

BUTTE-MEADE SANITARY WATER DISTRICT

INDEPENDENT AUDITOR'S REPORTS,
FINANCIAL STATEMENTS, AND REQUIRED
SUPPLEMENTARY INFORMATION

DECEMBER 31, 2018

CASEY  PETERSON
Leading the Way.

RAPID CITY, SOUTH DAKOTA
GILLETTE, WYOMING

Butte-Meade Sanitary Water 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 the Financial
Statements Performed in Accordance with *Government Auditing Standards*

Board of Directors
Butte-Meade Sanitary Water District
Newell, South Dakota

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 statements of net position, revenues, expenses and changes in net position, and cash flows of Butte-Meade Sanitary Water District, as of and for the year ended December 31, 2018, and the related notes to the financial statements, which collectively comprise Butte-Meade Sanitary Water District's basic financial statements and have issued our report thereon dated March 27, 2019.

Internal Control over Financial Reporting

In planning and performing our audit of the financial statements, we considered Butte-Meade Sanitary Water 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 Butte-Meade Sanitary Water District's internal control. Accordingly, we do not express an opinion on the effectiveness of Butte-Meade Sanitary Water 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 and, therefore, material weaknesses or significant deficiencies may exist that have not been identified. We did identify certain deficiencies in internal control, described in the accompanying Schedule of Audit Findings and Management's Responses as items 2018-001 through 2018-005 that we consider to be material weaknesses.



Compliance and Other Matters

As part of obtaining reasonable assurance about whether Butte-Meade Sanitary Water District's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* and which are described in the accompanying Schedule of Audit Findings and Management's Responses as items 2018-004 and 2018-005.

Butte-Meade Sanitary Water District's Response to Findings

Butte-Meade Sanitary Water District's response to the findings identified in our audit is described in the accompanying Schedule of Audit Findings and Management's Responses. Butte-Meade Sanitary Water 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 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. As required by South Dakota Codified Law 4-11-11, this report is a matter of public record and its distribution is not limited.



Casey Peterson, Ltd.

Rapid City, South Dakota

March 27, 2019

Butte-Meade Sanitary Water District
Schedule of Audit Findings and Management's Responses
December 31, 2018

FINDINGS - FINANCIAL STATEMENT AUDIT

Material Weakness

Internal Controls and Segregation of Duties

2018-001 *Condition:* The lack of accounting training among the few staff members does not allow the District to separate incompatible accounting functions or processes or provide appropriate oversight of accounting functions that is necessary under a properly designed system of internal controls.

Criteria: The District should have safeguards in place to separate accounting functions which is fundamental in a good system of internal controls. An ideal segregation of duties would separate who authorizes, records, reconciles, and has custody of assets.

Cause: The Business Office has a small staff size and there is a limited number of people in the District's governance with an accounting background.

Effect: The Office Manager performs all accounting transactions with limited oversight. The possibility of fraud or errors occurring and not being detected or corrected is present. There is a potential that intentional or unintentional errors could be made and not be detected.

Auditor's Recommendation: It is the responsibility of management and those charged with governance to make the decision whether to accept the degree of risk associated with Office Manager maintaining accounting records without proper oversight, because of cost or other considerations.

Management's Response: The District hired a third-party accounting firm to set up and train office personnel on QuickBooks. The third-party accounting firm also reviews accounting records quarterly. Processes are being evaluated in order to segregate responsibilities and implement new oversight procedures.

Material Weakness

Internal Controls Related to Drafting Financial Statements

2018-002 *Condition:* The small size of the District limits the ability of the Business Office to maintain adequate segregation of duties to prepare the financial statements and related notes to the financial statements that is required under a properly designed system of internal controls.

Criteria: Establishing internal controls over the preparation and drafting of the financial statements are the responsibility of management. The District should have an internal control system designed to provide for drafting the financial statements being audited.

Cause: This condition exists due to small staff size within the finance function of the District. These issues are common in an organization of this size.

Effect: The District engages its auditor to draft the financial statements and the notes to the financial statements. The possibility of fraud or errors occurring and not being detected or corrected is present in regard to the drafting of the financial statements and the notes to the financial statements.

Auditor's Recommendation: It is the responsibility of management and those charged with governance to make the decision whether to accept the degree of risk associated with the District's auditor drafting the financial statements because of cost or other considerations. If the District chooses not to accept this risk, another accountant with appropriate knowledge, skill, and experience can be hired to either prepare or review the financial statements.

Butte-Meade Sanitary Water District

Schedule of Audit Findings and Management's Responses

December 31, 2018

Management's Response: The District will have an outside accountant review the financial statements and notes to the financial statements prior to the audit being issued.

Material Weakness

Significant Accounting Adjustments

2018-003 *Condition:* A number of material adjustments were needed in order for the financial statements to be reasonably presented.

Criteria: Maintaining accurate accounting records is the responsibility of management. The District should have an internal control system designed to provide a review process to mitigate the risk of material misstatements and provide assurance that the accounting records are accurate.

Cause: This condition exists due to small staff size, with minimal accounting training; a lack of segregation of duties; and a manual accounting system within the finance function of the District.

Effect: The possibility of fraud or errors occurring and not being detected or corrected is present in regard to the drafting of the financial statements and the notes to the financial statements.

Auditor's Recommendation: Training should be provided to those employees responsible for accounting records, a computerized accounting system should be implemented, and oversight of accounting functions should be performed by the Board.

Management's Response: The District computerized accounting records and began using QuickBooks in late 2018. The District has hired a third-party accounting firm to provide training and to review records quarterly. All revenues and expenses are reported to the Board of Trustees monthly. The Board approves all bills and physically signs each check.

Material Weakness and Noncompliance

Payroll Processes

2018-004 *Condition:* The District did not comply with the U.S. Department of Labor's payroll requirements regarding the payment of overtime and wages to non-exempt staff.

Criteria: Every employer covered by the Fair Labor Standards Act must keep certain records for each covered, nonexempt worker. Payroll must be calculated in compliance with the U.S. Department of Labor's requirements.

Cause: Staff are being paid as if they are exempt from federal overtime rules.

Effect: Incorrect payroll payments are made to staff.

Auditor's Recommendation: Staff processing payroll must review and recalculate hours to be paid to ensure payments to employees are proper. We also suggest that the payroll register be approved prior to the issuance of paychecks. In addition, overtime should be paid in the period it is earned.

Management's Response: In late 2018, the District modified the calculation of wages in accordance with Department of Labor Regulations. The payroll register is attached to a voucher that is signed by the Office Manager and the District Manager. After approval at the monthly meeting, the voucher is signed by the Board President. This approval is performed prior to check issuance. Overtime is now being paid one month in arrears.

Butte-Meade Sanitary Water District
Schedule of Audit Findings and Management's Responses
December 31, 2018

Material Weakness and Noncompliance
Budgeting Processes

2018-005 *Condition:* The District does not comply with the South Dakota Codified Law 46A-3E-10, concerning budget adoption.

Criteria: The board of directors of a water development district shall at the time of the organization of the board and annually thereafter on a date established by the district, but before the first of October, adopt a budget and prepare an operations and budget report. The report shall present estimates and itemizations of all the expenses and obligations of the water development district, including expenses of directors, expenses of operating the office, debt service and retirement, and obligations and liabilities to the United States. Before approval of the budget by the district board of directors, a public hearing shall be held. Notice of the hearing shall be published once each week for two successive weeks in the water development district's official newspapers. The notice shall state the time and place of the hearing, its purpose, and that at the hearing all persons interested may appear, either in person or by representative, and be heard and given an opportunity for a full and complete discussion of all items in the budget. With the first notice, the budget shall be published in a form approved by the auditor general. At the conclusion of the hearing, the water development district board may eliminate or amend any portion of the budget before adoption.

Cause: The District does not approve a budget until February of the current fiscal year.

Effect: Noncompliance with State Codified Law and the District is unable to levy taxes.

Auditor's Recommendation: The District should approve the annual budget in compliance with the State Codified Law, before the first of October.

Management's Response: The District will adopt the annual budget in October for the ensuing year.

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Independent Auditor's Report

Board of Directors
Butte-Meade Sanitary Water District
Newell, South Dakota

We have audited the accompanying financial statements of Butte-Meade Sanitary Water District, which comprise the statement of net position as of December 31, 2018 and the related statements of revenues, expenses and changes in net position and cash flows 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; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our 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.

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 financial position of Butte-Meade Sanitary Water District, as of December 31, 2018, and the changes in financial position and cash flows 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, Schedule of Net Pension Liability (Asset) and Schedule of Pension Contributions on pages 9 through 11, 30, and 31 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 March 27, 2019 on our consideration of Butte-Meade Sanitary Water 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 Butte-Meade Sanitary Water District's internal control over financial reporting and compliance. As required by South Dakota Codified Law 4-11-11, this report is a matter of public record.

Casey Peterson, LTD.

Casey Peterson, Ltd.

Rapid City, South Dakota
March 27, 2019

**Butte-Meade Sanitary Water District
Management's Discussion and Analysis
December 31, 2018**

This section of Butte-Meade Sanitary Water District's (the District) annual financial report presents our discussion and analysis of the District's financial performance during the fiscal year ended December 31, 2018. Please read it in conjunction with the District's financial statements, which follow this section.

FINANCIAL HIGHLIGHTS

Butte-Meade Sanitary Water District's net position decreased by \$8,092 from 2017 to 2018. The decrease was mostly due to a decrease in demand related to weather conditions.

Water sales and other sales are directly linked to customer demand. 2018 water sales and other sales decreased from 2017 due to a decrease in demand. Other sales include new construction and repair and maintenance done by District customer. Customers buy material at cost, plus sales tax, through the District. Customer payments constitute other sales.

The District is still replacing customer meters to the new remote read system. At year-end 2018, over 95% had been replaced.

OVERVIEW OF THE FINANCIAL STATEMENTS

This report consists of two parts: management's discussion and analysis (this section) and the basic financial statements. The financial statements also include notes that explain some of the information in the financial statement and provide more detailed data.

FINANCIAL ANALYSIS OF THE DISTRICT AS A WHOLE

The District's combined net position was as follows:

**Table 1
Statement of Net Position**

	<u>2018</u>	<u>2017</u>	<u>Percent Change</u>
Current and Other Assets	\$ 818,228	\$ 842,328	-2.9%
Capital Assets	<u>2,809,485</u>	<u>2,837,143</u>	-1.0%
Total Assets	<u>3,627,713</u>	<u>3,679,471</u>	-1.4%
Deferred Outflows	<u>92,877</u>	<u>115,916</u>	-19.9%
Current Liabilities	167,400	163,665	2.3%
Long-term Liabilities	<u>1,057,219</u>	<u>1,127,307</u>	-6.2%
Total Liabilities	<u>1,224,619</u>	<u>1,290,972</u>	-5.1%
Deferred Inflows	<u>20,849</u>	<u>21,201</u>	-1.7%
Net Position:			
Invested in Capital Assets, Net of Related Debt	1,682,130	1,637,609	2.7%
Restricted	166,678	189,945	-12.2%
Unrestricted	<u>626,314</u>	<u>655,660</u>	-4.5%
Total Net Position	<u>\$ 2,475,122</u>	<u>\$ 2,483,214</u>	-0.3%

**Butte-Meade Sanitary Water District
Management's Discussion and Analysis
December 31, 2018**

The Statement of Net Position reports all financial and capital resources. The statement presents the assets and liabilities in order of relative liquidity. The liabilities with average maturities are presented in two components – the amount due within one year and the amount due in more than one year. The long-term liabilities of the District consisting of notes and bonds payable have been reposted in this manner in the Statement of Net Position. The difference between the District's assets and liabilities and deferred outflows and inflows of resources in its net position.

Changes in Net Position

The District's revenues totaled \$830,918, substantially all of which was received from customers. The District's expenses all related to providing service to customers and maintaining the system.

**Table 2
Statement of Revenues and Expenses**

	<u>2018</u>	<u>2017</u>	<u>Percent Change</u>
Water Sales	\$ 830,918	\$ 874,102	-4.9%
Operating Expenses	<u>778,879</u>	<u>765,317</u>	1.8%
Net Operating Income	52,039	108,785	-52.2%
Non-operating Income (Expense)			
Interest Income	612	540	13.3%
Interest Expense	(60,743)	(64,816)	-6.3%
Other Income	<u>-</u>	<u>41,927</u>	-100.0%
Total Non-operating Expense	<u>(60,131)</u>	<u>(22,349)</u>	169.1%
Change in Net Position	<u>\$ (8,092)</u>	<u>\$ 86,436</u>	-109.4%

Revenues of the District decreased by 4.9% and operating expenses increased by 1.8%.

CAPITAL ASSET ADMINISTRATION

By the end of FY 2018, the District had investments \$2,809,485 (net of depreciation) in a broad range of capital assets including land, buildings, and various machinery and equipment. (see Table 3) This amount represents a net decrease (including additions and deductions) of \$27,658. The capitalization threshold remains unchanged.

**Table 3
Change in Capital Assets (Net of Depreciation)**

	<u>2018</u>	<u>2017</u>	<u>Dollar Change</u>	<u>Percent Change</u>
Land	\$ 14,262	\$ 14,262	\$ -	0.0%
Furniture and Equipment	4,832	6,496	(1,664)	-25.6%
Buildings and Structures	44,900	48,403	(3,503)	-7.2%
Collection and Distribution System	2,726,276	2,740,001	(13,725)	-0.5%
Vehicles	<u>19,215</u>	<u>27,981</u>	<u>(8,766)</u>	-31.3%
	<u>\$ 2,809,485</u>	<u>\$ 2,837,143</u>	<u>\$ (27,658)</u>	-1.0%

This year's capital asset purchases were for equipment including the meter project, pumps, and line replacements.

**Butte-Meade Sanitary Water District
Management's Discussion and Analysis
December 31, 2018**

LONG-TERM DEBT

At year-end, the District had \$1,127,355 in notes payable and revenue bonds outstanding.

**Table 4
Outstanding Debt Obligations**

	<u>2018</u>	<u>2017</u>	<u>Dollar Change</u>	<u>Percent Change</u>
Notes Payable	\$ 184,973	\$ 224,752	\$ (39,779)	-17.7%
Revenue Bonds	942,382	974,782	(32,400)	-3.3%
	<u>\$ 1,127,355</u>	<u>\$ 1,199,534</u>	<u>\$ (72,179)</u>	-6.0%

The District made debt service principal and interest payments in the amount of \$72,179 for principal and \$60,743 for interest.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGET AND RATES

There were no significant changes in operations for the District from 2017 to 2018. The District will continue to replace manual water meters with remote read meters during 2019, only 12 remain to be replaced.

The District will be relocating some main line near the Owl Creek Hill on Highway 212 due to the highway and bridge work to be done by the State in 2019. In order to finance relocating the main line, a 2.25% Drinking Water SRF loan was approved by the State. The amount of the loan will not exceed \$413,000, for 20 years. The project was not yet started as of the date of this report. The project is expected to be completed in 2019.

Due to the addition of this loan, as well as the need to update and replace old line throughout the District, the District implemented a rate increase effective January 2019.

CONTACTING THE DISTRICT'S FINANCIAL MANAGEMENT

This financial report is designed to provide our taxpayers, customers, and creditors with a general overview of the District's finances and to demonstrate the District's accountability for the money it receives. If you have questions about this report or need additional information, contact the Butte-Meade Sanitary Water District's Business Office, 117 Girard Ave, Newell SD 57760.

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FINANCIAL STATEMENTS

Butte-Meade Sanitary Water District
Statement of Net Position
December 31, 2018

ASSETS

Current Assets:

Cash and Cash Equivalents	\$	439,300
Accounts Receivable, Net of Allowance for Doubtful Accounts of \$2,544		63,406
Inventory		66,445
Prepaid Expenses		<u>21,445</u>
Total Current Assets		<u>590,596</u>

Noncurrent Assets:

Land		14,262
Furniture and Equipment		67,105
Buildings and Structures		93,928
Collection and Distribution System		5,943,424
Vehicles		60,862
Less: Accumulated Depreciation		<u>(3,370,096)</u>

Total Capital Assets, Net of Accumulated Depreciation		<u>2,809,485</u>
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Capital Credits Receivable		49,783
Restricted for Debt Service		94,374
Restricted for Member Deposits		83,199
Restricted Pension Asset		<u>276</u>

Total Noncurrent Assets		<u>3,037,117</u>
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TOTAL ASSETS

3,627,713

DEFERRED OUTFLOWS OF RESOURCES

Pension-related Deferred Outflows		<u>92,877</u>
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LIABILITIES

Accrued Expenses		14,880
Current Portion of Long-term Liabilities		70,136
Meter Deposits		<u>82,384</u>

Total Current Liabilities		167,400
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Noncurrent Liabilities:

Long-term Debt, Net of Current Portion		<u>1,057,219</u>
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TOTAL LIABILITIES

1,224,619

DEFERRED INFLOWS OF RESOURCES

Pension-related Deferred Inflows		<u>20,849</u>
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The accompanying notes are an integral part of this financial statement.

NET POSITION

Net Investment in Capital Assets	1,682,130
Restricted:	
Restricted for Rural Development Reserve	94,374
Restricted for SDRS Pension Purposes	72,304
Unrestricted	<u>626,314</u>

TOTAL NET POSITION**\$ 2,475,122**

The accompanying notes are an integral part of this financial statement.

Butte-Meade Sanitary Water District
Statement of Revenues, Expenses, and Changes in Net Position
For the Year Ended December 31, 2018

OPERATING REVENUE	
Water Sales	\$ 830,918
OPERATING EXPENSES	
Wages and Benefits	372,617
Depreciation	113,490
Maintenance and Supplies	148,507
Utilities	57,729
Office Expense	36,842
Insurance	23,218
Professional Fees	22,359
Directors' Fees	<u>4,117</u>
Total Operating Expenses	<u>778,879</u>
Operating Income	<u>52,039</u>
NONOPERATING REVENUE (EXPENSE)	
Interest Income	612
Interest Expense	<u>(60,743)</u>
Total Non-operating Revenue (Expense)	<u>(60,131)</u>
CHANGE IN NET POSITION	(8,092)
NET POSITION - BEGINNING	<u>2,483,214</u>
NET POSITION - ENDING	<u>\$ 2,475,122</u>

The accompanying notes are an integral part of this financial statement.

Butte-Meade Sanitary Water District
Statement of Cash Flows
For the Year Ended December 31, 2018

CASH FLOWS PROVIDED BY OPERATING ACTIVITIES

Cash Receipts From Customers	\$ 842,927
Cash Payments to Employees for Services	(349,097)
Cash Payments to Suppliers of Goods and Services	<u>(288,468)</u>
Net Cash Provided by Operating Activities	<u>205,362</u>

CASH FLOW FROM INVESTING ACTIVITIES

Deposits to Reserves	(246)
Interest Received	<u>612</u>
Net Cash Provided by Investing Activities	<u>366</u>

CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES

Purchase of Capital Assets	(85,832)
Interest Paid on Capital Debt	(60,750)
Principal Paid on Capital Debt	<u>(72,179)</u>
Net Cash Used by Capital and Related Financing Activities	<u>(218,761)</u>

NET DECREASE IN CASH

(13,033)

BALANCE - BEGINNING OF YEAR

452,333

BALANCE - END OF YEAR

\$ 439,300

RECONCILIATION OF OPERATING INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES

Operating Income	\$ 52,039
Adjustments to Reconcile Operating Income to Net Cash Provided by Operating Activities:	
Pension Activities	23,520
Depreciation Expense	113,490
Changes in Assets and Liabilities:	
Receivables	9,826
Inventory	1,981
Prepaid Expenses	(1,215)
Accounts and Other Payables	3,538
Customer Deposits	<u>2,183</u>

NET CASH PROVIDED BY OPERATING ACTIVITIES

\$ 205,362

The accompanying notes are an integral part of this financial statement.

Butte-Meade Sanitary Water District
Notes to the Financial Statements
December 31, 2018

NOTE 1 - NATURE OF ACTIVITIES

The Butte-Meade Sanitary Water District (the District) is a government entity comprised of one enterprise fund. The financial statements are reported on the accrual basis of accounting. The accrual basis of accounting recognizes revenue when earned and expenditures when a liability is incurred. The District is a subdivision of the government of the State of South Dakota.

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. Basis of Presentation

The District is considered a single enterprise fund for financial reporting purposes. The District's financial statements have been prepared on the accrual basis of accounting, consistent with the governmental proprietary fund concept which pertains to financial activities that operate in a manner similar to private business enterprises and are financed through user charges for services. The District applies all applicable Government Accounting Standards Board (GASB) pronouncements.

Operating income includes revenues and expenses related to the primary, continuing operations of the District. Principal operating revenues are user fees for water services. Principal operating expenses are the costs of providing water and maintaining system assets. Other revenues and expenses are classified as non-operating in the financial statements.

B. Accounts Receivable

Accounts receivable are stated at the amount management expects to collect from outstanding balances. Management provides for uncollectible amounts through a charge to bad debt expense and an adjustment to a valuation allowance based on its assessment of the current status of individual accounts. Balances outstanding over 90 days have service disconnected until the outstanding balance is paid.

C. Inventory

Inventory is valued at cost, as determined on the first-in, first-out method and consists mainly of maintenance supplies.

D. Property and Equipment

Capital assets, which include the collection and distribution system, buildings, and other equipment are reported in the basic financial statements. The District defines capital assets as those with an initial individual cost of more than \$2,000 and an estimated useful life in excess of one year. Such assets are recorded at historical cost. Depreciation is calculated on the straight-line method over the estimated useful lives of the depreciable assets. The estimated useful lives are as follows:

Furniture and Equipment	5 - 10 years
Buildings and Structures	10 - 40 years
Vehicles	5 - 10 years
Collection and Distribution System	5 - 85 years

E. Vacation and Sick Leave

Annual leave is earned by the full-time employees at a rate of two weeks after 1 year, three weeks from 10 to 19 years and four weeks after 20 years. Sick leave is earned by full-time employees at a rate of twelve (12) days per year. Upon termination the employees are not entitled to receive compensation for their annual leave or sick leave balances.

Butte-Meade Sanitary Water District
Notes to the Financial Statements
December 31, 2018

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

F. Revenue and Expense Classifications

In the proprietary fund's Statement of Revenues, Expenses and Changes in Net Position, revenue 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, non-capital financing activities, or investing activities are not reported as components of operating revenues or expenses.

G. Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

H. Cash and Cash Equivalents

For the purpose of financial reporting, "cash and cash equivalents" includes all demand and savings accounts and certificates of deposit or short-term investments with a term to maturity at date of acquisition of three months or less. Investments in open-end mutual fund shares, or similar investments in external investments pools, are also considered to be cash equivalents.

I. Deferred Inflows and Deferred Outflows of Resources

In addition to assets, the statement of financial position reports a separate section for deferred outflows of resources. Deferred outflows of resources represent consumption of net position that applies to a future period or periods. These items will not be recognized as an outflow of resources until the applicable future period. The only deferred outflow of resources reported is a deferred amount arising from the District's pension plan for qualified retirees as discussed in Note 6.

In addition to liabilities, the statement of financial position reports a separate section for deferred inflows of resources. Deferred inflows of resources represent acquisitions of net position that applies to a future period or periods. These items will not be recognized as an inflow of resources until the applicable future period. The only deferred inflow of resources reported is a deferred amount arising from the District's pension plan for qualified retirees as discussed in Note 6.

J. Equity Classifications

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

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 improvement of those assets.

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.

Unrestricted Net Position - All other net position that do not meet the definition of "restricted" or "net investment in capital assets."

Butte-Meade Sanitary Water District
Notes to the Financial Statements
December 31, 2018

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

K. 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.

L. Pensions

For purposes of measuring the net pension liability (asset), deferred outflows of resources related to pensions, and pension expense (revenue), information about the fiduciary net position of the South Dakota Retirement System (SDRS) and additions to/deletions from SDRS's fiduciary net position have been determined on the same basis as they are reported by SDRS. Municipal contributions and net pension liability (asset) are recognized on an accrual basis of accounting.

NOTE 3 - DEPOSITS AND INVESTMENTS, CREDIT RISK, CONCENTRATIONS OF CREDIT RISK, AND INTEREST RATE RISK

Deposits and Investments

Various restrictions on deposits and investments are imposed by statutes. These restrictions are summarized below:

Deposits

The District's cash deposits are made in qualified public depositories as defined by SDCL 4-6A-1, 9-22-6, 9-22-6.1, and 9-22-6.2, 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 public depository may furnish a corporate surety bond of a corporation authorized to do business in South Dakota.

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 deposited in a safekeeping account with any banker trust company designated by the political subdivision as its fiscal agent. The District had no investments as of December 31, 2018.

Credit Risk - State law limits eligible investments for the District as discussed above. The District has no investment policy that would further limit its investment choices.

Butte-Meade Sanitary Water District
Notes to the Financial Statements
December 31, 2018

NOTE 4 - PROPERTY AND EQUIPMENT

A summary of changes in capital assets for the year ended December 31, 2018 is as follows:

	<u>Balance</u> <u>12/31/2017</u>	<u>Increase</u>	<u>Decrease</u>	<u>Balance</u> <u>12/31/2018</u>
Non-depreciable Capital Assets:				
Land	\$ 14,262	\$ -	\$ -	\$ 14,262
Depreciable Capital Assets:				
Furniture and Equipment	67,105	-	-	67,105
Buildings and Structures	93,928	-	-	93,928
Collection and Distribution System	5,857,592	85,832	-	5,943,424
Vehicles	<u>60,862</u>	<u>-</u>	<u>-</u>	<u>60,862</u>
Subtotal	6,093,749	85,832	-	6,179,581
Less: Accumulated Depreciation	<u>3,256,606</u>	<u>113,490</u>	<u>-</u>	<u>3,370,096</u>
Net Capital Assets	<u>\$ 2,837,143</u>	<u>\$ (27,658)</u>	<u>\$ -</u>	<u>\$ 2,809,485</u>

NOTE 5 - LONG-TERM DEBT

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

	<u>Balance</u> <u>12/31/2017</u>	<u>Increase</u>	<u>Decrease</u>	<u>Balance</u> <u>12/31/2018</u>	<u>Amounts Due</u> <u>Within 1 Year</u>
General Obligation Debt:					
Note Payable - First					
National Bank	\$ 107,572	\$ -	\$ 14,134	\$ 93,438	\$ 14,906
Revenue Bonds - RD	974,782	-	32,400	942,382	34,430
Note Payable - NRWS	5,346	-	5,346	-	-
Note Payable - SDDENR	<u>111,834</u>	<u>-</u>	<u>20,299</u>	<u>91,535</u>	<u>20,800</u>
Total Long-term Liabilities	<u>\$ 1,199,534</u>	<u>\$ -</u>	<u>\$ 72,179</u>	<u>\$ 1,127,355</u>	<u>\$ 70,136</u>

Butte-Meade Sanitary Water District
Notes to the Financial Statements
December 31, 2018

NOTE 5 - LONG-TERM DEBT (CONTINUED)

Long-term debt consisted of the following at December 31, 2018:

Loan due to First National Bank, payable in monthly installments of \$1,621 including interest of 5.25%, maturing July 2024. Interest expense was \$5,352 for the year ended December 31, 2018.	\$ 93,438
Revenue bond due to Rural Development, payable in monthly installments of \$5,236 including interest of 6.625%, maturing June 2032. Interest expense was \$37,356 for the year ended December 31, 2018.	549,950
Revenue bond due to Rural Development, payable in monthly installments of \$1,939 including interest of 4.125%, maturing July 2048. Interest expense was \$16,343 for the year ended December 31, 2018.	392,432
Loan due to South Dakota Department of Natural Resources in quarterly installments of \$5,661 including interest of 2.25%, maturing April 2023. Interest expense was \$2,346 for the year ended December 31, 2018.	<u>91,535</u>
	1,127,355
Less: Current Maturities	<u>(70,136)</u>
	<u>\$ 1,057,219</u>

A summary of required principal and interest payments on the long-term debt is as follows:

For the Year Ending December 31	Principal	Interest	Total
2019	\$ 70,136	\$ 58,059	\$ 128,195
2020	73,572	54,623	128,195
2021	77,203	50,992	128,195
2022	81,038	47,157	128,195
2023	67,712	43,233	110,945
2024 - 2028	275,574	165,431	441,005
2029 - 2033	236,196	76,535	312,731
2034 - 2038	72,779	43,561	116,340
2039 - 2043	89,418	26,922	116,340
2044 - 2048	83,727	6,479	90,206
	<u>\$ 1,127,355</u>	<u>\$ 572,992</u>	<u>\$ 1,700,347</u>

The terms of the revenue bonds require that the District maintain a debt service account. A sum equal to the minimum of 1/12 of the annual installment coming due on the next succeeding January 1, is to be deposited to this account each month. Principal and interest payments are to be made from this account. At December 31, 2018, the District was in complete compliance with these terms.

Butte-Meade Sanitary Water District
Notes to the Financial Statements
December 31, 2018

NOTE 5 - LONG-TERM DEBT (CONTINUED)

The terms of the revenue bonds also require that all the surplus net revenue, in excess of the amounts required in the maintenance of the debt service account noted above, be deposited in a reserve account. This account shall be used for major repairs, maintenance, and improvements on the water system. No funds were available for deposit to this account as of December 31, 2018.

NOTE 6 - PENSION PLAN

All employees, working more than 20 hours per week during the year, participate in the South Dakota Retirement System (SDRS), a cost sharing, multiple-employer hybrid defined benefit pension plan administered by SDRS to provide retirement benefits for employees of the State of South Dakota and its political subdivisions. The SDRS provides retirement, disability, and survivor 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 SDCL 3-12. The SDRS issues a publicly available financial report that includes financial statements and required supplementary information. That report may be obtained at <http://sdrs.sd.gov/publications.aspx> or by writing to the SDRS, P.O. Box 1098, Pierre, SD 57501-1098 or by calling (605) 773-3731.

Benefits Provided

SDRS has three different classes of employees, Class A general members, Class B public safety and judicial members, and Class C Cement Plant Retirement Fund Members.

Members that were hired before July 1, 2017, are Foundation members. Class A Foundation members and Class B Foundation members who retire after age 65 with three years of contributory service are entitled to an unreduced annual retirement benefit. An unreduced annual retirement benefit is also available after age 55 for Class A Foundation members where the sum of age and credited service is equal to or greater than 85 or after age 55 for Class B Foundation judicial members where the sum of age and credited service is equal to or greater than 80. Class B Foundation public safety members can retire with an unreduced annual retirement benefit after age 55 with three years of contributory service. An unreduced annual retirement benefit is also available after age 45 for Class B Foundation public safety members where the sum of age and credited service is equal to or greater than 75. All Foundation retirement benefits that do not meet the above criteria may be payable at a reduced level.

Members that were hired on/after July 1, 2017, are Generational members. Class A Generational members and Class B Generational judicial members who retire after age 67 with three years of contributory service are entitled to an unreduced annual retirement benefit. Class B Generational public safety members can retire with an unreduced annual retirement benefit after age 57 with three years of contributory service. At retirement, married Generational members may elect a single-life benefit, a 60 percent joint and survivor benefit, or a 100 percent joint and survivor benefit. All Generational retirement benefits that do not meet the above criteria may be payable at a reduced level. Generational members will also have a variable retirement account (VRA) established, in which they will receive up to 1.5 percent of compensation funded by part of the employer contribution. VRAs will receive investment earnings based on investment returns.

Legislation enacted in 2017 established the current COLA process. At each valuation date:

- Baseline actuarial accrued liabilities will be calculated assuming the COLA is equal to the long-term inflation assumption of 2.25%.
- If the fair value of assets is greater or equal to the baseline actuarial accrued liabilities, the COLA will be:
 - The increase in the 3rd quarter CPA-W, no less than 0.5% and no greater than 3.5%

**Butte-Meade Sanitary Water District
Notes to the Financial Statements
December 31, 2018**

NOTE 6 - PENSION PLAN (CONTINUED)

- If the fair of assets is less than the baseline actuarial accrued liabilities, the COLA will be:
 - The increase in the 3rd quarter CPI-W, no less than 0.5% and no greater a restricted maximum such that, that if the restricted maximum is assumed for future COLAs, the fair value of assets will be greater or equal to the accrued liabilities.

All benefits except those depending on the member’s accumulated contributions are annually increased by the cost-of-living adjustment.

Contributions

Per SDCL 3-12, contribution requirements of the active employees and the participating employers are established and may be amended by the SDRS Board. Covered employees are required by state statute to contribute the following percentages of their salary to the plan; Class A Members, 6.0% of salary; Class B Judicial Members, 9.0% of salary; and Class B Public Safety Members, 8.0% of salary. 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% 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 years ended December 31, 2018, 2017, and 2016 were \$15,030, \$14,739, and \$14,641 respectively, equal to the required contributions each year.

Pension Liabilities (Assets), Pension Expense (Revenue), and Deferred Outflows of Resources and Deferred Inflows of Resources to Pensions

At June 30, 2018, SDRS was 100.02% funded and accordingly, has a net pension asset. The proportionate shares of the components of the net pension asset of South Dakota Retirement System, for the District as of the measurement period ending June 30, 2018 and reported by the District as of December 31, 2018 are as follows:

Proportionate Share of Total Pension Liability	\$ 1,447,002
Less: Proportionate Share of Net Position Restricted for Pension Benefits	<u>1,447,278</u>
Proportionate Share of Net Pension Liability (Asset)	<u>\$ (276)</u>

At December 31, 2018, the District reported a liability (asset) of (\$276) for its proportionate share of the net pension liability (asset). The net pension liability (asset) was measured as of June 30, 2018 and the total pension liability (asset) used to calculate the net pension liability (asset) was based on a projection of the District’s share of contributions to the pension plan relative to the contributions of all participating entities. At June 30, 2018, the District’s proportion was .01182830%, which is a decrease of 0.0003227% from its proportion measured as of June 30, 2017.

Butte-Meade Sanitary Water District
Notes to the Financial Statements
December 31, 2018

NOTE 6 - PENSION PLAN (CONTINUED)

For the year ended December 31, 2018, the District recognized pension expense (reduction of pension expense) of \$23,513. At December 31, 2018, the District reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

	<u>Deferred Outflows of Resources</u>	<u>Deferred Inflows of Resources</u>
Difference Between Expected and Actual Experience	\$ 10,427	\$ -
Changes in Assumption	70,037	-
Net Difference Between Projected and Actual Earnings on Pension Plan Investments	-	20,849
Changes in Proportion and Difference Between District Contributions and Proportionate Share of Contributions	4,854	-
District Contributions Subsequent to the Measurement Date	<u>7,559</u>	<u>-</u>
Total	<u>\$ 92,877</u>	<u>\$ 20,849</u>

\$7,559 reported as deferred outflow of resources related to pensions resulting from District contributions subsequent to the measurement date will be recognized as a reduction of the net pension liability in the year ending December 31, 2019. Other amounts reported as deferred outflows of resources and deferred inflows of resources related to pensions will be recognized in pension expense (reduction of pension expense) as follows:

Year Ended December 31,	
2019	\$ 40,244
2020	29,426
2021	(3,047)
2022	(2,154)
2023	-
Thereafter	<u>-</u>
Total	<u>\$ 64,469</u>

Actuarial Assumptions

The total pension liability (asset) in the June 30, 2018 actuarial valuation was determined using the following actuarial assumptions, applied to all periods included in the measurement:

Inflation	2.25%
Salary Increases	Graded by years of service, from 6.50% at entry to 3.00% after 25 years of service
Discount Rate	6.50% net of plan investment expense

Butte-Meade Sanitary Water District
Notes to the Financial Statements
December 31, 2018

NOTE 6 - PENSION PLAN (CONTINUED)

Mortality rates were based on 97% of the RP-2014 Mortality Table, projected generationally with Scale MP-2016, white collar rates for females and total dataset rates for males. Mortality rates for disabled members were based on the RP-2014 Disabled Retiree Mortality Table projected generationally with Scale MP-2016.

Investment portfolio management is the statutory responsibility of the South Dakota Investment Council (SDIC), which may utilize the services of external money managers for management of a portion of the portfolio. SDIC is governed by the Prudent Man Rule (i.e., the council should use the same degree of care as a prudent man). Current SDIC investment policies dictate limits on the percentage of assets invested in various types of vehicles (equities, fixed income securities, real estate, cash, private equity, etc.). The long-term expected rate of return on pension plan investments was determined using a method in which best-estimate ranges of expected future real rates of return (expected returns, net of pension plan investment expense and inflation) are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighing the expected future real rates of return by the target asset allocation percentage and by adding expected inflation. Best estimates of real rates of return for each major asset class included in the pension plan's target asset allocation as of June 30, 2018 (see the discussion of the pension plan's investment policy) are summarized in the following table using geometric means:

<u>Asset Class</u>	<u>Target Allocation</u>	<u>Long-term Expected Real Rate of Return</u>
Global Equity	58.0%	4.8%
Fixed Income	30.0%	1.8%
Real Estate	10.0%	4.6%
Cash	<u>2.0%</u>	0.7%
Total	<u>100.0%</u>	

Discount Rate

The discount rate used to measure the total pension liability (asset) was 6.50%. The projection of cash flows used to determine the discount rate assumed that plan member contributions will be made at the current contribution rate and that matching employer contributions from will be made at rates equal to the member rate. Based on these assumptions, the pension plan's fiduciary net position was projected to be available to make all future benefit payments of current plan members. Therefore, the long-term expected rate of return on pension plan investments was applied to all periods of projected benefit payments to determine the total pension liability (asset).

Butte-Meade Sanitary Water District
Notes to the Financial Statements
December 31, 2018

NOTE 6 - PENSION PLAN (CONTINUED)

Sensitivity of Liability (Asset) to Changes in the Discount Rate

The following presents the District's proportionate share of net pension liability (asset) calculated using the discount rate 6.50%, as well as what the District's proportionate share of the net pension liability (asset) would be if it were calculated using a discount rate that is 1-percentage point lower (5.50%) or 1-percentage point higher (7.50%) than the current rate:

	1% Decrease	Current Discount Rate	1% Increase
District's Proportionate Share of the Net Pension Liability (Asset)	\$ 208,354	\$ (276)	\$ (169,985)

Pension Plan Fiduciary Net Position

Detailed information about the plan's fiduciary net position is available in the separately issued SDRS financial report.

NOTE 7 - RURAL DEVELOPMENT RESERVES

Cash held in Rural Development reserve accounts consists of funds set aside for debt service, repairs, replacements, improvements, and additions as approved by Rural Development.

NOTE 8 - RISK MANAGEMENT

The District purchases insurance for risks related to torts, thefts, or damage to property; errors and omissions of public officials; general workmen's compensation; and property insurance from commercial insurance carriers. The policies provide for a \$2.9 million limit on property and \$4 million limit on liability with a \$1 million umbrella policy. In prior years, settled claims resulting from these risks have not exceeded the District's liability coverage.

Unemployment Benefits - The 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. In prior years, settled claims have not exceeded the District's coverage.

NOTE 9 - SUBSEQUENT EVENTS

Subsequent to year-end, the State of South Dakota awarded the District a Drinking Water SRF Loan. The loan will not exceed \$413,000 and will require monthly payments including interest of 2.25% for a period of 20 years. The District will use the loan proceeds for line replacements. There are no commitments for construction as of the date of this report.

Subsequent events have been evaluated through the date of the independent auditor's report, which is the date the financial statements were available to be issued.

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REQUIRED SUPPLEMENTARY INFORMATION

**Butte-Meade Sanitary Water District
Schedule of Net Pension Liability (Asset)
For the Years Ended December 31**

Plan Year Ending	District's Proportion of Net Pension Liability/Asset	District's Proportionate Share of Net Pension Liability (Asset) (a)	District's Covered- employee Payroll (b)	District's Proportionate Share of Net Pension Liability (Asset) as a Percentage of its Covered- employee Payroll (a/b)	Plan Fiduciary Net Position a Percentage of the Total Pension Liability/Asset
6/30/2018	0.0118283%	\$ (276)	\$ 247,451	0.11%	100.02%
6/30/2017	0.0121510%	\$ (1,102)	\$ 243,562	0.45%	100.10%
6/30/2016	0.0124494%	\$ 42,053	\$ 236,725	17.76%	96.89%
6/30/2015	0.0141086%	\$ (59,839)	\$ 257,580	23.23%	104.10%

*The amounts presented for each year were determined as of the measurement date of the collective net pension liability (asset) which is 6/30.

See independent auditor's report.

**Butte-Meade Sanitary Water District
Schedule of Pension Contributions
For the Years Ended December 31**

Year Ending	Contractually- required Contribution (a)	Contributions in Relation to the Contractually- required Contribution (b)	Contribution Deficiency (Excess) (a-b)	District's Covered- employee Payroll (c)	Contributions as a Percentage of Covered- employee Payroll (b/c)
12/31/2018	\$ 15,030	\$ 15,030	\$ -	\$ 250,507	6.00%
12/31/2017	\$ 14,739	\$ 14,739	\$ -	\$ 243,882	6.04%
12/31/2016	\$ 14,641	\$ 14,641	\$ -	\$ 244,016	6.00%
12/31/2015	\$ 14,081	\$ 14,081	\$ -	\$ 234,684	6.00%

See independent auditor's report.