

September 20, 2010

Kami Kehoe, President
Cyndi Lewis-Wolfram, Secretary
Barbara Kemper, Treasurer
Mike Cardwell, Commissioner
Patricia Holloway, Commissioner

Clackamas River Water
16770 SE 82nd Dr
Clackamas OR 97015

We are engaged to audit the financial statements of Clackamas River Water as of June 30, 2010 and for the year then ended. Professional standards require that we provide you with the following information related to our audit. **Please read this entire letter carefully. It requires certain actions on your part and ours, well beyond the original contemplated scope of our services.**

Our Responsibility under U.S. Generally Accepted Auditing Standards

As stated in our engagement letter dated February 12, 2010, our responsibility, as described by professional standards, is to express certain opinions about whether the financial statements prepared by management with your oversight are fairly presented, in all material respects, in conformity with accounting principles generally accepted in the United States of America. Our audit of the financial statements does not relieve you or management of your responsibilities.

Our responsibility is to plan and perform the audit to obtain reasonable, but not absolute, assurance that the financial statements are free of material misstatement whether caused by error or fraud. As part of our audit, we must consider the internal control of Clackamas River Water. Such considerations are solely for the purpose of determining our audit procedures and not to provide any assurance concerning such internal control. Accordingly, a material misstatement may remain undetected. An audit is not designed to detect errors, fraud or illegal acts that are immaterial to the financial statements. We advised you of these audit limitations in our February 12, 2010 Engagement Letter.

Accounting principles generally accepted in the United States of America provide for certain required supplementary information ("RSI") to accompany Clackamas River Water's basic financial statements. Therefore, we must also apply certain limited procedures to Clackamas River Water's RSI. These limited procedures consist principally of inquiries of management regarding the methods of measurement and presentation, which management is responsible for affirming to us in its representation letter. Unless we encounter problems with the presentation of the RSI or with procedures relating to it, we will simply disclaim an opinion on it. The following RSI is required by generally accepted accounting principles and will be subjected to certain limited procedures, but will not be audited:

a. Management's Discussion and Analysis

Supplementary information other than RSI also accompanies Clackamas River Water's basic financial statements. We must subject the following supplementary information to the auditing procedures applied in our audit of the basic financial statements and will provide an opinion on the information in relation to the basic financial statements:

- a. Description of Budgetary Funds
- b. Combining Statement of Net Assets – All Funds on Budgetary Basis (including a reconciliation of net assets on a budgetary basis to net assets on GAAP basis)
- c. Schedules of Revenues and Expenditures – Budget and Actual (by individual fund)

As part of obtaining reasonable assurance about whether Clackamas River Water's basic financial statements are free of material misstatement, we must perform tests of 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 is not an objective of our audit and we will not express such an opinion.

Our Additional Responsibilities under Government Auditing Standards and OMB Circular A-133 – Audits of States, Local Governments, and Non-Profit Organizations

We must also consider internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133. To our knowledge, the only program under which Clackamas River Water has received federal funds is the U.S. Department of Homeland Security, FEMA Pre-Disaster Mitigation federal award (received as a sub-recipient) under the Clackamas County, Oregon Intergovernmental Cooperative Agreement Pre-Disaster Mitigation Program Contract FY05/PDM-C ID# pj-10-OR-2005-001.

Also in accordance with OMB Circular A-133, we must examine, on a test basis, evidence about Clackamas River Water's compliance with the types of compliance requirements described in the "U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement" applicable to each of its major federal programs for the purpose of expressing an opinion on Clackamas River Water's compliance with those requirements. While our audit will provide a reasonable basis for our opinion, it will not provide a legal determination as to Clackamas River Water's compliance with those requirements.

We will also provide a report (that does not include an opinion) on internal control related to the financial reporting and compliance with other matters which could have a material effect on the financial statements as required by *Government Auditing Standards*. The report on internal control and compliance will include a statement that the report is intended solely for the information and use of the District's Board of Commissioners and management, and is not intended to be and should not be used by anyone other than these specified parties.

Our Additional Responsibilities under Oregon Minimum Standards for Audits of Oregon Municipal Corporations

The Minimum Standards for Audits of Oregon Municipal Corporations (prescribed by the Secretary of State in cooperation with the Oregon State Board of Accountancy) require us to determine if Clackamas River Water has followed accounting principles generally accepted in the United States of America, established appropriate accounting systems and internal controls, and substantially complied with legal requirements in conducting its financial affairs. However, our consideration of these issues would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses as defined in our professional standards.

Planned Scope and Timing of the Audit

We are required by our professional standards to communicate significant matters (including potential fraud and illegal acts) related to the audit that are, in our professional judgment, relevant to your responsibilities in overseeing the financial reporting process. However, we are not required to design procedures specifically to identify such matters.

Certain matters have recently been brought to our attention which could potentially affect the fair presentation of your financial statements and, therefore, obligate us to report them to you. As a condition of our completing your audit, we will require you to investigate these matters to our satisfaction. We do not take this step lightly, but based on our decades of experience as auditors, we believe these are credible allegations which require your attention and investigation:

1. We understand that beginning in approximately 2007, Cyndi Lewis-Wolfram allegedly began submitting false expense reports, which were approved by the Board of Commissioners and paid by Clackamas River Water.
2. Cyndi Lewis-Wolfram may have recently used a disc containing Clackamas River Water e-mails to pressure Kami Kehoe, Lee Moore and Vance Voyles to allow the false expense reporting to continue. The emails were allegedly obtained from the previous IT Manager, who apparently collected them between 2007-2010 by intercepting emails within the Clackamas River Water email system (i.e. among employees, the Board of Commissioners, legal counsel and others) and forwarded them to his home email account.

3. The previous IT Manager was allegedly conducting a personal IT consulting business from Clackamas River Water facilities during business hours. Furthermore, certain computer equipment may have been wrongfully converted via purchases through Clackamas River Water's accounts payable system. The old computer equipment, in connection with the newly replaced equipment (which might not otherwise have needed replacing), was apparently not accounted for or tracked.
4. Beaver Creek Cooperative Telephone Company has constructed a building on (or partially on) land owned by Clackamas River Water without an underlying land lease between Clackamas River Water and Beaver Creek Cooperative Telephone Company. Furthermore, Bob George allegedly held a position (perhaps President) at Beaver Creek Cooperative Telephone Company at the time the building permit application was submitted to The Building Codes Division of Clackamas County. Bob George and Lee Moore apparently knew (or should have known) about the property line discrepancy prior to and during construction without investigating further and/or resolving the matter.
5. Clackamas River Water is apparently negotiating with the Sunrise Water Authority and/or The Water Division of the City of Milwaukie to share water resources, infrastructure and/or management. The negotiations have been alleged to lack the level of transparency expected with a matter of this magnitude. In light of the apparent lack of timeliness (and transparency) in resolving the land lease noted in #4 above, this allegation raises similar doubt as to whether these negotiations will maximize revenue to Clackamas River Water.
6. Certain of the general manager's activities and actions should be investigated due to their potential monetary effect on the rate payers:
 - The general manager apparently used a process which allowed him to approve a specific contractor to remodel the Clackamas River Water office facilities but does not appear to have met the goals of the competitive bid process required by law.
 - Certain vendor charge accounts were apparently established (at the general manager's direction) during 2009-2010 which have the potential to circumvent the normal internal control procedures established over the purchasing system.
 - Normal internal control procedures are allegedly not always followed with regard to the general manager's use of his Clackamas River Water Visa card.
 - The general manager allegedly refused to provide copies of accounting records (public records) supporting certain expense report reimbursements.
 - The general manager owns a personal business (or businesses) which he may be spending time on during business hours while being paid by Clackamas River Water.

While we have no personal knowledge of the matters delineated above, our professional standards require us to alert you to these matters as they reflect conduct which we as auditors are educated to be concerned about.

By delivering this letter, we have fulfilled our responsibility to inform "those charged with governance" of potential fraud or illegal acts as they have come to our attention, whether or not they are material to the financial statements. As a result, the completion of our audit of the financial statements of Clackamas River Water must be postponed according to the following timeline:

1. The Clackamas River Water Board of Commissioners should hire a qualified outside forensic specialist to thoroughly investigate each matter delineated above. At the conclusion of the investigation, we will determine whether the investigation was conducted by competent individuals, following appropriate investigative protocols, and whether or not the conclusions reached can be relied upon.
2. At such time as we are satisfied with the results of the forensic investigation we will resume our financial statement audit. Depending on the results of the investigation, our professional standards may require the scope of our financial statement audit to be significantly different than originally planned before the matters delineated above were brought to our attention. As such, we will continue our financial statement audit engagement on a time and expense reimbursement basis rather than the fixed fee arrangement originally contemplated in our February 12, 2010 Engagement Letter and the Auditing Services Contract #02398-06-2009 dated June 12, 2009.

3. If Clackamas River Water does not investigate each matter set out above to our satisfaction within a reasonable time, our professional standards require us to inform the Secretary of State of each of the matters delineated above.
4. The deadline for filing our audit report on Clackamas River Water's financial statements with the Secretary of State is December 31, 2010.
5. The "Increase in Engagement Scope" section of our Proposal to Provide Audit Services to Clackamas River Water dated March 20, 2009 specifies that, if, during our audit, we discover circumstances requiring additional examination beyond the scope of this proposal, we will discuss the necessary procedures with Clackamas River Water personnel. Our proposal indicates we will bill for additional services at our standard billing rates. Our time and expenses (including legal expenses) incurred to respond to these matters was not contemplated in our engagement letter dated February 12, 2010 or the Auditing Services Contract #02398-06-2009 dated June 12, 2009. We will therefore bill Clackamas River Water for these additional services and expenses.

This information is intended solely for the use of the Board of Commissioners of Clackamas River Water and is not intended to be and should not be used by anyone other than these specified parties. We look forward to hearing from you at your earliest convenience and are available to meet with you in person to answer any questions you may have.

Very truly yours,

Van Beek & Co., LLC

cc: Dean M. Phillips
Stephen F. English