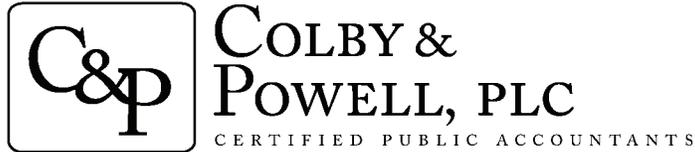


**TOWN OF PATAGONIA, ARIZONA**

Annual Financial Statements  
and Independent Auditors' Reports  
June 30, 2010

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## INDEPENDENT AUDITORS' REPORT

To the Town Council  
Town of Patagonia, Arizona

We have audited the accompanying financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the Town of Patagonia, Arizona, as of and for the year ended June 30, 2010, which collectively comprise the Town's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the Town of Patagonia, Arizona's management. Our responsibility is to express opinions on these financial statements based on our audit.

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. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and the significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the Town of Patagonia, Arizona, as of June 30, 2010, and the respective changes in financial position, and cash flows, where applicable, thereof for the year 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 January 25, 2011, on our consideration of the Town of Patagonia, Arizona's internal control over financial reporting and on our tests of its compliance with certain provisions 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 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 audit.

The Town of Patagonia has not presented the 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.

Accounting principles generally accepted in the United States of America require that the budgetary comparison information on pages 26 through 29 and Schedule of Agent Retirement Plan Funding Progress on page 30 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

*Colby + Powell PLLC*

January 25, 2011

**TOWN OF PATAGONIA, ARIZONA**  
**Statement of Net Assets**  
**June 30, 2010**

	Primary Government		
	Governmental Activities	Business-type Activities	Total
<b>ASSETS</b>			
Cash and cash equivalents	\$ 1,139,208	\$ 412,590	\$ 1,551,798
Accounts receivable	-	45,063	45,063
Taxes receivable	2,306	-	2,306
Due from other governments	23,758	-	23,758
Interest receivable	58	-	58
Prepaid expenses	29,850	14,925	44,775
Deposits	-	26,857	26,857
Cash, restricted	23,918	15,779	39,697
Capital assets, not being depreciated	355,867	150,540	506,407
Capital assets, being depreciated, net	<u>2,703,616</u>	<u>2,814,133</u>	<u>5,517,749</u>
<b>Total assets</b>	<u>4,278,581</u>	<u>3,479,887</u>	<u>7,758,468</u>
<b>LIABILITIES</b>			
Accounts payable	13,073	9,445	22,518
Accrued expenses	2,771	-	2,771
Refundable deposits	-	15,779	15,779
Compensated absences			
Due within 1 year	15,578	5,505	21,083
Noncurrent liabilities			
Due within 1 year	-	35,385	35,385
Due in more than 1 year	<u>-</u>	<u>527,198</u>	<u>527,198</u>
<b>Total liabilities</b>	<u>31,422</u>	<u>593,312</u>	<u>624,734</u>
<b>NET ASSETS</b>			
Invested in capital assets, net of related debt	3,059,483	2,503,796	5,563,279
Restricted for:			
Court enhancement	23,918	-	23,918
Highways and streets	144,460	-	144,460
Unrestricted (deficit)	<u>1,019,298</u>	<u>382,779</u>	<u>1,402,077</u>
<b>Total net assets</b>	<u>\$ 4,247,159</u>	<u>\$ 2,886,575</u>	<u>\$ 7,133,734</u>

*The accompanying notes are an integral part of these financial statements.*

**TOWN OF PATAGONIA, ARIZONA**  
**Statement of Activities**  
**Year Ended June 30, 2010**

Functions / Programs	Expenses	Program Revenue		Net (Expense) Revenue and Changes in Net Assets		
		Charges for Services	Operating Grants and Contributions	Governmental Activities	Primary Government	
					Business-type Activities	Total
<b>Primary government:</b>						
Governmental activities						
General government	\$ 270,223	\$ 36,713	\$ 13,900	\$ (219,610)	\$ -	\$ (219,610)
Public safety	344,695	28,481	-	(316,214)	-	(316,214)
Highways and streets	216,447	-	88,925	(127,522)	-	(127,522)
Culture and recreation	153,682	4,140	28,811	(120,731)	-	(120,731)
<b>Total governmental activities</b>	<u>985,047</u>	<u>69,334</u>	<u>131,636</u>	<u>(784,077)</u>	<u>-</u>	<u>(784,077)</u>
Business-type activities						
Water/wastewater	275,503	246,205	-	-	(29,298)	(29,298)
Solid waste	133,317	121,518	-	-	(11,799)	(11,799)
<b>Total business-type activities</b>	<u>408,820</u>	<u>367,723</u>	<u>-</u>	<u>-</u>	<u>(41,097)</u>	<u>(41,097)</u>
<b>Total primary government</b>	<u>\$ 1,393,867</u>	<u>\$ 437,057</u>	<u>\$ 131,636</u>	<u>(784,077)</u>	<u>(41,097)</u>	<u>(825,174)</u>
<b>General revenue:</b>						
Taxes:						
Town sales tax				163,962	-	163,962
Franchise fees				28,066	-	28,066
State sales tax				67,515	-	67,515
Auto lieu tax				57,928	-	57,928
State revenue sharing				193,666	-	193,666
Investment income				13,324	5,358	18,682
Miscellaneous				5,785	-	5,785
Total general revenue				<u>530,246</u>	<u>5,358</u>	<u>535,604</u>
Change in net assets				<u>(253,831)</u>	<u>(35,739)</u>	<u>(289,570)</u>
Net assets, July 1, 2009				<u>4,500,990</u>	<u>2,922,314</u>	<u>7,423,304</u>
Net assets, June 30, 2010				<u>\$ 4,247,159</u>	<u>\$ 2,886,575</u>	<u>\$ 7,133,734</u>

*The accompanying notes are an integral part of these financial statements.*

**TOWN OF PATAGONIA, ARIZONA**  
**Balance Sheet**  
**Governmental Funds**  
**June 30, 2010**

	General Fund	HURF/LTAF Fund	Grants Fund	Total Governmental Funds
<b>Assets</b>				
Cash and cash equivalents	\$ 1,028,149	\$ 123,589	\$ 11,388	\$ 1,163,126
Taxes receivable	2,306	-	-	2,306
Due from other governments	10,922	7,511	5,325	23,758
Interest receivable	58	-	-	58
Prepaid expenses	14,925	14,925	-	29,850
<b>Total assets</b>	<u>1,056,360</u>	<u>146,025</u>	<u>16,713</u>	<u>1,219,098</u>
<b>Liabilities</b>				
Accounts payable	11,378	1,565	130	13,073
Accrued expenses	2,771	-	-	2,771
Deferred revenue	-	-	5,325	5,325
<b>Total liabilities</b>	<u>14,149</u>	<u>1,565</u>	<u>5,455</u>	<u>21,169</u>
<b>Fund balances</b>				
Reserved for:				
Court enhancement	23,918	-	-	23,918
Prepaid expenses	14,925	14,925	-	29,850
Unreserved	1,003,368	129,535	11,258	1,144,161
<b>Total fund balance</b>	<u>1,042,211</u>	<u>144,460</u>	<u>11,258</u>	<u>1,197,929</u>
<b>Total liabilities and fund balance</b>	<u>\$ 1,056,360</u>	<u>\$ 146,025</u>	<u>\$ 16,713</u>	<u>\$ 1,219,098</u>

*The accompanying notes are an integral part of these financial statements.*

**TOWN OF PATAGONIA, ARIZONA**  
**Reconciliation of the Balance Sheet to the Statement of Net Assets**  
**Governmental Funds**  
**June 30, 2010**

Fund balances--total governmental funds	\$ 1,197,929
Amounts reported for governmental activities in the Statement of Net Assets are different because:	
Capital assets used in governmental activities are not financial resources and therefore, are not reported in the funds.	3,059,483
Some receivables are not available to pay for current-period expenditures and therefore, are deferred in the funds.	5,325
Some liabilities, are not due and payable in the current period and therefore, are not reported in the funds	<u>(15,578)</u>
Net assets of governmental activities	<u><u>\$ 4,247,159</u></u>

*The accompanying notes are an integral part of these financial statements.*

**TOWN OF PATAGONIA, ARIZONA**  
**Statement of Revenue, Expenditures, and Changes in Fund Balance**  
**Governmental Funds**  
**Year Ended June 30, 2010**

	General Fund	HURF/LTAF Fund	Grants Fund	Total Governmental Funds
<b>Revenues</b>				
Taxes	\$ 163,963	\$ -	\$ -	\$ 163,963
Intergovernmental	319,109	88,926	35,486	443,521
Franchise fees	28,067	-	-	28,067
Fines and forfeitures	28,482	-	-	28,482
Licenses and permits	10,179	-	-	10,179
Charges for services	28,499	-	-	28,499
Investment income	8,260	5,064	-	13,324
Other revenue	7,959	-	1,900	9,859
<b>Total revenues</b>	<b>594,518</b>	<b>93,990</b>	<b>37,386</b>	<b>725,894</b>
<b>Expenditures</b>				
Current				
General government	212,660	-	13,900	226,560
Public safety	329,710	-	-	329,710
Highways and streets	-	95,467	-	95,467
Culture and recreation	103,838	-	30,470	134,308
Capital outlay	2,704	-	-	2,704
<b>Total expenditures</b>	<b>648,912</b>	<b>95,467</b>	<b>44,370</b>	<b>788,749</b>
Net change in fund balances	(54,394)	(1,477)	(6,984)	(62,855)
Fund balance, July 1, 2009	1,096,605	145,937	18,242	1,260,784
Fund balance, June 30, 2010	<u>\$ 1,042,211</u>	<u>\$ 144,460</u>	<u>\$ 11,258</u>	<u>\$ 1,197,929</u>

*The accompanying notes are an integral part of these financial statements.*

**TOWN OF PATAGONIA, ARIZONA**  
**Reconciliation of the Statement of Revenue, Expenditures,**  
**and Changes in Fund Balances to the Statement of Activities**  
**Governmental Funds**  
**Year Ended June 30, 2010**

Net change in fund balances--total governmental funds		\$ (62,855)
<p>Amounts reported for governmental activities in the Statement of Activities are different because:</p>		
<p>Governmental funds report capital outlays as expenditures. However, in the Statement of Activities the cost of those assets is allocated over their estimated useful lives and reported as depreciation expense.</p>		
Capital outlay	2,704	
Depreciation expense	<u>(200,619)</u>	
		<u>(197,915)</u>
<p>Revenues in the Statement of Activities that do not provide current financial resources are not reported as revenues in the funds.</p>		
		5,325
<p>Some expenses reported in the Statement of Activities do not require the use of current financial resources and therefore, are not reported as expenditures in governmental funds.</p>		
		<u>1,614</u>
<b>Change in net assets of governmental activities</b>		<u><u>\$ (253,831)</u></u>

*The accompanying notes are an integral part of these financial statements.*

**TOWN OF PATAGONIA, ARIZONA**  
**Statement of Net Assets**  
**Proprietary Funds**  
**June 30, 2010**

	Business-type Activities--Enterprise Funds		
	Water/ Wastewater Fund	Solid Waste Fund	Total
<b>Assets</b>			
Current assets			
Cash and cash equivalents	\$ 378,248	\$ 34,342	\$ 412,590
Accounts receivable	30,121	14,942	45,063
Prepaid expenses	14,925	-	14,925
Total current assets	<u>423,294</u>	<u>49,284</u>	<u>472,578</u>
Noncurrent assets			
Deposit	26,857	-	26,857
Cash, restricted	11,303	4,476	15,779
Capital assets, net of accumulated depreciation, where applicable:			
Land	30,540	120,000	150,540
Utilities systems	2,092,362	668,480	2,760,842
Equipment	52,384	907	53,291
Capital assets, net	<u>2,175,286</u>	<u>789,387</u>	<u>2,964,673</u>
Total noncurrent assets	<u>2,213,446</u>	<u>793,863</u>	<u>3,007,309</u>
Total assets	<u>2,636,740</u>	<u>843,147</u>	<u>3,479,887</u>
<b>Liabilities</b>			
Current liabilities			
Accounts payable	8,945	500	9,445
Refundable deposits	11,303	4,476	15,779
Compensated absences	2,864	2,641	5,505
Notes payable, current	21,111	14,274	35,385
Total current liabilities	<u>44,223</u>	<u>21,891</u>	<u>66,114</u>
Noncurrent liabilities			
Estimated liability for landfill closure	-	101,705	101,705
Note payable	156,773	268,720	425,493
Total noncurrent liabilities	<u>156,773</u>	<u>370,425</u>	<u>527,198</u>
Total liabilities	<u>200,996</u>	<u>392,316</u>	<u>593,312</u>
<b>Net assets</b>			
Investment in capital assets, net of related debt	1,997,403	506,393	2,503,796
Unrestricted (deficit)	438,341	(55,562)	382,779
Total net assets	<u>\$ 2,435,744</u>	<u>\$ 450,831</u>	<u>\$ 2,886,575</u>

*The accompanying notes are an integral part of these financial statements.*

**TOWN OF PATAGONIA, ARIZONA**  
**Statement of Revenue, Expenses, and Changes in Fund Net Assets**  
**Proprietary Funds**  
**Year Ended June 30, 2010**

	Business-type Activities--Enterprise Funds		
	Water/ Waste water Fund	Solid Waste Fund	Total
<b>Operating revenue</b>			
Water (net of bad debts of \$3,476)	\$ 93,519	\$ -	\$ 93,519
Sewer (net of bad debts of \$4,461)	152,686	-	152,686
Refuse (net of bad debts of \$3,901)	-	121,518	121,518
Total operating revenue	<u>246,205</u>	<u>121,518</u>	<u>367,723</u>
<b>Operating expenses</b>			
Contract services	5,572	-	5,572
Depreciation	76,960	25,196	102,156
Insurance	10,576	3,272	13,848
Personnel	65,261	60,478	125,739
Repairs and maintenance	2,446	15,464	17,910
Landfill closure expense	-	6,507	6,507
Supplies	64,796	4,813	69,609
Travel and training	7,473	5,026	12,499
Utilities	35,966	579	36,545
Total operating expenses	<u>269,050</u>	<u>121,335</u>	<u>390,385</u>
Operating income (loss)	<u>(22,845)</u>	<u>183</u>	<u>(22,662)</u>
<b>Nonoperating revenue (expenses)</b>			
Investment income	5,333	25	5,358
Interest expense	(6,453)	(11,982)	(18,435)
Total nonoperating revenue (expenses)	<u>(1,120)</u>	<u>(11,957)</u>	<u>(13,077)</u>
Increase (decrease) in net assets	<u>(23,965)</u>	<u>(11,774)</u>	<u>(35,739)</u>
Total net assets, July 1, 2009	<u>2,459,709</u>	<u>462,605</u>	<u>2,922,314</u>
Total net assets, June 30, 2010	<u>\$ 2,435,744</u>	<u>\$ 450,831</u>	<u>\$ 2,886,575</u>

*The accompanying notes are an integral part of these financial statements.*

**TOWN OF PATAGONIA, ARIZONA**  
**Statement of Cash Flows**  
**Proprietary Funds**  
**Year Ended June 30, 2010**

	Business-type Activities--Enterprise Funds		
	Water/ Wastewater Fund	Solid Waste Fund	Total
<b>Cash Flows from Operating Activities</b>			
Receipts from customers	\$ 244,895	\$ 121,602	\$ 366,497
Payments to suppliers	(154,112)	(45,586)	(199,698)
Payments to employees	(42,553)	(43,788)	(86,341)
<b>Net cash provided (used) by operating activities</b>	<u>48,230</u>	<u>32,228</u>	<u>80,458</u>
<b>Cash Flows from Capital and Related Financing Activities</b>			
Purchase of capital assets	(4,993)	-	(4,993)
Interest payments on note payable	(6,453)	(11,982)	(18,435)
Principal payments on note payable	(20,404)	(13,699)	(34,103)
<b>Net cash provided (used) by capital and related financing activities</b>	<u>(31,850)</u>	<u>(25,681)</u>	<u>(57,531)</u>
<b>Cash Flows from Investing Activities</b>			
Interest received	5,924	57	5,981
<b>Net cash provided (used) by investing activities</b>	<u>5,924</u>	<u>57</u>	<u>5,981</u>
Net increase (decrease) in cash and cash equivalents	22,304	6,604	28,908
Cash and cash equivalents, beginning of year	<u>367,247</u>	<u>32,214</u>	<u>399,461</u>
<b>CASH AND CASH EQUIVALENTS, END OF YEAR</b>	<u>\$ 389,551</u>	<u>\$ 38,818</u>	<u>\$ 428,369</u>
Cash and cash equivalents	\$ 378,248	\$ 34,342	\$ 412,590
Cash, restricted	<u>11,303</u>	<u>4,476</u>	<u>15,779</u>
<b>CASH AND CASH EQUIVALENTS, END OF YEAR</b>	<u>\$ 389,551</u>	<u>\$ 38,818</u>	<u>\$ 428,369</u>

*The accompanying notes are an integral part of these financial statements.*

**TOWN OF PATAGONIA, ARIZONA**  
**Statement of Cash Flows**  
**Proprietary Funds**  
**Year Ended June 30, 2010**  
*(Continued)*

**Reconciliation of Operating Income (Loss) to Net Cash Provided (Used) by Operating Activities**

	Business-type Activities--Enterprise Funds		
	Water/ Wastewater Fund	Solid Waste Fund	Total
Operating income (loss)	\$ (22,845)	\$ 183	\$ (22,662)
Adjustments to reconcile operating income (loss) to net cash provided (used) by operating activities:			
Depreciation	76,960	25,196	102,156
Bad debt	7,937	3,901	11,838
(Increase) decrease in:			
Accounts receivable	(8,515)	(3,761)	(12,276)
Prepaid expenses	(4,873)	-	(4,873)
Increase (decrease) in:			
Accounts payable	(649)	155	(494)
Refundable deposits	(732)	(56)	(788)
Compensated absences	947	103	1,050
Estimated liability for landfill closure	-	6507	6,507
<b>Total adjustments</b>	<u>71,075</u>	<u>32,045</u>	<u>103,120</u>
<b>NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES</b>	<u>\$ 48,230</u>	<u>\$ 32,228</u>	<u>\$ 80,458</u>

*The accompanying notes are an integral part of these financial statements.*

**TOWN OF PATAGONIA, ARIZONA**  
**Notes to Financial Statements**  
**June 30, 2010**

***NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES***

The accompanying financial statements of the Town of Patagonia, Arizona have been prepared in conformity with U.S. generally accepted accounting principles applicable to governmental units adopted by the Governmental Accounting Standards Board (GASB). A summary of the Town's more significant accounting policies follows.

**A. Reporting Entity**

The Town is a general purpose local government that is governed by a separately elected Town Council. The accompanying financial statements present the activities of the Town (the primary government) and its component units.

Component units are legally separate entities for which the Town is considered to be financially accountable. Blended component units, although legally separate entities, are, in substance, part of the Town's operations. Therefore, data from these units is combined with data of the primary government. Discretely presented component units, on the other hand, are reported in a separate column in the combined financial statements to emphasize they are legally separate from the Town. The blended component unit discussed below has a June 30 year-end. The Town has no discretely presented component units.

**The Town of Patagonia Municipal Property Corporation** is a nonprofit corporation incorporated under the laws of the State of Arizona. The principal objective of the Corporation is to assist the Town of Patagonia, Arizona, in acquiring, constructing, financing, operating, improving or modifying public facilities for the benefit of all Town of Patagonia, Arizona, residents. The Corporation's board of directors consists of three members appointed by the Patagonia Town Council.

**TOWN OF PATAGONIA, ARIZONA**  
**Notes to Financial Statements**  
**June 30, 2010**

***NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – Continued***

**B. Basis of Presentation**

The basic financial statements include both government-wide statements and fund financial statements. The government-wide statements focus on the Town as a whole, while the fund financial statements focus on major funds. Each presentation provides valuable information that can be analyzed and compared between years and between governments to enhance the usefulness of the information.

Government-wide statements—provide information about the primary government (the Town). The statements include a statement of net assets and a statement of activities. These statements report the financial activities of the overall government. They also distinguish between the governmental and business-type activities of the Town. Governmental activities generally are financed through taxes and intergovernmental revenues. Business-type activities are financed in whole or in part by fees charged to external parties.

A statement of activities presents a comparison between direct expenses and program revenues for each function of the Town's governmental activities and segment of its business-type activities. Direct expenses are those that are specifically associated with a program or function and, therefore, are clearly identifiable to a particular function. The Town does not allocate indirect expenses to programs or functions. Program revenues include:

- charges to customers or applicants for goods, services, or privileges provided,
- operating grants and contributions, and
- capital grants and contributions.

Revenues that are not classified as program revenues, including internally dedicated resources and all taxes, are reported as general revenues.

Generally, the effect of interfund activity has been eliminated from the government-wide financial statements to minimize the double counting of internal activities. However, charges for interfund services provided and used are not eliminated if the prices approximate their external exchange values.

Fund financial statements—provide information about the Town's funds. Separate statements are presented for governmental and proprietary fund categories. The emphasis of fund financial statements is on major governmental and enterprise funds, each displayed in a separate column. All remaining governmental and enterprise funds are aggregated and reported as nonmajor funds.

**TOWN OF PATAGONIA, ARIZONA**  
**Notes to Financial Statements**  
**June 30, 2010**

***NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – Continued***

Proprietary fund operating revenues, such as charges for services, result from transactions associated with the fund's principal activity in which each party receives and gives up essentially equal values. Nonoperating revenues, such as subsidies and investment earnings, result from transactions in which the parties do not exchange equal values. Revenues generated by ancillary activities are also reported as nonoperating revenues.

The Town reports the following major governmental funds:

The ***General Fund*** is the Town's primary operating fund. It accounts for all financial resources of the general government, except those required to be accounted for in another fund.

The ***HURF/LTAF Fund*** accounts for specific revenue received from the State of Arizona Highway User Revenue Fund and Arizona Lottery proceeds, which is legally restricted to expenditures for authorized transportation purposes.

The ***Grants Fund*** accounts for specific revenue sources that are restricted to expenditures for specified purposes as defined by the grantor. The Town's grants include various public safety grants, library grants, and general improvement grants.

The Town reports the following major enterprise funds:

The ***Water/Wastewater*** and ***Solid Waste Funds*** account for operations that are financed and operated in a manner similar to private business enterprises, in which the intent of the Town Council is that the costs (expenses, including depreciation) of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges; or for which the Town Council has decided that periodic determination of revenue earned, expenses incurred, or net income is appropriate for capital maintenance, public policy, management control, accountability, or other purposes.

**C. Basis of Accounting**

The government-wide and proprietary fund financial statements are presented using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded at the time liabilities are incurred, regardless of when the related cash flows take place. Grants and donations are recognized as revenue as soon as all eligibility requirements the provider imposed have been met.

**TOWN OF PATAGONIA, ARIZONA**  
**Notes to Financial Statements**  
**June 30, 2010**

***NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – Continued***

Governmental funds in the fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Under this method, revenues are recognized when measurable and available. The Town considers all revenues reported in the governmental funds to be available if the revenues are collected within 60 days after year-end. Expenditures are recorded when the related fund liability is incurred, except for principal and interest on general long-term debt, and compensated absences, which are recognized as expenditures to the extent they are due and payable. General capital asset acquisitions are reported as expenditures in governmental funds. Issuances of general long-term debt and acquisitions under capital lease agreements are reported as other financing sources.

The Town's business-type activities and enterprise funds follow FASB Statements and Interpretations issued after November 30, 1989; Accounting Principles Board Opinions; and Accounting Research Bulletins, unless those pronouncements conflict with GASB pronouncements.

**D. Cash and Investments**

For purposes of its statement of cash flows, the Town considers only those highly liquid investments with a maturity of three months or less when purchased to be cash equivalents.

Nonparticipating interest-earning investment contracts are stated at cost. Money market investments and participating interest-earning investment contracts with a remaining maturity of one year or less at time of purchase are stated at amortized cost. All other investments are stated at fair value.

**E. Allowance for Uncollectible Accounts**

Allowances for uncollectible accounts receivable in the Liquid Waste Fund and the Solid Waste Fund are estimated by the Town. The amounts recorded as uncollectible in the Water/Wastewater and Solid Waste Funds at June 30, 2010 totaled \$6,700 and \$3,300, respectively.

**F. Fund Balance Reservations/Net Asset Restrictions**

As of June 30, 2010, \$23,918 was reserved in the governmental fund financial statements in the General Fund and restricted in the Governmental Activities column of the government-wide financial statements for court expenses which must be approved by the Arizona Administrative Office of the Courts.

When both restricted and unrestricted resources are available for use, it is the Town's policy to use restricted resources first, and then unrestricted resources, as they are needed.

**TOWN OF PATAGONIA, ARIZONA**  
**Notes to Financial Statements**  
**June 30, 2010**

**NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – Continued**

**G. Capital Assets**

Capital assets are reported at actual cost. 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 reported in the government-wide statements and proprietary funds are as follows:

	<u>Capitalization Threshold</u>	<u>Depreciation Method</u>	<u>Estimated Useful Life (years)</u>
Land	\$ 5,000	N/A	N/A
Buildings	5,000	Straight-line	40
Parks	5,000	Straight-line	40
Streets	5,000	Straight-line	20-30
Sewer collection system	5,000	Straight-line	10-40
Furniture and fixtures	5,000	Straight-line	5-10
Equipment	5,000	Straight-line	5-10

**H. Investment Income**

Investment income is composed of interest, dividends, and net changes in the fair value of applicable investments.

**I. Compensated Absences**

Compensated absences consist of vacation leave earned by employees based on services already rendered.

Employees may accumulate up to 240 hours of vacation hours depending on their years of service. Upon termination of employment, all unused vacation benefits are paid to employees. Accordingly, vacation benefits are accrued as a liability in the financial statements.

Employees may accumulate up to 360 hours of sick leave hours but any sick hours in excess of the maximum amount that are unused at year-end are forfeited. Because sick leave benefits do not vest with employees, a liability for sick leave benefits is not accrued in the financial statements.

**TOWN OF PATAGONIA, ARIZONA**  
**Notes to Financial Statements**  
**June 30, 2010**

**NOTE 2 – DEPOSITS AND INVESTMENTS**

Arizona Revised Statutes (A.R.S.) authorize the Town to invest public monies in the State Treasurer’s investment pool; U.S. Treasury obligations; specified state and local government bonds; and interest-earning investments such as savings accounts, certificates of deposit, and repurchase agreements in eligible depositories. The statutes require collateral for demand deposits, certificates of deposit, and repurchase agreements at 101 percent of all deposits not covered by federal depository insurance.

The Town has not formally adopted deposit and investment policies that limit the Town’s allowable deposits or investments and which address the specific types of risk to which the Town is exposed such as interest rate risk, credit risk, and custodial credit risk.

*Deposits* – At June 30, 2010, the carrying amount of the Town’s total cash in bank was \$307,028, and the bank balance was \$321,344. The entire bank balance was fully insured by the Federal Deposit Insurance Corporation (FDIC).

Restricted cash in the proprietary fund financial statements and the business-type activities in the government-wide financial statements of \$15,779 consists of cash restricted for customer utility deposits. Restricted cash of \$23,918 in the governmental activities of the government-wide financial statements consists of cash restricted for court enhancements.

*Investments* – At June 30, 2010, the investments consisted of the following:

Investment	Rating Organization	Credit Rating	Reported Amount	Fair Value
Arizona LGIP Pool 5	S&P	AAAf/S1	\$ 1,160,792	\$ 1,160,792
Arizona LGIP Pool 7	N/A	Unrated	90,290	90,290
Arizona LGIP Pool 500	N/A	Unrated	32,746	32,746
			<u>\$ 1,283,828</u>	<u>\$ 1,283,828</u>

The State Board of Investment provides oversight for the State Treasurer’s pools, and the Local Government Investment Pool Advisory Committee provides consultation and advice to the Treasurer. The fair value of a participant’s position in the pool approximates the value of that participant’s pool shares. Those shares are not identified with specific investments and are not subject to custodial credit risk. All other investments were insured or registered in the Town’s name, or were held by the Town or its agent in the Town’s name.

**TOWN OF PATAGONIA, ARIZONA**  
**Notes to Financial Statements**  
**June 30, 2010**

**NOTE 3 – DUE FROM OTHER GOVERNMENTS**

Amounts due from other governments at June 30, 2010 included \$5,773 in state-shared revenue from sales taxes, \$5,149 in county-shared revenue from auto lieu taxes, \$7,511 in state-shared revenue from highway user revenue fund (HURF) taxes, and \$5,325 in county library grants.

**NOTE 4 – CAPITAL ASSETS**

Capital asset activity for the year ended June 30, 2010, was as follows:

	<u>Balance</u> <u>July 1, 2009</u>	<u>Increases</u>	<u>Decreases</u>	<u>Balance</u> <u>June 30, 2010</u>
Governmental activities:				
Capital assets not being depreciated:				
Land	\$ 355,867	\$ -	\$ -	\$ 355,867
Construction in progress	116,673	-	(116,673)	-
<b>Total capital assets not</b>				
<b>being depreciated</b>	<u>472,540</u>	<u>-</u>	<u>(116,673)</u>	<u>355,867</u>
Capital assets being depreciated:				
Equipment	386,765	-	-	386,765
Buildings	1,521,826	116,673	-	1,638,499
Parks	236,705	2,704	-	239,409
Streets	3,475,263	-	-	3,475,263
<b>Total</b>	<u>5,620,559</u>	<u>119,377</u>	<u>-</u>	<u>5,739,936</u>
Less accumulated depreciation for:				
Equipment	(283,248)	(18,724)	-	(301,972)
Buildings	(525,043)	(51,230)	-	(576,273)
Parks	(155,127)	(10,138)	-	(165,265)
Streets	(1,872,283)	(120,527)	-	(1,992,810)
<b>Total</b>	<u>\$ (2,835,701)</u>	<u>\$ (200,619)</u>	<u>\$ -</u>	<u>(3,036,320)</u>
<b>Total capital assets</b>				
<b>being depreciated, net</b>	<u>2,784,858</u>	<u>(81,242)</u>	<u>-</u>	<u>2,703,616</u>
Governmental activities capital assets, net	<u>\$ 3,257,398</u>	<u>\$ (81,242)</u>	<u>\$ (116,673)</u>	<u>\$ 3,059,483</u>

**TOWN OF PATAGONIA, ARIZONA**  
**Notes to Financial Statements**  
**June 30, 2010**

**NOTE 4 – CAPITAL ASSETS – Continued**

	Balance July 1, 2009	Increases	Decreases	Balance June 30, 2010
Business-type activities:				
Capital assets not being depreciated:				
Land	\$ 150,540	\$ -	\$ -	\$ 150,540
<b>Total capital assets not       being depreciated</b>	<b>150,540</b>	<b>-</b>	<b>-</b>	<b>150,540</b>
Capital assets being depreciated:				
Land improvements	738,732	-	-	738,732
Buildings	1,737,224	-	-	1,737,224
Sewer collection system	980,094	-	-	980,094
Machinery and equipment	417,686	4,993	-	422,679
<b>Total</b>	<b>3,873,736</b>	<b>4,993</b>	<b>-</b>	<b>3,878,729</b>
Less accumulated depreciation for:				
Land improvements	(45,627)	(24,625)	-	(70,252)
Buildings	(235,068)	(43,431)	-	(278,499)
Sewer collection system	(319,554)	(26,903)	-	(346,457)
Machinery and equipment	(362,191)	(7,197)	-	(369,388)
<b>Total</b>	<b>\$ (962,440)</b>	<b>\$ (102,156)</b>	<b>\$ -</b>	<b>(1,064,596)</b>
<b>Total capital assets       being depreciated, net</b>	<b>2,911,296</b>	<b>(97,163)</b>	<b>-</b>	<b>2,814,133</b>
Business-type activities capital assets, net	<b>\$ 3,061,836</b>	<b>\$ (97,163)</b>	<b>\$ -</b>	<b>\$ 2,964,673</b>

Depreciation expense was charged to functions as follows:

Governmental activities:	
General government	\$ 44,068
Public safety	15,390
Highways and streets	121,384
Culture and recreation	19,777
Total governmental activities depreciation expense	<b>\$ 200,619</b>
Business-type activities:	
Water/Wastewater	\$ 76,960
Solid Waste	25,196
Total business-type activities depreciation expense	<b>\$ 102,156</b>

**TOWN OF PATAGONIA, ARIZONA**  
**Notes to Financial Statements**  
**June 30, 2010**

**NOTE 5 – LONG-TERM LIABILITIES**

The following schedule details the Town’s long-term liability and obligation activity for the year ended June 30, 2010.

	Balance July 1, 2009	Additions	Reductions	Balance June 30, 2010	Due within 1 year
Governmental activities:					
Compensated absences payable	\$ 17,192	\$ 14,331	\$ 15,945	\$ 15,578	\$ 15,578
Governmental activities long-term liabilities	<u>\$ 17,192</u>	<u>\$ 14,331</u>	<u>\$ 15,945</u>	<u>\$ 15,578</u>	<u>\$ 15,578</u>
Business-type activities					
Compensated absences payable	\$ 4,455	\$ 3,707	\$ 2,657	\$ 5,505	\$ 5,505
Landfill closure costs	95,198	6,507	-	101,705	-
Notes payable	494,981	-	34,103	460,878	35,385
Business-type activities long-term liabilities	<u>\$ 594,634</u>	<u>\$ 10,214</u>	<u>\$ 36,760</u>	<u>\$ 568,088</u>	<u>\$ 40,890</u>

The following schedule details debt service requirements to maturity for the Town’s notes payable at June 30, 2010.

Year Ending June 30	Business Activities	
	Notes Payable	
	Principal	Interest
2011	35,385	17,151
2012	36,991	15,818
2013	38,104	14,433
2014	39,540	12,996
2015	41,032	11,505
2016-2020	159,841	35,910
2021-2025	109,985	11,241
Total	<u>\$ 460,878</u>	<u>\$ 119,054</u>

**TOWN OF PATAGONIA, ARIZONA**  
**Notes to Financial Statements**  
**June 30, 2010**

**NOTE 5 – LONG-TERM LIABILITIES – Continued**

Notes payable consisted of the following:

<u>Description</u>	<u>Original Amount</u>	<u>Maturity Ranges</u>	<u>Interest Rates</u>	<u>Outstanding Principal</u>
<u>Business-type Activities</u>				
Note payable - Water Infrastructure Finance Authority of Arizona	\$ 375,000	2002-2021	3.420%	\$ 177,884
Note payable - United States Department of Agriculture	<u>302,235</u>	2009-2025	4.125%	<u>282,994</u>
	<u>\$ 677,235</u>			<u>\$ 460,878</u>

**NOTE 6 – RISK MANAGEMENT**

The Town is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. The Town carries commercial insurance for all such risks of loss, including workers' compensation and employees' health and accident insurance. Settled claims resulting from these risks have not exceeded commercial insurance coverage in any of the past three fiscal years.

**NOTE 7 – RETIREMENT PLANS**

Plan Descriptions – The Town contributes to the two plans described below. Benefits are established by state statute and generally provide retirement, death, long-term disability, survivor, and health insurance premium benefits.

The *Arizona State Retirement System* (ASRS) administers a cost-sharing multiple-employer defined benefit pension plan that covers general employees of the Town. The ASRS is governed by the Arizona State Retirement System Board according to the provisions of A.R.S. Title 38, Chapter 5, Article 2.

**TOWN OF PATAGONIA, ARIZONA**  
**Notes to Financial Statements**  
**June 30, 2010**

***NOTE 7 – RETIREMENT PLANS – Continued***

The *Public Safety Personnel Retirement System* (PSPRS) is an agent multiple-employer defined benefit pension plan that covers public safety personnel who are regularly assigned hazardous duty as employees of the State of Arizona or one of its political subdivisions. The PSPRS, acting as a common investment and administrative agent, is governed by a five-member board, known as The Fund Manager, and the participating local boards according to the provisions of A.R.S. Title 38, Chapter 5, Article 4.

Each plan issues a publicly available financial report that includes its financial statements and required supplementary information. A report may be obtained by writing or calling the applicable plan.

ASRS  
3300 N. Central Ave.  
Phoenix, AZ 85012-0250  
(602) 240-2000

PSPRS  
3010 E. Camelback Rd., Ste. 200  
Phoenix, AZ 85016  
(602) 255-5575

**Funding Policy** – The Arizona State Legislature establishes and may amend active plan members' and the Town's contribution rates.

*Cost-sharing plans* – For the year ended June 30, 2010, active ASRS members and the Town were each required by statute to contribute at the actuarially determined rate of 9.40 percent (9.00 percent retirement and 0.40 percent long-term disability) of the members' annual covered payroll. The Town's contributions to ASRS for the years ended June 30, 2010, 2009, and 2008, were \$24,450, \$25,964, and \$22,470, respectively, which were equal to the required contributions for the year.

*Agent plans* – For the year ended June 30, 2010, no active PSPRS members chose to participate in the plan.

**TOWN OF PATAGONIA, ARIZONA**  
**Notes to Financial Statements**  
**June 30, 2010**

**NOTE 7 – RETIREMENT PLANS – Continued**

Annual Pension Cost – The Town’s pension cost for the agent plan for the year ended June 30, 2010, and related information follows:

	PSPRS
Contribution rates:	
Town	N/A
Plan members	N/A
Annual pension cost	\$0
Contributions made	\$0
Actuarial valuation date	06/30/10
Actuarial cost method	Projected Unit Credit
Actuarial assumptions:	
Investment rate of return	8.50%
Projected salary increases	5.50% - 8.50%
Includes inflation at	5.50%
Cost-of-living adjustments	None
Amortization method	Level percent-of-pay closed
Remaining amortization period	26 years for under funded actuarial accrued liability, 20 years for overfunded
Asset valuation method	7-year smoothed market

Trend Information – Annual pension cost information for the current and 2 preceding years follows for each of the agent plans.

Plan	Year Ended June 30	Annual Pension Cost (APC)	Percentage of APC Contributed	Net Pension Obligation
PSPRS	2010	\$ -	100 %	\$ -
	2009	-	100	-
	2008	-	100	-

**TOWN OF PATAGONIA, ARIZONA**  
**Notes to Financial Statements**  
**June 30, 2010**

***NOTE 8 – CLOSURE AND POSTCLOSURE COSTS***

State and federal laws and regulations require the Town to place a final cover on its landfill when it stops accepting waste and to perform certain maintenance and monitoring functions at the site for 30 years after closure. Although closure and postclosure care costs will not be paid until near or after the date that the landfill stops accepting waste, the Town reports a portion of these closure and postclosure care costs as an operating expense in each period based on landfill capacity used as of each balance sheet date. The \$101,705 reported as landfill closure and post closure care liability at June 30, 2010, represents the cumulative amount reported to date based on the use of 25 percent of the estimated capacity of the landfill. The Town will recognize the remaining estimated cost of closure and postclosure care of \$417,178 as the remaining estimated capacity is filled. These amounts are based on what it would cost to perform all closure and postclosure care in fiscal year 2009-2010. The Town expects to close the landfill in the year 2050, and the actual cost may be higher due to inflation, changes in technology, and changes in regulations.

The Town of Patagonia is required to file certain information relating to the landfill closure, postclosure, and monitoring with the State of Arizona Department of Environmental Quality (ADEQ). The required information was filed with the State subsequent to June 30, 2010.

***NOTE 9 – CONTINGENT LIABILITIES***

Amounts received or receivable from grant agencies are subject to audit and adjustment by grantor agencies. Any disallowed claims, including amounts collected, may constitute a liability of the applicable funds. The amount, if any, of expenditures which may be disallowed by the grantor cannot be determined at this time.

**TOWN OF PATAGONIA, ARIZONA**  
**Required Supplementary Information**  
**Budgetary Comparison Schedule**  
**General Fund**  
**Year Ended June 30, 2010**

	Budgeted Amounts		Actual Amounts	Variance with Final Budget
	Original	Final		
<b>Revenues</b>				
Taxes	\$ 168,000	\$ 168,000	\$ 163,963	\$ (4,037)
Intergovernmental	324,390	324,390	319,109	(5,281)
Franchise fees	22,000	22,000	28,067	6,067
Fines and forfeitures	51,120	51,120	28,482	(22,638)
Licenses and permits	21,000	21,000	10,179	(10,821)
Charges for services	26,980	26,980	28,499	1,519
Investment income	10,500	10,500	8,260	(2,240)
Other revenue	30,680	30,680	7,959	(22,721)
<b>Total revenues</b>	<u>654,670</u>	<u>654,670</u>	<u>594,518</u>	<u>(60,152)</u>
<b>Expenditures</b>				
Current				
General government	270,742	270,742	212,660	58,082
Public safety	320,909	320,909	329,710	(8,801)
Culture and recreation	122,628	122,628	103,838	18,790
Capital outlay	297,259	297,259	2,704	294,555
<b>Total expenditures</b>	<u>1,011,538</u>	<u>1,011,538</u>	<u>648,912</u>	<u>362,626</u>
Net change in fund balances	(356,868)	(356,868)	(54,394)	302,474
Fund balance, July 1, 2009	<u>1,096,605</u>	<u>1,096,605</u>	<u>1,096,605</u>	<u>-</u>
Fund balance, June 30, 2010	<u>\$ 739,737</u>	<u>\$ 739,737</u>	<u>\$ 1,042,211</u>	<u>\$ 302,474</u>

*See accompanying notes to budgetary comparison schedule.*

**TOWN OF PATAGONIA, ARIZONA**  
**Required Supplementary Information**  
**Budgetary Comparison Schedule**  
**HURF/LTAF Fund**  
**Year Ended June 30, 2010**

	Budgeted Amounts		Actual Amounts	Variance with Final Budget
	Original	Final		
<b>Revenues</b>				
Intergovernmental	\$ 89,120	\$ 89,120	\$ 88,926	\$ (194)
Investment income	1,400	1,400	5,064	3,664
<b>Total revenues</b>	<u>90,520</u>	<u>90,520</u>	<u>93,990</u>	<u>3,470</u>
<b>Expenditures</b>				
Current				
Highways and streets	142,566	142,566	95,467	47,099
<b>Total expenditures</b>	<u>142,566</u>	<u>142,566</u>	<u>95,467</u>	<u>47,099</u>
Net change in fund balances	(52,046)	(52,046)	(1,477)	50,569
Fund balance, July 1, 2009	<u>145,937</u>	<u>145,937</u>	<u>145,937</u>	<u>-</u>
Fund balance, June 30, 2010	<u>\$ 93,891</u>	<u>\$ 93,891</u>	<u>\$ 144,460</u>	<u>\$ 50,569</u>

*See accompanying notes to budgetary comparison schedule.*

**TOWN OF PATAGONIA, ARIZONA**  
**Required Supplementary Information**  
**Budgetary Comparison Schedule**  
**Grants Fund**  
**Year Ended June 30, 2010**

	Budgeted Amounts		Actual Amounts	Variance with Final Budget
	Original	Final		
<b>Revenues</b>				
Intergovernmental	\$ 1,503,500	\$ 1,503,500	\$ 35,486	\$ (1,468,014)
Other revenue	-	-	1,900	1,900
<b>Total revenues</b>	<u>1,503,500</u>	<u>1,503,500</u>	<u>37,386</u>	<u>(1,466,114)</u>
<b>Expenditures</b>				
Current				
General government	13,900	13,900	13,900	-
Culture and recreation	30,470	30,470	30,470	-
Capital outlay	1,459,130	1,459,130	-	1,459,130
<b>Total expenditures</b>	<u>1,503,500</u>	<u>1,503,500</u>	<u>44,370</u>	<u>1,459,130</u>
Net change in fund balances	-	-	(6,984)	(6,984)
Fund balance, July 1, 2009	<u>18,242</u>	<u>18,242</u>	<u>18,242</u>	<u>-</u>
Fund balance, June 30, 2010	<u>\$ 18,242</u>	<u>\$ 18,242</u>	<u>\$ 11,258</u>	<u>\$ (6,984)</u>

*See accompanying notes to budgetary comparison schedule.*

**TOWN OF PATAGONIA, ARIZONA**  
**Required Supplementary Information**  
**Notes to Budgetary Comparison Schedules**  
**June 30, 2010**

***NOTE 1 – BUDGETING AND BUDGETARY CONTROL***

Arizona Revised Statutes (A.R.S.) require the Town to prepare and adopt a balanced budget annually for each governmental fund. The Town Council must approve such operating budgets on or before the third Monday in July to allow sufficient time for the legal announcements and hearings required for the adoption of the property tax levy on the third Monday in August. A.R.S. prohibits expenditures or liabilities in excess of the amounts budgeted.

Expenditures may not legally exceed appropriations at the department level. In certain instances, transfers of appropriations between departments or from the contingency account to a department may be made upon the Town Councils' approval.

**TOWN OF PATAGONIA, ARIZONA**  
**Required Supplementary Information**  
**Schedule of Agent Retirement Plan Funding Progress**  
**June 30, 2010**

Public Safety Personnel Retirement System

Actuarial Valuation Date	Actuarial Value of Plan Assets (a)	Actuarial Accrued Liability (b)	Funding (Liability) Excess (a-b)	Funded Ratio (a/b)	Annual Covered Payroll (c)	Unfunded Liability as Percentage of Covered Payroll ((a-b)/c)
2010	\$ 462,390	\$ 393,387	\$ 69,003	117.5 %	\$ 28,084	- %
2009	475,299	402,387	72,912	118.1	34,849	-
2008	355,906	312,109	43,797	114.0	-	-



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**INDEPENDENT AUDITORS' 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***

To the Town Council  
Town of Patagonia, Arizona

We have audited the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the Town of Patagonia, Arizona, as of and for the year ended June 30, 2010, which collectively comprise the Town of Patagonia, Arizona's basic financial statements and have issued our report thereon dated January 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 Town of Patagonia, Arizona's internal control over financial reporting 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 Town of Patagonia, Arizona's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Town of Patagonia, Arizona's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses and therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. However, as described in the accompanying schedule of findings and responses, we identified certain deficiencies in internal control over financial reporting that we consider to be material weaknesses and other deficiencies that we consider to be significant deficiencies.

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. We consider the deficiencies listed as reference numbers **07-02**, **07-03**, **10-02**, and **10-03** described in the accompanying schedule of findings and responses to be material weaknesses.

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. We consider the deficiencies listed as reference numbers **07-04** and **10-01** described in the accompanying schedule of findings and responses to be significant deficiencies.

### **Compliance and Other Matters**

As part of obtaining reasonable assurance about whether the Town of Patagonia, Arizona'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 or other matters that are required to be reported under *Government Auditing Standards*.

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

*Colby + Powell PLLC*

January 25, 2011

**TOWN OF PATAGONIA, ARIZONA**  
**Schedule of Findings and Responses**  
**June 30, 2010**

**Financial Statement Findings**

Audit findings and responses are as follows:

**Item: 07-02**

*Subject:* Internal controls over utility accounting.

*Criteria/Specific Requirements:* The billing adjustment function should be segregated from the cash receipting function. If it cannot be segregated, someone who does not receive cash should review billing adjustments on a regular basis.

*Condition:* Billing and payment adjustments are done by the same employee who collects cash for utility services.

*Effect:* A material misstatement could occur due to error or fraud and not be discovered by management in a reasonable amount of time.

*Recommendation:* Management should designate a responsible person to review utility billing adjustments on a monthly basis.

*Response:* Management agrees with this finding and will assign a separate employee apart from the cash receipting function and the billing function to review billing adjustments.

**Item: 07-03**

*Subject:* Computer access controls.

*Criteria/Specific Requirements:* Management should limit the access that employees have to the accounting software to only those areas that they are to required access for their respective positions.

*Condition:* Currently, every employee who uses Caselle can access every module of the software.

*Effect:* A misstatement could occur due to error or fraud and not be discovered by management in a reasonable amount of time.

*Recommendation:* Management should limit the access that employees have to the accounting software to only those areas that they are required to access for their respective positions by implemented Caselle's access controls.

**TOWN OF PATAGONIA, ARIZONA**  
**Schedule of Findings and Responses**  
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*Response:* Because the respective employee positions are not limited to any one section of software and because there are only five computers accessing the software it would be detrimental to efficiency and productivity to build restraints into the software and hardware applications not to mention the additional costs involved.

***Item: 07-04***

*Subject:* Employee time punch cards.

*Criteria/Specific Requirements:* Those in management who oversee and approve timecards should be able to verify the amount of time showing on the timecards as time worked.

*Condition:* Currently, there is no consistent method in place to appropriately approve the amount of time that employees record on their timesheets.

*Effect:* A misstatement could occur due to error or fraud and not be discovered by management in a reasonable amount of time.

*Recommendation:* The Town should implement a system for management to be able to review and appropriately approve time recorded on employee timesheets. Such a system could include the use of a time punch and timecards.

*Response:* The Town will implement a system for management to be able to review and appropriately approve time recorded on employee time sheets. This system will include the use of time punch and time cards. This system will be implemented initially in the Marshall's office prior to the next audit and in other offices of the Town at a later date.

***Item: 10-01***

*Subject:* Review of bank reconciliations.

*Criteria/Specific Requirements:* Monthly bank reconciliations should be reviewed regularly to ensure the correctness of the reconciliation report.

*Condition:* Currently, there is no review being performed of the bank reconciliation.

*Effect:* A misstatement could occur due to error or fraud and not be discovered by management in a reasonable amount of time.

*Recommendation:* The bank reconciliation should be reviewed monthly by someone who is independent of the bank reconciliation function. That person should initial and date the reconciliation reviewed to show evidence of the review.

**TOWN OF PATAGONIA, ARIZONA**  
**Schedule of Findings and Responses**  
**June 30, 2010**

*Response:* The Town will implement procedures for someone who is independent of the bank reconciliation function to review the monthly bank reconciliation reports.

***Item: 10-02***

*Subject:* Review policies and procedures for oversight of financial statement presentation and disclosure.

*Criteria/Specific Requirements:* Management must review, approve, and accept responsibility for its financial statements accompanying the audit.

*Condition:* Not unlike other governments of similar size and structure, the Town's absence of internal control over financial statement presentation does not provide procedures for the prevention or detection of possible material misstatement of the financial statements.

*Effect:* A material misstatement could occur and be undiscovered by management.

*Recommendation:* Management should reconcile general ledger amounts to draft financial statements, review all supporting documentation for audit adjusting journal entries, and review the adequacy of financial statement disclosures by utilizing, at a minimum, a disclosure checklist. If management is unable to do this, management could contract this portion to a responsible qualified individual.

*Response:* Management agrees with this finding and will implement procedures to properly accept responsibility for financial statements.

***Item: 10-03***

*Subject:* Landfill closure and post-closure costs.

*Criteria/Specific Requirements:* Management must estimate closure and post-closure costs of the landfill and recognize those costs as the landfill is filled.

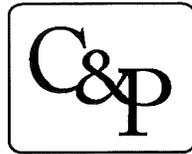
*Condition:* The Town has had significant improvements made to the existing landfill and has not had an engineering study done to determine the changes to the capacity of the landfill and the changes to estimated closure and post-closure costs.

*Effect:* A material misstatement could occur and be undiscovered by management.

*Recommendation:* The Town should have a qualified professional determine the landfill's new capacity, the amount used to date, and estimate closure and post-closure costs.

**TOWN OF PATAGONIA, ARIZONA**  
**Schedule of Findings and Responses**  
**June 30, 2010**

*Response:* Management agrees with this finding and will look into getting a study done in the near future.



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**INDEPENDENT AUDITORS' REPORT ON  
COMPLIANCE WITH REQUIREMENTS  
APPLICABLE TO THE USES OF HIGHWAY USER  
REVENUE FUND MONIES IN ACCORDANCE  
WITH ARS TITLE 28, CHAPTER 18, ARTICLE 2**

To the Town Council  
Town of Patagonia, Arizona

We have audited, in accordance with auditing standards generally accepted in the United States of America and *Government Auditing Standards*, issued by the Comptroller General of the United States, the financial statements of the governmental activities, business-type activities, each major fund, and aggregate remaining fund information of the Town of Patagonia as of and for the year ended June 30, 2010, which collectively comprise the Town's basic financial statements, and have issued our report thereon dated January 25, 2011.

In connection with our audit, nothing came to our attention that caused us to believe that the Town failed to use highway user revenue fund monies received by the Town pursuant to Arizona Revised Statutes Title 28, Chapter 18, Article 2 and any other dedicated state transportation revenues received by the Town solely for the authorized transportation purposes. However, our audit was not directed primarily toward obtaining knowledge of such noncompliance.

This report is intended solely for the information and use of management and the members of the Arizona State Legislature and is not intended to be and should not be used by anyone other than these specified parties. However, this report is a matter of public record, and its distribution is not limited.

*Colby + Powell PLC*

January 25, 2011