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NORTH MCLEAN COUNTY WATER DISTRICT

AUDIT REPORT

FOR THE YEARS ENDED
DECEMBER 31, 2018 AND 2017

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Board of Commissioners
North McLean County Water District
McLean County, Kentucky

Independent Auditor's Report

Report on the Financial Statements

We have audited the accompanying statements of net position of North McLean County Water District as of December 31, 2018 and 2017, and the related statements of revenue and expenses and changes in net position, and cash flows, and the related notes to the financial statements, for the years then ended.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express opinions on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness

of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of North McLean County Water District as of December 31, 2018 and 2017, and the changes in financial position and cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Management has omitted management's discussion and analysis that accounting principles generally accepted in the United States of America require to be presented to supplement the financial statements. Such missing information, although not part of the financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the financial statements in an appropriate operational, economic, or historical context. Our opinions on the financial statements are not affected by this missing information.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated May 1, 2019 on our consideration of North McLean County Water District's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is solely 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 effectiveness of North McLean County Water District's internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering North McLean County Water District's internal control over financial reporting and compliance.

Dover and Morris, PLLC

May 1, 2019

NORTH MCLEAN COUNTY WATER DISTRICT
STATEMENTS OF NET POSITION
December 31, 2018 and 2017

ASSETS	2018	2017
CURRENT ASSETS		
Cash in bank	\$ 182,703	\$ 193,198
Customer deposit checking	48,067	43,642
Certificates of deposit	181,189	173,547
Accounts receivable	56,676	55,145
AquaLine collection fee receivable	115	-
Due from other governments	48,927	451
Inventory	32,110	33,063
Interest receivable	431	260
Prepaid insurance	7,021	6,743
TOTAL CURRENT ASSETS	557,239	506,049
NONCURRENT ASSETS		
Restricted Assets:		
Sinking fund reserve	-	46,472
Replacement and extension fund	-	42,880
Capital Assets:		
Utility plant	3,712,227	3,414,403
Accumulated depreciation	(1,308,259)	(1,256,797)
Other assets:		
Refundable electric contract	3,412	-
TOTAL NONCURRENT ASSETS	2,407,380	2,246,958
TOTAL ASSETS	2,964,619	2,753,007
LIABILITIES AND NET POSITION		
CURRENT LIABILITIES		
Accounts payable	119,362	29,291
AquaLine payable	955	909
Accrued wages	4,205	-
Taxes payable	6,274	7,078
Employee IRA withholding	296	355
Accrued interest payable	418	4,956
Customer deposits	3,600	3,200
Bonds payable	-	12,000
Note payable	8,672	-
TOTAL CURRENT LIABILITIES	143,782	57,789
NONCURRENT LIABILITIES		
7 5/8% Revenue Bond, Series 1985	-	118,000
Note payable	41,968	-
Customer deposits	35,875	33,315
TOTAL NONCURRENT LIABILITIES	77,843	151,315
TOTAL LIABILITIES	221,625	209,104
NET POSITION		
Net investment in capital assets	2,261,470	2,027,606
Restricted for debt requirements	-	56,000
Unrestricted	481,524	460,297
TOTAL NET POSITION	\$ 2,742,994	\$ 2,543,903

The notes to the financial statements are an integral part of these statements.

NORTH MCLEAN COUNTY WATER DISTRICT
STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN NET POSITION
December 31, 2018 and 2017

	<u>2018</u>	<u>2017</u>
OPERATING REVENUES		
Water sales	\$ 706,771	\$ 631,818
Penalties and miscellaneous	<u>27,020</u>	<u>20,983</u>
TOTAL OPERATING REVENUES	<u>733,791</u>	<u>652,801</u>
OPERATING EXPENSES		
Salaries and wages	224,751	212,615
Employee benefits	9,277	-
Depreciation	66,764	65,081
Purchased water	339,762	340,812
Purchased power	6,855	6,367
Materials and supplies	40,500	33,324
Contractual services	29,374	31,930
Rents	2,040	2,040
Transportation expenses	13,974	13,795
Insurance	13,732	12,497
Miscellaneous	4,351	1,361
Advertising	582	884
Taxes	<u>18,726</u>	<u>18,130</u>
TOTAL OPERATING EXPENSES	<u>770,688</u>	<u>738,836</u>
OPERATING INCOME (LOSS)	<u>(36,897)</u>	<u>(86,035)</u>
NON-OPERATING REVENUES (EXPENSES)		
Gain on sale of assets	-	4,346
Interest income	6,016	4,025
Interest expense	<u>(3,313)</u>	<u>(10,148)</u>
TOTAL NON-OPERATING REVENUES (EXPENSES)	<u>2,703</u>	<u>(1,777)</u>
CHANGE IN NET POSITION BEFORE CONTRIBUTIONS	<u>(34,194)</u>	<u>(87,812)</u>
CAPITAL CONTRIBUTIONS	<u>233,285</u>	<u>9,460</u>
CHANGE IN NET POSITION	<u>199,091</u>	<u>(78,352)</u>
NET POSITION- BEGINNING	<u>2,543,903</u>	<u>2,622,255</u>
NET POSITION- ENDING	<u><u>\$ 2,742,994</u></u>	<u><u>\$ 2,543,903</u></u>

The notes to the financial statements are an integral part of these statements.

NORTH MCLEAN COUNTY WATER DISTRICT
STATEMENTS OF CASH FLOWS
For the Years Ended December 31, 2018 and 2017

	2018	2017
Cash Flows from Operating Activities		
Receipts from customers	\$ 728,141	\$ 653,454
Other receipts	6,965	6,222
Payments to suppliers	(472,388)	(487,749)
Payments to employees	(232,671)	(212,615)
Net cash provided (used) by operating activities	<u>30,047</u>	<u>(40,688)</u>
Cash Flows from Noncapital Financing Activities		
Net cash provided(used) by noncapital financing activities	<u>-</u>	<u>-</u>
Cash Flows from Capital & Related Financing Activities		
Proceeds from sale of capital assets	-	7,269
Purchase of capital assets	(221,269)	(22,259)
Principal paid on bonds	(130,000)	-
Loan proceeds	119,430	-
Principal paid on loan	(68,790)	-
Interest paid	(7,851)	(5,192)
Capital contributions	184,809	9,460
Net cash provided (used) by capital & related financing activities	<u>(123,671)</u>	<u>(10,722)</u>
Cash Flows from Investing Activities		
Decrease(increase) in certificates of deposit	23,924	(2,021)
Interest on investments	5,845	4,025
Net cash provided (used) by investing activities	<u>29,769</u>	<u>2,004</u>
Net increase (decrease) in cash & cash equivalents	(63,855)	(49,406)
Balances- Beginning of year	294,625	344,031
Balances- End of year	<u>\$ 230,770</u>	<u>\$ 294,625</u>
Reconciliation of Operating Income (Loss) to Net Cash Provided (Used) By Operating Activities:		
Operating income (loss)	\$ (36,897)	\$ (86,035)
Adjustments to reconcile operating income (loss) to net cash provided (used) by operating activities:		
Depreciation expense	66,764	65,081
(Increase) decrease in:		
Accounts and other receivables	(1,645)	3,365
Inventories	953	(876)
Prepaid insurance	(278)	930
Refundable electric contract	(3,412)	-
Increase (decrease) in:		
Accounts payable	(1,786)	(26,229)
AquaLine payable	46	909
Accrued wages	4,205	-
Taxes payable	(804)	(1,524)
Employee IRA withholding	(59)	181
Customer deposits	2,960	3,510
Net cash provided (used) by operating activities	<u>\$ 30,047</u>	<u>\$ (40,688)</u>
Noncash Investing, Capital, and Financing Activities:		
Construction in progress in accounts payable	\$ 91,858	\$ -
Capital grant in due from other governments	\$ 48,476	\$ -

The notes to the financial statements are an integral part of these statements.

NORTH MCLEAN COUNTY WATER DISTRICT
NOTES TO FINANCIAL STATEMENTS
For the Years Ended December 31, 2018 and 2017

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

North McLean County Water District is a Kentucky water district that was organized in 1971. McLean County Fiscal Court appoints the Board of Commissioners that manages the water district. The Water District's financial statements are prepared in accordance with generally accepted accounting principles (GAAP). The Governmental Accounting Standards Board (GASB) is responsible for establishing GAAP for state and local governments through its pronouncements (statements and interpretations).

REPORTING ENTITY

In evaluating how to define the District for financial reporting purposes, management has considered all potential component units. The decision to include a potential component unit in the reporting entity was made by applying the criteria set forth in GAAP. The basic- but not the only- criterion for including a potential component unit within the reporting entity is the governing body's ability to exercise oversight responsibility. The most significant manifestation of this ability is financial interdependency. Other manifestations of the ability to exercise oversight responsibilities include, but are not limited to the selection of governing authority, the designation of management, the ability to significantly influence operations and accountability for fiscal matters. The other criterion used to evaluate potential component units for inclusion or exclusion from the reporting entity is the existence of special financing relationships, regardless of whether the District is able to exercise oversight responsibilities. Based upon the application of these criteria, there are no component units required to be reported by the District.

PROPRIETARY FUND ACCOUNTING

The activities of the Water District are similar to those found in the private sector. Proprietary fund 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 when the related cash flows take place. Revenue from grants, entitlements, and donations is recognized in the fiscal year in which all eligibility requirements have been satisfied.

Proprietary funds distinguish operating revenues and expenses from non-operating revenues and expenses. Operating revenues and expenses generally result from providing services in connection with a proprietary fund's principal ongoing operations. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

INVENTORY

Inventory is stated at cost determined on a "first-in, first-out basis." Inventory consists mainly of supplies to be used for future repair and maintenance.

UTILITY PLANT IN SERVICE

Capital assets purchased or acquired with an original cost of \$500 or more are reported at historical cost. Contributed assets are reported at acquisition value as of the date received. Depreciation has been provided using the straight line method. Pumping, distribution equipment, and meters are being depreciated over a 20 to 40 year life. The transmission lines are being depreciated over a 60 to 80 year life and tanks are being depreciated over a 40 to 60 year life. Vehicles and other equipment are depreciated over 5 to 15 years.

CONTRIBUTION IN AID OF CONSTRUCTION

With approval of the water district, customers have in some cases constructed their own water lines and donated them to the district for future maintenance, control, etc. Those assets have been recorded on the water district's books and are being depreciated under the same policy as other assets.

NORTH MCLEAN COUNTY WATER DISTRICT
NOTES TO FINANCIAL STATEMENTS
For the Years Ended December 31, 2018 and 2017

The water district has implemented GASB Statement No. 33, which requires capital contributions to be recognized as revenue effective for periods beginning after June 15, 2000.

CASH AND EQUIVALENTS

For purposes of the statements of cash flows, the district considers all highly liquid debt instruments purchased with a maturity of three months or less to be cash equivalents. Below is a reconciliation of cash on the statements of net position to cash on the statements of cash flows.

	2018	2017
Cash in bank	\$ 182,703	\$ 193,198
Customer deposit checking	48,067	43,642
Sinking fund reserve	-	19,938
Replacement fund	-	37,847
	<u>\$ 230,770</u>	<u>\$ 294,625</u>

CASH AND INVESTMENTS

Cash includes amounts in bank accounts. The only investments include certificates of deposit. These investments are reported at cost, which reasonably estimates fair value.

KRS 66.480 authorizes the district to invest in the following, including but not limited to, obligations of the United States and of its agencies and instrumentalities, obligations and contracts for future delivery or purchase of obligations backed by the full faith and credit of the United States, obligations of any corporation of the United States government, bonds or certificates of indebtedness of this state, and certificates of deposit issued by or other interest-bearing accounts of any bank or savings and loan institution which are insured by the Federal Deposit Insurance Corporation (FDIC) or which are collateralized, to the extent uninsured, by any obligation permitted by KRS 41.240(4).

ESTIMATES

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. Actual results could differ from those estimates.

COMPENSATED ABSENCES

The District does not allow employees to accumulate unused personal or vacation days. Sick leave is earned at the rate of one day per month with a maximum accumulation of sixty days. Sick leave may only be used pursuant to a doctor's excuse and may not be converted to cash. No liability has been recorded in the accompanying financial statements. The District's policy is to recognize the cost of compensated absences when paid to employees.

CAPITALIZED INTEREST

The District capitalizes net interest cost as part of the cost of constructing various utility projects when material. All interest was expensed since no construction projects were financed during the current year.

ACCOUNTS RECEIVABLE

The District has not provided for an allowance for bad debts. It is management's opinion based on prior history that any uncollectible accounts would have no significant effect on the financial statements. Uncollectible accounts are written off annually directly to sales. Bad debt expense was \$4,105 for 2018 and \$3,019 for 2017.

NORTH MCLEAN COUNTY WATER DISTRICT
NOTES TO FINANCIAL STATEMENTS
For the Years Ended December 31, 2018 and 2017

2. DEPOSITS AND INVESTMENTS

A. Deposits

The District maintains deposits with depository institutions insured by the Federal Deposit Insurance Corporation (FDIC). According to law, the depository institution should pledge sufficient securities as collateral which, together with FDIC insurance equals or exceeds the amount on deposit at all times. In order to be valid against the FDIC in the event of failure or insolvency of the depository institution, this pledge of securities should be evidenced by an agreement that is (a) in writing, (b) approved by the board of directors of the depository institution or its loan committee, which approval must be reflected in the minutes of the board or committee, and (C) an official record of the depository institution. This agreement, signed by both parties, must be sufficient to create an enforceable and perfected security interest in the collateral under Kentucky law.

Custodial Credit Risk - Deposits

Custodial credit risk is the risk that in the event of a depository institution failure, the government's deposits may not be returned to it. The District does not have a deposit policy for custodial credit risk but rather follows the requirements of KRS 41.240 (4). As of December 31, 2018 all deposits including the certificates of deposit held as investments were covered by FDIC insurance or a properly executed collateral security agreement.

B. Investments

As of December 31, 2018, the District had the following investment:

<u>Investment</u>	<u>Maturity</u>	<u>Fair Value (Cost)</u>
Certificates of Deposit	Greater than 90 days	\$ 181,189

Interest Rate Risk

The District does not have a formal investment policy that limits its investment maturities as a means of managing its exposure to losses arising from changes in interest rates. In general, non-negotiable certificates of deposit are not subject to interest rate risk.

Credit Risk

KRS 66.480 limits the District's investments in the following: obligations of the United States and of its agencies and instrumentalities, including obligations subject to repurchase agreements, obligations and contracts for future delivery or purchase of obligations backed by the United States or its agencies and obligations of any corporation of the United States Government. Certificates of deposit issued by or other interest-bearing accounts of any bank or savings and loan institution insured by the Federal Deposit Insurance Corporation or similar entity. Uncollateralized certificates of deposit issued by a bank or savings and loan institutions rated in one of the three highest categories by a nationally recognized rating agency. Bankers' acceptances for banks rated in one of the three highest categories by a nationally recognized rating agency. Commercial paper rated in the highest category by a nationally recognized rating agency. Bonds or certificates of indebtedness of this state and of its agencies and instrumentalities, securities issued by a state or local government, or any instrumentality or agency thereof, in the United States and rated in one of the three highest categories by a nationally recognized rating agency. Shares of mutual funds meeting specific characteristics outlined in the statute shall be eligible investments. Also, the District is limited to investing no more than 20% in any one of the preceding investments as allowed by KRS 66.480. The District had no investment policy that would further limit its investments choices. In general, non-negotiable certificates of deposit are not subject to investment credit risk.

NORTH MCLEAN COUNTY WATER DISTRICT
NOTES TO FINANCIAL STATEMENTS
For the Years Ended December 31, 2018 and 2017

3. RESTRICTED ASSETS

Under the terms of the revenue bond ordinances, certain funds were created to set aside money for future bond payments. The funds that were created and a brief description follows:

Replacement and Extension Fund- Monthly transfers will be made in the amount of \$125.00 until the sum of \$32,000.00 is accumulated.

1985 Sinking Fund- Monthly transfers will be made to equal the next bond and interest payment until the sum of \$24,000.00 is accumulated.

Once the bonds were paid in full during 2018, these accounts were no longer required to be maintained.

When restricted and unrestricted resources are available for use, it is the district's policy to use restricted resources first.

A summary of the changes in restricted assets is as follows:

	1985 Sinking Fund	Reserve Replacement Fund
BALANCE, JANUARY 1, 2017	\$ 30,549	\$ 41,297
CASH RECEIPTS		
Transfers from operations	20,681	1,500
Interest income	198	240
CASH DISBURSEMENTS		
Correct prior year deposit error	-	157
Bond interest payments	4,956	-
BALANCE, DECEMBER 31, 2017	46,472	42,880
CASH RECEIPTS		
Transfers from operations	2,324	125
Interest income	46	61
CASH DISBURSEMENTS		
Transferred to unrestricted cash	5,125	5,032
Loan principal payment	26,564	38,034
Bond principal and interest payment	17,153	-
BALANCE, DECEMBER 31, 2018	\$ -	\$ -

NORTH MCLEAN COUNTY WATER DISTRICT
NOTES TO FINANCIAL STATEMENTS
For the Years Ended December 31, 2018 and 2017

4. PROPERTY AND EQUIPMENT

A summary of the property and equipment as of December 31, 2018 and 2017, is as follows:

	Jan. 1 2017	Increases	Decreases	Dec. 31 2017
Capital assets not being depreciated:				
Land	\$ 17,186	\$ -	\$ -	\$ 17,186
Construction in progress	1,500	-	1,500	-
Total capital assets not being depreciated	18,686	-	1,500	17,186
Capital assets being depreciated:				
Buildings and improvements	166,876	-	-	166,876
Equipment	189,754	1,376	2,028	189,102
Water distribution system	2,976,189	22,381	13,063	2,985,507
Vehicles	55,812	-	80	55,732
Total capital assets being depreciated	3,388,631	23,757	15,171	3,397,217
Less accumulated depreciation for:				
Buildings and improvements	41,990	4,606	-	46,596
Equipment	105,779	3,971	1,708	108,042
Water distribution system	1,011,376	54,475	10,460	1,055,391
Vehicles	44,819	2,029	80	46,768
Total accumulated depreciation	1,203,964	65,081	12,248	1,256,797
Total capital assets being depreciated, net	2,184,667	(41,324)	2,923	2,140,420
Capital assets, net	\$ 2,203,353	\$ (41,324)	\$ 4,423	\$ 2,157,606
	Jan. 1 2018	Increases	Decreases	Dec. 31 2018
Capital assets not being depreciated:				
Land	\$ 17,186	\$ 3,150	\$ -	\$ 20,336
Construction in progress	-	260,874	-	260,874
Total capital assets not being depreciated	17,186	264,024	-	281,210
Capital assets being depreciated:				
Buildings and improvements	166,876	-	-	166,876
Equipment	189,102	2,856	519	191,439
Water distribution system	2,985,507	17,717	-	3,003,224
Vehicles	55,732	28,529	14,783	69,478
Total capital assets being depreciated	3,397,217	49,102	15,302	3,431,017
Less accumulated depreciation for:				
Buildings and improvements	46,596	4,590	-	51,186
Equipment	108,042	4,105	519	111,628
Water distribution system	1,055,391	54,375	-	1,109,766
Vehicles	46,768	3,694	14,783	35,679
Total accumulated depreciation	1,256,797	66,764	15,302	1,308,259
Total capital assets being depreciated, net	2,140,420	(17,662)	-	2,122,758
Capital assets, net	\$ 2,157,606	\$ 246,362	\$ -	\$ 2,403,968

5. LONG-TERM DEBT

Revenue Bonds

The 1985 bondholders held a statutory mortgage lien against the assets of the water district. There was also a pledge of net revenues of the water district for future bond and interest payments. These bonds were paid in full during March 2018 with a loan from a local bank.

NORTH MCLEAN COUNTY WATER DISTRICT
NOTES TO FINANCIAL STATEMENTS
For the Years Ended December 31, 2018 and 2017

Note Payable- Independence Bank

On March 6, 2018, the Water District borrowed \$119,430 from Independence Bank to immediately repay the revenue bonds outstanding, as well as the related accrued interest. Once the bonds were paid in full, the Replacement and Extension Fund as well as the Bond Sinking Reserve became unrestricted. After the Sinking Fund certificate of deposit matured, the Water District redeemed it March 23, 2018, and used the entire \$26,564 balance as a principal payment on the new loan. On the same date, the District closed the Replacement and Extension Fund bank account and applied the entire \$38,034 balance as a principal payment on the loan as well.

The remaining \$54,832 loan balance (after the above additional principal payments) matures March 6, 2020 and carries an interest rate of 2.6%. Inventory, accounts receivable, and revenues serve as collateral for the note.

Construction Loan- Independence Bank

During April 2018, the District signed a promissory note for \$175,000 with a 2.6% interest rate and April 2020 maturity date. The loan was to be used for the construction of a pump station and to purchase real estate, if needed. The loan is collateralized by certificates of deposit. No draws have been made on this loan. The District decided to use other funds for the project instead.

Cash Flow Savings Related to Current Refunding of Debt

Cash flow required to service old debt	\$ 156,964
Cash flow required to service new debt	<u>124,472</u>
	<u>\$ 32,492</u>

NORTH MCLEAN COUNTY WATER DISTRICT
NOTES TO FINANCIAL STATEMENTS
For the Years Ended December 31, 2018 and 2017

The annual requirements to amortize the note outstanding as of December 31, 2018, follows:

	Interest	Principal	Total
2019	\$ 1,259	\$ 8,672	\$ 9,931
2020	543	41,968	42,511
	<u>\$ 1,802</u>	<u>\$ 50,640</u>	<u>\$ 52,442</u>

Changes in Long-Term Liabilities

The following is a summary of changes in long-term liabilities for the year ended December 31, 2018:

	Amount of Original Obligation	Final Maturity Date	Range of Interest Rates	Balance Jan 1, 2018	Issued	Retired	Balance Dec 31, 2018	Amount Due within One Year
1985 Revenue Bonds	\$ 245,000		7 5/8%	\$ 130,000	\$ -	\$ (130,000)	\$ -	\$ -
Note Payable- Independence Bank	119,430	2020	2.6%	-	119,430	(68,790)	50,640	8,672
Customer Deposits				36,515	7,650	(4,690)	39,475	3,600
TOTAL LONG TERM LIABILITIES				<u>\$ 166,515</u>	<u>\$ 127,080</u>	<u>\$ (203,480)</u>	<u>\$ 90,115</u>	<u>\$ 12,272</u>

NORTH MCLEAN COUNTY WATER DISTRICT
NOTES TO FINANCIAL STATEMENTS
For the Years Ended December 31, 2018 and 2017

6. INCOME TAXES

The water district is a local government unit which is exempt from income taxes.

7. PURCHASE COMMITMENTS

The water district is committed to purchasing water each month from the McLean County Regional Water Commission until approximately October 2055. Other than an emergency situation, the District may not purchase water from any other source without prior approval by the Commission.

8. RESTRICTED NET ASSETS

The District's net assets equivalent to the restricted assets of the revenue bonds were restricted for revenue bond retirement until the bonds were paid in full during 2018.

9. RISK MANAGEMENT

The District is exposed to various risks of losses related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees, and natural disasters. The District has obtained insurance coverage through a commercial insurance company.

10. CONTINGENCIES

The District participated in a KIA grant program, which is governed by various rules and regulations of the grantor agency. Costs charged to the grant program are subject to audit and adjustments by the grantor agencies; therefore, to the extent that the District did or did not comply with the rules and regulations governing the grant, refunds of any money received may be required and the collectability of any related receivable at December 31, 2018 may be impaired. In the opinion of the District, there are no significant contingent liabilities relating to compliance with the rules and regulations governing the grant; therefore, no provision has been recorded in the accompanying financial statements for such contingencies.

OTHER REPORTS

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INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*

Board of Commissioners
North McLean County Water District
Livermore, KY 42352

We have audited, 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, the statement of net position of North McLean County Water District as of and for the year ended December 31, 2018, and the statements of revenues, expenses and changes in net position, and cash flows, and the related notes to the financial statements, and have issued our report thereon dated May 1, 2019.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether North McLean County Water District's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, non-compliance 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*.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered North McLean County Water District's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of North McLean County Water District's internal control. Accordingly, we do not express an opinion on the effectiveness of North McLean County Water District's internal control.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A significant deficiency is a deficiency, or combination of deficiencies in internal control, that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be significant deficiencies or material weaknesses and therefore, significant deficiencies or material weaknesses may exist that have not been identified. We did identify certain deficiencies in internal control, described in the accompanying Schedule of Findings and Responses that we consider to be material weaknesses.

North McLean County Water District's Response to Findings

North McLean County Water District's response to the findings identified in our audit is described in the accompanying Schedule of Findings and Responses. North McLean County Water District's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Shover and Morris, PLLC
May 1, 2019

NORTH MCLEAN COUNTY WATER DISTRICT
Schedule of Findings and Responses
December 31, 2018

FINDINGS

2018-1 Material Weakness:

Segregation of Duties

Condition: The small size of the District's bookkeeping staff limits segregation of duties.

Criteria: The District does not have adequate segregation of duties.

Cause: Limited number of personnel.

Effect: The District only has two office employees who handle receipts, disbursements, utility billing and adjustments, bookkeeping, tax reporting, and financial reporting. Theft could occur or a misstatement made and not be timely detected by management. Material adjusting journal entries were required for the current year.

Recommendation: We recommend office staff review each other's work and that duties be segregated as much as possible for the small organization.

Response: The District does not feel it is economically feasible to hire additional office staff. Office staff will review each other's work and try to segregate duties as much as reasonably possible.

2018-2 Material Weakness:

Financial Reporting

Condition: District personnel lack the expertise in financial reporting to draft the financial statements and related note disclosures.

Criteria: The District should have adequate controls in place over financial reporting to ensure that the financial statements are not materially misstated.

Cause: Lack of personnel with expertise in financial reporting.

Effect: The financial statements or related note disclosures could contain a material departure from US GAAP.

Recommendation: We recommend that the District carefully review the draft financial statements for errors.

Response: The District will carefully review the draft financial statements for errors.

HOOVER AND MORRIS, PLLC

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May 1, 2019

To the Board of Commissioners
North McLean County Water District

We have audited the financial statements of North McLean County Water District for the year ended December 31, 2018. Professional standards require that we provide you with information about our responsibilities under generally accepted auditing standards and *Government Auditing Standards*, as well as certain information related to the planned scope and timing of our audit. We have communicated such information in our letter to you dated March 18, 2019. Professional standards also require that we communicate to you the following information related to our audit.

Significant Audit Findings

Qualitative Aspects of Accounting Practices

Management is responsible for the selection and use of appropriate accounting policies. The significant accounting policies used by North McLean County Water District are described in Note 1 to the financial statements. No new accounting policies were adopted and the application of existing policies was not changed during 2018. We noted no transactions entered into by North McLean County Water District during the year for which there is a lack of authoritative guidance or consensus. All significant transactions have been recognized in the financial statements in the proper period.

Accounting estimates are an integral part of the financial statements prepared by management and are based on management's knowledge and experience about past and current events and assumptions about future events. Certain accounting estimates are particularly sensitive because of their significance to the financial statements and because of the possibility that future events affecting them may differ significantly from those expected. The most sensitive estimate affecting the financial statements was:

Management's estimate of depreciation expense is based on estimated useful lives. We evaluated the key factors and assumptions used to develop depreciation in determining that it is reasonable in relation to the financial statements taken as a whole.

The financial statement disclosures are neutral, consistent, and clear.

Difficulties Encountered in Performing the Audit

We encountered no significant difficulties in dealing with management in performing and completing our audit.

Corrected and Uncorrected Misstatements

Professional standards require us to accumulate all known and likely misstatements identified during the audit, other than those that are clearly trivial, and communicate them to the appropriate level of management. Management has corrected all such misstatements. The following misstatements, detected as a result of audit procedures and corrected by management, were material either individually or in the aggregate to the financial statements:

- Recorded \$20,765 retainage as accounts payable and construction in progress.
- Corrected \$12,000 transfer between bank accounts which was coded incorrectly.
- Reclassified \$8,204 of meters from expense accounts.
- Adjusted accrued interest by \$4,538.
- Recorded \$4,205 of accrued wages.
- Reclassified \$4,192 of loan principal paid.
- Adjusted Sewer Collection Payable \$4,215 related to billing adjustments.
- Recorded \$4,085 of engineering costs as accounts payable and construction in progress.

Disagreements with Management

For purposes of this letter, a disagreement with management is a financial accounting, reporting, or auditing matter, whether or not resolved to our satisfaction, that could be significant to the financial statements or the auditor's report. We are pleased to report that no such disagreements arose during the course of our audit.

Management Representations

We have requested certain representations from management that are included in the management representation letter dated May 1, 2019.

Management Consultations with Other Independent Accountants

In some cases, management may decide to consult with other accountants about auditing and accounting matters, similar to obtaining a "second opinion" on certain situations. If a consultation involves application of an accounting principle to the North McLean County Water District's financial statements or a determination of the type of auditor's opinion that may be expressed on those statements, our professional standards require the consulting accountant to check with us to determine that the consultant has all the relevant facts. To our knowledge, there were no such consultations with other accountants.

Other Audit Findings or Issues

We generally discuss a variety of matters, including the application of accounting principles and auditing standards, with management each year prior to retention as North McLean County Water District's auditors. However, these discussions occurred in the normal course of our professional relationship and our responses were not a condition to our retention.

Internal Control

By definition, there is a deficiency in internal control design. With an office staff of only two employees, the bookkeeping, payroll, cash collections, accounts receivable, and disbursement of

funds can not be completely segregated. This fact does not bear in any way on the integrity or competence of these employees. This situation does require that the commissioners regularly review transactions affecting the District's operation.

Sales Tax

Three of the invoices or receipts we selected for disbursement testing included \$57 of sales tax paid. Since the District is exempt from paying sales tax, personnel should examine invoices and receipts to verify sales tax is not being paid on purchases.

IRA Withholding

Employees withheld \$296 of individual retirement account contributions (from December 31, 2018 paychecks) that were never remitted. These contributions should be refunded to the employees, if not already refunded.

McLean County Withholding

When the 2018 annual reconciliation was filed with the county in January 2019, a balance due of \$336 was remitted for the year 2018. Money should not have been remitted with the annual reconciliation, because the District had already remitted the withholding with quarterly withholding returns. The overpayment resulted from reporting taxable wages on the reconciliation incorrectly. The District should file an amended 2018 reconciliation and request a refund.

941 Forms

The first and second quarter 941 forms were prepared incorrectly, resulting in overpayments of \$798. Amended returns should be filed for these quarters to request the overpayments be refunded. Additionally, the District paid over \$1,000 in IRS penalties during 2018 due to incorrectly filing returns or making payments.

School Tax

Sales reported on the April and August 2018 school tax returns exceeded sales on the Billing Register by approximately \$18,000. Amended returns should be filed to request refunds of around \$540 due to this over reporting of sales.

Restriction on Use

This information is intended solely for the information and use of the board of commissioners and management of North McLean County Water District and is not intended to be, and should not be, used by anyone other than these specified parties.

Very truly yours,

Hoover and Morris, PLLC

NORTH MCLEAN COUNTY WATER DISTRICT
ANALYTICAL PROCEDURES

	<u>2018</u>	<u>2017</u>	<u>2016</u>	<u>2015</u>	<u>2014</u>	<u>2013</u>	<u>2012</u>	<u>2011</u>	<u>2010</u>	<u>2009</u>
Water sold	706,771	631,818	597,720	593,502	584,071	554,037	599,587	595,071	592,923	552,774
Water cost	(339,762)	(340,812)	(301,542)	(272,860)	(271,697)	(260,664)	(276,054)	(267,386)	(276,905)	(237,872)
Gross profit	367,009	291,006	296,178	320,642	312,374	293,373	323,533	327,685	316,018	314,902
Operating expenses	(364,162)	(332,943)	(287,219)	(298,905)	(299,117)	(272,465)	(267,187)	(259,706)	(244,585)	(222,132)
Interest expense	(3,313)	(10,148)	(10,871)	(11,550)	(12,200)	(13,052)	(13,344)	(13,878)	(14,335)	(15,310)
Depreciation	(66,764)	(65,081)	(64,743)	(63,466)	(64,012)	(63,016)	(61,685)	(76,791)	(59,518)	(53,452)
Other non-operating expense	-	-	-	-	-	-	-	-	-	(35,525)
Interest income	6,016	4,025	3,438	3,065	3,200	3,287	3,473	3,922	5,080	6,116
Late payment penalties/ misc.	27,020	25,329	19,915	19,520	18,895	19,749	20,839	18,969	21,565	55,556
Net income before contributions & grants	(34,194)	(87,812)	(43,302)	(30,694)	(40,860)	(32,124)	5,629	201	24,225	50,155
Capital contributions & grants	233,285	9,460	1,981	6,113	4,902	205,616	4,131	5,930	451,635	8,740
Net income (loss)	199,091	(78,352)	(41,321)	(24,581)	(35,958)	173,492	9,760	6,131	475,860	58,895
Gross profit %	51.93%	46.06%	49.55%	54.03%	53.48%	52.95%	53.96%	55.07%	53.30%	56.97%
Current assets	557,239	506,049	574,357	553,775	537,598	533,372	570,711	539,013	520,850	503,910
Less current liabilities	143,782	57,789	79,296	38,231	37,047	43,195	41,611	35,635	35,252	26,876
Current working capital	413,457	448,260	495,061	515,544	500,551	490,177	529,100	503,378	485,598	477,034
Total cash & CD's	411,959	499,739	547,122	538,172	518,905	518,677	559,600	522,012	503,609	456,481
Gallons purchased (1,000)	127,116	132,141	125,779	119,298	118,443	113,036	119,604	117,160	123,464	120,882
Less gallons sold/ used	109,454	107,445	100,795	99,936	97,107	93,450	99,225	100,544	102,637	99,393
Gallons lost	17,662	24,696	24,984	19,362	21,336	19,586	20,379	16,616	20,827	21,489
Water loss %	13.89%	18.69%	19.86%	16.23%	18.01%	17.33%	17.04%	14.18%	16.87%	17.78%