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**Diamond Valley Water User's Corporation**

**Financial Statements**

**Year Ended December 31, 2006**

Arizona Corporation Commission

**DOCKETED**

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**Diamond Valley Water User's Corporation**

**Financial Statements**

**For the Year Ended December 31, 2006**

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# Darlene Wood

*Certified Public Accountant*

## INDEPENDENT AUDITOR'S REPORT

To the Management of  
**Diamond Valley Water User's Corporation**  
Prescott Valley, Arizona

I have audited the accompanying balance sheet of Diamond Valley Water User's Corporation as of December 31, 2006, and the related statements of income, retained earnings, and cash flows for the year then ended. These financial statements are the responsibility of Diamond Valley Water User's Corporation management. My responsibility is to express an opinion on these financial statements based on my audit.

Except as discussed in the following paragraph, I conducted my audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that I 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 significant estimates made by management, as well as evaluating the overall financial statement presentation. I believe that my audit provides a reasonable basis for my opinion.

Because of the inadequacy of accounting records for the years prior to 2006, I am unable to form an opinion regarding the amounts at which property and equipment and accumulated depreciation are recorded in the accompanying balance sheet at December 31, 2006 (stated at \$97,202 and \$44,545 respectively), or the amount of depreciation expense for the year then ended (stated at \$5,674). Also, in accordance with the terms of our engagement, we have not applied audit procedures necessary to satisfy ourselves about the classifications and amounts comprising the balance sheet at December 31, 2005. The classifications and amounts comprising the balance sheet at that date materially affect the determination of the results of operations and cash flows for the year ended December 31, 2006.

Because of the matter discussed in the preceding paragraph, the scope of our work was not sufficient to enable us to express, and we do not express, an opinion on the results of operations and cash flows for the year ended December 31, 2006, or on the consistency of application of accounting principles with the preceding year.

In our opinion, except for the effects of such adjustments, if any, as might have been determined to be necessary had prior-year records concerning property and equipment and related accumulated depreciation been adequate, the accompanying balance sheet referred to in the first paragraph presents fairly, in all materials respects, the financial position of Diamond Valley Water User's Corporation as of December 31, 2006, in conformity with accounting principles generally accepted in the United States of America.

  
Darlene Wood, CPA

Prescott, Arizona  
May 23, 2007

# Diamond Valley Water User's Corporation

## Balance Sheet

As of December 31, 2006

### ASSETS

#### CURRENT ASSETS

Cash (Note 3)	\$	15,736
Accounts receivable (Note 4)		9,980
Inventory		2,938
Prepaid expenses		964
Total current assets		<u>29,618</u>

#### PROPERTY AND EQUIPMENT

Property and equipment (Note 5)		97,202
Less accumulated depreciation		<u>(44,545)</u>
Net property and equipment		<u>52,657</u>

TOTAL ASSETS \$ 82,275

### LIABILITIES AND STOCKHOLDERS' EQUITY

#### CURRENT LIABILITIES

Accounts payable and accrued expenses (Note 6)	\$	24,827
Customer deposits (Note 3)		12,550
Deferred revenue (Note 7)		250
Property tax payable (Note 6)		4,490
Sales tax payable		1,699
Property tax (back taxes - Note 6)		1,625
Water charge balance (Note 6)		1,023
Water facility charge (Note 6)		<u>47,500</u>
Total current liabilities		<u>93,964</u>

#### EQUITY

Retained earnings		<u>(11,689)</u>
Total equity		<u>(11,689)</u>

TOTAL LIABILITIES AND EQUITY \$ 82,275

See accompanying notes to financial statements

**Diamond Valley Water User's Corporation**  
**Statement of Income**  
**For the Year Ended December 31, 2006**

REVENUES	
Water sales	\$ 345,658
Surcharge collections	21,000
Non utility income	3,000
Establishment fees	3,290
Total revenue	<u>372,948</u>
COST OF GOODS SOLD	
Cost of water	<u>163,326</u>
Total cost of goods sold	<u>163,326</u>
GROSS PROFIT	209,622
GENERAL AND ADMINISTRATIVE EXPENSE	<u>125,737</u>
Operating income	83,885
OTHER INCOME (EXPENSE)	
Miscellaneous income	250
Interest expense	<u>(328)</u>
Total other income (expense)	(78)
INCOME BEFORE INCOME TAXES	83,807
STATE INCOME TAX	<u>(50)</u>
NET INCOME	83,757
Retained earnings, beginning of year	(34,199)
Prior period adjustments (Note 12)	<u>(61,247)</u>
Retained earnings, end of year	<u>\$ (11,689)</u>

See accompanying notes to financial statements

**Diamond Valley Water User's Corporation**  
**Statement of Cash Flows**  
**For the Year Ended December 31, 2006**

**Reconciliation of operating income to net cash provided by operating activities:**

Operating income	\$ 83,757
Adjustments to reconcile operating income to net cash provided by operating activities:	
Depreciation	5,674
Changes in assets and liabilities:	
(Increase) Decrease in accounts receivable	(9,980)
(Increase) Decrease in other assets	(964)
(Increase) Decrease in inventory	(2,938)
Increase (Decrease) in accounts payable and accrued expenses	<u>51,828</u>
Net cash provided by operating activities	<u>127,377</u>
 <b>Cash flows from capital and related financing activities:</b>	
Additions to capital assets	<u>(58,330)</u>
Net cash used by capital and related financing activities	<u>(58,330)</u>
 Net increase in cash and cash equivalents	69,047
 Prior period adjustments (Note 7)	(61,247)
 Cash and cash equivalents at beginning of year	<u>7,936</u>
 Cash and cash equivalents at end of year	<u>\$ 15,736</u>

See accompanying notes to financial statements

**Diamond Valley Water User's Corporation**  
**Statement of Retained Earnings**  
**For the Twelve Months Ended December 31, 2006**

	<u>December 31, 2006</u>
Net Income	\$ 83,757
Retained Earnings (Deficit) at December 31, 2005	(34,199)
Prior period adjustments (Note 12)	<u>(61,247)</u>
Retained Earnings (Deficit) at December 31, 2006	<u>\$ (11,689)</u>

See accompanying notes to financial statements

**Diamond Valley Water User's Corporation**  
**Summary of General and Administrative Expenses**  
**For the Year Ended December 31, 2006**

Bad debts expense	\$ 1,400
Depreciation expense	5,674
Consultation expense	9,030
Property tax expense	8,208
Insurance expense	566
Legal expenses	190
Miscellaneous expense	99
Accounting fees	463
Postage	3,957
Printing	451
Software	450
Telephone expense	688
Utilities expense	16,488
Locates	223
Management fee (Note 7)	67,170
Water testing	470
Meter fee refund	405
Repairs and maintenance	<u>9,805</u>
Total general and administrative expenses	<u>\$ 125,737</u>

See accompanying notes to financial statements

Diamond Valley Water User's Corporation  
Notes to Financial Statements  
December 31, 2006

NOTE 1 – DESCRIPTION OF ENTITY

Description of Operations

Diamond Valley Water User's Corporation (the Company) is a regulated by the Arizona Corporation Commission (Commission). It provides water to residents in the Diamond Valley, Arizona area. In a previous year, the Company's corporate status was administratively dissolved by the Arizona Corporation Commission for failure to file annual reports under A.R.S. Title 10. In accordance with Arizona Corporation Commission Decision No. 63547 (April 1, 2001), the Division has been vested with the authority to appoint an interim manager for the Company in order to continue operations (Note 7). The Company operates under the Commission's Rules on Water established by the Arizona Administrative Code, Title 14, Article 4.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation and Accounting

The significant accounting policies followed by the Corporation, as summarized below, are in conformity with generally accepted accounting principles applicable to governmental units as promulgated by the Financial Accounting Standards Board (FASB) in the United States of America.

Accounts Receivable

Accounts receivable are reported at the amount of principal outstanding. Balances are written off through charges to earnings only after management has exhausted reasonable collection efforts and concluded that additional collection efforts are not cost-effective.

Estimates

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

Cash

For purposes of the statements of cash flows, the Company considers all demand deposit accounts and highly liquid debt instruments purchased with a maturity of three months or less to be cash equivalents.

Plant and Equipment

All improvements to the water system or new services are capitalized and are carried at cost over a fifteen year period. The Company has set a capitalization limit of \$1,000. Depreciation is recorded using the straight line method over periods ranging from three to fifteen years. Depreciation for the year ending December 31, 2006 was \$5,674.

Inventory

Inventory consists principally of capital items that are recorded as inventory when purchased. Depreciation of said inventory will begin when inventory is placed into service.

Operating Revenues and Expenses

Operating revenues and expenses consist of those revenues that result from the ongoing principal operations of the Company. Operating revenues consist primarily of charges for services. Nonoperating revenues and expenses consist of those revenues and expenses that are related to financing and investing type of activities and result from nonexchange transactions or ancillary activities.

Diamond Valley Water Users Corporation  
Notes to Financial Statements  
December 31, 2006

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Equity

Equity comprises the various net income (loss) from operations, and nonoperating revenues and expenses.

NOTE 3 – CASH AND RESTRICTED CASH

Deposits

The carrying amount of the Company's deposits was \$15,736 and the bank balance was \$28,826. The difference between the bank balance and the carrying amount represents outstanding checks and deposits in transit.

Restricted Cash

At December 31, 2006 the Company held 148 customer deposits at \$80 per deposit for a total amount of \$11,840 in reserves. Per R14-2-403, section B.3 of the Arizona Corporation Commission's Rules on Water, interest on deposits shall be calculated annually at an interest rate filed by the utility and approved by the Arizona Corporation Commission in a tariff proceeding. In absence of such, the interest rate shall be 6%. The Company has no such tariff and customers' deposits accrue at 6% annually. The total amount of accrued interest on security deposits for the year ending December 31, 2006 was \$710. The total amount held as restricted cash for the Company's customer deposits totaled \$12,550.

NOTE 4 – ACCOUNTS RECEIVABLE

The Company's receivables primarily consist of amounts due from individuals and businesses in the Diamond Valley, Arizona area. The total accounts receivables were \$9,980 for the year ending December 31, 2006. There was no allowance for doubtful accounts for the same period. Uncollectible accounts written off totaled \$1,400 at December 31, 2006.

NOTE 5 – PROPERTY, PLANT AND EQUIPMENT

Property, plant, and equipment detail for the period ending December 31, 2006 follows:

	<u>Cost</u>	Accum. <u>Depr.</u>	Cost, Net of Accum Depr.
2006 Capital Improvements	44,073	3,066	41,007
Ramada Pump Station	30,500	24,833	5,667
Rose Quartz East Pump Station	8,500	8,500	-
Opal Pump Station	6,364	4,073	2,291
Rose Quartz West Pump Station	-	-	-
Lisa Pump Station	2,038	2,038	-
Emerald Pump Station	500	500	-
Corner of Ramada and Victor	500	500	-
Office Equipment	4,727	1,035	3,692
Total	<u>97,202</u>	<u>44,545</u>	<u>52,657</u>

Diamond Valley Water User's Corporation  
Notes to Financial Statements  
December 31, 2006

NOTE 6 – CURRENT LIABILITIES

The Company purchases water from the Town of Prescott Valley and in December of 2005 it came to the attention of current management (Note 7) that the Company owed \$30,923 to the Prescott Valley Water District for unpaid back water charges. The remaining balance for the back water charge at December 31, 2006 totaled \$1,023. This amount is reflected in the financial statements.

A balance due of \$47,500 to the Prescott Valley Water District for prior year accrued water facility charges were identified during the fiscal year. No amounts have been paid on this debt at December 31, 2006. The Company has agreed to pay \$2,300 a month for said balance starting January 2007.

Additionally, in August of 2006, a debt of \$13,405 to for back property taxes was identified. The amount remaining unpaid at December 31, 2006 totaled \$1,625. 2006 property tax payable totaled \$4,490.

Accounts payable for the year ending December 31, 2006 amounted to \$24,827. This amount is comprised of \$13,785 due to the Town of Prescott Valley for December 2006 water usage, \$11,000 due to Don's Water Company for multiple repair and maintenance services (see NOTE 10) and other minor payables in the amount of \$42.

Customer deposits totaled \$12,550.

NOTE 7 – CONTRACTUAL AGREEMENTS

On September 13, 2005 the Commission entered into a management agreement with the current manager. The agreed upon fee for the operations and management of the water system is \$4,000 per month or \$9 per meter, whichever was greater. The contract may be cancelled by either party with 30 days written notice. It is agreed that the manager is separate and independent of the Company and as such, is not responsible or liable for any violations, judgments, claims, or debt incurred prior to his management term. Fees paid by the Company to the manger for the year ending December 31, 2006 totaled \$67,170.

On August 30, 2006 the Company entered into an agreement with Shepard Wesnitzer, Inc. The purpose of the agreement was for Shepard Wesnitzer, Inc. to provide engineering services to the Company for completing an infrastructure design of the water system for the Company in accordance with ADEQ and City of Prescott standards. The total proposed cost of the engineering services is \$63,000, of which \$35,000 is to be paid directly to Shepard Wesnitzer, Inc., by a WIFA grant (See NOTE 8) and the remaining \$28,000 paid directly by the Company. The total amount paid by the Company for the contractual agreement as of December 31, 2006 was \$7,117 which consists of a \$6,300 retainer along with expenses of \$817.

In August of 2000, the Company entered into an easement agreement with Verizon Wireless. It was agreed that Verizon would pay to the company the amount of \$250 per month as compensation for a tract of land in which Verizon has authority to construct, reconstruct, modify, operate, maintain, and remove telecommunication equipment. The agreement further states that Verizon shall hold ingress and regress rights to said property. The term of the contract is for twenty-five years. The total amount of non-utility income for rental of the property was \$3,000 for the year ending December 31, 2006. The total amount of deferred revenue under the agreement for the year ending December 31, 2006 was \$250.

Diamond Valley Water Users Corporation  
Notes to Financial Statements  
December 31, 2006

NOTE 8 – WIFA GRANT

For the year ending December 31, 2006 the Company has been awarded a Drinking Water Project grant from the Water Infrastructure Finance Authority (WIFA) agency. Under the terms of the grant, the Company may receive benefits for WIFA approved expenses. In accordance with the provisions of the grant, WIFA will pay pre-approved expenses directly to WIFA-approved vendors. For expenses to be pre-approved by WIFA, proper grant reporting guidelines must be followed in addition to the Company's financial obligation of matched funds described more specifically in Note 7 of these financial statements. As of the financial statement date, specific reporting requirements have not been met. No grant expenditures have been paid by WIFA as of December 31, 2006.

NOTE 9 – RISK MANAGEMENT

The Company is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; and natural disasters. The Company carries commercial property, general liability, commercial crime, and business automobile insurance for all such risks of loss. Settled claims resulting from these risks have not exceeded commercial insurance coverage in any of the past three years.

NOTE 10 – RELATED PARTY TRANSACTIONS

The Company currently receives repair, maintenance, and construction services from Don's Water Company, the management company, which is separate and apart from the monthly maintenance agreement (Note 7). Fees for service are billed to the Company when incurred by Don's Water Company.

Additionally, the Company collects construction fees on behalf of Don's Water Company for construction costs of new water services. Since the fee is collected on the behalf of Don's Water Company and is not revenue to the Company, the fee is booked as a liability when collected from the customer and is reversed when payment is made to Don's Water Company.

NOTE 11 – WATER CAPACITY FEE

The Company collects a \$1,200 water capacity fee for the installation of all new meters. The fee is collected on behalf of the Town of Prescott Valley and is not revenue to the Company. As such, the fee is booked as a liability when collected from the customer and reversed when payment is made to the Town of Prescott Valley.

NOTE 12 – PRIOR PERIOD ADJUSTMENTS

No fixed assets had been recorded to the Company's financial statements prior to December 31, 2006. A prior period adjustment to establish assets and accumulated depreciation was posted for a net prior period adjustment of \$6,667. Additional prior period adjustments include the establishment of balance sheet accounts for prior periods in the amount of \$54,580. The total net prior period adjustment for the year ending December 31, 2006 was \$61,247.

NOTE 13 – SUBSEQUENT EVENTS

As of the date of the financial statements, the Arizona Corporation Commission was considering relinquishing control of the Company by means of forming an independent Domestic Water Improvement District. No agreement has been made and no date has been established as to when the Commission's authority over the Company might be transferred.

