

AUDIT REPORT

LATIMER COUNTY RURAL WATER DISTRICT #3
LATIMER COUNTY, OKLAHOMA

DECEMBER 31, 2018



KERSHAW CPA & ASSOCIATES, PC

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LATIMER COUNTY RURAL WATER DISTRICT #3
LATIMER COUNTY, OKLAHOMA
DECEMBER 31, 2018

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LATIMER COUNTY RURAL WATER DISTRICT #3
LATIMER COUNTY, OKLAHOMA
DECEMBER 31, 2018

BOARD OF DIRECTORS

<u>NAME</u>	<u>POSITION</u>
CHARLOTTE ELLIS	CHAIRMAN
MARY HESTON	VICE CHAIRMAN
HALEY JUDKINS	SECRETARY/TREASURER
FRANCES BROWN	MEMBER
JAMIE STEPHENS	MEMBER

STAFF

PHILIP JUDKINS*	MANAGER/BOOKKEEPER
BUD ELLIS	OPERATOR

*Resigned in May 2019

Unaudited

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INDEPENDENT AUDITOR'S REPORT

To the Board of Directors
Latimer County Rural Water District #3
Latimer County, Oklahoma

Report on Financial Statements

We have audited the accompanying modified cash basis financial statements of Latimer County Rural Water District #3, as of and for the fiscal year ended December 31, 2018, as listed in the table of contents and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with the 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 the financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America, and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, and in accordance with Oklahoma Statutes. 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 District's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances but not for the purpose of expressing an opinion on the effectiveness of the District's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used, and the reasonableness of significant accounting

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estimates made, by management, as well as evaluating the overall presentation of the financial statements.

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective modified cash basis financial position of the Latimer County Rural Water District #3, Latimer County, Oklahoma, as of December 31, 2018, and the respective changes in modified cash basis financial position thereof for the year then ended in conformity with the basis of accounting described in Note 1.

Basis of Accounting

We draw attention to Note 1 of the financial statements that 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 opinion is not modified with respect to this matter.

Other Matters

Supplementary and Other Information

The introductory section listed in the accompanying table of contents is presented for the purpose of additional analysis and is not a required part of the basic financial statements of the District. Such additional information has not been subjected to the auditing procedures applied in our 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 December 16, 2019, on our consideration of the Latimer County Rural Water District #3'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 Latimer County Rural Water District #3's internal control over financial reporting or on compliance. That report is an integral part of an audit performed in compliance with

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Government Auditing Standards in considering Latimer County Rural Water District #3's internal control over financial reporting and compliance.

Kershaw CPA & Associates, P.C.

Kershaw CPA & Associates, PC
Muskogee, Oklahoma

December 16, 2019

LATIMER COUNTY RURAL WATER DISTRICT #3
LATIMER COUNTY, OKLAHOMA
STATEMENT OF NET POSITION - MODIFIED CASH BASIS
DECEMBER 31, 2018

	Total 2018	Total (Memo Only) 2017
<u>ASSETS</u>		
<u>Current Assets:</u>		
Cash and Cash Equivalents	\$ 68,376	\$ 78,535
Prepaid Payroll Taxes	-	-
Total Current Assets	68,376	78,535
<u>Restricted Assets:</u>		
Meter Deposits	7,250	7,250
Reserve Fund	8,828	8,775
Total Restricted Assets	16,078	16,025
<u>Capital Assets:</u>		
Water Distribution System	661,351	656,567
Less: Accumulated Depreciation	(393,727)	(375,480)
Total Capital Assets	267,624	281,087
<u>Other Assets:</u>		
ORWA Water Assistance Certificate	1,000	1,000
Total Other Assets	1,000	1,000
TOTAL ASSETS	\$ 353,077	\$ 376,647
 <u>LIABILITIES</u>		
<u>Current Liabilities:</u>		
Payroll Taxes Payable	\$ -	\$ -
Water Deposits Payable	7,250	7,250
Current Portion of Long-Term Debt	5,235	4,980
Total Current Liabilities	12,485	12,230
<u>Long-Term Liabilities:</u>		
Notes Payable - USDA Rural Development	52,282	58,102
Less: Current Portion of Long-Term Debt	(5,235)	(4,980)
Total Long-Term Liabilities	47,047	53,122
TOTAL LIABILITIES	59,532	65,352
<u>NET POSITION</u>		
Net investment in capital assets	215,342	222,984
Restricted for debt service	16,078	16,025
Unrestricted	62,126	72,285
TOTAL NET POSITION	293,546	311,294
TOTAL LIABILITIES & NET POSITION	\$ 353,077	\$ 376,647

See Accountant's Audit Report & Notes Which Accompany These Financial Statements

**LATIMER COUNTY RURAL WATER DISTRICT #3
LATIMER COUNTY, OKLAHOMA
STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET POSITION
- MODIFIED CASH BASIS -
FOR THE FISCAL YEAR ENDED DECEMBER 31, 2018**

	Total 2018	Total (Memo Only) 2017
<u>Operating Revenues:</u>		
Water Sales	\$ 76,946	\$ 76,218
Membership Fees	-	-
Late Fees & Other Miscellaneous	-	-
Total Operating Revenues	76,946	76,218
<u>Operating Expenses:</u>		
Salaries	25,201	23,998
Payroll Taxes	714	1,940
Depreciation	18,247	18,087
Office Supplies	1,285	1,409
Repairs and Maintenance	4,911	2,692
Postage	-	-
Travel Expense	2,466	2,613
Insurance & Bonds	2,619	2,405
Legal & Professional	2,066	2,511
Utilities	4,339	4,028
Water Purchases	29,868	20,909
Miscellaneous	700	697
Total Operating Expenses	92,415	81,288
Operating Income (Loss)	(15,470)	(5,070)
<u>Non-Operating Revenues (Expenses):</u>		
Grant Income	-	-
Interest Income	494	377
Interest Expense	(2,773)	(3,056)
Total Non-operating Revenues (Expenses)	(2,279)	(2,679)
Change in Net Position	(17,749)	(7,748)
Total Net Position - Beginning	311,294	319,043
Total Net Position - Prior Year Adjustment	-	-
Total Net Position - Ending	\$ 293,546	\$ 311,294

See Accountant's Audit Report & Notes Which Accompany These Financial Statements

**LATIMER COUNTY RURAL WATER DISTRICT #3
LATIMER COUNTY, OKLAHOMA
STATEMENT OF CASH FLOWS - MODIFIED CASH BASIS
FOR THE FISCAL YEAR ENDED DECEMBER 31, 2018**

	2018	Memorandum Only 2017
<u>Cash Flows from Operating Activities:</u>		
Cash Receipts from Customers	\$ 76,946	\$ 76,218
Payments to Suppliers for Goods & Services	(48,254)	(37,262)
Payments to Employees	(25,915)	(25,938)
	<u>2,777</u>	<u>13,018</u>
<u>Cash Flows from Capital & Related Financing Activities:</u>		
Additions to Capital Assets	(4,784)	-
Grant Income	-	-
Principal paid on Debt	(5,821)	(5,537)
Interest paid on Debt	(2,773)	(3,056)
	<u>(13,377)</u>	<u>(8,593)</u>
<u>Cash Flows from Investing Activities:</u>		
(Increase)Decrease in Reserve Fund	(53)	(39)
Interest Income	494	377
	<u>441</u>	<u>338</u>
Net Increase (Decrease) in Cash and Cash Equivalents	(10,159)	4,762
Cash & Cash Equivalents, Beginning of Year	78,535	73,773
Cash & Cash Equivalents, Prior Year Adjustment	-	-
Cash & Cash Equivalents, End of Year	<u>\$ 68,376</u>	<u>\$ 78,535</u>
<u>Reconciliation of operating income (loss) to net cash provided operating activities:</u>		
Operating Income (Loss)	\$ (15,470)	\$ (5,070)
Adjustments to reconcile operating income (loss) to net cash provided (used) by operating activities		
Depreciation	18,247	18,087
(Increase)Decrease in Prepaid Expenses	-	-
Increase(Decrease) in Payroll Tax Payable	-	-
	<u>2,777</u>	<u>13,018</u>
Net Cash Provided (Used) by Operating Activities	<u>\$ 2,777</u>	<u>\$ 13,018</u>

See Accountant's Audit Report & Notes Which Accompany These Financial Statements

LATIMER COUNTY RURAL WATER DISTRICT #3
LATIMER COUNTY, OKLAHOMA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2018

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

As discussed further in Note 1.C, these financial statements are presented on a modified cash basis of accounting, which is a basis of accounting other than accounting principles generally accepted in the United States of America (GAAP) established by the Governmental Accounting Standards Board (GASB). These modified cash-basis financial statements generally meet the presentation and disclosure requirements applicable to GAAP, in substance, but are limited to the elements presented in the financial statements and the constraints of the measurement and recognition criteria of the modified cash basis of accounting.

A. Organization & Reporting Entity

Latimer County Rural Water District #3, Latimer County, Oklahoma, operates as a nonprofit corporation under Oklahoma Statutes, Title 82, Sections 1234.1 through 1234.26, as amended. The District was organized to acquire water and water rights and to build and acquire pipelines and other water distribution facilities, and to operate the same for the purpose of furnishing water to serve the needs of owners and occupants of land located within the District.

B. Basis of Presentation

The accounts of the District are organized on the basis of proprietary fund type, specifically an enterprise fund. The activities of this fund are accounted for with a separate set of self-balancing accounts that comprise the District's assets, liabilities, net position, revenues and expenses. Enterprise Funds account for activities (1) that are financed with debt that is secured solely by a pledge of the net revenues from fees and charges of the activity; or (2) that are required by laws or regulations that the activity's costs of providing services, including capital costs (such as depreciation or debt service), be recovered with fees and charges, rather than with taxes or similar revenues; or (3) that the pricing policies of the activity establish fees and charges designed to recover its costs, including capital costs (such as depreciation or debt service).

LATIMER COUNTY RURAL WATER DISTRICT #3
LATIMER COUNTY, OKLAHOMA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2018

C. Measurement Focus and Basis of Accounting

Measurement Focus

The District utilizes an economic resources measurement focus within the limitations of the modified cash basis of accounting. The accounting objectives of this measurement focus are the determination of operating income, changes in net position (or cost recovery), net financial position, and cash flows. All assets, deferred outflows, liabilities, and deferred inflows (whether current or noncurrent or financial or nonfinancial) associated with their activities are generally reported within the limitations of the modified cash basis of accounting.

Basis of Accounting

The financial statements are presented on a modified cash basis of accounting, which is a basis of accounting other than GAAP as established by GASB. This basis of accounting involves modifications to the cash basis of accounting to report in the statements of net position cash transactions or events that provide a benefit or result in an obligation that covers a period greater than the period in which the cash transaction or event occurred. Such reported balances include investments, and short-term and long-term liabilities arising from cash transactions or events. Revenues are recognized when received and expenses are recorded when paid and depreciation is not included as the District does not maintain capital asset ledgers and depreciation.

This modified cash basis of accounting differs from GAAP primarily because certain assets and their related revenues (such as accounts receivable and revenue billed or provided services not yet collected and other accrued revenue and receivables) and certain liabilities and their related expenses (such as accounts payable and expenses for goods or services received but not yet paid and other accrued expenses and liabilities) are not recorded in these financial statements. In addition, other economic assets, deferred outflows, liabilities, and deferred inflows that do not arise from a cash transaction or event are not reported, and the measurement of reported assets and liabilities does not involve adjustment to fair value.

LATIMER COUNTY RURAL WATER DISTRICT #3
LATIMER COUNTY, OKLAHOMA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2018

If the District utilized the basis of accounting recognized as generally accepted in the United States, the fund financial statements for proprietary fund types would use the accrual basis of accounting.

D. Financial Position

Cash & Cash Equivalents

For the purpose of financial reporting, "cash & cash equivalents" includes all demand and savings accounts and certificates of deposit or short-term investments with an original maturity of three months or less.

Inventories

Supplies inventory is not recorded in the financial statements as the value of supplies at December 31, 2018 is not material to the financial statements.

Capital Assets

Property and equipment, consisting of a water distribution system, are stated at cost and are depreciated over the estimated useful life of such assets. Useful lives are range from 7-40 years. Depreciation is computed using the straight-line method.

Capitalization Policy - Purchases of capital items in excess of \$1,000.00 that increase the capacity or operation efficiency or extend the useful life of any asset are capitalized. Repairs and maintenance are expensed as incurred.

Long-Term Debt

Long-term debt is reported at face value, net of applicable discounts and deferred loss on refunding. Costs related to the issuance of debt are deferred and amortized over the lives of various debt issues.

Equity Classification

Equity is classified as net position and displayed in three components:

LATIMER COUNTY RURAL WATER DISTRICT #3
LATIMER COUNTY, OKLAHOMA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2018

1. Net investment in capital assets – Consists of capital assets including restricted capital assets, net of accumulated depreciation and reduced by the outstanding balances of any bonds, mortgages, notes, or other borrowings that are attributable to the acquisition, construction, or improvements of those assets and adjusted for any deferred inflows and outflows of resources attributable to capital assets and related debt.
2. Restricted – Consists of restricted assets reduced by liabilities and deferred inflows or resources related to those assets, with restriction constraints placed on the use either by (a) external groups such as creditors, grantors, contributors, or laws and regulations of other governments; or (b) law through constitutional provisions or enabling legislation.
3. Unrestricted - 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.

It is the District's policy to first use restricted net resources prior to the use of unrestricted net resources when an expense is incurred for purposes for which both restricted and unrestricted net resources are available.

E. Revenues, expenditures & expenses

Operating revenues and expenses for proprietary funds result from providing services and producing and delivering goods and/or services. They also include all revenues and expenses not related to capital and related financing, noncapital financing, or investing activities.

F. Income Tax Status

The District is exempt from income taxes under Section 501(c)(6) of the Internal Revenue Code.

G. Enterprise Fund

The Enterprise Fund is used to account for the operations of the District that are financed and operated in a manner similar to private business enterprises where the intent is that costs of

LATIMER COUNTY RURAL WATER DISTRICT #3
LATIMER COUNTY, OKLAHOMA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2018

providing goods or services be recovered in whole or part through user fees or charges.

H. Estimates

The preparation of financial statements in conformity with the modified cash basis of accounting used by the District requires management to make estimates and assumptions that affect certain reported amounts and disclosures (such as estimated useful lives in determining depreciation expense); accordingly, actual results could differ from those estimates.

I. Memorandum Only

The "Memorandum Only" captions above the total columns mean that totals are presented for overview information purposes only.

NOTE 2 - STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY

As a local government unit, the District is subject to various federal, state, and local laws and contractual regulations.

Finance-related Legal & Contractual Provisions

The reserve requirement for the USDA Note Payable is \$7,812.00, which the District has set aside in a restricted account.

Deficit Fund Balance or Retained Earnings

As indicated in the financial statements, there are no fund balance or retained earnings deficits for the District for this fiscal year.

NOTE 3 - CASH AND INVESTMENTS

Custodial Credit Risk

At December 31, 2018, the District held deposits of approximately \$84,454 at financial institutions. The District's cash deposits, including interest-bearing certificates of deposit are covered by Federal Depository Insurance (FDIC) or direct obligation of the U.S. Government insured or collateralized with securities held by the District or by its agent in the District's name.

LATIMER COUNTY RURAL WATER DISTRICT #3
LATIMER COUNTY, OKLAHOMA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2018

Investment Interest Rate Risk

The District does not have a formal investment policy that limits investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates.

Investment Credit Risk

The District has no policy that limits its investment choices other than the limitation of state law as follows:

- a. Direct obligations of the U.S. Government, its agencies and instrumentalities to which the full faith and credit of the U.S. Government is pledged, or obligations to the payment of which the full faith and credit of the State is pledged.
- b. Certificates of deposits or savings accounts that are either insured or secured with acceptable collateral with in-state financial institutions, and fully insured certificates of deposit or savings accounts in out-of-state financial institutions.
- c. With certain limitation, negotiable certificates of deposit, prime bankers' acceptances, prime commercial paper and repurchase agreements with certain limitations.
- d. County, municipal or school district tax supported debt obligations, bond or revenue anticipation notes, money judgments, or bond or revenue anticipation notes of public trusts whose beneficiary is a county, municipality or school district.
- e. Notes or bonds secured by mortgage or trust deed insured by the Federal Housing Administrator and debentures issued by the Federal Housing Administrator, and in obligations of the National Mortgage Association.
- f. Money market funds regulated by the SEC and in which investments consist of the investments mentioned in the previous paragraphs (a.-d.).

NOTE 4 - RESTRICTED ASSETS

The loan agreement with the United States Department of Agriculture Rural Development (USDA) requires the District to set aside into a Reserve Account an accumulated amount equal to the sum of the annual installment (\$7,812), after which deposits may be suspended, except to replace withdrawals. The District cannot withdraw funds from the reserve account without USDA approval. As of December 31, 2018, the District was required to have at least \$7,812.00 set aside in the reserve account; as of that date the account balance for the reserve

LATIMER COUNTY RURAL WATER DISTRICT #3
LATIMER COUNTY, OKLAHOMA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2018

account was \$8,827.81, which complies with the covenants of the loan agreement.

NOTE 5 - CAPITAL ASSETS

Capital asset activity, resulting from the modified cash basis transactions, for the fiscal year ended December 31, 2018, was as follows:

	Balance at Dec. 31, 2017	Additions	Deductions	Balance at Dec. 31, 2018
Water Line & Pump Station	\$ 635,463	\$ 4,784	\$ -	\$ 640,247
New Pumps	21,104	-	-	21,104
Subtotal	656,567	4,784	-	661,351
Less: Accum. Depr.	(375,480)	(18,247)	-	(393,727)
Total Capital Assets (Net of Depreciation)	<u>\$ 281,087</u>	<u>\$ (13,463)</u>	<u>\$ -</u>	<u>\$ 267,624</u>

NOTE 6 - LONG-TERM DEBT

The District has a note payable with to the United States Department of Agriculture Rural Development (USDA), payable in 480 monthly installments of \$651.00 until maturity, including interest at 5.00%. The note was dated August 10, 1990 in the original amount of \$132,500.00. The note is secured by all facilities of the District.

Changes in Long-Term Debt

The following is a summary of changes in long-term debt for the year ended December 31, 2018:

	Balance at Dec. 31, 2017	Additions	Deductions	Balance at Dec. 31, 2018
Notes Payable - USDA RD	\$ 58,102.36	\$ -	\$ 5,820.53	\$ 52,281.83
Total Long-Term Debt	<u>\$ 58,102.36</u>	<u>\$ -</u>	<u>\$ 5,820.53</u>	<u>\$ 52,281.83</u>

Debt Services Requirements to Maturity

The annual debt service requirements to maturity, including principal and interest, for long-term debt, as of December 31, 2018, are as follows:

LATIMER COUNTY RURAL WATER DISTRICT #3
LATIMER COUNTY, OKLAHOMA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2018

Year Ended December 31,	Principal	Interest	Total
2019	\$ 5,235	\$ 2,577	\$ 7,812
2020	5,503	2,309	7,812
2021	5,784	2,028	7,812
2022	6,080	1,732	7,812
2023	6,391	1,421	7,812
2024-2027	23,289	2,286	25,575
Total	<u>\$ 52,282</u>	<u>\$ 12,353</u>	<u>\$ 64,635</u>

NOTE 7 - FUND EQUITY

As described in Note 1 above, equity is classified as net position and displayed in three components:

1. Net investment in capital assets
2. Restricted
3. Unrestricted

The restricted amount includes assets restricted for the repayment of refundable water deposits and those related to Note 4 above.

NOTE 8 - CONTINGENCIES

Litigation

The District currently has no pending litigation.

Federally Assisted Programs

In the normal course of operations, the District participates in various federal or state/loan programs from year to year. The grant/loan programs are often subject to additional audits by agents of the granting or loaning agency, the purpose of which is to ensure compliance with the specific conditions of the grant or loan. Any liability of reimbursement that may arise as a result of these audits cannot be reasonably determined at this time, although it is believed the amount, if any, would not be material.

NOTE 9 - RETIREMENT AND DEFERRED COMPENSATION PLAN

The District has no retirement or deferred compensation plan for employees.

LATIMER COUNTY RURAL WATER DISTRICT #3
LATIMER COUNTY, OKLAHOMA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2018

NOTE 10 - SUBSEQUENT EVENTS

The District did not have any subsequent events through December 16, 2019, which is the date the financial statements were issued, for events requiring recording or disclosure in the financial statements for the year ending December 31, 2018.

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

To the Board of Directors
Latimer County Rural Water District #3
Latimer County, Oklahoma

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, and in accordance with Oklahoma Statutes, the modified cash basis financial statements of the Latimer County Rural Water District #3, as of and for the year ended December 31, 2018, and the related notes to the financial statements, which were prepared on the modified cash basis of accounting, which is a comprehensive basis of accounting other than generally accepted accounting principles, and have issued our report thereon dated December 16, 2019.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Latimer County Rural Water District #3's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Latimer County Rural Water District #3's internal control. Accordingly, we do not express an opinion on the effectiveness of Latimer County Rural Water District #3's internal control.

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

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. Given these limitations,

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during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. We did identify certain deficiencies in internal control described in the accompanying Schedule of Findings as Item 18-01 that we consider to be significant deficiencies.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Latimer County Rural Water District #3's financial statements are free of material misstatement, we performed tests of 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 one instance of noncompliance that is required to be reported under *Government Auditing Standards*, which is included in the Schedule of Findings as Item 18-02. The results of our tests disclosed no instances of other matters that are required to be reported under *Government Auditing Standards*.

Latimer County Rural Water District #3's Response to Findings

Latimer County Rural Water District #3's response to the findings identified in our audit is described in the accompanying Schedule of Findings. Latimer County Rural Water District #3's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the 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.

Kershaw CPA & Associates, P.C.

Kershaw CPA & Associates, PC
Muskogee, Oklahoma

December 16, 2019

LATIMER COUNTY RURAL WATER DISTRICT #3
LATIMER COUNTY, OKLAHOMA
SCHEDULE OF FINDINGS
DECEMBER 31, 2018

SIGNIFICANT DEFICIENCIES OF INTERNAL CONTROL:

Item 18-01: Segregation of Duties

Criteria: A good system of internal control requires a proper segregation of duties to prevent one person from being in a position to authorize, execute, and record the same transaction.

Condition: Due to the size of the District's major areas of internal control, that would be prevalent in a larger District, such segregation of duties is not available for this size operation. Duties are concentrated in the hands of a few individuals, who are responsible for all phases of the accounting functions. Because of this lack of division of responsibility, internal control is determined to be weak, and in some instances, non-existent.

Cause/Effect: Due to the limited number of personnel, a breach of internal controls could occur and not be detected in the normal course of operations.

Recommendation: The Board should continue to be actively involved in the operations of the organization.

Response: The Board continues to be actively involved in the operations of the District.

SIGNIFICANT DEFICIENCIES OF COMPLIANCE:

Item 18-02: Payroll Reporting and Compliance

Criteria: The District is required to withhold one half social security tax and applicable federal and state income tax from gross wages and timely remit such funds to the United States Treasury, the Oklahoma Tax Commission and the OESC. Reporting payroll activity on IRS forms 941, Oklahoma forms OW-8, OES-3 is required at various periods during the year, monthly, quarterly or annually.

Condition: Payroll taxes for the current year were not paid in a timely manner and were still past due at fiscal yearend.

LATIMER COUNTY RURAL WATER DISTRICT #3
LATIMER COUNTY, OKLAHOMA
SCHEDULE OF FINDINGS
DECEMBER 31, 2018

Cause/Effect: The past due taxes have left the District subject to additional tax liability, penalties, and interest charges by the taxing agencies.

Recommendation: The District needs to get in compliance with the federal and state payroll tax requirements.

Response: The District was made aware of the missed payment and will correct the problem.