or ordinance. If approval is not made within 30 days, there is no legal liability on the part of the subdivision or taxing district.

Amounts of less than $3,000, may be paid by the fiscal officer without such affirmation of the taxing authority upon completion of the "then and now" certificate, provided that the expenditure is otherwise lawful. This does not eliminate any otherwise applicable requirement for approval of expenditures by the taxing authority.

The Authority did not obtain purchase orders for all expenditures, nor did it obtain "then and now" certification when appropriate.

The Authority should complete purchase orders or "then and now" certificates for all purchases.

Client Response

For many, many years the Rural Lorain County Water Authority (RLCWA) has note obtained purchase orders for recurring items such as payroll deductions and employee benefit type items. Neither has RLCWA obtained purchase orders for routine utility bills. In light of the citation, we will be reviewing our procedures for purchase orders.

Mary Taylor, CPA
Auditor of State

RURAL LORAIN COUNTY WATER AUTHORITY

LORAIN 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
NOVEMBER 8, 2007

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