

**TONTITOWN WATER & SEWER
COMMISSION**

FINANCIAL STATEMENTS AND INDEPENDENT AUDITOR'S REPORT

For the Years Ended December 31, 2010 and 2009

Tontitown Water & Sewer Commission
December 31, 2010 and 2009

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TONTITOWN WATER & SEWER COMMISSION
MANAGEMENT'S DISCUSSION AND ANALYSIS
DECEMBER 31, 2010 AND 2009

Our discussion and analysis of the Tontitown Water and Sewer Commission's (the Commission) financial performance provides an overview of the Commission's financial activities for the years ended December 31, 2010 and 2009. The Commission provides water and sewer services to residential, commercial, and industrial customers in and around Tontitown, Arkansas.

REPORT LAYOUT

In addition to Management's Discussion and Analysis ("MD&A"), the report consists of the Commission's financial statements, notes to the financial statements and supplementary information. The Balance Sheets and the Statements of Income and Changes in Net Assets provide information about the activities of the Commission and presents a longer-term view of the Commission's finances.

One of the most important questions asked about the Commission's finances is, "Is the Commission as a whole better off or worse off as a result of the year's activities?" The Balance Sheets and the Statements of Income and Changes in Net Assets help answer this question. These statements include all assets and liabilities using the accrual basis of accounting, which is similar to the accounting used by most private-sector companies. All of the current year's revenues and expenses are taken into account regardless of when cash is received or paid.

These statements report the Commission's net assets and changes in them. You can think of the Commission's net assets (assets less liabilities) as a way to measure the Commission's financial health. Over time, increases or decreases in the Commission's net assets are one indicator of whether its financial health is improving or deteriorating. However, you will need to consider other nonfinancial factors such as changes in the Commission's long range goals and the condition of the economy in which the Commission is located in order to assess its overall financial health.

FINANCIAL HIGHLIGHTS

	<u>2010</u>	<u>2009</u>
Total assets	\$ 16,395,985	\$ 15,020,548
Total net capital assets	12,626,351	11,210,767
Total long-term liabilities	5,323,864	5,493,313
Total liabilities	5,701,267	5,796,178
Net assets		
Invested in capital assets, net of related debt	7,130,024	5,553,284
Restricted	340,683	308,309
Unrestricted	3,224,011	3,362,777
Total net assets	10,694,718	9,224,370
Total operating revenues	773,708	712,157
Total operating expenses	853,571	769,214
Total non-operating income	2,040,237	570,789
Total non-operating expenses	243,212	253,164
Totals transfers in	219,672	216,316

Operating revenues increased \$61,551. This increase came primarily from increases in water revenue. We expect continued increases in operating revenues as the water and sewer system continues to increase its customer base. The operating loss increased \$106,778 compared to 2009. This increase is primarily due to increased sewer treatment cost (due to commencement of NACA operations) and depreciation. Payroll (including taxes) increased, however the increase is essentially neutralized when consideration is made for internalization of expenses related to repairs, locates and GIS maintenance which was previously done by outside contractors.

FINANCIAL CONTACT

The Commission's financial statements are designed to present users (citizens, taxpayers, customers, investors, and creditors) with a general overview of the Commission's finances and to demonstrate the Commission's accountability. If you have any questions about the report or need additional financial information, please contact the Commission's office at Tontitown Water Utilities, P.O. Box 127, Tontitown, Arkansas 72770.

DANIEL R. McCORMICK, C.P.A., P.A.

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INDEPENDENT AUDITOR'S REPORT

To the Chairman
Tontitown Water & Sewer Commission
Tontitown, Arkansas

We have audited the accompanying financial statements of the **Tontitown Water & Sewer Commission**, a component unit of the City of Tontitown, Arkansas as of December 31, 2010 and 2009 and for the years then ended. These component unit financial statements are the responsibility of the **Tontitown Water & Sewer Commission's** management. Our responsibility is to express an opinion on these financial statements based upon our audits.

We conducted our audits in accordance with generally accepted auditing standards and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the component unit 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.

The component unit financial statements present only the **Tontitown Water & Sewer Commission** and are not intended to present fairly the financial position and results of operations of the City of Tontitown, Arkansas in conformity with generally accepted accounting principles in the United States of America.

In our opinion, the component unit financial statements referred to above present fairly, in all material respects, the financial position of the **Tontitown Water & Sewer Commission** as of December 31, 2010 and 2009, 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 our report dated February 25, 2011, on our consideration of the **Tontitown Water & Sewer Commission's** internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grants.

Daniel R. McCormick, C.P.A., P.A.

Fayetteville, Arkansas
February 25, 2011

TONTITOWN WATER & SEWER COMMISSION
BALANCE SHEETS
December 31, 2010 and 2009

<u>ASSETS</u>	<u>2010</u>	<u>2009</u>
CURRENT ASSETS		
Cash	\$ 2,347,170	2,397,639
Accounts receivable-net of allowance for losses of \$700 as of December 31, 2010 and 2009	52,141	45,185
Sales tax receivable	44,641	73,982
Inventory	33,967	28,059
Total current assets	<u>2,477,919</u>	<u>2,544,865</u>
RESTRICTED ASSETS		
Meter deposits	30,288	31,154
Depreciation fund	99,556	82,703
Debt service fund	194,652	194,452
Total restricted assets	<u>324,496</u>	<u>308,309</u>
Advance to Northwest Arkansas Conservation Authority	<u>864,620</u>	<u>849,536</u>
FIXED ASSETS		
Land and improvements	232,506	85,789
Shop Building	89,608	-
Construction in progress	15,031	27,773
Equipment	472,079	427,631
Sewer system	8,631,824	7,163,118
Water system	4,916,093	4,873,772
Less: Accumulated depreciation	<u>(1,730,790)</u>	<u>(1,367,316)</u>
Total fixed assets	<u>12,626,351</u>	<u>11,210,767</u>
OTHER ASSETS		
Bond issue cost-net of accumulated amortization	28,624	29,882
Underwriter discount-net of accumulated amortization	73,125	76,339
Other assets	850	850
Total other assets	<u>102,599</u>	<u>107,071</u>
TOTAL ASSETS	<u><u>\$ 16,395,985</u></u>	<u><u>15,020,548</u></u>

<u>LIABILITIES AND NET ASSETS</u>	<u>2010</u>	<u>2009</u>
CURRENT LIABILITIES		
Accounts payable	\$ 107,456	34,533
Accrued liabilities	60,040	67,983
Total current liabilities	<u>167,496</u>	<u>102,516</u>
CURRENT LIABILITIES PAYABLE FROM RESTRICTED ASSETS		
Meter deposits	40,401	36,308
Water and sewer revenue bonds payable	169,506	164,041
Total current liabilities payable from restricted assets	<u>209,907</u>	<u>200,349</u>
LONG-TERM DEBT		
Water and sewer revenue bonds payable	5,323,864	5,493,313
TOTAL LIABILITIES	<u>5,701,267</u>	<u>5,796,178</u>
NET ASSETS		
Invested in capital assets, net of related debt	7,130,024	5,553,284
Restricted	340,683	308,309
Unrestricted	3,224,011	3,362,777
Total net assets	<u>10,694,718</u>	<u>9,224,370</u>
TOTAL LIABILITIES AND NET ASSETS	<u>\$ 16,395,985</u>	<u>15,020,548</u>

See accompanying notes to financial statements.

TONTITOWN WATER & SEWER COMMISSION
STATEMENTS OF INCOME AND CHANGES IN NET ASSETS
For the Years Ended December 31, 2010 and 2009

	2010	%	2009	%
OPERATING REVENUES				
Water revenue	\$ 577,418	74.63%	526,207	73.89%
Sewer revenue	60,005	7.76%	51,508	7.23%
Sewer access and tapping fees	-	0.00%	2,800	0.39%
Solid waste revenue	136,285	17.61%	131,642	0.00%
Total operating revenues	<u>773,708</u>	<u>100.00%</u>	<u>712,157</u>	<u>100.00%</u>
COST OF SALES				
Water purchases	245,770	31.77%	215,767	30.30%
Sewer service purchases	104,986	13.57%	44,274	6.22%
Solid waste reimbursement	115,730	14.96%	104,471	14.67%
Total cost of sales	<u>466,486</u>	<u>60.29%</u>	<u>364,512</u>	<u>51.18%</u>
GROSS PROFIT	307,222	39.71%	347,645	48.82%
OPERATING EXPENSES				
Amortization	4,473	0.58%	4,472	0.63%
Auto expense	12,233	1.58%	10,892	1.53%
Bad debts	137	0.02%	323	0.05%
Bank service charges	3,074	0.40%	3,977	0.56%
Bond processing fees	3,840	0.50%	3,840	0.54%
Computer support	21,128	2.73%	27,125	3.81%
Contract labor	60	0.01%	15,829	2.22%
Depreciation	363,473	46.98%	345,619	48.53%
Dues and subscriptions	12,975	1.68%	9,683	1.36%
Insurance, taxes and bonds	75,914	9.81%	41,327	5.80%
Materials and supplies	11,550	1.49%	9,265	1.30%
Miscellaneous	3,198	0.41%	3,510	0.49%
Office supplies and postage	16,797	2.17%	17,834	2.50%
Professional fees	52,254	6.75%	73,879	10.37%
Rent expense	18,000	2.33%	14,255	2.00%
Repairs and maintenance	101,758	13.15%	94,091	13.21%
Payroll and taxes	138,169	17.86%	83,973	11.79%
Utilities	14,538	1.88%	9,320	1.31%
Total operating expenses	<u>853,571</u>	<u>110.32%</u>	<u>769,214</u>	<u>99.42%</u>
OPERATING LOSS	(546,349)	-70.61%	(421,569)	-54.49%
NON-OPERATING REVENUES (EXPENSES)				
Sales tax revenue	549,164	70.98%	536,384	69.33%
State tribal assistance grant	-	0.00%	-	0.00%
Infrastructure contributions	1,446,230	186.92%	-	0.00%
Interest income	44,843	5.80%	49,257	6.37%
Interest expense	(243,212)	-31.43%	(248,692)	-32.14%
Total non-operating revenues	<u>1,797,025</u>	<u>232.26%</u>	<u>336,949</u>	<u>43.55%</u>
INCOME (LOSS) BEFORE TRANSFERS	1,250,676	161.65%	(84,620)	-10.94%
Transfers in	<u>219,672</u>	<u>28.39%</u>	<u>201,464</u>	<u>26.04%</u>
CHANGE IN NET ASSETS	1,470,348	190.04%	116,844	15.10%
NET ASSETS, JANUARY 1	9,224,370		9,107,526	
NET ASSETS, DECEMBER 31	<u>\$ 10,694,718</u>		<u>9,224,370</u>	

See accompanying notes to financial statements.

TONTITOWN WATER & SEWER COMMISSION
STATEMENTS OF CASH FLOWS
For the Years Ended December 31, 2010 and 2009

	2010	2009
OPERATING ACTIVITIES:		
Cash received from customers	\$ 781,008	666,523
Cash paid to suppliers and employees	(888,947)	(796,665)
NET CASH (USED) BY OPERATING ACTIVITIES	(107,939)	(130,142)
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES:		
Sales tax revenue	549,164	536,384
Transfers in	219,672	201,464
NET CASH PROVIDED FROM NONCAPITAL FINANCING ACTIVITIES	768,836	737,848
CAPITAL AND RELATED FINANCING ACTIVITIES:		
Additions to water system	(42,321)	(50,626)
Additions to sewer system	(185,137)	(10,087)
Additions to equipment	(44,447)	(138,542)
Additions to land and improvements	(236,325)	(85,789)
Additions to construction in progress	(15,031)	(27,773)
Principal paid on revenue bonds	(163,984)	(158,584)
Interest expense	(243,212)	(253,164)
Reimbursement of easement acquisition costs	190,435	-
NET CASH FROM CAPITAL AND RELATED FINANCING ACTIVITIES	(740,022)	(724,565)
INVESTING ACTIVITIES:		
Interest earned on cash deposits	44,843	49,257
NET CASH FROM INVESTING ACTIVITIES	44,843	49,257
NET DECREASE IN CASH AND RESTRICTED CASH	(34,282)	(67,602)
CASH AND RESTRICTED CASH, BEGINNING OF YEAR	2,705,948	2,773,550
CASH AND RESTRICTED CASH, END OF YEAR	\$ 2,671,666	2,705,948
RECONCILIATION OF OPERATING LOSS TO NET CASH USED IN OPERATING ACTIVITIES:		
Operating loss	\$ (546,349)	(417,097)
Adjustments to reconcile operating loss to cash:		
Provision for bad debts	323	323
Amortization	4,472	4,472
Depreciation	363,473	345,619
Changes in assets and liabilities:		
Accounts receivable	(7,279)	(17,657)
Sales tax receivable	29,340	(20,501)
Inventory	(5,908)	3,279
Accrued interest on NACA receivable	(15,084)	(11,948)
Customer deposits	4,093	544
Accounts payable and accrued expenses	64,980	(17,176)
NET CASH FROM OPERATING ACTIVITIES	\$ (107,939)	(130,142)
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:		
Interest paid	\$ 244,113	249,529
SUPPLEMENTAL DISCLOSURE OF NONCASH INVESTING ACTIVITIES:		
Infrastructure contributions	\$ 1,444,728	-

See accompanying notes to financial statements.

TONTITOWN WATER & SEWER COMMISSION
NOTES TO FINANCIAL STATEMENTS
For the Years Ended December 31, 2010 and 2009

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Tontitown Water & Sewer Commission (the Commission) is a component unit of the City of Tontitown, Arkansas. These financial statements present only the Tontitown Water & Sewer Commission, and are not intended to present the financial position and results of operations of the City of Tontitown, Arkansas in conformity with accounting principles generally accepted in the United States of America.

The Commission utilizes the accrual basis of accounting. Accordingly, revenue is recognized when earned rather than when received, and expenditures are recognized when incurred rather than when paid.

Customers' ability to honor their obligations to the Commission is dependent upon the general economic conditions in the areas surrounding the City of Tontitown.

Inventory is valued at cost.

Depreciation is computed on the straight-line method over the estimated lives of the related assets. The estimated useful lives are as follows:

Equipment	5-7 years
Sewer system	40 years
Water system	40 years
Building	39 years

The Commission capitalizes net interest costs and interest earned as part of the cost of constructing various projects when those costs are material.

Subsequent events have been evaluated through February 25, 2011, which is the date the financial statements were available to be issued.

2. CASH AND CERTIFICATES OF DEPOSIT

At December 31, 2010, the carrying amount and bank balance of the Commission's bank accounts and certificates of deposit were approximately \$2,672,000. Of the bank balances, \$500,000 was covered by federal depository insurance and \$2,093,000 was covered by collateral pledged by the depository institutions, and \$78,000 was on deposit with a bank in excess of the insured amount and not collateralized.

TONTITOWN WATER & SEWER COMMISSION
NOTES TO FINANCIAL STATEMENTS (continued)
For the Years Ended December 31, 2010 and 2009

Cash and restricted cash for cash flow reporting purposes are composed of the following:

	2010	2009
Petty cash	\$ 1,113	638
Operations and maintenance fund	19,750	(8,989)
Depreciation fund cash	99,556	82,703
Meter deposits	30,288	31,154
Capital improvements fund cash	266,596	241,425
Debt service fund	194,652	194,452
Sales and use tax fund	133,395	99,360
Water and sewer fund cash	1,926,316	2,065,205
	\$ 2,671,666	2,705,948

3. ADVANCE TO NORTHWEST ARKANSAS CONSERVATION AUTHORITY

The Commission has advanced funds to the Northwest Arkansas Conservation Authority (NACA), which was created to develop and build a wastewater treatment facility and related collection lines.

	2010	2009
Advance to NACA to obtain grant	\$354,845	354,845
State Tribal Assistance Grant funds	433,700	433,700
Accrued interest receivable	76,075	60,991
	\$864,620	849,536

The advance, related matching grant, and accrued interest are recorded as a liability to the Commission on the books of NACA and were due to be repaid to the Commission in 2010 together with accrued interest at the prime rate plus 1% (4.25% at December 31, 2010) on the \$354,845 advance. However, under the terms of the service agreement between NACA and the Commission (Note 7), the Commission is to be given credit towards the service agreement contract amount for the amount which the Commission has advanced to NACA pursuant to the grant. The terms of the repayment are to be agreed upon between NACA and the Commission, or if there is no agreement, over a period of three years. As of December 31, 2010, no credit had been applied to the service fees. The Commission's collection system was connected to the NACA system and NACA began treating the Commission's waste water in December, 2010.

TONTITOWN WATER & SEWER COMMISSION
NOTES TO FINANCIAL STATEMENTS (continued)
For the Years Ended December 31, 2010 and 2009

4. FIXED ASSETS

	<u>01/01/2010</u>	<u>Additions</u>	<u>Disposals</u>	<u>12/31/2010</u>
Equipment	\$ 427,631	44,447	-	472,078
Sewer system	7,163,118	1,468,707	-	8,631,825
Water system	4,873,772	42,321	-	4,916,093
Property and improvements	85,789	236,325	-	322,114
Construction in progress	27,773	(12,742)	-	15,031
Accumulated depreciation	<u>(1,367,316)</u>	<u>(363,474)</u>	-	<u>(1,730,790)</u>
Net fixed assets	<u>\$11,210,767</u>	<u>1,415,584</u>	<u>-</u>	<u>12,626,351</u>

5. WATER REVENUE BONDS PAYABLE

Water revenue bonds payable consisted of the following at December 31, 2010 and 2009:

	<u>2010</u>	<u>2009</u>
Water System Revenue Bond, serviced by Regions Bank and payable to the Arkansas Soil and Water Conservation Commission. Semi-annual installments of principal plus accrued interest are due each June 1 and December 1 until the scheduled maturity on June 1, 2027. Interest rate is fixed at 4.6%. Bond is collateralized by the water system and its related revenues.	\$ 218,370	227,354
Sewer System Revenue Bonds, serviced by Bank of the Ozarks and payable to Cede and Company. Bonds are collateralized by 75% of the net collections of the 1% sales and use tax levied within the city of Tontitown. Installments of accrued interest are due each April and installments of principal plus accrued interest are due each October until the final scheduled maturity on October 1, 2032. Interest rates are fixed and vary from 3.55% to 4.7%.	<u>5,275,000</u>	<u>5,430,000</u>
	5,493,370	5,657,354
Less current maturities	<u>(169,506)</u>	<u>(164,041)</u>
	<u>\$ 5,323,864</u>	<u>5,493,313</u>

TONTITOWN WATER & SEWER COMMISSION
NOTES TO FINANCIAL STATEMENTS (continued)
For the Years Ended December 31, 2010 and 2009

Debt service requirements at December 31, 2010 are as follows:

<u>Year Ended</u> <u>December 31,</u>	<u>Principal</u>	<u>Interest</u>
2011	169,506	238,234
2012	174,952	232,108
2013	180,420	225,617
2014	185,910	218,753
2015	196,422	211,503
2016 to 2020	1,100,683	932,435
2021 to 2025	1,357,632	678,131
2026 to 2030	1,597,845	351,883
2031 to 2032	<u>530,000</u>	<u>32,900</u>
Total	<u>\$5,493,370</u>	<u>\$3,121,564</u>

6. CONTINGENCIES

Significant losses are covered by commercial insurance for all major programs for which the Water and Sewer Commission retains risk of loss. For insured programs, there have been no significant reductions in insurance coverage.

7. COMMITMENTS

On April 24, 2007, the Commission entered into a service contract with NACA . The agreement as amended provides for the advance to NACA as discussed in Note 3, and for the treatment of waste water for the Commission by NACA beginning upon connection of the Commissions collection system with the completed NACA system. The connection was completed in December, 2010. The agreement also provides that the commission will share in the cost of operating the NACA facilities primarily based on the commission's pro rata share of treated waste water, that the Commission will charge its customers at rates adequate to cover the cost of NACA's services (to the extent allowed by law), and that the commission will not be required to compensate NACA in amounts in excess of its waste water revenues. Anticipated billings from NACA for 2011 (based on NACA's budget) are approximately \$730,000. The agreement has a term expiring the later of April, 2047 or such time as all NACA debt has been retired.

8. LEASES

The Company is obligated under a lease with CMP Properties, LLC for its Tontitown, Arkansas offices. The 24 month lease was effective October 1, 2009 with monthly payments of \$1,500. Rent expense for the year ended December 31, 2010 was \$18,000. The lease expires in 2011 and rental payments of \$13,500 are due during that year.

DANIEL R. McCORMICK, C.P.A., P.A.

Certified Public Accountant

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

To the Chairman
Tontitown Water & Sewer Commission
Tontitown, Arkansas

We have audited the balance sheets of the **Tontitown Water & Sewer Commission** as of December 31, 2010 and 2009 and the related statements of income and changes in net assets, and cash flows for the year then ended and have issued our report thereon dated February 25, 2011. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

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

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 control deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the **Tontitown Water and Sewer Commission'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 **Tontitown Water and Sewer Commission's** financial statements that is more than inconsequential will not be prevented or detected by the **Tontitown Water and Sewer Commission'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 **Tontitown Water and Sewer Commission's** internal control.

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

Compliance

As part of obtaining reasonable assurance that the component unit financial statements of the **Tontitown Water & Sewer Commission** are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, 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 report is intended for the information of the audit committee, management, and federal awarding agencies and pass-through entities. However, this report is a matter of public record and its distribution is not limited.

Daniel R. McCannick, C.P.A., P.A.

Fayetteville, Arkansas
February 25, 2011