

AUDIT REPORT

MCLEAN-SHERIDAN RURAL WATER DISTRICT
Turtle Lake, North Dakota

For the Year Ended December 31, 2017

RATH & MEHRER, P.C.
CERTIFIED PUBLIC ACCOUNTANTS

MCLEAN-SHERIDAN RURAL WATER DISTRICT
Turtle Lake, North Dakota

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MCLEAN-SHERIDAN RURAL WATER DISTRICT
Turtle Lake, North Dakota

DISTRICT OFFICIALS

Clifton Dockter	Chairman
Eldon Erhman	Vice Chairman
Char Anderson	Secretary/Treasurer
Walter Lipp	Board Member
Marshall Maxwell	Board Member
Lynn Oberg	Board Member
Darwin Saari	Board Member
Lynn Oberg	General Manager
Ann Oberg	Office Manager

Rath & Mehrer, P.C.

Certified Public Accountants

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INDEPENDENT AUDITOR'S REPORT

Board of Directors
McLean-Sheridan Rural Water District
Turtle Lake, North Dakota

Report on the Financial Statements

We have audited the accompanying financial statements of the major fund of the McLean-Sheridan Rural Water District, Turtle Lake, North Dakota, as of and for the year ended December 31, 2017, and the related notes to the financial statements, which collectively comprise the district's basic financial statements as 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

Our responsibility is to express opinions 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 judgement, 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 district'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 district'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 respective financial position of the major fund of the McLean-Sheridan Rural Water District, Turtle Lake, North Dakota, as of December 31, 2017, and the respective changes in financial position and cash flows, where applicable, for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 4 through 8 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We 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 the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated March 23, 2018 on our consideration of the 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 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 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 district's internal control over financial reporting and compliance.



Rath and Mehrer, P.C.

Bismarck, North Dakota

March 23, 2018

MCLEAN-SHERIDAN RURAL WATER DISTRICT

Management's Discussion and Analysis

December 31, 2017

The Management's Discussion and Analysis (MD&A) of the McLean-Sheridan Rural Water District's financial performance provides an overall review of the district's financial activities for the fiscal year ended December 31, 2017. The intent of the MD&A is to look at the district's financial performance as a whole. It should, therefore, be read in conjunction with the basic financial statements and related notes.

The MD&A is a new element of the Required Supplementary Information specified in the Government Accounting Standards Board's (GASB) Statement No. 34 "*Basic Financial Statements - and Management's Discussion and Analysis - For State and Local Governments*". Certain comparative information between the current fiscal year and the prior year is required to be presented in the MD&A.

FINANCIAL HIGHLIGHTS

Key financial highlights for the year ended December 31, 2017 are as follows:

- * Total net position of the district increased \$187,077 as a result of the current year's operations.
- * Enterprise Fund net position totaled \$6,278,950.
- * Total revenues from all sources were \$998,709.
- * Total expenses were \$811,632.

USING THIS ANNUAL REPORT

This annual report presents the following two components of the financial statements:

1. Fund financial statements provide detailed information for the district's significant fund.
2. Notes to the financial statements provide additional information that is essential to understanding the fund statements.

Fund Financial Statements

A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The McLean-Sheridan Rural Water District uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements.

The fund financial statements provide detailed information about the district's significant fund. The district's fund is considered a proprietary fund.

Proprietary Funds - The McLean-Sheridan Rural Water District maintains one type of proprietary funds. Enterprise funds are used to report activities that charge for services it provides to outside customers. The district uses its enterprise fund to account for its water distribution system.

Notes to the Financial Statements

The notes provide additional information that is essential to a full understanding of the data provided in the fund financial statements.

FINANCIAL ANALYSIS OF THE DISTRICT

Table I provides a summary of the district's net position as of December 31, 2017. A comparative analysis of district-wide data is presented for both current and prior year.

As indicated in the financial highlights above, the district's net position increased by \$187,077 for the year ended December 31, 2017. Changes in net position may serve over time as a useful indicator of the district's financial position.

As of December 31, 2017, the district's net position of \$6,278,950 is segregated into three separate categories. Net investment in capital assets represents 90% of the district's total net position. It should be noted that these assets are not available for future spending. The restricted component of net position represents 8% of the district's net position and represents resources that are subject to external restrictions on how they must be spent. The remaining unrestricted component of net position represents 2% of the district's net position and is available to meet the district's ongoing obligations.

Table I
Net Position
As of December 31, 2017
(With comparative totals for December 31, 2016)

	<u>2017</u>	<u>2016</u>
<u>Assets</u>		
Current Assets	639,748	492,414
Capital Assets (net of accumulated depreciation)	8,498,196	8,610,617
Total Assets	9,137,944	9,103,031
<u>Liabilities</u>		
Current Liabilities	163,835	155,000
Long-Term Liabilities	2,695,158	2,856,158
Total Liabilities	2,858,993	3,011,158
<u>Net Position</u>		
Net Investment in Capital Assets		
Restricted	5,642,038	5,599,459
Unrestricted	516,921	342,697
	119,991	149,717
Total Net Position	6,278,950	6,091,873
	=====	=====

Table II shows the changes in net position for the fiscal year ended December 31, 2017. A comparative analysis of district-wide data is presented for both current and prior year.

Table II
Changes in Net Position
As of December 31, 2017
(With comparative totals for December 31, 2016)

	2017	2016
Revenues		
<u>Program Revenues:</u>		
Charges for Services	854,472	817,906
Operating Grants and Contributions	8,000	10,000
Capital Grants and Contributions	71,422	9,594
<u>General Revenues:</u>		
Interest Earnings and Other Revenue	57,516	12,527
Gain on Sale of Capital Assets	7,300	2,550
Total Revenues	998,709	852,578
Expenses		
Enterprise	811,632	807,694
Net Change in Position	187,077	44,884

Operating grants and contributions constituted 1%, capital grants and contributions 7% and charges for services made up 86% of the total revenues of all activities of the district for the fiscal year ended December 31, 2017.

Enterprise services constituted 100% of total expenses for all activities during the fiscal year ended December 31, 2017.

CAPITAL ASSETS

As of December 31, 2017, the district had \$8,498,196 invested in capital assets. The following table shows the balance as of December 31, 2017.

Table III
Capital Assets
(Net of Accumulated Depreciation)
As of December 31, 2017
(With comparative totals for December 31, 2016)

	2017	2016
Construction in Progress	2,274,807	2,206,058
Buildings and Infrastructure	5,913,787	6,078,942
Vehicles	23,192	34,519
Other Assets	286,410	291,098
Total (net of depreciation)	8,498,196	8,610,617

This total represents a decrease of \$112,421 in capital assets from January 1, 2017. This change includes the ongoing construction of water lines to Brush Lake and the sale of a 2012 Ford F250 pickup. For a detailed breakdown of the additions and deletions to capital assets, readers are referred to Note 4 to the audited financial statements which follow this analysis.

DEBT ADMINISTRATION

As of December 31, 2017, the district had \$2,856,158 in outstanding debt of which \$161,000 was due within one year. During fiscal year 2017, the district did not issue any new long-term debt obligations.

For a detailed breakdown of the long-term debt, readers are referred to Note 6 to the audited financial statements which follow this analysis.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES

Water sales for 2017 increased \$36,566 from the prior year. This was the result of an increase of approximately 15 patrons from the prior year and fluctuation in water usage. The rural water district's operating expenses for 2017 increased by \$11,151 compared to the totals for 2016. This was mainly due to an increase in employee salaries and benefits of \$18,664 being offset by various fluctuations in other operating expenses. Overall, the district reported an operating income of \$127,129 compared to \$101,714 for the prior year.

Starting January 1, 2018, the district increased its minimum water charge from \$49 to \$59 and effective April 15, 2018, rates for bulk water sales will increase by \$.50, from \$3.30 to \$3.80. The district expects these increased rates to generate an additional \$75,000 in water sales.

System maintenance costs are expected to remain the same as in previous years. The district is committed to the repair and replacement of all major pumps, motors and variable drives as needed to keep the system in good working condition.

The McLean-Sheridan Rural Water District is working on an expansion of services to the Brush Lake/Blue Lake area north of the City of Mercer, located in McLean County. This expansion project has the potential of adding an additional 250 water users in future years and currently has about 135 new water users committed to use water with this project. The district is working with the North Dakota State Water Commission and has been approved for a total of \$1,435,000 in grant funding for this expansion project. During the year ending December 31, 2017, the district received a total of \$71,422 in grant funds. The district has received a total of \$1,300,526 of funding for this project since its commencement in 2013. The governing board has voted to approve a long-term loan of \$1,350,000 to finance the balance of the project and has been approved to receive this funding as part of the Drinking Water State Revolving Fund Program from the North Dakota Public Finance Authority. During the year, the district did not request any additional funds from the North Dakota Public Finance Authority. Since the inception of this project, the district has received a total of \$1,280,158 of the \$1,350,000 available. As of December 31, 2017, this project is approximately 98% completed and is estimated to be completed during 2018.

The district has been approved by the North Dakota State Water Commission for an application for phase 1 of the construction of a water tower. This project consist of the construction of a 350,000 gallon water tower in the City of Turtle Lake. The water district would use 250,000 gallons for storage so as to allow the system to provide additional water to other parts of the water system. Phase 1 of this project includes pre-construction engineering through the bid phase. If approved, work on this project would start later in 2018.

The district's governing board will continue to review the operating budget and cash flow in 2018 to determine if the rates are adequate to maintain required levels of operating funds to make timely loan payments and replace worn or outdated equipment.

CONTACTING THE WATER RESOURCE DISTRICT'S FINANCIAL MANAGEMENT

This financial report is designed to provide our patrons and creditors with a general overview of the water resource district's finances and to show the water resources district's accountability for the money it receives to provide the best possible services to the rural water users. Anyone who has questions about information contained in this report or who is interested in receiving additional information is encouraged to contact McLean-Sheridan Rural Water District, Turtle Lake, ND 58575.

MCLEAN-SHERIDAN RURAL WATER DISTRICT
Turtle Lake, North Dakota

Statement of Net Position
Proprietary Fund
December 31, 2017

	Enterprise Fund
<u>ASSETS</u>	
<u>Current Assets:</u>	
Cash and Cash Equivalents	396,909.65
Investments	172,935.00
Accounts Receivable	69,902.92
Total Current Assets	639,747.57
<u>Noncurrent Assets:</u>	
Capital Assets (net of accumulated depr):	
Construction in Progress	2,274,807.00
Buildings and Infrastructure	5,913,787.00
Vehicles	23,192.00
Other Assets	286,410.00
Total Noncurrent Assets	8,498,196.00
Total Assets	9,137,943.57
<u>LIABILITIES</u>	
<u>Current Liabilities:</u>	
Payroll Taxes Payable	2,835.49
Revenue Bonds Payable	161,000.00
Total Current Liabilities	163,835.49
<u>Noncurrent Liabilities:</u>	
Revenue Bonds Payable	2,695,158.00
Total Liabilities	2,858,993.49
<u>NET POSITION</u>	
Net Investment in Capital Assets	5,642,038.00
Restricted for Debt Service	516,921.37
Unrestricted	119,990.71
Total Net Position	6,278,950.08

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

MCLEAN-SHERIDAN RURAL WATER DISTRICT
Turtle Lake, North Dakota

Statement of Revenues, Expenses and Changes in Fund Net Position
Proprietary Fund

For the Year Ended December 31, 2017

	Enterprise Fund
<u>Operating Revenues:</u>	
Charges for Sales and Services:	
Water Sales	845,202.91
Late Fees	9,269.06
Total Operating Revenues	854,471.97
<u>Operating Expenses:</u>	
Governing Board	9,695.14
Salaries and Benefits	199,897.73
Workman's Compensation	811.55
Utilities	82,420.06
Chemicals	22,248.80
Supplies	693.99
Office Expense	16,055.30
Repairs and Maintenance	96,333.77
Vehicle Expense	31,725.70
Insurance	5,041.35
Professional Fees	8,368.00
Education and Training	4,201.82
Water Purchases	44,390.84
Advertising	2,361.81
Dues and Subscriptions	2,227.00
Depreciation	196,175.00
Other	4,695.26
Total Operating Expenses	727,343.12
Operating Income	127,128.85
<u>Non-Operating Revenues (Expenses):</u>	
Garrison Diversion Conservancy District:	
MR&I Funds	71,421.89
Connection Fees	8,000.00
Proceeds from Legal Settlement	50,000.00
Interest/Dividend Income	6,639.33
Gain on Sale of Capital Assets	7,300.00
Other Revenues	876.27
Other Expenses	(3,760.01)
Interest Expense	(72,334.43)
Service Charges	(8,194.86)
Total Non-Operating Revenues (Expenses)	59,948.19
Change in Net Position	187,077.04
Net Position - January 1	6,091,873.04
Net Position - December 31	6,278,950.08

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

MCLEAN-SHERIDAN RURAL WATER DISTRICT
Turtle Lake, North Dakota

Statement of Cash Flows
Proprietary Fund
For the Year Ended December 31, 2017

	Enterprise Fund
<u>Cash flows from operating activities:</u>	
Receipts from customers	851,125.35
Payments to suppliers	(331,270.39)
Payments to employees	(197,062.24)
Net cash provided (used) by operating activities	322,792.72
<u>Cash flows from noncapital financing activities:</u>	
Connection fees	8,000.00
Proceeds from legal settlement	50,000.00
Other receipts	876.27
Other disbursements	(3,760.01)
Net cash provided (used) by noncapital financing activities	55,116.26
<u>Cash flows from capital and related financing activities:</u>	
Garrison Diversion Conservancy District Grants:	
MR&I funds	71,421.89
Sale of capital assets	7,300.00
Purchase of capital assets	(15,005.00)
Brush lake project	(68,749.00)
Principal payments	(155,000.00)
Interest expense	(72,334.43)
Service charges	(8,194.86)
Net cash provided (used) by capital and related financing activities	(240,561.40)
<u>Cash flows from investing activities:</u>	
Interest/dividend income	6,639.33
Net increase in cash and cash equivalents	143,986.91
Cash and cash equivalents, January 1	252,922.74
Cash and cash equivalents, December 31	396,909.65

(continued)

MCLEAN-SHERIDAN RURAL WATER DISTRICT
Turtle Lake, North Dakota

Statement of Cash Flows
Proprietary Fund
For the Year Ended December 31, 2017
(continued)

	<u>Enterprise Fund</u>
<u>Reconciliation of Operating Income to Net Cash Provided (Used) by Operating Activities</u>	
Operating income	127,128.85
<u>Adjustments to reconcile operating income to net cash provided (used) by operating activities:</u>	
Depreciation expense	196,175.00
Net (increase) in accounts receivable	(3,346.62)
Net increase in payroll taxes payable	2,835.49
Net cash provided (used) by operating activities	<u>322,792.72</u> =====

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

MCLEAN-SHERIDAN RURAL WATER DISTRICT
Turtle Lake, North Dakota

Notes to the Financial Statements
December 31, 2017

Note 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The financial statements of the water resource district have been prepared in conformity with accounting principles generally accepted in the United States of America (GAAP) as applied to government units. The Government Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. The more significant of the government's accounting policies are described below.

A. Financial Reporting Entity

The accompanying financial statements present the activities of the water resource district. The water resource district has considered all potential component units for which the water resource district is financially accountable and other organizations for which the nature and significance of their relationships with the water resource district are such that exclusion would cause the district's financial statements to be misleading or incomplete. The Government Accounting Standards Board has set forth criteria to be considered in determining financial accountability. This criteria includes appointing a voting majority of an organization's governing body and (1) the ability of the water resource district to impose its will on that organization or (2) the potential for the organization to provide specific financial benefits to, or impose specific financial burdens on the district.

Based on these criteria, there are no component units to be included within the McLean-Sheridan Rural Water District as a reporting entity.

B. Basis of Presentation

Governments engaged only in a single business-type activity should present only the financial statements required for enterprise funds.

Fund Financial Statements: The fund financial statements provide information about the water resource district's fund. The emphasis of fund financial statements is on the major enterprise fund.

Proprietary fund operating revenues, such as charges for services, result from exchange transactions associated with the principal activity of the fund. Exchange transactions are those in which each party receives and gives up essentially equal values. Nonoperating revenues, such as subsidies and investments earnings, result from nonexchange transactions or ancillary activities.

The water resource district reports the following major enterprise fund:

Enterprise Fund. This fund accounts for the activities of the district's water distribution system.

C. Measurement Focus and Basis of Accounting

Measurement focus is a term used to describe "how" transactions are recorded within the various financial statements. Basis of accounting refers to "when" transactions are recorded regardless of the measurement focus applied.

Measurement Focus

The proprietary funds utilize an "economic resources" measurement focus. The accounting objectives of this measurement focus are the determination of operating income, changes in net position (or cost recovery), financial position and cash flows. All assets and liabilities (whether current or noncurrent, financial or nonfinancial) associated with their activities are reported. Proprietary fund equity is classified as net position.

Basis of Accounting

The fund financial statements are reported using a 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. Nonexchange transactions, in which the district gives (or receives) value without directly receiving (or giving) equal value in exchange, include grants, entitlements and donations. On an accrual basis, revenue from grants, entitlements and donations is recognized in the fiscal year in which all eligibility requirements have been satisfied.

D. Cash, Cash Equivalents and Investments

Cash and cash equivalents include amounts in demand deposits, money market accounts and highly liquid short-term investments with original maturities of three months or less.

Investments consist of certificates of deposit, stated at cost.

E. Capital Assets

Capital assets include plant and equipment. Capital assets are defined by the water resource district as assets with an initial, individual cost of \$5,000 or more. Such assets are recorded at cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at estimated fair market value at the date of donation. The costs of normal maintenance and repairs that do not add to the value of the asset or materially extend assets lives are not capitalized. Major outlays for capital assets and improvements are capitalized as projects are constructed. Interest incurred during the construction phase of capital assets is not capitalized.

Capital assets are depreciated using the straight line method over the following estimated useful lives:

Buildings and Infrastructure	6 to 80 years
Vehicles	5 years
Other Assets	5 to 20 years

F. Compensated Absences

No liability is recorded for nonvesting accumulating rights to receive sick pay benefits.

Vested or accumulated vacation leave is not reported as it is considered immaterial.

G. Long-Term Obligations

The long-term debt financed from the proprietary fund operations are accounted for in those funds.

H. Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America, requires management to make estimates and assumptions that affect certain reported amounts and disclosures (such as estimated useful lives in determining depreciation expense); accordingly, actual results could differ from those estimates.

Note 2 DEPOSITS AND INVESTMENTS

In accordance with North Dakota Statutes, the district maintains deposits at the depository banks designated by the governing board. All depositories are members of the Federal Reserve System.

Deposits must either be deposited with the Bank of North Dakota or in other financial institutions situated and doing business within the state. Deposits, other than with the Bank of North Dakota, must be fully insured or bonded. In lieu of a bond, a financial institution may provide a pledge of securities equal to 110% of the deposits not covered by insurance or bonds.

Authorized collateral includes bills, notes or bonds issued by the United States government, its agencies or instrumentalities, all bonds and notes guaranteed by the United States government, Federal Land Bank bonds, bonds, notes, warrants, certificates of indebtedness, insured certificates of deposit, shares of investments companies registered under the Investment Companies Act of 1940, and all other forms of securities issued by the State of North Dakota, its boards, agencies or instrumentalities or by any county, city, township, school district, park district or any other political subdivision of the State of North Dakota, whether payable from special revenues or supported by the full faith and credit of the issuing body and bonds issued by another state of the United States or other securities approved by the banking board.

At December 31, 2017 the water resource district's carrying amount of deposits was \$569,845 and the bank balance was \$602,489. Of the bank balance, \$329,940 was covered by Federal Depository Insurance. The remaining balance of \$272,549 was collateralized with securities held by the pledging financial institution's agent in the government's name.

Credit Risk

The water resource district may invest idle funds as authorized in North Dakota Statutes, as follows:

- (1) Bonds, treasury bills and notes, or other securities that are a direct obligation insured or guaranteed by, the treasury of the United States, or its agencies, instrumentalities or organizations created by an act of Congress.
- (2) Securities sold under agreements to repurchase written by a financial institution in which the underlying securities for the agreement to repurchase are of the type listed above.
- (3) Certificates of deposit fully insured by the federal deposit insurance corporation.
- (4) Obligations of the State.

At December 31, 2017 the water resource district held certificates of deposit in the amount of \$172,935, which are all considered deposits.

Concentration of Credit Risk

The water resource district does not have a limit on the amount the district may invest in any one issuer.

Note 3 ACCOUNTS RECEIVABLE

Accounts receivable consist of amounts due from patrons for monthly water usage.

Note 4 CAPITAL ASSETS

The following is a summary of changes in capital assets for the year ended December 31, 2017:

	<u>Balance January 1</u>	<u>Increases</u>	<u>Decreases</u>	<u>Balance December 31</u>
<i>Capital assets not being depreciated:</i>				
Construction in Progress	2,206,058	68,749		2,274,807
<i>Capital assets being depreciated:</i>				
Buildings and Infrastructure	9,867,555			9,867,555
Vehicles	81,625		24,991	56,634
Other Assets	370,143	15,005		385,148
Total	10,319,323	15,005	24,991	10,309,337
<i>Less accumulated depreciation for:</i>				
Buildings and Infrastructure	3,788,613	165,155		3,953,768
Vehicles	47,106	11,327	24,991	33,442
Other Assets	79,045	19,693		98,738
Total	3,914,764	196,175	24,991	4,085,948
Total capital assets being depreciated, net	6,404,559	(181,170)		6,223,389
Total Capital Assets	8,610,617	(112,421)	-0-	8,498,196

Depreciation expense was charged to functions/programs of the water resource district as follows:

Enterprise Fund	196,175
	=====

Note 5 PAYROLL TAXES PAYABLE

Payroll taxes payable consist of amounts owed to federal and state agencies for taxes withheld from employee's salaries as of December 31, but not yet remitted.

Note 6 LONG-TERM DEBT

Changes in Long-Term Liabilities. During the year ended December 31, 2017, the following changes occurred in liabilities reported in the long-term debt of the enterprise fund:

	<u>Balance</u> <u>January 1</u>	<u>Increases</u>	<u>Decreases</u>	<u>Balance</u> <u>December 31</u>	<u>Due Within</u> <u>One Year</u>
Revenue Bonds Payable	3,011,158	-0-	155,000	2,856,158	161,000
	=====	=====	=====	=====	=====

Outstanding debt at December 31, 2017 consists of the following:

Revenue Bonds. The water resource district has issued bonds whereby the district pledges income derived from the acquired or constructed assets to pay debt service. Revenue bonds outstanding at December 31, 2017 are as follows:

\$1,645,000 Water Revenue Refunding Bonds, Series 2014B, due in annual installments of \$75,000 to \$135,000 through September 1, 2029; interest is at 2% to 3.5%.	1,345,000.00
\$519,104 Rural Water System Revenue Bonds, due in annual installments of \$26,000 to \$32,000 through September 1, 2027; interest is at 2.5%.	291,000.00
Total Revenue Bonds	1,636,000.00

The annual requirements to amortize the outstanding revenue bonds are as follows:

<u>Year Ending</u> <u>December 31</u>	<u>Principal</u>	<u>Interest</u>
2018	131,000	45,050
2019	132,000	42,300
2020	132,000	39,525
2021	138,000	36,750
2022	144,000	33,850
2023-2027	749,000	105,988
2028-2029	210,000	9,975
Total	1,636,000	313,438

The water resource district also received funding as part of the Drinking Water State Revolving Fund Program, from the North Dakota Public Finance Authority. The water resource district is in the process of a water line construction project and issued revenue bonds in the amount of \$1,350,000. As of December 31, 2017, the district had requested drawdowns of \$1,280,158 and repaid principal of \$60,000. This project was not completed as of December 31, 2017 and a final debt repayment schedule is not yet available since the district has not received the full amount of the drawdowns under this agreement. The outstanding balance at December 31, 2017 was \$1,220,158. The water resource district still has \$69,842 of funding available as of December 31, 2017.

Note 7 RISK MANAGEMENT

The McLean-Sheridan Rural Water District is exposed to various risks of loss relating to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters.

In 1986, state agencies and political subdivisions of the State of North Dakota joined together to form the North Dakota Insurance Reserve Fund (NDRIF), a public entity risk pool currently operating as a common risk management and insurance program for the state and over 2,000 political subdivisions. The water resource district pays an annual premium to NDRIF for its general liability and automobile insurance coverage. The coverage by NDRIF is limited to losses of \$2,000,000 per occurrence for general liability and \$1,000,000 for automobile.

The water resource district also participates in the North Dakota Fire and Tornado Fund and the State Bonding Fund. The district pays an annual premium to the Fire and Tornado Fund to cover property damage to buildings and personal property. Replacement cost coverage is provided by estimating replacement cost in consultation with the Fire and Tornado Fund. The Fire and Tornado Fund is reinsured by a third party insurance carrier for losses in excess of \$1,000,000 per occurrence during a 12 month period. The State Bonding Fund currently provides the water resource district with a blanket fidelity bond coverage in the amount of \$278,000 for its employees. The State Bonding Fund does not currently charge any premium for this coverage.

The water resource district has worker's compensation with the Department of Workforce Safety and Insurance; and purchases commercial insurance for employee health and accident insurance.

Settled claims resulting from these risks have not exceeded insurance coverage in any of the past three fiscal years.

Note 8 PENSION PLAN

The water resource district provides benefits for all of its full-time employees through a defined contribution plan with Morgan Stanley. In a defined contribution plan, benefits depend solely on amounts contributed to the plan plus investment earnings. The water resource district contributes 3% of the employee's gross salary for the year. During the year ended December 31, 2017, the water resource district contributed \$4,834.98.

Rath & Mehler, P.C.

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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

INDEPENDENT AUDITOR'S REPORT

Board of Directors
McLean-Sheridan Rural Water District
Turtle Lake, North Dakota

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 major fund of the McLean-Sheridan Rural Water District, Turtle Lake, North Dakota, as of and for the year ended December 31, 2017, and the related notes to the financial statements, which collectively comprise the district's basic financial statements, and have issued our report thereon dated March 23, 2018.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the 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 opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the district's internal control. Accordingly, we do not express an opinion on the effectiveness of the 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 district'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 were not identified. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, 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 as items II-1 and II-2, that we consider to be significant deficiencies.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the district's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

District's Response to Findings

The district's response to the findings identified in our audit are described in the accompanying *Schedule of Findings and Responses*. The 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 district's internal control or on compliance. This is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the district's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.



Rath and Mehrer, P.C.

Bismarck, North Dakota

March 23, 2018

MCLEAN-SHERIDAN RURAL WATER DISTRICT
Turtle Lake, North Dakota

Schedule of Findings and Responses
For the Year Ended December 31, 2017

SECTION I - SUMMARY OF AUDIT RESULTS:

Financial Statements

Type of Auditor's Report Issued:

Major Fund

Unmodified

Internal control over financial reporting:

* Material weakness(es) identified?

_____ Yes X No

* Significant deficiency(ies) identified?

 X Yes _____ None Reported

Noncompliance Material to financial
statements noted?

_____ Yes X No

SECTION II - FINANCIAL STATEMENT FINDINGS:

Significant Deficiencies

1. Segregation of Duties

Condition: The district has one person responsible for most accounting functions.

Criteria: There should be sufficient accounting personnel so duties of employees are segregated. The segregation of duties would provide better control over assets of the district.

Effect: There is no segregation of duties as one employee is responsible to collect monies, deposit monies, issue checks, send checks to vendors, record receipts and disbursements in journals, maintain the general ledger and prepare financial statements. This increases the risk of misstatement of the district's financial condition.

Recommendation: Due to the size of the district, it is not feasible to obtain proper separation of duties and no recommendation will be made.

Client Response: No response is considered necessary.

2. Financial Statement Preparation

Condition: The district's financial statements as of December 31, 2017 are prepared by the district's external auditors.

Criteria: A good system of internal controls requires the district to determine that the financial statements are prepared based on accounting principles generally accepted in the United States of America. This means that the district must maintain knowledge of current accounting principles and required financial statement disclosures.

Effect: A control system is not in place to determine that the financial statements are properly stated and in compliance with accounting principles generally accepted in the United States of America.

Recommendation: We recommend the district obtain the necessary knowledge of current accounting principles to prepare financial statements or outsource the preparation of its financial statements.

Client Response: It is not cost effective for the district to prepare its own financial statements.