

**City of Hazen, Arkansas
Waterworks and Sewer System**

**Financial Statements
December 31, 2021 and 2020**

(With Independent Auditor's Report Thereon)

City of Hazen, Arkansas

Waterworks and Sewer System

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INDEPENDENT AUDITOR'S REPORT

The Honorable Members of the City Council
City of Hazen, Arkansas

Report on the Audit of the Financial Statements

Opinion

We have audited the modified cash basis financial statements of the **City of Hazen, Arkansas Waterworks and Sewer System** (the System) as of and for the years ended December 31, 2021 and 2020, and the related notes to the financial statements, which collectively comprise the System's basic financial statements, as listed in the table of contents.

In our opinion, the accompanying financial statements present fairly, in all material respects, the modified cash basis financial position of the System as of December 31, 2021 and 2020, and the changes in modified cash basis financial position and cash flows thereof for the years then ended in accordance with the modified cash basis of accounting described in Note 2.

Basis for Opinion

We conducted our audits in accordance with auditing standards generally accepted in the United States of America (U.S. GAAS) and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Statements* section of our report. We are required to be independent of the System and to meet our other ethical responsibilities, in accordance with the relevant ethical requirements relating to our audits. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Emphasis of Matter – Basis of Accounting

We draw attention to Note 2, which describes the basis of accounting. The financial statements are prepared on the modified cash basis of accounting, which is a basis of accounting other than accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

Emphasis of Matter – Other

As discussed in Note 1, the financial statements present only the System and do not purport to, and do not, present fairly the financial position of the City of Hazen, Arkansas as of December 31, 2021 and 2020, the changes in its financial position or its cash flows for the years then ended in accordance with the modified cash basis of accounting. Our opinion is not modified with respect to this matter.

Report on the Audit of the Financial Statements (*Continued*)

Responsibilities of Management for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with the modified cash basis of accounting described in Note 2, and for determining that the modified cash basis of accounting is an acceptable basis for the preparation of the financial statements in the circumstances. Management is also responsible for the design, implementation and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance but is not absolute assurance and therefore is not a guarantee that an audit conducted in accordance with U.S. GAAS and *Government Auditing Standards* will always detect a material misstatement when it exists. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations or the override of internal control. Misstatements are considered material if there is a substantial likelihood that, individually or in the aggregate, they would influence the judgment made by a reasonable user based on the financial statements.

In performing an audit in accordance with U.S. GAAS and *Government Auditing Standards*, we:

- Exercise professional judgment and maintain professional skepticism throughout the audits.
- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, and design and perform audit procedures responsive to those risks. Such procedures include examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements.
- Obtain an understanding of internal control relevant to the audits in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the System's internal control. Accordingly, no such opinion is expressed.
- Evaluate the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluate the overall presentation of the financial statements.

We are required to communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit, significant audit findings and certain internal control-related matters that we identified during the audits.

The Honorable Members of the City Council
City of Hazen, Arkansas

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated June 14, 2022, on our consideration of the System's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, grant agreements and other matters. The purpose of that report is solely 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 effectiveness of internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the System's internal control over financial reporting and compliance.

A handwritten signature in black ink that reads "Landmark PLC". The signature is written in a cursive, flowing style.

Little Rock, Arkansas
June 14, 2022

City of Hazen, Arkansas

Waterworks and Sewer System

Statements of Net Position – Modified Cash Basis December 31, 2021 and 2020

	<u>2021</u>	<u>2020</u>
ASSETS		
Current Assets		
Cash and cash equivalents	\$ 332,545	\$ 180,941
Restricted Assets		
Cash and cash equivalents	45,262	44,970
Investments	54,683	55,733
Total Restricted Assets	<u>99,945</u>	<u>100,703</u>
Capital Assets, Net	<u>1,497,973</u>	<u>1,641,915</u>
Total Assets	<u>1,930,463</u>	<u>1,923,559</u>
DEFERRED OUTFLOW OF RESOURCES		
Deferred Loss on Refunding of Bonds Payable	<u>16,323</u>	<u>17,684</u>
TOTAL ASSETS AND DEFERRED OUTFLOW OF RESOURCES	<u><u>\$ 1,946,786</u></u>	<u><u>\$ 1,941,243</u></u>
LIABILITIES AND NET POSITION		
Current Liabilities Payable from Current Assets		
Customer deposits	\$ 23,413	\$ 23,428
Over billings due to customer	13,996	-
	<u>37,409</u>	<u>23,428</u>
Current Liabilities Payable from Restricted Assets		
Current portion of long-term debt	<u>45,000</u>	<u>45,000</u>
Total Current Liabilities	<u>82,409</u>	<u>68,428</u>
Long-Term Debt, Net	<u>1,458,635</u>	<u>1,502,054</u>
Total Liabilities	<u>1,541,044</u>	<u>1,570,482</u>
Net Position		
Net investment in capital assets	10,661	112,545
Restricted - expendable:		
Debt service	99,945	100,703
Unrestricted	295,136	157,513
Total Net Position	<u>405,742</u>	<u>370,761</u>
TOTAL LIABILITIES AND NET POSITION	<u><u>\$ 1,946,786</u></u>	<u><u>\$ 1,941,243</u></u>

See accompanying notes to financial statements.

City of Hazen, Arkansas

Waterworks and Sewer System

Statements of Revenues, Expenditures and Changes in Net Position – Modified Cash Basis Years Ended December 31, 2021 and 2020

	<u>2021</u>	<u>2020</u>
OPERATING REVENUES		
Collections for water and sewer sales and services	\$ 550,496	\$ 521,362
Collections for sewer recovery funds	16,640	-
Collection for leachate sales and services	200,160	47,520
Penalties	17,775	16,329
Customer repairs and other	11,923	5,216
Total Operating Revenues	<u>796,994</u>	<u>590,427</u>
OPERATING EXPENDITURES		
Salaries and wages	152,270	155,039
Payroll taxes	11,381	11,829
Depreciation and amortization	201,923	196,729
Utilities and telephone	59,477	55,576
Repairs and maintenance	83,439	32,667
Professional services	11,500	11,500
Operating supplies	90,120	81,927
Insurance	22,771	22,593
Office supplies	6,566	4,391
Retirement plan contributions	21,989	22,934
Other general operating expenses	20,034	20,250
Total Operating Expenditures	<u>681,470</u>	<u>615,435</u>
Operating Income (Loss)	<u>115,524</u>	<u>(25,008)</u>
NONOPERATING REVENUES (EXPENDITURES)		
Interest received	764	1,058
Interest paid	(60,105)	(61,420)
Amortization	(2,942)	(2,942)
Net Nonoperating Expenditures	<u>(62,283)</u>	<u>(63,304)</u>
Income (Loss) Before Operating Transfers	53,241	(88,312)
NET OPERATING TRANSFERS (TO) FROM OTHER CITY FUNDS	<u>(18,260)</u>	<u>77,892</u>
Increase (Decrease) in Net Position	34,981	(10,420)
NET POSITION, BEGINNING OF YEAR	<u>370,761</u>	<u>381,181</u>
NET POSITION, END OF YEAR	<u><u>\$ 405,742</u></u>	<u><u>\$ 370,761</u></u>

See accompanying notes to financial statements.

City of Hazen, Arkansas

Waterworks and Sewer System

Statements of Cash Flows – Modified Cash Basis Years Ended December 31, 2021 and 2020

	<u>2021</u>	<u>2020</u>
CASH FLOWS FROM OPERATING ACTIVITIES		
Receipts For		
Water and sewer sales and services	\$ 564,477	\$ 521,702
Sewer recovery	16,640	-
Leachate sales and services	200,160	47,520
Penalties	17,775	16,329
Customer repairs and other	7,698	5,216
Total Operating Receipts	<u>806,750</u>	<u>590,767</u>
Disbursements For		
Salaries, wages, and employee benefits	185,640	189,802
Goods and services	293,907	228,904
Total Operating Disbursements	<u>479,547</u>	<u>418,706</u>
Net Cash Provided by Operating Activities	<u>327,203</u>	<u>172,061</u>
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES		
Net operating transfers (to) from other city funds	<u>(30,260)</u>	<u>77,892</u>
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Payments of long-term debt	(45,000)	(56,620)
Proceeds from sale of capital assets	4,725	-
Purchases of capital assets	(46,481)	(74,392)
Interest paid	<u>(60,105)</u>	<u>(61,420)</u>
Net Cash Used by Capital and Related Financing Activities	<u>(146,861)</u>	<u>(192,432)</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Change in investments, net	1,050	(858)
Interest received	<u>764</u>	<u>1,058</u>
Net Cash Provided by Investing Activities	<u>1,814</u>	<u>200</u>
NET INCREASE IN CASH AND CASH EQUIVALENTS	151,896	57,721
CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR	<u>225,911</u>	<u>168,190</u>
CASH AND CASH EQUIVALENTS, END OF YEAR	<u>\$ 377,807</u>	<u>\$ 225,911</u>

(Continued)

See accompanying notes to financial statements.

City of Hazen, Arkansas

Waterworks and Sewer System

Statements of Cash Flows – Modified Cash Basis *(Continued)* Years Ended December 31, 2021 and 2020

	<u>2021</u>	<u>2020</u>
RECONCILIATION OF OPERATING INCOME (LOSS) TO NET CASH PROVIDED BY OPERATING ACTIVITIES		
Operating Income (Loss)	\$ 115,524	\$ (25,008)
Adjustments to Reconcile Operating Income (Loss) to Net Cash Provided by Operating Activities		
Depreciation and amortization	201,923	196,729
Gain on disposal of capital assets	(4,225)	-
Changes in customer deposits	(15)	340
Over billings due to customer	13,996	-
NET CASH PROVIDED BY OPERATING ACTIVITIES	<u><u>\$ 327,203</u></u>	<u><u>\$ 172,061</u></u>
RECONCILIATION OF CASH AND CASH EQUIVALENTS TO STATEMENTS OF NET POSITION - MODIFIED CASH BASIS		
Current Assets - cash and cash equivalents	\$ 332,545	\$ 180,941
Restricted Assets - cash and cash equivalents	45,262	44,970
TOTAL CASH AND CASH EQUIVALENTS	<u><u>\$ 377,807</u></u>	<u><u>\$ 225,911</u></u>
SUPPLEMENTAL DISCLOSURE OF NONCASH TRANSACTIONS		
Donated capital asset included in net operating transfers (to) from other city funds	<u><u>\$ 12,000</u></u>	<u><u>\$ -</u></u>

See accompanying notes to financial statements.

City of Hazen, Arkansas

Waterworks and Sewer System

Notes to Financial Statements **December 31, 2021 and 2020**

NOTE 1: REPORTING ENTITY

The City of Hazen, Arkansas Waterworks and Sewer System (the System) provides water sales and sewer treatment services to the citizens of the City of Hazen, Arkansas (the City) and to commercial and industrial customers located within the System's service area. The City Council serves as the governing board of the System and approves rates and fees for user charges.

These financial statements present only balances and transactions that are directly attributable to the System, and are not intended to present, and do not present, the financial position and changes therein of the City or its other proprietary funds.

NOTE 2: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Measurement Focus and Basis of Accounting

Although the System is not included in the regulatory financial statements of the City, the System is an enterprise fund of the City. An enterprise fund is used to account for business-type operations that are financed and operated in a manner similar to a private business enterprise, where the intent is that the costs, including depreciation, of providing goods or services to the general public on a continuing basis are financed or recovered primarily through user charges. The measurement focus of an enterprise fund is usually an economic resources measurement focus, the objectives of which are the determination of operating income, changes in financial position and cash flows. Under an economic resources measurement focus, all assets, deferred outflows of resources, deferred inflows of resources and liabilities (whether current or noncurrent, financial or nonfinancial) are reported. However, as explained in the paragraph that follows, certain modifications to the economic resources measurement focus result from the basis of accounting utilized by the System.

The System's transactions are recorded on the modified cash basis of accounting, which is a basis of accounting other than accounting principles generally accepted in the United States of America. Under the modified cash basis of accounting, the System generally recognizes assets, deferred outflows of resources, deferred inflows of resources, liabilities, revenues and expenditures when cash is received or paid. Therefore, these financial statements do not report accounts receivable and revenues for services billed or provided but not collected. In addition, these financial statements do not reflect deferred outflows of resources, deferred inflows of resources and liabilities or expenditures for goods or services received before year end for which payment has not yet been made. The only transactions reported in these financial statements that are not directly attributable to the receipts or disbursements of cash are depreciation and amortization of the System's capital assets over the estimated useful lives of the assets.

City of Hazen, Arkansas

Waterworks and Sewer System

Notes to Financial Statements
December 31, 2021 and 2020

NOTE 2: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Basis of Presentation

The presentation of the System's financial statements follows the requirements of Governmental Accounting Standards Board (GASB) Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*, as amended, as applicable to enterprise funds. In accordance with the requirements of this standard, the System's net position is categorized into net investment in capital assets, restricted and unrestricted, as applicable.

In addition, operating revenues and expenditures derived from or related directly to the distribution of water and treatment of wastewater are distinguished from nonoperating revenues and expenditures for purposes of presentation in the System's statements of revenues, expenses and changes in net position – modified cash basis. Operating revenues consist primarily of user charges and operating expenditures include the costs of maintaining and operating the water distribution and wastewater systems. Nonoperating revenues and expenditures consist of those revenues and expenses that are related to financing and investing type activities.

When an expenditure is incurred for purposes for which there are both restricted and unrestricted net position available, it is the System's policy to first apply that expenditure to restricted net position to the extent such are available and then to unrestricted net position.

Cash and Cash Equivalents

Cash and cash equivalents consist of all demand deposit, money market accounts and certificates of deposit with original maturities of three months or less.

Investments

Investments consist of certificates of deposit with original maturities in excess of three months. Investments are carried at cost, which approximates market value.

Capital Assets

The System's capital assets are reported at historical cost. Contributed assets are recorded at their estimated fair value at the time of contribution. Depreciation is provided using the straight-line method over the estimated useful lives of the assets, which range from three to forty years.

The System capitalizes all significant direct costs, including salaries, materials and supplies, related to construction and improvements completed by System personnel, while costs of repairs and maintenance that do not add significant value or extend the useful life of the related asset are expensed as incurred. Interest cost related to acquiring or constructing capital assets is capitalized as part of the cost of the related asset.

City of Hazen, Arkansas

Waterworks and Sewer System

Notes to Financial Statements
December 31, 2021 and 2020

NOTE 2: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Deferred Outflow of Resources

In addition to assets, the statements of net position – modified cash basis will sometimes report a separate section for deferred outflows of resources. This separate financial statement element represents a consumption of net position that applies to future periods and will not be recognized as an outflow of resources (expenditure) until then. The only item that qualifies for reporting in this category on the System's financial statements is the deferred loss on a refunding of bonds payable. A deferred loss on refunding results from the difference in the carrying value of refunded debt and its related reacquisition price. These deferred charges are amortized using the straight-line method over the shorter of the life of the refunded or refunding debt.

Long-Term Debt

Long-term debt is reported net of any applicable premiums or discounts. Premiums and discounts are deferred and amortized over the life of the bonds using the effective interest method.

Tax Status

The City, and thus the System, is exempt from income taxes under Section 115 of the Internal Revenue Code.

Estimates

The preparation of financial statements requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results may differ from those estimates.

Fund Transfers

All reallocations of resources between the System and other funds of the City are considered permanent in nature for financial statement reporting purposes. Thus, all interfund transfers affecting the System have been classified as operating transfers as reflected in the statements of revenues, expenditures and changes in net position – modified cash basis.

NOTE 3: DEPOSITS WITH FINANCIAL INSTITUTIONS

State of Arkansas (State) statutes require the City, and thus the System, to maintain cash balances on deposit with financial institutions located within the State. There is risk that, in the event of a bank failure, these deposits may not be returned to the System. To mitigate this risk, it is generally the System's policy to obtain collateral for all deposit balances in excess of Federal Deposit Insurance Corporation (FDIC) insurance and that such collateral be held in the System's name by an agent of the System. At December 31, 2021 and 2020, unrestricted and restricted deposit balances that were not FDIC insured, if any, were secured by collateral held by the System's agent in the System's name.

City of Hazen, Arkansas

Waterworks and Sewer System

Notes to Financial Statements December 31, 2021 and 2020

NOTE 4: RESTRICTED ASSETS

Certain proceeds of the water and sewer system improvement and refunding revenue bonds (see Note 6), as well as certain resources set aside for their repayment, are classified as restricted assets in the statements of net position – modified cash basis since their use is limited by applicable bond covenants. The bond fund is used to provide funds for the payment of principal and interest on the bonds as they become due and payable. The bond agreement requires monthly deposits to the bond fund equal to one-sixth of the next interest payment and one-twelfth of the next scheduled principal payment. In the event the monies held in the bond fund are not sufficient to pay scheduled principal and interest payments, amounts held in the debt service reserve fund will be used to the extent necessary. Balances in these funds at December 31, 2021 and 2020 are as follows:

	<u>2021</u>	<u>2020</u>
Bond fund	\$ 45,262	\$ 44,970
Debt service reserve fund	<u>54,683</u>	<u>55,733</u>
Restricted assets	<u><u>\$ 99,945</u></u>	<u><u>\$ 100,703</u></u>

NOTE 5: CAPITAL ASSETS

A summary of changes in major components of the System's capital assets and related activities resulting from modified cash basis transactions for the years ended December 31, 2021 and 2020:

		<u>2021</u>		
	<u>Estimated Useful Life</u>	<u>Balance Beginning of Year</u>	<u>Increases</u>	<u>Balance End of Year</u>
Non-depreciable:				
Land and improvements		\$ 13,702	\$ -	\$ 13,702
Construction in progress		426,566	-	426,566
		<u>440,268</u>	<u>-</u>	<u>440,268</u>
Depreciable:				
Water and wastewater plants and systems	15 - 40 years	5,636,035	11,129	5,647,164
Equipment and vehicles	3 - 7 years	366,364	47,351	376,473
		6,002,399	58,480	6,023,637
Less accumulated depreciation		<u>(4,800,752)</u>	<u>(201,923)</u>	<u>(4,965,932)</u>
		<u>1,201,647</u>	<u>(143,443)</u>	<u>1,057,705</u>
Capital assets, net		<u><u>\$ 1,641,915</u></u>	<u><u>\$ (143,443)</u></u>	<u><u>\$ 1,497,973</u></u>

City of Hazen, Arkansas

Waterworks and Sewer System

Notes to Financial Statements December 31, 2021 and 2020

NOTE 5: CAPITAL ASSETS (Continued)

		2020			
	Estimated Useful Life	Balance Beginning of Year	Increases	Decreases	Balance End of Year
Non-depreciable:					
Land and improvements		\$ 13,702	\$ -	\$ -	\$ 13,702
Construction in progress		426,566	-	-	426,566
		<u>440,268</u>	<u>-</u>	<u>-</u>	<u>440,268</u>
Depreciable:					
Water and wastewater plants and systems	15 - 40 years	5,562,262	73,773	-	5,636,035
Equipment and vehicles	3 - 7 years	365,745	619	-	366,364
		<u>5,928,007</u>	<u>74,392</u>	<u>-</u>	<u>6,002,399</u>
Less accumulated depreciation		<u>(4,604,023)</u>	<u>(196,729)</u>	<u>-</u>	<u>(4,800,752)</u>
		<u>1,323,984</u>	<u>(122,337)</u>	<u>-</u>	<u>1,201,647</u>
Capital assets, net		<u>\$ 1,764,252</u>	<u>\$ (122,337)</u>	<u>\$ -</u>	<u>\$ 1,641,915</u>

Certain balances and transactions, as reflected above, represent the System's portion of assets shared with other departments or funds of the City.

NOTE 6: LONG-TERM DEBT

Balances and repayment terms of the System's long term debt are as follows as of December 31, 2021 and 2020:

	2021	2020
\$1,810,000 City of Hazen, Arkansas Water and Sewer System Improvement and Refunding Revenue Bonds, Series 2014; term bonds payable annually through 2044; interest payable semiannually at rates ranging from 2.00% to 4.125%; payable from pledged operating revenues.	\$ 1,540,000	\$ 1,585,000
Less original bond issue discount	<u>(36,365)</u>	<u>(37,946)</u>
	1,503,635	1,547,054
Less current portion	<u>(45,000)</u>	<u>(45,000)</u>
Long-term debt, net of current portion	<u>\$ 1,458,635</u>	<u>\$ 1,502,054</u>

City of Hazen, Arkansas

Waterworks and Sewer System

Notes to Financial Statements December 31, 2021 and 2020

NOTE 6: LONG-TERM DEBT (Continued)

Long-term debt activity is summarized as follows for the years ended December 31, 2021 and 2020:

	<u>2021</u>	<u>2020</u>
Total long-term debt, beginning of year	\$ 1,585,000	\$ 1,641,620
Retirements	<u>(45,000)</u>	<u>(56,620)</u>
Total long-term debt, end of year	<u>\$ 1,540,000</u>	<u>\$ 1,585,000</u>

Scheduled principal and interest payments of long-term debt at December 31, 2021 are as follows:

<u>Year</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2022	\$ 45,000	\$ 58,755	\$ 103,755
2023	45,000	57,405	102,405
2024	45,000	56,055	101,055
2025	50,000	54,536	104,536
2026	50,000	52,849	102,849
2027-2031	275,000	237,740	512,740
2032-2036	330,000	183,436	513,436
2037-2041	410,000	111,700	521,700
2042-2044	<u>290,000</u>	<u>24,544</u>	<u>314,544</u>
	<u>\$ 1,540,000</u>	<u>\$ 837,020</u>	<u>\$ 2,377,020</u>

The Water and Sewer System Improvement and Refunding Revenue Bonds, Series 2014 (Series 2014 Bonds) were issued to finance the cost of certain capital improvements, to establish a debt service reserve and to refund the then outstanding Series 2003 Bonds. The difference between the reacquisition price and the net carrying amount of the refunded bonds is reported as a deferred outflow of resources in the statements of net position – modified cash basis and is being amortized through the year 2033 using the straight-line method. At December 31, 2021 and 2020, the deferred loss on refunding of bonds payable balance was \$16,323 and \$17,684, respectively. The Series 2014 Bonds are special obligations of the System, payable solely from the stabilized net revenues of the System, as defined in the related bond agreements. Principal and interest payments are due semi-annually with the final payment scheduled in 2044.

In addition to requiring the maintenance of certain restricted account balances (see Note 4), related bond covenants require that the System maintain rates as necessary to ensure at least 110% debt service coverage, as defined in related documents. The System was in compliance with the debt service coverage ratio for the years ended December 31, 2021 and 2020.

NOTE 7: ECONOMIC DEPENDENCY

City of Hazen, Arkansas

Waterworks and Sewer System

Notes to Financial Statements December 31, 2021 and 2020

Water and sewer sales to one industrial customer accounted for approximately 8% and 11% of total operating revenues for the years ended December 31, 2021 and 2020, respectively.

NOTE 8: RETIREMENT PLANS

The pension plan in which System employees participate meets the criteria set forth in GASB Statement No. 68, *Accounting and Financial Reporting for Pensions – An Amendment of GASB Statement No. 27*, as amended. Although reporting the liability and certain disclosures related to actuarial calculations for determining the total pension liability are not relevant to modified cash basis financial statements, required disclosures related to the description of the plan, types of benefits provided, funding policy, contribution requirements and rates, and actual cash contributions are applicable to the modified cash basis of accounting and are provided in the paragraphs that follow.

Plan Description

Employees of the System that meet certain eligibility requirements participate in the Arkansas Public Employees Retirement System (APERS), which is a cost-sharing multiple-employer defined benefit plan created by the Arkansas Legislature. APERS provides retirement and disability benefits, annual cost of living adjustments and death benefits to plan members and beneficiaries. Plan participants are fully vested in benefits provided under APERS upon reaching five years of service. Benefits, which are established and amended by State statute, are calculated on the basis of age, final average salary, years of service and a benefit factor. An annual stand-alone financial report for APERS may be obtained by making a written request at 124 West Capitol Avenue, Suite 400, Little Rock, Arkansas 72201 or by calling 501-682-7800 or 800-682-7377.

Contributions

Plan participants hired after July 1, 2005, are required to contribute 5.00% of their annual covered salary, and the System is required to contribute a percent of covered salary at rates established by the APERS Board of Trustees, based on actuarially determined rates. Employer contribution rates were 15.32% for both of the years ended December 31, 2021 and 2020. Contribution requirements are set forth in state statute. The System's proportionate share of contributions for employees directly involved in management and operation of the System for the years ended December 31, 2021 and 2020 were approximately \$22,000 and \$22,900, respectively, which were equal to the required contributions for each year.

NOTE 9: TRANSACTIONS WITH OTHER CITY FUNDS

Management has estimated that the economic benefit of certain administrative services provided by the City without charge to the System are immaterial, and thus has not allocated any portion of such expenses to the System. However, certain asset purchases and common expenditures funded partially by the System and partially by other city funds are reflected in the System's financial statements.

NOTE 9: TRANSACTIONS WITH OTHER CITY FUNDS (Continued)

City of Hazen, Arkansas

Waterworks and Sewer System

Notes to Financial Statements **December 31, 2021 and 2020**

Transfers (to) from other city funds for operations and capital improvements are reflected as operating transfers (to) from other city funds in the statements of revenues, expenditures and changes in net position – modified cash basis and totaled (\$18,260) and \$77,892 during the years ended December 31, 2021 and 2020, respectively.

NOTE 10: RISK MANAGEMENT

The System is exposed to various levels of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. The City has purchased commercial insurance to address these risks. There have been no significant reductions in the System's coverage during the years ended December 31, 2021 and 2020. In addition, there have been no settlements in excess of the System's coverage in any of the prior three fiscal years.

NOTE 11: RISKS AND UNCERTAINTIES

The COVID-19 pandemic remains a rapidly evolving situation. The extent of the impact of the COVID-19 pandemic on the System and financial results will depend on future developments, including the duration and spread of the outbreak and the related impact on consumer confidence and spending, all of which are highly uncertain.

NOTE 12: SEWER RECOVERY FUNDS

During the year ended December 31, 2020, it was determined that sewer rates had not been updated to reflect the appropriate sewer rates since 2017, and thus were lower than they should have been. Management of the System calculated the amount of sewer under billings for each citizen and commercial and industrial customer of the City, as applicable, and will be billed over thirty-six months. Effective June 2021, the sewer under billings began to be collected, and are recorded as collections for sewer recovery funds on the statements of revenues, expenditures and changes in net position – modified cash basis.

NOTE 13: OVER BILLINGS DUE TO CUSTOMER

During the year ended December 31, 2021, it was determined that the water meter for one of the System's customers was broken, resulting in increased meter readings and water revenue payments beginning in September 2021. Management has estimated these water over billings to be \$13,996, and is recorded as over billings due to customer on the statements of net position – modified cash basis as of December 31, 2021. On May 20, 2022, the System paid the customer these over billings in full.

Supplementary Information



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

The Honorable Members of the City Council
City of Hazen, Arkansas

We have audited, in accordance with the 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, the modified cash basis financial statements of the **City of Hazen, Arkansas Waterworks and Sewer System** (the System), which comprise the statement of net position – modified cash basis as of December 31, 2021, and the related statements of revenues, expenditures and changes in net position – modified cash basis, and cash flows – modified cash basis for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated June 14, 2022.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the System's internal control over financial reporting (internal control) as a basis for designing audit procedures that are appropriate in the circumstances 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 System's internal control. Accordingly, we do not express an opinion on the effectiveness of the System's internal control.

A *deficiency* in internal control 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 and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies, and therefore, material weaknesses or significant deficiencies may exist that have not been identified. We did identify certain deficiencies in internal control, described in the accompanying schedule of findings and responses as items 2021-1 and 2021-2 that we consider to be material weaknesses.

The Honorable Members of the City Council
City of Hazen, Arkansas

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the System's financial statements are free from 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 financial statements. 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 or other matters that are required to be reported under *Government Auditing Standards*.

The System's Response to Findings

The System's responses to the findings identified in our audit is described in the accompanying schedule of findings and responses. The System's responses were not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the System's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the System's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

A handwritten signature in black ink that reads "Landmark PLC". The signature is written in a cursive, flowing style.

Little Rock, Arkansas
June 14, 2022

City of Hazen, Arkansas

Waterworks and Sewer System

Schedule of Findings and Responses Year Ended December 31, 2021

Material Weakness in Internal Control over Financial Reporting

Finding **2021-1**

Criteria A good system of internal control provides for a proper segregation of accounting functions. Although proper segregation is not always possible in a small system, segregation to the extent possible can and should be implemented to reduce the risk of errors or fraud.

Condition During the year ended December 31, 2021, there were inherent limitations in the System's controls primarily due to the limited number of personnel.

Effect The limitations could allow the misappropriations of System funds.

Cause Internal controls showed a lack of segregation of duties primarily due to the limited number of personnel. This will likely be an ongoing issue due to its impracticality from a cost benefit standpoint.

Recommendation We recommend that management take steps to develop and implement new procedures to improve segregation of duties.

Response Client diligently attempts to segregate duties, but it is beyond current staffing capabilities.

See Independent Auditor's Report

City of Hazen, Arkansas

Waterworks and Sewer System

Schedule of Findings and Responses Year Ended December 31, 2021

Material Weakness in Internal Control over Financial Reporting

Finding **2021-2**

Criteria City Ordinance No. 470, Section 1, states that water user charges will be based on the number of gallons of water consumed.

Condition During the year ended December 31, 2021, it was brought to the System's attention that meter readings for a specific customer were abnormally high. After investigation, it was determined the meter was reading incorrect water usage beginning in September 2021.

Effect The System over billed a customer for water usage from September 2021 through December 31, 2021.

Cause Beginning in September 2021, the incorrect meter reading was charged to the customer, resulting in over billing of water revenue. For each month, there was no review in place to identify abnormalities in month-to-month usage.

Recommendation A report from the billing software should be produced on a monthly basis once all water meters have been read, with an appropriate member of management reviewing the report for large increases/decreases in water usage between the current and previous month. We recommend investigating differences over 10% between months.

Response Management determined the amount owed to the customer between September 2021 and March 2022, and recorded on the statements of net position – modified cash basis. On May 20, 2022, management paid the customer for the amounts owed for that same period. In addition, management is determining what report can be run for them to review month to month.

See Independent Auditor's Report.