

NEW APPLICATION

ORIGINAL



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RECEIVED

BEFORE THE ARIZONA CORPORATION COMMISSION

JAN 29 11:56

COMMISSIONERS

AZ CORP COMMISSION
DOCKET CONTROL

KRISTIN K. MAYES, Chairman
GARY PIERCE
PAUL NEWMAN
SANDRA D. KENNEDY
BOB STUMP

Arizona Corporation Commission
DOCKETED

JAN 29 2009

G-02527A-09-0032

DOCKETED BY [Signature]

IN THE MATTER OF THE APPLICATION OF)
GRAHAM COUNTY UTILITIES, INC. GAS)
DIVISION FOR APPROVAL OF A LOAN)

DOCKET NO. G-02527A-09-____
FINANCE APPLICATION

Pursuant to A.R.S. § 40-301 et seq., Graham County Utilities, Inc. Gas Division ("GCU"), hereby files with the Arizona Corporation Commission ("Commission") an Application ("Finance Application") for authorization to borrow \$800,000 from the National Rural Utilities Cooperative Finance Corporation ("CFC") to finance prior construction of plant in accordance with GCU's construction work plan. In support of its Finance Application, GCU states as follows:

1. GCU is a non-profit corporation and public service corporation.

GCU holds a Certificate of Convenience and Necessity, to provide Gas Distribution Service to its member-customers in Graham County, Arizona.

2. The Commission has jurisdiction over GCU and the subject matter of this Finance Application.

3. GCU currently provides gas service to approximately 5,061 members.

4. On January 7, 2009, GCU's Board of Directors approved a Resolution to make application to the CFC for a loan in the approximate amount of \$1,050,000 (\$800,000 for GCU

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1 Gas Division, \$250,000 for GCU Water Division), to finance prior construction of plant. GCU
2 has attached to this application a schedule showing the net plant additions for the years 2000
3 through 2008. Among other things, GCU expended funds on new gas mains, services, meters and
4 regulators and miscellaneous distribution equipment to improve and work on the gas distribution
5 system. Graham County Electric Cooperative Inc. ("GCEC") has provided temporary financing
6 to GCU for these plant additions. GCU will be using the CFC Loan to repay GCEC for funds that
7 it has advanced to GCU.
8

9 5. GCU submitted an application for long-term financing to CFC in the amount of
10 \$1,050,000 (\$800,000 for GCU Gas Division, \$250,000 for GCU Water Division), with a
11 maturity date to cover a period of thirty (30) years, to fund the construction of the facilities
12 identified in GCU's schedule of net plant additions. On January 12, 2009, GCU received a
13 conditional commitment letter (attached) from CFC to finance up to \$1,050,000 contingent upon
14 and subject to the following condition among five others:
15

16 * a guaranty from Graham County Electric Cooperative Inc., in the amount
17 of the total credit facility extended to Graham County Utilities, secured by a first
18 mortgage lien on Graham County Utilities' assets and revenues.

19 6. A copy of the GCU Board of Directors' resolution approving the submission of the
20 CFC Loan Application is attached here to. A copy of the Graham County Electric Cooperative
21 Inc. Board of Directors' resolution approving the guarantee of the CFC Loan Application is also
22 attached here to.
23

1 7. GCU intends to repay, in substantial part, the cost of the CFC Loan
2 over a thirty (30) year period through the use of its general funds. GCU intends to file an
3 application for a rate case within the next month for both the Gas and Water Division

4 8. GCU's CFC Loan request is: (1) for lawful purpose; (2) within
5 GCU's corporate powers; (3) compatible with the public interest; (4) within sound financial
6 practices; and (5) within the proper performance of the Cooperative as a public service
7 corporation. The CFC Loan will improve GCU's ability to continue to provide safe and reliable
8 gas distribution service to its member-customers.

9
10 9. The CFC Loan is dependant upon authorization by this Commission.

11 10. The aggregate amount of securities outstanding, and proposed to be
12 outstanding, will not exceed the fair value of GCU's properties and business. A copy of GCU's
13 audited financial statements for the years ended September 30, 2008 and 2007 is also attached
14 here to.

15
16 11. GCU requests that the Commission act on this application as soon as possible to
17 assist GCU financially to maintain reliable gas distribution service.

18 12. All correspondence with regard to this Finance Application should be
19 sent to:

20
21 John V. Wallace
22 Grand Canyon State Electric Cooperative Association, Inc.
23 120 N. 44th Street, Suite 100
 Phoenix, Arizona 85034
 E-mail: jwallace@gcseca.coop

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With a copy to:

Russ Barney
GRAHAM COUNTY ELECTRIC COOPERATIVE, INC.
P. O. Drawer B
Pima, Arizona 85543
Email: russb@gce.coop

WHEREFORE, GCU, having fully stated its Application and showing that it is in the public interest for the Cooperative to obtain the CFC Loan to fund prior construction of facilities to serve its member-customers, hereby requests that the Commission:

1. Accept GCU's Finance Application for filing.
2. Authorize GCU to borrow \$1,050,000 (\$800,000 for GCU Gas Division, \$250,000 for GCU Water Division) from CFC for the lawful purposes set forth in this Finance application, and to authorize the Cooperative to take such actions necessary and appropriate to execute a mortgage to secure the CFC Loan; and
3. Grant such other relief as may be in the public interest.

RESPECTFULLY SUBMITTED this 29th day of January 2009.

By 
John V. Wallace
Grand Canyon State Electric Cooperative Association, Inc.
120 N. 44th Street, Suite 100
Phoenix, Arizona 85034

1 Original and thirteen (13) copies of
2 GCU's Financial Application
3 filed this 29th day of January, 2009
4 with:

5 DOCKET CONTROL
6 Arizona Corporation Commission
7 1200 West Washington Street
8 Phoenix, Arizona 85007
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GRAHAM COUNTY ELECTRIC COOPERATIVE, INC.
GRAHAM COUNTY UTILITIES, INC.
P.O. Drawer B
Pima, Arizona 85543

*Serving The Beautiful Gila Valley
In Southeastern Arizona*

Telephone (928) 485-2451
FAX (928) 485-9491

Arizona Corporation Commission
ATTN: Docket Control Center
1200 West Washington St., Room 130
Phoenix, AZ 85507

January 12, 2009

RE: Application for Financing for Graham County Utilities, Inc. – Gas Division for prior construction.

Graham County Utilities, Inc. – Gas Division requests permission to incur additional long-term debt of \$800,000.00 for prior new construction.

The amount of the loan will be \$800,000.00. The loan will be obtained from National Rural Utilities Cooperative Finance Corporation (CFC) for a period of 30 years at the interest rate prevailing at the time the funds are borrowed. Based on today's interest rates, the quarterly payments will be approximately \$14,414 with level quarterly payments.

The following attachments are included for your review:

- (1) A copy of the commitment letter from CFC.
- (2) September 2008 audited financial statements.
- (3) A schedule on increases by plant account for the years 2000, 2001, 2002, 2003, 2004, 2005, 2006, 2007 & 2008.
- (4) Public notice of proposed financing application to be published in local paper.
- (5) Board resolution requesting long-term financing from CFC.
- (6) Board resolution from Graham County Electric Cooperative, Inc. agreeing to guarantee the loan.

Graham County Utilities, Inc. – Gas Division has not borrowed any money since December 31, 1999 for new construction. The gas company has increased total plant in service by over \$1,314,500 since it last borrowed for new construction. In addition Graham County Utilities, Inc. – Gas Division is filing with this finance package a rate case that if approved would result in an approximate rate increase of 10% to be able to adequately service any new additional debt.

Sincerely,



Steve Lines
General Manager



**National Rural Utilities
Cooperative Finance Corporation**

2201 Cooperative Way
Herndon, Virginia 20171
703-709-6700 | www.nrucfc.coop

A Touchstone Energy® Cooperative 

January 12, 2009

Mr. Steve Lines
General Manager
Graham County Utilities, Inc.
P. O. Drawer B
Pima, AZ 85543-0290

Dear Mr. Lines:

The National Rural Utilities Cooperative Finance Corporation ("CFC") is pleased to offer Graham County Utilities, Inc. ("Graham County Utilities") this conditional commitment to finance up to \$1,050,000 in costs associated with improvements to Graham County's gas and water operations.

This commitment is contingent upon and subject to the following conditions:

- a guaranty from Graham County Electric Cooperative, Inc., in the amount of the total credit facility extended to Graham County Utilities, secured by a first mortgage lien on all of Graham County Utilities' assets and revenues;
- receipt of all permits, consents, waivers and approvals required by any federal, state or local governmental boards, commissions, authorities or other regulatory bodies in connection with this transaction, including but not limited to those required by the Arizona Corporation Commission;
- completion of all filings and notices required by applicable law;
- due diligence review by CFC, of all contracts material to the transaction, including any management agreements, participation agreements and partnership agreements;
- execution and delivery of promissory notes, loan agreements, security agreements, assignments, mortgages, pledge agreements and such other documents as required by CFC, in form and substance satisfactory to CFC and its counsel;
- further negotiation and completion of mutually agreeable financing terms (including additional collateral security) and documentation which will include terms, provisions, representations, warranties, covenants, conditions precedent, defaults, indemnities and remedies that are typical to this type of financing, although not expressly described in this letter.

This conditional commitment is delivered to you with the understanding that you will not disclose its contents or the financing terms of the transaction to any party other than governmental or regulatory bodies which require such disclosure, or to those who are in a confidential relationship with you in connection with this transaction, such as your legal counsel, accountants, consultants, the Board of Directors and officers of Graham County Utilities, Inc. and Graham County Electric Cooperative, Inc., or as otherwise required by law.

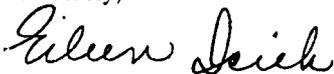
CFC LETTER
AZ700-A-9004 (ICIEKE)
130687-1

Mr. Steve Lines
Jan. 12, 2009
Page Two

If the terms of this conditional commitment are acceptable to you, please sign where indicated below and return the executed copy to CFC. This conditional commitment is not assignable and shall become effective upon your signature below and receipt by CFC.

We at CFC look forward to working with you toward a successful completion of this transaction.

Sincerely,



Eileen Iciek
Associate Vice President

Acknowledged and Agreed:

Graham County Utilities, Inc.

By: Steve Lines

Steve Lines

Date: 1-14-09

**GRAHAM COUNTY UTILITIES, INC. - GAS
NET ADDITIONS TO PLANT
FISCAL YEARS ENDED SEPTEMBER 30**

<u>GL</u>	<u>FYE 2000</u>	<u>FYE 2001</u>	<u>FYE 2002</u>	<u>FYE 2003</u>	<u>FYE 2004</u>	<u>FYE 2005</u>	<u>FYE 2006</u>	<u>FYE 2007</u>	<u>FYE 2008</u>	<u>TOTAL</u>
235000 Land & Land Rights			325							325
237600 Mains	37,268	22,513	87,182	80,261	48,189	44,694	64,067	62,074	109,129	555,377
238000 Services	38,992	22,150	23,844	30,375	18,609	22,096	58,139	44,552	50,949	309,705
238100 Meters & Regulators	42,711	39,629	26,549	(17,669)	28,031	39,785	24,996	70,385	81,024	335,441
239200 Transportation Equipment										
239400 Tools & Shop Equipment				(4,563)						
239600 Power Operated Equipment	5,485	7,912	4,860	3,349	1,531	10,107	21,120			(4,563)
	<u>118,971</u>	<u>84,292</u>	<u>143,384</u>	<u>102,315</u>	<u>99,689</u>	<u>109,923</u>	<u>148,733</u>	<u>187,118</u>	<u>320,109</u>	<u>1,314,535</u>

LOAN AMOUNT REQUESTED \$800,000

Includes net additions from 1/1/2000 through 9/30/2008.
Last CFC borrowing for plant was through 12/31/1999.

RECONCILIATION:

	<u>FYE 9/30/1999</u>	<u>FYE 9/30/2000</u>	<u>FYE 9/30/2001</u>	<u>FYE 9/30/2002</u>	<u>FYE 9/30/2003</u>	<u>FYE 9/30/2004</u>	<u>FYE 9/30/2005</u>	<u>FYE 9/30/2006</u>	<u>FYE 9/30/2007</u>	<u>FYE 9/30/2008</u>
PER AUDIT INCREASE	2,243,720	2,402,353	2,486,645	2,630,029	2,732,344	2,832,033	2,941,956	3,090,689	3,277,807	3,597,916
DIFFERENCE	158,633	84,292	143,384	102,315	99,689	109,923	148,733	187,118	320,109	(0)
	(39,662)	0	0	0	(0)	0	(0)	(0)	(0)	0

PUBLIC NOTICE
OF
AN APPLICATION FOR AN ORDER

AUTHORIZING THE BORROWING OF \$800,000
BY GRAHAM COUNTY UTILITIES, INC. – GAS DIVISION

Graham County Utilities, Inc. – Gas Division (“Company”) filed an Application with the Arizona Corporation Commission (“Commission”) for an order authorizing Applicant to borrow \$800,000 for thirty (30) years to finance construction. The application is available for inspection during regular business hours at the office of the Commission in Phoenix, Arizona, and the Company’s offices located at 9 West Center Street, Pima, Arizona.

Intervention in the Commission’s proceedings on the application shall be permitted to any person entitled by law to intervene and having a direct substantial interest in this matter. Persons desiring to intervene must file a Motion to Intervene with the Commission which must be served upon applicant and which, at a minimum, shall contain the following information:

1. The name, address and telephone number of the proposed intervenor and of any person upon whom service of documents is to be made if different than the intervenor.
2. A short statement of the proposed intervenor’s interest in the proceeding.
3. Whether the proposed intervenor desires a formal evidentiary hearing on the application and the reasons for such a hearing.
4. A statement certifying that a copy of the Motion to Intervene has been mailed to Applicant.

The granting of Motions to Intervene shall be governed by A.A.C. R14-3-105, except that all Motions to Intervene must be filled on, or before, the 15th day after this notice.

GRAHAM COUNTY UTILITIES, INC.
BOARD RESOLUTION REQUESTING LONG TERM FINANCING

WHEREAS, the Board of Directors of Graham County Utilities, Inc., has determined that it will seek financing for reimbursement of prior new gas construction.

Total Financing Requested: \$800,000.00

NOW, THEREFORE BE IT RESOLVED, that Graham County Utilities, Inc., (Gas Division) make application to NRUCFC or another similar lending institution for a commitment in the amount of \$800,000.00 to be used for reimbursement of prior new gas construction.

BE IT ALSO RESOLVED, that the financing shall provide for the repayment of the Loan; in quarterly installments, including interest and principal payments. The term of the loan will be 30 years and the interest rate will be determined at the time the funds are drawn.

BE IT FURTHER RESOLVED, that the management be authorized to file with the Arizona Corporation Commission an application requesting financing.

IN WITNESS WHEREOF, I have hereunto set my hand and affixed the seal of Graham County Utilities, Inc., this 7th day of January, 2009.



Jerald L. Kempton, Secretary

CORPORATE SEAL

**GRAHAM COUNTY ELECTRIC COOPERATIVE, INC.
BOARD RESOLUTION GUARANTEEING GRAHAM COUNTY UTILITIES,
INC. REQUEST FOR LONG TERM FINANCING**

WHEREAS, the Board of Directors of Graham County Electric Cooperative, Inc., agrees to guarantee a new loan request from Graham County Utilities, Inc. (Gas Division), to borrow from NRUCFC for prior new gas construction.

Total Financing Requested: \$800,000.00

NOW, THEREFORE BE IT RESOLVED, that this guarantee is based upon approval from the Arizona Corporation Commission.

IN WITNESS WHEREOF, I have hereunto set my hand and affixed the seal of Graham County Electric Cooperative, Inc., this 7th day of January, 2009.



M. Max Peck, Secretary

CORPORATE SEAL

GRAHAM COUNTY UTILITIES, INC.

PIMA, ARIZONA

FINANCIAL STATEMENTS WITH ACCOMPANYING INFORMATION

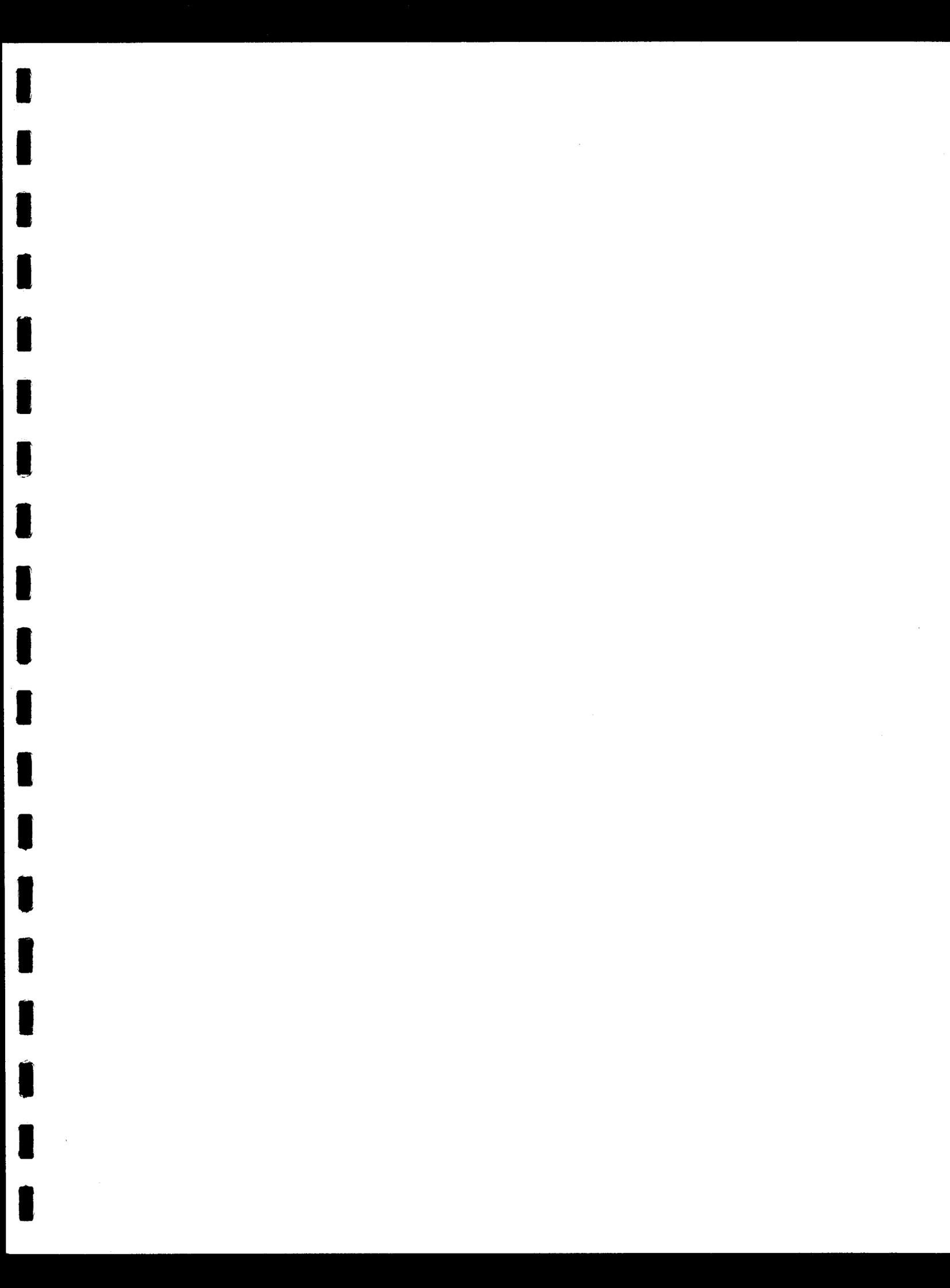
FOR THE YEARS ENDED SEPTEMBER 30, 2008 AND 2007

AND

REPORT OF CERTIFIED PUBLIC ACCOUNTANTS

BOLINGER, SEGARS, GILBERT & MOSS, L.L.P.

**CERTIFIED PUBLIC ACCOUNTANTS
LUBBOCK, TEXAS**



GRAHAM COUNTY UTILITIES, INC.

PIMA, ARIZONA

FINANCIAL STATEMENTS WITH ACCOMPANYING INFORMATION

FOR THE YEARS ENDED SEPTEMBER 30, 2008 AND 2007

AND

REPORT OF CERTIFIED PUBLIC ACCOUNTANTS

**GRAHAM COUNTY UTILITIES, INC.
PIMA, ARIZONA**

**FINANCIAL STATEMENTS WITH ACCOMPANYING INFORMATION
FOR THE YEARS ENDED SEPTEMBER 30, 2008 AND 2007**

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BOLINGER, SEGARS, GILBERT & MOSS, L.L.P.

CERTIFIED PUBLIC ACCOUNTANTS

PHONE: (806) 747-3806

FAX: (806) 747-3815

8215 NASHVILLE AVENUE

LUBBOCK, TEXAS 79423-1954

INDEPENDENT AUDITORS' REPORT

Board of Directors
Graham County Utilities, Inc.
Pima, Arizona

We have audited the accompanying balance sheets of Graham County Utilities, Inc., as of September 30, 2008 and 2007, and the related statements of income and accumulated margins, and cash flows for the years then ended. These financial statements are the responsibility of the Cooperative's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audits 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. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Graham County Utilities, Inc. as of September 30, 2008 and 2007, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued a report dated November 3, 2008, on our consideration of Graham County Utilities, Inc.'s internal control over financial reporting and on its compliance with certain provision 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 audits.

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

Bolinger, Segars, Gilbert & Moss LLP

Certified Public Accountants

November 3, 2008

-2-
GRAHAM COUNTY UTILITIES, INC.

Exhibit A

**BALANCE SHEET
FOR THE YEARS ENDED SEPTEMBER 30, 2008 AND 2007**

ASSETS

	September 30,	
	2008	2007
UTILITY PLANT		
Plant in Service	\$ 5,814,817	\$ 5,405,462
Construction Work in Progress	1,287,278	779,909
Plant Acquisition Adjustment	1,025,652	1,025,652
	\$ 8,127,747	\$ 7,211,023
Less: Accumulated Provision for Depreciation and Amortization	3,848,763	3,602,152
	\$ 4,278,984	\$ 3,608,871
 OTHER PROPERTY AND INVESTMENTS		
Investments in Associated Organizations	\$ 243,099	\$ 253,219
 CURRENT ASSETS		
Cash - General	\$ 44,517	\$ 51,571
Accounts Receivable (Less allowance for uncollectibles of \$80,217 in 2008 and \$59,203 in 2007)	71,765	102,206
Accounts Receivable - GCEC		26,193
Underbilled Consumers Fuel Cost	32,417	
Materials and Supplies	142,225	139,621
Other Current and Accrued Assets	32,475	51,933
Total Current Assets	\$ 323,399	\$ 371,524
 DEFERRED CHARGES	\$ 35,878	\$ 44,219
	\$ 4,881,360	\$ 4,277,833
EQUITIES AND LIABILITIES		
 MEMBERS' EQUITY		
Memberships	\$ 30,629	\$ 30,680
Accumulated Margins	355,541	488,992
	\$ 386,170	\$ 519,672
 LONG - TERM DEBT		
CFC Mortgage Notes Less Current Maturities	\$ 1,536,299	\$ 1,693,208
AEPCO Note Payable Less Current Maturities	25,667	45,834
Graham County Electric Cooperative Note Payable Less Current Maturities	14,607	56,335
USDA Rural Development Note Payable Less Current Maturities	1,557,427	1,372,878
	\$ 3,134,000	\$ 3,168,255
 CURRENT LIABILITIES		
Current Maturities of Long-Term Debt	\$ 238,628	\$ 217,761
Accounts Payable - Other	158,717	107,392
Accounts Payable - Graham County Electric Coop	817,693	
Overbilled Consumers Fuel Cost		113,137
Customers' Deposits and Prepayments	75,810	79,065
Accrued Taxes	55,232	57,135
Accrued Interest	15,110	15,416
Total Current Liabilities	\$ 1,361,190	\$ 589,906
	\$ 4,881,360	\$ 4,277,833

See accompanying notes to financial statements.

GRAHAM COUNTY UTILITIES, INC.

Exhibit B

STATEMENT OF INCOME AND ACCUMULATED MARGINS
FOR THE YEARS ENDED SEPTEMBER 30, 2008 AND 2007

	September 30,	
	2008	2007
OPERATING REVENUES	\$ 4,373,004	\$ 4,241,224
OPERATING EXPENSES		
Purchased Gas	\$ 2,398,790	\$ 2,293,478
Power for Pumping	32,595	40,810
Operations	345,717	339,378
Maintenance	441,186	352,392
Consumer Accounts	334,466	290,383
Administrative and General	495,840	353,604
Depreciation and Amortization	246,611	223,187
Other Interest	35,768	27,458
Total Operating Expenses	\$ 4,330,973	\$ 3,920,690
OPERATING MARGINS - BEFORE FIXED CHARGES	\$ 42,031	\$ 320,534
Interest on Long-Term Debt	195,057	166,362
OPERATING MARGINS (LOSS) - AFTER FIXED CHARGES	\$ (153,026)	\$ 154,172
Capital Credits	14,142	15,724
NET OPERATING MARGINS (LOSS)	\$ (138,884)	\$ 169,896
NONOPERATING MARGINS		
Interest	5,433	7,295
NET MARGINS (LOSS)	\$ (133,451)	\$ 177,191
ACCUMULATED MARGINS - BEGINNING OF YEAR	488,992	311,801
ACCUMULATED MARGINS - END OF YEAR	\$ 355,541	\$ 488,992

See accompanying notes to financial statements.

GRAHAM COUNTY UTILITIES, INC.

Exhibit C

STATEMENT OF CASH FLOWS
FOR THE YEARS ENDED SEPTEMBER 30, 2008 AND 2007

	September 30,	
	2008	2007
CASH FLOWS FROM OPERATING ACTIVITIES		
Net Margins (Loss)	\$ (133,451)	\$ 177,191
Adjustments to Reconcile Net Margins to		
Net Cash Provided by (Used in) Operating Activities		
Depreciation and Amortization	246,611	223,187
Capital Credits - Noncash	(4,242)	(4,717)
Over/(Under)billed Fuel Cost	(145,554)	36,328
Deferred Charges	8,341	8,340
Accounts Receivable	30,441	(7,879)
Inventories and Other Current Assets	16,853	(12,411)
Payables and Accrued Expenses	45,862	(44,654)
Net Payments to (from) - Graham County Electric Cooperative	843,886	(101,954)
Net Cash Provided by Operating Activities	<u>\$ 908,747</u>	<u>\$ 273,431</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Additions to Plant	\$ (916,725)	\$ (818,808)
Investments in Associated Organizations	14,362	14,015
Net Cash Used in Investing Activities	<u>\$ (902,363)</u>	<u>\$ (804,793)</u>
CASH FLOWS FROM FINANCING ACTIVITIES		
Advances on Long-Term Debt from USDA	\$ 206,278	\$ 893,722
Payments on Note Payable to AEPCO	(20,166)	(22,000)
Payments on Long-Term Debt to CFC	(146,108)	(264,393)
Payments on Long-Term Debt to GCEC	(38,761)	(36,004)
Payments on Long-Term Debt to USDA	(14,630)	(8,684)
Memberships	(51)	735
Net Cash Provided by (Used in) Financing Activities	<u>\$ (13,438)</u>	<u>\$ 563,376</u>
INCREASE (DECREASE) IN CASH	<u>\$ (7,054)</u>	<u>\$ 32,014</u>
CASH - BEGINNING OF YEAR	<u>51,571</u>	<u>19,557</u>
CASH - END OF YEAR	<u>\$ 44,517</u>	<u>\$ 51,571</u>
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION		
Cash Paid During the Year for:		
Interest on Long-Term Debt	<u>\$ 200,791</u>	<u>\$ 166,362</u>
Federal Income Tax	<u>\$ 0</u>	<u>\$ 0</u>

See accompanying notes to financial statements.

GRAHAM COUNTY UTILITIES, INC.

NOTES TO FINANCIAL STATEMENTS

1. Nature of Operations and Summary of Significant Accounting Policies

Nature of Operations

Graham County Utilities, Inc. (the Cooperative) is organized as a cooperative to provide gas and water utility services to customers in Graham County, Arizona. The Cooperative was incorporated February 14, 1989, and began operations in November, 1989, with the purchase of assets and liabilities from two private utility companies. The Cooperative has been granted exemption from Federal income taxes under Internal Revenue Code Section 501(c)(12).

Basis of Accounting

The Cooperative accounts for assets, liabilities, income, and expenses separately for each utility service furnished. Separate accounting is maintained for the gas department and the water department.

Recognition is given to all services rendered and facilities provided by each department, as well as those services provided by Graham County Electric Cooperative, Inc. under the operating and management agreement executed by both Cooperatives. These services are billed at predetermined rates. The accrual basis of accounting is followed in all departments.

Operating Revenues

Gas and water revenues are under the jurisdiction of the Arizona Corporation Commission.

The Cooperative records revenues as billed to the customers on a monthly basis. Revenue is not accrued for utility services delivered but not billed at the end of each month. The unbilled and unrecorded revenue at September 30, 2008 and 2007, was estimated to be \$58,032 and \$68,146 in the gas department and \$36,270 and \$37,874 in the water department.

The Cooperative's tariffs include an adjustment for flow-through of purchased natural gas costs. In order to match fuel costs and related revenues, costs billed in advance are recorded as overbilled consumers fuel cost and costs to be billed in the subsequent period are recorded as underbilled consumers fuel cost. For the years ended September 30, 2008 and 2007, the Cooperative was underbilled \$32,417 and overbilled \$113,137, respectively.

Group Concentration of Credit Risk

The Cooperative's headquarters is located in Pima, Arizona. The service area includes members located in Graham County, Arizona, and also includes retail service to the towns of Pima and Ft. Thomas, and wholesale services to Eden Water Company. The Cooperative records a receivable for gas and water service as billed on a monthly basis. The Cooperative requires a deposit from customers upon connection which is applied to any unpaid bills upon default. The deposit accrues interest annually at the rate of six percent. Deposits on hand totaled \$75,810 and \$79,065 at September 30, 2008 and 2007, respectively.

Patronage Capital Certificates

Patronage capital from associated organizations is recorded at the stated amount of the certificate.

GRAHAM COUNTY UTILITIES, INC.

NOTES TO FINANCIAL STATEMENTS

Inventories

Inventories which consist of construction materials and supplies are valued at average unit cost.

Federal Income Tax Status

The Cooperative qualifies for tax exempt status under Internal Revenue Code section 501(c)(12) with more than 85% of income consisting of amounts received from members.

Allowance for Uncollectible Accounts

The Cooperative uses the aging method to allow for uncollectible accounts receivable. During the year, management makes an evaluation of past due accounts to determine collection ability. The accounts deemed uncollectible are written off upon approval by the Board of Directors.

Use of Estimates in the Preparation of Financial Statements

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect 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.

2. Assets Pledged

All assets are pledged as security for the long-term debt due the National Rural Utilities Cooperative Finance Corporation (CFC) and USDA.

3. Utility Plant and Depreciation

Utility plant is stated at the original cost of construction including the construction costs incurred by the utility from which the Cooperative acquired plant in November 1989. Original cost includes the cost of contracted services, direct labor, materials, and overhead reduced by contributions in aid to construction received in connection with new construction.

Maintenance and repairs including the renewal of minor items of plant not comprising a retirement unit are charged to the appropriate maintenance accounts.

GRAHAM COUNTY UTILITIES, INC.

NOTES TO FINANCIAL STATEMENTS

Major classes of utility plant are summarized as follows:

	September 30, 2008			September 30,
	Gas	Water	Total	2007
	Department	Department		Total
Utility Plant in Service				
Intangible	\$ 42,522	\$ 37,708	\$ 80,230	\$ 80,230
Production		555,938	555,938	554,337
Transmission		983,468	983,468	983,468
Distribution	3,359,500	505,829	3,865,329	3,427,206
General	194,478	111,451	305,929	336,298
Land and Land Rights	1,416	22,507	23,923	23,923
Total Plant in Service	\$ 3,597,916	\$ 2,216,901	\$ 5,814,817	\$ 5,405,462
Construction Work in Progress	101,760	1,185,518	1,287,278	779,909
Utility Plant Acquisition Adjustment	415,484	610,168	1,025,652	1,025,652
Total Utility Plant	\$ 4,115,160	\$ 4,012,587	\$ 8,127,747	\$ 7,211,023

Provision has been made for depreciation on straight-line composite rates as follows:

	Gas Department	Water Department
Production		4%
Transmission		4%
Distribution		4%
Gas Mains	2.80%	
Services	4.10%	
Meters - Regulators	2.60%	
Structures	2.30%	
General	6.7% - 13.3%	10% - 20%

Depreciation accruals charged to expense for the periods ended September 30, 2008 and 2007, totaled \$246,611 and \$223,187, respectively.

A plant acquisition adjustment was created when Graham County Utilities, Inc. purchased the assets and liabilities of City Utilities, Inc. and General Utilities, Inc. The acquisition adjustment, representing the amount of the purchase price over the book value of the net assets acquired, amounted to \$415,484 in the gas department and \$610,168 in the water department. Plant acquisition adjustments are amortizable over the estimated useful life of the plant acquired. The Cooperative has elected to amortize these costs over a 25-year period. The annual charge to expense is \$16,619 in the gas department and \$24,407 in the water department.

GRAHAM COUNTY UTILITIES, INC.

NOTES TO FINANCIAL STATEMENTS

The plant acquisition costs and related provision for amortization at September 30, 2008, are summarized as follows:

	<u>Gas Department</u>	<u>Water Department</u>
Acquisition Adjustment	\$ <u>415,484</u>	\$ <u>610,168</u>
Less: Amortization		
Prior Periods	\$ 299,149	\$ 439,320
Current Year	<u>16,619</u>	<u>24,407</u>
	\$ <u>315,768</u>	\$ <u>463,727</u>
 Unamortized Adjustment	 <u>\$ 99,716</u>	 <u>\$ 146,441</u>

4. Investments in Associated Organizations

Investments in associated organizations consisted of the following:

	<u>September 30,</u>	
	<u>2008</u>	<u>2007</u>
CFC		
Capital Term Certificates	\$ 152,510	\$ 160,547
Patronage Capital	83,463	85,545
Memberships	<u>1,000</u>	<u>1,000</u>
	\$ 236,973	\$ 247,092
 Graham County Electric Coöperative, Inc.		
Patronage Capital	<u>\$ 6,126</u>	<u>\$ 6,127</u>
	<u>\$ 243,099</u>	<u>\$ 253,219</u>

GRAHAM COUNTY UTILITIES, INC.

NOTES TO FINANCIAL STATEMENTS

5. Deferred Charges

Deferred charges consisted of the following:

	September 30,	
	<u>2008</u>	<u>2007</u>
Gas Department		
Rate Filing Costs	\$	\$ 1,043
Unamortized Debt Expense	19,015	22,883
	<u>\$ 19,015</u>	<u>\$ 23,926</u>
Water Department		
Unamortized Debt Expense	\$ 16,863	\$ 20,293
	<u>\$ 35,878</u>	<u>\$ 44,219</u>

During 1998, the Cooperative converted a CFC note to a lower interest rate of 7.1% for 15 years with a conversion fee of \$109,457. Amortization expense for the years ended September 30, 2008 and 2007, is \$7,297.

6. Memberships

Memberships are comprised of the following:

	September 30,	
	<u>2008</u>	<u>2007</u>
Class A Memberships		
Graham County Electric Cooperative, Inc., entitled to one vote	\$ 5,000	\$ 5,000
Class B Memberships		
All qualified members of Graham County Electric Cooperative, Inc., \$5 membership fee, entitled to one vote per membership	20,964	21,015
Class C Memberships		
All others who receive service, \$5 membership fee, entitled to one vote per membership	<u>4,665</u>	<u>4,665</u>
	<u>\$ 30,629</u>	<u>\$ 30,680</u>

GRAHAM COUNTY UTILITIES, INC.

NOTES TO FINANCIAL STATEMENTS

7. Accumulated Margins (Deficits)

This balance consists of net margins or (losses) as follows:

Calendar Year	Gas Department	Water Department	Total
1989	\$ 23,321	\$ (694)	\$ 22,627
1990	(30,746)	2,845	(27,901)
1991	(91,410)	(23,047)	(114,457)
1992	(41,115)	(13,851)	(54,966)
1993	(64,937)	5,078	(59,859)
1994	(46,268)	26,494	(19,774)
1995	(172,043)	(28,602)	(200,645)
1996	(68,293)	(3,410)	(71,703)
1997	(65,806)	(23,095)	(88,901)
1998	225,309	31,474	256,783
1999	97,405	62,256	159,661
2000	1,467	46,927	48,394
2001	39,062	40,741	79,803
2002	61,124	1,125	62,249
2003	(5,764)	69,524	63,760
2004	62,759	7,767	70,526
2005	92,446	47,242	139,688
2006	141,801	42,157	183,958
2007	69,003	36,636	105,639
2008 Nine Months	(101,532)	(15,774)	(117,306)
	<u>\$ 125,783</u>	<u>\$ 311,793</u>	<u>\$ 437,576</u>
Patronage Capital Retired		<u>(82,035)</u>	<u>(82,035)</u>
	<u>\$ 125,783</u>	<u>\$ 229,758</u>	<u>\$ 355,541</u>

The Board of Directors has adopted the policy of separating each department's net gains or losses for allocation purposes. Patronage capital is allocated after all deficits have been recovered. During the year ended September 30, 2008 and 2007, no retirements of patronage capital were made.

Under the mortgage agreement with CFC, until the equities or margins equal or exceed 30% of the total assets of the Cooperative, the return to patrons of capital contributed by them is limited.

GRAHAM COUNTY UTILITIES, INC.

NOTES TO FINANCIAL STATEMENTS

8. Mortgage Notes – CFC

Following is a summary of long-term debt due CFC maturing September 30, 2014, June 30, 2026, and September 30, 2031:

	September 30,	
	<u>2008</u>	<u>2007</u>
Fixed - 7.10%	\$ 743,396	\$ 839,549
Variable (4.90% in 2008, 7.05% in 2007)	256,966	288,114
Fixed - 7.45%	323,387	335,228
Fixed - 6.25%	366,550	373,517
	<u>\$ 1,690,299</u>	<u>\$ 1,836,408</u>
Less: Current Maturities	<u>154,000</u>	<u>143,200</u>
	<u>\$ 1,536,299</u>	<u>\$ 1,693,208</u>

Principal and interest installments on the above notes are due quarterly in amounts of approximately \$64,900. As of September 30, 2008, annual maturities of long-term debt due CFC for the next five years is as follows:

2009	154,000
2010	164,400
2011	175,600
2012	187,500
2013	200,300

The mortgages contain requirements requiring certain financial ratios to be maintained or exceeded. These requirements were met during the year ended September 30, 2008 and 2007.

9. USDA Rural Development Note Payable

Following is a summary of long-term debt due USDA Rural Development:

	September 30,	
	<u>2008</u>	<u>2007</u>
5.000% Note Maturing March, 2032	\$ 144,052	\$ 147,205
4.500% Note Maturing August, 2035	252,271	257,006
4.500% Note Maturing July, 2040	87,529	88,746
4.125% Note Maturing March, 2047	1,094,475	893,721
	<u>\$ 1,578,327</u>	<u>\$ 1,386,678</u>
Less: Current Maturities	<u>20,900</u>	<u>13,800</u>
	<u>\$ 1,557,427</u>	<u>\$ 1,372,878</u>

GRAHAM COUNTY UTILITIES, INC.

NOTES TO FINANCIAL STATEMENTS

Principal and interest installments on the above notes are due monthly in amounts of \$7,393. As of September 30, 2008, annual maturities of long-term debt due USDA Rural Development for the next five years are as follows:

2009	20,900
2010	21,900
2011	22,900
2012	23,900
2013	24,900

10. Graham County Electric Note Payable

During 1998, the Cooperative financed an accounts payable due to Graham County Electric Cooperative. The total cost of \$500,000 is to be paid over 10 years in monthly payments including interest at the rate of 7.4%. The balance outstanding at September 30, 2008, is \$56,335. Annual maturities due to Graham County Electric Cooperative for the next two years are as follows:

2009	41,728
2010	14,607

11. AEPCO Note Payable

During 1999, the Cooperative obtained a zero interest loan from the Arizona Electric Power Cooperative, Inc. through the Rural Economic Development Program of RUS. The total loan was \$220,000, payable in monthly payments of \$1,833 for 120 months. The balance at September 30, 2008, is \$47,667. Annual maturities due to AEPCO for the next three years are as follows:

2009	22,000
2010	22,000
2011	3,667

12. Related Parties

Graham County Utilities, Inc. (GCU) is related by having substantially identical Boards of Directors and management with Graham County Electric Cooperative, Inc. (GCEC). GCEC provides administrative and general, management, operations, consumer accounting, and construction services to GCU under an operating and management agreement signed by both parties on June 20, 1989.

GCEC is also the guarantor of the mortgage loan executed by GCU to CFC.

GRAHAM COUNTY UTILITIES, INC.

NOTES TO FINANCIAL STATEMENTS

Intercompany balances between the two Cooperatives are summarized as follows:

	September 30,	
	<u>2008</u>	<u>2007</u>
Graham County Utilities, Inc.		
Accounts Payable	\$ (820,100)	\$
Accounts Receivable		26,193
Note Payable	<u>(56,335)</u>	<u>(95,096)</u>
Net Due to Affiliated Cooperative	<u>\$ (876,435)</u>	<u>\$ (68,903)</u>
Graham County Electric Cooperative, Inc.		
Accounts Receivable	\$ 820,100	\$
Accounts Payable		(26,193)
Note Receivable	<u>56,335</u>	<u>95,096</u>
Net Due from Affiliated Cooperative	<u>\$ 876,435</u>	<u>\$ 68,903</u>

13. Litigation

The Cooperative is not involved in any litigation that would materially affect the financial statements.

ACCOMPANYING INFORMATION

BOLINGER, SEGARS, GILBERT & MOSS, L.L.P.

CERTIFIED PUBLIC ACCOUNTANTS

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**INDEPENDENT AUDITORS' REPORT ON
ACCOMPANYING INFORMATION**

Our audits of the basic financial statements presented in the preceding section of this report were made for the purpose of forming an opinion on such financial statements taken as a whole. The accompanying information shown on pages 15 through 20 is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audits of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

Bolinger, Segars, Gilbert & Moss LLP

Certified Public Accountants

November 3, 2008

GRAHAM COUNTY UTILITIES, INC.
GAS DEPARTMENT

Schedule 1

BALANCE SHEET
SEPTEMBER 30, 2008 AND 2007

ASSETS

	September 30,	
	<u>2008</u>	<u>2007</u>
UTILITY PLANT		
Plant in Service	\$ 3,597,916	\$ 3,277,807
Construction Work in Progress	101,760	17,984
Plant Acquisition Adjustment	415,484	415,484
	<u>\$ 4,115,160</u>	<u>\$ 3,711,275</u>
Less: Accumulated Provision for Depreciation and Amortization	2,070,451	1,940,945
	<u>\$ 2,044,709</u>	<u>\$ 1,770,330</u>
OTHER PROPERTY AND INVESTMENTS AT COST OR STATED VALUE		
Investments in Associated Organizations	\$ 135,593	\$ 139,355
CURRENT ASSETS		
Cash	\$	\$ 10,330
Accounts Receivable (Less allowance for uncollectibles of \$65,606 in 2008 and \$47,607 in 2007)	57,220	80,176
Underbilled Consumers Fuel Cost	32,417	
Materials and Supplies	91,067	84,695
Other Current and Accrued Assets	20,562	35,952
Total Current Assets	<u>\$ 201,266</u>	<u>\$ 211,153</u>
Deferred Charges	\$ 19,015	\$ 23,926
	<u>\$ 2,400,583</u>	<u>\$ 2,144,764</u>

EQUITIES AND LIABILITIES

MEMBERS' EQUITY		
Memberships	\$ 28,129	\$ 28,180
Accumulated Deficits	125,783	234,158
	<u>\$ 153,912</u>	<u>\$ 262,338</u>
LONG -TERM DEBT		
Note Payable - Graham County Electric Cooperative	\$ 14,607	\$ 56,335
CFC Mortgage Notes Less Current Maturities	1,113,729	1,221,807
	<u>\$ 1,128,336</u>	<u>\$ 1,278,142</u>
CURRENT LIABILITIES		
Current Maturities of Long-Term Debt	\$ 148,128	\$ 123,361
Accounts Payable - Other	103,777	70,330
Accounts Payable - Graham County Electric Cooperative	750,751	16,156
Accounts Payable - Water Department		160,862
Overbilled Consumers Fuel Cost		113,137
Accrued Taxes	35,549	37,568
Customers' Deposits and Prepayments	67,270	69,875
Accrued Interest	12,860	12,995
Total Current Liabilities	<u>\$ 1,118,335</u>	<u>\$ 604,284</u>
	<u>\$ 2,400,583</u>	<u>\$ 2,144,764</u>

GRAHAM COUNTY UTILITIES, INC.
GAS DEPARTMENT

Schedule 2

STATEMENT OF INCOME AND ACCUMULATED MARGINS
FOR THE YEARS ENDED SEPTEMBER 30, 2008 AND 2007

	September 30,		Increase (Decrease)
	2008	2007	
OPERATING REVENUES			
Residential	\$ 2,658,038	\$ 2,717,738	\$ (59,700)
Irrigation	5,263	8,601	(3,338)
Commercial and Industrial	936,481	944,533	(8,052)
Fuel Cost Under (Over) Billed	144,749	(37,223)	181,972
Other Operating Revenues	21,520	22,280	(760)
Total Operating Revenues	<u>\$ 3,766,051</u>	<u>\$ 3,655,929</u>	<u>\$ 110,122</u>
OPERATING EXPENSES			
Purchased Gas	\$ 2,398,790	\$ 2,293,478	\$ 105,312
Operations	285,961	266,967	18,994
Maintenance	285,370	237,776	47,594
Customer Accounts	276,124	239,796	36,328
Administrative and General	394,362	264,696	129,666
Depreciation and Amortization	129,506	117,205	12,301
Other Interest	29,948	16,670	13,278
Total Operating Expenses	<u>\$ 3,800,061</u>	<u>\$ 3,436,588</u>	<u>\$ 363,473</u>
OPERATING MARGINS (LOSS) - Before Fixed Charges	\$ (34,010)	\$ 219,341	\$ (253,351)
FIXED CHARGES			
Interest on Long-Term Debt	<u>86,266</u>	<u>98,668</u>	<u>(12,402)</u>
OPERATING MARGINS (LOSS) - After Fixed Charges	\$ (120,276)	\$ 120,673	\$ (240,949)
Capital Credits	<u>10,168</u>	<u>9,372</u>	<u>796</u>
NET OPERATING MARGINS (LOSS)	\$ (110,108)	\$ 130,045	\$ (240,153)
NONOPERATING MARGINS			
Interest	<u>1,733</u>	<u>3,579</u>	<u>(1,846)</u>
NET MARGINS (LOSS)	\$ (108,375)	\$ 133,624	<u>\$ (241,999)</u>
ACCUMULATED MARGINS - BEGINNING OF YEAR	<u>234,158</u>	<u>100,534</u>	
ACCUMULATED MARGINS - END OF YEAR	<u>\$ 125,783</u>	<u>\$ 234,158</u>	

GRAHAM COUNTY UTILITIES, INC.
GAS DEPARTMENT

Schedule 3

STATEMENT OF CASH FLOWS
FOR THE YEARS ENDED SEPTEMBER 30, 2008 AND 2007

	September 30,	
	<u>2008</u>	<u>2007</u>
CASH FLOWS FROM OPERATING ACTIVITIES		
Net Margins (Loss)	\$ (108,375)	\$ 133,624
Adjustments to Reconcile Net Margins to Net Cash		
Provided by (Used in) Operating Activities		
Depreciation and Amortization	129,506	117,205
Capital Credits - Noncash	(3,050)	(2,812)
Deferred Charges	4,911	4,911
Over/(Under)billed Fuel Cost - Net	(145,554)	36,328
Accounts Receivable	22,956	(1,194)
Inventories and Other Current Assets	9,018	(23,911)
Payables and Accrued Expenses	28,688	(31,566)
Net Payments to - Water Department	(160,862)	132,812
Net Payments to - Graham County Electric Cooperative	734,595	(61,799)
Net Cash Provided by Operating Activities	<u>\$ 511,833</u>	<u>\$ 303,598</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Additions to Gas Utility Plant	\$ (403,886)	\$ (184,075)
Investments in Associated Organizations	6,812	7,150
Net Cash Used in Investing Activities	<u>\$ (397,074)</u>	<u>\$ (176,925)</u>
CASH FLOWS FROM FINANCING ACTIVITIES		
Payments on Long-Term Debt - CFC	\$ (86,277)	\$ (81,074)
Payments on Long-Term Debt - Graham County Electric Cooperative	(38,761)	(36,004)
Memberships	(51)	735
Net Cash Used in Financing Activities	<u>\$ (125,089)</u>	<u>\$ (116,343)</u>
INCREASE (DECREASE) IN CASH	<u>\$ (10,330)</u>	<u>\$ 10,330</u>
CASH - BEGINNING OF YEAR	<u>10,330</u>	<u>0</u>
CASH - END OF YEAR	<u><u>\$ 0</u></u>	<u><u>\$ 10,330</u></u>
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION		
Paid During the Year for:		
Interest on Long-Term Debt	<u>\$ 92,006</u>	<u>\$ 98,668</u>
Federal Income Tax	<u>\$ 0</u>	<u>\$ 0</u>

GRAHAM COUNTY UTILITIES, INC.
WATER DEPARTMENT

Schedule 4

BALANCE SHEET
SEPTEMBER 30, 2008 AND 2007

ASSETS

	September 30,	
	<u>2008</u>	<u>2007</u>
UTILITY PLANT AT COST		
Water Plant in Service	\$ 2,216,901	\$ 2,127,655
Construction Work in Progress	1,185,518	761,925
Plant Acquisition Adjustment	610,168	610,168
	<u>\$ 4,012,587</u>	<u>\$ 3,499,748</u>
Less: Accumulated Provision for Depreciation and Amortization	1,778,312	1,661,207
	<u>\$ 2,234,275</u>	<u>\$ 1,838,541</u>
OTHER PROPERTY AND INVESTMENTS AT COST OR STATED VALUE		
Investments in Associated Organizations	\$ 107,506	\$ 113,864
CURRENT ASSETS		
Cash - General	\$ 44,517	\$ 41,241
Accounts Receivable - Customers (Less allowance for uncollectibles of \$14,611 in 2008 and \$11,596 in 2007)	14,545	22,030
Accounts Receivable - Graham County Electric Cooperative		42,349
Accounts Receivable - Gas Department		160,862
Materials and Supplies	51,158	54,926
Other Current and Accrued Assets	11,914	15,981
Total Current Assets	<u>\$ 122,134</u>	<u>\$ 337,389</u>
DEFERRED CHARGES	\$ 16,863	\$ 20,293
	<u>\$ 2,480,778</u>	<u>\$ 2,310,087</u>

EQUITIES AND LIABILITIES

EQUITY		
Memberships	\$ 2,500	\$ 2,500
Accumulated Margins	229,758	254,834
	<u>\$ 232,258</u>	<u>\$ 257,334</u>
LONG-TERM DEBT		
CFC Mortgage Notes Less Current Maturities	\$ 422,570	\$ 471,401
AEPCO Notes Payable Less Current Maturities	25,667	45,834
USDA Rural Development Notes Less Current Maturities	1,557,427	1,372,878
	<u>\$ 2,005,664</u>	<u>\$ 1,890,113</u>
CURRENT LIABILITIES		
Current Maturities of Long-Term Debt	\$ 90,500	\$ 94,400
Accounts Payable - Other	54,940	37,062
Accounts Payable - Graham County Electric Cooperative	66,942	
Accrued Taxes	19,684	19,567
Customers' Deposits and Prepayments	8,540	9,190
Accrued Interest	2,250	2,421
Total Current Liabilities	<u>\$ 242,856</u>	<u>\$ 162,640</u>
	<u>\$ 2,480,778</u>	<u>\$ 2,310,087</u>

**GRAHAM COUNTY UTILITIES, INC.
WATER DEPARTMENT**

Schedule 5

**STATEMENT OF INCOME AND ACCUMULATED MARGINS
FOR THE YEARS ENDED SEPTEMBER 30, 2008 AND 2007**

	September 30,		Increase (Decrease)
	2008	2007	
OPERATING REVENUES			
Residential	\$ 520,702	\$ 495,134	\$ 25,568
Commercial and Industrial	48,371	50,055	(1,684)
Sales for Resale	33,910	37,395	(3,485)
Other Operating Revenues	3,970	2,710	1,260
Total Operating Revenues	\$ 606,953	\$ 585,294	\$ 21,659
OPERATING EXPENSES			
Purchased Power - Pumping	\$ 32,595	\$ 40,810	\$ (8,215)
Operations	59,756	72,411	(12,655)
Maintenance	155,816	114,616	41,200
Customer Accounts	58,342	50,587	7,755
Administrative and General	101,478	88,907	12,571
Depreciation and Amortization	117,105	105,982	11,123
Other Interest	5,820	11,679	(5,859)
Total Operating Expenses	\$ 530,912	\$ 484,992	\$ 45,920
OPERATING MARGINS - Before Fixed Charges	\$ 76,041	\$ 100,302	\$ (24,261)
FIXED CHARGES			
Interest on Long-Term Debt	108,791	67,694	41,097
OPERATING MARGINS (LOSS) - After Fixed Charge	\$ (32,750)	\$ 32,608	\$ (65,358)
Capital Credits	3,974	6,352	(2,378)
NET OPERATING MARGINS (LOSS)	\$ (28,776)	\$ 38,960	\$ (67,736)
NONOPERATING MARGINS			
Interest	3,700	4,607	(907)
NET MARGINS (LOSS)	\$ (25,076)	\$ 43,567	\$ (68,643)
ACCUMULATED MARGINS - BEGINNING OF YEAR	254,834	211,267	
ACCUMULATED MARGINS - END OF YEAR	\$ 229,758	\$ 254,834	

GRAHAM COUNTY UTILITIES, INC.
WATER DEPARTMENT

Schedule 6

STATEMENT OF CASH FLOWS
FOR THE YEARS ENDED SEPTEMBER 30, 2008 AND 2007

	September 30,	
	2008	2007
CASH FLOWS FROM OPERATING ACTIVITIES		
Net Margins (Loss)	\$ (25,076)	\$ 43,567
Adjustments to Reconcile Net Margins to Net Cash Provided by Operating Activities		
Depreciation and Amortization	117,105	105,982
Capital Credits - Noncash	(1,192)	(1,906)
Deferred Charges	3,430	3,429
Accounts Receivable	7,485	(6,685)
Inventories and Other Current Assets	7,835	11,500
Payables and Accrued Expenses	17,174	(13,089)
Net Advances from (to) - Gas Department	160,862	(132,812)
Net Payments from (to) - Graham County Electric Cooperative	109,291	(40,155)
Net Cash Provided by (Used in) Operating Activities	\$ 396,914	\$ (30,169)
CASH FLOWS FROM INVESTING ACTIVITIES		
Additions to Plant	\$ (512,839)	\$ (634,732)
Investments in Associated Organizations	7,550	6,866
Net Cash Used in Investing Activities	\$ (505,289)	\$ (627,866)
CASH FLOWS FROM FINANCING ACTIVITIES		
Advances on Long-Term Debt from USDA	\$ 206,278	\$ 893,722
Payments on Note Payable to AEPCO	(20,166)	(22,000)
Payments on Long-Term Debt to CFC	(59,831)	(183,319)
Payments on Long-Term Debt to USDA	(14,630)	(8,684)
Net Cash Provided by Financing Activities	\$ 111,651	\$ 679,719
INCREASE IN CASH	\$ 3,276	\$ 21,684
CASH - BEGINNING OF YEAR	41,241	19,557
CASH - END OF YEAR	\$ 44,517	\$ 41,241
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION		
Paid During the Year for:		
Interest on Long-Term Debt	\$ 108,785	\$ 67,694
Federal Income Tax	\$ 0	\$ 0

COMPLIANCE AND INTERNAL CONTROL SECTION

BOLINGER, SEGARS, GILBERT & MOSS, L.L.P.

CERTIFIED PUBLIC ACCOUNTANTS

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8215 NASHVILLE AVENUE

LUBBOCK, TEXAS 79423-1954

**LETTER TO BOARD OF DIRECTORS REGARDING POLICIES CONCERNING
AUDITS OF CFC BORROWERS**

Board of Directors
Graham County Utilities, Inc.
Pima, Arizona

We have audited, in accordance with auditing standards generally accepted in the United States of America, the financial statements of Graham County Utilities, Inc., for the year ended September 30, 2008, and have issued our report thereon dated November 3, 2008.

In connection with our audits nothing came to our attention that caused us to believe that the Cooperative failed to comply with the terms of Article V of the National Rural Utilities Cooperative Finance Corporation Loan Agreement insofar as they relate to accounting matters. However, our audits were not directed primarily toward obtaining knowledge of such noncompliance.

This report is intended solely for the information and use of the Boards of Directors and management of Graham County Utilities, Inc. and the National Rural Utilities Cooperative Finance Corporation and is not intended to be and should not be used by anyone other than these specified parties.

Bolinger, Segars, Gilbert & Moss L.L.P.

Certified Public Accountants

November 3, 2008

BOLINGER, SEGARS, GILBERT & MOSS, L.L.P.

CERTIFIED PUBLIC ACCOUNTANTS

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

Board of Directors
Graham County Utilities, Inc.
Pima, Arizona

We have audited the financial statements of Graham County Utilities, Inc. as of and for the year ended September 30, 2008, and have issued our report thereon dated November 3, 2008. 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 Graham County Utilities, Inc.'s internal control over financial reporting (internal control) 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 Cooperative's internal control. Accordingly, we do not express an opinion on the effectiveness of the company's internal control.

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.

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 internal control was for the limited purpose described in the first paragraph and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control that we consider to be material weaknesses, as defined above.

Board of Directors
Graham County Utilities, Inc.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Graham County Utilities, Inc.'s financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

This communication is intended for the information of the Board of Directors, management, USDA Rural Development, and supplemental lenders, and is not intended to be and should not be used by anyone other than these specified parties.

Bolinger, Segars, Gilbert & Moss LLP

Certified Public Accountants

November 3, 2008

BOLINGER, SEGARS, GILBERT & MOSS, L.L.P.

CERTIFIED PUBLIC ACCOUNTANTS

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

Board of Directors
Graham County Utilities, Inc.
Pima, Arizona

Compliance

We have audited the compliance of Graham County Utilities, Inc. with the types of compliance requirements described in the U. S. Office of Management and Budget (OMB) *Circular A-133 Compliance Supplement* that are applicable to each of its major federal programs for the year ended September 30, 2008. Graham County Utilities, Inc.'s major federal programs are identified in the summary of auditors' results section of the accompanying schedule of A-133 findings and questioned costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs is the responsibility of Graham County Utilities, Inc.'s management. Our responsibility is to express an opinion on Graham County Utilities, Inc.'s compliance based on our audit.

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

In our opinion, Graham County Utilities, Inc. complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended September 30, 2008.

Internal Control Over Compliance

The management of Graham County Utilities, Inc. is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered Graham County Utilities, Inc.'s internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of Graham County Utilities, Inc.'s internal control over compliance.

Board of Directors
Graham County Utilities, Inc.

A *control deficiency* in an entity's internal control over compliance 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 noncompliance with a type of compliance requirement of a federal program on a timely basis. A *significant deficiency* is a control deficiency, or combination of control deficiencies, that adversely affects the Cooperative's ability to administer a federal program such that there is more than a remote likelihood that noncompliance with a type of compliance requirement of a federal program that is more than inconsequential will not be prevented or detected by the Cooperative's internal control.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that material noncompliance with a type of compliance requirement of a federal program will not be prevented or detected by the Cooperative's internal control.

Our consideration of the internal control over compliance 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 or material weaknesses. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses, as defined above.

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

Bolinger, Segars, Gilbert & Moss LLP

Certified Public Accountants

November 3, 2008

FEDERAL FINANCIAL ASSISTANCE SECTION

GRAHAM COUNTY UTILITIES, INC.
SCHEDULE OF A-133 FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED SEPTEMBER 30, 2008

I. Summary of Auditors' Results

1. Type of auditor's report issued on the financial statements: **Unqualified**
2. Significant Deficiencies: **None.**
3. There were no significant deficiencies noted; therefore, there were no material weaknesses.
4. Noncompliance which is material to the financial statements: **None**
5. Type of auditor's report on compliance for major programs: **Unqualified**
6. Did the audit disclose findings which are required to be reported under Sec. __510(a): **No**
7. Major programs include:
 - 10.760 – Water and Waste Disposal Systems for Rural Communities
 - Dollar threshold used to distinguish between Type A and Type B programs: **\$300,000**
8. Low risk auditee: **No**

II. Findings Related to the Financial Statements

The audit disclosed no findings required to be reported.

III. Findings and Questioned Costs Related to the Federal Awards

The audit disclosed no findings required to be reported.

GRAHAM COUNTY UTILITIES, INC.
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED SEPTEMBER 30, 2008

<u>Federal Grantor/Program Title</u>	<u>Federal CFDA Number</u>	<u>Federal Expenditures and Indirect Costs</u>
<u>U.S. DEPARTMENT OF AGRICULTURE</u> Water and Waste Disposal Systems for Rural Communities	10.760	\$ 837,241

