

**STATE BOARD OF ACCOUNTS**  
**302 West Washington Street**  
**Room E418**  
**INDIANAPOLIS, INDIANA 46204-2769**

EXAMINATION REPORT  
OF  
DEPARTMENT OF WATER WORKS  
CITY OF MICHIGAN CITY  
LAPORTE COUNTY, INDIANA  
January 1, 2012 to December 31, 2012



**FILED**  
11/12/2013



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OFFICIALS

<u>Office</u>	<u>Official</u>	<u>Term</u>
Controller	Yvonne Hoffmaster Donna Pappas	01-01-12 to 01-31-12 02-01-12 to 12-31-13
Mayor	Ron Meer	01-01-12 to 12-31-15
President of the Board of Public Works and Safety	Michael Palmer (Vacant) Steve Janus	01-01-12 to 08-31-12 09-01-12 to 09-16-12 09-17-12 to 12-31-13
President of the Common Council	Marc Espar Duane Parry	01-01-12 to 12-31-12 01-01-13 to 12-31-13
Treasurer of the Water Works Board of Directors	Ted Gawronski Ken Behrendt	01-01-12 to 12-31-12 01-01-13 to 12-31-13
Office Manager	Ronald Plamowski	01-01-12 to 12-31-13
Superintendent	Randall E. Russell	01-01-12 to 12-31-13
President of the Water Works Board of Directors	Larry J. Jordan, III	01-01-12 to 12-31-13



**STATE OF INDIANA**  
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302 WEST WASHINGTON STREET  
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INDIANAPOLIS, INDIANA 46204-2769

Telephone: (317) 232-2513  
Fax: (317) 232-4711  
Web Site: [www.in.gov/sboa](http://www.in.gov/sboa)

INDEPENDENT ACCOUNTANT'S REPORT

TO: THE OFFICIALS OF THE DEPARTMENT OF WATER WORKS,  
CITY OF MICHIGAN CITY, LAPORTE COUNTY, INDIANA

We have examined the accompanying financial statements of the major enterprise fund of the Department of Water Works (Water Works), a department of the City of Michigan City, as of and for the year ended December 31, 2012. The Water Works' management is responsible for the financial statements presented herein. Our responsibility is to express an opinion based on our examination.

Our examination was conducted in accordance with attestation standards established by the American Institute of Certified Public Accountants and, accordingly, included examining, on a test basis, evidence supporting the financial statements presented herein and performing such other procedures as we considered necessary in the circumstances. We believe that our examination provides a reasonable basis for our opinion.

As discussed in Note I, the financial statements of the Water Works, are intended to present the financial position, and the changes in financial position and cash flows of only that portion of the major enterprise fund of the City that is attributable to the transactions of the Water Works. They do not purport to, and do not, present fairly the financial position of the City of Michigan City as of December 31, 2012, and the changes in its financial position and its cash flows, where applicable, for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the major enterprise fund for the Water Works, as of December 31, 2012, and the respective changes in financial position and cash flows thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

The Water Works has not presented Management's Discussion and Analysis that accounting principles generally accepted in the United States of America has determined is necessary to supplement, although not required to be part of, the basic financial statements.

Bruce Hartman  
State Examiner

August 1, 2013

DEPARTMENT OF WATER WORKS  
CITY OF MICHIGAN CITY  
STATEMENT OF NET POSITION  
December 31, 2012

<u>Assets</u>	<u>Water</u>
Current assets:	
Cash and cash equivalents	\$ 1,578,697
Accounts receivable (net of allowance)	514,788
Inventories	362,432
Prepaid expense	<u>45,036</u>
Total current assets	<u>2,500,953</u>
Noncurrent assets:	
Restricted cash, cash equivalents and investments:	
Improvement cash and investments	1,487,475
Bond and interest cash and investments	403,240
Customer deposits cash and investments	510,637
Pension assets	<u>71,955</u>
Total restricted assets	<u>2,473,307</u>
Deferred charges	<u>133,063</u>
Capital assets:	
Land, improvements to land and construction in progress	171,176
Other capital assets (net of accumulated depreciation)	<u>46,804,290</u>
Total capital assets (net of accumulated depreciation)	<u>46,975,466</u>
Total noncurrent assets	<u>49,581,836</u>
Total assets	<u>52,082,789</u>
<u>Liabilities</u>	
Current liabilities:	
Accounts payable	131,270
Accrued wages payable	74,622
Taxes payable	19,160
Unearned revenue	98,255
Current liabilities payable from restricted assets:	
Customer deposits	510,403
Revenue bonds payable	870,000
Loans payable	30,000
Accrued interest payable	<u>106,071</u>
Total current liabilities	<u>1,839,781</u>
Noncurrent liabilities:	
Revenue bonds payable (net of unamortized discounts and deferred amount on refunding)	2,977,770
Loans payable	5,934,916
Advances for construction	<u>20,907</u>
Total noncurrent liabilities	<u>8,933,593</u>
Total liabilities	<u>10,773,374</u>
<u>Net Position</u>	
Net investment in capital assets	37,162,780
Restricted for debt service	403,240
Restricted for capital outlay	1,487,475
Restricted for other purposes	582,592
Unrestricted	<u>1,673,328</u>
Total net position	<u>\$ 41,309,415</u>

The notes to the financial statements are an integral part of this statement.

DEPARTMENT OF WATER WORKS  
CITY OF MICHIGAN CITY  
STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET POSITION  
For The Year Ended December 31, 2012

	Water
Operating revenues:	
Metered water revenue:	
Residential	\$ 3,681,253
Industrial	1,085,612
Fire protection revenue	1,143,289
Penalties	36,029
Sales for resale	430,453
Other revenue	222,494
Total operating revenues	6,599,130
Operating expenses:	
Source of supply - operations and maintenance	618,025
Treatment expense - operations and maintenance	904,964
Transmission and distribution	975,798
Customer accounts	338,402
Administration and general	982,384
In lieu of tax	441,844
Gross income tax	200,458
Depreciation	1,202,400
Total operating expenses	5,664,275
Operating income	934,855
Nonoperating revenues (expenses):	
Interest and investment revenue	24,172
Amortization of bond issue costs	(53,367)
Interest expense	(330,889)
Total nonoperating revenues (expenses)	(360,084)
Income before contributions	574,771
Capital contributions	176,585
Change in net position	751,356
Total net position - beginning	40,558,059
Total net position - ending	\$ 41,309,415

The notes to the financial statements are an integral part of this statement.

DEPARTMENT OF WATER WORKS  
CITY OF MICHIGAN CITY  
STATEMENT OF CASH FLOWS  
For The Year Ended December 31, 2012

	Water
Cash flows from operating activities:	
Receipts from customers and users	\$ 5,862,880
Payments to suppliers and contractors	(1,717,434)
Payments to employees	(2,263,966)
Interfund services provided	782,694
Interfund services used	<u>(441,844)</u>
Net cash provided by operating activities	<u>2,222,330</u>
Cash flows from capital and related financing activities:	
Capital contributions	149,558
Acquisition and construction of capital assets	(2,217,909)
Principal paid on revenue bonds	(830,000)
Principal paid on state revolving fund loan	(40,000)
Interest paid on revenue bonds	(167,106)
Interest paid on state revolving fund loan	(173,853)
Refund on customer advances for construction	<u>(591)</u>
Net cash used by capital and related financing activities	<u>(3,279,901)</u>
Cash flows from investing activities:	
Interest received	<u>24,172</u>
Net decrease in cash and cash equivalents	(1,033,399)
Cash and cash equivalents, January 1	<u>5,013,448</u>
Cash and cash equivalents, December 31	<u>\$ 3,980,049</u>
Reconciliation of operating income to net cash provided by operating activities:	
Operating income	<u>\$ 934,855</u>
Adjustments to reconcile operating income to net cash provided by operating activities:	
Depreciation expense	1,202,400
(Increase) decrease in assets:	
Accounts receivable	(51,233)
Prepaid items	21,940
Inventories	6,016
Pension assets	923
Increase (decrease) in liabilities:	
Accounts payable	12,266
Accrued wages payable	(356)
Taxes payable	(2,158)
Unearned revenue	76,371
Customer deposits	<u>21,306</u>
Total adjustments	<u>1,287,475</u>
Net cash provided by operating activities	<u>\$ 2,222,330</u>
Noncash investing, capital and financing activities:	
Work in progress on account	\$ 965
Work in progress through accrued wages	1,889
Transfer of work in progress to depreciated capital assets	2,148,125
Contributed capital from customer advances for construction	27,027
Purchase of capital assets with trade-in	2,500
Disposal of capital assets	700,676

The notes to the financial statements are an integral part of this statement.

DEPARTMENT OF WATER WORKS  
CITY OF MICHIGAN CITY  
NOTES TO FINANCIAL STATEMENTS

**I. Summary of Significant Accounting Policies**

**A. Reporting Entity**

The financial statements reflect only the activity of the Department of Water Works (Water Works) and are not intended to present fairly the position of the City of Michigan City (City), and the results of its operations and cash flows of its enterprise funds. The Water Works, whose operations are controlled by the Water Works Board of Directors, per Indiana Code 8-1.5-4-1.5(b), represents a substantial portion of the City's enterprise funds.

**B. Fund Financial Statements**

Major enterprise fund financial statements consist of the Statement of Net Position; Statement of Revenues, Expenses, and Changes in Net Position; and the Statement of Cash Flows. Major enterprise funds rely to a significant extent on fees and charges for support.

**C. Measurement Focus, Basis of Accounting and Financial Statement Presentation**

The accounts of the major enterprise funds are maintained and the financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Under the accrual basis of accounting, revenues are recognized when earned and expenses are recognized when incurred.

Enterprise funds distinguish operating revenues and expenses from nonoperating items. Operating receipts and disbursements generally result from providing services and producing and delivering goods in connection with an enterprise fund's principal ongoing operations. The principal operating receipts of the enterprise funds are charges to customers for sales and services. Operating disbursements for enterprise funds include the cost of sales and services, administrative expenses, and depreciation on capital assets. All receipts and disbursements not meeting this definition are reported as nonoperating receipts and disbursements.

**D. Assets, Liabilities, and Net Position or Equity**

**1. Deposits and Investments**

The Water Works' cash and cash equivalents are considered to be cash on hand, demand deposits and short-term investments with original maturities of three months or less from the date of acquisition.

State statute (IC 5-13-9) authorizes the Water Works to invest in securities, including but not limited to, federal government securities, repurchase agreements, and certain money market mutual funds. Certain other statutory restrictions apply to all investments made by local governmental units.

Investment income, including changes in the fair value of investments, is reported as revenue in the operating statement.

**2. Inventories and Prepaid Items**

All inventories are valued at cost using the first in/first out (FIFO) method. Inventories are recorded as expenditures when consumed rather than when purchased.

DEPARTMENT OF WATER WORKS  
CITY OF MICHIGAN CITY  
NOTES TO FINANCIAL STATEMENTS  
(Continued)

Certain payments to vendors reflect costs applicable to future accounting periods and are recorded as prepaid items.

3. *Restricted Assets*

Certain proceeds of the enterprise fund, revenue bonds, as well as certain resources set aside for their repayment, are classified as restricted assets on the Statement of Net Position because their use is limited by applicable bond covenants.

4. *Capital Assets*

Capital assets, which include property, plant, and equipment, are reported in the financial statements.

Capital assets are reported at actual historical cost. Contributed or donated assets are reported at estimated fair value at the time received.

Capitalization thresholds (the dollar values above which asset acquisitions are added to the capital asset accounts), depreciation methods, and estimated useful lives of capital assets are as follows:

	<u>Capitalization Threshold</u>	<u>Depreciation Method</u>	<u>Estimated Useful Life</u>
Buildings	\$ 500	Composite	2%
Improvements other than buildings	500	Composite	2%
Machinery and equipment	500	Composite	2%
Transportation equipment	500	Composite	2%

For depreciated assets, the cost of normal maintenance and repairs that do not add to the value of the asset or materially extend asset lives are not capitalized.

Net operating gains/losses from disposal of assets and trade-ins are reported as increases/decreases to accumulated depreciation.

5. *Compensated Absences*

- a. Sick Leave – Water Works employees earn sick leave at the rate of 8 hours per month. Unused sick leave may be accumulated to a maximum of 180 days. Accumulated sick leave is not paid to employees upon termination.
- b. Vacation Leave – Water Works employees earn vacation leave at rates from 5 days to 20 days per year based upon the number of years of service. Vacation leave does not accumulate from year to year.
- c. Personal Leave – Water Works employees earn personal leave at the rate of 2 days per year. Personal leave does not accumulate from year to year.

No liability is reported for vacation, sick, and personal leave.

DEPARTMENT OF WATER WORKS  
CITY OF MICHIGAN CITY  
NOTES TO FINANCIAL STATEMENTS  
(Continued)

6. *Long-Term Obligations*

Long-term debt and other long-term obligations are reported as liabilities in the Statement of Net Position. Bond premiums and discounts, as well as issuance costs, are deferred and amortized over the life of the bonds using the straight-line method. Bonds payable are reported net of the applicable bond premium or discount. Bond issuance costs are reported as deferred charges and amortized over the term of the related debt.

7. *Net Position Restricted by Enabling Legislation*

The Water Works Statement of Net Position reports \$2,473,307 of restricted net position, of which \$2,473,307 is restricted by enabling legislation.

**II. Detailed Notes on All Funds**

A. *Deposits and Investments*

Custodial credit risk is the risk that in the event of a bank failure, the government's deposits may not be returned to it. Indiana Code 5-13-8-1 allows a political subdivision of the State of Indiana to deposit public funds in a financial institution only if the financial institution is a depository eligible to receive state funds and has a principal office or branch that qualifies to receive public funds of the political subdivision. The Water Works does not have a deposit policy for custodial credit risk. At December 31, 2012, the Water Works had deposit balances in the amount of \$3,980,049.

B. *Capital Assets*

Capital asset activity for the year ended December 31, 2012, was as follows:

	<u>Beginning Balance</u>	<u>Increases</u>	<u>Decreases</u>	<u>Ending Balance</u>
Capital assets, not being depreciated:				
Land	\$ 91,291	\$ -	\$ -	\$ 91,291
Construction in progress	<u>209,136</u>	<u>2,035,919</u>	<u>2,165,170</u>	<u>79,885</u>
Total capital assets, not being depreciated	<u>300,427</u>	<u>2,035,919</u>	<u>2,165,170</u>	<u>171,176</u>
Capital assets, being depreciated:				
Buildings	20,733,826	937,756	-	21,671,582
Improvements other than buildings	33,317,904	577,389	38,324	33,856,969
Machinery and equipment	<u>6,685,384</u>	<u>820,324</u>	<u>662,352</u>	<u>6,843,356</u>
Total capital assets, being depreciated:	<u>60,737,114</u>	<u>2,335,469</u>	<u>700,676</u>	<u>62,371,907</u>

DEPARTMENT OF WATER WORKS  
CITY OF MICHIGAN CITY  
NOTES TO FINANCIAL STATEMENTS  
(Continued)

	Beginning Balance	Increases	Decreases	Ending Balance
Less accumulated depreciation for:				
Buildings	5,163,412	410,464	-	5,573,876
Improvements other than buildings	8,878,840	659,588	38,324	9,500,104
Machinery and equipment*	1,021,141	134,848	662,352	493,637
Total accumulated depreciation	15,063,393	1,204,900	700,676	15,567,617
Total capital assets, being depreciated, net	45,673,721	1,130,569	-	46,804,290
Total capital assets, net	\$ 45,974,148	\$ 3,166,488	\$ 2,165,170	\$ 46,975,466

\*Includes Trade-ins of \$2,500.

Depreciation expense was charged to functions/programs of the Water Works as follows:

Business-type activities:	
Water Works	\$ 1,202,400

*C. Construction Commitments*

Construction work in progress is composed of the following:

Project	Expended to December 31, 2012	Committed
U.S. HWY 35/212 Main Project	\$ 79,885	\$ 703,308

*D. Long-Term Liabilities*

*1. Revenue Bonds*

The Water Works issues bonds to be paid by income derived from the acquired or constructed assets. Revenue bonds outstanding at year end are as follows:

Purpose	Interest Rates	Balance at December 31	Less: Deferral on Refunding	Revenue Bonds
2004 Waterworks refunding revenue bonds	3.5% to 3.75%	\$ 3,970,000	\$ 122,230	\$ 3,847,770

DEPARTMENT OF WATER WORKS  
CITY OF MICHIGAN CITY  
NOTES TO FINANCIAL STATEMENTS  
(Continued)

Revenue bonds debt service requirements to maturity are as follows:

Year Ended December 31	Water Works	
	Principal	Interest
2013	\$ 870,000	\$ 137,706
2014	905,000	106,794
2015	945,000	73,500
2016	970,000	37,781
2017	280,000	5,250
Totals	<u>\$ 3,970,000</u>	<u>\$ 361,031</u>

2. *Loan Payable*

The Water Works has entered into a State Revolving Fund Loan. Annual debt service requirements to maturity for the loan, including Interest of \$1,228,562, are as follows:

Year Ended December 31	Water Works	
	Principal	Interest
2013	\$ 30,000	\$ 172,765
2014	30,000	171,895
2015	25,000	171,098
2016	30,000	170,373
2017	760,000	166,240
2018-2022	<u>5,089,916</u>	<u>376,191</u>
Totals	<u>\$ 5,964,916</u>	<u>\$ 1,228,562</u>

3. *Advance Refunding*

In 2004, the Water Works defeased revenue bonds of 1995, by placing the proceeds of new bonds in an irrevocable trust to provide for all future debt service payments of the old bonds. Accordingly, the trust account assets and the liability for the defeased bonds are not included in the Water Works' financial statements. The following outstanding bonds, at December 31, 2012, were considered defeased:

\$ 4,115,000

DEPARTMENT OF WATER WORKS  
CITY OF MICHIGAN CITY  
NOTES TO FINANCIAL STATEMENTS  
(Continued)

4. *Changes in Long-Term Liabilities*

Long-term liability activity for the year ended December 31, 2012, was as follows:

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending Balance</u>	<u>Due Within One Year</u>
Water Works:					
Revenue bonds payable:					
2004 Waterworks refunding	\$ 4,800,000	\$ -	\$ 830,000	\$ 3,970,000	\$ 870,000
Less deferred amount on refunding	<u>151,566</u>	<u>-</u>	<u>29,336</u>	<u>122,230</u>	<u>29,335</u>
Total revenue bonds payable	<u>4,648,434</u>	<u>-</u>	<u>800,664</u>	<u>3,847,770</u>	<u>840,665</u>
Loans payable:					
State revolving fund	6,004,916	-	40,000	5,964,916	30,000
Less advances for construction	<u>48,525</u>	<u>-</u>	<u>27,618</u>	<u>20,907</u>	<u>-</u>
Total loans payable	<u>5,956,391</u>	<u>-</u>	<u>12,382</u>	<u>5,944,009</u>	<u>30,000</u>
Total long-term liabilities	<u>\$ 10,604,825</u>	<u>\$ -</u>	<u>\$ 813,046</u>	<u>\$ 9,791,779</u>	<u>\$ 870,665</u>

E. *Restricted Assets*

The balances of restricted asset accounts in the major enterprise fund are as follows:

Improvement cash and investment	\$ 1,487,475
Bond and interest cash and investments	403,240
Customer deposits cash and investments	510,637
Pension obligation	<u>71,955</u>
Total restricted assets	<u>\$ 2,473,307</u>

III. *Other Information*

A. *Risk Management*

The Water Works is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; job related illnesses or injuries to employees; medical benefits to employees and dependents (excluding postemployment benefits); and natural disasters.

The risks of torts; theft of, damage to, and destruction of assets; errors and omissions; job related illnesses or injuries to employees; medical benefits to employees and dependents (excluding post-employment benefits); and natural disasters are covered by commercial insurance from independent third parties. Settled claims from these risks have not exceeded commercial insurance coverage for the past three years. There were no significant reductions in insurance by major category of risk.

DEPARTMENT OF WATER WORKS  
CITY OF MICHIGAN CITY  
NOTES TO FINANCIAL STATEMENTS  
(Continued)

*B. Rate Structure*

The current rate structure was approved by the Indiana Utility Regulatory Commission on March 31, 2004. The Water Works has 12,642 customers.

*C. Pension Plan*

*Plan Description*

The Water Works has a defined contribution pension plan administered by McKready and Keene, Inc., as authorized by Indiana Code 8-1.5-3-7. The plan provides retirement, disability, and death benefits to plan members and beneficiaries. The plan was established by written agreement between the governing board of the Water Works and the Plan Administrator. The Plan Administrator issues a publicly available financial report that includes financial statements and required supplementary information of the plan. That report may be obtained by contacting:

McKready and Keene, Inc.  
7941 Castleway Drive  
P.O. Box 50460  
Indianapolis, IN 46250-0460  
Ph. (317) 849-4333

*Funding Policy and Annual Pension Cost*

The contribution requirements of plan members are established by the written agreement between the governing board of the Water Works and the Plan Administrator. Plan members are required to contribute 3 percent of the annual covered salary. The Water Works is required to contribute at an actuarially determined rate. The current rate is 0 percent of the annual covered payroll. Employer and employee contributions to the plan were \$0 and \$52,482, respectively.

Actuarial Information for the Above Plan

Annual required contribution	\$	-
Interest on net pension obligation		(4,373)
Adjustment to annual required contribution		<u>5,296</u>
Decrease in net pension obligation		923
Net pension obligation, beginning of year		<u>(72,878)</u>
Net pension obligation, end of year	\$	<u><u>(71,955)</u></u>

DEPARTMENT OF WATER WORKS  
CITY OF MICHIGAN CITY  
NOTES TO FINANCIAL STATEMENTS  
(Continued)

Contribution rates:	
Water Works	0%
Plan members	3%
Actuarial valuation date	01-01-13
Actuarial cost method	Entry age normal cost
Amortization method	Ten year level funding
Amortization period	30 years

Actuarial Assumptions

Investment rate of return	6.00%
Projected future salary increases:	4.00%

Three Year Trend Information

<u>Year Ending</u>	<u>Annual Pension Cost (APC)</u>	<u>Percentage of APC Contributed</u>	<u>Net Pension Obligation</u>
12-31-10	\$ 947	0.0%	\$ (73,813)
12-31-11	935	0.0%	(72,878)
12-31-12	923	0.0%	(71,955)

DEPARTMENT OF WATER WORKS  
CITY OF MICHIGAN CITY  
REQUIRED SUPPLEMENTARY INFORMATION  
SCHEDULE OF FUNDING PROGRESS

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) (b)	Assets Over Unfunded AAL (a-b)	Funded Ratio (a/b)	Covered Payroll (c)	Unfunded AAL as a Percentage of Covered Payroll ((a-b)/c)
01-01-08	\$ 8,923,668	\$ 5,910,351	\$ 3,013,317	151%	\$ 1,680,098	179%
01-01-09	7,534,128	6,174,000	1,360,128	122%	1,709,726	80%
01-01-10	8,601,372	6,560,416	2,040,956	131%	1,703,301	120%
01-01-11	9,243,455	6,113,433	3,130,022	151%	1,819,252	172%
01-01-12	9,063,628	6,834,945	2,228,683	133%	1,758,656	127%
01-01-13	9,651,039	7,112,954	2,538,085	136%	1,698,158	149%

The Schedule of Funding Progress, presented as RSI for the above plans following the Notes to the Financial Statements, presents multiyear trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liability for benefits.

DEPARTMENT OF WATER WORKS  
CITY OF MICHIGAN CITY  
EXIT CONFERENCE

The contents of this report were discussed on August 1, 2013, with Randall E. Russell, Superintendent; Ronald Plamowski, Office Manager; and Larry J. Jordan, III, President of the Water Works Board of Directors. Our examination disclosed no material items that warrant comment at this time.