

UNITED UTILITIES GROUP
ANNUAL FINANCIAL REPORT
For the Year Ended December 31, 2012
and
INDEPENDENT AUDITOR'S REPORT

UNITED UTILITIES GROUP

ANNUAL FINANCIAL REPORT

December 31, 2012

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INTRODUCTORY SECTION

UNITED UTILITIES GROUP

MEMBERS AND DIRECTORS

December 31, 2012

MEMBER UTILITY DISTRICTS

Public Utility District of Jefferson and Cocke Counties, Tennessee
Powell-Clinch Utility District of Anderson and Campbell Counties, Tennessee
Elk River Public Utility District
The Sevier County Utility District

BOARD OF DIRECTORS

Matt Ballard	Chairman / President
Tommy C. Bible	Secretary / Treasurer
Mike Gundersen	Member
Rob Neil	Member

FINANCIAL SECTION

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MEMBERS
 AMERICAN INSTITUTE OF
 CERTIFIED PUBLIC ACCOUNTANTS

Independent Auditor's Report

To the Board of Directors
 United Utilities Group
 Newport, Tennessee

We have audited the accompanying statement of net position of United Utilities Group (a nonprofit association) as of December 31, 2012, and the related statements of revenue, expenses and changes in net position and cash flows for the year then ended.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes 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 Responsibility

Our responsibility is to express an opinion 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 from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements 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 entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the net position of United Utilities Group as of December 31, 2012, and the respective changes in net position and cash flow for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters*Required Supplementary Information*

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and budgetary comparison information on pages 4 - 6 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.

Other Information

Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise United Utilities Group's basic financial statements. The introductory section is presented for purposes of additional analysis and is not a required part of the basic financial statements.

The introductory section has not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we do not express an opinion or provide any assurance on it.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated June 26, 2013 on our consideration of United Utilities Group'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* in considering United Utilities Group's internal control over financial reporting and compliance.



MANAGEMENT'S DISCUSSION AND ANALYSIS

This section of the United Utilities Group (the Association) annual financial report presents analysis of the Association's financial performance during the year ended December 31, 2012. Please read it in conjunction with the financial statements, which follow this section.

FINANCIAL HIGHLIGHTS

- The Association's total assets increased by \$29,622 to \$133,638 at year-end and were more than liabilities by \$1,099 (i.e., Net Position). Of the total assets, \$41,098 was unrestricted cash, while fees and member receivables were \$92,540, an increase of \$46,072 over the previous year.
- For the year 2012, the Association charged \$186,134 for pipeline imbalance fees with \$306,330 charged for the year 2011. The decrease in fees was due to the Association having a smaller monthly imbalance on the pipeline each month. Member fees were \$711,705 for the year ended December 31, 2012 and \$636,842 for 2011.
- During the year, the Association's operating revenue decreased to \$897,839 (4.81%), while operating expenses decreased to \$892,357 (9.79%). The decrease in revenue was primarily the result of the decrease in revenue from the monthly pipeline imbalance offset by an increase in member assessments. The decrease in expenses was primarily due to decreases in imbalance fees and decreases in consulting expenses. Members are only billed or paid for their own individual imbalances each month, which fluctuates based on the actual imbalance for each member.
- Increase in Net Position was \$5,607 for the year 2012 compared to a decrease of \$(45,641) for the year 2011.

OVERVIEW OF THE FINANCIAL STATEMENTS

This annual report includes the management's discussion and analysis, the independent auditor's report and the basic financial statements of the Association. The financial statements also include notes that explain in more detail some of the information in the financial statements.

REQUIRED FINANCIAL STATEMENTS

The financial statements report information about the Association using accounting methods similar to those used by private sector companies. These statements offer short and long-term information about its activities.

The statement of net position includes all of the Association's position and liabilities and provides information about the nature and amounts of investments in resources (assets) and the obligations to the Association's creditors (liabilities). It also provides the basis for computing rate of return, evaluating the capital structure of the Association and assessing the liquidity and financial flexibility of the Association.

All of the current year's revenue and expenses are accounted for in the statement of revenue, expenses and changes in net position. This statement measures the success of the Association's operations over the past year and can be used to determine whether the Association has successfully recovered all its costs through its fees and other charges.

The other required financial statement is the statement of cash flows. The primary purpose of this statement is to provide information about the Association's cash receipts and cash payments during the reporting period. This statement reports cash receipts, cash payments and net changes in cash resulting from operations, investing and financing activities, and provides answers to such questions as "where did the cash come from, what was the cash used for and what was the change in cash balance during the reporting period?."

**MANAGEMENT'S DISCUSSION AND ANALYSIS
(CONTINUED)**

FINANCIAL ANALYSIS OF THE ASSOCIATION AS A WHOLE

The statement of net position and the statement of revenue, expenses and changes in net position report information about the Association's activities, net position of the Association and changes in them.

While the statements of net position (Table I) show the change in financial position, the statements of revenue, expenses and changes in net position (Table II) provide the answers as to the nature and source of these changes.

**TABLE I
CONDENSED STATEMENTS OF NET POSITION**

	December 31, 2012	December 31, 2011	Dollar Change	Total Percent Change
Current assets	<u>\$ 133,638</u>	<u>\$ 104,016</u>	<u>\$ 29,622</u>	28.48%
Current liabilities	\$ 132,539	\$ 108,524	\$ 24,015	22.13%
Net position	<u>1,099</u>	<u>(4,508)</u>	<u>5,607</u>	124.38%
	<u>\$ 133,638</u>	<u>\$ 104,016</u>	<u>\$ 29,622</u>	28.48%

**TABLE II
CONDENSED STATEMENTS OF REVENUE, EXPENSES AND CHANGES IN NET POSITION**

	December 31, 2012	December 31, 2011	Dollar Change	Total Percent Change
Operating revenue	\$ 897,839	\$ 943,172	\$ (45,333)	-4.81%
Operating expenses	892,357	989,182	(96,825)	-9.79%
Other revenue	<u>125</u>	<u>369</u>	<u>(244)</u>	-66.12%
Change in net position	5,607	(45,641)	51,248	112.29%
Beginning net position (deficit)	<u>(4,508)</u>	<u>41,133</u>	<u>(45,641)</u>	-110.96%
Ending net position (deficit)	<u>\$ 1,099</u>	<u>\$ (4,508)</u>	<u>\$ 5,607</u>	124.38%

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

As shown in Table I, current assets increased by 28.48% and current liabilities increased by 22.13%. The increase in current assets and increase in current liabilities was primarily due to changes in both fees receivable and fees payable.

Table II shows operating revenue decreased by \$(45,333) which was primarily due to individual members having a larger monthly imbalance on the pipeline each month offset by a decrease in member assessments. Operating expenses also decreased by \$(96,825) as a result of individual members having a larger imbalance on the pipeline each month and small increases in consulting and professional fees. Net loss from operations was the source of the increase in net position of \$5,607.

CONTACTING THE ASSOCIATION'S FINANCIAL MANAGER

This annual report is designed to provide our customers and creditors with a general overview of the Association's finances and to demonstrate the Association's accountability for the money it receives. If you have any questions about this report or need additional financial information, contact United Utilities Group, 122 Highway 25E, Newport, TN 37821.

UNITED UTILITIES GROUP
STATEMENT OF NET POSITION

December 31, 2012

ASSETS

Current assets:

Cash in bank	\$ 41,098
Member accounts receivable	<u>92,540</u>

Total current assets	<u>133,638</u>
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LIABILITIES

Current liabilities:

Member accounts payable	67,540
Accounts payable	<u>64,999</u>

Total current liabilities	<u>132,539</u>
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NET POSITION

Unrestricted	<u>1,099</u>
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Total net position	<u><u>\$ 1,099</u></u>
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The accompanying notes are an integral
part of these financial statements.

UNITED UTILITIES GROUP

STATEMENT OF REVENUE, EXPENSES AND CHANGES IN NET POSITION

For the Year Ended December 31, 2012

Operating revenue:	
Pipeline imbalance fees	\$ 186,134
Member assessments	<u>711,705</u>
Total operating revenue	<u>897,839</u>
Operating expenses:	
Pipeline imbalance fees	181,913
Consulting	652,693
Professional services	56,476
Miscellaneous	585
Meeting expense	<u>690</u>
Total operating expenses	<u>892,357</u>
Operating income	<u>5,482</u>
Other non-operating revenue (expenses):	
Other income	4,000
Other expense	(4,000)
Interest income	<u>125</u>
Total other non-operating revenue (expenses)	<u>125</u>
Change in net position	5,607
Net position (deficit), beginning	<u>(4,508)</u>
Net position, ending	<u>\$ 1,099</u>

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

UNITED UTILITIES GROUP

STATEMENT OF CASH FLOWS

For the Year Ended December 31, 2012

Cash flows from operating activities:	
Cash received from members	\$ 851,767
Cash paid to suppliers	(682,208)
Cash paid to members	<u>(186,134)</u>
Net cash used by operating activities	<u>(16,575)</u>
Cash flows from non-capital financing activities:	
Cash received from other income non-operating income	4,000
Cash paid for other non-operating expenses	<u>(4,000)</u>
Net cash provided (used) by non-capital financing activities	<u>-</u>
Cash flows from investing activities:	
Interest received	<u>125</u>
Net cash provided by investing activities	<u>125</u>
Net decrease in cash and cash equivalents	(16,450)
Cash and cash equivalents, beginning of year	<u>57,548</u>
Cash and cash equivalents, end of year	<u><u>\$ 41,098</u></u>
<u>Reconciliation of operating income to net cash used by operating activities:</u>	
Operating income	\$ 5,482
Adjustments to reconcile operating income to net cash used by operating activities:	
Increase in member accounts receivable	(46,072)
Increase in member accounts payable	20,852
Increase in accounts payable	<u>3,163</u>
Net cash used by operating activities	<u><u>\$ (16,575)</u></u>

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

UNITED UTILITIES GROUP

NOTES TO FINANCIAL STATEMENTS

December 31, 2012

1. Summary of Significant Accounting Policies

The significant accounting policies of United Utilities Group (the Association) are summarized below to assist the reader in reviewing the financial statements and other data contained in this report.

Nature of Business

The Association is a voluntary non-profit association operating as a separate legal natural gas authority created by an interlocal cooperation agreement of certain natural gas utility districts in East Tennessee. Membership is divided into two classes, full members and associate members. Full members are composed of the four (4) founding utility districts that retain voting rights. Associate memberships are available on such terms and conditions as may be prescribed and set forth by a majority of the full members. The primary purpose of the Association is to purchase, move and resell gas at the lowest possible price for the benefit of customers of the member districts.

Basis of Accounting and Presentation

The Association uses the accrual method of accounting. Operating revenues are recognized when they are earned. Operating expenses are recognized when they are incurred. Operating revenues consist of fees and assessments collected from members. Non-operating revenue consists of investment income and gain or loss on disposal of assets. Investment income is interest earned on cash deposits or investments. The Association's policy for use of restricted funds is to spend all restricted funds first and designate unrestricted funds for restricted purposes only when restricted funds are fully depleted.

The accounting and financial reporting treatment applied to the Association is determined by its measurement focus. The transactions of the Association are accounted for on a flow of economic resources measurement focus. With this measurement focus, all assets and all liabilities associated with the operations are included on the statement of net position. Net position (i.e., total assets net of total liabilities) is segregated as follows:

- Invested in capital assets, net of related debt - This component of net position consists of capital assets, including restricted capital assets, net of accumulated depreciation and reduced by the outstanding balances of any bonds, mortgages, notes or other borrowings that are attributable to the acquisition, construction or improvement of those assets. If there are significant unspent related debt proceeds at year-end, the portion of the debt attributable to the unspent proceeds are not included in the calculation of invested in capital assets, net of related debt. Rather, that portion of the debt is included in the same net position component as the unspent proceeds.
- Restricted - This component of net position consists of constraints placed on net position use through external constraints imposed by creditors (such as through debt covenants), grantors, contributors or laws or regulations of other governments or constraints imposed by law through constitutional provisions or enabling legislation.

UNITED UTILITIES GROUP

NOTES TO FINANCIAL STATEMENTS
(Continued)1. Summary of Significant Accounting Policies (Continued)Basis of Accounting and Presentation (Continued)

- Unrestricted - This component of net position consists of net position that does not meet the definition of "restricted" or "invested in capital assets, net of related debt."

Recently Issued and Adopted Accounting Pronouncements

In December 2010, the GASB issued Statement 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*. GASB 62 incorporates into the GASB's authoritative literature certain accounting and financial reporting guidance that is included in the following pronouncements issued on or before November 30, 1989, which does not conflict with or contradict GASB pronouncements: Financial Accounting Standards Board (FASB) Statements and Interpretations, Accounting Principles Board Opinions and Accounting Research Bulletins of the American Institute of Certified Public Accountants' (AICPA) Committee on Accounting Procedure. This statement is effective for periods beginning after December 15, 2011.

In June 2011, the GASB issued Statement 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*. GASB 63 provides guidance for reporting deferred outflows of resources, deferred inflows of resources, and net position in a statement of financial position and related disclosures. The statement of net assets is renamed the statement of net position and includes four components: assets, deferred outflows of resources, liabilities and deferred inflows of resources. The provisions of this statement are effective for financial statements for periods beginning after December 15, 2011.

The adoption of these accounting pronouncements did not have any significant effect on the Association's financial statements.

Cash and Cash Equivalents

The Association considers all highly liquid investments available for current use with an initial maturity of three (3) months or less to be cash equivalents.

Accounts Receivable

The Association considers member accounts receivable to be fully collectible; accordingly, no allowance for uncollectible accounts has been established.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

UNITED UTILITIES GROUP

NOTES TO FINANCIAL STATEMENTS
(Continued)2. Deposits and Investments

Tennessee Code Annotated (TCA) Section 7-82-108 authorizes the Association to invest in direct obligations of or obligations unconditionally guaranteed by the U.S. Government, and certain U.S. federal agencies or instrumentalities, certificates of deposit and repurchase agreements.

Tennessee State Law requires utility districts to secure deposits by having financial institutions pledge governmental securities as collateral for deposits not insured by the Federal Deposit Insurance Corporation (FDIC).

United Utilities Group had no deposits in excess of FDIC insurance for 2012.

Information related to the carrying value and bank balances of deposits at December 31, 2012 is as follows:

	<u>Carrying Value</u>	<u>Bank Balance</u>
Depository Account Insured:		
Deposits in financial institutions	<u>\$41,098</u>	<u>\$98,203</u>

Interest Rate Risk

The Association's primary investment objectives are to place investments in a manner to ensure the preservation of capital, remain sufficiently liquid to meet all operating requirements and to maximize the yield of return. The Association minimizes its exposure to interest rate risk by adhering to Tennessee State Law requirements for the investment of public funds. This includes types of investments, as described above, and investment maturity. The maximum is four (4) years from the date of investment. The Association also limits its exposure by holding investments to maturity unless cash flow requirements dictate otherwise.

Credit Risk

The Association's general investment policy is to apply the prudent-person rule: Investments are made with judgment and care, under circumstances then prevailing, which persons of prudence, discretion and intelligence exercise in the management of their own affairs, not for speculation, but for investment, considering the probable income to be derived, as well as the probable safety of their capital.

3. Commitments

Effective October 1, 2010, and revised April 1, 2011, the Association entered into an agreement with CH₄Concepts, a Partnership (Agent) whereby the Agent is responsible for the purchase and transportation of gas to the systems and facilities of the members of the Association. The agreement provides an initial annual fee of \$.029 per dekatherm times an estimated total aggregate annual city gate metered volume of 8,500,000 dekatherms. All additional volumes will be charged at a rate of 60% of the base rate. The estimated annual fee is payable in monthly payments of \$20,542. The term of this agreement is five years and automatically renews for an additional five years unless terminated by either party under the terms of the agreement. As of December 31, 2012, no termination notice has been made by either party. The agreement also provides for revenue sharing at a rate of 10% share of revenues generated from release capacity or bundled delivered sales.

UNITED UTILITIES GROUP

NOTES TO FINANCIAL STATEMENTS
(Continued)3. Commitments (Continued)

Effective April 1, 2008, and revised April 1, 2011, the Association entered into an agreement with Revelation Energy Resources, LLC (Agent) whereby the Agent is responsible for all gas supplied to the Association for use at its member systems. The agreement shall be for a primary term of five years and shall continue for an additional five year period unless terminated by either party by at least one hundred and eighty (180) days written notice prior to the commencement of the ensuing yearly period.

The Agent agrees to manage all aspects of the gas supply volume requirements, help market any unused transportation capacity on pipelines and make bundled delivered gas sales when favorable market opportunities are available, and any customary accounting and reporting in connection with all of the foregoing. The agreement provides an initial annual fee of \$180,000 payable on a monthly basis; the fee shall be adjusted each contract year beginning April 1, 2012 by percentage increase in the U.S. Consumer Price Index; for the city gate volumes in excess of 8,500,000 dekatherms. All additional volumes will be charged at a rate of 60% of the base rate. The agreement also provides for revenue sharing at a rate of 10% share of revenues generated from release capacity or bundled delivered sales.

4. Related Parties

The Association charges member districts membership fees to facilitate operations. Assessment was \$711,705 for the year ended December 31, 2012.

During 2012, all revenue was received from members as discussed above.

5. Risk Management

The Association is exposed to various risks of loss related to torts; errors and omissions; and natural disasters. The Association does not consider such risk significant to warrant commercial insurance. Each member of the Association is individually insured against such losses.

6. Economic Dependency

The Association received membership dues from member utility districts listed in the introductory section of the Association's annual report. Loss of member dues would have a significant impact on the Association's ability to continue as a going concern.

7. Fair Value of Instruments

The Association's financial instruments are cash, accounts receivable and accounts payable. The recorded values of cash, accounts receivable and accounts payable approximate their fair values based on their short-term nature.

8. Subsequent Events

The Association has evaluated subsequent events through June 26, 2013. No disclosures are necessary.

INTERNAL CONTROL AND COMPLIANCE SECTION

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MEMBERS
AMERICAN INSTITUTE OF
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**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***

To the Board of Directors
United Utilities Group
Newport, Tennessee

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 financial statements of United Utilities Group (a nonprofit association), as of and for the year ended December 31, 2012, and the related notes to the financial statements, which collectively comprise United Utilities Group's basic financial statements, and have issued our report thereon dated June 26, 2013.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered United Utilities Group's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of United Utilities Group's internal control. Accordingly, we do not express an opinion on the effectiveness of United Utilities Group'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. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether United Utilities Group'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 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*.

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 entity'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 entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.



CERTIFIED PUBLIC ACCOUNTANTS

Knoxville, Tennessee
June 26, 2013