

LAKE MADISON SANITARY DISTRICT
AUDITED FINANCIAL STATEMENTS
FOR THE YEARS ENDED
DECEMBER 31, 2012 AND 2011

LAKE MADISON SANITARY DISTRICT
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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

Governing Board
Lake Madison Sanitary District
Lake County, South Dakota

We have audited, in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, the financial statements of the business-type activities of Lake Madison Sanitary District, Lake County, South Dakota, as of December 31, 2012 and 2011, and for each of the years 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 29, 2015.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered Lake Madison Sanitary 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 opinion 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.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. However, as described in the accompanying Schedule of Current Audit Findings, we identified certain deficiencies in internal control that we consider to be material weaknesses.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. *A material weakness* is a deficiency, or combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the District's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiency described in the accompanying Schedule of Current Audit Findings as item 2012-1 to be a material weakness.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Lake Madison Sanitary 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 no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

District's Response to Findings

Lake Madison Sanitary District's response to the finding identified in our audit is described in the accompanying Schedule of Current Audit Findings. 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 entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose. As required by South Dakota Codified Law 4-11-11, this report is a matter of public record and its distribution is not limited.

KMWF + Associates, PC

Dell Rapids, South Dakota
January 29, 2015

LAKE MADISON SANITARY DISTRICT
SCHEDULE OF PRIOR AND CURRENT AUDIT FINDINGS
DECEMBER 31, 2012

SCHEDULE OF PRIOR AUDIT FINDINGS

Prior Audit Findings:

Finding No. 2011-1:

A reportable condition in controls existed due to a lack of segregation of duties. This finding has not been corrected and is restated as current audit finding number 2012-1.

SCHEDULE OF CURRENT AUDIT FINDINGS

Current Audit Findings:

Internal Control Related Findings – Material Weaknesses:

Finding No. 2012-1:

Criteria: Internal controls should be in place that provide reasonable assurance that management directives are carried out in regards to the recording and processing of financial data.

Condition: A reportable condition in controls existed due to a lack of segregation of duties. This is the ninth consecutive audit report in which this finding has appeared.

Effect: Employees perform related functions which creates the potential for errors occurring and not being detected during the course of employees performing their assigned functions.

Recommendation: Implementation of compensating controls.

Management response: The District agrees with the finding and is aware of the weakness. Because of the small size of the office staff complete segregation of duties is impossible. Management intends to maintain a constant awareness of the weakness and implement compensating controls where appropriate.



INDEPENDENT AUDITOR'S REPORT

Governing Board
Lake Madison Sanitary District
Lake County, South Dakota

Report on the Financial Statements

We have audited the accompanying financial statements of the business-type activities of Lake Madison Sanitary District, Lake County, South Dakota (District), as of December 31, 2012 and 2011 and for each of the years 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

The District's 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 controls relevant to the preparation and fair presentation of financial statements that are free from material misstatements, 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. 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 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.

Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the business-type activities of Lake Madison Sanitary District as of December 31, 2012 and 2011, and the respective changes in financial position and, where applicable, cash flows thereof for each of the years 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 (MD&A) on pages 6 through 9 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 29, 2015 on our consideration of the District's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with Government Auditing Standards in considering the District's internal control over financial reporting and compliance.

KMWF + Associates, PC

Dell Rapids, South Dakota
January 29, 2015

MANAGEMENT'S DISCUSSION AND ANALYSIS

This discussion and analysis of the Lake Madison Sanitary District's financial performance provides an overview of the District's financial activities for the year ended December 31, 2012. Please read it in conjunction with the District's financial statements and notes to the financial statements to enhance your understanding of the District's financial performance.

FINANCIAL HIGHLIGHTS

- Private and commercial entities serviced by the District were 798 in 2009, 806 in 2010, 809 in 2011, and 809 in 2012, generally showing increases of 1-1.5% per year. On January 1, 2012 the monthly user fee was increased from \$30.00 to \$36.00, after many years without a change.
- Operating revenues totaled \$376,533 in 2012, an increase of \$39,519 over the previous year. This compares to a \$19,121 increase from 2010 to 2011. In 2012 sewer charges (user fees) accounted for \$355,444 of the total revenue and connection fees accounted for \$19,900. Revenue from sewer charges increased by 15% from the previous year, mainly due to the increase in monthly fees. However, new construction continues, as illustrated by the hookup fees, showing continued growth around Lake Madison and the need for expansion of sewer services.
- The growth trend the District has experienced since its inception has led to previous expansions of the System collection and treatment capacity. The goal of the Board and District staff is to continue the upgrading and maintenance of the mechanical and underground transportation infrastructure of the System, to maximize the capability to handle expected growth. As our System ages we have also been investing in improvements and maintenance of the pumping and communication systems. This will allow the District to meet their overall purpose, which is protection of the water quality in Lake Madison and the surrounding area.

OVERVIEW OF THE FINANCIAL STATEMENTS

This annual report consists of a series of financial statements: Statement of Net Position; Statement of Revenues, Expenses, and Changes in Net Position; and Statement of Cash Flows. These statements are presented using the economic resources measurement focus and the accrual basis of accounting. One of the most important questions to be asked about the District's finances is "Is the District as a whole better off or worse off as a result of the year's activities?"

These statements report information about the District as a whole and about its activities to help answer this question. They report the District's net position and changes in them. Over time increases or decreases in the net position of the District are one indicator of whether the financial health is improving or deteriorating. The other nonfinancial factors to consider are the commitment of the District to continue to meet the needs of its users, both short and long term, balancing environmental and health protection with the ongoing development of Lake Madison and the surrounding area.

FINANCIAL ANALYSIS OF THE DISTRICT

The following table summarizes the financial position of the District as of December 31:

Condensed Statement of Net Position

	2012	2011	Dollar Change
Current and other assets	\$ 413,867	\$ 365,021	\$ 48,846
Capital assets, net	987,178	1,050,121	(62,943)
Total assets	<u>\$ 1,401,045</u>	<u>\$ 1,415,142</u>	<u>\$ (14,097)</u>
Current liabilities	\$ 68,488	\$ 64,757	\$ 3,731
Long-term liabilities	396,753	423,507	(26,754)
Total liabilities	<u>465,241</u>	<u>488,264</u>	<u>(23,023)</u>
Net position:			
Net investment in capital assets	569,563	604,957	(35,394)
Restricted for:			
Insurance cumulative reserve	7,777	2,484	5,293
Debt service	-	-	-
Unrestricted net position	<u>358,464</u>	<u>319,437</u>	<u>39,027</u>
Total net position	<u>935,804</u>	<u>926,878</u>	<u>8,926</u>
Total net position and liabilities	<u>\$ 1,401,045</u>	<u>\$ 1,415,142</u>	<u>\$ (14,097)</u>
	2011	2010	Dollar Change
Current and other assets	\$ 365,021	\$ 405,581	\$ (40,560)
Capital assets, net	1,050,121	1,094,221	(44,100)
Total assets	<u>\$ 1,415,142</u>	<u>\$ 1,499,802</u>	<u>\$ (84,660)</u>
Current liabilities	\$ 64,757	\$ 68,887	\$ (4,130)
Long-term liabilities	423,507	453,164	(29,657)
Total liabilities	<u>488,264</u>	<u>522,051</u>	<u>(33,787)</u>
Net position:			
Net investment in capital assets	604,957	622,453	(17,496)
Restricted for:			
Insurance cumulative reserve	2,484	4,707	(2,223)
Debt service	-	-	-
Unrestricted net position	<u>319,437</u>	<u>350,591</u>	<u>(31,154)</u>
Total net position	<u>926,878</u>	<u>977,751</u>	<u>(50,873)</u>
Total net position and liabilities	<u>\$ 1,415,142</u>	<u>\$ 1,499,802</u>	<u>\$ (84,660)</u>

The following table summarizes the changes in financial position of the District for the years ended December 31, 2012 and 2011:

Condensed Statement of Revenues,
Expenses, and Changes in Net Position

	2012	2011	Dollar Change
Operating revenues	\$ 376,533	\$ 337,014	\$ 39,519
Other revenues	2,112	3,016	(904)
Total revenues	<u>378,645</u>	<u>340,030</u>	<u>38,615</u>
Operating expenses	354,497	374,738	(20,241)
Interest expense	15,222	16,165	(943)
Total expenses	<u>369,719</u>	<u>390,903</u>	<u>(21,184)</u>
Excess (Deficiency) before contributions and transfers	<u>8,926</u>	<u>(50,873)</u>	<u>59,799</u>
Change in net position	<u>8,926</u>	<u>(50,873)</u>	<u>59,799</u>
Net position - beginning	<u>926,878</u>	<u>977,751</u>	
Net position - ending	<u>\$ 935,804</u>	<u>\$ 926,878</u>	

	2011	2010	Dollar Change
Operating revenues	\$ 337,014	\$ 317,893	\$ 19,121
Other revenues	3,016	10,807	(7,791)
Total revenues	<u>340,030</u>	<u>328,700</u>	<u>11,330</u>
Operating expenses	374,738	371,343	3,395
Interest expense	16,165	21,485	(5,320)
Total expenses	<u>390,903</u>	<u>392,828</u>	<u>(1,925)</u>
Excess (Deficiency) before contributions and transfers	<u>(50,873)</u>	<u>(64,128)</u>	<u>13,255</u>
Change in net position	<u>(50,873)</u>	<u>(64,128)</u>	<u>13,255</u>
Net position - beginning	<u>977,751</u>	<u>1,041,879</u>	
Net position - ending	<u>\$ 926,878</u>	<u>\$ 977,751</u>	

CAPITAL ASSET ADMINISTRATION

By the end of 2012, the District had invested \$4,484,007 in a broad range of capital assets, including, land, buildings, various machinery and equipment.

	Business-type Activities		Total \$ Change	Total % Change
	2012	2011	11 to 12	11 to 12
Land	\$ 24,224	\$ 24,224	\$ -	0%
Buildings	151,365	151,365	-	0%
Machinery and Equipment	4,308,418	4,285,521	22,897	0.5%
Total Capital Assets	<u>\$ 4,484,007</u>	<u>\$ 4,461,110</u>	<u>\$ 22,897</u>	<u>0.5%</u>

	2011	2010	10 to 11	10 to 11
	Land	\$ 24,224	\$ 24,224	\$ -
Buildings	151,365	151,365	-	0.0%
Machinery and Equipment	4,285,521	4,243,921	41,600	1.0%
Total Capital Assets	<u>\$ 4,461,110</u>	<u>\$ 4,419,510</u>	<u>\$ 41,600</u>	<u>0.9%</u>

LONG-TERM DEBT

At year-end, the District had \$417,616 in SRF loan obligations.

Outstanding Debt and Obligations

	Business-type Activities		Total Dollar Change
	2012	2011	2011-2012
State Revolving Fund Loan	<u>\$ 417,616</u>	<u>\$ 445,164</u>	<u>\$ (27,548)</u>
Total Outstanding Debt and Obligations	<u>\$ 417,616</u>	<u>\$ 445,164</u>	<u>\$ (27,548)</u>

	2011	2010	2010-2011
	State Revolving Fund Loan	<u>\$ 445,164</u>	<u>\$ 471,768</u>
Total Outstanding Debt and Obligations	<u>\$ 445,164</u>	<u>\$ 471,768</u>	<u>\$ (26,604)</u>

During 2012, the District made principal payments of \$27,548. Repayment will be made over twenty years.

CONTACTING THE DISTRICT'S FINANCIAL MANAGEMENT

This financial report is designed to provide a general overview of the District's finances for all those with an interest. Questions concerning any of the information provided in this report or requests for additional information about Lake Madison Sanitary District should be directed to the District Office at PO Box 123, Madison, SD 57042.

LAKE MADISON SANITARY DISTRICT
STATEMENTS OF NET POSITION
DECEMBER 31, 2012 AND 2011

	Enterprise Fund	
	2012	2011
ASSETS		
Current Assets		
Cash and cash equivalents	\$ 106,269	\$ 64,395
Certificates of deposit	243,615	242,452
Accounts receivable	25,836	25,211
Inventory	25,488	25,488
Prepaid insurance	4,882	4,991
Total Current Assets	<u>406,090</u>	<u>362,537</u>
Noncurrent Assets		
Restricted Assets:		
Deposits	7,777	2,484
Capital Assets:		
Land	24,224	24,224
Buildings and equipment	4,459,783	4,436,886
Less: accumulated depreciation	<u>(3,496,829)</u>	<u>(3,410,989)</u>
Total Noncurrent Assets	<u>994,955</u>	<u>1,052,605</u>
TOTAL ASSETS	<u><u>\$ 1,401,045</u></u>	<u><u>\$ 1,415,142</u></u>
LIABILITIES		
Current Liabilities		
Accounts payable	\$ 898	\$ 807
Customer deposits	39,065	36,402
Current portion of long-term debt	<u>28,525</u>	<u>27,548</u>
Total Current Liabilities	<u>68,488</u>	<u>64,757</u>
Noncurrent Liabilities		
Accrued leave payable	7,662	5,891
Notes payable	417,616	445,164
Current portion of long-term debt	<u>(28,525)</u>	<u>(27,548)</u>
Total Noncurrent Liabilities	<u>396,753</u>	<u>423,507</u>
Total Liabilities	<u>465,241</u>	<u>488,264</u>
NET POSITION		
Net Investment in Capital Assets	569,563	604,957
Restricted for:		
Insurance cumulative reserve	7,777	2,484
Unrestricted Net Position	<u>358,464</u>	<u>319,437</u>
Total Net Position	<u>935,804</u>	<u>926,878</u>
TOTAL LIABILITIES AND NET POSITION	<u><u>\$ 1,401,045</u></u>	<u><u>\$ 1,415,142</u></u>

See the notes to the financial statements.

LAKE MADISON SANITARY DISTRICT
 STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN FUND NET POSITION
 FOR THE YEARS ENDED DECEMBER 31, 2012 AND 2011

	Enterprise Fund	
	2012	2011
Operating Revenue:		
Charges for goods or services:		
Sewer charges	\$ 355,444	\$ 307,815
Connection fees	19,900	23,750
Miscellaneous income	1,159	5,449
Sewer inspection revenue	30	-
Total Operating Revenues	<u>376,533</u>	<u>337,014</u>
Operating Expenses:		
Depreciation	85,840	85,701
Salaries & wages	151,299	142,663
Utilities	41,327	42,737
Insurance	18,533	25,730
Shop supplies	9,877	15,164
Repairs & maintenance	3,049	13,228
Professional fees	9,161	12,874
Employer FICA	11,281	10,920
SD retirement system	8,848	8,565
Vehicle expense	5,132	7,736
Office supplies	4,540	5,041
Water testing	990	858
Travel & conferences	1,049	280
Dues & subscriptions	274	462
South Dakota unemployment	234	248
Miscellaneous	3,063	2,531
Total Operating Expenses	<u>354,497</u>	<u>374,738</u>
Operating Loss	<u>22,036</u>	<u>(37,724)</u>
Nonoperating Revenue (Expense):		
Interest income	2,112	3,016
Interest expense	(15,222)	(16,165)
Total Nonoperating Revenue (Expense)	<u>(13,110)</u>	<u>(13,149)</u>
Change in Net Position	<u>8,926</u>	<u>(50,873)</u>
Net Position - Beginning	<u>926,878</u>	<u>977,751</u>
Net Position - Ending	<u>\$ 935,804</u>	<u>\$ 926,878</u>

See the notes to the financial statements.

LAKE MADISON SANITARY DISTRICT
STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2012 AND 2011

	Enterprise Fund	
	2012	2011
Cash Flows from Operating Activities:		
Cash receipts from customers	\$ 378,571	\$ 338,996
Cash payments to employees for services	(169,891)	(164,505)
Cash payments to suppliers of goods and services	(102,088)	(132,753)
Net Cash Provided by Operating Activities	106,592	41,738
Cash Flows from Capital and Related Financing Activities:		
Redemption of Long-Term Debt	(27,548)	(26,604)
Purchase of Capital Assets	(22,897)	(41,601)
Interest Expense	(15,222)	(16,165)
Net Cash (Used) by Capital and Related Financing Activities	(65,667)	(84,370)
Cash Flows from Investing Activities:		
Interest Earnings	2,112	3,016
Interest added to Certificates of Deposit	(1,163)	(2,079)
Net Cash Provided (Used) by Investing Activities	949	937
Net Increase (Decrease) in Cash and Cash Equivalents	41,874	(41,695)
Cash and Cash Equivalents at Beginning of Year	64,395	106,090
Cash and Cash Equivalents at End of Year	106,269	64,395
Net Increase (Decrease) in Cash and Cash Equivalents	\$ 41,874	\$ (41,695)
RECONCILIATION OF OPERATING INCOME (LOSS) TO NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES:		
Cash Flows from Operating Activities:		
Operating Income (Loss)	\$ 22,036	\$ (37,724)
Adjustments to Reconcile Operating Income to Net Cash Provided (Used) by Operating Activities:		
Depreciation Expense	85,840	85,701
Changes in Assets and Liabilities:		
(Increase) Decrease in Accounts Receivable	(625)	(1,128)
(Increase) Decrease in Prepaids	109	(151)
(Increase) Decrease in Deposits	(5,293)	2,223
Increase (Decrease) in Accounts Payable	91	(8,184)
Increase (Decrease) in Customer Deposits	2,663	3,110
Increase (Decrease) in Accrued Leave Payable	1,771	(2,109)
Net Cash Provided (Used) by Operating Activities	\$ 106,592	\$ 41,738

See the notes to the financial statements.

LAKE MADISON SANITARY DISTRICT
NOTES TO THE FINANCIAL STATEMENTS
DECEMBER 31, 2012

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

a. Financial Reporting Entity:

The fund included in this report is controlled by or dependent upon the Lake Madison Sanitary District governing board.

The accounting policies of the Sanitary District conform to generally accepted accounting principles as applicable to governments.

b. Basis of Presentation:

The accounts are organized on the basis of an enterprise fund.

Proprietary Funds:

Enterprise Funds – Enterprise funds may be used to report any activity for which a fee is charged to external users for goods or services. Activities are required to be reported as enterprise funds if any one of the following criteria is met.

Governments should apply each of these criteria in the context of the activity's principal revenue sources.

- a. The activity is financed with debt that is secured solely by a pledge of the net revenues from fees and charges of the activity. Debt that is secured by a pledge of net revenues from fees and charges and the full faith and credit of a related primary government or component unit – even if that government is not expected to make any payments – is not payable solely from fees and charges of the activity. (Some debt may be secured, in part, by a portion of its own proceeds but should be considered as payable “solely” from the revenues of the activity.)
- b. Laws or regulations require 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.
- c. The pricing policies of the activity establish fees and charges designed to recover its costs, including capital costs (such as depreciation or debt service).

The sanitary sewer fund is the only enterprise fund maintained by the entity. This fund is financed primarily by user charges and accounts for the construction and operation of the sanitary sewer system and related facilities.

c. Measurement Focus and Basis of Accounting:

Measurement focus is a term used to describe “how” transactions are recorded within the various financial statements. Basis of accounting refers to “when” revenues and expenditures or expenses are recognized in the accounts and reported in the financial statements, regardless of the measurement focus.

LAKE MADISON SANITARY DISTRICT
 NOTES TO THE FINANCIAL STATEMENTS
 DECEMBER 31, 2012

Measurement Focus:

In the financial statements, the “economic resources” measurement focus and the accrual basis of accounting are applied to the proprietary funds.

Basis of Accounting:

All proprietary funds are accounted for using the accrual basis of accounting. Their revenues are recognized when they are earned, and their expenses are recognized when they are incurred.

d. Capital Assets:

Capital assets include land, buildings, machinery and equipment, and all other tangible or intangible assets that are used in operations and that have initial useful lives extending beyond a single reporting period.

Capital assets are recorded at historical cost. Donated capital assets are valued at their estimated fair value on the date donated. Reported cost values include ancillary charges necessary to place the asset into its intended location and condition for use. Subsequent to initial capitalization, improvements or betterments that are significant and which extend the useful life of a capital asset are also capitalized.

For capital assets used in business-type activities/proprietary fund's operations, construction period interest is capitalized in accordance with USGAAP.

Depreciation of all exhaustible fixed assets used by proprietary funds is charged as an expense against their operations. Accumulated depreciation is reported on proprietary fund balance sheets.

Capitalization thresholds (the dollar values above which asset acquisitions are added to the capital asset accounts), depreciation methods and estimated useful lives of capital assets reported in the proprietary funds are as follows:

	<u>Capitalization Threshold</u>	<u>Depreciation Method</u>	<u>Estimated Useful Life</u>
Land	All	----N/A----	----N/A----
Building	\$500	Straight-line	30
Storage Building	\$500	Straight-line	39
Furniture & Equip.	\$500	Straight-line	7 & 5
Vehicles	\$500	Straight-line	5
Lift Station	\$500	Straight-line	20
Forced Main	\$500	Straight-line	20
Lagoons	\$500	Straight-line	30
Gravity Sewer	\$500	Straight-line	30
Auxiliary Generators	\$500	Straight-line	20
Monitoring System	\$500	Straight-line	20

Land is an inexhaustible capital asset and is not depreciated.

LAKE MADISON SANITARY DISTRICT
NOTES TO THE FINANCIAL STATEMENTS
DECEMBER 31, 2012

e. Proprietary Funds Revenue and Expense Classifications:

In the proprietary fund's Statement of Revenues, Expenses and Changes in Net Position, revenues and expenses are classified in a manner consistent with how they are classified in the Statement of Cash Flows. That is, transactions for which related cash flows are reported as capital and related financing activities, noncapital financing activities, or investing activities are not reported as components of operating revenues or expenses.

f. Cash and Cash Equivalents:

For the purpose of preparing the Statement of Cash Flows, the Sanitary District considers all highly liquid investments and deposits with a term to maturity of three months or less, at date of acquisition, to be cash equivalents.

g. Equity Classifications

Equity is classified as Net Position and is displayed in three components:

1. Net Investment in Capital Assets – Consists of capital assets, including restricted capital assets, net of accumulated depreciation (if applicable) and reduced by the outstanding balances of any bonds, mortgages, notes, or other borrowings that are attributable to the acquisition, construction, or improvement of those assets.
2. Restricted Net Position – Consists of net position with constraints placed on their 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 Position – All other net position that do not meet the definition of "restricted" or "net investment in capital assets."

h. Application of Net Position:

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 both restricted and unrestricted net position are available.

2. DEPOSITS AND INVESTMENTS

Deposits: The District's cash deposits are made in qualified public depositories as defined by SDCL 4-6A-1, and may be in the form of demand or time deposits. Qualified depositories are required by SDCL 4-6A-3 to maintain at all times, segregated from their other assets, eligible collateral having a value equal to at least 100 percent of the public deposit accounts which exceed deposit insurance such as the FDIC and NCUA. In lieu of pledging eligible securities, a qualified public depository may furnish irrevocable standby letters of credit issued by federal home loan banks accompanied by written evidence of that bank's public debt rating which may not be less than "AA" or a qualified

LAKE MADISON SANITARY DISTRICT
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public depository may furnish a corporate surety bond of a corporation authorized to do business in South Dakota.

The carrying amount of deposits on the December 31, 2012 statement of net assets was \$349,884.

Deposits: The actual bank balances at December 31, 2012 were as follows:

	2012
Insured (FDIC/NCUA)	\$ 391,813
Uninsured, uncollateralized	-
Total deposits	\$ 391,813

Investments: In general, SDCL 4-5-6 permits District funds to be invested only in (a) securities of the United States and securities guaranteed by the United States Government either directly or indirectly; or (b) repurchase agreements fully collateralized by securities described in (a) above; or in shares of an open-end, no-load fund administered by an investment company whose investments are in securities described in (a) above and repurchase agreements described in (b) above. Also, SDCL 4-5-9 requires investments to be in the physical custody of the political subdivision or may be deposited in a safekeeping account with any bank or trust company designated by the political subdivision as its fiscal agent.

As of December 31, 2012, Lake Madison Sanitary District had no investments.

3. INVENTORY

Inventory is valued at the lower of cost or market using the first-in, first-out method and consists of uninstalled replacement parts associated with the sanitary sewer system.

4. PROPERTY TAXES

Property taxes are levied on or before October 1, of the year preceding the start of the fiscal year. They attach as an enforceable lien on property, and become due and payable as of the following January 1, the first day of the fiscal year. Taxes are payable in two installments on or before April 30 and October 31 of the fiscal year.

The sanitary district is permitted by state statute to levy property taxes as necessary per \$1,000 of taxable valuation of property in the sanitary district. State statute allows the tax rates to be raised by special election of the district voters. The combined tax rate to finance sanitary district services including principal and interest on long-term debt for the year ended December 31, 2012, was \$0.00 per \$1,000 of taxable valuation.

LAKE MADISON SANITARY DISTRICT
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5. FIXED ASSETS

A summary of changes in capital assets for the year ended December 31, 2012 is as follows:

	Balance 1/1/2012	Increases	Decreases	Balance 12/31/2012
Capital assets, not being depreciated:				
Land	\$ 24,224	\$ -	\$ -	\$ 24,224
Capital assets, being depreciated:				
Buildings	151,366			151,366
Machinery and Equipment	612,357	22,897		635,254
Lift Stations	829,309			829,309
Forced Main	1,017,623			1,017,623
Lagoons	927,368			927,368
Gravity Sewers	898,863			898,863
Totals	<u>4,436,886</u>	<u>22,897</u>	<u>-</u>	<u>4,459,783</u>
Less accumulated depreciation for:				
Buildings	(93,113)	(4,797)		(97,910)
Machinery and Equipment	(527,603)	(21,206)		(548,809)
Lift Stations	(708,554)	(8,617)		(717,171)
Forced Main	(966,243)	(6,059)		(972,302)
Lagoons	(328,130)	(30,913)		(359,043)
Gravity Sewers	(787,346)	(14,248)		(801,594)
Total Accumulated Depreciation	<u>(3,410,989)</u>	<u>(85,840)</u>	<u>-</u>	<u>(3,496,829)</u>
Total capital assets being depreciated, net	<u>1,025,897</u>	<u>(62,943)</u>	<u>-</u>	<u>962,954</u>
Business-type activity capital assets, net	<u>\$ 1,050,121</u>	<u>\$ (62,943)</u>	<u>\$ -</u>	<u>\$ 987,178</u>

6. LONG-TERM LIABILITIES

A summary of the changes in long-term liabilities follows:

	Beginning Balance	Additions	Deletions	Ending Balance	Due Within One Year
Business-Type Activities:					
State Revolving Loan	\$ 445,164	\$ -	\$ (27,548)	\$ 417,616	\$ 28,525
Accrued Compensated Absences	5,891	9,537	(7,766)	7,662	-
Total Business-Type Activities	<u>\$ 451,055</u>	<u>\$ 9,537</u>	<u>\$ (35,314)</u>	<u>\$ 425,278</u>	<u>\$ 28,525</u>

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SD Clean Water State Revolving Fund

Note dated April 6, 2004, payable in quarterly installments, including interest at a rate of 3.5% per annum beginning July 1, 2005, and thereafter until fully paid in 2025.

The annual debt service requirements to maturity for all debt outstanding as of December 31, 2012, are as follows:

Year Ending December 31,	SRF Loan	
	<u>Principal</u>	<u>Interest</u>
2013	28,525	14,245
2014	29,536	13,233
2015	30,584	12,186
2016	31,668	11,101
2017	32,791	9,978
2018-2022	182,245	31,602
2023-2027	82,267	3,273
TOTALS	<u>\$ 417,616</u>	<u>\$ 95,618</u>

Accumulated Unpaid Vacation and Sick Leave: Part time employees get 10 days per year vacation and 1/2 day per month sick leave with a maximum of 30 days.

Full-time employees get up to 20 days per year vacation and 1/2 day per month sick leave. Four and one-half weeks vacation and 30 days personal leave can be accumulated. Upon termination employees are entitled to receive compensation for their accrued vacation balance. The vacation balances as of December 31, 2012 and 2011 were \$7,662 and \$5,891, respectively.

7. RESTRICTED NET POSITION

Restricted Net Position for the year ended December 31, 2012 were as follows:

<u>Restriction</u>	<u>Restricted by</u>	<u>Amount</u>
Insurance	Contract agreement	\$ 7,777

8. RETIREMENT PLAN

All employees participate in the South Dakota Retirement System (SDRS), a cost-sharing, multiple employer public employee retirement system established to provide retirement benefits for employees of the State of South Dakota and its political subdivisions. The SDRS provides retirement, disability and survivor's benefits. The right to receive retirement benefits vests after three years of credited service. Authority for establishing, administering and amending plan provisions are found in South Dakota Codified Law 3-12. The SDRS issues a publicly available financial report that includes financial statements and required supplementary information. That report may be obtained by writing to the SDRS, P.O. Box 1098, Pierre, SD 57501-1098 or by calling (605) 773-3731.

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General employees are required by state statute to contribute 6 percent of their salary to the plan, while public safety and judicial employees contribute at 8 percent and 9 percent, respectively. State statute also requires the employer to contribute an amount equal to the employee's contribution. State statute also requires the employer to make an additional contribution in the amount of 6.2 percent for any compensation exceeding the maximum taxable amount for social security for general employees only. The District's share of contributions to the SDRS for the fiscal years ended December 31, 2012, 2011 and 2010 were \$8,848, \$8,565, and \$8,286, (EMPLOYER'S SHARE) respectively, equal to the required contributions each year.

10. RISK MANAGEMENT

The District 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. During the period ended December 31, 2012, the District managed its risks as follows:

Liability Insurance:

The District joined the South Dakota Public Assurance Alliance (SDPAA), a public entity risk pool currently operating as a common risk management and insurance program for South Dakota local government entities. The objective of the SDPAA is to administer and provide risk management services and risk sharing facilities to the members and to defend and protect the members against liability, to advise members on loss control guidelines and procedures, and provide them with risk management services, loss control and risk reduction information and to obtain lower costs for that coverage. The District's responsibility is to promptly report to and cooperate with the SDPAA to resolve any incident which could result in a claim being made by or against the District. The District pays an annual premium, to provide liability coverage detailed below, under a claims-made policy and the premiums are accrued based on the ultimate cost of the experience to date of the SDPAA member, based on their exposure or type of coverage. The District pays an annual premium to the pool to provide coverage for general liability, auto liability, property damage, and wrongful acts.

The agreement with the SDPAA provides that the above coverages will be provided to a \$3,000,000 limit. Member premiums are used by the pool for payment of claims and to pay for reinsurance for claims in excess of \$250,000 for property coverage and \$500,000 for liability coverage to the upper limit. A portion of the member premiums are also allocated to a cumulative reserve fund. The District would be eligible to receive a refund for a percentage of the amount allocated to the cumulative reserve fund on the following basis:

End of District's First Full Year	50%
End of District's Second Full Year	60%
End of District's Third Full Year	70%
End of District's Fourth Full Year	80%
End of District's Fifth Full Year	90%
End of District's Sixth Full Year and Thereafter	100%

As of December 31, 2012, the District has vested balance in the cumulative reserve fund of \$7,777.

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The District carries a \$500 deductible for wrongful acts coverage. Building, contents, and equipment coverage is based on a per item statement of values and carries a \$1,000 deductible.

The District does not carry additional insurance to cover claims in excess of the upper limit. Settled claims resulting from these risks have not exceeded the liability coverage during the past three years.

Worker's Compensation:

The District joined the South Dakota Municipal League Worker's Compensation Fund (Fund), a public entity risk pool currently operating as a common risk management and insurance program for South Dakota local government entities. The objective of the Fund is to formulate, develop, and administer, on behalf of the member organizations, a program of worker's compensation coverage, to obtain lower costs for that coverage, and to develop a comprehensive loss control program. The District's responsibility is to initiate and maintain a safety program to give its employees safe and sanitary working conditions and to promptly report to and cooperate with the Fund to resolve any worker's compensation claims. The District pays an annual premium, to provide worker's compensation coverage for its employees, under a self-funded program and the premiums are accrued based on the ultimate cost of the experience to date of the Fund members. Coverage limits are set by state statute. The pool pays the first \$650,000 of any claim per individual. The pool has reinsurance which covers up to statutory limits in addition to a separate combined employer liability limit of \$2,000,000 per incident.

The District does not carry additional insurance to cover claims in excess of the upper limit. Settled claims resulting from these risks have not exceeded the liability coverage over the past three years.

Unemployment Benefits:

The Sanitary District provides coverage for unemployment benefits by paying into the Unemployment Compensation Fund established by state law and managed by the State of South Dakota. During the year ended December 31, 2012 no claims for unemployment benefits were paid. At December 31, 2012 no claims had been filed for unemployment benefits and none are anticipated in the next fiscal year.