

Annual Financial Report

Lincoln Pipestone Rural Water System

Lake Benton, Minnesota

For the Year Ended
December 31, 2018

Lincoln Pipestone Rural Water System
 Lake Benton, Minnesota
 Annual Financial Report
 Table of Contents
 For the Year Ended December 31, 2018

	<u>Page No.</u>
Introductory Section	
Board of Directors and Administration	4
Financial Section	
Independent Auditor's Report	6
Management's Discussion and Analysis	8
Basic Financial Statements	
Fund Financial Statements - Enterprise Fund	
Statement of Net Position	13
Statement of Activities	14
Statement of Revenues, Expenses and Changes in Net Position	15
Statement of Cash Flows	17
Notes to the Financial Statements	18
Other Required Reports	
Independent Auditor's Report on Minnesota Legal Compliance	29
Independent Auditors 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	30
Federal Financial Award Programs	
Independent Auditor's Report on Compliance for Each Major Federal Program and Report on Internal Control Over Compliance Required By the Uniform Guidance	33
Schedule of Expenditures of Federal Awards	35
Notes to the Schedule of Expenditures of Federal Awards	36
Schedule of Findings, Responses and Questioned Costs	37

INTRODUCTORY SECTION
LINCOLN PIPESTONE RURAL WATER SYSTEM
LAKE BENTON, MINNESOTA

FOR THE YEAR ENDED
DECEMBER 31, 2018

Lincoln Pipestone Rural Water System
Lake Benton, Minnesota
Board of Commissioners and Administration
For the Year Ended December 31, 2018

Board of Commissioners

<u>Name</u>	<u>Title</u>
Earl DeWilde	Chairperson
Mitch Kling	Vice-Chairperson
Jan Moen	Secretary
Rod Spronk	Treasurer
Frank Engels	Commissioner
Bill Ufkin	Commissioner
Jerry Lonneman	Commissioner
Randy Kraus	Commissioner
J. Brent Feikema	Commissioner
Ken Buysse	Commissioner
Joe Weber	Commissioner
Ron Schramel	Board Attorney

Administration

Jason Overby	General Manager
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FINANCIAL SECTION
LINCOLN PIPESTONE RURAL WATER SYSTEM
LAKE BENTON, MINNESOTA

FOR THE YEAR ENDED
DECEMBER 31, 2018



INDEPENDENT AUDITOR'S REPORT

Board of Commissioners
Lincoln Pipestone Rural Water System
Lake Benton, Minnesota

Report on the Financial Statements

We have audited the accompanying financial statements of the Lincoln Pipestone Rural Water System (the System), Lake Benton, Minnesota, as of and for the year ended December 31, 2018 and the related notes to the financial statements, which collectively comprise the System'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 the 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 of 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 Board'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 System'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 statement.

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

Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the System as of December 31, 2018, and the respective changes in financial position and cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Other Matters

Report on Summarized Comparative Information

We have previously audited the System's 2017 financial statements, and we expressed unmodified opinions on the respective proprietary fund financial statements in our report dated March 27, 2018. In our opinion, the summarized comparative information presented herein for the respective proprietary fund financial statements as of and for the year ended December 31, 2017, is consistent, in all material respects, with the audited financial statements from which it has been derived.

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis starting on page 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 Information

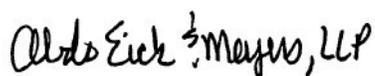
Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the System's basic financial statements. The introductory section, is presented for purposes of additional analysis and is not a required part of the basic financial statements. The schedule of expenditures of federal awards is presented for purposes of additional analysis as required by Title 2 U.S. Code of Federal Regulations (CFR) Part 200, Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards, and is also not a required part of the basic financial statements.

The Schedule of Expenditures of Federal Awards are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, individual fund financial schedules and the Schedule of Expenditures of Federal Awards are fairly stated, in all material respects, in relation to the basic financial statements as a whole.

The introductory section has not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we do not express an opinion or provide any assurance on it.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated March 28, 2019, on our consideration of the System's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is solely to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the System's internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the System's internal control over financial reporting and compliance.



ABDO, EICK & MEYERS, LLP
Mankato, Minnesota
March 28, 2019

Management's Discussion and Analysis

As management of the Lincoln Pipestone Rural Water System, (the System), Lake Benton, Minnesota, we offer readers of the System's financial statements this narrative overview and analysis of the financial activities of the System for the fiscal year ended December 31, 2018.

Financial Highlights

- The assets of the System exceeded its liabilities at the close of the most recent fiscal year by \$54,961,701 (net position). Of this amount, \$5,130,277 (unrestricted net position) may be used to meet the System's ongoing obligations to its users and creditors and provide for future rate stabilization.
- The System's total net position increased by \$505,585 as compared to an increase of \$4,701,163 in the previous year. The change from the previous year is due to a decrease in state and federal grants by \$4,020,591 mainly attributable to the system receiving a grant in the prior year.

Overview of the Financial Statements

This discussion and analysis is intended to serve as an introduction to the System's basic financial statements. The System's basic financial statements comprise two components: 1) fund financial statements, and 2) notes to the financial statements. The notes explain some of the information in the financial statements and provide more detailed data. The statements are followed by a supplementary schedules that further explains and supports the information in the financial 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 System, like other State and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. The System maintains one type of fund: a proprietary fund.

Proprietary fund. The System maintains one type of proprietary fund. The System uses an enterprise fund to account for its water functions.

The basic proprietary fund financial statements can be found starting on page 13 of this report.

Notes to the Financial Statements. The notes provide additional information that is essential to a full understanding of the data provided in the fund financial statements. The notes to the financial statements can be found starting on page 18 of this report.

Fund Financial Analysis

As noted earlier, net position may serve over time as a useful indicator of a government's financial position. In the case of the System, assets exceeded liabilities by \$54,961,701 at the close of the most recent fiscal year.

A large portion of the System's net position (56.2 percent) reflects its investment in capital assets (e.g., land, buildings, machinery and equipment), less any related debt used to acquire those assets that are still outstanding. The System uses these capital assets to provide services to citizens; consequently, these assets are not available for future spending. Although the System's investment in its capital assets is reported net of related debt, it should be noted that the resources needed to repay this debt must be provided from other sources, since the capital assets themselves cannot be used to liquidate these liabilities.

Lincoln Pipestone Rural Water System's Summary of Net Position

	Business-type Activities		
	2018	2017	Increase (Decrease)
Current and Other Assets	\$ 6,624,565	\$ 11,210,434	\$(4,585,869)
Restricted Assets	24,144,175	25,092,324	(948,149)
Capital Assets	66,228,627	67,132,511	(903,884)
Total Assets	96,997,367	103,435,269	(6,437,902)
Long-term Liabilities Outstanding	41,120,258	47,921,206	(6,800,948)
Other Liabilities	915,408	1,057,947	(142,539)
Total Liabilities	42,035,666	48,979,153	(6,943,487)
Net Investment in Capital Assets	30,857,853	31,118,967	(261,114)
Restricted	18,973,571	19,130,974	(157,403)
Unrestricted	5,130,277	4,206,175	924,102
Total Net Position	\$ 54,961,701	\$ 54,456,116	\$ 505,585

An additional portion of the System's net position (34.5 percent) represents resources that are subject to external restrictions on how they may be used. The remaining balance, \$5,130,277 or (9.3 percent) represents unrestricted net position which may be used to meet the System's ongoing obligations to citizens and creditors.

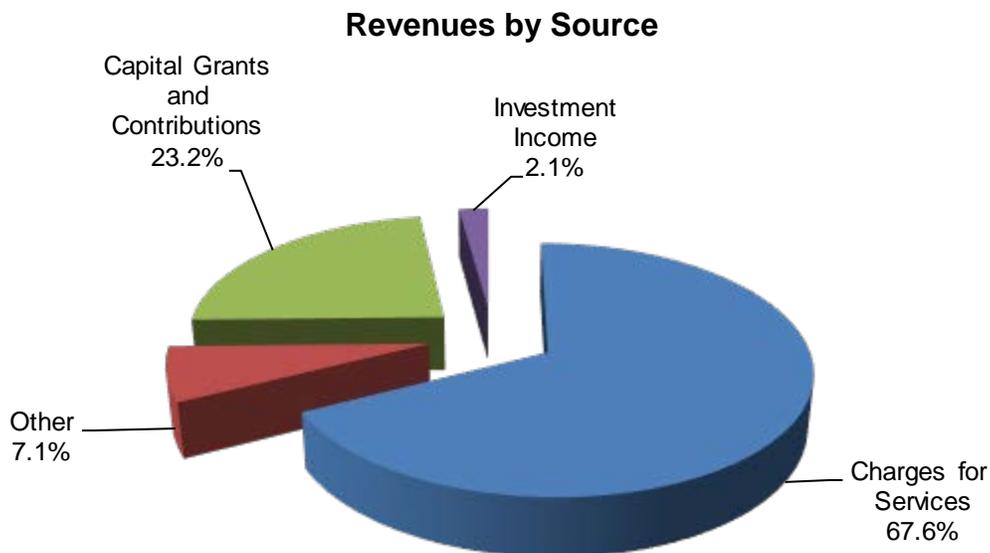
At the end of the current fiscal year, the System is able to report positive balances in both categories of net position.

The System's net position increased by \$505,585 during the current fiscal year. Key elements of this increase are as follows:

Lincoln Pipestone Rural Water System's Changes in Net Position

	Business-type Activities		
	2018	2017	Increase (Decrease)
Revenues			
Program Revenues			
Charges for services	\$ 5,755,523	\$ 5,551,853	\$ 203,670
Capital Grants and Contributions	1,976,114	6,172,120	(4,196,006)
General Revenues			
Investment income	183,129	116,947	66,182
Other	605,986	866,445	(260,459)
Total Revenues	<u>8,520,752</u>	<u>12,707,365</u>	<u>(4,186,613)</u>
Expenses			
Operating Expenses	7,062,851	6,779,597	283,254
Non-operating	952,316	1,226,605	(274,289)
Total expenses	<u>8,015,167</u>	<u>8,006,202</u>	<u>8,965</u>
Change in Net Position	505,585	4,701,163	(4,195,578)
Net Position - January 1	<u>54,456,116</u>	<u>49,754,953</u>	<u>4,701,163</u>
Net Position - December 31	<u>\$ 54,961,701</u>	<u>\$ 54,456,116</u>	<u>\$ 505,585</u>

The following graph shows revenues by source for 2018:



Capital Asset and Debt Administration

Capital assets. The System's investment in capital assets as of December 31, 2018, amounts to \$66,228,627 (net of accumulated depreciation). This investment in capital assets includes land, buildings and distribution system. The total decrease in the System's investment in capital assets for the current fiscal year was 1.3 percent.

The major capital asset events during the current fiscal year included the following:

- New Computers and Server - \$35,335
- KHC Holland Plant Media Filter - \$50,804
- Three work trucks - \$80,445
- Improvements added to construction in progress of \$1,169,928

Lincoln Pipestone Rural Water System's Capital Assets (net of depreciation)

	Water System		Increase (Decrease)
	2018	2017	
Land and Improvements	\$ 3,866,544	\$ 3,869,469	\$ (2,925)
Construction in Progress	389,539	10,614,494	(10,224,955)
Distribution System	61,703,598	52,320,549	9,383,049
Buildings	40,394	45,604	(5,210)
Machinery and Equipment	85,903	118,900	(32,997)
Vehicles	141,021	158,156	(17,135)
Office Equipment	1,628	5,339	(3,711)
Total	<u>\$ 66,228,627</u>	<u>\$ 67,132,511</u>	<u>\$ (903,884)</u>

Additional information on the System's capital assets can be found in Note 2C starting on page 24 of this report.

Long-term debt. At the end of the current fiscal year, the System had total bonded debt outstanding of \$40,841,000 . All of which is revenue debt. While all of the System's bonds have revenue streams, they are all backed by the full faith and credit of the System.

Lincoln Pipestone Rural Water System's Outstanding Debt

	Water System		Increase (Decrease)
	2018	2017	
Revenue Bonds	<u>\$ 40,841,000</u>	<u>\$ 47,572,000</u>	<u>\$ (6,731,000)</u>

The System's total debt decreased \$6,731,000, or 14.1 percent during the current fiscal year.

Additional information of the System's long-term debt can be found on Note 2D starting on page 25 of this report.

Factors Bearing on the Systems Future

The system is dependent on the United States Department of Agriculture for the vast majority of it funding. The continuation of this funding is dependent on the actions taken by the Minnesota and Federal legislature in the future.

Requests for Information

This financial report is designed to provide a general overview of the System's finances for all those with an interest in the System's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the Lincoln Pipestone Rural Water System's office, 415 East Benton Street, Box 188, Lake Benton, MN 56149.

FUND FINANCIAL STATEMENTS
ENTERPRISE FUND
LINCOLN PIPESTONE RURAL WATER SYSTEM
LAKE BENTON, MINNESOTA

FOR THE YEAR ENDED
DECEMBER 31, 2018

Lincoln Pipestone Rural Water System
Lake Benton, Minnesota
Statement of Net Position
December 31, 2018
With Comparative Totals for December 31, 2017

	2018	2017
Assets		
Current Assets		
Cash and temporary investments	\$ 4,386,544	\$ 4,168,664
Cash with fiscal agent	-	5,254,051
Receivables		
Interest	1,258	1,486
Accounts	477,824	100,346
Inventories	334,815	369,612
Special assessment - current portion	741,048	663,919
Prepaid items	36,987	19,851
Total Current Assets	5,978,476	10,577,929
Noncurrent Assets		
Restricted assets		
Cash and investments	12,073,001	12,545,391
Receivables		
Notes	52,395	70,995
Special Assessments	12,018,779	12,475,938
Other assets		
Patronage Dividend Receivable	646,089	632,505
Capital assets		
Nondepreciable	3,866,544	3,869,469
Construction in progress	389,539	10,614,494
Depreciable, net	61,972,544	52,648,548
Total Noncurrent Assets	91,018,891	92,857,340
Total Assets	96,997,367	103,435,269
Liabilities		
Current Liabilities		
Accounts payable	79,028	141,908
Due to other governments	1,568	1,458
Accrued salaries payable	30,257	26,324
Compensated absences payable	47,358	44,934
Unearned revenue	43,149	58,984
Accrued interest payable	714,048	784,339
Current portion of long-term liabilities	11,093,000	6,391,000
Total Current Liabilities	12,008,408	7,448,947
Noncurrent Liabilities		
Compensated absences payable - net of current portion	8,286	13,388
Bonds payable - net of current portion	30,018,972	41,516,818
Total Noncurrent Liabilities	30,027,258	41,530,206
Total Liabilities	42,035,666	48,979,153
Net Position		
Net investment in capital assets	30,857,853	31,118,967
Restricted for:		
Debt Service	17,847,256	18,534,656
Short-term Assets	755,466	415,960
Tank Maintenance	370,849	180,358
Unrestricted	5,130,277	4,206,175
Total Net Position	\$ 54,961,701	\$ 54,456,116

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

Lincoln Pipestone Rural Water System
Statement of Activities
For the Year Ended December 31, 2018
With Comparative Totals for Year Ended December 31, 2017

Functions/Programs	Program Revenues				Net (Expenses) Revenues and Changes in Net Position	
	Expenses	Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	2018	2017
Business-Type Activities						
Water	<u>\$ 8,015,167</u>	<u>\$ 6,048,041</u>	<u>\$ -</u>	<u>\$ 1,976,114</u>	<u>\$ 8,988</u>	<u>\$ 3,717,771</u>
General revenues						
Unrestricted investment earnings					183,129	116,947
Other revenues					313,468	866,445
Total General Revenues					<u>496,597</u>	<u>983,392</u>
Change in net position					505,585	4,701,163
Net position, January 1					<u>54,456,116</u>	<u>49,754,953</u>
Net position, December 31					<u>\$ 54,961,701</u>	<u>\$ 54,456,116</u>

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

Lincoln Pipestone Rural Water System
 Lake Benton, Minnesota
 Statement of Revenues, Expenses and Changes in Net Position
 For the Year Ended December 31, 2018
 With Comparative Actual Amounts for Year Ended December 31, 2017

	2018	2017
Operating Revenues		
Charges for sales and services		
Consumers	\$ 4,291,133	\$ 4,022,275
Municipalities	1,372,040	1,402,064
Other	92,350	127,514
Total Operating Revenues	5,755,523	5,551,853
Operating Expenses		
Sources of supply and pumping		
Salaries	193,150	185,184
Employee benefits	84,169	71,258
Transportation	10,461	12,746
Purchased power	284,151	322,708
New water source/well head protection	22,518	110,122
Repairs and materials	182,965	196,117
Chemical and supplies	235,602	275,290
Telephone	11,412	10,765
Licenses, Permits, Fees	57,017	64,989
Water Purchases	967,634	715,364
Total Source of Supply and Pumping	2,049,079	1,964,543
SCADA		
Salaries	77,556	85,633
Employee benefits	34,427	31,181
Transportation	13,643	8,027
Purchased power	221,652	186,498
Repairs and materials	65,076	12,282
Utilities	1,872	5,400
Telephone	11,758	5,785
Total SCADA	425,984	334,806
Distribution		
Salaries	376,995	389,534
Employee benefits	180,435	155,449
Transportation	70,693	71,053
Repairs and materials	138,013	105,625
Gopher Location	7,011	9,271
Telephone	22,047	11,027
Damage claims	6,289	7,489
Purchased power	3,427	13,359
Total Distribution	804,910	762,807
General and administrative		
Salaries	253,127	253,014
Employee benefits	92,748	80,482
Directors fees	76,514	73,716
Board Meetings	4,048	3,273
Supplies	22,494	34,001
Other services and charges	149,374	163,003
Repairs and materials	37,295	26,789
Transportation	12,398	8,262
Advertising and promotion	17,399	16,924
Dues and memberships	11,398	3,263
Training	2,000	6,848
Insurance	65,248	72,190
Utilities	15,448	10,155
Real estate taxes	32,808	33,026
Other	8,913	19,169
Total General and administrative	801,212	804,115
Depreciation	2,981,666	2,913,326
Total Operating Expenses	7,062,851	6,779,597
Operating Loss	(1,307,328)	(1,227,744)

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

Lincoln Pipestone Rural Water System
 Lake Benton, Minnesota
 Statement of Revenues, Expenses and Changes in Net Position (Continued)
 For the Year Ended December 31, 2018
 With Comparative Actual Amounts for Year Ended December 31, 2017

	2018	2017
Nonoperating Revenues (Expenses)		
Interest income	\$ 183,129	116,947
Capacity charges	292,518	563,611
Farm rental (net)	178,987	129,306
Intergovernmental		
Federal	95,840	831,092
State	29,734	3,315,073
Amortization of bond premium	64,846	64,846
Miscellaneous income	134,481	173,528
Bond issuance costs	(4,245)	(1,200)
Interest expense	(1,015,568)	(1,289,198)
Miscellaneous expense	(1,000)	(1,053)
Gain (loss) on sale of capital assets	3,651	-
Total Nonoperating Revenues (Expenses)	(37,627)	3,902,952
Income (Loss) Before Contributions	(1,344,955)	2,675,208
Special assessment revenue	1,507,115	1,546,129
Capital Contributions	343,425	479,826
Change in Net Position	505,585	4,701,163
Net Position, January 1	54,456,116	49,754,953
Net Position, December 31	\$ 54,961,701	\$ 54,456,116

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

Lincoln Pipestone Rural Water System
Lake Benton, Minnesota
Statement of Cash Flows
For the Year Ended December 31, 2018
With Comparative Actual Amounts for Year Ended December 31, 2017

	2018	2017
Cash Flows From Operating Activities		
Receipts from customers	\$ 5,348,626	\$ 5,490,546
Payments to suppliers and vendors	(2,833,687)	(2,875,393)
Payments to and on behalf of employees	(1,291,352)	(1,269,986)
Net Cash Provided (Used) By Operating Activities	1,223,587	1,345,167
Cash Flows From Noncapital Financing Activities		
Miscellaneous non-operating expense	(1,000)	(1,053)
Miscellaneous non-operating income	134,481	173,528
Net Cash Provided by Noncapital Financing Activities	133,481	172,475
Cash Flows From Capital and Related Financing Activities		
Acquisition of capital assets	(2,080,707)	(4,802,880)
Intergovernmental - Federal	95,840	941,352
Intergovernmental - State	29,734	3,315,073
Proceeds from sale of capital assets	6,576	17,683
Capacity charges	292,518	563,611
Farm rental income	178,987	129,306
Notes receivable	18,600	21,881
Interest on notes receivable	4,968	4,849
Special assessments	1,887,145	1,810,807
Capital contributions and grants	343,425	479,826
Principal paid on long-term debt	(6,731,000)	(1,374,000)
Interest and fees paid on long-term debt	(1,090,104)	(1,222,857)
Net Cash Used By Capital and Related Financing Activities	(7,044,018)	(115,349)
Cash Flows From Investing Activities		
Interest received on cash and investments	178,389	112,314
Net Increase (Decrease) in Cash and Cash Equivalents	(5,508,561)	1,514,607
Cash and Cash Equivalents, January 1	21,968,106	20,453,499
Cash and Cash Equivalents, December 31	\$ 16,459,545	\$ 21,968,106
Reconciliation Of Cash and Temporary Investments		
Cash and temporary investments - Unrestricted	\$ 4,386,544	\$ 4,168,664
Cash held with fiscal agent	-	5,254,051
Cash and temporary investments - Restricted	12,073,001	12,545,391
Total Cash and Temporary Investments	\$ 16,459,545	\$ 21,968,106
Reconciliation of Operating Loss to Net		
Cash Provided (Used) By Operating Activities:		
Operating loss	\$ (1,307,328)	\$ (1,227,744)
Adjustments to reconcile operating loss to net cash provided (used) by operating activities		
Depreciation	2,981,666	2,913,326
Prior period adjustment	-	(41,135)
(Increase) decrease in assets		
Accounts receivable	(377,478)	(84,283)
Inventories	34,797	(5,166)
Prepaid items	(17,136)	4,631
Patronage dividend	(13,584)	(36,008)
Increase in liabilities		
Accounts payable	(62,880)	(261,553)
Due to other governments	110	1,231
Accrued salaries payable	3,933	26,839
Compensated absences payable	(2,678)	(3,955)
Unearned revenue	(15,835)	58,984
Net Cash Provided (Used) By Operating Activities	\$ 1,223,587	\$ 1,345,167
Noncash Investing, Capital and Financing Activities		
Book value of disposed/traded capital assets	\$ 2,925	\$ 17,683
Amortization of bond (premium) discount	\$ (64,846)	\$ (64,846)

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

Lincoln Pipestone Rural Water System
Lake Benton, Minnesota
Notes to the Financial Statements
December 31, 2018

Note 1: Summary of Significant Accounting Policies

A. Reporting Entity

The Lincoln Pipestone Rural Water System (the System) was established pursuant to MN Statutes 116A under the jurisdiction of the Fifth Judicial District. The participating counties of Lincoln, Pipestone, Jackson, Murray, Rock, Nobles, Lyon, Lac qui Parle, Redwood and Yellow Medicine have agreed to guarantee their share of the debt arising within each respective county. The Lincoln Pipestone Rural Water System provides water for participating rural water users and cities within the water district.

The System is governed by an eleven member board appointed for terms of four years by the District Court. The board of Commissioners has control over all activities relating to Lincoln Pipestone Rural Water System.

The System considered all potential units for which it is financially accountable, and other organizations for which the nature and significance of their relationship with the System are such that exclusion would cause the System's financial statements to be misleading or incomplete. The Governmental Accounting Standards Board (GASB) has set forth criteria to be considered in determining financial accountability. These criteria include appointing a voting majority of an organization's governing body, and (1) the ability of the primary government to impose its will on that organization or (2) the potential for the organization to provide specific benefits to, or impose specific financial burdens on the primary government. The System has no component units that meet the GASB criteria.

B. Measurement Focus, Basis of Accounting and Financial Statement Presentation

The System's financial statements are reported using the *economic resources measurement focus* and the *accrual basis of accounting* in accordance with accounting principles generally accepted in the United States of America. Under this method, revenues are recorded when earned and expenses are recorded when a liability is incurred.

The System is accounted for as an enterprise fund. Enterprise funds are used to account for operations that are financed and operated in a manner similar to private business enterprises, where the determination of net income is necessary or useful to sound financial administration. The intent of the governing body is that the costs of providing goods or services to the members and cities on a continuing basis be financed or recovered primarily through user charges.

Revenue resulting from exchange transactions, in which each party gives and receives essentially equal value, is recorded on the accrual basis when the exchange takes place.

Non-exchange transactions, in which the System receives value without directly giving equal value in return, include grants, entitlement and donations. Revenue from grants, entitlements and donations is recognized in the year in which all eligibility requirements have been satisfied. Eligibility requirements include timing requirements, which specify the year when the resources are required to be used or the year when use is first permitted, matching requirements, in which the System must provide local resources to be used for a specified purpose, and expenditure requirements, in which the resources are provided to the System on a reimbursement basis.

Unearned revenue arises when assets are recognized before revenue recognition criteria have been satisfied. Grants and entitlements received before eligibility requirements are met are also recorded as unearned revenue.

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. Accordingly, actual results could differ from those estimates.

The System reports the following major proprietary fund:

The *Water fund* accounts for the activities of the System's water distribution system operations.

Lincoln Pipestone Rural Water System
Lake Benton, Minnesota
Notes to the Financial Statements
December 31, 2018

Note 1: Summary of Significant Accounting Policies (Continued)

Proprietary funds distinguish *operating* revenues and expenses from *nonoperating* items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. The principal operating revenues of the System's enterprise fund is charges to customers for sales and services. The System also recognizes as operating revenue the portion of tap fees intended to recover the cost of connecting new customers to the system. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

When both restricted and unrestricted resources are available for use, it is the System's policy to use restricted resources first, then unrestricted resources as they are needed.

C. Assets, Liabilities and Net Position

Deposits and Investments

The System's cash and cash equivalents are considered to be cash on hand, demand deposits and short-term investments with original maturities of three months or less from the date of acquisition. Cash balances are invested to the extent available in various deposits and investments authorized by Minnesota State statutes. For purposes of the statement of cash flows, cash equivalents include demand deposit account balances and certificates of deposit.

The System may also invest idle funds as authorized by Minnesota statutes, as follows:

1. Direct obligations or obligations guaranteed by the United States or its agencies.
2. Shares of investment companies registered under the Federal Investment Company Act of 1940 and received the highest credit rating, rated in one of the two highest rating categories by a statistical rating agency, and have a final maturity of thirteen months or less.
3. General obligations of a state or local government with taxing powers rated "A" or better; revenue obligations rated "AA" or better.
4. General obligations of the Minnesota Housing Finance Agency rated "A" or better.
5. Obligation of a school district with an original maturity not exceeding 13 months and (i) rated in the highest category by a national bond rating service or (ii) enrolled in the credit enhancement program pursuant to statute section 126C.55.
6. Bankers' acceptances of United States banks eligible for purchase by the Federal Reserve System.
7. Commercial paper issued by United States banks corporations or their Canadian subsidiaries, of highest quality category by at least two nationally recognized rating agencies, and maturing in 270 days or less.
8. Repurchase or reverse repurchase agreements and securities lending agreements with financial institutions qualified as a "depository" by the government entity, with banks that are members of the Federal Reserve System with capitalization exceeding \$10,000,000, a primary reporting dealer in U.S. government securities to the Federal Reserve Bank of New York, or certain Minnesota securities broker-dealers.
9. Guaranteed investment contracts (GIC's) issued or guaranteed by a United States commercial bank, a domestic branch of a foreign bank, a United States insurance company, or its Canadian subsidiary, whose similar debt obligations were rated in one of the top two rating categories by a nationally recognized rating agency.

Broker money market funds operate in accordance with appropriate state laws and regulations. The reported value of the pool is the same as the fair value of the shares.

Lincoln Pipestone Rural Water System
Lake Benton, Minnesota
Notes to the Financial Statements
December 31, 2018

Note 1: Summary of Significant Accounting Policies (Continued)

The System categorizes its fair value measurements within the fair value hierarchy established by generally accepted accounting principles. The hierarchy is based on the valuation inputs used to measure the fair value of the asset. Level 1 inputs are quoted prices in active markets for identical assets; Level 2 inputs are significant other observable inputs; Level 3 inputs are significant unobservable inputs.

The System has the following recurring fair value measurements as of December 31, 2018:

- Negotiable certificates of deposit of \$1,484,067 are valued using a matrix pricing model (Level 2 inputs)

The Minnesota Municipal Money Market Fund is regulated by Minnesota statutes and the Board of Directors of the League of Minnesota Cities and is an external investment pool not registered with the Securities Exchange Commission (SEC) that follows the regulatory rules of the SEC. In accordance with GASB Statement No. 79, the System's investment in this pool is valued at amortized cost, which approximates fair value. There are no restrictions or limitations on withdrawals from the 4M Liquid Asset Fund. Investments in the 4M Plus must be deposited for a minimum of 14 calendar days. Withdrawals prior to the 14-day restriction period will be subject to a penalty equal to seven days interest on the amount withdrawn. Seven days' notice of redemption is required for withdrawals of investments in the 4M Term Series withdrawn prior to the maturity date of that series. A penalty could be assessed as necessary to recoup the Series for any charges, losses, and other costs attributable to the early redemption. Financial statements of the 4M Fund can be obtained by contracting RBC Global Management at 100 South Fifth Street, Suite 2300, Minneapolis, MN 55402-1240.

The System has not adopted a formal investment policy that addresses interest rate and credit risk.

Restricted Cash

The System has received monies restricted for specific purposes. The balance in restricted cash represents unspent deposits of \$12,073,001 to be used for capital improvements and debt payments.

Accounts Receivable

Accounts receivable include amounts billed for services provided before year end. Unbilled utility enterprise fund receivables are also included for services provided in 2018. All receivables are reported at their gross value and, if appropriate, reduced by the estimated portion that is expected to be uncollectible. Uncollectible accounts are periodically charged to operations on a direct write-off method. There is no allowance for uncollectible amounts in the fund.

Special Assessments

Special assessments represent the financing for public improvements paid for by benefiting property owners. These assessments are recorded as receivable upon certification to the County. Special assessments are recognized as revenue when they are received in cash or within 60 days after year end.

Inventories and Prepaid Items

All inventories are valued at the lower of cost or market using the first-in, first-out (FIFO) method.

Certain payments to vendors reflect costs applicable to future accounting periods and are recorded as prepaid items.

Lincoln Pipestone Rural Water System
 Lake Benton, Minnesota
 Notes to the Financial Statements
 December 31, 2018

Note 1: Summary of Significant Accounting Policies (Continued)

Capital Assets

Capital assets, which include property, plant and equipment, are reported in the financial statements. Capital assets are defined by the System as assets with an initial estimated useful life in excess of one year. Such assets are recorded at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at acquisition 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 as constructed. Interest incurred during the construction phase of capital assets of business-type activities is included as part of the capitalized value of the assets constructed.

Property, plant and equipment are depreciated in the proprietary fund of the System using the straight line method over the following estimated useful lives:

<u>Assets</u>	<u>Years</u>
Distribution System	7 - 40
Machinery and Equipment	5 - 20
Buildings	20

Compensated Absences

The established vacation year is the calendar year, January 1 through December 31 each year. Vacations are accrued or earned based on the employee's length of service and the time actually worked. Employees will not continue to accrue vacation time once they have accrued 125 percent of the maximum number of hours they can earn in the current calendar year.

Full-time employees will accrue paid vacation according to the following schedule, (annual totals will be rounded to the nearest whole hour):

<u>Service Period</u>	<u>Paid Vacation Accrual Rate</u>
First calendar year or part thereof	3.333 hours per month worked (40 hours per year maximum earned)
Calendar years 2 through 5	6.666 hours per month worked (80 hours per year maximum earned)
Calendar years 6 through 15	10.0 hours per month worked (120 hours per year maximum earned)
Calendar years 16 and over	13.33 hours per month worked (160 hours per year maximum earned)

Employees may not receive vacation pay in lieu of time off. In addition, employee will cease to earn additional vacation time once they have accrued 125 percent of the maximum number of hours they can earn in the current calendar year.

When employment is terminated, employees will received vacation pay for any unused vacation accrued at the time of termination.

Lincoln Pipestone Rural Water System
Lake Benton, Minnesota
Notes to the Financial Statements
December 31, 2018

Note 1: Summary of Significant Accounting Policies (Continued)

Long-term Obligations

Long-term debt and other long-term obligations are reported as liabilities. The recognition of bond premiums and discounts are deferred and amortized over the life of the bonds using the straight line method. Bonds payable are reported net of the applicable bond premium or discount. Bond issuance costs are reported as an expense in the period incurred.

Net Position

Net position represents the difference between assets and liabilities. Net position is displayed in three components:

- a. Net Investment in capital assets - Consists of capital assets, net of accumulated depreciation reduced by any outstanding debt attributable to acquire capital assets.
- b. Restricted net position - Consists of net position restricted when there are limitations imposed on their use through external restrictions imposed by creditors, grantors, laws or regulations of other governments.
- c. Unrestricted net position - All other net position that do not meet the definition of "restricted" or "Net investment in capital assets."

Note 2: Detailed Notes

A. Deposits and Investments

Deposits

Custodial credit risk for deposits and investments is the risk that in the event of a bank failure, the System's deposits may not be returned or the System will not be able to recover collateral securities in the possession of an outside party. In accordance with Minnesota statutes and as authorized by the System, the System maintains deposits at those depository banks, all of which are members of the Federal Reserve System.

Minnesota statutes require that all System deposits be protected by insurance, surety bond, or collateral. The market value of collateral pledged must equal 110 percent of the deposits not covered by insurance or bonds.

Authorized collateral in lieu of a corporate surety bond includes:

- United States government Treasury bills, Treasury notes, Treasury bonds;
- Issues of United States government agencies and instrumentalities as quoted by a recognized industry quotation service available to the government entity;
- General obligation securities of any state or local government with taxing powers which is rated "A" or better by a national bond rating service, or revenue obligation securities of any state or local government with taxing powers which is rated "AA" or better by a national bond rating service;
- General obligation securities of a local government with taxing powers may be pledged as collateral against funds deposited by that same local government entity;
- Irrevocable standby letters of credit issued by Federal Home Loan Banks to a municipality accompanied by written evidence that the bank's public debt is rated "AA" or better by Moody's Investors Service, Inc., or Standard & Poor's Corporation; and
- Time deposits that are fully insured by any federal agency.

Lincoln Pipestone Rural Water System
 Lake Benton, Minnesota
 Notes to the Financial Statements
 December 31, 2018

Note 2: Detailed Notes (Continued)

Minnesota statutes require that all collateral shall be placed in safekeeping in a restricted account at a Federal Reserve Bank, or in an account at a trust department of a commercial bank or other financial institution that is not owned or controlled by the financial institution furnishing the collateral. The selection should be approved by the government entity.

At year end, the System's carrying amount of deposits was \$7,376,219 and the bank balance was \$7,536,235. At the end of the year, \$6,241,198 was covered by FDIC insurance. The remaining was covered by collateral.

Investments

As of December 31, 2018, the System had the following investments that are insured or registered, or securities held by the System's agent in the System's name:

Types of Investments	Credit Quality/ Ratings (1)	Segmented Time Distribution (2)	Amount	Fair Value Measurement Using	
				Level 1	Level 2
Pooled Investments at Amortized Costs					
4M Fund	N/A	less than 6 months	\$ 4,270,278		
4M Fund	N/A	6 months to 1 year	1,462,800		
4M Fund	N/A	1 to 3 years	1,475,882		
Non-pooled Investments at Amortized Costs					
Money Market Funds	N/A	less than 6 months	390,011		
Non-Pooled Investments at Fair Value					
Negotiable certificates of deposits	N/A	less than 6 months	499,740	\$ -	\$ 499,740
Negotiable certificates of deposits	N/A	6 months to 1 year	984,327	-	984,327
Total Investments			<u>\$ 9,083,038</u>	<u>\$ -</u>	<u>\$ 1,484,067</u>

(1) Ratings are provided by various credit rating agencies where applicable to indicate associated credit risk.

(2) Interest rate risk is disclosed using the segmented time distribution method.

N/A Indicates not applicable or available.

A reconciliation of cash and investments as shown on the statement of net position for the System follows:

Carrying Amount of Deposits	\$ 7,376,219
Investments	9,083,038
Cash on Hand	<u>288</u>
Total	<u>\$ 16,459,545</u>
Cash and Temporary Investments	\$ 4,386,544
Restricted Cash and Temporary Investments	<u>12,073,001</u>
Total Deposits	<u>\$ 16,459,545</u>

Lincoln Pipestone Rural Water System
 Lake Benton, Minnesota
 Notes to the Financial Statements
 December 31, 2018

Note 2: Detailed Notes (Continued)

B. Notes Receivable

Municipalities which are benefited by the Rural Water System have contracted to pay their share of the cost of the construction. The contract for a period of 27 years in the form of a direct reduction loan at 5 percent interest. The balance of the loans outstanding at December 31, 2018, are as follows:

Municipality	Balance at Year End
Fairview	\$ 18,086
Ihlen	7,562
Hardwick	26,747
Total	\$ 52,395

C. Capital Assets

Capital asset activity for the System for the year ended December 31, 2018 was as follows:

	Beginning Balance	Increases	Decreases	Ending Balance
Capital Assets Not Being Depreciated				
Land	\$ 3,869,469	\$ -	\$ (2,925)	\$ 3,866,544
Construction in progress	10,614,494	1,169,928	(11,394,883)	389,539
Total capital assets not being depreciated	14,483,963	1,169,928	(11,397,808)	4,256,083
Capital Assets Being Depreciated				
Distribution System	97,012,214	12,225,217	-	109,237,431
Buildings	193,138	-	-	193,138
Vehicles	504,268	80,445	(69,140)	515,573
Machinery and equipment	1,206,916	-	-	1,206,916
Office Equipment	88,526	-	-	88,526
Total Capital Assets Being Depreciated	99,005,062	12,305,662	(69,140)	111,241,584
Less Accumulated Depreciation for				
Distribution System	(44,691,665)	(2,842,168)	-	(47,533,833)
Buildings	(147,534)	(5,210)	-	(152,744)
Vehicles	(346,112)	(97,580)	69,140	(374,552)
Machinery and equipment	(1,088,016)	(32,997)	-	(1,121,013)
Office Equipment	(83,187)	(3,711)	-	(86,898)
Total Accumulated Depreciation	(46,356,514)	(2,981,666)	69,140	(49,269,040)
Total Capital Assets Being Depreciated, Net	52,648,548	9,323,996	-	61,972,544
Total Capital Assets, Net	\$ 67,132,511	\$ 10,493,924	\$(11,397,808)	\$ 66,228,627

The depreciation was all part of the water system and totaled \$2,981,666.

Lincoln Pipestone Rural Water System
 Lake Benton, Minnesota
 Notes to the Financial Statements
 December 31, 2018

Note 2: Detailed Notes (Continued)

D. General Long-term Debt

General Obligation Revenue Bonds

The following bonds will be repaid from future revenues.

Description	Authorized and Issued	Interest Rate	Issue Date	Maturity Date	Balance at Year End
G.O. Water System Refunding Bonds of 2012	\$ 1,050,000	2.00 %	02/15/12	01/01/22	\$ 370,000
G.O. Water Revenue Crossover Refunding Bonds of 2012A	1,595,000	2.00	04/01/12	01/01/24	770,000
G.O. Water Revenue Bonds of 2011A	5,000,000	3.00	12/20/11	01/01/52	4,553,000
G.O. Water Revenue Bonds of 2011B	5,917,000	3.00	12/20/11	01/01/52	5,387,000
G.O. Water System Refunding Bonds of 2013A	3,055,000	2.00 - 2.35	12/11/13	01/01/23	1,380,000
G.O. Water Revenue Bonds of 2010 Jackson-Nobles	8,500,000	3.75	12/20/10	01/01/50	7,330,000
G.O. Water Bonds	800,000	3.25	09/22/10	01/01/49	704,000
G.O. Water Revenue Refunding Bonds of 2013A	2,910,000	3.00 - 3.75	12/11/13	03/01/32	2,400,000
G.O. Water Revenue Refunding Bonds of 2016A	4,260,000	2.00 - 2.50	06/01/16	01/01/34	4,020,000
G.O. Water Revenue Refunding Bonds of 2016A - Pipestone	1,080,000	1.75 - 2.10	03/15/16	01/01/28	980,000
G.O. Water Temporary Water Revenue Bonds of 2016B	9,890,000	1.00	10/03/16	10/01/19	9,890,000
G.O. Water Revenue Bonds of 2016B - Lincoln	3,108,000	2.25	06/16/16	01/01/56	<u>3,057,000</u>
Total Revenue Bonds					<u><u>\$ 40,841,000</u></u>

Lincoln Pipestone Rural Water System
 Lake Benton, Minnesota
 Notes to the Financial Statements
 December 31, 2018

Note 2: Detailed Notes (Continued)

The annual service requirements to maturity for the general obligation revenue bonds are as follows:

Year Ending December 31,	Revenue Bonds		
	Business-type Activities		
	Principal	Interest	Total
2019	\$ 11,093,000	\$ 940,605	\$ 12,033,605
2020	1,565,000	851,206	2,416,206
2021	1,537,000	806,061	2,343,061
2022	1,443,000	770,821	2,213,821
2023	1,137,000	736,233	1,873,233
2024 - 2028	5,218,000	3,285,139	8,503,139
2029 - 2033	5,063,000	2,568,213	7,631,213
2034 - 2038	3,475,000	1,913,640	5,388,640
2039 - 2043	3,525,000	1,382,055	4,907,055
2044 - 2048	3,946,000	796,083	4,742,083
2049 - 2053	2,492,000	191,228	2,683,228
2054 - 2056	347,000	15,725	362,725
Total	<u>\$ 40,841,000</u>	<u>\$ 14,257,009</u>	<u>\$ 55,098,009</u>

Changes in Long-term Liabilities

During the year ended December 31, 2018, the following changes occurred in non-current liabilities reported on the government-wide statements.

	Beginning Balance	Increases	Decreases	Ending Balance	Due Within One Year
Business-Type Activities:					
Bonds Payable					
Revenue bonds	\$ 47,572,000	\$ -	\$ (6,731,000)	\$ 40,841,000	\$ 11,093,000
Bond Premium	335,818	-	(64,846)	270,972	-
Compensated Absences Payable	58,322	59,999	(62,677)	55,644	47,358
Business-Type Activity Long-term Liabilities	<u>\$ 47,966,140</u>	<u>\$ 59,999</u>	<u>\$ (6,858,523)</u>	<u>\$ 41,167,616</u>	<u>\$ 11,140,358</u>

Note 3: Other Information

A. Retirement Plan

The System has adopted a SAR/SEP retirement plan effective January 1, 1986. The plan allows employees to make contributions immediately upon becoming employed, provided they are at least 21 years old. The System may make employer contributions up to 15 percent of an eligible employee's compensation. The total company contributions for 2018 were \$46,315 and total employee contributions paid were \$53,160.

B. Concentration

The System provides only water as its main source of revenue. If these water sales or any of the major customers were to experience any substantial changes it may have an adverse effect on the revenues of the system.

Lincoln Pipestone Rural Water System
Lake Benton, Minnesota
Notes to the Financial Statements
December 31, 2018

Note 3: Other Information (Continued)

C. Risk Management

The System is exposed to various risks of loss related to torts; theft of, damage to and destruction of assets; errors and omissions; injuries to employees; and natural disasters for which the System carries insurance. The System obtains insurance through participation in the League of Minnesota Cities Insurance Trust (LMCIT) which is a risk sharing pool with approximately 800 other governmental units. The System pays an annual premium to LMCIT for its property and casualty insurance. The LMCIT is self-sustaining through member premiums and will reinsure for claims above a prescribed dollar amount for each insurance event. Settled claims have not exceeded the System's coverage in any of the past three fiscal years.

Liabilities are reported when it is probable that a loss has occurred and the amount of the loss can be reasonably estimated. Liabilities, if any, include an amount for claims that have been incurred but not reported (IBNRs). The System's management is not aware of any incurred but not reported claims.

OTHER REQUIRED REPORTS
LINCOLN PIPESTONE RURAL WATER SYSTEM
LAKE BENTON, MINNESOTA

FOR THE YEAR ENDED
DECEMBER 31, 2018



INDEPENDENT AUDITOR'S REPORT ON
MINNESOTA LEGAL COMPLIANCE

Board of Commissioners
Lincoln Pipestone Rural Water System
Lake Benton, Minnesota

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 the Government Auditing Standards, issued by the Comptroller General of the United States, the accompanying financial statements of the Lincoln Pipestone Rural Water System (the System) as of and for the year ended December 31, 2018, and the related notes to the financial statements, and have issued our report thereon dated March 28, 2019.

The *Minnesota Legal Compliance Audit Guide for Other Political Subdivisions*, promulgated by the State Auditor pursuant to Minnesota Statute §6.65, contains seven categories of compliance to be tested: contracting and bidding, deposits and investments, conflicts of interest, public indebtedness, claims and disbursements, miscellaneous provisions and tax increment financing. Our audit considered all of the listed categories except tax increment financing because the System has not established any tax increment financing districts.

In connection with our audit, nothing came to our attention that caused us to believe that the System failed to comply with the provisions of the *Minnesota Legal Compliance Audit Guide for Other Political Subdivisions*. However, our audit was not directed primarily toward obtaining knowledge of such noncompliance. Accordingly, had we performed additional procedures, other matters may have come to our attention regarding the System's noncompliance with the above referenced provisions.

ABDO, EICK & MEYERS, LLP
Mankato, Minnesota
March 28, 2019



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

Board of Commissioners
Lincoln Pipestone Rural Water System
Lake Benton, Minnesota

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 enterprise fund activities of the Lincoln Pipestone Rural Water System (the System), as of and for the year ended December 31, 2018, and the related notes to the financial statements, which collectively comprise the System's basic financial statements, and have issued our report thereon dated March 28, 2019.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the System'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 System's internal control. Accordingly, we do not express an opinion on the effectiveness of the System's internal control.

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

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the System'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*.

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 System'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 System's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

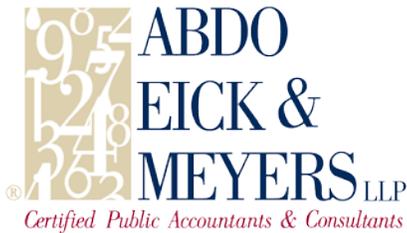
Abdo Eick & Meyers, LLP

ABDO, EICK & MEYERS, LLP
Mankato, Minnesota
March 28, 2019

FEDERAL FINANCIAL AWARD PROGRAMS

CITY OF SAMPLE
SAMPLE, MINNESOTA

FOR THE YEAR ENDED
DECEMBER 31, 2018



INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE
FOR EACH MAJOR FEDERAL PROGRAM AND REPORT
ON INTERNAL CONTROL OVER COMPLIANCE REQUIRED
BY THE UNIFORM GUIDANCE

Board of Commissioners
Lincoln Pipestone Rural Water System
Lake Benton, Minnesota

Report on Compliance for Each Major Federal Program

We have audited the Lincoln Pipestone Rural Water System (the System), Lake Benton, Minnesota compliance with the types of compliance requirements described in the *OMB Compliance Supplement* that could have a direct and material effect on each of the System's major federal programs for the year ended December 31, 2018. The System's major federal programs are identified in the summary of auditor's results section of the accompanying Schedule of Findings and Questioned Costs.

Management's Responsibility

Management is responsible for compliance with federal statutes, regulations, and the terms and conditions of its federal awards applicable to its federal programs.

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for each of the System's major federal programs based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and the audit requirements of Title 2 U.S. Code of Federal Regulations Part 200, Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards (Uniform Guidance). Those standards and the Uniform Guidance require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the System's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

We believe that our audit provides a reasonable basis for our opinion on compliance for each major federal program. However, our audit does not provide a legal determination of the System's compliance.

Opinion on Each Major Federal Program

In our opinion, the System complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended December 31, 2018.

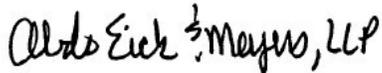
Report on Internal Control Over Compliance

Management of the System is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered the System's internal control over compliance with the types of requirements that could have a direct and material effect on each major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major federal program and to test and report on internal control over compliance in accordance with the Uniform Guidance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the System's internal control over compliance.

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

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

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of the Uniform Guidance. Accordingly, this report is not suitable for any other purpose.



ABDO, EICK & MEYERS, LLP
Mankato, Minnesota
March 28, 2019

Lincoln Pipestone Rural Water System
 Schedule of Expenditures of Federal Awards
 For the Year Ended December 31, 2018

<u>Federal Funding Source</u>	<u>Program Name</u>	<u>Federal Domestic Assistance Number</u>	<u>Pass-Through Entity Identifying Number</u>	<u>Total Federal Expenditures</u>
U.S. Department of Agriculture	Water and Waste Disposal Systems for Rural Communities	10.760	N/A	<u>\$ 753,568</u>

Lincoln Pipestone Rural Water System
Lake Benton, Minnesota
Notes to the Schedule of Expenditures of Federal Awards
For the Year Ended December 31, 2018

1. Basis of Presentation

The accompanying Schedule of Expenditures of Federal Awards includes the federal grant activity of the Lincoln Pipestone Rural Water System (the System) for the year ended December 31, 2018. The System's reporting entity is defined in Note 1A to the System's financial statements. The information in this schedule is presented in accordance with the requirement of the Uniform Guidance, Audits of States, Local Governments, and Non-Profit Organizations. All Federal awards received directly from Federal agencies as well as Federal awards passed through other government agencies are included on the schedule.

2. Summary of Significant Accounting Policies for Expenditures

Expenditures reported on this schedule are reported on the modified accrual basis of accounting.

3. Pass-through Entity Identifying Numbers

Pass-through entity identifying numbers are presented where available.

4. Subrecipients

No federal expenditures presented in this schedule were provided to subrecipients.

5. Indirect Cost Rate

During the year ended December 31, 2018, the System did not elect to use the 10 percent de minimis indirect cost rate.

Lincoln Pipestone Rural Water System
 Schedule of Findings, Responses and Questioned Costs
 For the Year Ended December 31, 2018

Section I - Summary of Auditor's Results

Financial Statements

Type of auditor's report issued	Unmodified
Internal control over financial reporting	
Material weaknesses identified?	No
Significant deficiencies identified not considered to be material weaknesses?	None reported
Noncompliance material to financial statements noted?	No

Federal Awards

Internal control over major programs	
Material weaknesses identified?	No
Significant deficiencies identified not considered to be material weaknesses?	None reported
Type of auditor's report issued on compliance for major programs	Unmodified
Any audit findings disclosed that are required to be reported in accordance with 2CFR section 200.516(a)?	No

Identification of Major Programs/Projects

	CFDA No.
Water and Waste Disposal Systems for Rural Communities	10.760
Dollar threshold used to distinguish between Type A and Type B Programs	\$ 750,000
Auditee qualified as low-risk auditee?	Yes

Section II - Financial Statement Findings

None

Section III - Major Federal Award Findings and Questioned Costs

There are no significant deficiencies, material weaknesses, or instances of noncompliance including questioned costs that are required to be reported in accordance with Uniform Guidance.

Section IV - Schedule of Prior Year Audit Findings

None