TOWN OF CLAYTON
KENT COUNTY, DELAWARE

FINANCIAL STATEMENTS

DECEMBER 31, 2009

TOWN OF CLAYTON

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INDEPENDENT AUDITORS' REPORT

April 29, 2010

To the Honorable Mayor and Town Council
Town of Clayton
Clayton, Delaware

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 Clayton, Clayton, Delaware, as of and for the year ended December 31, 2009, 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 Clayton's management. Our responsibility is to express an opinion on these financial statements based on our audit. The prior year summarized comparative information has been derived from the Town's 2008 financial statements and, in our report dated August 31, 2009, we expressed an unqualified opinion on the respective financial statements of the governmental activities, the business-type activities, each major fund and the aggregate remaining fund information.

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 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 opinion.

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 Clayton, Clayton, Delaware, as of December 31, 2009, 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 April 29, 2010, on our consideration of the Town of Clayton's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the 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.

BARBACANE
THORNTON
&COMPANY
CERTIFIED PUBLIC ACCOUNTANTS

To the Honorable Mayor and Town Council
Town of Clayton

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Town of Clayton's basic financial statements. The combining nonmajor governmental fund financial statements on pages 33 and 34 are presented for purposes of additional analysis and are not a required part of the basic financial statements. The combining nonmajor governmental fund financial statements have been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, are fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

The Management's Discussion and Analysis on pages 3 - 9 and the budgetary comparison schedule - general fund on page 32 are not required parts of the basic financial statements but are supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Barbacane, Thornton & Company

BARBACANE, THORNTON & COMPANY

This discussion and analysis of the Town of Clayton, Delaware (the "Town") provides an overview of the Town's financial performance for the fiscal year ended December 31, 2009. Please read it in conjunction with the Town's financial statements which begin on page 10.

FINANCIAL HIGHLIGHTS

The assets of the Town exceeded its liabilities at December 31, 2009 by $6.3 million (net assets). Of this amount, $903 thousand (unrestricted net assets) may be used to meet the Town's ongoing obligations to its citizens and creditors. The Town's total net assets decreased by $260 thousand. The current year decrease in the Town's net assets is due primarily to current year expenses, including transfers, exceeding revenues. Also, effective January 1, 2009, trash rates increased from $17.35 to $19.20 per month.

As of December 31, 2009, the Town's governmental funds reported combined ending fund balances of $2.9 million, an increase of $85 thousand as compared to the prior year. The current year increase in fund balance can be attributed to transfers from other funds in order to cover expenditures throughout the course of the year.

As of December 31, 2009, the Town's proprietary funds reported combined net assets of $2.5 million, a decrease of $236 thousand as compared to the prior year. The current year decrease in net assets can be attributed to an increase in electric service charges, offset by an increase in transfers to other funds, and an increase in depreciation. Electric billing rates remained the same for 2009 compared to the prior year. Sewer billing rates increased by $1.00 from $15.50 to $16.50 for 3000 gallons per month. In addition, approximately $775 thousand was transferred from the proprietary funds to subsidize the government's primary operations.

Overview of the Financial Statements

The financial statements consist of three parts – management's discussion and analysis, the basic financial statements and required supplementary information. This discussion and analysis is intended to serve as an introduction to the Town of Clayton's basic financial statements. The Town of Clayton's basic financial statements are comprised of three components: 1) entity-wide financial statements; 2) fund financial statements; and 3) notes to the financial statements. This report also contains other supplementary information in addition to the basic financial statements.

The basic financial statements include two kinds of statements that present different views of the Town:

- The first two statements are entity-wide financial statements that provide both long-term and short-term information about the Town's overall financial status.

- The remaining statements are fund financial statements that focus on individual parts of the Town government, reporting the Town's operations in more detail than the entity-wide statements.

The financial statements also include notes that explain some of the information in the financial statements and provide more detailed data. The statements are followed by a section of required supplementary information that further explains and supports the information in the financial statements.

Entity-wide Financial Statements. The entity-wide financial statements are designed to provide readers with a broad overview of the Town's finances, in a manner similar to a private-sector business. These statements are prepared using the accrual basis of accounting.

The statement of net assets presents information on all of the Town's assets and liabilities, with the difference between the two reported as net assets. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of the Town is improving or deteriorating.

The statement of activities presents information showing how the Town's net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will result in cash flows only in future fiscal periods.

Both of the entity-wide financial statements distinguish functions of the Town that are principally supported by taxes and intergovernmental revenues (governmental activities) from other functions that are intended to recover all or a significant portion of their costs through user fees and charges (business-type activities). The governmental activities of the Town include general government, public safety, public works, and licensing and inspection. Business-type activities consist of the Town's electric distribution system and water supply and sewage collection system.

Fund Financial Statements. Traditional readers of government financial statements will find the fund financial statement presentation more familiar where the focus is on the Town's most significant funds. A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The Town uses fund accounting to ensure and demonstrate fiscal accountability. The Town uses governmental and proprietary fund financial statements to provide more detailed information about the Town's most significant funds rather than the Town as a whole.

Governmental Funds. Most of the Town's basic services are reported in governmental funds, which focus on how money flows into and out of those funds and the balances left at year end that are available for spending. These funds are reported using the modified accrual accounting method, which measures cash and all other financial assets that can be readily converted to cash. The governmental fund statements provide a detailed short-term view of the Town's general government operations and the basic services it provides. Governmental fund information helps the reader determine whether there are more or fewer financial resources that can be spent in the near future to finance the Town's programs. The relationship (or differences) between governmental activities (reported in the Statement of Net Assets and the Statement of Activities) and governmental funds is described in a reconciliation.

Proprietary funds. Proprietary funds are used to account for operations that are financed and operated in a manner similar to private business enterprises in which costs are recovered primarily through user charges. Proprietary fund financial statements, like entity-wide financial statements, provide both long-term and short-term financial information. The fund financial statements provide more detail and additional information, such as cash flows, for the Town's proprietary funds. The proprietary funds are used to report the same functions presented as business-type activities in the entity-wide financial statements. The Town uses proprietary funds to account for its electric distribution system and water supply and sewage collection system. The Town purchases 100 percent of its electric supply requirements from the Delaware Municipal Electric Corporation ("DEMEC") under a long-term full requirements service contract. In addition, the Town is charged a fee by the Town of Smyrna and Kent County to discharge the Town's proportionate share of wastewater into their respective facilities under an operating contract.

Notes to the Basic Financial Statements. The notes to the basic financial statements provide additional information that is essential to a full understanding of the data provided in the entity-wide and fund financial statements.

Required Supplementary Information. In addition to the basic financial statements and accompanying notes, this report presents certain required supplementary information concerning the Town. A budgetary comparison schedule has been provided for the General Fund.

FINANCIAL ANALYSIS OF THE TOWN AS A WHOLE

Entity-wide Financial Analysis

The following table presents a summary of the Statement of Net Assets for the Town as of December 31, 2009 and 2008:

Table 1 – Condensed Statement of Net Assets

	Governmental Activities		Business-type Activities		Totals	
	2009	2008	2009	2008	2009	2008
ASSETS						
Current and other assets	$ 3,001,165	$ 2,891,411	$ 566,279	$ 553,731	$ 3,567,444	$ 3,445,142
Capital assets, net	900,201	1,013,116	3,130,655	3,299,665	4,030,856	4,312,781
TOTAL ASSETS	3,901,366	3,904,527	3,696,934	3,853,396	7,598,300	7,757,923
LIABILITIES						
Other liabilities	79,291	61,229	426,783	313,505	506,074	374,734
Long-term liabilities	15,256	13,212	784,143	817,516	799,399	830,728
TOTAL LIABILITIES	94,547	74,441	1,210,926	1,131,021	1,305,473	1,205,462
NET ASSETS						
Invested in capital assets, net of related debt	900,201	1,013,116	2,313,139	2,449,665	3,213,340	3,462,781
Restricted	2,176,969	1,885,651	-	-	2,176,969	1,885,651
Unrestricted	729,649	931,319	172,869	272,710	902,518	1,204,029
TOTAL NET ASSETS	$ 3,806,819	$ 3,830,086	$ 2,486,008	$ 2,722,375	$ 6,292,827	$ 6,552,461

Invested in capital assets net of related debt decreased as a result of depreciation expense exceeding capital additions for the year. The largest portion of the Town's net assets reflects its investment in capital assets, less any related debt used to acquire those assets that is still outstanding. Capital assets are used to provide services to residents and they are not available for future spending. Although the investment in capital assets is reported net of related debt, it should be noted that the resources needed to repay this debt must be provided from other sources, since the capital assets themselves cannot be used to liquidate these liabilities. Restricted net assets increased due to the accumulation of resources restricted to public works projects and future growth initiatives.

Table 2 – Changes in Net Assets

	Governmental Activities		Business-type Activities		Totals	
	2009	2008	2009	2008	2009	2008
REVENUES						
Program revenues:						
Charges for services	$ 455,175	$ 735,413	$ 2,943,710	$ 2,617,191	$ 3,398,885	$ 3,352,604
Operating grants/contributions	62,827	94,894	-	-	62,827	94,894
Capital grants/contributions	-	2,098	-	-	-	2,098
General revenues:						
Taxes	452,454	580,080	-	-	452,454	580,080
Investment earnings	1,342	31,387	435	2,375	1,777	33,762
Franchise fees	15,097	12,824	-	-	15,097	12,824
Miscellaneous	1,795	990	-	-	1,796	990
Transfers/Contributions	775,490	200,050	-	-	775,490	200,050
TOTAL REVENUES	1,764,180	1,657,736	2,944,145	2,619,566	4,708,325	4,277,302
EXPENSES						
General government	485,551	498,391	-	-	485,551	498,391
Public safety	862,664	707,237	-	-	862,664	707,237
Public works	379,146	361,572	-	-	379,146	361,572
Licensing and inspection	60,086	57,439	-	-	60,086	57,439
Electric operations	-	-	1,766,588	1,863,505	1,766,588	1,863,505
Water/Sewer operations	-	-	638,434	805,495	638,434	805,495
Transfers	-	-	775,490	200,050	775,490	200,050
TOTAL EXPENSES	1,787,447	1,624,639	3,180,512	2,869,050	4,967,959	4,493,689
INCREASE (DECREASE) IN NET ASSETS	(23,267)	33,097	(236,367)	(249,484)	(259,634)	(216,387)
NET ASSETS, BEGINNING OF YEAR	3,830,086	3,796,989	2,722,375	2,971,859	6,552,461	6,768,848
NET ASSETS, END OF YEAR	$ 3,806,819	$ 3,830,086	$ 2,486,008	$ 2,722,375	$ 6,292,827	$ 6,552,461

Governmental Activities

The cost of all governmental activities in 2009 was $1.8 million. The amount that taxpayers ultimately financed for these activities through Town taxes was $452 thousand, or 25 percent. Other costs were paid by those who directly benefited from the programs ($455 thousand, or 25 percent) or by government agencies and organizations that subsidized funding with intergovernmental aid and contributions ($62 thousand, or three percent).

Charges for services decreased due primarily to a decrease in building permit and impact fees in the amount of approximately $312 thousand which can be attributed to the decrease in development within Town limits. Decreases in taxes relate primarily to a decrease in transfer taxes from the prior year in the amount of $135 thousand net of an increase in property taxes of $7 thousand. The decrease in transfer taxes is due to the decrease in development within Town limits; the increase in property taxes is due to additional assessments related to development in prior years.

As indicated by the governmental program expenses, general government programs accounted for 27 percent of the Town's governmental activities and remained consistent with prior year amounts. Public safety expenses accounted for 48 percent of the Town's governmental activities, public works expenses accounted for 21 percent, and licensing and inspection expenses accounted for three percent, all consistent with prior year amounts.

Business-type Activities and Proprietary Funds

Charges for services represent the principal revenue source for the Town's business-type activities and proprietary funds and increased by $326 thousand over the prior year. Increases in charges for services can be attributed to an increase in electric usage in the current year. The overall expenses of the business-type activities decreased by approximately 10 percent. Expense decreases are due to a decrease in employee benefits, sewer charges and supplies.

FINANCIAL ANALYSIS OF THE TOWN'S FUNDS

The Town uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements.

Governmental Funds

The focus of the Town's governmental funds is to provide information on near-term inflows, outflows and balances of spendable resources. Such information is valuable in assessing the Town's financing requirements. In particular, the unreserved fund balance may serve as a useful measure of a government's net resources available for spending at the end of the fiscal year.

As of December 31, 2009, the Town's governmental funds reported combined ending fund balances of $2.9 million, an increase of $85 thousand as compared to the prior year. Approximately 75 percent, or $2.2 million, constitutes fund balance reserved for special purposes, leaving $729 thousand available for spending at the Town's discretion.

The General Fund is the chief operating fund of the Town. As of December 31, 2009, the total fund balance of the General Fund was approximately $741 thousand, of which $688 thousand is unreserved and undesignated, $42 thousand has been designated by the Town to fund future costs for post-employment benefits and $11 thousand has been reserved for future police pension costs. The fund balance decreased by $197 thousand during the year ended December 31, 2009.

The other major fund of the Town is the Impact Fees Fund which is used to accumulate resources for future growth initiatives as mandated by law.

Significant changes in revenues and expenditures for the governmental funds are consistent with the prior analysis of the governmental activities revenues and expenses. Other financing sources consisted of transfers from the proprietary funds to subsidize the government's primary governmental operations.

GENERAL FUND BUDGETARY HIGHLIGHTS

The schedule comparing the Town's budget and actual results can be found on page 32. There were no amendments to the original budget. A summary of significant variations between budget amounts and actual results are as follows:

- Transfer tax revenue was $46 thousand less than budget due to the timing of the completion of development projects and the sale of the associated properties.

- Intergovernmental revenue was $66 thousand less than budget due to anticipated governmental support programs no longer offering support.

- General government expenditures were $369 thousand less than budget due to the expectation of significant increases related to health insurance and property insurance.

- Public safety expenses were over budget by $208 thousand due to the need for additional employees resulting in an increase in salaries and benefits for the public safety department.

- Public works expenditures were $206 thousand less than budget due to the expectation of a need for additional employees and increasing premiums related to health insurance and property insurance.

- Capital outlay expenditures were $96 thousand under budget due to the timing of the completion of repaving projects.

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets

The Town's capital assets for its governmental and business-type activities as of December 31, 2009 amounted to $4 million net of accumulated depreciation. Capital assets include land, building and improvements, improvements other than buildings, machinery and equipment, vehicles and infrastructure. The total net decrease in the Town's capital assets for the current fiscal year was approximately $282 thousand. Current year depreciation expense of $270 thousand exceeded additions of $23 thousand. In addition, there was $35 thousand in capital assets sales.

More detailed information about the Town's capital assets is presented in the notes to the basic financial statements.

Debt Administration

During the year ended December 31, 2009, the Town paid approximately $32 thousand to bring the total debt to approximately $818 thousand through the Delaware Department of Natural Resources and Environmental Control to finance the Town's water treatment facilities.

More detailed information about the Town's long-term liabilities is presented in the notes to the basic financial statements.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGET AND RATES

The primary economic factor affecting the budget for the Town of Clayton is the residential housing market. Industrial and commercial activities are minimal. Impact fees imposed upon new residential construction support infrastructure improvements. Permit fees and transfer taxes support the operations of Public Works and Administrative department operations, respectively.

Rates for taxes and fees for services will remain consistent in 2010 in relation to 2009.

REQUESTS FOR INFORMATION

This financial report is designed to provide our citizens, customers, investors and creditors with a general overview of the Town's finances. If you have questions about this report or need any additional information, please contact the Town of Clayton, 414 Main Street, P.O. Box 1130, Clayton, Delaware, 19938-1130.

TOWN OF CLAYTON
STATEMENT OF NET ASSETS
DECEMBER 31, 2009
(With Summarized Comparative Data for December 31, 2008)

	Governmental Activities	Business-type Activities	Totals 2009	Totals 2008*
ASSETS				
Current Assets:				
Cash and cash equivalents	$ 2,941,227	$ 445,569	$ 3,386,796	$ 3,257,364
Taxes receivable	15,482	-	15,482	33,828
Accounts receivable	20,390	56,616	77,006	51,102
Other receivables	4,379	15,356	15,356	21,384
Inventory	6,171	45,360	51,531	42,258
Prepaid expenses	13,516	3,378	16,894	39,206
Total Current Assets	3,001,165	566,279	3,567,444	3,445,142
Noncurrent Assets:				
Capital assets, net	900,201	3,130,655	4,030,856	4,312,781
TOTAL ASSETS	$ 3,901,366	$ 3,696,934	$ 7,598,300	$ 7,757,923
LIABILITIES AND NET ASSETS				
LIABILITIES:				
Accounts payable	$ 1,424	$ 241,934	$ 243,358	$ 137,189
Impact fee escrows	39,674	-	39,674	3,506
Accrued salaries and benefits	15,307	3,826	19,133	47,739
Accrued interest	-	9,625	9,625	9,633
Loan payable	-	33,373	33,373	32,484
Accumulated compensated absences	22,886	23,852	46,738	34,960
Utility deposits	-	114,173	114,173	109,223
Total Current Liabilities	79,291	426,783	506,074	374,734
Noncurrent Liabilities:				
Loan payable	-	784,143	784,143	817,516
Accumulated compensated absences	15,256	-	15,256	13,212
Total Noncurrent Liabilities	15,256	784,143	799,399	830,728
TOTAL LIABILITIES	94,547	1,210,926	1,305,473	1,205,462
NET ASSETS				
Invested in capital assets, net of related debt	900,201	2,313,139	3,213,340	3,462,781
Unrestricted	729,649	172,869	902,518	1,204,029
Restricted for police	16,115	-	16,115	7,104
Restricted for public works	108,412	-	108,412	139,456
Restricted for future growth initiatives	2,052,442	-	2,052,442	1,739,091
TOTAL NET ASSETS	3,806,819	2,486,008	6,292,827	6,552,461
TOTAL LIABILITIES AND NET ASSETS	$ 3,901,366	$ 3,696,934	$ 7,598,300	$ 7,757,923

* Restated for comparative purposes.

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

TOWN OF CLAYTON
STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED DECEMBER 31, 2009
(With Summarized Comparative Data for the Year Ended December 31, 2008)

		Program Revenues			Net (Expense) Revenue and Changes in Net Assets			
	Expenses	Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	Governmental Activities	Business-type Activities	Totals 2009	Totals 2008*
GOVERNMENTAL ACTIVITIES								
General government	$ 485,551	$ 6,359	$ -	$ -	$ (479,192)	$ -	$ (479,192)	$ (490,409)
Public safety	862,664	65,439	62,827	-	(734,398)	-	(734,398)	(570,399)
Public works	379,146	364,174	-	-	(14,972)	-	(14,972)	273,873
Licensing and inspection	60,086	19,203	-	-	(40,883)	-	(40,883)	(5,299)
TOTAL GOVERNMENTAL ACTIVITIES	1,787,447	455,175	62,827	-	(1,269,445)	-	(1,269,445)	(792,234)
BUSINESS-TYPE ACTIVITIES								
Electric	1,766,588	2,290,066	-	-	-	523,478	523,478	166,373
Water/Sewer	638,434	653,644	-	-	-	15,210	15,210	(218,182)
TOTAL BUSINESS-TYPE ACTIVITIES	2,405,022	2,943,710	-	-	-	538,688	538,688	(51,809)
TOTAL PRIMARY GOVERNMENT	$ 4,192,469	$ 3,398,885	$ 62,827	$ -	(1,269,445)	538,688	(730,757)	(844,043)
GENERAL REVENUES								
Real estate taxes					278,307	-	278,307	271,268
Real estate transfer taxes					174,147	-	174,147	308,812
Franchise fees					15,097	-	15,097	12,824
Interest income					1,342	435	1,777	33,762
Miscellaneous					1,795	-	1,795	990
TRANSFERS					775,490	(775,490)	-	-
TOTAL GENERAL REVENUES AND TRANSFERS					1,246,178	(775,055)	471,123	627,656
CHANGE IN NET ASSETS					(23,267)	(236,367)	(259,634)	(216,387)
NET ASSETS, BEGINNING OF YEAR					3,830,086	2,722,375	6,552,461	6,768,848
NET ASSETS, END OF YEAR					$ 3,806,819	$ 2,486,008	$ 6,292,827	$ 6,552,461

* Restated for comparative purposes.

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

TOWN OF CLAYTON
BALANCE SHEET - GOVERNMENTAL FUNDS
DECEMBER 31, 2009
(With Summarized Comparative Data for December 31, 2008)

	General Fund	Impact Fees Fund	Nonmajor Governmental Funds	Totals 2009	Totals 2008*
ASSETS					
Cash and cash equivalents	$ 892,724	$1,932,358	$ 116,145	$2,941,227	$2,818,530
Taxes receivable	15,482	-	-	15,482	33,828
Accounts receivable	20,390	-	-	20,390	3,208
Other receivables	4,379	-	-	4,379	-
Inventory	6,171	-	-	6,171	4,481
Prepaid expenses	13,516	-	-	13,516	31,364
Due from other funds	1,625	159,758	-	161,383	-
TOTAL ASSETS	$ 954,287	$2,092,116	$ 116,145	$3,162,548	$2,891,411
LIABILITIES AND FUND BALANCES					
LIABILITIES:					
Accounts payable	$ -	$ -	$ 1,424	$ 1,424	$ 24,239
Impact fee escrows	-	39,674	-	39,674	3,506
Accrued salaries and benefits	15,307	-	-	15,307	26,348
Accumulated compensated absences	22,886	-	-	22,886	7,136
Deferred revenue	15,482	-	-	15,482	8,290
Due to other funds	159,758	-	1,625	161,383	-
TOTAL LIABILITIES	213,433	39,674	3,049	256,156	69,519
FUND BALANCES:					
Unreserved - undesignated	687,742	-	-	687,742	894,560
Unreserved - designated for:					
post-employment benefits	41,681	-	-	41,681	41,681
Reserved for police	11,431	-	4,684	16,115	7,104
Reserved for public works	-	-	108,412	108,412	139,456
Reserved for future growth initiatives	-	2,052,442	-	2,052,442	1,739,091
TOTAL FUND BALANCES	740,854	2,052,442	113,096	2,906,392	2,821,892
TOTAL LIABILITIES AND FUND BALANCES	$ 954,287	$2,092,116	$ 116,145	$3,162,548	$2,891,411

* Restated for comparative purposes.

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

TOWN OF CLAYTON
RECONCILIATION OF BALANCE SHEET - GOVERNMENTAL FUNDS TO STATEMENT OF NET ASSETS
DECEMBER 31, 2009

TOTAL GOVERNMENTAL FUND BALANCES	$ 2,906,392
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.	900,201
Some of the Town's assets are not available soon enough to pay for current period expenditures and therefore are deferred in the funds.	15,482
Expenses accrued for compensated absences reported in the statement of activities that do not require the use of current financial resources are not reported as expenditures in the governmental funds.	(15,256)
NET ASSETS OF GOVERNMENTAL ACTIVITIES	$ 3,806,819

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

TOWN OF CLAYTON
STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES - GOVERNMENTAL FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2009
(With Summarized Comparative Data for the Year Ended December 31, 2008)

	General	Impact Fees Fund	Nonmajor Governmental Funds	Totals 2009	Totals 2008*
REVENUES					
Taxes:					
Property taxes	$ 262,825	$ -	$ -	$ 262,825	$ 268,587
Transfer taxes	174,147	-	-	174,147	308,812
Special assessment/impact fees	-	131,129	-	131,129	410,969
Charges for services	252,248	-	-	252,248	239,227
Intergovernmental	40,244	-	22,583	62,827	96,991
Licenses and fees	6,359	-	-	6,359	7,982
Fines and forfeits	65,439	-	-	65,439	77,235
Franchise fees	15,097	-	-	15,097	12,824
Interest income	1,169	41	132	1,342	31,387
Miscellaneous	1,795	-	-	1,795	990
TOTAL REVENUES	819,323	131,170	22,715	973,208	1,455,004
EXPENDITURES					
Current:					
General government	439,951	-	-	439,951	472,297
Public safety	750,534	-	54,331	804,865	660,556
Public works	328,229	26,000	-	354,229	327,836
Licensing and inspection	58,700	-	-	58,700	54,136
Capital outlays	22,747	-	-	22,747	168,946
TOTAL EXPENDITURES	1,600,161	26,000	54,331	1,680,492	1,683,771
EXCESS (DEFICIENCY) OF REVENUES OVER (UNDER) EXPENDITURES	(780,838)	105,170	(31,616)	(707,284)	(228,767)
OTHER FINANCING SOURCES (USES)					
Proceeds from sale of capital assets	16,294	-	-	16,294	-
Transfers in	567,309	208,181	-	775,490	484,870
Transfers out	-	-	-	-	(284,820)
TOTAL OTHER FINANCING SOURCES	583,603	208,181	-	775,490	200,050
NET CHANGES IN FUND BALANCES	(197,235)	313,351	(31,616)	84,500	(28,717)
FUND BALANCES, BEGINNING OF YEAR	938,089	1,739,091	144,712	2,821,892	2,850,609
FUND BALANCES, END OF YEAR	$ 740,854	$2,052,442	$ 113,096	$2,906,392	$2,821,892

* Restated for comparative purposes.

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

TOWN OF CLAYTON
RECONCILIATION OF STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES - GOVERNMENTAL FUNDS TO STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED DECEMBER 31, 2009

NET CHANGES IN FUND BALANCES - TOTAL GOVERNMENTAL FUNDS	$	84,500
Amounts reported for governmental activities in the statement of activities are different because:		
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 as depreciation expense. This is the amount by which depreciation ($100,777) exceeded capital outlays ($22,747).		(78,030)
Because some property taxes will not be collected for several months after the Town's fiscal year ends, they are not considered as "available" revenues in the governmental funds. Deferred tax revenues increased by this amount this year.		7,192
Expenses accrued for compensated absences reported in the statement of activities that do not require the use of current financial resources are not reported as expenditures in the governmental funds.		(2,044)
Sales and other disposals of capital assets must be reported in the entity-wide statement of net assets. Gains on such disposals should be reported as general revenues. Losses should not be reported as direct expenses of specific functions but should instead be included as part of the general government function.		(34,885)
CHANGE IN NET ASSETS OF GOVERNMENTAL ACTIVITIES	$	(23,267)

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

TOWN OF CLAYTON
STATEMENT OF NET ASSETS - PROPRIETARY FUNDS
DECEMBER 31, 2009
(With Summarized Comparative Data for December 31, 2008)

	Electric Fund	Water and Sewer Fund	Totals 2009	Totals 2008*
ASSETS				
Current Assets:				
Cash and cash equivalents	$ 410,722	$ 34,847	$ 445,569	$ 438,834
Accounts receivable	42,673	13,943	56,616	47,894
Other receivables	15,356	-	15,356	21,384
Inventory	43,518	1,842	45,360	37,777
Prepaid expenses	1,689	1,689	3,378	7,842
Total Current Assets	513,958	52,321	566,279	553,731
Noncurrent Assets:				
Capital assets, net	1,113,363	2,017,292	3,130,655	3,299,665
TOTAL ASSETS	$1,627,321	$2,069,613	$3,696,934	$3,853,396
LIABILITIES AND NET ASSETS				
Current Liabilities:				
Accounts payable	$ 145,569	$ 96,365	$ 241,934	$ 112,950
Accrued salaries and benefits	1,913	1,913	3,826	21,391
Accrued interest	-	9,625	9,625	9,633
Loan payable	-	33,373	33,373	32,484
Accumulated compensated absences	8,348	15,504	23,852	27,824
Utility deposits	114,173	-	114,173	109,223
Total Current Liabilities	270,003	156,780	426,783	313,505
Noncurrent Liabilities:				
Loan payable	-	784,143	784,143	817,516
TOTAL LIABILITIES	270,003	940,923	1,210,926	1,131,021
NET ASSETS				
Invested in capital assets, net of related debt	1,113,363	1,199,776	2,313,139	2,449,665
Unrestricted (Deficit)	243,955	(71,086)	172,869	272,710
TOTAL NET ASSETS	1,357,318	1,128,690	2,486,008	2,722,375
TOTAL LIABILITIES AND NET ASSETS	$1,627,321	$2,069,613	$3,696,934	$3,853,396

* Restated for comparative purposes.

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

TOWN OF CLAYTON
STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS - PROPRIETARY FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2009
(With Summarized Comparative Data for the Year Ended December 31, 2008)

	Electric Fund	Water and Sewer Fund	Totals 2009	Totals 2008*
OPERATING REVENUES				
User service charges	$ 2,250,221	$ 604,169	$ 2,854,390	$ 2,528,204
Other operating revenue	39,845	49,475	89,320	88,987
Total Operating Revenues	2,290,066	653,644	2,943,710	2,617,191
OPERATING EXPENSES				
Electric purchased	1,497,883	-	1,497,883	1,493,516
Utility tax	8,753	-	8,753	11,081
Sewer charges	-	225,195	225,195	249,392
System upgrades and maintenance	44,828	53,541	98,369	179,556
Salaries and wages	75,439	152,908	228,347	231,049
Employee benefits	39,146	39,146	78,292	234,428
Depreciation	72,982	96,028	169,010	131,766
Supplies	2,811	37,042	39,853	101,930
Administration expenses	3,055	3,332	6,387	7,194
Professional services	21,691	8,349	30,040	19,455
Total Operating Expenses	1,766,588	615,541	2,382,129	2,659,367
OPERATING INCOME (LOSS)	523,478	38,103	561,581	(42,176)
NONOPERATING REVENUES (EXPENSES)				
Interest income	435	-	435	2,375
Interest expense	-	(22,893)	(22,893)	(9,633)
Total Nonoperating Revenues (Expenses)	435	(22,893)	(22,458)	(7,258)
INCOME (LOSS) BEFORE TRANSFERS AND CONTRIBUTIONS	523,913	15,210	539,123	(49,434)
Transfers in	-	-	-	145,975
Transfers out	(599,273)	(176,217)	(775,490)	(346,025)
CHANGE IN NET ASSETS	(75,360)	(161,007)	(236,367)	(249,484)
NET ASSETS, BEGINNING OF YEAR	1,432,678	1,289,697	2,722,375	2,971,859
NET ASSETS, END OF YEAR	$ 1,357,318	$ 1,128,690	$ 2,486,008	$ 2,722,375

* Restated for comparative purposes.

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

TOWN OF CLAYTON
STATEMENT OF CASH FLOWS - PROPRIETARY FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2009
(With Summarized Comparative Data for the Year Ended December 31, 2008)

	Electric Fund	Water and Sewer Fund	Totals 2009	Totals 2008*
CASH FLOWS FROM OPERATING ACTIVITIES:				
Received from customers	$ 2,290,796	$ 650,220	$ 2,941,016	$ 2,792,704
Paid to suppliers for goods and services	(1,433,748)	(341,917)	(1,775,665)	(2,151,333)
Paid to employees for services	(121,550)	(206,626)	(328,176)	(438,716)
NET CASH PROVIDED BY OPERATING ACTIVITIES	735,498	101,677	837,175	202,655
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES:				
Transfers in	-	-	-	145,975
Transfers out	(599,273)	(176,217)	(775,490)	(346,025)
NET CASH USED BY NONCAPITAL FINANCING ACTIVITIES	(599,273)	(176,217)	(775,490)	(200,050)
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES:				
Loan payment	-	(32,484)	(32,484)	32,120
Acquisition and construction of capital assets	-	-	-	(420,993)
Interest paid	-	(22,901)	(22,901)	(9,633)
NET CASH USED BY CAPITAL AND RELATED FINANCING ACTIVITIES	-	(55,385)	(55,385)	(398,506)
CASH FLOWS FROM INVESTING ACTIVITIES:				
Interest income	435	-	435	2,375
NET CASH PROVIDED BY INVESTING ACTIVITIES	435	-	435	2,375
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	136,660	(129,925)	6,735	(393,526)
CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR	274,062	164,772	438,834	832,360
CASH AND CASH EQUIVALENTS, END OF YEAR	$ 410,722	$ 34,847	$ 445,569	$ 438,834
CASH FLOWS FROM OPERATING ACTIVITIES:				
Operating income (loss)	$ 523,478	$ 38,103	$ 561,581	$ (42,176)
Adjustments to reconcile operating income (loss) to net cash provided by operating activities:				
Depreciation	72,982	96,028	169,010	131,766
Changes in assets and liabilities:				
Decrease (Increase) in accounts receivable	730	(3,424)	(2,694)	189,697
(Increase) in inventory	(7,478)	(105)	(7,583)	(14,400)
Decrease (Increase) in prepaid expenses	2,232	2,232	4,464	(1,185)
Increase (Decrease) in accounts payable	145,569	(16,585)	128,984	(94,572)
(Decrease) Increase in accrued salaries and benefits	(9,363)	(8,202)	(17,565)	14,632
Increase (Decrease) in compensated absences	2,398	(6,370)	(3,972)	12,937
Increase in utility deposits	4,950	-	4,950	5,956
NET CASH PROVIDED BY OPERATING ACTIVITIES	$ 735,498	$ 101,677	$ 837,175	$ 202,655

* Restated for comparative purposes.

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

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Town of Clayton complies with generally accepted accounting principles ("GAAP"). GAAP includes all relevant Governmental Accounting Standards Board ("GASB") pronouncements. The accounting and reporting framework and the more significant accounting policies are discussed in subsequent subsections of this Note.

Financial Reporting Entity

The Town of Clayton, Delaware (the "Town") was incorporated in 1887, under the provisions of the State of Delaware. The Town operates under a Council form of government and provides the following services as authorized by its charter: public safety, public works, utilities, licensing and inspection, and general government.

The Government Accounting Standards Board established the criteria for determining the activities, organizations and functions of government to be included in the financial statements of the reporting entity. The criteria used in determining whether such organizations should be included in the Town's financial reporting entity are financial interdependences, selection of governing authority, designation of management, ability to significantly influence operations, accountability for fiscal matters, scope of public service and special financing relationships.

The Town has determined that no other outside agency meets the above criteria and, therefore, no other agency has been included as a component unit in the Town's financial statements. In addition, the Town is not aware of any entity which would exercise such oversight which would result in the Town being considered a component unit of the entity.

Entity-wide And Fund Financial Statements

The entity-wide financial statements (i.e., the statement of net assets and the statement of changes in net assets) report information on all of the nonfiduciary activities of the Town. Governmental activities, which normally are supported by taxes and inter-governmental revenues, are reported separately from business-type activities, which rely to a significant extent on fees and charges for support.

The statement of activities demonstrates the degree to which the direct expenses of a given function or segment are offset by program revenues. Direct expenses are those that are clearly identifiable with a specific function or segment. Program revenues include 1) charges to customers who purchase, use or directly benefit from goods, services or privileges provided by a function or segment, and 2) grants and contributions that are restricted to meeting the operational or capital requirements of a function or segment. Taxes and other items not properly included among program revenues are reported instead as general revenues.

Separate financial statements are provided for governmental funds and proprietary funds. Major individual governmental funds and major individual proprietary funds are reported as separate columns in the fund financial statements. All remaining governmental funds are aggregated and reported as nonmajor funds.

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont'd)

Measurement Focus, Basis Of Accounting And Financial Statement Presentation

The entity-wide financial statements are reported 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 the timing of the related cash flows. Property taxes are recognized as revenue in the year for which they are levied. Grants and similar items (nonexchange transactions) are recognized as revenue as soon as all eligibility requirements imposed by the provider have been satisfied.

The entity-wide financial statements report net assets in one of three components. Invested in capital assets, net of related debt consists of capital assets, net of accumulated depreciation and reduced by the outstanding balances of borrowing attributable to acquiring, constructing or improving those assets. Net assets are reported as restricted when constraints placed on net asset use are either externally imposed by creditors (such as through debt covenants), grantors, contributors, or laws or regulations of other governments or imposed by law through constitutional provisions or enabling legislation. Those restrictions affect net assets arising from special revenue and capital funds. Unrestricted net assets consist of net assets that do not meet the definition of "invested in capital assets, net of related debt" or "restricted."

Except for interfund activity and balances between the funds that underlie governmental activities and the funds that underlie business-type activities, which are reported as transfers and internal balances, the effect of interfund activity has been removed from these statements.

The governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as soon as they become both measurable and available. Revenues are considered to be available if they are collected within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the Town considers property tax revenue to be available if collected within 60 days of the end of the fiscal period. Revenue from federal, state and other grants designated for payment of specific Town expenditures is recognized when the related expenditures are incurred; accordingly, when such funds are received, they are reported as deferred revenues until earned. Other revenues, including charges for services and miscellaneous revenues, are recorded as revenue when received in cash because they generally are not measurable until actually received.

Expenditures are recorded when the related fund liability is incurred (upon receipt of goods or services), except for claims and judgments, and compensated absences, which are recognized as expenditures to the extent they have matured. General capital asset acquisitions are reported as expenditures in governmental funds.

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont'd)

The Town reports the following major governmental funds:

General Fund – This fund is used to account for the general operating activities of the Town. General government, public safety, public works, and licensing and inspections are financed through this fund with receipts from general property taxes, transfer taxes, licenses and permits, investment interest, fines, charges for current services, intergovernmental and other revenue.

Impact Fees Fund – This fund is used to account for impact fees until they are transferred to the appropriate fund for specific, eligible projects.

Proprietary funds are accounted for using the accrual basis of accounting. These funds account for operations that are financed primarily by user charges. The economic resource focus concerns determining costs as a means of maintaining the capital investment and management control. Revenues are recognized when they are earned and expenses are recognized when they are incurred.

These funds distinguish operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and producing and delivering goods or services in connection with the proprietary fund's principal ongoing operations. The principal operating revenues of the Town's proprietary funds are electric and water/sewer charges. Operating expenses for the Town's proprietary funds include salaries, employee benefits, production costs, supplies and administrative costs. All revenues or expenses not meeting this definition are reported as nonoperating revenues and expenses.

The Town reports the following major proprietary funds:

Electric Fund - Used to account for the operation of an electric distribution system.

Water and Sewer Fund - Used to account for the operation of a water supply and sewage collection system.

In accordance with the Financial Standards Accounting Board's Accounting Standards Codification ("FASB ASC"), the entity-wide and business-type activities and proprietary funds of the Town follow the standards of accounting and financial reporting issued on or before November 30, 1989 to the extent that those standards do not conflict with or contradict guidance of the Governmental Accounting Standards Board ("GASB"). The Town also has the option to follow subsequent private-sector guidance for its business-type activities and proprietary funds with certain limitations, but has elected not to do so.

Cash And Cash Equivalents

For the purpose of the statement of cash flows, the proprietary funds consider all highly liquid investments with an original maturity of three months or less when purchased to be cash equivalents.

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont'd)

Allowance For Doubtful Accounts

The Town of Clayton's water, sewer and electric utilities experience very small losses from uncollectible accounts. Water and sewer fees constitute a lien against real property and usually can be collected in full when title transfers. Only balances that remain after tax sales are written off each year. Electric fees do not constitute a lien; however, maintenance of adequate customer deposits, monthly billing and diligent collection procedures minimize losses from uncollectible accounts. Accordingly, an allowance for doubtful accounts has not been established by the Town for its proprietary funds.

Inventories And Prepaid Expenses

Inventories of business-type activities and proprietary fund types are presented at the lower of cost or market on a first-in, first-out basis, and are expensed when used. Certain payments to vendors reflect costs applicable to future accounting periods and are recorded as prepaid expenses.

Capital Assets

Capital assets, including property, plant and equipment, are reported in the applicable governmental or business-type activities columns in the entity-wide financial statements. During the year ended December 31, 2007, the Town adopted a capitalization threshold of $5,000 with an estimated life in excess of one year. Capital assets placed in service prior to January 1, 2007 with a cost of less than $5,000 will continue to be depreciated until the asset is fully depreciated or disposed. Capital assets may be purchased or constructed and are recorded at cost. Donated capital assets are recorded at estimated fair value at the date of donation. The costs of normal maintenance and repairs that do not add to the value of the asset or materially extend the asset's life are not capitalized. Major outlays for capital assets and improvements are capitalized as projects are constructed, inclusive on ancillary costs.

GASB Statement No. 34 permits Phase III local governments to elect not to report infrastructure retroactively and report general infrastructure prospectively only. Management has assessed the impact of infrastructure capitalization on the financial statements and has determined that the cost outweighs the benefit of reporting the Town's infrastructure retroactively.

Capital assets of the Town are depreciated using the straight-line method over the estimated useful lives of the related assets as follows:

Buildings	40 years
Vehicles	5-8 years
Land improvements	20 years
Machinery and equipment	5-10 years

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont'd)

Compensated Absences

Regular, full-time employees are allowed sick leave on the basis of 10 days per year. Each January, employees have the option to continue accruing sick leave or be paid for unused sick leave from the previous year. Upon termination or retirement, an employee shall be paid a maximum of 45 days of accrued unused sick leave.

Regular, full-time employees accrue vacation leave on the basis of two weeks per year after completion of one year of continuous service. After three years of continuous service, two weeks vacation per year will be accrued. After six years of continuous service, three weeks vacation will be accrued. After 14 years of continuous service, four weeks vacation will be accrued. If an employee resigns or is terminated for any reason including dismissal or dies with unused annual leave credit, the employee, or in the case of his/her death, his/her estate, shall be paid for unused vacation time. Employees leaving the Town's employment on or before the 15th of a month will not receive credit for that month. Those employees departing the Town's employment after the 15th of a month will receive full credit for that month.

Accumulated vacation and sick leave is accrued when incurred in the entity-wide financial statements and proprietary fund types. A liability is reported in the governmental funds only if it is expendable from available financial resources. Historically, the General Fund has been responsible for liquidation of compensated absences associated with governmental fund activities. Compensated absences associated with proprietary funds are liquidated from the fund in which the liability was generated.

Fund Equity

In the fund financial statements, governmental funds report reservations of fund balance for amounts that are not available for appropriation or are legally restricted by outside parties for use for a specific purpose. The proprietary funds report the same three components of net assets as do the entity-wide financial statements. 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.

Property Taxes

Property taxes attach as an enforceable lien on property when levied. All liens continue until property taxes are paid in full. Taxes are levied on July 1 and are payable on or before September 30. Taxes paid after the payable date are assessed interest at one percent per month after the due date. The Town bills and collects its own property taxes. Town property tax revenues are recognized on a *pro rata* basis. Delinquent taxes are considered fully collectible and, therefore, no allowance for uncollectible taxes is provided. The property tax rate for 2009 was 65 cents per $100 of assessed value.

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont'd)

Use Of Estimates In The Preparation Of Financial Statements

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

Comparative Data

Comparative totals for the prior year have been presented in the accompanying financial statements in order to provide an understanding of changes in the Town's financial position and operations. However, presentation of prior year totals by fund and activity type have not been presented in each of the statements since their inclusion would make the statements unduly complex and difficult to read. Summarized comparative information should be read in conjunction with the Town's financial statements for the year ended December 31, 2008, from which the summarized information was derived.

Restatement of Entity-wide Financial Statements

For the year ended December 31, 2008, net assets decreased by $119,058, which represents $13,212 of compensated absences which should have been recorded as a long-term liability; pension expense improperly recorded in the amount of $24,926; and pumping fees of $80,920 which should have been recorded in the prior year.

NOTE 2 STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY

Budgetary Information

The Town follows these procedures in establishing the budgetary data reflected in the financial statements:

a. Formal budgetary integration is employed as a management control device during the year for the General Fund. This budget is adopted on a basis consistent with generally accepted accounting principles.

b. The Town Council adopts legal annual budgets for the General Fund and Proprietary Funds. The Town Council also adopts legal project length budgets for its Impact Fees Fund and certain nonmajor governmental funds. Since project periods may differ from the Town's fiscal year, a comparison of budgetary information for the combined Impact Fees Fund and certain nonmajor governmental funds would not be meaningful and has not been presented in the accompanying financial statements.

NOTE 2 STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY (cont'd)

c. Management is authorized to transfer budget amounts between departments within any fund; however, any revisions that alter the total appropriations of any fund must be approved by the Town Council. Therefore, the level of budgetary responsibility is by total appropriations; however, for report purposes, this level has been expanded to a functional basis.

d. Unused appropriations for all of the above annually budgeted funds lapse at year end.

e. For 2009, there were no revisions to any legally adopted budgets.

Excess of Expenditures Over Appropriations

For the year ended December 31, 2009, the General Fund incurred expenditures in excess of appropriations in the following functions:

Public safety	$ 207,738
Licensing and inspection	$ 15,525

All excess of expenditures over appropriations were funded by higher than anticipated revenues, transfers from other funds and the use of existing fund balances.

NOTE 3 CASH, CASH EQUIVALENTS AND INVESTMENTS

The Town of Clayton as a depositor and an investor generally requires full and continuous collateralization based upon fair value in the form of:

- Obligations of or guaranteed by the United States of America, or
- Obligations of the Federal National Mortgage Association, the Federal Home Mortgage Corporation, Public Housing Authority or an agency or instrumentality of the United States of America, or
- General or revenue obligations of the State of Delaware or its municipalities, subdivisions, public housing authorities or any agency or instrumentality of the State of Delaware.

As an investor, the Town of Clayton may invest in any of the above cited instruments and/or certificates of deposit or repurchase agreements fully collateralized by one or more of the above-cited instruments.

The Town maintains a cash and investment pool that is available for use by all funds. This pool is displayed on the balance sheet and the statement of net assets as cash and cash equivalents. Deposits and investments of governmental and proprietary funds are reported at fair value.

NOTE 3 CASH, CASH EQUIVALENTS AND INVESTMENTS (cont'd)

Deposits

Custodial Credit Risk

Custodial credit risk is the risk that in the event of a bank failure, the government's deposits may not be returned. The Town does not have a policy regarding custodial credit risk for deposits. At December 31, 2009, the carrying amount of the Town's deposits was $3,386,796 and the bank balance was $3,409,875. Of the bank balance, $250,000 was covered by federal depository insurance, and $3,159,875 was uninsured and collateralized with securities held by the pledging financial institution's trust department, but not in the Town's name.

NOTE 4 CAPITAL ASSETS

The capital asset activity for the year ended December 31, 2009 was as follows:

	Beginning Balance*	Increase	Decrease	Ending Balance
Governmental Activities:				
Capital assets not being depreciated:				
Land	$ 427,982	$ 5,934	$ -	$ 433,916
Total Capital Assets Not Being Depreciated	427,982	5,934	-	433,916
Capital assets being depreciated:				
Buildings	289,794	-	-	289,794
Improvements	130,997	-	-	130,997
Vehicles	574,349	16,813	109,824	481,338
Machinery and equipment	405,708	-	-	405,708
Total Capital Assets Being Depreciated	1,400,848	16,813	109,824	1,307,837
Accumulated depreciation:				
Buildings	98,775	6,795	-	105,570
Land Improvements	26,248	5,810	-	32,058
Vehicles	380,774	59,545	74,939	365,380
Machinery and equipment	309,917	28,627	-	338,544
Total Accumulated Depreciation	815,714	100,777	74,939	841,552
Total Capital Assets Being Depreciated, Net	585,134	(83,964)	34,885	466,285
Governmental Activities Assets, Net	$1,013,116	$ (78,030)	$ 34,885	$ 900,201
Business-type Activities:				
Capital assets being depreciated:				
Buildings and infrastructure	$4,127,138	$ -	$ -	$4,127,138
Vehicles	219,455	-	-	219,455
Machinery and equipment	94,379	-	-	94,379
Total Capital Assets Being Depreciated	4,440,972	-	-	4,440,972

* Restated for comparative purposes.

NOTE 4 CAPITAL ASSETS (cont'd)

	Beginning Balance*	Increase	Decrease	Ending Balance
Accumulated depreciation:				
Buildings and improvements	1,060,114	125,225	-	1,185,339
Vehicles	77,214	34,745	-	111,959
Machinery and equipment	3,979	9,040	-	13,019
Total Accumulated Depreciation	1,141,307	169,010	-	1,310,317
Business-type Activities Assets, Net	$3,299,665	$ (169,010)	$ -	$3,130,655

* Restated for comparative purposes.

Depreciation expense was charged to the functions as follows:

Governmental Activities:	
General government	$ 22,244
Public safety	47,048
Public works	31,485
Total Depreciation Expense - Governmental Activities	$ 100,777
Business-type Activities:	
Electric	$ 72,982
Water	96,028
Total Depreciation Expense - Business-type Activities	$ 169,010

NOTE 5 CHANGES IN COMPENSATED ABSENCES

	Beginning Balance*	Increase	Decrease	Ending Balance
Governmental Activities:				
Accumulated compensated absences	$ 26,543	$ 38,381	$ 26,782	$ 38,142
Business-type Activities:				
Accumulated compensated absences				
Electric	$ 7,570	$ 9,829	$ 9,051	$ 8,348
Sewer	14,059	18,254	16,809	15,504
	$ 21,629	$ 28,083	$ 25,860	$ 23,852

* Restated for comparative purposes.

NOTE 6 INTERFUND RECEIVABLES, PAYABLES, AND TRANSFERS

The composition of interfund balances as of December 31, 2009 is as follows:

Due To	Amount	Due From	Amount
Impact Fees Fund	$ 159,798	General Fund	$ 159,798
General Fund	1,625	SALLE Fund	1,625
Total	$ 161,423		$ 161,423

Interfund balances between funds represent temporary loans recorded at year end subsequent to a final allocation of expenses. The balances generally are paid shortly after year end.

The composition of interfund transfers for the year ended December 31, 2009 was as follows:

	Transfer In	Transfer Out
Impact Fees Fund	$ 208,181	$ -
General Fund	567,309	-
Electric Fund	-	599,273
Water and Sewer Fund	-	176,217
Total	$ 775,490	$ 775,490

Transfers from the electric fund and water and sewer funds to the impact fees fund and general fund were to subsidize those funds' operating activities.

NOTE 7 LONG-TERM DEBT

A schedule of changes in the long-term debt is as follows:

	Beginning Balance	Increases	Decreases	Ending Balance
Business-type Activities:				
Loan payable	$ 850,000	$ -	$ 32,484	$ 817,516

The loan payable is issued by the Delaware Department of Natural Resources and Environmental Control and administered by the Delaware Department of Health and Social Services to finance the arsenic removal project. The revolving loan converted to permanent financing on August 1, 2008 and bears interest at 3.72 percent payable on February 1 and August 1. The loan matures on August 1, 2028.

NOTE 7 LONG-TERM DEBT (cont'd)

Maturities of debt obligations, including interest, are as follows:

Year Ended December 31,	Principal	Interest	Total
2010	$ 33,373	$ 22,011	$ 55,384
2011	34,287	21,097	55,384
2012	35,227	20,157	55,384
2013	36,190	19,194	55,384
2014	37,182	18,202	55,384
2015-2019	201,754	75,166	276,920
2020-2024	230,932	45,988	276,920
2025-2028	208,571	12,966	221,537
	$ 817,516	$ 234,781	$ 1,052,297

NOTE 8 PENSIONS

Delaware County and Municipal Police/Firefighter Pension Plan

The Town contributes to the Delaware County and Municipal Police/Firefighter Pension Plan, which is a cost-sharing multiple-employer defined benefit plan administered by the Delaware Public Employees' Retirement System. The plan covers Town police employees hired on or after February 1, 1993. The plan provides retirement, disability and death benefits to plan members and beneficiaries. The contribution policy is set by State law and requires contributions by active members and participating employers. Plan members are required to contribute seven percent of base compensation. The contributions required of participating employers are based on an actuarial valuation and are expressed as a percentage of annual covered payroll during the period from which the amount is determined. The Town's contributions to the plan for the years ended December 31, 2009, 2008 and 2007 were $51,211, $46,559 and $32,508, respectively. The Delaware Public Employees' Retirement System issues a separate plan financial report that includes financial statements for the plan. That report may be obtained by writing to the State Board of Pension Trustees and Office of Pensions, McArdle Building, Suite No. 1, 860 Silver Lake Boulevard, Dover, Delaware 19904-2402.

State Employees' Pension Plan

The Town contributes to the State Employees' Pension Plan, which is a cost-sharing multiple-employer defined benefit plan administered by the Delaware Public Employees' Retirement System. The plan covers full-time or regular part-time employees. Benefit provisions of the plan are established under the provisions of State law and may be amended by an act of the State legislature. The plan provides retirement, disability and death benefits to plan

NOTE 8 PENSIONS (cont'd)

members and beneficiaries. The contribution policy is set by State law and requires contributions by active members and participating employers. Plan members are required to contribute three percent of total compensation that exceeds $6,000 per year. The contributions required of participating employers are based on an actuarial valuation and are expressed as a percentage of annual covered payroll during the period from which the amount is determined. The Town's contributions to the plan for the years ended December 31, 2009, 2008 and 2007 were $34,613, $24,125 and $22,958, respectively. The Delaware Public Employees Retirement System issues a separate plan financial report that includes financial statements of the plan. That report may be obtained by writing to the State Board of Pension Trustees and Office of Pensions, McArdle Building, Suite No. 1, 860 Silver Lake Boulevard, Dover, Delaware 19904-2402.

NOTE 9 COMMITMENTS AND CONTINGENCIES

Government Grants and Awards

The Town participates in state and county assisted grant programs. These programs are subject to program compliance audits by the grantors or their representatives. The Town is potentially liable for any expenditures which may be disallowed pursuant to the terms of these grant programs. Management is not aware of any material items of noncompliance which would result in the disallowance of program expenditures.

Delaware Municipal Electric Corporation

The Town is a member of the Delaware Municipal Electric Corporation ("DEMEC"). DEMEC is a public corporation constituted as a joint action agency and a wholesale electric utility. DEMEC was established in 1979 and represents nine municipal electric distribution utilities located in the State of Delaware. DEMEC provides full requirements wholesale electric power supply service to seven of the nine members, including the Town, through the operation of owned generation assets and various contractual wholesale supply contracts with external parties.

The Town purchases 100 percent of its electric supply requirements from DEMEC under a long-term full requirements service contract that became effective January 1, 2004 and which will remain in effect unless terminated upon one year's written notice by either party. The obligation of the Town to purchase and pay for full requirements service, including its allocated costs under any then current forward contract for capacity and energy between DEMEC and a third party in effect as of the date of notice of termination, shall survive the termination of this agreement.

NOTE 9 COMMITMENTS AND CONTINGENCIES (cont'd)

The Town has entered into a separate power sales agreement effective May 1, 2001 to purchase an interest in the capacity produced by Unit No. 1 of the Warren F. "Sam" Beasley Power Station located in Smyrna, Delaware, owned by DEMEC. The Town is entitled to a percentage of all power supply and ancillary products generated from the existing nominal 45 MW natural gas fired combustion turbine generator for the useful life of the facility.

Under the terms of the various agreements, DEMEC is authorized to act as agent for the Town in all matters relating to the acquisition and delivery of its wholesale power supply and management of energy cost risk on behalf of the Town in the deregulated energy markets.

NOTE 10 RISK MANAGEMENT

The Town maintains commercial insurance coverage for risk of losses relating to general, automotive, police professional, public officials and crime. There have been no significant changes in coverage, and there have been no losses above insurance limits during the past year.

NOTE 11 SUBSEQUENT EVENTS

The Town has evaluated all subsequent events through April 29, 2010, the date the financial statements were available to be issued.

REQUIRED SUPPLEMENTARY INFORMATION

TOWN OF CLAYTON
BUDGETARY COMPARISON SCHEDULE - GENERAL FUND
FOR THE YEAR ENDED DECEMBER 31, 2009

	Original and Final Appropriated Budget	Actual Amounts (Budgetary Basis)	Variance Positive (Negative)
REVENUES			
Taxes:			
Property taxes	$ 270,500	$ 262,825	$ (7,675)
Transfer taxes	220,000	174,147	(45,853)
Charges for services	269,200	252,248	(16,952)
Intergovernmental	105,861	40,244	(65,617)
Licenses and fees	18,850	6,359	(12,491)
Fines and forfeits	74,250	65,439	(8,811)
Franchise fees	12,000	15,097	3,097
Interest income	15,000	1,169	(13,831)
Miscellaneous	7,000	1,795	(5,205)
TOTAL REVENUES	992,661	819,323	(173,338)
EXPENDITURES			
Current:			
General government	808,816	439,951	368,865
Public safety	542,796	750,534	(207,738)
Public works	533,917	328,229	205,688
Licensing and inspection	43,175	58,700	(15,525)
Capital outlays	119,152	22,747	96,405
TOTAL EXPENDITURES	2,047,856	1,600,161	447,695
EXCESS (DEFICIENCY) OF REVENUES OVER (UNDER) EXPENDITURES	(1,055,195)	(780,838)	274,357
OTHER FINANCING SOURCES			
Proceeds from sale of capital assets	-	16,294	16,294
Transfers in	-	567,309	567,309
TOTAL OTHER FINANCING SOURCES	-	583,603	583,603
NET CHANGE IN FUND BALANCE	(1,055,195)	(197,235)	857,960
FUND BALANCE, BEGINNING OF YEAR	938,089	938,089	-
FUND BALANCE, END OF YEAR	$ (117,106)	$ 740,854	$ 857,960

* Restated for comparative purposes.

COMBINING NONMAJOR FUND STATEMENTS

TOWN OF CLAYTON
COMBINING BALANCE SHEET - NONMAJOR GOVERNMENTAL FUNDS
DECEMBER 31, 2009

	Municipal Street Aid Fund	S.A.L.L.E. Fund	E.I.D.E. Fund	Seized Asset/ Illegal Drug Enforcement Fund	Total
ASSETS					
Cash and cash equivalents	$ 108,412	$ 3,054	$ 4,255	$ 424	$ 116,145
TOTAL ASSETS	$ 108,412	$ 3,054	$ 4,255	$ 424	$ 116,145
LIABILITIES AND FUND BALANCES					
Accounts payable	$ -	$ 1,424	$ -	$ -	$ 1,424
Due to other funds	-	1,625	-	-	1,625
TOTAL LIABILITIES	-	3,049	-	-	3,049
FUND BALANCES					
Unreserved, designated for:					
Police expenditures	-	5	4,255	424	4,684
Public works expenditures	108,412	-	-	-	108,412
TOTAL FUND BALANCES	108,412	5	4,255	424	113,096
TOTAL LIABILITIES AND FUND BALANCES	$ 108,412	$ 3,054	$ 4,255	$ 424	$ 116,145

TOWN OF CLAYTON
COMBINING STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES - NONMAJOR GOVERNMENTAL FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2009

	Municipal Street Aid Fund	S.A.L.L.E. Fund	E.I.D.E. Fund	Seized Asset/ Illegal Drug Enforcement Fund	Total
REVENUES					
Intergovernmental	$ -	$ 4,790	$ 7,353	$ 10,440	$ 22,583
Interest income	132	-	-	-	132
TOTAL REVENUES	132	4,790	7,353	10,440	22,715
EXPENDITURES					
Current:					
Public safety	31,176	4,790	6,720	11,645	54,331
TOTAL EXPENDITURES	31,176	4,790	6,720	11,645	54,331
CHANGE IN FUND BALANCES	(31,044)	-	633	(1,205)	(31,616)
FUND BALANCES, BEGINNING OF YEAR	139,456	5	3,622	1,629	144,712
FUND BALANCES, END OF YEAR	$ 108,412	$ 5	$ 4,255	$ 424	$ 113,096

OTHER REPORTS

200 Springer Building
3411 Silverside Road
Wilmington, Delaware 19810
302.478.8940

FAX: 302.477.1607
www.btcpa.com

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*

April 29, 2010

To the Honorable Mayor and Town Council
Town of Clayton
Clayton, Delaware

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 Clayton, Clayton, Delaware, as of and for the year ended December 31, 2009, which collectively comprise the Town's basic financial statements, and have issued our report thereon dated April 29, 2010.

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 Clayton'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 Clayton's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Town's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. However, as discussed below, we identified certain deficiencies in internal control over financial reporting that we consider to be significant deficiencies.

A control deficiency exists when a design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the Town's ability to initiate, authorize, record, process or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the Town's financial statements that is more than inconsequential will not be prevented or detected by the Town's internal control. We

BARBACANE THORNTON & COMPANY
CERTIFIED PUBLIC ACCOUNTANTS

consider the deficiencies described in the accompanying schedule of findings and recommendations as items #06-1, #06-2, #08-1, #08-2, #09-1 and #09-2 to be significant deficiencies in internal control over financial reporting.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the Town's internal control.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, the significant deficiencies described in the accompanying schedule of findings and recommendations as items #06-1, #06-2, #08-1 and #09-1 are considered to be material weaknesses.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Town of Clayton'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*.

We also noted certain matters that we reported to management of the Town of Clayton in a separate letter dated April 29, 2010.

The Town of Clayton, Clayton, Delaware's response to the findings identified in our audit is described in the accompanying schedule of findings and recommendations. We did not audit the Town of Clayton's response and, accordingly, we express no opinion on it.

This report is intended solely for the information and use of the Mayor, Town Council and management, and is not intended to be and should not be used by anyone other than these specified parties.

Barbacane, Thornton & Company

BARBACANE, THORNTON & COMPANY

TOWN OF CLAYTON

SCHEDULE OF FINDINGS AND RECOMMENDATIONS

STATUS OF PRIOR YEAR FINDINGS

06-1 FINANCIAL REPORTING

Condition: The Town does not report financial data reliably in accordance with generally accepted accounting principles. Reporting deficiencies noted during our audit procedures are as follows:

- The Town does not maintain financial data on a fund-based presentation. Authoritative accounting and financial reporting standards for state and local governments require that financial statements be accompanied by a fund-based presentation. A fund is a separate, self-balancing set of accounts used to account for resources that are segregated for specific purposes in accordance with special regulations, restrictions or limitations.

- The Town lacks employees or management who have the qualifications and training to apply generally accepted accounting principles to the Town's financial transactions or in the preparation of its financial statements. As a result, the Town relies on its auditor to record adjusting journal entries, maintain certain subsidiary ledgers and draft audited financial statements in accordance with generally accepted accounting principles.

Criteria: The Governmental Accounting Standards Board requires the financial reporting of governments to be in accordance with generally accepted accounting principles.

Cause: Lack of oversight by the Town Council and management over the financial reporting requirements necessary to comply with generally accepted accounting principles.

Effect: The Town's current financial reporting structure does not allow for the Town to initiate, process or report financial data in accordance with generally accepted accounting principles.

Recommendation: The Town needs to evaluate its current financial reporting structure given the state of growth it is currently experiencing. Management and the Town Council need to take appropriate measures in respect to the above-noted deficiencies in financial reporting. We recommended that the Town explore the cost benefit of employing the services of a person or outside agency with the necessary background and knowledge to consistently apply generally accepted accounting principles to the financial data of the Town.

Status: During our current year audit, we noted that the Town still does not maintain financial data on a fund-based presentation as of December 31, 2009. In addition, the Town continued to rely on its auditor to record adjusting journal entries and draft financial statements in accordance with generally accepted accounting principles. Currently, the Town is evaluating the above-noted deficiencies to determine a cost-effective approach to resolve each deficiency given the current organizational structure of the Town.

Corrective Action Plan: The Town currently contracts with an outside individual to prove and close out its books on a monthly basis. Management will explore the option of retaining this same individual to record adjusting entries prior to the Town's being audited.

STATUS OF PRIOR YEAR FINDINGS

06-2 LACK OF SEGREGATION OF DUTIES AND INTERNAL CONTROL-RELATED ISSUES

Condition: The current structure of the Town's operations does not employ proper segregation of duties or internal controls. Deficiencies noted during our audit procedures include, but are not limited to, the following:

- Mail is opened and cash receipts are listed by personnel having access to cash receipts and accounts receivable records.
- The general cashier function is not segregated from the general ledger and subsidiary ledger functions.
- Supporting documentation does not accompany checks when presented for signature.
- Only one authorized signature is required for all checks. Dual signatures should be required on all checks over a specific amount.
- Custody of checks after signature and before mailing are handled by someone who is not independent of all payable, disbursing, cash, receiving and general ledger functions.
- Bank reconciliations are prepared by someone who is not independent of the cash receipts and disbursements functions.
- Completed bank reconciliations are not reviewed by a responsible member of management or Town official.
- The billing function is not separate from the collection function.
- Approval of payment and account distribution is not clearly indicated on the face of paid invoices.
- Personnel in the payables function are not independent of purchasing, disbursing and general ledger functions.
- The person preparing the payroll is not independent of other payroll duties (e.g., timekeeping, distribution of checks) and has access to other payroll data.
- Payroll is not subject to final approval before payment by someone independent of payroll preparation and timekeeping.
- Journal entries are not supported by adequate documentation or approval by a responsible member of management or a Town official.

Criteria: Proper internal controls promote efficiency, reduce risk of asset loss and help to ensure the reliability of financial reporting.

Cause: Lack of oversight by the Town Council and management relevant to the internal control structure of the Town.

Effect: Material misstatements in relation to the financial reporting of the Town caused by error or fraud may occur and not be detected within a timely period by employees or Town officials in the normal course of performing their assigned functions.

STATUS OF PRIOR YEAR FINDINGS

Recommendation: Segregation of duties and the implementation of proper internal controls normally is difficult to accomplish within a small organization, but management and Town officials should be sensitive to areas that can be improved upon. Sometimes the cost outweighs the benefit of implementation depending on the size and structure of the organization. We recommended that management and the Town Council review the above-noted deficiencies and the current assignment of accounting functions. Where possible, duties should be segregated and internal controls set in place to help mitigate the risk of errors and fraud.

Status: The following lack of segregation of duties and internal control-related issues have been addressed by the Town based on our current year auditing procedures:

- Supporting documentation accompanies all checks for signature.
- Bank reconciliations are being reviewed by a responsible member of management.
- Approval of payment and account distribution are being clearly indicated on the face of paid invoices.
- Completed bank reconciliations are reviewed by a responsible member of management or Town official.
- Payroll is subject to final approval before payment by someone independent of payroll preparation and timekeeping.

The remaining lack of segregation of duties and internal control-related issues noted during our prior year audit are still applicable based on our current year auditing procedures. We continue to recommend that management and the Town Council evaluate each noted deficiency to determine whether the cost of implementation outweighs the benefits based on the Town's current organizational structure.

Corrective Action Plan: The Town of Clayton is a very small municipality. Many of these deficiencies have already been addressed with the change of personnel. Segregation of certain duties is difficult. The Town has put in place several checks and balances. Checks over $2,000 are signed by two Council members. Payroll and accounts payable checks are presented to a Council member for review and signed by those with signature privileges.

08-1 CREDIT CARD RECEIPTS AND USAGE

Condition: The Town pays credit card invoices that are not supported by receipts and/or are made up of personal expenses.

Criteria: The Town should be paying invoices related to Town expenditures only.

Cause: Lack of oversight by the Town Council and management over the monitoring of credit card payments.

Effect: Without supporting documentation or evidence of a personal expense, there is a risk of overstatement of expenditures on the Town's financial statements or fraudulent activity by an employee(s).

STATUS OF PRIOR YEAR FINDINGS

Recommendation: The Town needs to evaluate its current credit card policy. Management and the Town Council need to take appropriate measures in respect to the above-noted deficiency. We recommended that the Town require a receipt for all credit card expenses. We further recommended that procedures be adopted to identify personal expenditures when they are incurred and to charge them back to the employees.

Status: During our current year audit, we noted that there were expenditures that did not have the proper supporting documentation and/or have been deemed personal expenses. The personal expenses have been repaid as evidenced through additional testing. However, with the lack of supporting documentation for other credit card expenditures paid by the Town in 2009, this finding is still applicable for the current year.

Corrective Action Plan: The Town has adopted a credit card policy. With the change of personnel, all receipts are collected and verified that they are qualified expenses.

08-2 FRAUD RISK ASSESSMENT

Condition: The Town does not have a risk assessment process in place.

Criteria: In light of the spate of notorious frauds involving large organizations in prior years, there may be a misperception that fraud affects only large organizations. However, fraud occurs in organizations of all sizes, and almost any employee may be capable of perpetrating a fraudulent act given the right set of circumstances. In fact, fraud may be a more significant problem for small companies.

Cause: Lack of oversight by the Town Council and management over the assessment of fraud risks.

Effect: Whereas the highly publicized frauds at large public companies involved fraudulent financial reporting, for small organizations, one of the primary fraud risks is the ever-present risk of misappropriation of assets (theft), particularly fraudulent cash disbursements. The opportunity to commit and conceal fraud exists where there are assets susceptible to misappropriation and inadequate controls to prevent or detect the fraud.

Recommendation: We recommended that the Town perform a risk assessment to identify, analyze and manage the risk of asset misappropriation. Risk assessment, including fraud risk assessment, is one element of internal control. Thus, ideally, the Town's internal control should include performance of this assessment, even though our annual financial statement audits include consideration of fraud. The fraud risk assessment can be informal and performed by a management-level individual who has extensive knowledge of the Town that might be used in the assessment. Ordinarily, the management-level individual would conduct interviews or lead group discussions with personnel who have extensive knowledge of the Town, its environment (including industry and country-specific characteristics), and its processes. The fraud risk assessment process should consider the Town's vulnerability to misappropriation of assets. When conducting the self-assessment, questions such as the following can be considered:

STATUS OF PRIOR YEAR FINDINGS

- *What Individuals in the Town Have the Opportunity to Misappropriate Assets?* These are individuals who have access to assets susceptible to theft and to records that can be falsified or manipulated to conceal the theft.

- *Are There Any Known Pressures That Would Motivate Employees with the Opportunity to Misappropriate Assets?* Pressures may relate to financial stress or dissatisfaction. In assessing whether these pressures may exist, the assessor should consider whether there is any information that indicates potential financial stress or dissatisfaction of employees with access to assets susceptible to misappropriation.

- *What Assets of the Town Are Susceptible to Misappropriation?*

- *Are There Any Known Internal Control Weaknesses That Would Allow Misappropriation of Assets to Occur and Remain Undetected?*

- *How Could Assets Be Stolen?* Assets can be stolen in many ways besides merely removing them from the premises. For example, cash can be stolen by writing checks to fictitious employees or vendors and cashing them for personal use. Inventory or other assets can be stolen through sales to fictitious customers. Assets can also be stolen by unauthorized trading in securities.

- *How Could Potential Misappropriation of Assets Be Concealed?* Because many frauds create accounting anomalies, the perpetrator must hide the fraud by running through an adjustment to another account. Generally, fraud perpetrators may use accounts that are not closely monitored (for example, fixed assets, inventory and consulting expenses).

- *What Factors Might Indicate That the Town Has a Culture or Environment That Would Enable Management or Employees to Rationalize Committing Fraud?*

Status: During our current year audit, we noted that the Town had not yet implemented a process for fraud risk assessment. This finding is still applicable for the current year.

Corrective Action Plan: The Town has adopted an identity theft program in 2009. Currently, management records assets of $5,000 or more in an asset program. When removed, a disposal form is completed and signed off on. The Council will review a risk assessment process for the Town.

CURRENT YEAR FINDINGS AND RECOMMENDATIONS

09-01 YEAR-END CLOSING PROCEDURES

Condition: The Town did not have the financial records ready prior to the commencement of the audit. We made several journal entries to accrue liabilities, to reclassify capital outlays, to record debt payments and to record transfers between funds.

STATUS OF PRIOR YEAR FINDINGS

Criteria: As described in Statement of Auditing Standards (SAS) No. 115, "Communicating Internal Control- Related Matters Identified in an Audit," the auditor is required to report to those charged with governance any deficiencies in internal control identified during the audit. Specifically, deficiencies in "controls over the period-end financial reporting process, including controls over procedures used to initiate, authorize, record and process journal entries into the general ledger" are to be reported.

Cause: Lack of procedures established for the completion of year-end closing procedures.

Effect: When the auditor is making the journal entries as well as conducting the audit, the perception of independence may arise.

Recommendation: We recommend that the Town establish and implement procedures for conducting year-end closing procedures, such as making journal entries to accrue liabilities, to reclassify capital outlays, to book debt payments and to record transfers of funds prior to the commencement of the audit.

Corrective Action Plan: With the change of personnel and duties in December 2009, the new staff did not receive the year-end closing procedures. The procedures will be written out to be followed for next year's audit.

09-02 CUSTODIAL CREDIT RISK

Condition: The Town does not have a policy regarding custodial credit risk.

Criteria: Custodial credit risk is the risk that in the event of a bank failure, the Town's deposits may not be returned. Accounts at these financial institutions are insured by the Federal Deposit Insurance Corporation ("FDIC") up to $250,000. The Town has not experienced any losses related to these accounts and believes it is not exposed to any significant credit risk.

Cause: No policy approved and implemented to identify custodial credit risk and limitations regarding the total amount of funds held in one financial institution.

Effect: Deposits in excess of the FDIC limits are exposed to credit risk.

Recommendation: We recommend that the Town approve and implement a policy regarding custodial credit risk.

Corrective Action Plan: The Town currently has its bank account in an institution that is FDIC insured. Management has a letter on file stating that the Town has collateralized funds for a majority of its accounts. The Town currently is exploring its options as to other banking institutions. The Council will look into a custodial credit risk policy.