

LAKE VILLAGE WATER ASSOCIATION, INC.

AUDITED FINANCIAL STATEMENTS

DECEMBER 31, 2020

KERBAUGH, RODES & BUTLER, PLLC

CERTIFIED PUBLIC ACCOUNTANTS

DANVILLE, KENTUCKY

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INDEPENDENT AUDITOR'S REPORT

Chairman and Commissioners
Lake Village Water Association, Inc.
Burgin, Kentucky 40310

Report on the Financial Statements

We have audited the accompanying financial statements of Lake Village Water Association, Inc. (a nonprofit organization) (the Association), which comprise the Statement of Assets, Liabilities, and Members' Equity-Statutory Basis as of December 31, 2020, and the related Statements of Operations, Members' Equity, Operating Expenses, and Cash Flows-Statutory Basis for the year then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with the financial reporting practices prescribed or permitted by the U.S. Department of Agriculture, Rural Development Agency and the Commonwealth of Kentucky Public Service Commission (statutory basis) as described in Note 2; this includes determining that the statutory basis of accounting is an acceptable basis for the preparation of the financial statements in the circumstances. Management is also responsible for the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

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

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

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the assets, liabilities, and members' equity of the Association as of December 31, 2020, and the results of its' operations, cash flows, and operating expenses for the year then ended in accordance with the statutory basis of accounting as described in Note 2.

Basis of Accounting

We draw attention to Note 2 of the financial statements, which describes the basis of accounting. As described in Note 2 to the financial statements, the financial statements are prepared on the statutory basis of accounting, which is a basis of accounting other than accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

Report on Summarized Comparative Information

We have previously audited the Association's 2019 financial statements, and we expressed an unmodified opinion on those financial statements in our report dated March 27, 2020. In our opinion, the summarized comparative information presented herein as of and for the year ended December 31, 2019, is consistent, in all material respects, with the audited financial statements from which it has been derived.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated March 27, 2021, on our consideration of the Association'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 effectiveness of the Association'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 the Association's internal control over financial reporting and compliance.

Kerbaugh, Rodes & Butler, PLLC

Kerbaugh, Rodes & Butler, PLLC
Certified Public Accountants

Danville, Kentucky
March 27, 2021

LAKE VILLAGE WATER ASSOCIATION, INC.
STATEMENT OF ASSETS, LIABILITIES, AND MEMBERS' EQUITY-STATUTORY BASIS
DECEMBER 31, 2020
(With comparative Totals for December 31, 2019)

	2020	2019
<u>Assets</u>		
Current Assets:		
Cash (Note 3)	\$ 13,743	\$ 9,577
Accounts Receivable, Net (Note 2 and 7)	128,620	144,994
Inventory (Note 2)	34,824	37,369
Prepaid Expenses (Note 2)	12,821	21,672
Total Current Assets	190,008	213,612
Restricted Assets:		
Cash (Note 3)	100,193	117,307
Property & Equipment, Net (Note 2 and 4)	5,216,037	5,484,197
Total Assets	\$ 5,506,238	\$ 5,815,116

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

LAKE VILLAGE WATER ASSOCIATION, INC.
STATEMENT OF ASSETS, LIABILITIES, AND MEMBERS' EQUITY-STATUTORY BASIS
DECEMBER 31, 2020
(With comparative Totals for December 31, 2019)

	2020	2019
<u>Liabilities & Members' Equity</u>		
Current Liabilities:		
Current Portion - Debt (Note 5)	\$ 214,039	\$ 201,737
Cash Overdraft (Note 3)	107,679	78,688
Accounts Payable	49,113	50,454
Accounts Payable - Contractors	1,861	45,509
Due to Mercer Sanitation District	22,636	22,358
Accrued Interest	83,958	86,656
Other Current Liabilities	90,291	69,981
Total Current Liabilities	569,577	555,383
Long - Term Debt (Note 5)	3,575,663	3,685,810
Total Liabilities	4,145,240	4,241,193
Members' Equity:		
Memberships	749,168	738,368
Contributions in Aid of Construction	3,665,469	3,665,469
Retained Deficit	(3,053,639)	(2,829,914)
Total Equity	1,360,998	1,573,923
Total Liabilities & Members' Equity	\$ 5,506,238	\$ 5,815,116

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

LAKE VILLAGE WATER ASSOCIATION, INC.
STATEMENT OF OPERATIONS-STATUTORY BASIS
FOR THE YEAR ENDED DECEMBER 31, 2020
(With Comparative Totals for the Year Ended December 31, 2019)

	<u>2020</u>	<u>2019</u>
Operating Revenue:		
Water Sales	\$ 1,444,027	\$ 1,402,914
Management Fee Income	35,000	35,000
Other Operating Revenue	<u>8,776</u>	<u>31,497</u>
Total Operating Revenue	1,487,803	1,469,411
Operating Expenses	<u>1,257,340</u>	<u>1,234,916</u>
Net Operating Income Before Depreciation	230,463	234,495
Depreciation (Note 2)	<u>311,352</u>	<u>312,915</u>
Net Operating Income (Loss)	(80,889)	(78,420)
Non-Operating Income (Expenses):		
Interest Income	827	1,082
Interest Expense	<u>(143,663)</u>	<u>(146,053)</u>
Total Non-Operating Income (Expenses):	<u>(142,836)</u>	<u>(144,971)</u>
Net Income (Loss)	<u>\$ (223,725)</u>	<u>\$ (223,391)</u>

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

LAKE VILLAGE WATER ASSOCIATION, INC.
STATEMENT OF MEMBERS' EQUITY-STATUTORY BASIS
FOR THE YEAR ENDED DECEMBER 31, 2020
(With Comparative Totals for the Year Ended December 31, 2019)

	<u>Memberships</u>	<u>Contributions in Aid of Construction</u>	<u>Retained Deficit</u>	<u>Total</u>
Balance at January 1, 2019	\$ 725,318	\$ 3,665,469	\$ (2,606,523)	\$ 1,784,264
2019 Net Loss	-	-	(223,391)	(223,391)
Memberships	<u>13,050</u>	<u>-</u>	<u>-</u>	<u>13,050</u>
Balance at December 31, 2019	738,368	3,665,469	(2,829,914)	1,573,923
2020 Net Loss	-	-	(223,725)	(223,725)
Memberships	<u>10,800</u>	<u>-</u>	<u>-</u>	<u>10,800</u>
Balance at December 31, 2020	<u>\$ 749,168</u>	<u>\$ 3,665,469</u>	<u>\$ (3,053,639)</u>	<u>\$ 1,360,998</u>

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

LAKE VILLAGE WATER ASSOCIATION, INC.
STATEMENT OF OPERATING EXPENSES-STATUTORY BASIS
FOR THE YEAR ENDED DECEMBER 31, 2020
(With Comparative Totals for the Year Ended December 31, 2019)

	<u>2020</u>	<u>2019</u>
Source of Supply Expense:		
Water Purchases	\$ 552,238	\$ 520,333
Total	552,238	520,333
Transmission & Distribution Expense:		
Maintenance & Repairs	<u>53,772</u>	<u>57,757</u>
Total	53,772	57,757
Customer Accounts Expense:		
Uncollectible Accounts	4,577	-
Supplies & Postage	<u>16,678</u>	<u>15,837</u>
Total	21,255	15,837
Administrative & General:		
Salaries	363,454	353,680
Insurance	35,336	36,909
Utilities	30,358	40,090
Office Supplies & Expense	20,195	25,199
Transportation Expense	11,619	12,963
Payroll Taxes	27,024	26,586
Staff Benefits	74,829	72,234
Legal Expense	3,775	4,510
Audit & Accounting	6,300	5,850
Commissioners' Fees	23,850	22,800
Engineering Fees	4,886	3,912
Miscellaneous General Expense	25,510	33,439
Other Licenses & Taxes	<u>2,939</u>	<u>2,817</u>
Total Administrative & General	<u>630,075</u>	<u>640,989</u>
Total Operating Expenses	<u>\$ 1,257,340</u>	<u>\$ 1,234,916</u>

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

LAKE VILLAGE WATER ASSOCIATION, INC.
STATEMENT OF CASH FLOWS-STATUTORY BASIS
FOR THE YEAR ENDED DECEMBER 31, 2020
(With Comparative Totals for the Year Ended December 31, 2019)

	<u>2020</u>	<u>2019</u>
Cash Flows From Operating Activities		
Net Income (Loss)	\$ (223,725)	\$ (223,391)
Adjustments to Reconcile Net Loss to Net Cash Provided by Operating Activities:		
Depreciation	311,352	312,915
Decrease (Increase) in Accounts Receivable	16,374	(16,862)
Decrease (Increase) in Inventory	2,545	(11,565)
Decrease (Increase) in Prepaid Expenses	8,851	(1,431)
Increase (Decrease) in Accounts Payable	(1,341)	(6,051)
Increase (Decrease) in Due to Sanitation District	278	5,095
Increase (Decrease) in Accrued Interest	(2,698)	(957)
Increase (Decrease) in Other Current Liabilities	<u>20,310</u>	<u>673</u>
Net Cash Provided By (Used In) Operating Activities	<u>131,946</u>	<u>58,426</u>
Cash Flows From Investing Activities		
Construction/Acquisition of Property & Equipment	<u>(86,840)</u>	<u>(85,206)</u>
Net Cash Provided By (Used In) Investing Activities	<u>(86,840)</u>	<u>(85,206)</u>
Cash Flows From Financing Activities		
Memberships (Tap Fees)	10,800	13,050
New Borrowings on Debt	106,431	89,299
Principal Payments on Debt	<u>(204,276)</u>	<u>(101,473)</u>
Net Cash Provided By (Used In) Financing Activities	<u>(87,045)</u>	<u>876</u>
Net Increase (Decrease) in Cash	(41,939)	(25,904)
Cash at Beginning of Year	<u>48,196</u>	<u>74,100</u>
Cash at End of Year	<u>\$ 6,257</u>	<u>\$ 48,196</u>
Supplemental Disclosure of Cash Flow Information:		
Cash Paid During the Year for Interest	<u>\$ 146,361</u>	<u>\$ 147,010</u>
Supplemental Disclosure of Non-Cash Investing Activities:		
Property & Equipment Acquired and Included in Accounts Payable - Contractors	<u>\$ 1,861</u>	<u>\$ 45,509</u>

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

LAKE VILLAGE WATER ASSOCIATION, INC.
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2020

1. General

Lake Village Water Association, Inc., (the "Association") is a not-for-profit corporation. The Association provides water services to the rural sections of Boyle and Mercer counties.

2. Summary of Significant Accounting Policies

- A. The Association uses the accrual method of accounting, and accordingly reflects all significant prepaids, receivables, payables, and other liabilities. Certain disclosures have been included in this report to conform to Rural Development Agency (RD) requirements. Also, the Association's financial statements differ from financial statements prepared in accordance with accounting principles generally accepted in the United States of America in that the statements include a statement of assets, liabilities, and members' equity, statement of operations, statement of members' equity, statement of operating expenses, and statement of cash flows.
- B. For purposes of the statement of cash flows, the Association considers all highly liquid investments with an initial maturity of three months or less to be cash equivalents.
- C. Management uses estimates and assumptions in preparing the financial statements. Those estimates and assumptions affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities, and the reported revenues and expenses. Actual results could differ from those estimates.
- D. Receivables are reported at their gross value and, where appropriate, are reduced by the estimated portion that is expected to be uncollectible. All receivables in excess of 90 days old comprise the allowance for uncollectibles.
- E. Property and equipment are stated at cost and are depreciated over the estimated useful life of the asset using the straight-line method of depreciation. Transmission lines and standpipes are being depreciated over a 33-year life; office furniture and equipment over a 5 to 10-year life; buildings and improvements over a 20-year life.
- F. A statutory mortgage lien exists on the utility plant in favor of the Rural Development Agency (RD), with loans being collateralized by and payable from gross revenues of the Association including all assets of the Association.
- G. Material inventory is stated at cost using the first-in, first-out (FIFO) method.
- H. Prepaid items include payments made to vendors that will benefit future periods.
- I. Restricted assets represent cash for which use is limited by applicable loan covenants.
- J. Management has evaluated subsequent events through March 27, 2021, the date the financial statements were issued, and has determined that there are no items requiring disclosure.

LAKE VILLAGE WATER ASSOCIATION, INC.
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2020

3. Cash

Cash is composed of the following with restriction for use noted:

Cash on Hand		\$	50
Cash on Deposit-Operating Account	A		(107,679)
Cash on Deposit-Revenue Account	B		13,594
Cash on Deposit-Customer Deposits	C		7,021
Cash on Deposit-Construction Project	D		2,678
Savings Accounts:			
Debt Service Account	E		7,028
Sinking Fund	F		78,433
Depreciation Account	G		99
Reserve Account	H		5,033
TOTAL			\$ 6,257

The Association maintains cash in two local banks and is required by Rural Development (RD) loan agreements to have the financial institutions pledge securities having a current quoted market value at least equal to the uninsured deposits. At year end, the carrying amount of the Association's cash was \$6,257 and the bank balance was \$115,921. At December 31, 2020, all bank balances were covered by federal depository insurance.

- (A) The operating and maintenance account is the primary operating account of the Association. It is funded by transfers from the revenue account and is used to pay all operating expenses of the Association. The operating and maintenance account operates on an imprest basis; thus, the overdraft in this account represents outstanding checks at year-end.
- (B) The revenue account, required by RD loan agreements, is used for the deposit of all funds collected and for the disbursement of funds to the proper bank accounts.
- (C) The customer deposit account is used to handle required deposits by new customers.
- (D) This account is maintained by the Association to account for the cash receipts and disbursements related to certain water system improvement projects undertaken during the year.
- (E) The Association is required to transfer funds monthly to the debt service account to meet the monthly installments for principal and interest on the RD loans outstanding.
- (F) The Association is required to transfer funds monthly to the sinking fund account to meet the monthly installments for principal and interest on the Kentucky Rural Water Finance Corporation loans outstanding.
- (G) The depreciation account is used by the Association to maintain excess unrestricted funds so that they will earn interest.
- (H) The Association is required to transfer funds monthly to the reserve account in amounts specified by RD. The use of this fund is restricted to paying the cost of repairing or replacing, making extensions or improvements, or when necessary for payment of principal and interest.

During the year ended December 31, 2020, the association did not make the required monthly transfers to the reserve accounts in the amounts specified by RD.

LAKE VILLAGE WATER ASSOCIATION, INC.
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2020

4. Property and Equipment

Property and equipment consists of the following at December 31:

Land	\$	62,409
Buildings & Improvements		141,085
Supply Mains		15,500
Pump Station		200,431
Standpipes & Storage Tanks		2,450,633
Water Lines		7,083,677
Customer Services		189,926
Meters		485,298
Hydrants		1,960
Office Furniture		79,021
Transportation Equipment		195,609
Other Equipment		83,968
Other Tangible Plant		223,235
Construction in Process		<u>197,738</u>
Total		11,410,490
Less: Accumulated Depreciation		<u>(6,194,453)</u>
Property & Equipment, Net		<u><u>\$ 5,216,037</u></u>

5. Long-Term Debt

The following debt obligations were outstanding at December 31, 2020:

Loan 91-09 - 4.5% promissory note payable to the Department of Agriculture, Rural Development, due in annual installments of \$49,038, including principal and interest.	\$	756,712
Loan 91-10 - 4.0% promissory note payable to the Department of Agriculture, Rural Development, due in annual installments of \$79,733, including principal and interest.		1,378,273
Note payable - Kentucky Rural Water Finance Corporation Public Projects Taxable Refunding Revenue Bonds (Flexible Term Program), Series 2016C. Fixed interest rate ranging from 3.0% to 4.25%. Interest payments are due semi-annually. Principal payments are due annually in amounts ranging from \$25,000 to \$70,000.		915,000
Loan 91-11 - 2.75%, \$656,000 promissory note to the Department of Agriculture, Rural Development, due in annual installments ranging from \$27,940 to \$28,044 beginning July 11, 2019 through 2056, including principal and interest.		635,717
Note payable - Kentucky Rural Water Finance Corporation Flexible Term Finance Program, \$104,000. Fixed interest rate at 1.16%. Interest payments are due semi-annually. Balloon principal payment is due at maturity, which is August 1, 2021.		<u>104,000</u>
Total Outstanding Bonds		3,789,702
LESS: Current Portion		<u>(214,039)</u>
Long-Term Debt		<u><u>\$ 3,575,663</u></u>

The note payable to Kentucky Rural Water Finance Corporation in the amount of \$101,000 was refinanced in 2020 in the amount of \$104,000. The balance is expected to be refinanced through Rural Development with the Contract 14 Project (See Note 9) funding that has not yet been finalized. As a result, this loan is included in the current portion of long-term debt.

LAKE VILLAGE WATER ASSOCIATION, INC.
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2020

The above notes are secured by gross revenues and all property and equipment of the Association.

A schedule of maturities on the above debt is as follows:

Year Ending December 31,	Amount
2021	\$ 214,039
2022	111,985
2023	114,009
2024	121,112
2025	123,301
2026-2030	627,524
2031-2035	671,993
2036-2040	506,612
2041-2045	589,749
2046-2050	556,279
2051-2055	125,907
2056	27,192
Total	\$ 3,789,702

6. Income Taxes

During 1973, the Association applied for and obtained tax exempt status from the Internal Revenue Service under Section 501(C) (12) of the Internal Revenue Code.

7. Other Matters

(A) The Association has not been assessed or paid any property, intangible or franchise tax in prior years. Since there is some uncertainty about the taxability of a "water association", the financial statements do not reflect any liability for unpaid taxes, if any.

(B) Active Meter Customers - December 31, 2020 2,275

(C) Water Loss (Gallons):

Water Purchases 209,499,130

Water Sold and Used in Operations 162,258,000

Line loss 47,241,130

Percentage of Line Loss 22.55%

(D) Accounts receivable aging at December 31, 2020:

Current	\$ 122,842
30-59 Days	11,960
60-89 Days	874
Over 90 Days	9,160
Less: Allowance	(16,216)
Accounts Receivable, Net	\$ 128,620

LAKE VILLAGE WATER ASSOCIATION, INC.
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2020

8. Risk Management

The Association is exposed to a variety of accidental losses, and has attempted to minimize its risk by carrying commercial insurance. There have been no significant reductions in coverage from coverage in the prior year.

9. Capital Projects Planned and in Process

On October 11, 2018, the Association entered into a loan agreement for \$101,000 from the Kentucky Rural Water Finance Corporation Flexible Term Program to finance preliminary and design engineering for the Contract 14 Project, which is a systemwide rehabilitation project. This loan was refinanced in 2020 in the amount of \$104,000. As of December 31, 2020, there were no remaining funds to be drawn down on this loan. As of December 31, 2020, \$175,343, had been spent related to this project for the preliminary and design engineering related to this project. The Association has received a letter of conditions for a loan in the amount of \$2,089,290 for funding construction of the project. The interest rate on the loan will be 2.375% with a term of 40 years. The total Contract 14 Project cost is estimated to be \$2,089,290. As of December 31, 2020, no funds have been drawn on the loan.

10. Contract with Mercer County Sanitation District

On August 1, 2016, the Association entered into an agreement with the Mercer County Sanitation District whereby the Association provides management, secretarial, billing, bookkeeping, budgeting, office space, and various other services to the Sanitation District for an annual fee of \$35,000 payable in equal monthly installments of \$2,916.67. The contract term is five years and is cancelable by either party upon 60 days written notice.

11. Retirement Plan

The Association sponsors a Simple Employee Pension IRA for all qualifying employees. Under the terms of the plan, the Association makes a discretionary contribution up to 10% of the employee's salary. For the year ended December 31, 2020, the Association contributed \$30,000 to the plan.

12. COVID-19 Uncertainty

During 2020, the World Health Organization characterized an outbreak of a novel strain of coronavirus (COVID-19) as a pandemic. Multiple jurisdictions in the U.S. have declared a state of emergency, including the Commonwealth of Kentucky. As a result of this pandemic, the PSC issued an order on May 16, 2020, suspending until further notice the ability of utilities to shut off service due to nonpayment and the assessment of late payment fees. On September 21, 2020, the PSC lifted the moratorium on disconnects for nonpayment beginning October 20, 2020, subject to certain conditions, and continued the moratorium on the assessment of late payment charges for residential customers only until December 31, 2020. Under the terms of the October 20, 2020 order, utilities were required to create payment plans for all residential customers with respect to arrearages accumulated from service rendered on or after March 16, 2020 and before October 1, 2020, to the extent that past due balances exist. The term of the default payment plans shall be no less than six months and no longer than two years. As a result of these orders, service fees decreased, and accounts receivable collections may be delayed when compared to previous years.

13. Subsequent Event

In January 2021, the Association failed to make the debt payment due January 12, 2021 for RD Loan 91-10 in the amount of \$79,733. The Association entered into a Workout Agreement with RD on March 18, 2021, which requires the payment to be made in three monthly installments beginning April 1, 2021. The agreement states that as long as the Association meets the terms of the Workout Agreement, the debt will not be accelerated. As a result of the Workout Agreement, the balance of RD Loan 91-10 has not been included in current liabilities.

LAKE VILLAGE WATER ASSOCIATION, INC.
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2020

In addition, on March 9, 2021, the PSC approved an application to refinance two of its outstanding RD loans (including 91-10) through Kentucky Rural Water Finance Corporation in the amount of \$2,100,000 with interest rates ranging from 2.75% to 3.35%. The estimated savings over the 30 year term will be approximately \$245,000. The closing date of the refinance has not been determined as of the date of this report.

COMPLIANCE SECTION

Kerbaugh, Rodes & Butler, PLLC

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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*

Chairman and Commissioners
Lake Village Water Association, Inc.
Burgin, Kentucky 40310

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, the financial statements of the Lake Village Water Association, Inc. (a nonprofit organization) (the Association), which comprise the statement of assets, liabilities, and members' equity-statutory basis as of December 31, 2020, and the related statements of operations, members' equity, operating expenses, and cash flows-statutory basis for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated March 27, 2021.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Association'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 the Association's internal control. Accordingly, we do not express an opinion on the effectiveness of the Association'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 reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected, on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that have not been identified. However, as described below, we identified a certain deficiency in internal control over financial reporting that we consider to be a material weakness.

1. As is common within the system of internal control of most small organizations, the accounting function of the Association does not prepare the financial statements complete with footnotes in accordance with the statutory basis of accounting described in Note 2 to the financial statements. Accordingly, the Association has not established internal controls over the preparation of its

financial statements. This condition is considered to be a material weakness in the Association's system of internal control.

During the course of performing an audit, it is not unusual for the auditor to prepare various journal entries to present the financial statements in accordance with the statutory basis of accounting. This reliance on the auditor to detect and make these necessary adjustments is considered to be a material weakness in the system of internal control. AU-C Section 265 does not make exceptions for reporting deficiencies that are adequately mitigated with non-audit services rendered by the auditor or deficiencies for which the remedy would be cost prohibitive.

Communication of the material weakness above helps to emphasize that the responsibility for financial reporting rests entirely with the Association and not the auditor. Stated another way, if an Association is unable to issue, without the auditor's involvement, complete financial statements with footnotes in accordance with the statutory basis of accounting and free of material misstatement, that inability is a symptom of a material weakness in the system of internal control.

Management's Response

The Association engages consultants who possess industry knowledge and expertise to provide financial services, as well as legal, engineering, and other professional services. Based on the auditor's unmodified opinion and after reading the financial statements, management believes the financial statements to be materially correct. Management does not think that the addition of an employee or consultant to oversee the annual financial reporting process is necessary nor would it be cost effective.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Association's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed an instance of noncompliance that is required to be reported under *Government Auditing Standards*.

1. Certain of the Association's debt covenants require monthly transfers into debt service accounts and reserve accounts. However, during the year ended December 31, 2020, the required transfers into the RD depreciation reserve account and short-lived assets account were not made, resulting in the accounts being underfunded. We recommend the Association resume the required monthly transfers into its depreciation and short-lived asset reserve accounts as required by certain debt covenants.

The Association's Response to Findings

The Association's response to the findings identified in our audit is described above. The Association'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 Association'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 Association's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Kerbaugh, Rodes & Butler, PLLC

Kerbaugh, Rodes & Butler, PLLC
Certified Public Accountants

Danville, Kentucky
March 27, 2021