

**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**

September 25, 2009

To the Board of Directors of  
Hudson River-Black River Regulating District:

We have audited the financial statements of the business type activities of the Hudson River-Black River Regulating District (the Regulating District), as of and for the year ended June 30, 2009 which collectively comprise the Regulating District's basic financial statements, and have issued our report thereon dated September 25, 2009. 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 Regulating District'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 Regulating District's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Regulating District's internal control over financial reporting.

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

A *control deficiency* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A *significant deficiency* is a control deficiency, or combination of control deficiencies, that adversely affects the Regulating District'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 Regulating District's financial statements that is more than inconsequential will not be prevented or detected by the Regulating District's internal control. We consider the deficiency described below to be a significant deficiency in internal control over financial reporting.

**Finding 2009-01 – Capitalization of Assets**

*Condition:* Certain asset additions and improvements were expensed rather than capitalized in accordance with the Regulating District's policies.

*Criteria:* In order to comply with generally accepted accounting principles, assets purchased which improve the useful life of an existing asset should be capitalized.

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(Continued)

**Internal Control Over Financial Reporting (Continued)**

**Finding 2009-01 - Capitalization of Assets (Continued)**

*Effect:* The Regulating District recorded a material adjustment of approximately \$312,000 to capitalize assets related to the Conklingville Dam Intake Repair Construction Project and the Conklingville Dam Geotechnical Investigation Contract.

*Cause:* The existing controls at the Regulating District were not sufficient to identify the error had occurred.

*Recommendation:* We recommend that the Regulating District review its year-end closing procedures to ensure all assets have been capitalized.

*Management Response:* The aforementioned adjustment represents two capital projects, Geotechnical Investigation (\$59,955) and Dam Intake Repair Construction (\$252,045) that were originally budgeted as repairs to structures (expense), then subsequently reclassified as capital improvements (capital asset). However, the journal entry to move the applicable expenses was not made. The Regulating District has revised its year-end closing review to include the verification that capital improvement projects are in fact journalized properly.

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 Regulating District's internal control.

Our consideration of the 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 we consider the significant deficiency described above (Finding 2009-01) to be a material weakness.

**Compliance and Other Matters**

As part of obtaining reasonable assurance about whether the Regulating District'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 noted certain other matters that we reported to management of the Regulating District in a separate letter dated September 2009.

The Regulating District's response to the finding identified in our audit is described above. We did not audit the Regulating District's response and, accordingly, we express no opinion on it.

This report is intended solely for the information and use of management, the audit committee, Board of Directors, and others within the entity and is not intended to be and should not be used by anyone other than these specified parties. However, this report is a matter of public record and its distribution is not limited.