

SOUTHERN WATER AND SEWER DISTRICT
REPORT OF AUDIT OF FINANCIAL STATEMENTS
AND SUPPORTING DATA
YEAR ENDED DECEMBER 31, 2019

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INDEPENDENT AUDITOR'S REPORT

To the Board of Commissioners
Southern Water and Sewer District
McDowell, Kentucky

Report on the Financial Statements

I have audited the accompanying financial statements of the business-type activities of Southern Water and Sewer District, as of and for the years ended December 31, 2019 and 2018, and the related notes to the financial statements, which collectively comprise the Southern Water and Sewer District's basic financial statement listed in the table of contents.

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

My responsibility is to express opinions on these financial statements based on my audit. I conducted my audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that I plan and perform the audit to obtain reasonable assurance about whether the financial statement are free from material misstatement.

An audit involves performing procedure to obtain audit evidence about the amounts and disclosures in the financial statements. The procedure 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 presentations 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, I 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.

I believe that the evidence I obtained is sufficient and appropriate to provide a basis for my audit opinions.

Opinions

In my opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the business-type activities of Southern Water and Sewer District, as of December 31, 2019 and 2018, and the respective changes in financial position and where applicable, cash flows thereof for the year ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter


Southern Water and Sewer is involved with transfer of the Harold Sewer Plant to the City Of Prestonsburg, Kentucky. See note 5 page 15 for details.

Other Matters

Accounting principles generally accepted in the United States of America require that management's discussion and analysis and budgetary comparison information on pages 3-7 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by Governmental Accounting Standards Board, who considers it to be an essential part of financial statements in an appropriate operational, economic, or historical context. I have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America; which consisted of inquiries of management about methods of preparing the information and comparing the information for consistency with management's responses to my inquiries, the basic financial statements, and other knowledge I obtained during my audit of the basic financial statements. I do not express an opinion or provide any assurance on the information because the limited procedures do not provide me with sufficient evidence to express an opinion or provide assurance.

Other Reporting Required by Governmental Auditing Standards

In accordance with Governmental Auditing Standards, I have also issued my report dated October 21, 2020, on my consideration of Southern Water and Sewer District's internal control over financial reporting and on tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of my 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 Governmental Auditing Standards in considering Southern Water and Sewer District's internal control over financial reporting and compliance.



Richard F. Paulmann CPA, LLC
Pewee Valley, KY
October 21, 2020

SOUTHERN WATER AND SEWER DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS
Years ended December 31, 2019 and 2018

This discussion and analysis of the Southern Water and Sewer District's financial performance provides an overview of the District's financial activities for the years ended December 31, 2019 and December 31, 2018. This information is presented in conjunction with the audited financial statements that follow this section.

FINANCIAL HIGHLIGHTS

- The District assets exceeded its liabilities at the end of the year by \$15,549,943. This was a decrease of \$2,166,759 from the year ended December 31, 2018.
- At December 31, 2019, the District had \$22,551,022 in assets and \$7,001,079 in liabilities. The investment in capital assets, net of related debt, balance at this date was \$12,231,810. The restricted for capital projects balance was \$190,444. The restricted for maintenance balance was \$228,281. The restricted for debt service balance was \$288,087. The restricted for deposits was \$184,354. The unrestricted balance was \$2,426,967.
- The District had a net loss of \$2,166,759 for the year ended December 31, 2019. For the year ended December 31, 2018 the net loss was \$461,698.
- The District's water sales were \$4,014,408 for the year ended December 31, 2019. For the year ended December 31, 2018 the water sales were \$2,966,441. This represented an increase of 35.3% which was a result of factors affecting revenue such as increased water usage and increased customers.

OVERVIEW OF FINANCIAL STATEMENTS

This discussion and analysis is intended to serve as an introduction to the District's basic financial statements. The District's basic financial statements comprise two components: 1) financial statements, and 2) notes to the financial statements. This report also contains other supplementary information in addition to the basic financial statements themselves.

Financial statements. The financial statements are designed to provide readers with a broad overview of the District's finances, in a manner similar to a private – sector business.

The balance sheets present information on all of the District's assets and liabilities, in a comparative format showing the balances as of December 31, 2019 and December 31, 2018. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of the District is improving or deteriorating.

The statements of revenues, expenses and changes in retained earnings present information showing the District's net income or (loss) for the years then ended.

The statements of cash flows shows the increase or decrease in the cash and cash equivalents for the years ended by the different types of activities.

The financial statements can be found on pages 8 through 12 of this report.

Notes to the financial statements. The notes provide additional information that is essential to a full understanding of the data provided in the financial statements. The notes to the financial statements can be found on pages 13 through 21 of this report.

SOUTHERN WATER AND SEWER DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS
Years ended December 31, 2019 and 2018

FINANCIAL ANALYSIS

Net assets may serve over time as a useful indicator of the District's financial position. In the case of the District, assets exceeded liabilities by \$15,549,943 at the close of the most recent year.

Southern Water and Sewer District's Net Assets

		2019
Current assets	\$	3,193,699
Restricted assets		891,167
Fixed assets		18,412,030
Other assets		54,126
 Total assets		 22,551,022
 Current liabilities		 1,427,274
Long-term liabilities		5,573,805
 Total liabilities		 7,001,079
 Net assets:		
Investment in		
Capital Assets		12,231,810
Restricted		891,166
Unrestricted		2,426,967
 Total net assets	 \$	 15,549,943

By far the largest portion of the District's net assets reflects its investment in fixed assets (e.g., land, water lines, tanks), less any related debt used to acquire those assets still outstanding.

Grant income was \$229,535 during the year. Grant monies and customer contributions accounted for this increase. These monies were used for water line expansions.

SOUTHERN WATER AND SEWER DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS
Years ended December 31, 2019 and 2018

Southern Water and Sewer District's Statements of Revenues, Expenses, and Changes in Retained Earnings

	2019
Revenues:	
Water sales	\$ 4,014,408
Solid waste revenue	857,465
Penalties and service charges	68,530
Other	0
Total revenues	4,940,403
Expenses:	
Water treatment supplies	163,217
Depreciation and amortization	903,793
Purchased water	390,442
Solid Waste payments	831,720
Power for pumping	325,201
Outside services	81,005
Miscellaneous	46,029
Insurance	89,335
Distribution supplies and expense	318,020
Taxes and other	67,130
Customer accounts expense	133,887
Wages	625,154
Sewer supplies and expense	11,321
Employee benefits	290,004
Management Fees	207,637
Pumping supplies and expense	37,519
Total operating expenses	4,521,414
Net operating income	418,989
Non-operating income (expense)	
Grants income	229,535
Loan Service Fees	(3,325)
Gain/(Loss) on Sale of Assets	(2,462,661)
Interest income	238
Interest expense	(208,192)
Interest and penalty	(122)
Provision for bad debts	(141,221)
Total non-operating (expense)	(2,585,748)
Net income (loss) before contributions and transfers	(2,166,759)
Total net assets, beginning	17,716,702
Total net assets, ending	15,549,943

Operations.

The District showed a net income (loss) of (\$2,166,759).

Key elements of this income are as follows:

- Depreciation for the year was \$903,793.
- Grant income of \$229,535 was received during the year.

SOUTHERN WATER AND SEWER DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS
Years ended December 31, 2019 and 2018

Southern Water and Sewer District Budget Comparison

	Actual Amounts	Original Budget Amounts	Variance Positive (Negative) 2019
	2019	2019	
Revenues:			
Water sales	\$ 4,014,408	\$ 4,159,031	\$ (144,623)
Solid waste revenue	857,465	870,432	(12,967)
Penalties and service charges	68,530	92,854	(24,324)
Other	0	0	0
Total revenues	<u>4,940,403</u>	<u>5,122,317</u>	<u>(181,914)</u>
Expenses:			
Water treatment supplies	163,217	112,091	(51,126)
Depreciation and amortization	903,793	865,007	(38,786)
Purchased water	390,442	452,525	62,083
Solid Waste payments	831,720	845,403	13,683
Power for pumping	325,201	422,480	97,279
Outside services	81,005	87,254	6,249
Miscellaneous	46,029	145,822	99,793
Insurance	89,335	131,076	41,741
Distribution supplies expense	318,020	396,419	78,399
Taxes and other	67,130	84,422	17,292
Customer accounts expense	133,887	26,456	(107,431)
Wages	625,154	937,795	312,641
Sewer supplies and expense	11,321	0	(11,321)
Employee benefits	290,004	376,489	86,485
Management Fees	207,637	0	(207,637)
Transportation expense	0	122,497	122,497
Pumping supplies expense	37,519	0	(37,519)
Total operating expenses	<u>4,521,414</u>	<u>5,005,736</u>	<u>484,322</u>
Net operating income	418,989	116,581	302,408
Non-operating income (expense)			
Grant income	229,535	585,578	356,043
Loan Service Fees	(3,325)	0	(3,325)
Gain/(Loss) on Sale of Assets	(2,462,661)	19,300	(2,481,961)
Interest income	238	5,087	(4,849)
Interest expense	(208,192)	(206,291)	(1,901)
Miscellaneous nonutility income	(122)	0	(122)
Provision for Bad Debts	(141,221)	(134,000)	(7,221)
Total non-operating income	<u>(2,585,748)</u>	<u>269,674</u>	<u>(2,855,422)</u>
Net income (loss)	<u>(2,166,759)</u>	<u>386,255</u>	<u>(2,553,014)</u>
Total net assets, beginning	17,716,702		
Total net assets, ending	<u>\$ 15,549,943</u>	<u>\$</u>	<u>\$</u>

Budget Comparisons

- Revenues were \$144,623 less than budgeted as a result of water sales being down, a decrease in the number of customers and various other differences. Operating expenses were \$484,322 less than budgeted as a result of decreased costs and various other expenses.

SOUTHERN WATER AND SEWER DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS
Years ended December 31, 2019 and 2018

FINANCIAL ANALYSIS OF THE DISTRICT'S FUNDS

The District uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. Proprietary funds are accounted for on a flow of economic resources measurement focus. With this measurement focus, all assets and liabilities associated with the operation of these funds are included on the balance sheet. Fund equity (i.e., net total assets) is segregated into contributed capital and retained earnings components. Proprietary fund type operating statements present increases (i.e., revenues) and decreases (i.e., expenses) in net total assets.

The accrual basis of accounting is utilized by the District. Under this method, revenues are recorded when earned and expenses are recorded at the time the liabilities are incurred.

Capital Assets

The District's investment in utility plant as of December 31, 2019 amounts to \$18,412,030 (net of accumulated depreciation). The investment in utility plant includes the expansion of the water system. The decrease in the District's investment in utility plant (net of accumulated depreciation) for the current year was 27.2% percent, before current depreciation.

Additional information on the District's utility plant can be found in Note (5) of the financial statements.

Debt Administration

At the end of the current fiscal year, the District had total debt outstanding of \$7,001,079. Additional information on the District's long-term debt can be found in Note (14) of the financial statements.

Contacting the District's Financial Management

This financial report is designed to provide our customers, creditors, and other users with a general overview of the District's finances and to show the District's accountability for the money it receives. If you have questions about this report or need additional financial information, contact the District's Manager, at the Southern Water and Sewer District, P.O. Box 610, McDowell, KY 41647, telephone number (606) 377-9296.

SOUTHER WATER AND SEWER DISTRICT
STATEMENT OF NET POSITION
DECEMBER 31, 2019 AND 2018
(with prior year data for comparison purposes only)

	2019	2018
Assets		
Current Assets:		
Cash and Cash Equivalents	\$ 245,060	\$ 36,475
Accounts Receivable (Net of Allowance for Delinquencies of \$199,909 in 2018 and \$241,732 in 2017)	1,292,723	1,097,144
Receivable Sale Pride on River Inventory	1,600,000	-
	55,916	39,503
Total Current Assets	3,193,699	1,173,122
Noncurrent Assets		
Restricted Cash	891,167	637,380
Capital Assets:		
Land	208,285	208,285
Plumbing and Distribution System	39,504,889	44,699,222
Transportation Equipment	485,770	551,048
Furniture, Fixtures and Equipment	200,711	200,711
Construction in Progress	485,893	3,160,904
Total Capital Assets	40,885,548	48,820,170
Less: Accumulated Depreciation	(22,473,518)	(23,532,878)
Net Capital Assets	18,412,030	25,287,292
Other Assets		
Prepaid Interest	98,410	98,410
Less Accumulated Amortization	(44,284)	(41,824)
Total Other Assets	54,126	56,586
Total Noncurrent Assets	19,357,323	25,981,258
Total Assets	\$ 22,551,022	\$ 27,154,380

See accompanying notes to the basic financial statements

SOUTHER WATER AND SEWER DISTRICT
STATEMENT OF NET POSITION
DECEMBER 31, 2019 AND 2018
(with prior year data for comparison purposes only)

	<u>2019</u>	<u>2018</u>
Liabilities		
Current Liabilities		
Accounts Payable	\$ 296,636	\$ 351,559
Accounts Payable Solid Waste	401,821	372,268
Accrued Sick and Vacation pay	73,473	143,919
Customer Deposits	39,849	218,664
Deposit Harold Sewer		2,008,875
Note Payable Line of Credit	225,788	235,773
Note Payable Current	213,786	304,717
Bonds Payable Current	91,000	88,000
Accounts Payable Construction in Progress	9,080	9,080
Accrued Interest	75,841	77,846
Total Current Liabilities	<u>1,427,274</u>	<u>3,810,701</u>
Noncurrent Liabilities		
Notes Payable-Net of Current Portion	3,053,805	3,040,977
Bonds Payable-Net of Current Portion	2,520,000	2,586,000
Total Long Term Liabilites	<u>5,573,805</u>	<u>5,626,977</u>
Total Liabilities	<u>7,001,079</u>	<u>9,437,678</u>
Net Position:		
Invested in Capital Assets, Net of Related Debt	12,231,810	16,945,104
Restricted for Capital Projects	190,444	50,267
Restricted for Maintenance	228,281	191,023
Restricted for Debt Service	288,087	177,500
Restricted for Deposits	184,354	218,590
Unrestricted	2,426,967	134,218
Total Net Position	<u>\$ 15,549,943</u>	<u>\$ 17,716,702</u>

See accompanying notes to the basic financial statements

SOUTHERN WATER AND SEWER DISTRICT
STATEMENT OF REVENUE EXPENDITURE AND CHANGES IN NET POSITION
For the Years Ended December 31, 2019 and 2018
(with prior data for comparison purposes only)

	For the Year Ended December 31	
	2019	2018
Operating Revenue:		
Water Sales	\$ 4,014,408	\$ 2,966,441
Solid Waste Revenue	857,465	869,686
Penalties and Service Charges	68,530	56,765
Other	-	-
Total Operating Revenue	4,940,403	3,892,892
Operating Expenses:		
Water Treatment Supplies	163,217	149,780
Depreciation and Amortization	903,793	892,298
Purchased Water	390,442	352,353
Solid Waste Payments	831,720	843,595
Power for Pumping	325,201	365,312
Outside Services	81,005	47,780
Management Fees	207,637	-
Miscellaneous and Commissioners	46,029	59,460
Insurance	89,335	124,225
Distribution Supplies	329,341	400,781
Payroll and Other Taxes	67,130	77,072
Customer Accounts	133,887	149,087
Wages	625,154	848,941
Sewer Supplies	-	11,321
Employee Benefits	290,004	343,403
Pumping Supplies	37,519	62,618
Total Operating Expense	4,521,414	4,728,026
Operating Income (Loss)	418,989	(835,134)
Non-Operating Revenue (Expense)		
Interest Income	238	524
Interest Expense	(208,192)	(215,195)
Interest and Penalty	(122)	-
Loan Service Fees	(3,325)	(1,669)
Provisions for Bad Debts	(141,221)	(22,171)
Insurance Recovery	-	-
(Loss) Transfer Harold Sewer plant See pg 15	(2,398,810)	-
Gain (Loss) on Sale of Assets	(63,851)	19,300
Total Non-Operating Revenue (Expenses)	(2,815,283)	(219,211)
Income (Loss) Before Capital Contributions	(2,396,294)	(1,054,345)
Capital Contributions		
Grant Income	229,535	592,647
Capital Contributions	-	-
Total Capital Contributions	229,535	592,647
Change in Net Position	(2,166,759)	(461,698)
Total Net Position, Beginning	17,716,702	18,178,400
Total Position Assets, Ending	15,549,943	17,716,702

See accompanying notes to the basic financial statements

SOUTHERN WATER AND SEWER DISTRICT
Statement of Cash Flows
For the Years Ended December 31, 2019 and 2018
(with prior year data for comparison purposes only)

	For the Year Ended December 31	
	2019	2018
Cash flows from operating activity		
Cash received from customers	\$ 4,603,603	\$ 3,951,399
Cash payments to suppliers for goods and services	(3,731,855)	(3,945,903)
Cash received from deposits	(178,815)	16,971
Net cash provided by operating activities	692,933	22,467
Cash flows from noncapital financing activities		
Subsidy From Federal and State Grant	229,535	592,647
Net Cash Provided (Used) By Noncapital Financing Activities	229,535	592,647
Cash flows from capital and related financing activities		
(Increase) decrease in Restricted Assets Accounts	(253,787)	(29,528)
Loan Proceeds	150,000	-
Deposits from Prestonsburg for the Harold Sewer Plant	483,035	546,180
Interest Paid	(210,319)	(218,974)
Principle Payment on Notes	(518,997)	(224,074)
Principle Payment on Bonds	(63,000)	(59,500)
Purchase of Utility Plant in Service	(2,976,064)	(713,496)
Purchase of Automotive Equipment	-	-
Decrease (Increase) in Consturction in progress	2,675,011	71,435
Proceeds from insurance recovery	-	-
Proceeds on Sale of Assets	-	19,300
Net cash provided by (used for) capital and related financing activities	(714,121)	(608,657)
Cash flows from investing activities		
Proceeds from earnings on investments	238	524
Net cash provided by (used for) investing activities	238	524
Total increase (decrease) in cash and cash equivalents	208,585	6,981
Cash and cash equivalents at beginning of year	36,475	29,494
Cash and cash equivalents at end of year (Note 2)	\$ 245,060	\$ 36,475

See accompanying notes to the basic financial statements

SOUTHERN WATER AND SEWER DISTRICT
Statement of Cash Flows
For the Years Ended December 31, 2019 and 2018
(with prior year data for comparison purposes only)

	For the Year Ended December 31	
	2019	2018
Reconciliation of Income from operations to net cash provided by operated activities:		
Income from operations	\$ 418,989	\$ (835,134)
Provisions for Bad Debt	(141,221)	(22,171)
Adjustment to reconcile income from operations to net cash provided by operating activities:		
Operating Activities:		
Depreciation and amortization	903,793	892,298
Changes in assets and liabilities:		
Decrease (increase) in utility accounts receivable	(195,579)	58,507
Decrease (increase) in prepaid expense	-	-
Decrease (increase) in material and supplies inventory	(16,413)	(3,370)
Increase (decrease) in accounts payable and other payable	(95,816)	(82,737)
Increase (decrease) in customer deposits	(178,815)	16,971
Increase (decrease) in accrued interest	(2,005)	(1,897)
Net cash provided by operating activities	\$ <u>692,933</u>	\$ <u>22,467</u>
 Non-cash operating activities		
Acquisition of Property and Equipment Included in accounts payable	\$ <u>11,536</u>	\$ <u>5,651</u>

SOUTHERN WATER AND SEWER DISTRICT
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2019 AND 2018

Note 1 – Summary of Significant Accounting Policies

The significant policies of the district are as follows:

Organization and Business Activities – The district is a governmental organization with its primary activities consisting of sale of water and sewer services to residents in Floyd County Kentucky, pursuant to Chapter 74 of the Kentucky Revised Statutes to operate a water distribution system.

Basis of Accounting – The accounting and reporting policies of the Southern Water and Sewer District relating to the funds included in the accompanying basic financial statements conform to accounting principles generally accepted in the United States of America applicable for local governments. Generally accepted accounting principles for local Governments includes those principles presented by the Governmental Accounting Standards Board (GASB), the American Institute of Certified Public Accountants in the publications entitled Audits of State and Local Governments and by the Financial Accounting Standards Board (when applicable). As allowed in section PBO of GASB's Codification of Governmental Accounting and Financial Reporting Standards the District has elected not to apply Financial Accounting Board Statements and Interpretations, Accounting Research Bulletins of the Committee of Accounting Principle Board Opinions, and Accounting Research Bulletins of the Committee of Accounting and Procedures issued after November 30, 1969. The District first applies restricted resources when an expense is incurred for restricted and unrestricted purposes. The more significant polices of the district are described below.

Basis of Presentation

In accordance with Governmental Accounting Standards Board (GASB) Statement No. 34, the district uses Proprietary Fund financial statement reporting including a Statement of Net Assets, Statements of Revenues, Expenditures and Changes in Net Assets, and a Statement of Cash Flows.

The Statement of Net Assets includes the District's assets and liabilities and provides Information about the nature and amounts of investments in resources (assets) and the obligations to the District's creditors (liabilities). The difference between the assets and liabilities is shown as net assets. The statement also provides the basis of evaluating the capital structure of the district and assessing its liquidity and financial flexibility.

The statement of Revenue, Expenditure and Changes in Net Assets accounts for the current year's revenue and expense. This statement measures the success of the district's operations over the past year and determines whether the district has recovered its cost through user fees and other charges.

The final required financial statement is the Statement of Cash Flows. This statement reports cash receipts, cash disbursements, and changes in cash resulting from operations and investments during the reporting period.

SOUTHERN WATER AND SEWER DISTRICT
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2019 AND 2018

Note 1 – Summary of Significant Accounting Policies (Continued)

The Notes to the basic financial statements provide a description of the accounting policies used to prepare the financial statements and present disclosures required by generally accepted accounting principles that are not otherwise present in the financial statements.

The District's basic financial statements include the accounts of all district operations. The District's criteria for including organizations as component units with the District's reporting entity, as set forth in Section 2100 of GASB's Codification of Governmental Accounting and Financial Standards includes whether:

- The Organization is legally separate (can sue and be sued in their own name).
- The District holds the corporate powers of the organization.
- The District appoints voting majority of the organization.
- The Organization has the potential to impose a financial benefit/burden on the Association.
- There is fiscal dependency by the organization on the District.

Component Unit Presentation – Based on the aforementioned criteria the district has no component units.

Cash - For the purpose of the statement of cash flows, the District considers cash to include cash on hand and unrestricted cash in bank.

Inventory – Inventory consists primarily of pipes and supplies to be used for future expansion and repairs of existing lines. Inventory is valued at the lower of cost or market under first-in, first-out (FIFO) method.

Allowance for Doubtful Accounts – The District utilizes the allowance method for accounting for bad debts. This method is based on historical experience and evaluation of outstanding accounts at year end. The Allowance for Doubtful as of December 31, 2019 and 2018 is \$235,708 and \$199,909.

Operating and Non – Operating Revenue – Only water and solid waste revenue and related service charges and penalties are considered as operating revenue.

Applying Resources – Restricted resources are applied first for expenses incurred for which both restricted and unrestricted net assets are available.

Use of 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. Accordingly, actual results can differ from those estimates.

SOUTHERN WATER AND SEWER DISTRICT
 NOTES TO FINANCIAL STATEMENTS
 DECEMBER 31, 2019 AND 2018

Note 2 – Restricted Cash Accounts

The District had the following restricted cash accounts as of December 31, 2019 and 2018.

	<u>2019</u>	<u>2018</u>
KIA Project	\$ 23,051	\$ 57,830
Repair and Maintenance reserve	228,282	191,023
Construction reserve	190,444	42,381
Bond Depreciation Reserve	190,906	71,238
Road Construction Account	0	7,886
Deposit Refunds	184,354	218,590
Insurance Reserve	<u>74,130</u>	<u>48,432</u>
Totals	<u>\$ 891,167</u>	<u>\$ 637,380</u>

The amounts held were below the required minimum for 2019 and 2018 for all restricted requirements.

Note 3 – Prepaid Items

Prepaid items include prepayment of service contracts, software rights and insurance. These amounts represent payments made in the current year for which services will be provided in the subsequent fiscal year.

Note 4 – Deposits with Financial Institutions

As of December 31, 2019, the company had amounts of \$1,136,227 on deposit with financial institutions with \$250,000 insured by FDIC and \$886,227 insured by pledged US Treasury Bills.

As of December 31, 2018, the company had amounts of \$673,855 on deposit with financial institutions with \$250,000 insured by FDIC and \$958,879 insured by pledged US Treasury Bills.

Note 5 – Transfer of Pride on River Extraordinary Event

Southern Water and Sewer District and the Prestonsburg City's Utilities Commission entered into an agreement for Prestonsburg City's Utilities Commission to purchase the sewer operations and assets from the District. Prestonsburg City's Utilities Commission took over the operations on July 1, 2017. After appraisal and completion of the transfer, Southern Water and sewer recognized realized loss of \$\$2,398,810.

SOUTHERN WATER AND SEWER DISTRICT
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2019 AND 2018

Note 6 – Subsequent Events

In preparing these financial statements, the District has evaluated events and transactions for the potential recognition or disclosure through October 21, 2020, the date the financial statements were available to be issued.

As a result of the spread of the COVID-19 coronavirus, economic uncertainties have arisen which could negatively impact Net Assets. Other financial impact could occur however such potential impact is unknown at this time.

Note 7 – Capital and Net Assets

Changes in contributed capital and net assets during the years ended December 31, 2019 and December 31, 2018.

	Contributed <u>Capital</u>	<u>Reserves</u>	Net Assets <u>(Deficit)</u>	<u>Total</u>
Balance December 31, 2017	<u>\$35,251,120</u>	<u>\$ 270,910</u>	<u>\$(17,343,630)</u>	<u>\$18,178,400</u>
Federal Grants and Loans	109,449			109,449
Department of transportation	25,452			25,452
State Contribution DOT				
Grant in Aid – Fema	74,037			74,037
Other				
Transfer		29,528	(29,528)	
Net Income (Loss)			<u>(670,636)</u>	<u>(670,636)</u>
Balance December 31, 2018	<u>\$35,460,058</u>	<u>\$ 300,438</u>	<u>\$(18,043,794)</u>	<u>\$17,716,702</u>
Federal Grants and Loans	115,705			115,705
Department of transportation				
Grant in aid-State Grant Funds				
State Contribution DOT				
Grant in Aid – Fema	113,830			113,830
Other				
Transfer		253,787	(253,787)	
Net Income (Loss)			<u>(2,396,294)</u>	<u>(2,396,294)</u>
Balance December 31, 2019	<u>\$35,689,593</u>	<u>\$554,225</u>	<u>\$(20,693,875)</u>	<u>\$15,549,943</u>

Note 8 Retirement Plan

The District maintains a defined contribution retirement plan under the provisions of section 401 (K) of the Internal Revenue Code. The plan is a deferred compensation plan which is available to all employees. The maximum salary deferral is limited to amounts allowed per the Internal Revenue Code, which for 2019 and 2018 was \$19,000 and \$18,500 respectively. Normally the District contributes 3% of the employee's basic pay. All contributions are immediately vested. Expenses charged to operations for the retirement plan were \$12,847 and \$19,452 respectively.

SOUTHERN WATER AND SEWER DISTRICT
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2019 AND 2018

Note 9 – Risk Management

Significant losses covered by commercial insurance with premiums (based on industry information adjusted for any District Claims) for general liability, vehicles, personal and real property. Settlement amounts have not exceeded insurance coverage for the current year or the prior years.

Note 10 - Property and Equipment

Capital assets, which include property, plant, equipment and vehicles, are reported in the applicable governmental column in the government – wide financial statements. All capital assets are valued at their historical cost or estimated historical cost if actual historical is not available. Donated assets are valued at their market value on the date donated. Repairs and maintenance are recorded as expenses. Renewals and betterments are capitalized.

Depreciation has been calculated on each class of depreciable property using the straight – line method. Estimated useful lives are as follows.

Depreciation has been calculated on each class of depreciable property using the straight – line method. Estimated useful lives are as follows:

Buildings	20 – 50 Years
Improvements	20 – 50 Years
Vehicles	5 – 10 Years
Equipment	7 – 20 Years

The following summarizes the changes to capital assets for 2019:

	Balance <u>01/01/19</u>	Additions	Disposals	Balance <u>12/31/18</u>
Land	\$ 208,285	\$ 0	\$ -0-	\$ 208,285
Water and Distribution System	44,699,222	2,863,879	8,058,212-	39,504,889
Automotive Equipment	551,048	4,995	70,273	485,770
Furniture, fixtures and Equipment:	200,711	0	-0-	200,711
Construction in Progress	<u>3,160,904</u>	<u>107,190-</u>	<u>2,782,201</u>	<u>485,893</u>
OTAL ASSETS	\$ 48,820,170	\$ 2,976,064	\$ 10,910,686	\$ 40,885,548
Less				
Accumulated Depreciation				
Water Distribution System	23,073,150	837,633	1,890,420	22,020,363
Automotive Equipment	333,740	56,074	70,273	319,541
Furniture, fixtures and Equipment:	<u>125,988</u>	<u>7,626</u>	<u>-0-</u>	<u>133,614</u>
Total Accumulated	23,532,878	901,333	1,960,693	22,473,518
Balance – December 31	<u>\$ 25,278,292</u>			<u>\$ 18,412,030</u>

SOUTHERN WATER AND SEWER DISTRICT
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2019 AND 2018

Note 10 - Property and Equipment (Continued)

The following summarizes the changes to capital assets for 2018:

	Balance <u>01/01/18</u>	Additions	Disposals	Balance <u>12/31/18</u>
Land	\$ 206,256	\$ 2,029	\$ -0-	\$ 208,285
Water and Distribution System	43,989,850	709,372	0	44,699,222
Automotive Equipment	600,847	0	49,799	551,048
Furniture, fixtures and Equipment:	198,616	2,095	-0-	200,711
Construction in Progress	<u>3,232,338</u>	<u>0</u>	<u>71,434-</u>	<u>3,160,904</u>
TOTAL ASSETS	\$ 48,227,907	\$ 713,496	\$ 121,233	\$ 48,820,170
Less				
Accumulated Depreciation				
Water Distribution System	22,262,877	810,273	0	23,073,150
Automotive Equipment	312,870	70,669	49,799	333,740
Furniture, fixtures and Equipment:	<u>117,093</u>	<u>8,895</u>	<u>-0-</u>	<u>125,988</u>
Total Accumulated	22,692,840	889,837	49,799	23,532,878
Balance – December 31	<u>\$ 23,535,067</u>			<u>\$ 25,278,292</u>

Note 11 – Concentrations of Credit Risk

Concentrations of credit risk are limited due to the large number of customers comprising the district's customer base.

Note 12 – Notes and Bonds Payable

All notes and bonds are secured by the Water Distributions system and related assets unless stated as non – secured:

	<u>2019</u>	<u>2018</u>
Summary of Short term line of Credit		
6.25% line of credit First Guaranty National Bank interest due monthly. With principal due upon demand	\$ 225,788	\$ 235,773

SOUTHERN WATER AND SEWER DISTRICT
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2019 AND 2018

Note 13 – Notes and Bonds Payable (Continued)

	<u>2019</u>	<u>2018</u>
Summary of Notes Payable		
a) Kentucky Infrastructure Authority 3% installment note, 60 semi - annual payments of \$34,607 including interest due 06/01 and 12/1. Final payment 2024	\$ 319,161	\$ 377,485
b) Kentucky Infrastructure Authority 3% installment note, 60 semi – annual payments of \$71,898 including interest due 06/01 and 12/1. Final payment 2027	1,016,007	1,126,822
c) A purchase agreement, original balance of \$25,018 At 5.9% interest, secured by vehicle; payments are \$483 for 60 months maturing September 2019	0	4,239
d) First Guaranty Bank 4.25 installment note monthly payments of \$1990 including interest final Balloon payment during November 2019 Secured by 5 trucks	87,518	105,581
e) First Guaranty Bank, 4.316% installment note monthly payments of \$940 including interest final payment 2019	0	5,567
f) Regions Bank, 2.6% to convert to RD installment Note \$45,188 principal Jan 1 plus interest and interest only payment each July 1. Maturity January 2056.	1,701,000	1,726,000
g) First Guaranty Bank 4.571% installment note monthly payments of \$2,090 including interest payment during August 2026 Secured by trucks	143,905	0
Total long – term Notes Payable	<u>\$ 3,267,591</u>	<u>\$ 3,345,694</u>
Less Current maturities	<u>213,786</u>	<u>304,717</u>
Notes Payable less current portion	<u>\$ 3,053,805</u>	<u>\$3,040,977</u>

SOUTHERN WATER AND SEWER DISTRICT
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2019 AND 2018

Summary of Bonds Payable

a) Rural Development Revenue Bonds 4.5% installments, with set principal and interest payment due on the first of each year and an interest payment due each July 1. Final payment 2042.	\$ 1,970,000	\$ 2,019,000
b) Rural Development Revenue Bonds 4.25% installments, with set principal and interest payment due on the first of each year and an interest payment due each July 1. Final payment 2044.	183,000	187,000
c) Rural Development Revenue Bonds 2.25% installments, with set principal and interest payment due on the first of each year and an interest payment due each July 1. Final payment 2049.	<u>458,000</u>	<u>468,000</u>
Total Long – Term Bonds Payable	<u>\$ 2,611,000</u>	<u>\$ 2,674,000</u>
Less Current maturities	<u>91,000</u>	<u>88,000</u>
Notes Payable less current portion	<u>\$ 2,520,000</u>	<u>\$ 2,586,000</u>

Note

Following are maturities of long – term debt as of December 31, 2019:

	<u>Principal</u>	<u>Interest</u>
2020	\$ 304,786	\$ 173,646
2021	334,801	163,574
2022	342,387	153,155
2023	361,895	142,377
2024	356,520	132,743
2025-2029	1,089,083	530,937
2030-2034	739,940	398,917
2035-2039	861,440	264,629
2040-2044	807,940	156,690
2045-2049	334,440	105,690
2050-2054	225,940	37,218
2055-2059	<u>119,420</u>	<u>12,719</u>
Total	<u>\$ 5,878,592</u>	<u>\$ 2,272,295</u>

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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

October 21, 2020

To the Board of Commissioners
Southern Water and Sewer District
McDowell, KY

I 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 business-type activities, each major fund, and the aggregate remaining fund information of Southern Water and Sewer District, (a Kentucky Special District) as of and for the year ended December 31, 2019, and the related notes to the financial statements; which collectively comprise Southern Water and Sewer District's basic financial statements and have issued my report thereon dated October 21, 2020.

Internal Control Over Financial Reporting

In planning and performing my audit of the financial statements, I considered Southern Water and Sewer 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 my opinion on the financial statements; but not for the purpose of expressing an opinion on the effectiveness of Southern Water and Sewer District's internal control. Accordingly, I do not express an opinion on the effectiveness of Southern Water and Sewer 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 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*, or a combination of deficiencies in internal control 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.

My 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. Given these limitations, during my audit I did not identify any deficiencies in internal control that I consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Southern Water and Sewer District's financial statements are free of material misstatement, I 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 my audit, and, accordingly, I do not express such an opinion. The results of my tests disclosed no instances of noncompliance or other matters that are required to be reported under Government Auditing Standards.

Purpose of this Report

The purpose of this report is solely to describe the scope of my testing on 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 purposes.



Richard F. Paulmann, LLC
October 21, 2020