

Rural Water and Sewer District No. 20
Pittsburg County, Oklahoma

Financial Statements and Independent Auditor's Reports

As of and for the Year Ended December 31, 2020



2020

**RURAL WATER AND SEWER DISTRICT NO 20
PITTSBURG COUNTY, OKLAHOMA**

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Board of Directors

Daryl Nieto	Chairman
Austin Tunnel	Vice Chairman
Joe Carrick	Secretary/Treasurer
Caleb Conner	Director
Bert Scott	Director

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INDEPENDENT AUDITOR'S REPORT

To the Members of the Board
Rural Water and Sewer District No. 20
Pittsburg County, Oklahoma

Report on the Financial Statements

We have audited the accompanying financial statements of the Rural Water and Sewer District No. 20, Pittsburg County, Oklahoma ("District"), as of December 31, 2020 and for the year then ended, and the related notes to the financial statements, which collectively comprise the District's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America. Management is also responsible for the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to error or fraud.

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. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

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

Basis for Qualified Opinion on Utility System Valuation and Related Note Payable to Developer

As discussed in footnote 3, the District was created to serve a startup planned community and was entirely financed by the developer who also served as the Chairman of the Board of Trustees until May, 2013 and continued to serve as operational manager for the District for the majority of 2019. The utility system was purchased from the developer at a price determined by the developer by the issuance of a note to

the developer. The District has not had sufficient operating income to amortize the note. As is often inherent with related party transactions, it may not be possible to determine whether a particular transaction would have taken place if the parties had not been related, or what the terms and conditions would have been. In addition, as discussed in footnote 2B, the District is in the process of building a new waste water treatment plant which is expected to replace a significant portion of the sewer system assets. No impairment for these assets has been recorded in the financial statements. Consequently, we were unable to obtain sufficient audit evidence related to the capital assets and note payable; the effect on the financial statements has not been determined.

Qualified Opinion

In our opinion, except for the matters discussed in the “Basis for Qualified Opinion on Utility System Valuation and Related Note Payable to Developer” paragraph, the financial statements referred to above present fairly, in all material respects the financial position of the Rural Water and Sewer District No. 20, Pittsburg County, Oklahoma as of December 31, 2020, and the changes in financial position thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

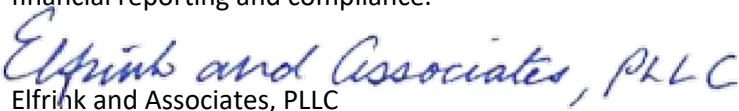
Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management’s discussion and analysis on pages 4-7 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management’s responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated January 24, 2022, on our consideration of the District’s internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the District’s internal control over financial reporting and compliance.


Elfrink and Associates, PLLC

Tulsa, Oklahoma
January 24, 2022

MANAGEMENT'S DISCUSSION AND ANALYSIS

The management of the Rural Water and Sewer District No. 20, Pittsburg County, Oklahoma ("District") is pleased to provide this annual financial report to demonstrate its accountability and communicate the District's financial condition and activities as of and for the year ended December 31, 2020. Management of the District is responsible for the fair presentation of this annual report, for maintaining appropriate controls over financial reporting, and for complying with applicable laws, regulations, and provisions of grants and contracts.

FINANCIAL HIGHLIGHTS

- The District's total net position decreased by \$116,578 and the liabilities of the District exceeded its assets at December 31, 2020 by \$28,461 (deficit net position). Of that, \$211,065 is invested in capital assets, net of related debt, leaving the District with a deficit unrestricted net position of \$239,526.
- The District showed an operating loss of \$52,276, as operating expenses outpaced increases in utility revenues and the District began amortization of an asset retirement obligation related to its sewer lagoons.
- During the year, the carrying value of utility systems and related equipment increased by \$108,870 which included continuation of construction of a new water treatment plant in the amount of \$38,397 and the purchase of a tract of land valued at \$100,000, partially offset by \$29,527 in depreciation.

ABOUT THE DISTRICT

The Rural Water and Sewer District No. 20, Pittsburg County was created August 15, 2012 under Title 82, Section 1324.1 of the laws of the State of Oklahoma.

The purpose of the District is to provide water, sewer, and trash services to the Town of Carlton Landing, a planned community in Pittsburg County, Oklahoma.

This annual report includes all activities for which District's Board of Directors is financially accountable.

FINANCIAL STATEMENTS

The District's activities are entirely business-type and are reported as an enterprise fund. Enterprise funds are proprietary funds used to report business-type services provided to the general public. Proprietary funds are reported using an economic resources measurement focus. For example, proprietary fund capital assets are capitalized and depreciated and principal payments on long-term debt are recorded as a reduction to the liability. The District reports under a full accrual basis of accounting, similar to a commercial enterprise.

The notes provide additional information that is essential to gain an understanding of the data provided in the financial statements and can be found on pages 11-17 of this report.

Condensed Statement of Net Position - December 31

	<u>2020</u>	<u>2019*</u>	<u>Variance</u>	<u>Var%</u>
Assets:				
Current and other assets	\$ 197,712	\$ 132,474	\$ 65,238	49%
Capital assets, net	<u>1,769,044</u>	<u>1,660,174</u>	<u>108,870</u>	7%
Total Assets	<u>1,966,756</u>	<u>1,792,648</u>	<u>174,108</u>	10%
Deferred outflows of resources:				
Related to ARO	<u>374,000</u>	<u>561,000</u>	<u>(187,000)</u>	-33%
Liabilities:				
Other liabilities	63,238	69,589	(6,351)	-9%
Asset retirement obligation	748,000	748,000	-	
Notes payable	<u>1,557,979</u>	<u>1,447,942</u>	<u>110,037</u>	8%
Total liabilities	<u>2,369,217</u>	<u>2,265,531</u>	<u>103,686</u>	5%
Net position:				
Net investment in capital assets	211,065	231,732	(20,667)	-9%
Unrestricted (deficit)	<u>(239,526)</u>	<u>(143,615)</u>	<u>(95,911)</u>	67%
Total net position	<u>\$ (28,461)</u>	<u>\$ 88,117</u>	<u>\$ (116,578)</u>	-132%

The District's net position reflects its investment in capital assets, less any related debt used to acquire those assets that is still outstanding and is offset by an unrestricted deficit net position of \$239,526. The deficit unrestricted net position was higher by \$95,911 from the prior year as the amortization of an asset retirement obligation for the closure of its sewer lagoons more than outpaced an increase in utility revenues. The \$748,000 estimated cost to reclaim the sewer lagoons, expected to occur in 2022, is being amortized over 4 years at \$187,000 per year.

For the year ended December 31, 2020, The District's net position decreased by \$116,578.

Change in Net Position - Year Ended December 31,

	<u>2020</u>	<u>2019</u>	<u>Variance</u>	<u>Var%</u>
Operating revenues:				
Charges for sales and services	\$ 492,549	\$ 290,043	\$ 202,506	70%
Tap fees	42,148	20,330	21,818	107%
Total operating revenues	<u>534,697</u>	<u>310,373</u>	<u>224,324</u>	72%
Operating expenses:				
Depreciation and amortization	216,527	216,409	118	0%
All other operating expenses	370,446	398,430	(27,984)	-7%
Total operating expenses	<u>586,973</u>	<u>614,839</u>	<u>(27,866)</u>	-5%
Operating loss	<u>(52,276)</u>	<u>(304,466)</u>	252,190	-83%
Nonoperating income (expense):				
ODEQ penalty	-	(31,800)	31,800	-100%
Interest expense	<u>(64,302)</u>	<u>(60,158)</u>	<u>(4,144)</u>	7%
Total nonoperating income (expense)	(64,302)	(91,958)	27,656	-30%
Change in net position	<u><u>(116,578)</u></u>	<u><u>(396,424)</u></u>	<u><u>279,846</u></u>	-71%

Operating loss for the year ended December 31, 2020 decreased by \$252,190 over the prior year which included a 70% increase in utility revenue due to higher residential property sales and occupancy rates in the planned community as well as 5% lower operating costs.

CAPITAL ASSETS

The District's investment in capital assets was \$1,769,044 net of accumulated depreciation, an increase of \$108,870 from the prior year. Significant capital asset activity during the year included:

- Additional engineering fees for the new water treatment plant in the amount of \$38,397.
- The purchase of land for the new water treatment plant in the amount of \$100,000.

ECONOMIC FACTORS AND OTHER POTENTIALLY SIGNIFICANT MATTERS

OVERVIEW

The District is dedicated to providing water, sewer and sanitation services for the Town of Carlton Landing, a developing planned community on Lake Eufaula. As the community expands, the District is challenged with providing services to the new residents. Inherent is the need for additional capital for infrastructure expansion and to address several issues with the existing system. On December 26, 2018, the District entered into a revolving construction loan agreement with Core Bank, secured by collateral pledged by the developer, The note was renewed on June 25, 2020 and is due July 15, 2021. As of December 31, 2020, \$422,815 of the available \$1,500,000 had been drawn against the note. In addition, a third amendment to the note payable to the developer was executed to include the purchase of a tract of land from the developer and rolling the unpaid interest accrual into the note principal. This is a summary of the note activity in the current year:

	Balance 12/31/2019	Additions	Deductions	Balance 12/31/2020
Note payable - related party	\$ 1,019,889	\$ 153,275	\$ 38,000	\$ 1,135,164
Note payable - Core Bank	408,553	14,262	-	422,815
	\$ 1,428,442	\$ 167,537	\$ 38,000	\$ 1,557,979

REQUESTS FOR INFORMATION

This financial report is designed to provide a general overview of the Rural Water and Sewer District No. 20, Pittsburg County, Oklahoma’s finances for all interested parties. Questions concerning any of the information provided in this report or requests for additional information should be addressed to:

Lisa Graddy
RW&SD #20, Pittsburg County
C/O OK Water, LLC
PO Box 9446
Oklahoma City, OK 94460
405-905-8070
lgrady@okwater.org

Statement of Net Position – December 31, 2020

ASSETS

Current assets:

Cash and cash equivalents	\$ 120,474
Cash and cash equivalents - reserve accounts	23,228
Cash restricted for debt service	3,969
Accounts receivable, net of allowance for uncollectible	48,541
Inventory - water meters	1,500
	197,712

Noncurrent assets:

Capital assets, net of accumulated depreciation	1,769,044
Total assets	1,966,756

DEFERRED OUTFLOWS OF RESOURCES

Deferred amount on asset retirement obligation	374,000
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LIABILITIES

Current Liabilities:

Accrued interest	811
Accrued interest - related party	42,927
Note payable - Core Bank	422,815
Note payable - related party - current portion	53,297
Total current liabilities	519,850

Noncurrent Liabilities:

Meter deposits payable	19,500
Note payable - related party	1,081,867
Asset retirement obligation - lagoon closure	748,000
Total Noncurrent Liabilities	1,849,367
Total liabilities	2,369,217

NET POSITION

Net investment in capital assets	211,065
Unrestricted (deficit)	(239,526)
Total net position	\$ (28,461)

See accompanying notes to the basic financial statements

Statement of Revenue, Expense and Change in Net Position – Year Ended December 31, 2020

Operating revenues:

Charges for sales and services:

Water	\$	274,618
Sewer		112,198
Sanitation		98,436
Tap Fees		42,148
Late fees		6,994
Miscellaneous		303
Total operating revenues		534,697

Operating expenses:

Costs of sales and services:

Water purchases		65,697
Sanitation contractor		50,440
Operations and maintenance		97,672
Management fees		150,000
Legal fees		6,637
Amortization (asset retirement)		187,000
Depreciation		29,527
Total operating expenses		586,973
Operating loss		(52,276)

Nonoperating expense:

Interest expense		(64,302)
Total nonoperating expense		(64,302)

Change in net position (116,578)

Net position - beginning (restated see footnote 1D) 88,117

Net position - ending \$ (28,461)

See accompanying notes to the basic financial statements

Statement of Cash Flows – Year Ended December 31, 2020

Cash flows from operating activities:

Receipts from members	\$ 523,208
Payments to suppliers	(385,261)
	137,947

Cash flows from capital and related financing activities:

Interest paid on capital debt - Core Bank	(73,838)
Proceeds from capital debt	129,537
Purchase of capital assets	(138,397)
	(82,698)

Net increase in cash and cash equivalents 55,249

Cash and equivalents - beginning of year 92,422

Cash and equivalents - end of year \$ 147,671

Reconciliation of operating income to net cash provided by operating activities:

Operating loss	\$ (52,276)
Depreciation and amortization	216,527
Increase in accounts receivable	(11,489)
Decrease in inventory	1,500
Decrease in accounts payable	(16,315)
	\$ 137,947

See accompanying notes to the basic financial statements

Notes to the Basic Financial Statements

1. Summary of Significant Accounting Policies

The Rural Water and Sewer District No. 20 complies with accounting principles generally accepted in the United States of America (GAAP) as applicable to government units. The Governmental Accounting Standards Board (GASB) is responsible for establishing GAAP for state and local governments through its pronouncements (Statements and Interpretations). The more significant accounting policies established in GAAP and used by the District are discussed below.

A. Financial Reporting Entity

The Rural Water and Sewer District No. 20, Pittsburg County, Oklahoma ("District") was incorporated on August 15, 2012 under Title 82, Section 1324.1 as amended, of the laws of the State of Oklahoma. The District is exempt from Federal and State income tax. The purpose of the District is to provide water and sewer services to the owners and occupants of property located within the District which primarily includes the Town of Carlton Landing, and others as authorized by law.

The District is governed by a board of five directors, elected by a majority vote of the homeowners present at the meeting in which the vote is taken. Elected positions include Chairman, Vice-Chairman, Secretary/Treasurer and two Directors.

B. Basis of Presentation

The accounting policies of Rural Water and Sewer District No. 20, Pittsburg County, Oklahoma conform to the basic principles of governmental accounting and financial reporting set forth by the Governmental Accounting Standards Board (GASB).

The District's fund is an enterprise fund. Enterprise funds are proprietary funds used to account for business-like activities provided to the general public. These activities are financed primarily by user charges and the measurement of financial activity focuses on net income measurement similar to the private sector.

C. Measurement Focus and Basis of Accounting

Measurement focus refers to how transactions are recorded within the various financial statements. Basis of accounting refers to when transactions are recorded regardless of the measurement focus applied.

The District's financial statements use the economic resources measurement. The District utilizes the basis of accounting generally accepted in the United States. Under this basis of

accounting, revenues are recognized when earned and expenses are recorded when the liability is incurred or economic asset is used.

D. Assets, Liabilities, Deferred Outflows, and Net Position

Cash and cash equivalents

For the purpose of the statement of cash flows, the District considers all cash on hand, demand deposit accounts, interest bearing checking accounts, and time deposit accounts including certificates of deposit with maturities of three months or less to be cash and cash equivalents.

Capital assets and depreciation

Depreciable assets are recorded at cost when purchased or constructed. Improvements are capitalized; the cost of normal maintenance and repairs that do not add to the value of the asset or materially extend the asset's life is not. Depreciation is calculated on a straight-line basis over the estimated useful lives of the depreciable assets.

Capital assets consist of utility infrastructure with an estimated useful life of 50 years. A capitalization threshold of \$2,000 is used to report capital assets.

Deferred Outflow of Resources

In addition to assets and liabilities, the statement of financial position reports a separate section for deferred outflows of resources. These represent a consumption of net position that applies to a future period which will not be recognized as an outflow of resources until that time. At June 30, 2020 the District reported a deferred outflow of resources related to its asset retirement obligation for the lagoon closure. The deferred outflow is being amortized over a four-year period, the expected remaining useful life, as the lagoons are expected to be closed in 2022.

Long-term Debt

All long term debt is reported as the liability is incurred. The long-term debt is presently comprised of a note payable to the developer and a note payable to a commercial developer, pledged by certain assets of the developer.

Net position

Net position is divided into three components:

- a. *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 attributed to the acquisition, construction, or improvement of those assets.

b. *Restricted net position* – Consists of net assets with constraints placed on the use by 1) external groups such as creditors, grantors, contributors, or laws and regulations of other governments, or 2) law through constitutional provisions or enabling legislation.

c. *Unrestricted net position*- All other net assets that do not meet the definition of “restricted” or “net investment in capital assets”.

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

The prior year net position was restated as follows:

Restatement of Beginning Net Position:

December 31, 2019 net position as previously reported	\$	(99,710)
Add:		
Correction of accrued interest payable - related party		<u>187,827</u>
January 1, 2019 net position as restated	\$	<u><u>88,117</u></u>

E. Revenues and expenses

Operating Revenues – Operating revenues include activities that have the characteristics of exchange transactions, such as service fees.

Nonoperating revenues – Nonoperating revenues include activities that have the characteristics of nonexchange transactions such as grants from other governments, gifts and contributions, and other revenue sources that are defined as nonoperating revenue.

Operating Expenses – Operating expenses are those that are essential for delivery of services to the District’s customers.

Nonoperating Expenses - Nonoperating expenses are those that relate to the financing of the District’s activity, such as interest expense, and non-recurring and/or unusual expenses such as penalties.

2. Detailed Notes on Transaction Classes/Accounts

A. Cash and investments

Deposits and investments - State statutes govern the District’s investment policy. Permissible investments include direct obligations of the United States Government and Agencies; certificates of deposit of savings and loan associations, and bank and trust companies. Collateral is required for demand deposits and certificates of deposit for all amounts not covered by federal deposit insurance. Investments are stated at cost plus accrued interest.

Custodial Credit Risk – Custodial credit risk is the risk that in the event of a bank failure, the District’s deposits may not be returned to it. The District does not have a written policy for

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ANNUAL FINANCIAL REPORT
As of and for the Year Ended December 31, 2020

custodial credit risk. At December 31, 2020, all of the District's cash was held in demand accounts bearing no interest and was fully covered by federal deposit insurance.

B. Capital Assets and Depreciation

For the year ended December 31, 2020, capital asset balances changed as follows:

	Balance 12/31/2019	Additions	Deletions	Balance 12/31/2020
Capital assets not being depreciated:				
Land	\$ 109,000	\$ 100,000	\$ -	\$ 209,000
Construction in progress (sewer)	245,913	38,397	-	284,310
Total capital assets not being depreciated	<u>354,913</u>	<u>138,397</u>	<u>-</u>	<u>493,310</u>
Capital assets being depreciated:				
Sewer system	888,761	-	-	888,761
Water system	587,578	-	-	587,578
Total capital assets being depreciated	<u>1,476,339</u>	<u>-</u>	<u>-</u>	<u>1,476,339</u>
Less accumulated depreciation:				
Sewer system	(109,831)	(17,775)		(127,606)
Water system	(61,247)	(11,752)		(72,999)
	<u>(171,078)</u>	<u>(29,527)</u>	<u>-</u>	<u>(200,605)</u>
Net capital assets	<u>\$ 1,660,174</u>	<u>\$ 108,870</u>	<u>\$ -</u>	<u>\$ 1,769,044</u>

The District is in the process of building a new waste water treatment plant, expected to become operational in 2022 at which time a significant portion of the current sewer assets will be phased out of operations. Management was unable to determine the remaining book value of the impaired assets related to this effort, but it could have a significant effect on the carrying value of the assets.

C. Long Term Debt

The following is a summary of long-term debt transactions of the District:

	Balance 12/31/2019	Additions	Deductions	Balance 12/31/2020	Amount Due in Next Year
Note payable - related party	\$ 1,019,889	\$ 153,275	\$ 38,000	\$ 1,135,164	\$ 53,297
Note payable - Core Bank	408,553	14,262	-	422,815	422,815
	<u>\$ 1,428,442</u>	<u>\$ 167,537</u>	<u>\$ 38,000</u>	<u>\$ 1,557,979</u>	<u>\$ 476,112</u>

Payment requirements to maturity:

Year ended December 31,	Core Bank Note		Humphreys 2009 Note	
	Principal	Interest	Principal	Interest
2021	\$ 422,815	\$ 21,141	\$ 53,297	\$ 38,501
2022			38,683	36,160
2023			40,159	34,684
2024			41,691	33,152
2025			43,282	31,561
2026-2030			242,473	131,740
2031-2035			292,393	81,821
2036-2040			383,186	22,676
Total	\$ 422,815	\$ 21,141	\$1,135,164	\$ 410,295

At December 31, 2020, the District's long term debt consisted of the following notes:

Note payable – related party

Note payable to Humphreys Partners 2009, LLC, dated September 10, 2013 in the original amount of \$1,361,000 and amended on August 15, 2015 to the amount of \$966,139 retroactively, with a fixed simple interest rate of 5.0%, and payable monthly in the amount equal to the excess of the District's monthly revenues less operating expenses, with payments beginning July 31, 2015.

On May 29, 2020, the District issued a second amended and restated promissory note that increased the principal amount to \$1,019,889 and changes the interest rate to be a floating one at 0.50% per annum in excess of the Wall Street Prime Rate and grants the developer a priority security interest in the assets of the District.

On April 14, 2020, the District issued a third amended and restated promissory note to include \$100,000 for the purchase of a tract of land from the developer.

In the event of default, all obligations become due and payable at the option of the developer.

The District began making payments toward the note principal in December 2020. \$1,135,164

The developer's note has been subordinated to the Core Bank Note shown below.

Core Bank Note Payable

On December 26, 2018 the District entered in a loan agreement with Core Bank in the amount of \$1,500,000 to construct a wastewater treatment plant, secured by collateral pledged by the developer. The District may make draws against the loan as needed. The related note provides for monthly interest-only payments at the Wall Street Prime Rate + 1%. On June 25, 2020, the due date for the entire balance of the note was extended to July 15, 2021. \$422,815

Total notes payable \$1,557,979

3. Related Party Transactions

The District was originally financed by and had significant transactions with the developer of the planned community it serves. In addition, the water and sewer system infrastructure that was constructed by the developer was sold to the District at an amount determined by the developer. The District was managed by a company owned by the developer until December 2019 at which time management was assumed by OK Water, LLC, an entity that is independent of the developer.

4. Asset Retirement Obligation

The District has incurred certain asset retirement obligations related to the operation of its wastewater utility system. The estimated liability of the legally required closure costs for the wastewater utility system is \$748,000 as of December 31, 2020. This cost estimate is for reclamation of the three sewer lagoons as required by regulations promulgated by the Oklahoma Department of Environmental Quality. The District is currently constructing a wastewater treatment plant. Upon completion, the lagoons will no longer be used. The reclamation process is expected to take place in 2022. Consequently, the cost is being amortized over 4 years, with \$187,000 expensed in the year ended December 31, 2020.

5. Management Agreement

On October 1, 2019, the District entered into an agreement with OK Water, LLC of Oklahoma City, Oklahoma to operate and maintain its water and sewer systems. The agreement expires October 31, 2022. On December 1, 2019, the District also entered into an agreement with OK Water, LLC to provide accounting and administrative services. This agreement expires on November 30, 2022. During the year ended December 31, 2020, the District paid \$150,000 related to these agreements. The District does not have employees.

6. Risk Management

The District is exposed to various risks of loss related to torts, errors, and omissions. To help mitigate this risk, the District carries the following insurance coverage:

<u>Coverage</u>	<u>Each Loss/Annual Aggregate</u>
Property (\$1,000 deductible)	\$25,000/\$1,000,000
Comprehensive General Liability	\$25,000/\$1,000,000
Errors and Omissions/Directors and Officers Liability	\$125,000/\$1,000,000
Employee Dishonesty and Crime	\$10,000

7. Commitments and Contingencies

The District is not involved in any legal proceedings, which normally occur in the course of operations, at this time. While legal proceedings cannot be foreseen, the District believes that any settlement or judgment would not have a material effect on the financial condition of the District.

ODEQ Consent Order Case No. 21-019

On March 21, 2019, the District entered into a consent order with the Oklahoma Department of Environmental Quality (“ODEQ”) regarding unpermitted discharges and operation and maintenance violations from the wastewater treatment system. The consent order called for a new wastewater treatment system to be constructed beginning February 2020 with an objective of three months compliance with the OPDES permit by June 2021.

On March 29, 2021, the District informed the ODEQ that it would not be able to meet the specified deadlines of the consent order due to global supply chain delays for construction materials. Consequently, on July 7, 2021, a revised consent order was entered into with a modification of the task deadlines to begin construction by October 2021 and attain six consecutive months of compliance with the OPDES Permit by September 2022. Failure to meet the specified task deadlines in the consent order could result in penalties not to exceed \$70,000.

8. Subsequent Events

Core Bank Loan Renewal

On June 30, 2021, the District executed an agreement to renew the Core Bank Note Payable for another year under the same terms and expanded the total available credit from \$1,500,000 to \$3,200,000 due to increased estimated costs to complete the wastewater treatment plant. The District is required to make interest payments beginning October 2021 with the entire principal balance is due July 1, 2022.

Management has evaluated events and transactions that occurred after the balance sheet date for potential recognition and disclosure through the date on which the financial statements were available to be issued and has determined that no additional disclosures are required.

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

To the Members of the Board
Rural Water and Sewer District No. 20
Pittsburg 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, the financial statements of the Rural Water and Sewer District No. 20, Pittsburg County, Oklahoma ("District"), as of December 31, 2020 and for the year then ended, and the related notes to the financial statements, which collectively comprise the District's basic financial statements and have issued our report thereon dated January 24, 2022. We qualified our opinion due to inability to certify the value of the fixed assets or the substance of the associated debt resulting from transactions initiated and executed by a related party at the formation stages of the District.

Internal Control Over Financial Reporting

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

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or 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 District's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations,

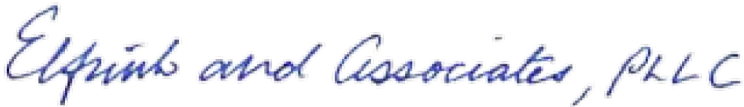
and contracts, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed an instance of noncompliance or other matters that are required to be reported under *Government Auditing Standards* described in the accompanying schedule of findings and management responses as 2020-01.

The District's Responses to Finding

The District's response to the finding identified in our audit is described in the accompanying schedule of finding and management response. The District's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

Purpose of This Report

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



Elfrink and Associates, PLLC

Tulsa, Oklahoma
January 24, 2022

SCHEDULE OF FINDING AND MANAGEMENT RESPONSE

This schedule is presented as an addendum to accompany the *“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”*. Consideration of items listed should be made in conjunction with that report.

2020-01 – Member (Customer) Files

CONDITION: A review of 24 customer files at the time of fieldwork in the prior year indicated 6 still did not have applications or security deposits on file. **UPDATE:** Management reports that approximately 100 of the 280 current active customers did not have applications for service or security deposits on file.

POTENTIAL EFFECT OF CONDITION: The terms and entitlement for service could be ambiguous and/or not consistently applied. The District may not be able to enforce collection of amounts due. The District may not be complying with the requirements of membership designated by its chosen organizational form under Title 82 of the Oklahoma Statutes.

CAUSE OF CONDITION: The District did not have policies and procedures in place to require that a member file, application and agreement for service be maintained in 2020. The District was not issuing benefit unit certificates at the time of establishment of service.

CRITERIA: Title 82 Chapter 18 Section 1324.12 of the Oklahoma Statutes requires each landowner within the district to subscribe to a number of such units in proportion to the extent s/he desires to participate in the benefits of the improvements. Good business practice dictates that an agreement for services be executed that outlines the terms of those services prior to the services being provided.

RECOMMENDATION: The District should continue its effort to obtain applications and agreements and issue benefit units from/for all landowners.

MANAGEMENT’S RESPONSE: We are now obtaining Member Applications during the property closing process when title to a property changes ownership. Applications are included with the property closing documents and the application fee is collected with the closing fees. All property owners now have Benefit Unit Certificates. We are working to close the gap on the signed service agreements and deposits by the end of 2021.