R & T WATER SUPPLY COMMERCE AUTHORITY
RAY, NORTH DAKOTA

AUDITED FINANCIAL STATEMENTS

FOR THE YEARS ENDED DECEMBER 31, 2016 AND 2015

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BRADY
MARTZ
CERTIFIED PUBLIC ACCOUNTANTS
AND CONSULTANTS

INDEPENDENT AUDITOR'S REPORT

To the Board of Directors
R & T Water Supply Commerce Authority
Ray, North Dakota

We have audited the accompanying modified cash basis financial statements of the business-type activities of R & T Water Supply Commerce Authority as of and for the years ended December 31, 2016 and 2015, and the related notes to the financial statements, which collectively comprise R & T Water Supply Commerce Authority'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 the modified cash basis of accounting described in Note 1; this includes determining that the modified cash 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 audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Governmental Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

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

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective modified cash basis financial position of the business-type activities of R & T Water Supply Commerce Authority as of December 31, 2016 and 2015, and the respective changes in modified cash basis financial position and where applicable, cash flows thereof for the years then ended in accordance with the modified cash basis of accounting described in Note 1.

Basis of Accounting

We draw attention to Note 1 of the financial statements, which describes the basis of accounting. The financial statements are prepared on the modified cash basis of accounting, which is a basis of accounting other than accounting principles generally accepted in the United States of America. Our opinions are not modified with respect to this matter.

Other Matters

Required Supplementary Information

Management has omitted the management discussion and analysis that the modified cash basis of accounting principles require to be presented to supplement the basic financial statements. Such missing 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. Our opinion on the basic financial statements is not affected by the missing information.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated June 26, 2017 on our consideration of R & T Water Supply Commerce Authority'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 the 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 R & T Water Supply Commerce Authority's internal control over financial reporting and compliance.

Brady Martz

BRADY, MARTZ & ASSOCIATES, P. C.
Minot, North Dakota

June 26, 2017

R & T WATER SUPPLY COMMERCE AUTHORITY
STATEMENTS OF NET POSITION – MODIFIED CASH BASIS
DECEMBER 31, 2016 AND 2015

	2016	2015
ASSETS		
Current assets		
Cash and cash equivalents	$ 4,429,856	$ 4,492,848
Current portion of receivable from WAWSA	376,057	443,750
Total current assets	4,805,913	4,936,598
Noncurrent assets		
Beneficial interest in trust	58,583	67,829
Restricted cash	1,729,503	1,505,000
Capital assets, net of accumulated depreciation	19,497,893	20,005,324
Cost shared infrastructure, net of accumulated amortization	4,123,861	-
Receivable from WAWSA, net of current portion	6,739,615	7,115,672
Total noncurrent assets	32,149,455	28,693,825
Total assets	36,955,368	33,630,423
DEFERRED OUTFLOWS OF RESOURCES		
Deferred outflows - cost shared infrastructure	174,628	-
LIABILITIES		
Current liabilities		
Current portion of bonds payable	369,789	445,000
Current portion of liability on cost shared infrastructure	147,196	-
Total current liabilities	516,985	445,000
Long-term liabilities		
Bonds payable	6,730,000	7,099,789
Liability on cost shared infrastructure	4,043,550	-
Total long-term liabilities	10,773,550	7,099,789
Total liabilities	11,290,535	7,544,789
DEFERRED INFLOWS OF RESOURCES		
Deferred inflows - customer security deposits	727,000	505,000
Deferred inflows - Western Area Water Supply Authority	11,772,009	11,678,345
Total deferred inflows of resources	12,499,009	12,183,345
NET POSITION		
Net investment in capital assets	7,849,510	8,341,612
Restricted for:		
Beneficial interest in trust	58,583	67,829
Debt service	1,002,503	1,000,000
Unrestricted	4,429,856	4,492,848
Total net position	$ 13,340,452	$ 13,902,289

SEE NOTES TO THE FINANCIAL STATEMENTS

R & T WATER SUPPLY COMMERCE AUTHORITY
STATEMENTS OF REVENUES, EXPENSES, AND
CHANGES IN NET POSITION – MODIFIED CASH BASIS
FOR THE YEARS ENDED DECEMBER 31, 2016 AND 2015

	2016	2015
Operating revenue		
Water sales	$ 1,532,767	$ 1,809,773
Bulk sales	45,461	107,898
WAWSA operating reimbursement	973,563	1,861,892
Total operating revenue	2,551,791	3,779,563
Operating expenses		
Governing board	12,000	12,400
Salaries	634,289	695,558
Retirement	34,618	38,169
Health and dental insurance	59,708	69,745
Education and training	3,465	10,381
Utilities	97,673	114,337
Chemicals	162,414	268,305
Maintenance, repairs and supplies	109,689	348,834
Office expense	2,625	11,252
Insurance	14,553	13,306
Dues and subscriptions	1,010	654
Cost of water sold	1,081,194	1,215,915
Depreciation	859,475	837,605
Amortization	105,739	-
Professional fees	84,370	187,695
Total operating expenses	3,262,822	3,824,156
Operating income (loss)	(711,031)	(44,593)
NON-OPERATING REVENUE (EXPENSES)		
Increase (decrease) of beneficial interest in trust	(9,246)	(34,009)
Interest/dividend income	55,590	151,015
WAWSA interest reimbursement	191,265	204,489
Interest expense on cost shared infrastructure liability	(22,039)	-
Interest expense on bonds payable	(152,871)	(161,571)
Amortization of WAWSA deferred inflows	123,916	121,649
Other revenues	8,845	17,372
Other expenses	(46,266)	(52,352)
Total nonoperating revenues (expenses)	149,194	246,593
CHANGE IN NET POSITION	(561,837)	202,000
NET POSITION - JANUARY 1	13,902,289	13,700,289
NET POSITION - DECEMBER 31	$ 13,340,452	$13,902,289

SEE NOTES TO THE FINANCIAL STATEMENTS

R & T WATER SUPPLY COMMERCE AUTHORITY
STATEMENTS OF CASH FLOWS – MODIFIED CASH BASIS
FOR THE YEARS ENDED DECEMBER 31, 2016 AND 2015

	2016	2015
CASH FLOWS FROM OPERATING ACTIVITIES		
Receipts from customers	$ 1,800,228	$ 1,996,671
Operating reimbursement from related party	973,563	1,861,892
Payments to suppliers	(1,556,993)	(2,170,679)
Payments on behalf of employees	(94,326)	(107,914)
Payments to employees	(646,289)	(707,958)
Net cash provided (used) by operating activities	476,183	872,012
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES:		
Other revenue (expenses)	(37,421)	(34,980)
Net cash provided (used) by noncapital financing activities	(37,421)	(34,980)
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES:		
Acquisition and construction of capital assets	(352,044)	(527,039)
Reimbursement from WAWSA for capital expenditures	217,580	418,200
Payment on bonds payable	(445,000)	(430,000)
Payment on cost shared infrastructure liability	(38,854)	-
Prepayment on cost shared infrastructure liability	(174,628)	-
Reimbursement from WAWSA for bond payments	635,015	633,656
Interest expense on cost shared infrastructure liability	(22,039)	-
Interest expense on bonds payable	(152,871)	(161,571)
Net cash provided (used) by capital and related financing activities	(332,841)	(66,754)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Interest/dividend income	55,590	151,015
Net cash provided (used) by investing activities	55,590	151,015
NET CHANGE IN CASH AND CASH EQUIVALENTS	161,511	921,293
CASH AND CASH EQUIVALENTS - JANUARY 1	5,997,848	5,076,555
CASH AND CASH EQUIVALENTS - DECEMBER 31	$ 6,159,359	$ 5,997,848

SEE NOTES TO THE FINANCIAL STATEMENTS

R & T WATER SUPPLY COMMERCE AUTHORITY

STATEMENTS OF CASH FLOWS – MODIFIED CASH BASIS - CONTINUED
FOR THE YEARS ENDED DECEMBER 31, 2016 AND 2015

	2016	2015
RECONCILIATION OF CASH PRESENTATION TO CASH AND CASH EQUIVALENTS		
Current assets		
Cash and cash equivalents	$ 4,429,856	$ 4,492,848
Noncurrent assets		
Restricted cash	1,729,503	1,505,000
Total cash and cash equivalents	$ 6,159,359	$ 5,997,848
RECONCILIATION OF OPERATING INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES:		
Operating income (loss)	$ (711,031)	$ (44,593)
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation expense	859,475	837,605
Amortization expense	105,739	-
Effects on operating cash flows due to changes in:		
Customer deposits	222,000	79,000
Net cash provided by operating activities	$ 476,183	$ 872,012
SUPPLEMENTAL SCHEDULE OF NONCASH INVESTING AND FINANCING ACTIVITIES		
Increase in value of beneficial interest in trust	$ 41,183	$ 114,806
Distribution of beneficial interest in trust	(50,429)	(148,815)
Amortization of WAWSA deferred inflows	123,916	121,649
Cost shared infrastructure acquired with long-term liability	(4,229,600)	-

SEE NOTES TO THE FINANCIAL STATEMENTS

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

This summary of significant accounting policies of R & T Water Supply Commerce Authority is presented to assist in understanding the Authority's financial statements.

The Authority reports as a business-type activity, as defined by the Governmental Accounting Standards Board (GASB). Business-type activities are those that are financed in whole or in part by fees charged to external parties for goods or services.

Nature of operations and history

R & T Water Supply Commerce Authority provides a water system and water supply to the areas surrounding western North Dakota. Effective October 19, 1978, an association was created and established by a joint powers agreement between the cities of Ray and Tioga and the William County Water Management District. Effective February 15, 2012, the association was reorganized into a commerce authority in accordance with Chapter 11-37 of the North Dakota Century Code. It is exempt from federal income tax under section 501(c)1 of the Internal Revenue Code. The Authority is accounted for as a special purpose government engaged in a business-type activity. Business-type activities are used to account for operations that are financed or operated in a manner similar to the private sector, where the intent is that cost of providing services to the general public on a continuous basis be financed or recovered primarily through user charges.

Reporting entity

Component units are legally separate organizations for which the Authority is financially accountable. The Government Accounting Standards Board has set forth criteria to be considered in determining financial accountability. This criterion includes appointing a voting majority of an organization's governing body and (1) the ability of the water supply commerce authority 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 Authority. Component units may also include organizations that are fiscally dependent on the Authority.

Based on the above criteria, the Authority has no component units included in its report.

Basis of accounting

Basis of accounting determines when transactions are recorded in the financial records and reported in the financial statements. The accompanying financial statements have been presented using the modified cash basis of accounting. This basis recognizes assets, deferred outflows of resources, liabilities, deferred inflows of resources, net position, revenues, and expenditures/expenses when they result from cash transactions with a provision for depreciation. This basis is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America.

As a result of the use of this modified cash basis of accounting, certain assets and their related revenues (such as accounts receivable and revenue for billed or provided services not yet collected) and certain liabilities and their related expenses (such as accounts payable and expenses for goods or services received but not yet paid, and accrued expenses and liabilities) are not recorded in these financial statements.

If the Authority utilized the basis of accounting recognized as generally accepted, the statements would be prepared on the accrual basis of accounting.

The Authority's activities are accounted for similar to those often found in the private sector using the flow of economic resources measurement focus. The accounting objectives of this measurement focus are the determination of net income, financial position, and cash flows. All assets, deferred outflows of resources, liabilities, deferred inflows of resources, net position, revenues and expenses are accounted for through a single business-type activity. Current assets include cash and amounts convertible to cash during the next normal operating cycle or one year. Current liabilities include those obligations to be liquidated with current assets. Equity is classified as net position.

Business-type activities distinguish operating from nonoperating revenues and expenses. Operating revenues and expenses are those that generally result from providing service and producing and delivering goods and/or services. It also includes all revenue and expenses not related to capital and related financing, noncapital financing, or investing activities. Revenue from water sales, hookups, memberships, penalties and sales of supplies are reported as operating revenue. Interest income is reported as nonoperating revenue. All expenses related to operating the Authority are reported as operating expenses. Interest expense and financing cost are reported as nonoperating.

Cash and cash equivalents

For purpose of the statement of cash flows, the Authority considers all highly liquid debt instruments purchased with a maturity of three months or less to be cash equivalents, except for certificates of deposits which are considered cash equivalents regardless of their term since there is no loss of principal for early withdrawal, and reserve funds which are considered noncash equivalents regardless of the maturity terms.

Restricted cash and cash equivalents

Restricted cash and cash equivalents consist of cash set aside for the reserve for debt service and customer deposits.

Reserve for debt service

Reserve for debt service consists of cash and cash equivalents set aside for debt retirement.

Investment policy

The Authority does not have a formal investment policy. State statutes authorize local governments to invest in:

(1) Bonds, treasury bills and notes, or other securities that are a direct obligation of, or an 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.

Beneficial interest in trust

The Authority is the beneficiary of a trust, which derives the majority of its income from oil royalties. The Authority's interest in the trust is recorded at cost in accordance with the modified cash basis of accounting.

Receivable from Western Area Water Supply Authority

The Authority transacts under a service concession arrangement with Western Area Water Supply Authority (WAWSA). Under this arrangement, WAWSA is required to reimburse R&T Water Supply Authority for their outstanding principal payments on their debt. This receivable represents the present value of the principal payment reimbursements required by WAWSA.

Capital assets

Capital assets are recorded at historical costs less accumulated depreciation. A portion of the cost of the capital assets is charged against earnings each year as depreciation expense. Depreciation is computed on the straight-line basis, over the estimated useful life of the asset. The Authority established a capitalization threshold of $5,000. The cost of normal maintenance and repairs that do not add to the value of the assets or materially extend asset lives are not capitalized.

The Authority has established the following useful lives:

Buildings and Infrastructure	15 to 40 years
Equipment and Vehicles	5 to 20 years

Cost shared infrastructure

Cost shared infrastructure is capitalized at contract cost. A portion of the cost is charged against earnings each year as amortization expense. Amortization is computed on the straight-line basis, over the estimated useful life of the infrastructure, which ranges from 20 to 30 years.

Pensions

For purposes of measuring pension expense, information about additions to/deductions from NDPERS' fiduciary net position have been determined on the same basis as they are reported by NDPERS. For this purpose, benefit payments (including refunds of employee contributions) are recognized on the modified cash basis of accounting. Investments are reported at fair value.

Net Position

Net position represents the difference between (a) assets and deferred outflows of resources and (b) liabilities and deferred inflows of resources in the Authority's financial statements. Net investment in capital assets consists of capital assets, net of accumulated depreciation, reduced by the outstanding balances of any long-term debt attributable to the acquisition, construction, or improvement of those assets. Restricted Net Position consists of restricted assets reduced by liabilities and deferred inflows of resources related to those assets. Unrestricted Net Position is the net amount of assets, deferred outflows of resources, liabilities, and deferred inflows of resources that are not included in the determination of net investment in capital assets or the restricted component of net position.

<u>Net Position Flow Assumption</u>

Sometimes, the government will fund capital outlays for particular purposes for both restricted (e.g., restricted bond or grant proceeds) and unrestricted resources. In order to calculate the amounts to report as restricted - net position and unrestricted - net position in the financial statements, a flow assumption must be made about the order in which the resources are considered to be applied. It is the government's policy to consider restricted - net position to have been depleted before unrestricted - net position is applied.

Deferred Outflows/Inflows of Resources

In addition to assets, the statement of net position will sometimes report a separate section for deferred outflows of resources. This separate financial statement element, *deferred outflows of resources*, represents a consumption of net position that applies to a future period(s) and so will not be recognized as an outflow of resource (expense/expenditure) until then. The Authority has one item that qualifies for reporting in this category. Deferred Outflows of Resources – cost shared infrastructure represents payments on the cost shared infrastructure liability in excess of the required balance due. The Authority will recognize the reduction of the cost shared infrastructure liability in future periods.

In addition to liabilities, the statement of net position will sometimes report a separate section for deferred inflows of resources. This separate financial statement element, *deferred inflows of resources,* represents an acquisition of net position that applies to future period(s) and so will not be recognized as an inflow of resources (revenue) until that time. The District has two items that qualify for reporting in this category. Deferred Inflows of Resources - WAWSA represents a reimbursement from WAWSA for capital expenditures and debt principal payments. The Authority transacts under a service concession arrangement with Western Area Water Supply Authority (WAWSA). This deferred inflow of resources, under GASB 60 - Service Concession Arrangements guidance, is to be amortized over the life of the agreement with WAWSA, which is 99 years. Refer to Note 8 for a full description of the relationship between the entities. Deferred Inflows of Resources – Customer Security Deposits represents a payment from R & T customers for water hookup services. The Authority will recognize this revenue once the customer hookup process is completed.

Use of Estimates

The preparation of financial statements in conformity with the modified cash basis of accounting used by the Authority requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent asset and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates.

Reclassifications

Certain reclassifications have been made to the 2015 financial statements to confirm to 2016 presentation. Such reclassifications had no effect on the change in net position as previously reported.

NOTE 2 CUSTODIAL CREDIT RISK

The Authority maintains cash deposits at various financial institutions. The amounts on deposit were insured by the FDIC/NCUA up to $250,000 per financial institution. At December 31, 2016, the Authority had approximately $5,225,000 in excess of the FDIC/NCUA limit on deposit. The entire amount in excess of the FDIC/NCUA depository insurance was covered by pledged securities at December 31, 2016.

NOTE 3 CAPITAL ASSETS

The following is a summary of changes in capital assets for the years ended December 31, 2016 and 2015:

	Balance 1/1/2016	Additions	Disposals	Balance 12/31/2016
Capital assets, not being depreciated				
Land	$ 235,254	$ 145,000	$ -	$ 380,254
Construction in progress	125,159	51,469	16,635	159,993
Total capital assets, not being depreciated	360,413	196,469	16,635	540,247
Capital assets being depreciated				
Buildings and infrastructure	24,280,222	141,442	-	24,421,664
Machinery and vehicles	160,820	30,768	-	191,588
Equipment	113,588	-	-	113,588
Total capital assets being depreciated	24,554,630	172,210	-	24,726,840
Less accumulated depreciation				
Buildings and infrastructure	4,809,609	831,147	-	5,640,756
Machinery and vehicles	81,374	16,969	-	98,343
Equipment	18,736	11,359	-	30,095
Total accumulated depreciation	4,909,719	859,475	-	5,769,194
Total capital assets being depreciated, net	19,644,911	(687,265)	-	18,957,646
Net capital assets	$ 20,005,324	$ (490,796)	$ 16,635	$ 19,497,893

	Balance 1/1/2015	Additions	Disposals	Balance 12/31/15
Capital assets, not being depreciated				
Land	$ 235,254	$ -	$ -	$ 235,254
Construction in progress	24,042	101,117	-	125,159
Total capital assets, not being depreciated	259,296	101,117	-	360,413
Capital assets being depreciated				
Buildings and infrastructure	23,910,121	370,101	-	24,280,222
Machinery and vehicles	154,635	6,185	-	160,820
Equipment	63,952	49,636	-	113,588
Total capital assets being depreciated	24,128,708	425,922	-	24,554,630
Less accumulated depreciation				
Buildings and infrastructure	3,993,267	816,342	-	4,809,609
Machinery and vehicles	67,232	14,142	-	81,374
Equipment	11,615	7,121	-	18,736
Total accumulated depreciation	4,072,114	837,605	-	4,909,719
Total capital assets being depreciated, net	20,056,594	(411,683)	-	19,644,911
Net capital assets	$20,315,890	$ (310,566)	$ -	$20,005,324

Depreciation expense was $859,475 and $837,605, respectively, for the years ended December 31, 2016 and 2015.

NOTE 4 LONG-TERM LIABILITIES

Long-term liability activity for the years ended December 31, 2016 and 2015 was as follows:

2016

	Balance January 1	Increases	Decreases	Balance December 31	Due Within One Year
Revenue bonds 2008	$ 395,000	$ -	$ 25,000	$ 370,000	$ 25,000
2012 SRF Bonds	7,149,789	-	420,000	6,729,789	344,789
	$ 7,544,789	$ -	$ 445,000	$ 7,099,789	$ 369,789

2015

	Balance January 1	Increases	Decreases	Balance December 31	Due Within One Year
Revenue bonds 2008	415,000	-	20,000	395,000	25,000
2012 SRF Bonds	7,559,789	-	410,000	7,149,789	420,000
	$ 7,974,789	$ -	$ 430,000	$ 7,544,789	$ 445,000

Outstanding liabilities at December 31, 2016 and 2015 consisted of the following:

Revenue Bonds 2008: The Authority issued revenue bonds of 2008 whereby the Authority pledges income derived from the acquired or constructed assets to pay debt service. These bonds were in the amount of $1,452,760. Principal payments are due annually on September 1. Interest is due March 1 and September 1 of each year. These bonds carry an interest rate of 2.5% and will mature on September 1, 2028.

2012 SRF Bonds: The Authority issued SRF bonds of 2012 whereby the Authority pledges income derived from the acquired or constructed assets to pay debt service. These bonds were issued in the amount of $9,349,789. Principal payments are due annually on September 1. Interest is due March 1 and September 1 of each year. These bonds carry an interest rate of 2.0% and will mature on September 1, 2032.

The future required payments on long-term debt including interest are as follows:

Year Ending December 31	Principal	Interest	Total
2017	$ 369,789	$ 143,846	$ 513,635
2018	385,000	136,325	521,325
2019	395,000	128,500	523,500
2020	410,000	120,475	530,475
2021	420,000	112,125	532,125
2022-2026	2,265,000	428,000	2,693,000
2027-2031	2,445,000	188,525	2,633,525
2032	410,000	8,200	418,200
	$ 7,099,789	$ 1,265,996	$ 8,365,785

NOTE 5 RISK MANAGEMENT

The R & T Water Supply Commerce Authority 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 (NDIRF), 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 Authority pays an annual premium to NDIRF for its general liability, automobile and equipment insurance coverage. The coverage by NDIRF is limited to losses of $2,000,000 per occurrence for general liability and automobile; and $45,968 for equipment.

The Authority also participates in the North Dakota Fire and Tornado Fund and the State Bonding Fund. The Authority 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 Authority with blanket fidelity bond coverage in the amount of $2,000,000 for its employees. The State Bonding Fund does not currently charge any premium for this coverage.

The Authority 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 6 PENSION PLAN

North Dakota Public Employees Retirement System (Main System)

The following brief description of NDPERS is provided for general information purposes only. Participants should refer to NDCC Chapter 54-52 for more complete information.

NDPERS is a cost-sharing multiple-employer defined benefit pension plan that covers substantially all employees of the State of North Dakota, its agencies and various participating political subdivisions. NDPERS provides for pension, death and disability benefits. The cost to administer the plan is financed through the contributions and investment earnings of the plan.

Responsibility for administration of the NDPERS defined benefit pension plan is assigned to a Board comprised of seven members. The Board consists of a Chairman, who is appointed by the Governor; one member appointed by the Attorney General; one member appointed by the State Health Officer; three members elected by the active membership of the NDPERS system; and one member elected by the retired public employees. Effective July 1, 2015, the board was expanded to include two members of the legislative assembly appointed by the chairman of the legislative management.

Pension Benefits

Benefits are set by statute. NDPERS has no provisions or policies with respect to automatic and ad hoc post-retirement benefit increases. Member of the Main System are entitled to unreduced monthly pension benefits beginning when the sum of age and years of credited service equal or exceed 85 (Rule of 85), or at normal retirement age (65). For members hired on or after January 1, 2016 the Rule of 85 will be replaced with the Rule of 90 with a minimum age of 60. The monthly pension benefit is equal to 2.00% of their average monthly salary, using the highest 36 months out of the last 180 months of service, for each year of service. The plan permits early retirement at ages 55-64 with three or more years of service.

Members may elect to receive the pension benefits in the form of a single life, joint and survivor, term-certain annuity, or partial lump sum with ongoing annuity. Members may elect to receive the value of their accumulated contributions, plus interest, as a lump sum distribution upon retirement or termination, or they may elect to receive their benefits in the form of an annuity. For each member electing an annuity, total payment will not be less than the members' accumulated contributions plus interest.

Death and Disability Benefits

Death and disability benefits are set by statute. If an active member dies with less than three years of service for the Main System, a death benefit equal to the value of the member's accumulated contributions, plus interest, is paid to the member's beneficiary. If the member has earned more than three years of credited service for the Main System, the surviving spouse will be entitled to a single payment refund, life-time monthly payments in an amount equal to 50% of the member's accrued normal retirement benefit, or monthly payments in an amount equal to the member's accrued 100% Joint and Survivor retirement benefit if the member had reached normal retirement age prior to date of death. If the surviving spouse dies before the member's accumulated pension benefits are paid, the balance will be payable to the surviving spouse's designated beneficiary.

Eligible members who become totally disabled after a minimum of 180 days of service, receive monthly disability benefits equal to 25% of their final average salary with a minimum benefit of $100. To qualify under this section, the member has to become disabled during the period of eligible employment and apply for benefits within one year of termination. The definition for disabled is set by the NDPERS in the North Dakota Administrative Code.

Refunds of Member Account Balance

Upon termination, if a member of the Main System is not vested (is not 65 or does not have three years of service), they will receive the accumulated member contributions and vested employer contributions, plus interest, or may elect to receive this amount at a later date. If the member has vested, they have the option of applying for a refund or can remain as a terminated vested participant. If a member terminated and withdrew their accumulated member contribution and is subsequently reemployed, they have the option of repurchasing their previous service.

Member and Employer Contributions

Member and employer contributions paid to NDPERS are set by statute and are established as a percent of salaries and wages. Member contribution rates are 7% and employer contribution rates are 7.12% of covered compensation.

The member's account balance includes the vested employer contributions equal to the member's contributions to an eligible deferred compensation plan. The minimum member contribution is $25 and the maximum may not exceed the following:

1 to 12 months of service – Greater of one percent of monthly salary or $25
13 to 24 months of service – Greater of two percent of monthly salary or $25
25 to 36 months of service – Greater of three percent of monthly salary or $25
Longer than 36 months of service – Greater of four percent of monthly salary or $25

Pension Expense

For the years ended December 31, 2016 and 2015, the Authority recognized pension expense of $34,618 and $38,169, respectively. As the Authority uses the modified cash basis of accounting, no deferred outflows of resources and deferred inflows of resources related to pension are reported.

Pension plan fiduciary net position. Detailed information about the pension plan's fiduciary net position is available in the separately issued NDPERS financial report. Requests to obtain or review this report should be addressed to the Executive Director - NDPERS; P.O. Box 1657; Bismarck, ND 58502-1657.

Payables to the pension plan

No amount was payable to the pension plan at year end.

NOTE 7 COMMITMENTS

Water supply contract—The Authority has entered into a water supply contract with the Cities of Tioga, Ray, Ross, Stanley, Wildrose, and Hess Corporation, whereby the Authority supplies water at a rate agreed upon by both parties based on the terms in the contract.

Construction contract—The Authority has entered into contracts for the modifications of the R&T Water Treatment Facility. The total costs to complete these projects are estimated to be $1,100,000. As of December 31, 2016, the Authority had incurred and capitalized approximately $1,068,000 in costs related to the project. Estimated costs to complete the project are $32,000.

NOTE 8 JOINTLY GOVERNED ORGANIZATIONS

WAWSA was formed to own, finance, construct, and operate the Western Area Water Supply Project. The project is a comprehensive water supply project largely utilizing the Missouri River water treated at the Williston Regional Water Treatment Plant and distributed to meet the municipal, rural and industrial water needs for all or part of McKenzie, Williams, Divide, Burke, and Mountrail counties. The project is financed by a series of loans issued by the State of North Dakota. The Authority holds two of ten seats on the board of WAWSA.

During 2012, R&T Water Supply Authority entered into the following agreements with WAWSA:

Infrastructure Operating Agreement: Under this agreement, the Authority will be responsible for all repairs and maintenance of infrastructure owned by WAWSA as identified in the agreement. The Authority may also make approved capital expenditures with respect to the WAWSA infrastructure in accordance with an approved budget. The Authority will have the authority and responsibility for the general management and operation of the identified infrastructure, establishing and implementing purchasing and administrative policies, programs and other operational matters. Under the agreement, the Authority is entitled to reimbursement for costs identified in the agreement and in accordance with an approved budget. WAWSA will bear the risk of loss to the infrastructure. The agreement is in effect until the earlier of: (i) repayment of all WAWSA debt or ii) 99 years after the effective date of the agreement.

Access and Use Agreement: This agreement sets forth the terms and conditions on which the Member will permit WAWSA to access and use identified infrastructure owned by R&T Water Supply Authority. This includes infrastructure identified under sub-agreements with the cities of Ray, Stanley, and Tioga. The Authority will be responsible for all repairs and maintenance of the access infrastructure identified in the agreement. The Authority will have the authority and responsibility for the general management and operation of the identified infrastructure, establishing and implementing purchasing and administrative policies, ensuring compliance with applicable legal requirements, budgeting and accounting procedures, programs and other operational matters. The Authority retains ownership of the infrastructure unless a purchase option is exercised. As consideration of this agreement, WAWSA will make payments equal to the amount of debt service requirements on the Authority's water revenue bonds. The Authority is also entitled to reimbursement for costs identified in the agreement and in accordance with an approved budget. The Authority bears the risk of loss to the infrastructure. The term of the agreement continues until the earlier of: (i) repayment of all WAWSA debt or ii) 99 years after the effective date of the agreement.

Water Supply Agreement: Under this agreement, R&T Water Supply Commerce Authority commits to purchasing water from WAWSA. Subject to a minimum monthly quantity, peak instantaneous flow, and minimum pressure limitation set forth in the agreement, WAWSA agrees to provide, pump, transmit and deliver treated water to the Authority. The Authority will pay for the water using an agreed-upon base rate plus supplemental rate as outlined in the agreement, which is subject to change. This agreement is not effective until WAWSA's water supply is connected at identified delivery points. The agreement remains in effect until all of WAWSA's debt is repaid.

R&T Output Agreement: This agreement sets forth the terms and conditions on which the Authority will sell to WAWSA the entire output of the plant. As consideration for the entire output of the treated water from the plant to WAWSA, WAWSA will make payments equal to the debt service paid by the Authority during the term, approved operation and maintenance costs, capital expenditure reimbursements, and baseline 2010 industrial water sales revenue.

As part of the above agreements, all industrial water sales will be for the benefit of WAWSA. The Authority will be reimbursed an amount as outlined in the agreements based on their 2010 industrial water sales revenue. As of January 1, 2016, these payments have been suspended.

Under the above agreements, R & T Water Supply Commerce Authority received as follows:

Under the above agreements, the Authority received $17,039 and $64,320 for sales of water to Western Area Water Supply Authority, along with $37,380 and $448,563 baseline sales reimbursement during the years ended December 31, 2016 and 2015, respectively. Reimbursements from WAWSA for the years ended December 31, 2016 and 2015 included principal debt payment reimbursements of $443,750 and $429,167, interest and administrative fee reimbursements of $191,265 and $204,489, operations and maintenance reimbursements $936,183 and $1,413,329 and capital expenditure reimbursements of $217,580 and $418,200, respectively. The Authority also purchased water from WAWSA during 2016 and 2015 for a total of $1,081,194 and $1,215,915, respectively.

The deferred inflow of resources from WAWSA consists of the following items for the years ended December 31, 2016 and 2015:

	2016	2015
Debt reimbursement receivable as of December 31	$ 7,115,672	$ 7,559,422
Principal debt payment reimbursements	1,449,951	1,006,201
Accumulated capital expenditure reimbursements	3,603,009	3,385,429
Accumulated amortization	(396,623)	(272,707)
Deferred inflow of resources from WAWSA	$ 11,772,009	$ 11,678,345

NOTE 9 COST SHARED INFRASTRUCTURE

During the year ended December 31, 2016, the Authority entered into an agreement with Western Area Water Supply Authority to facilitate the development of water distribution infrastructure within the Authority’s borders. Under the agreement, the Authority agreed to re-pay a portion of the capital invested in the infrastructure over 20 to 30 years. In exchange, the Authority has the right to use the infrastructure installed over the period of the loan. As a result, upon entering into the agreement, the Authority recognized a right of use of $4,229,600, and an offsetting liability on cost shared infrastructure for the same amount.

The right of use asset recognized under the agreement is being amortized over 20 to 30 years. The amortization expense recognized during the year ended December 31, 2016 was $105,739. Accumulated amortization and net book value of this asset were $105,739 and $4,123,861, respectively, as of December 31, 2016.

The liability on the cost shared infrastructure is being repaid over 20 to 30 years at an interest rate of 1.50%. The liability requires varying monthly payments maturing January 2036 to September 2046. Expected future payments are as follows:

2017	$ 147,196
2018	148,970
2019	152,535
2020	154,009
2021	157,620
2022-2026	824,024
2027-2031	898,790
2032-2036	861,680
2037-2041	403,926
2042-2046	441,996
	$4,190,746

NOTE 10 NEW ACCOUNTING PRONOUNCEMENTS

GASB Statement No. 74, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*, is to improve the usefulness of information about postemployment benefits other than pensions (other postemployment benefits or OPEB) included in the general purpose external financial reports of state and local governmental OPEB plans for making decisions and assessing accountability. This Statement is effective for financial statements for fiscal years beginning after June 15, 2016. Earlier application is encouraged.

GASB Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions,* is to improve accounting and financial reporting by state and local governments for postemployment benefits other than pensions (other postemployment benefits or OPEB). It also improves information provided by state and local governmental employers about financial support for OPEB that is provided by other entities. This Statement is effective for fiscal years beginning after June 15, 2017. Earlier application is encouraged.

GASB Statement No. 80, *Blending Requirements for Certain Component Units and amendment of GASB Statement No. 14*, amends the blending requirements for the financial statement presentation of component units of all state and local governments. The additional criteria require blending of a component unit incorporated as a not-for-profit corporation in which the primary government is the sole corporate member. The additional criterion does not apply to component units included in the financial reporting entity pursuant to the provisions of Statement No. 39, *Determining Whether Certain Organization Are Component Units*. The requirements of this Statement are effective for reporting periods beginning after June 15, 2016. Earlier application is encouraged.

GASB Statement No. 81, *Irrevocable Split-Interest Agreements*, provides recognition and measurement guidance for situations in which a government is a beneficiary of the agreement. This Statement requires that a government that receives resources pursuant to an irrevocable split-interest agreement recognize assets, liabilities, and deferred inflows of resources at the inception of the agreement. Furthermore, this Statement requires that a government recognize assets representing its beneficial interests in irrevocable split-interest agreements that are administered by a third party, if the government controls the present service capacity of the beneficial interests. This Statement requires that a government recognize revenue when the resources become applicable to the reporting period. The requirements of this Statement are effective for financial statements for periods beginning after December 15, 2016, and should be applied retroactively. Earlier application is encouraged.

GASB Statement No. 82, *Pension Issues – an amendment of GASB Statements No. 67 and No. 73*, provides further guidance regarding (1) the presentation of payroll-related measures in required supplementary information, (2) the selection of assumptions and the treatment of deviations from the guidance in an Actuarial Standard of Practice for financial reporting purposes, and (3) the classification of payments made by employers to satisfy employee (plan member) contribution requirements. This Statement amends GASB Statements No. 67 and No. 68 to require the presentation of covered payroll to be defined as the payroll on which contributions to a pension plan are based, rather than the payroll of employees that are provided with pensions through the pension plan. The requirements of this Statement are effective for reporting periods beginning after June 15, 2016, except for the requirements of this Statement for the selection of assumptions in a circumstance in which an employer's pension liability is measured as of a date other than the employer's most recent fiscal year-end. In that circumstance, the requirements for the selection of assumptions are effective for that employer in the first reporting period in which the measurement date of the pension liability is on or after June 15, 2017. Earlier application is encouraged.

GASB Statement No. 84, *Fiduciary Activities*, provides guidance regarding the identification of fiduciary activities for accounting and financial reporting purposes and how those activities should be reported. This Statement establishes criteria for identifying fiduciary activities of all state and local governments. The focus of the criteria generally is on (1) whether a government is controlling the assets of the fiduciary activity and (2) the beneficiaries with whom a fiduciary relationship exists. Separate criteria are included to identify fiduciary component units and postemployment benefit arrangements that are fiduciary activities. The requirements of this Statement are effective for reporting periods beginning after December 15, 2018. Earlier application is encouraged.

GASB Statement No. 85, *Omnibus 2017*, addresses practice issues that have been identified during implementation and application of certain GASB Statements. This Statement addresses a variety of topics including issues related to blending component units, goodwill, fair value measurement and application, and postemployment benefits (pensions and other postemployment benefits [OPEB]). The requirements of this Statement are effective for reporting periods beginning after June 15, 2017. Earlier application is encouraged.

Management has not yet determined the effect these statements will have on the Authority's financial statements.

NOTE 11 SUBSEQUENT EVENTS

No significant events occurred subsequent to the Authority's year end. Subsequent events have been evaluated through June 26, 2017, which is the date these financial statements were available to be issued.

BRADY MARTZ
CERTIFIED PUBLIC ACCOUNTANTS AND CONSULTANTS

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*

To the Board of Directors
R & T Water Supply Commerce Authority
Ray, North Dakota

We have audited, in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the business-type activities of R & T Water Supply Commerce Authority as of and for the year ended December 31, 2016, and the related notes to the financial statements, which collectively comprise R & T Water Supply Commerce Authority's basic financial statements, and have issued our report thereon dated June 26, 2017.

Internal Control over Financial Reporting

In planning and performing our audits of the financial statements, we considered R & T Water Supply Commerce Authority'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 R & T Water Supply Commerce Authority's internal control. Accordingly, we do not express an opinion on the effectiveness of R & T Water Supply Commerce Authority's internal control.

Our consideration of internal control was for the limited purposes described in the preceding paragraph 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. However, as described in the accompanying schedule of findings and responses, we identified certain deficiencies in internal control that we consider to be material weaknesses and significant deficiencies.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiencies described in the accompanying schedule of findings and responses as items 2016-01 and 2016-02 to be material weaknesses.

A *significant deficiency* is a deficiency, or combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider the deficiency described in the accompanying schedule of findings and responses as item 2016-03 to be a significant deficiency.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether R & T Water Supply Commerce Authority'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 no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

R & T Water Supply Commerce Authority's Responses to Findings

R & T Water Supply Commerce Authority's responses to the findings identified in our audit are described in the accompanying schedule of findings and responses. R & T Water Supply Commerce Authority's responses were not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on them.

Purpose of this Report

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

Brady Martz

BRADY, MARTZ & ASSOCIATES, P.C.
Minot, North Dakota

June 26, 2017

R & T WATER SUPPLY COMMERCE AUTHORITY
SCHEDULE OF FINDINGS AND RESPONSES
DECEMBER 31, 2016

I. Findings Relating to Financial Statements

2016-01 *Significant Adjusting Entries - Material Weakness*

Criteria:	The Authority is required to maintain internal controls at a level where underlying support for general ledger accounts can be developed and a determination can be made that the general ledger accounts are properly reflected on the modified cash basis of accounting.
Condition:	During our audits, material adjusting entries to the financial statements were proposed in order to bring the financial statements into compliance with the modified cash basis of accounting. The Authority is required to maintain internal controls at a level where a determination can be made that the general ledger accounts are properly reflected on the modified cash basis of accounting.
Context:	Accounts related to property, depreciation, receivables, deferred inflows of resources, and notes payable are adjusted throughout the financial statement preparation process.
Cause:	The Authority has a limited number of staff available to determine the proper balance of each general ledger account prior to the start of the audit.
Effect:	The Authority does not maintain internal controls at a level where a determination can be made that the general ledger accounts are properly reflected on the modified cash basis of accounting.
Recommendation:	In order to comply with this requirement, accounting personnel will need to determine the proper balance of each general ledger account prior to the start of the audit.
View of responsible officials and corrective actions:	Due to the small size of the Authority, it is not cost effective for the Authority to properly address this significant control deficiency.

2016-02 *Financial Statement Preparation - Material Weakness*

Criteria:	An appropriate system of internal controls requires that the Authority must make a determination that financial statements are properly stated in compliance with the modified cash basis of accounting. This requires the Authority's personnel to maintain knowledge of current accounting principles and required financial statement disclosures.
Condition/Context:	The Authority's auditors prepared the financial statements as of December 31, 2016 and 2015. The Authority does not have controls necessary to assess whether all relevant disclosures have been included in the financial statements as required by modified cash basis of accounting. The lack of appropriate disclosures may affect the user's judgment related to financial condition, results of operations and cash flows of the Authority.
Cause:	The Authority has a limited number of staff available to maintain knowledge of current accounting principles and required financial statement disclosures.
Effect:	An appropriate system of internal controls is not present to make a determination that financial statements are properly stated in compliance with modified cash basis of accounting.
Recommendation:	Compensating controls over financial statement disclosure requirements could be provided by the use of current disclosure checklists or the outsourcing of the financial statement preparation or review function.
View of responsible officials and corrective actions:	Due to the small size of the Authority, it is not cost effective for the Authority to properly address this significant control deficiency.

2016-03 *Segregation of Duties - Significant Deficiency*

Criteria:	Generally, an appropriate system of internal control has the proper separation of duties between authorization, custody, record keeping, and reconciliation functions.
Condition/Context:	The Authority has one person responsible for most accounting functions.
Cause:	The Authority has a limited number of staff available due to the size of the organization.
Effect:	Under the current system, one individual has the ability to collect monies, deposit monies, issue checks, enter new customers, prepare customer's billings, receive and post customers payments, and reconcile the Authority's bank accounts.
Recommendation:	While the Authority does have some monitoring controls in place, we recommend that the Authority review its current process to determine if the monitoring controls can be expanded and if any segregation controls can be economically implemented.
View of responsible officials and corrective actions:	Due to the small size of the Authority, it is not cost effective for the Authority to properly address this significant control deficiency.