

SOUTH WALTON UTILITY COMPANY, INC.

**FINANCIAL STATEMENTS AND
SUPPLEMENTARY INFORMATION**

SEPTEMBER 30, 2019 AND 2018



SOUTH WALTON UTILITY COMPANY, INC.
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SEPTEMBER 30, 2019 AND 2018

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INDEPENDENT AUDITORS' REPORT

To the Board of Directors
South Walton Utility Company, Inc.

We have audited the accompanying financial statements of South Walton Utility Company, Inc., which comprise the balance sheets as of September 30, 2019 and 2018, and the related statements of operations, members' equity and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with 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.

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. 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 auditors' 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 auditors consider 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 South Walton Utility Company, Inc. as of September 30, 2019 and 2018, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Supplementary Information

Our audits were conducted for the purpose of forming an opinion on the financial statements as a whole. The Statement of Operations – Comparison of Budget to Actual on page 22 is presented for purposes of additional analysis and is not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information, except for the portion marked unaudited, has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.

The statistical information on pages 23-27 has not been subjected to the auditing procedures applied in the audit of the basic financial statements, and, accordingly, we do not express an opinion or provide any assurance on it.

Warren Averett, LLC

Destin, Florida

November 21, 2019

SOUTH WALTON UTILITY COMPANY, INC.
BALANCE SHEETS
SEPTEMBER 30, 2019 AND 2018

| ASSETS | 2019 | 2018 |
|---|----------------------|----------------------|
| UTILITY PLANT IN SERVICE, NET (See Note 2) | \$ 56,971,566 | \$ 57,788,121 |
| RESTRICTED AND DESIGNATED ASSETS | | |
| Cash and cash equivalents – designated (See Note 1) | 1,464,751 | 403,771 |
| Cash and cash equivalents – restricted (See Note 1) | 18,168 | 142,018 |
| Investments – designated (See Note 4) | 3,344,363 | 2,965,077 |
| Investments – restricted (See Note 4) | 1,420,585 | 1,215,990 |
| Total restricted and designated assets | 6,247,867 | 4,726,856 |
| CURRENT ASSETS | | |
| Cash and cash equivalents | 2,176,396 | 2,203,048 |
| Accounts receivable, net | 1,134,542 | 1,118,188 |
| Other receivables | 80,985 | 100,796 |
| Due from other utility companies (See Note 6) | 254,083 | 245,488 |
| Prepaid expenses | 127,974 | 135,588 |
| Inventory | 279,144 | 275,918 |
| Total current assets | 4,053,124 | 4,079,026 |
| OTHER ASSETS | | |
| Prepaid debt service deposit | 153,504 | 153,504 |
| Investment in WRP, Inc. (See Note 5) | 9,067,394 | 9,325,450 |
| Due from other utility companies (See Note 6) | 200,755 | 454,838 |
| Total other assets | 9,421,653 | 9,933,792 |
| TOTAL ASSETS | \$ 76,694,210 | \$ 76,527,795 |

See notes to the financial statements.

SOUTH WALTON UTILITY COMPANY, INC.
BALANCE SHEETS – CONTINUED
SEPTEMBER 30, 2019 AND 2018

| | 2019 | 2018 |
|--|----------------------|----------------------|
| LIABILITIES AND MEMBERS' EQUITY | | |
| MEMBERS' EQUITY | | |
| Contributions in aid of construction | | |
| Designated for future expansion | \$ 1,730,945 | \$ 624,618 |
| Undesignated | 56,822,827 | 56,322,827 |
| Accumulated amortization | (27,279,282) | (25,853,596) |
| Retained earnings | | |
| Undesignated | 29,181,081 | 27,699,308 |
| Total members' equity | 60,455,571 | 58,793,157 |
| LONG-TERM LIABILITIES | | |
| Customer deposits | 362,300 | 344,250 |
| Loan deposits | 395,419 | 385,175 |
| Prepaid tap fees | 516,432 | 530,957 |
| Due to WRP, Inc. (See Note 5) | 3,698,069 | 3,936,096 |
| Notes payable, net (See Note 7) | 1,258,581 | 1,930,187 |
| RUA debt obligation, net (See Note 8) | 7,401,385 | 8,067,971 |
| Total long-term liabilities | 13,632,186 | 15,194,636 |
| CURRENT LIABILITIES | | |
| Accounts payable | 108,969 | 132,200 |
| Contracts payable | 95,165 | - |
| Retainage payable | 58,448 | 185,234 |
| Other payable WRP true-up | 890 | 237 |
| Due to WRP, Inc. (See Note 5) | 223,780 | 218,422 |
| Accrued wages and benefits | 136,835 | 131,885 |
| Notes payable (See Note 7) | 682,364 | 660,151 |
| RUA debt obligation (See Note 8) | 679,886 | 660,212 |
| Accrued interest payable | 620,116 | 551,661 |
| Total current liabilities | 2,606,453 | 2,540,002 |
| TOTAL LIABILITIES | 16,238,639 | 17,734,638 |
| TOTAL LIABILITIES AND MEMBERS' EQUITY | \$ 76,694,210 | \$ 76,527,795 |

See notes to the financial statements.

SOUTH WALTON UTILITY COMPANY, INC.
STATEMENTS OF OPERATIONS
FOR THE YEARS ENDED SEPTEMBER 30, 2019 AND 2018

| | <u>2019</u> | <u>2018</u> |
|-----------------------------------|----------------------------|----------------------------|
| REVENUE FROM OPERATIONS | \$ 9,778,066 | \$ 9,637,839 |
| OPERATING EXPENSES | | |
| Operating and maintenance | 6,703,288 | 6,435,536 |
| Depreciation and amortization | <u>1,267,318</u> | <u>1,257,602</u> |
| Total operating expenses | <u>7,970,606</u> | <u>7,693,138</u> |
| OPERATING INCOME | <u>1,807,460</u> | <u>1,944,701</u> |
| OTHER REVENUES (EXPENSES) | | |
| Loss from investment in WRP, Inc. | (272,792) | (272,790) |
| Interest income | 116,148 | 72,295 |
| Interest expense | (410,173) | (448,536) |
| Miscellaneous income | 225,831 | 218,294 |
| Gain on disposal of assets | <u>15,299</u> | <u>30,479</u> |
| Total other revenues (expenses) | <u>(325,687)</u> | <u>(400,258)</u> |
| NET INCOME | <u><u>\$ 1,481,773</u></u> | <u><u>\$ 1,544,443</u></u> |

See notes to the financial statements.

**SOUTH WALTON UTILITY COMPANY, INC.
STATEMENTS OF MEMBERS' EQUITY
FOR THE YEARS ENDED SEPTEMBER 30, 2019 AND 2018**

| | <u>2019</u> | <u>2018</u> |
|---|-----------------------------|-----------------------------|
| CONTRIBUTIONS IN AID OF CONSTRUCTION | | |
| Beginning balance | \$ 31,093,849 | \$ 31,647,575 |
| Tap contributions | 1,606,328 | 871,951 |
| Amortization | <u>(1,425,687)</u> | <u>(1,425,677)</u> |
| Ending balance | <u>31,274,490</u> | <u>31,093,849</u> |
| RETAINED EARNINGS | | |
| Beginning of year | 27,699,308 | 26,154,865 |
| Net income | <u>1,481,773</u> | <u>1,544,443</u> |
| End of year | <u>29,181,081</u> | <u>27,699,308</u> |
| TOTAL MEMBERS' EQUITY | <u><u>\$ 60,455,571</u></u> | <u><u>\$ 58,793,157</u></u> |

See notes to the financial statements.

SOUTH WALTON UTILITY COMPANY, INC.
STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED SEPTEMBER 30, 2019 AND 2018

| | <u>2019</u> | <u>2018</u> |
|--|---------------------|---------------------|
| CASH FLOWS FROM OPERATING ACTIVITIES | | |
| Cash received from customers | \$ 10,025,404 | \$ 9,904,565 |
| Interest income | 116,148 | 72,295 |
| Cash paid to suppliers and customers | (6,716,528) | (6,360,012) |
| Interest expense | <u>(341,718)</u> | <u>(379,769)</u> |
| Net cash provided by operating activities | <u>3,083,306</u> | <u>3,237,079</u> |
| CASH FLOWS FROM INVESTING ACTIVITIES | | |
| Acquisition and construction of utility plant in service | (1,871,167) | (2,375,295) |
| Loan deposits | 10,244 | 1,488 |
| Investment in WRP, Inc. | (247,405) | (252,799) |
| Proceeds from due from other utility companies | 245,488 | 237,184 |
| Proceeds from held-to-maturity investments | 2,140,000 | 2,350,000 |
| Purchase of held-to-maturity investments | <u>(2,721,428)</u> | <u>(3,457,686)</u> |
| Net cash flows used in investing activities | <u>(2,444,268)</u> | <u>(3,497,108)</u> |
| CASH FLOWS FROM FINANCING ACTIVITIES | | |
| Principal payments on notes payable | (662,063) | (79,517) |
| Principal payments on RUA debt obligation | (658,300) | (1,200,257) |
| Capital contributed by members | <u>1,591,803</u> | <u>852,651</u> |
| Net cash provided by (used in) financing activities | <u>271,440</u> | <u>(427,122)</u> |
| NET CHANGE IN CASH | 910,478 | (687,151) |
| CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR | <u>2,748,837</u> | <u>3,435,988</u> |
| CASH AND CASH EQUIVALENTS AT END OF YEAR | <u>\$ 3,659,315</u> | <u>\$ 2,748,837</u> |
| COMPOSITION OF CASH AND CASH EQUIVALENTS: | | |
| Restricted | \$ 18,168 | \$ 142,018 |
| Designated | 1,464,751 | 403,771 |
| Unrestricted | <u>2,176,396</u> | <u>2,203,048</u> |
| TOTAL CASH AND CASH EQUIVALENTS | <u>\$ 3,659,315</u> | <u>\$ 2,748,837</u> |

See notes to the financial statements.

SOUTH WALTON UTILITY COMPANY, INC.
STATEMENTS OF CASH FLOWS – CONTINUED
FOR THE YEARS ENDED SEPTEMBER 30, 2019 AND 2018

| | <u>2019</u> | <u>2018</u> |
|---|---------------------|---------------------|
| CASH FLOWS FROM OPERATING ACTIVITIES | | |
| Net income | \$ 1,481,773 | \$ 1,544,443 |
| Adjustments to reconcile net income to net cash flows from operating activities: | | |
| Depreciation and amortization | 1,267,318 | 1,257,602 |
| Gain on disposal of assets | (15,299) | (30,479) |
| Loss from investment in WRP, Inc. | 272,792 | 272,790 |
| (Increase) decrease in operating assets: | | |
| Accounts receivable | (16,354) | (61,410) |
| Other receivables | 19,811 | 87,612 |
| Other receivable – WRP true-up | - | 445 |
| Prepaid expenses | 7,614 | 3,623 |
| Inventory | (3,226) | 24,827 |
| Increase (decrease) in operating liabilities: | | |
| Accounts payable | (23,231) | 27,739 |
| Other payable – WRP true-up | 653 | 237 |
| Customer deposits | 18,050 | 22,230 |
| Accrued wages and benefits | 4,950 | 18,653 |
| Accrued interest payable | 68,455 | 68,767 |
| Net cash flows provided by operating activities | <u>\$ 3,083,306</u> | <u>\$ 3,237,079</u> |

See notes to the financial statements.

SOUTH WALTON UTILITY COMPANY, INC.
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2019 AND 2018

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES AND DESCRIPTION OF BUSINESS

Background

South Walton Utility Company, Inc., (hereinafter referred to as the Company), was organized on August 9, 1968, as a not-for-profit corporation to provide water and sewer services to the residents of South Walton County. The Company has qualified under Internal Revenue Code Section 501(c)(12) as an exempt organization and, as such, is not liable for income taxes. By Florida Statute, the Company is also exempt from sales tax and Ad Valorem taxes.

The Company's operations are located in South Walton County, Florida, and its customers are located primarily in South Walton County and the surrounding areas. The Company's major source of revenue is derived from water and sewer services to customers in this area.

The Company has joint operations with Destin Water Users, Inc. (DWU) pertaining to water supply and water line capacity.

Basis of Accounting

The Company prepares its financial statements on the accrual basis of accounting. The Company recognizes revenue for services as they are billed monthly to members; connection fees are deferred and capitalized until they are used; and capital contributions are recorded as equity when received and are amortized over the life of the related improvement.

Utility Plant in Service and Depreciation

Property, plant and equipment are recorded at cost when acquired by purchase, at estimated fair market value when donated or at developer cost when contributed. Depreciation is computed using the straight-line method over the estimated useful lives of the assets. Useful lives range from six to forty-five years.

Restricted and Designated Cash and Investments

Cash and investments have been restricted pursuant to the requirements of the Florida Department of Environmental Protection Loan Fund, to meter deposits held for customers and by agreement for the Wellfield Project.

The Board has designated cash and investments for future water and sewer expansion needs, emergency reserves, operating reserves and renewal and replacement reserves. Designated cash at September 30, 2019 and 2018, was \$1,464,751 and \$403,771, respectively. Investment securities designated for future expansion correspond to the amount of designated capital for future expansion in Members' Equity.

Investment restrictions and designations are detailed within Note 4.

Cash and Cash Equivalents

For purposes of the statements of cash flows, the Company considers all funds received and deposited in operating and money market bank accounts and debt securities purchased within three months of maturity to be cash equivalents.

SOUTH WALTON UTILITY COMPANY, INC.
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2019 AND 2018

**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES AND DESCRIPTION OF BUSINESS
– CONTINUED**

Investments

Management determines the appropriate classification of investment securities at the time they are acquired and evaluates the appropriateness of such classifications at each balance sheet date. All of the investments held by the Company, which consist of certificates of deposit and money market funds, are classified as held-to-maturity and reported at cost.

Equity Method Investment

The Company maintains a 50% investment in WRP, Inc., which it accounts for by using the equity method. The 50% interest is carried at cost and is adjusted for the Company's proportionate share of the undistributed earnings and losses, in accordance with the equity method of accounting for investments.

Customer Receivables

Customer receivables are due the first business day of the month following receipt of billings. If an account is not paid by the second business day of the month following billings, a late fee of 10% of the current unpaid water and sewer charges is assessed. If an account is 60 days in arrears, a door hanger is sent to contact the Company by a specified date, or the account is subject to disconnection. If not contacted, the meter is locked. If the account is not paid by six months after the meter is locked, the account is final billed. If the final bill is not paid, 30-day and 60-day letters are sent. Following the 60-day letter, the account is sent to a commercial collection agency.

For the year ended September 30, 2019, there were 74 accounts written off totaling \$6,041. For the year ended September 30, 2018, there were 90 accounts written off totaling \$4,618.

Management has determined the allowance for doubtful accounts by doing an analysis of prior period write-offs. Annually, the Board approves writing off accounts deemed uncollectible. The allowance for doubtful accounts was \$11,700 at September 30, 2019 and 2018.

Inventory

Inventories are priced at the lower of cost or net realizable value using the first in, first out (FIFO) method. The inventory of operating supplies is reported using the consumption method under which operating supplies are expensed, and additions to the system are recorded as the supplies are used.

Contributions in Aid of Construction

This account represents the total amount or value of contributions received from customers and/or developers, including other utility companies in the form of money to be used for capital improvements and/or facilities to be used in operations of the water and sewer system. Contributions are reported net of the related cost and are amortized over the life of the improvement or the length of the related agreement. Amortization of contributions in aid of construction is credited to depreciation expense.

**SOUTH WALTON UTILITY COMPANY, INC.
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2019 AND 2018**

**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES AND DESCRIPTION OF BUSINESS
– CONTINUED**

Debt Issue Costs

Issue costs for the State of Florida revolving loans are deferred and amortized over the term of the debt using the straight-line method. Issue costs are included as a reduction to reported debt, net of any accumulated amortization. Accumulated amortization of debt issue costs was \$311,758 and \$287,700 at September 30, 2019 and 2018, respectively.

The following is a summary of debt issue costs as of September 30, 2019 and 2018:

| | 2019 | 2018 |
|-------------------------------|-------------|-------------|
| Debt issue costs | \$ 481,182 | \$ 481,182 |
| Less accumulated amortization | (311,758) | (287,700) |
| | \$ 169,424 | \$ 193,482 |

Customer Deposits

This account represents deposits made by customers utilizing water and sewer services provided by the Company. The liability is funded by restricted investments.

Loan Deposits

This account represents deposits made by Destin Water Users for their representative portion of the sinking fund required by the state loan from the Florida Department of Environmental Protection. The monies are held as restricted investments.

Prepaid Tap Fees

Prepaid tap fees consist of payments made by individuals, businesses and developers for future water and/or sewer connection fees under the terms of contracts between the parties and the Company.

Annual and Sick Leave

Annual leave is earned from date of hire, but may not be utilized until the employee has completed one year of service. Employees earn annual leave at the rate of eight (8) hours per month of employment, up to 10 years. From 10 to 15 years, annual leave is accrued at fifteen (15) days per year. From 15 to 20 years of service, annual leave is accrued at twenty (20) days per year. After 20 years of service, employees earn twenty-five (25) days per year. An employee may not accrue more than one hundred sixty (160) hours earned annual leave into the next calendar year.

The policy of the Company is that full-time employees will accrue sick leave at a rate of eight (8) hours per month. Upon termination, no sick leave will be compensated; therefore, no accrual for sick leave has been recorded.

**SOUTH WALTON UTILITY COMPANY, INC.
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2019 AND 2018**

**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES AND DESCRIPTION OF BUSINESS
– CONTINUED**

Use of 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 certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

Reclassifications

Certain amounts presented in the prior year have been reclassified in order to be consistent with the current year presentation.

Events Occurring after Reporting Date

The Company has evaluated events and transactions that occurred between September 30, 2019, and November 21, 2019, which is the date that the financial statements were available to be issued, for possible recognition or disclosure in the financial statements.

2. UTILITY PLANT IN SERVICE

Annual provisions for depreciation, net of amortization, of Utility Plant In Service total \$1,267,318 (depreciation of \$2,693,005 net of amortization of \$1,425,687) and \$1,257,602 (depreciation of \$2,683,279 net of amortization of \$1,425,677) for 2019 and 2018, respectively.

The following is a summary of Utility Plant in Service as of September 30, 2019 and 2018:

| | <u>2019</u> | <u>2018</u> |
|---------------------------------|----------------------|----------------------|
| Land | \$ 2,266,624 | \$ 2,266,624 |
| Plant | 82,798,254 | 82,461,852 |
| Buildings | 5,735,677 | 5,735,677 |
| Computer equipment and software | 303,633 | 378,001 |
| Furniture and fixtures | 102,535 | 84,646 |
| Equipment | 1,486,387 | 1,484,933 |
| Vehicles | 670,759 | 636,050 |
| Construction in progress | <u>6,980,609</u> | <u>5,655,806</u> |
| | 100,344,478 | 98,703,589 |
| Less accumulated depreciation | <u>(43,372,912)</u> | <u>(40,915,468)</u> |
| | <u>\$ 56,971,566</u> | <u>\$ 57,788,121</u> |

SOUTH WALTON UTILITY COMPANY, INC.
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2019 AND 2018

3. CONCENTRATIONS OF CREDIT RISK

The Company has a sweep arrangement with a local financial institution in which its deposits are swept overnight into a separate account and thus are not exposed to credit risk for exceeding FDIC insured limits. A total of \$2,860,000 and \$1,590,000 were held in the sweep account at September 30, 2019 and 2018, respectively. There is credit risk associated with the arrangement; however, this risk is mitigated by all the securities under the arrangement consisting of fully collateralized federal agency securities and United States Treasury securities. In addition, investments under this arrangement are subject to interest rate risk, resulting from fluctuations in interest rates.

The Company maintains its restricted and designated cash and investments within brokerage accounts. The investments that consist of certificates of deposit are fully insured by the FDIC. Restricted and designated cash balances also consist of governmental and U.S. Treasury Securities. These funds are not necessarily insured by the FDIC; however, they consist of repurchase agreements that are fully collateralized by U.S. Treasury securities or deposited in qualifying trust and/or cash accounts with major U.S. banks, as well as high quality, short-term securities that are issued or guaranteed by the U.S. government or by U.S. government agencies or instrumentalities, which mitigates credit risk. As of September 30, 2019, cash held within brokerage accounts totaled \$1,485,373.

**SOUTH WALTON UTILITY COMPANY, INC.
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2019 AND 2018**

4. INVESTMENTS

Investments are recorded at cost, classified as held-to-maturity and consist of the following at September 30:

| | <u>2019</u> | <u>2018</u> |
|--|---------------------|---------------------|
| Due within one year | \$ 2,448,001 | \$ 2,426,181 |
| Due after one year through three years | <u>2,316,947</u> | <u>1,754,886</u> |
| Total held-to-maturity investments | <u>\$ 4,764,948</u> | <u>\$ 4,181,067</u> |
| Federal Agency Securities | \$ 1,924,310 | \$ 1,528,589 |
| U.S. Treasury | 968,651 | 318,021 |
| Certificates of deposit | <u>1,871,987</u> | <u>2,334,457</u> |
| Total investments | <u>4,764,948</u> | <u>4,181,067</u> |
| Less amounts designated: | | |
| Amount designated for operating reserves | (1,613,421) | (2,340,470) |
| Amount designated for future expansion | <u>(1,730,942)</u> | <u>(624,607)</u> |
| Total investments – designated | <u>(3,344,363)</u> | <u>(2,965,077)</u> |
| Less amounts restricted: | | |
| Amount restricted for customer deposits | (362,300) | (344,250) |
| Amount restricted for loan repayment | (876,263) | (731,926) |
| Amount restricted for plant construction | <u>(182,022)</u> | <u>(139,814)</u> |
| Total investments – restricted | <u>(1,420,585)</u> | <u>(1,215,990)</u> |
| Total available investments – unrestricted | <u>\$ -</u> | <u>\$ -</u> |

**SOUTH WALTON UTILITY COMPANY, INC.
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2019 AND 2018**

5. INVESTMENT IN WRP, INC. AND AMOUNT DUE TO WRP, INC.

In 1996, the Company and DWU formed WRP, Inc. (WRP), a not-for-profit organization incorporated in the State of Florida, for the purpose of acquiring land and developing well fields and pipelines capable of providing potable water to the Company and DWU. The Company accounts for its 50% ownership interest in WRP using the equity method of accounting in accordance with generally accepted accounting principles. In 2011, WRP began the Phase IV Water System Improvements, General Brown Wellfield Transmission Main Project, (hereinafter referred to as the Phase IV Project). The Phase IV Project was completed and placed into service during 2013. The cost of the Phase IV Project was shared equally between the Company and DWU.

The construction costs associated with the Phase IV Project were funded through a State Revolving Funds Loan (SRF Loan) through the Florida Department of Environmental Protection (FDEP) for \$16,000,000 obtained by WRP, as well as contributions from the Company and from DWU. Based on the agreement with DWU, the Company's portion of the SRF loan for the Phase IV Project is 37.2%. The SRF loan bears interest at 2.5% and is payable in semiannual principal and interest payments of \$449,742. The SRF loan is secured by pledged revenues of the Company and DWU. As of September 30, 2019, WRP had total principal outstanding of \$10,334,847 on the SRF loan, of which \$3,921,849 is the responsibility of the Company.

The Company's share of costs incurred on the Phase IV Project, including its share of the balances of the SRF Loan and line of credit, are recognized as an increase to the Company's investment in WRP. As of September 30, 2019, the Company owed WRP \$3,921,849, which includes the Company's share of the SRF loan and accrued interest. As of September 30, 2018, the Company owed WRP \$4,154,518 for costs associated with the Phase IV Project, which included the Company's share of WRP's SRF loan, loan service fees and accrued interest for the project. The amounts due to WRP by the Company are tied to the related debt on WRP's books and accordingly, have corresponding maturities, which are summarized as follows at September 30, 2019:

| | <u>Amount</u> |
|------------------------|---------------------|
| 2020 | \$ 223,780 |
| 2021 | 244,027 |
| 2022 | 250,166 |
| 2023 | 256,459 |
| 2024 | 262,911 |
| Thereafter | <u>2,684,506</u> |
| Total due to WRP, Inc. | <u>\$ 3,921,849</u> |

**SOUTH WALTON UTILITY COMPANY, INC.
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2019 AND 2018**

5. INVESTMENT IN WRP, INC. AND AMOUNT DUE TO WRP, INC. – CONTINUED

During the year ended September 30, 2019, the Company contributed \$14,736 to WRP related to the costs of the Phase IV project and recognized its share of WRP's net loss of \$272,792. During the year ended September 30, 2018, the Company contributed \$22,648 to WRP related to the costs of the Phase IV project and recognized its 50% share of WRP's net loss of \$272,791. The Company's investment in WRP totaled \$9,067,394 and \$9,325,450 at September 30, 2019 and 2018, respectively.

The following is a summary of the Company's investment in WRP, Inc. as of September 30, 2019 and 2018:

| | <u>2019</u> | <u>2018</u> |
|-------------------------------------|---------------------|---------------------|
| Beginning balance | \$ 9,325,450 | \$ 9,572,402 |
| Contributions to WRP, Inc. | 14,736 | 22,648 |
| Amortization of contributed capital | (233,064) | (233,064) |
| WRP, Inc. net loss | (39,728) | (39,727) |
| Prior year true-up adjustment | - | 3,191 |
| SWUCI Investment in WRP, Inc. | <u>\$ 9,067,394</u> | <u>\$ 9,325,450</u> |

**SOUTH WALTON UTILITY COMPANY, INC.
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2019 AND 2018**

5. INVESTMENT IN WRP, INC. AND AMOUNT DUE TO WRP, INC. – CONTINUED

The Company's investment in WRP is accounted for under the equity method of accounting. Pertinent financial information for WRP, Inc. as of September 30 is as follows:

Balance Sheets

| | 2019 | 2018 |
|--------------------------------|---------------|---------------|
| ASSETS | | |
| Cash | \$ 323,853 | \$ 294,380 |
| Other receivable – SWU true-up | 890 | 237 |
| Due from SWUCI | 3,921,849 | 4,154,518 |
| Due from DWU | 6,609,972 | 7,002,119 |
| Property and equipment, net | 17,710,891 | 18,241,108 |
| Total assets | \$ 28,567,455 | \$ 29,692,362 |
| LIABILITIES | | |
| Accrued interest payable | \$ 36,700 | \$ 37,997 |
| Other payable – DWU true-up | 890 | 237 |
| SRF loan payable | 10,334,847 | 10,941,410 |
| Contributed Capital – DWU | 8,806,139 | 9,026,055 |
| Contributed capital – SWU | 8,745,909 | 8,964,238 |
| Retained earnings | 642,970 | 722,425 |
| Total liabilities and equity | \$ 28,567,455 | \$ 29,692,362 |

Statements of Operations and Gains

| | Year ended 2019 | Year ended 2018 |
|--|----------------------------|----------------------------|
| Revenue | \$ 14,134 | \$ 14,052 |
| Expenses | (93,589) | (93,505) |
| Excess of revenues over expenses | (79,455) | (79,453) |
| Company's share of excess of WRP, Inc. (50%) | | |
| Net loss | (39,728) | (39,727) |
| Less amortization of contributed capital | (233,064) | (233,064) |
| Company's recognized loss on investment in WRP, Inc. | \$ (272,792) | \$ (272,790) |

**SOUTH WALTON UTILITY COMPANY, INC.
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2019 AND 2018**

6. DUE TO/FROM OTHER UTILITY COMPANIES

The Company has recorded amounts due from DWU for their share of the Florida Department of Environmental Protection loan (see Note 7) acquired by the Company for the Phase I Water Supply Project. The debt bears interest ranging from 3.05% to 3.52%. Interest payments received by the Company from DWU are netted with the interest expense paid by the Company on the debt for income statement presentation. Additionally, there is a long-term and short-term amount.

| | 2019 | 2018 | 2019 | 2018 |
|--------------------------|-------------------|-------------------|------------------|------------------|
| | Short-term | Short-term | Long-term | Long-term |
| Due from DWU for Phase I | \$ 254,083 | \$ 245,488 | \$ 200,755 | \$ 454,838 |

7. NOTES PAYABLE

Capitalization Grants for Drinking Water State Revolving Fund

The Company obtained a \$6,302,378 20-year revolving note in 2000 from the Florida Department of Environmental Protection (FDEP) to fund the majority of the Phase I Water Supply Project. The note bears interest at a rate of 3.52% and is secured by pledged revenues. In 2001, the Company amended the note, providing additional funding for the Water Supply Project in the amount of \$1,251,087. The note amendment bears interest at a rate of 3.05%. The total amount of the note from the FDEP was \$7,553,465. The Company began repaying the note on December 15, 2001. Principal and interest payments of \$267,525 are due semiannually on June 15 and December 15, with a final installment equal to the remaining principal and interest balance due on June 15, 2021. The loan agreement requires that the Company maintain a loan repayment reserve account in the amount of \$498,519. As of September 30, 2019, the balance of the reserve account was \$791,776 and is included in restricted cash and investments on the balance sheet. The outstanding note balances at September 30, 2019 and 2018, were \$1,025,229 and \$1,511,981, respectively.

The Company obtained a \$3,021,280 20-year revolving note in 2003 from the FDEP to fund the Company's share of the Phase II Water Supply Project. The note bears interest at a rate of 2.96% and is secured by pledged revenues. The Company began repaying the note on February 15, 2005. Principal and interest payments of \$102,655 are due semiannually on August 15 and February 15, with a final installment equal to the remaining principal and interest balance due on August 15, 2024. The loan agreement requires that the Company maintain a loan repayment reserve account in the amount of \$102,655. As of September 30, 2019, the balance of the reserve account was \$102,655, which is included in restricted investments on the balance sheet. The outstanding note balances at September 30, 2019 and 2018, were \$947,707 and \$1,121,106, respectively.

**SOUTH WALTON UTILITY COMPANY, INC.
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2019 AND 2018**

7. NOTES PAYABLE – CONTINUED

| | 2019 | 2018 | 2019 | 2018 |
|-----------------------------------|-------------------|-------------------|---------------------|---------------------|
| | Short-term | Short-term | Long-term | Long-term |
| SRL Phase I | \$ 503,794 | \$ 486,751 | \$ 521,435 | \$ 1,025,229 |
| SRL Phase II | 178,570 | 173,399 | 769,137 | 947,707 |
| Total note payable for SRL | 682,364 | 660,150 | 1,290,572 | 1,972,936 |
| Less unamortized debt issue costs | - | - | (31,991) | (42,749) |
| Total note payable for SRL, net | <u>\$ 682,364</u> | <u>\$ 660,150</u> | <u>\$ 1,258,581</u> | <u>\$ 1,930,187</u> |

Combined maturities of the FDEP notes are as follows:

| | |
|------|---------------------|
| 2020 | \$ 682,364 |
| 2021 | 705,329 |
| 2022 | 189,378 |
| 2023 | 195,025 |
| 2024 | 200,840 |
| | <u>\$ 1,972,936</u> |

8. RUA DEBT OBLIGATION

In 2009, the Company obtained a \$10,000,000, 20-year revolving note from the FDEP to fund the majority of the Wastewater Treatment Facility Project. The loan was obtained by Regional Utility Authority (RUA) on the Company's behalf in exchange for the Company's deeding of the land and the facility over to RUA. The Company has leased the land and facility back from RUA in what has been deemed to be a capital lease transaction, since the assets revert back to the Company at the end of the lease term. Therefore, the land and buildings have not been removed from the financial statements of the Company. In December 2009, the RUA loan agreement with FDEP was amended to increase the funding to \$13,300,000.

The \$10,000,000 portion of the note bears interest at a rate of 3.01%, and the \$3,300,000 portion bears interest at a rate of 2.87%, and is secured by pledged revenues. Principal and interest payments of \$458,886 are due semiannually on February 15 and August 15, with a final installment equal to the remaining principal and interest balance due on February 15, 2030. The outstanding note balances at September 30, 2019 and 2018, were \$8,218,704 and \$8,878,916, respectively.

**SOUTH WALTON UTILITY COMPANY, INC.
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2019 AND 2018**

8. RUA DEBT OBLIGATION – CONTINUED

| | <u>2019</u> <u>Short-term</u> | <u>2018</u> <u>Short-term</u> | <u>2019</u> <u>Long-term</u> | <u>2018</u> <u>Long-term</u> |
|-----------------------------------|----------------------------------|----------------------------------|---------------------------------|---------------------------------|
| Note payable for RUA | \$ 679,886 | \$ 660,212 | \$ 7,538,818 | \$ 8,218,704 |
| Less unamortized debt issue costs | - | - | (137,433) | (150,733) |
| Total note payable for RUA, net | <u>\$ 679,886</u> | <u>\$ 660,212</u> | <u>\$ 7,401,385</u> | <u>\$ 8,067,971</u> |

Maturities of the RUA debt obligation are as follows:

| | <u>Amount</u> |
|------------|---------------------|
| 2020 | \$ 679,886 |
| 2021 | 700,147 |
| 2022 | 721,011 |
| 2023 | 742,496 |
| 2024 | 764,622 |
| Thereafter | <u>4,610,542</u> |
| | <u>\$ 8,218,704</u> |

9. RETIREMENT PLAN

The Company has a 401(k) retirement plan covering all employees who have completed one year of service. The Company matches employee contributions up to 8%.

The Company may also contribute a discretionary amount, which amount, if any, shall be deemed an Employer Non-Elective Contribution based on three groups of participants. The participant groups are based on the individual employee's length of service with the Company and are as follows:

| <u>Group</u> | <u>Years of Service</u> |
|--------------|-------------------------|
| A | 1-10 |
| B | 10-20 |
| C | more than 20 |

The Company's contributions for the years ended September 30, 2019 and 2018, were \$227,048 and \$203,330, respectively.

**SOUTH WALTON UTILITY COMPANY, INC.
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2019 AND 2018**

9. RETIREMENT PLAN – CONTINUED

The following table represents the vesting schedule of the Company's contributions:

| <u>Years of service</u> | <u>Vesting Percentages</u> |
|-----------------------------|--------------------------------|
| Less than 2 years | 0% |
| 2 years | 20% |
| 3 years | 40% |
| 4 years | 60% |
| 5 years | 80% |
| 6 years | 100% |

Forfeitures under the plan are used to reduce the Company's contribution in the succeeding year.

10. COMMITMENTS

Meter Upgrade Project

During November 2015, the Company entered into a contract to upgrade meters for a total contract amount of \$1,595,123. As of September 30, 2019, the Company had open contract commitments in the amount of \$173,818. The project is expected to be completed during the 2022 fiscal year.

Six Lane Utility Relocation Project

During November 2015, the Company entered into a contract for the purpose of the U.S. Highway 98 widening project for a total contract amount of \$3,896,559. As of September 30, 2019, the Company had open contract commitments in the amount of \$58,449. The project is expected to be completed during the 2020 fiscal year.

SUPPLEMENTARY INFORMATION

SOUTH WALTON UTILITY COMPANY, INC.
STATEMENT OF OPERATIONS – COMPARISON OF BUDGET TO ACTUAL
FOR THE YEAR ENDED SEPTEMBER 30, 2019

| | (Unaudited) Budget | Actual | Variance Favorable (Unfavorable) |
|-----------------------------------|-----------------------|---------------------|--|
| OPERATING REVENUES | | | |
| Water | \$ 4,542,407 | \$ 4,579,447 | \$ 37,040 |
| Sewer | 4,572,190 | 4,615,215 | 43,025 |
| Wholesale water | 385,000 | 394,516 | 9,516 |
| Other | 180,000 | 188,888 | 8,888 |
| Total operating revenues | <u>9,679,597</u> | <u>9,778,066</u> | <u>98,469</u> |
| OPERATING EXPENSES | | | |
| Bad debts | 10,000 | 4,929 | 5,071 |
| Chemicals | 138,500 | 136,915 | 1,585 |
| Contributions | 16,500 | 7,700 | 8,800 |
| Depreciation and amortization | 1,385,000 | 1,267,318 | 117,682 |
| Education and travel | 43,500 | 42,257 | 1,243 |
| Engineering and fees | 19,400 | 8,485 | 10,915 |
| G and A expense | 36,000 | 36,000 | - |
| Insurance – employees and other | 812,706 | 743,509 | 69,197 |
| Lab supplies | 37,500 | 31,811 | 5,689 |
| Legal and accounting | 76,700 | 55,894 | 20,806 |
| License and fees | 110,000 | 116,435 | (6,435) |
| Miscellaneous | 101,708 | 84,337 | 17,371 |
| Office expenses | 25,200 | 23,642 | 1,558 |
| Operating supplies | 352,200 | 447,813 | (95,613) |
| Payroll taxes | 187,328 | 181,778 | 5,550 |
| Professional fees | 205,000 | 288,232 | (83,232) |
| Repairs and maintenance | 1,154,000 | 1,019,493 | 134,507 |
| Retirement plans | 222,296 | 227,048 | (4,752) |
| Salaries | 2,580,000 | 2,472,638 | 107,362 |
| Telephone and sanitation | 78,800 | 74,701 | 4,099 |
| Uniforms | 26,585 | 14,693 | 11,892 |
| Utilities | 681,000 | 676,784 | 4,216 |
| WRP operating expenses | - | 8,194 | (8,194) |
| Total operating expenses | <u>8,299,923</u> | <u>7,970,606</u> | <u>329,317</u> |
| OPERATING INCOME | <u>1,379,674</u> | <u>1,807,460</u> | <u>427,786</u> |
| OTHER REVENUES (EXPENSES) | | | |
| Gain on disposal of assets | - | 15,299 | 15,299 |
| Loss from investment in WRP, Inc. | 25,000 | (272,792) | (297,792) |
| Interest income | 60,762 | 116,148 | 55,386 |
| Interest expense | (410,174) | (410,173) | 1 |
| Miscellaneous income | 109,963 | 225,831 | 115,868 |
| Total other revenues (expenses) | <u>(214,449)</u> | <u>(325,687)</u> | <u>(111,238)</u> |
| NET INCOME | <u>\$ 1,165,225</u> | <u>\$ 1,481,773</u> | <u>\$ 316,548</u> |

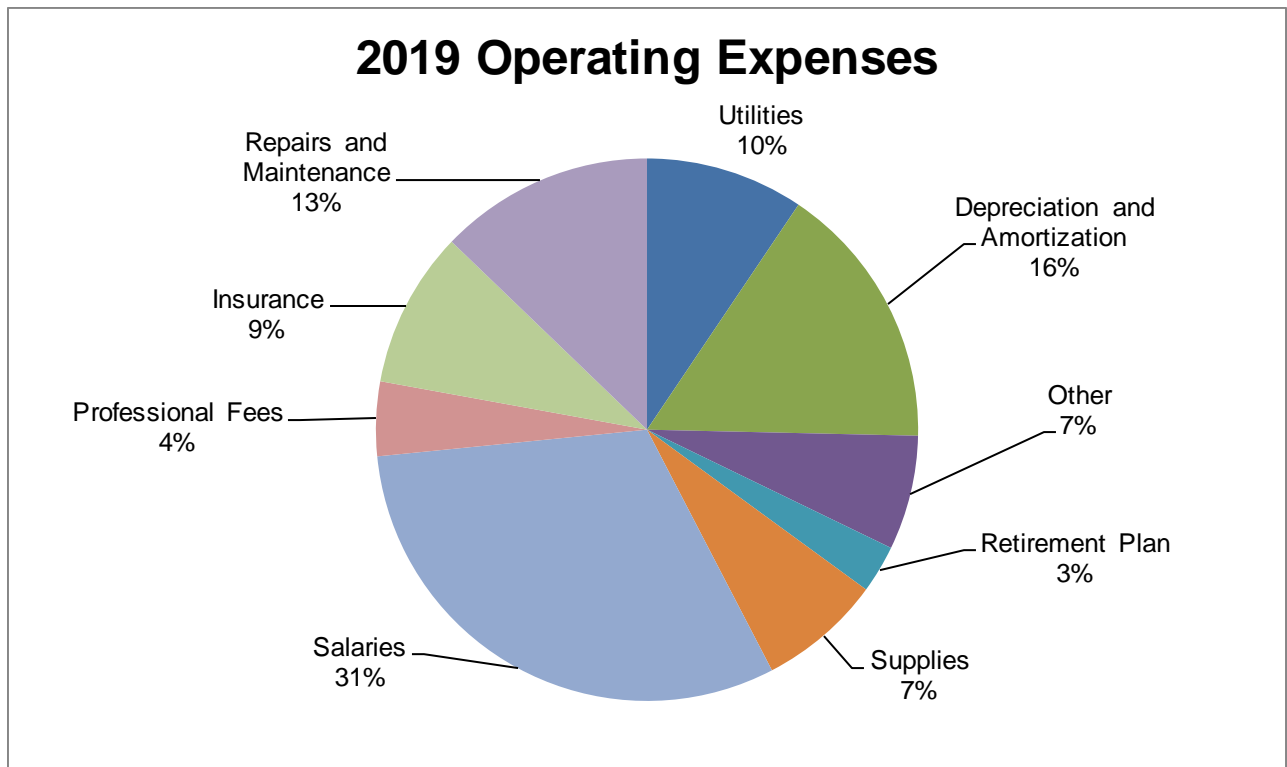
See independent auditors' report.

**SOUTH WALTON UTILITY COMPANY, INC.
STATISTICAL INFORMATION**

**Water and Sewer Consumption Analysis
(Unaudited)**

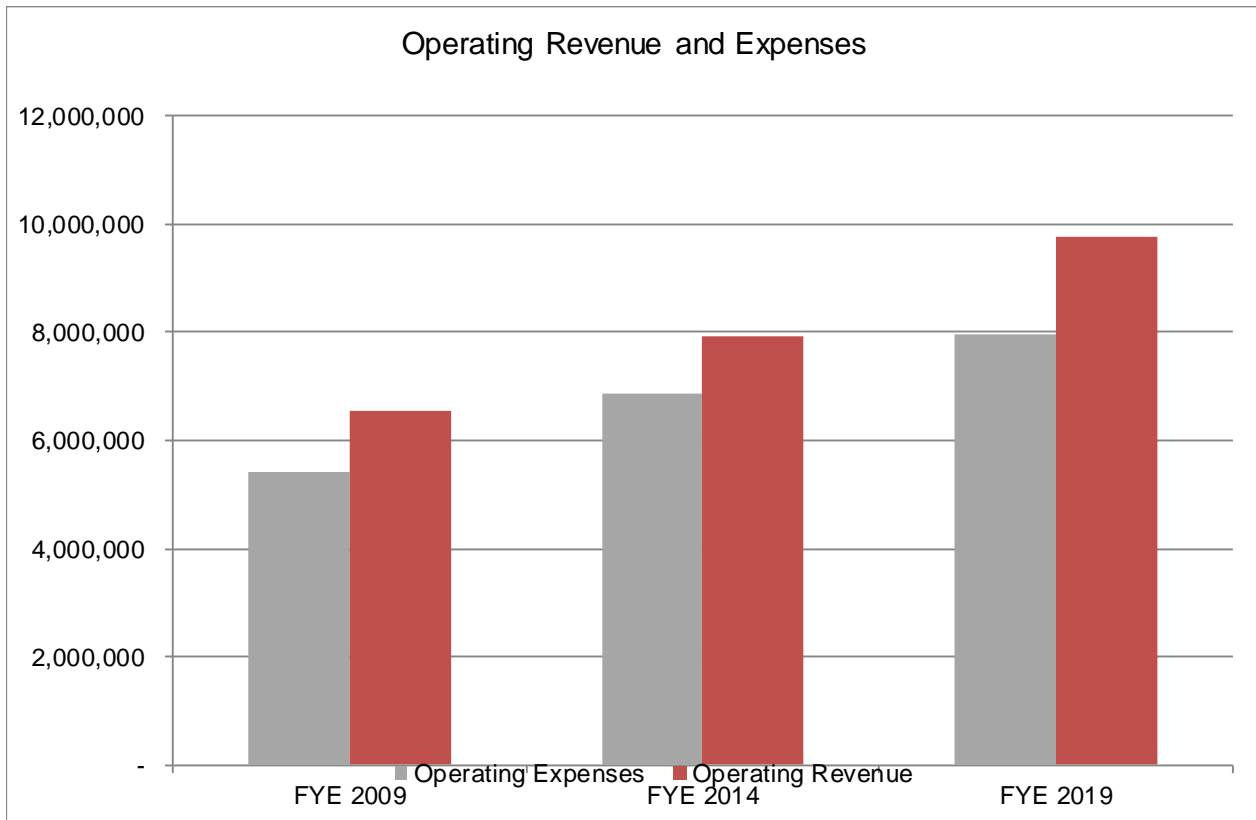
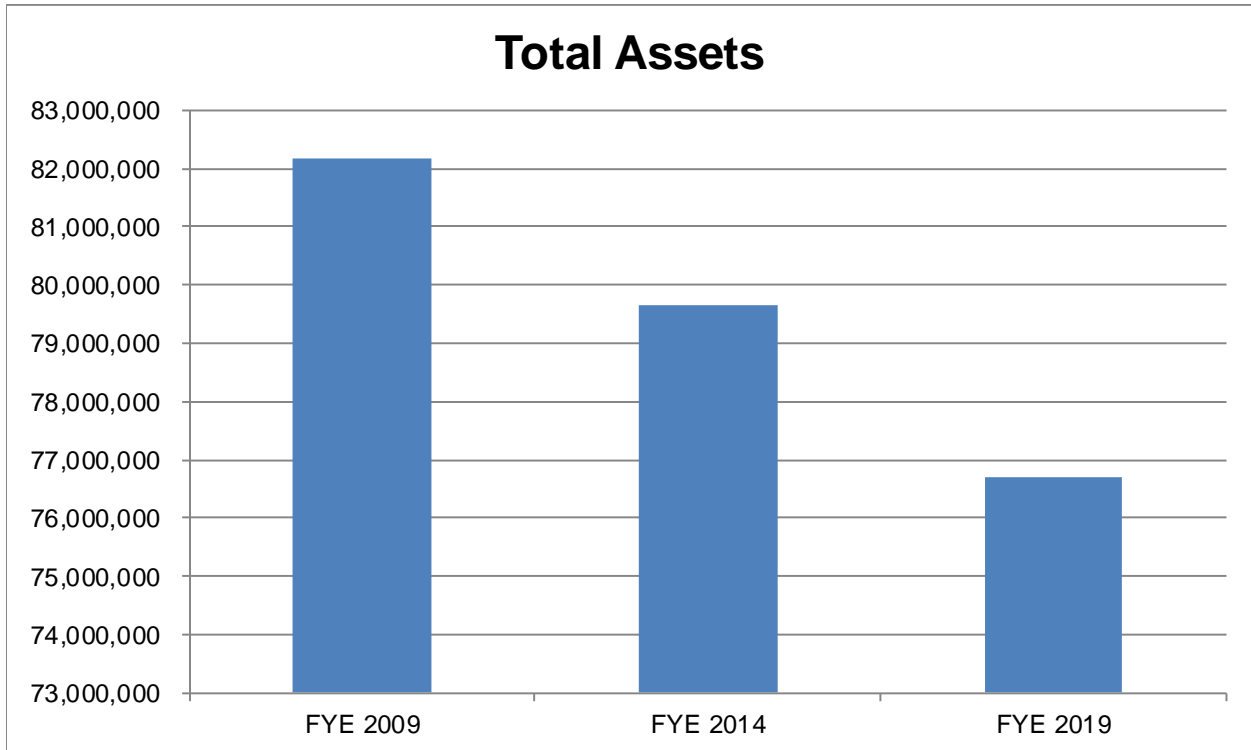
The table below compares total water consumption for fiscal years 2019 and 2018.

| | Fiscal Year 2019 | Fiscal Year 2018 |
|-------------------------|-----------------------------|-----------------------------|
| Water consumption | 1,108,904,000 | 1,101,377,000 |
| Wholesale water | 991,130,000 | 967,140,000 |
| Number of units – water | 18,467 | 18,087 |
| Number of units – sewer | 9,813 | 9,588 |
| Number of members | 9,947 | 9,801 |



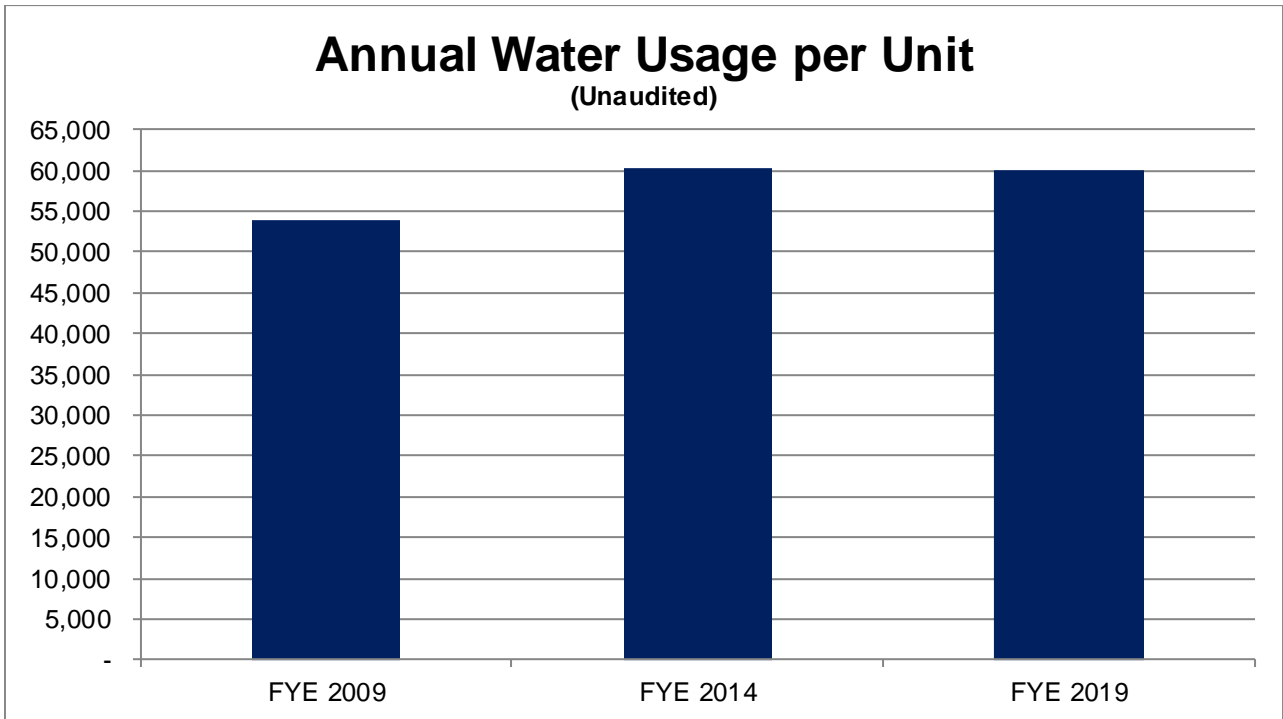
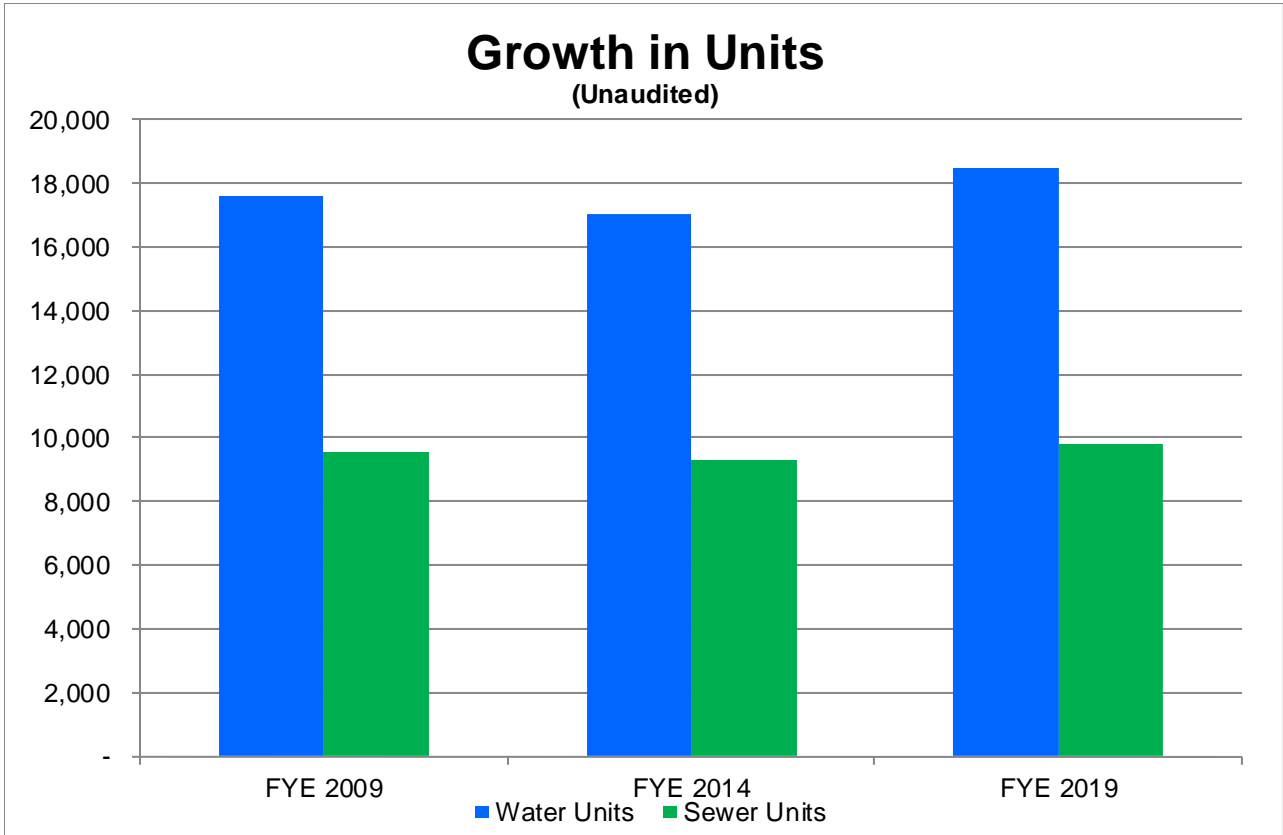
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**SOUTH WALTON UTILITY COMPANY, INC.
STATISTICAL INFORMATION – CONTINUED**



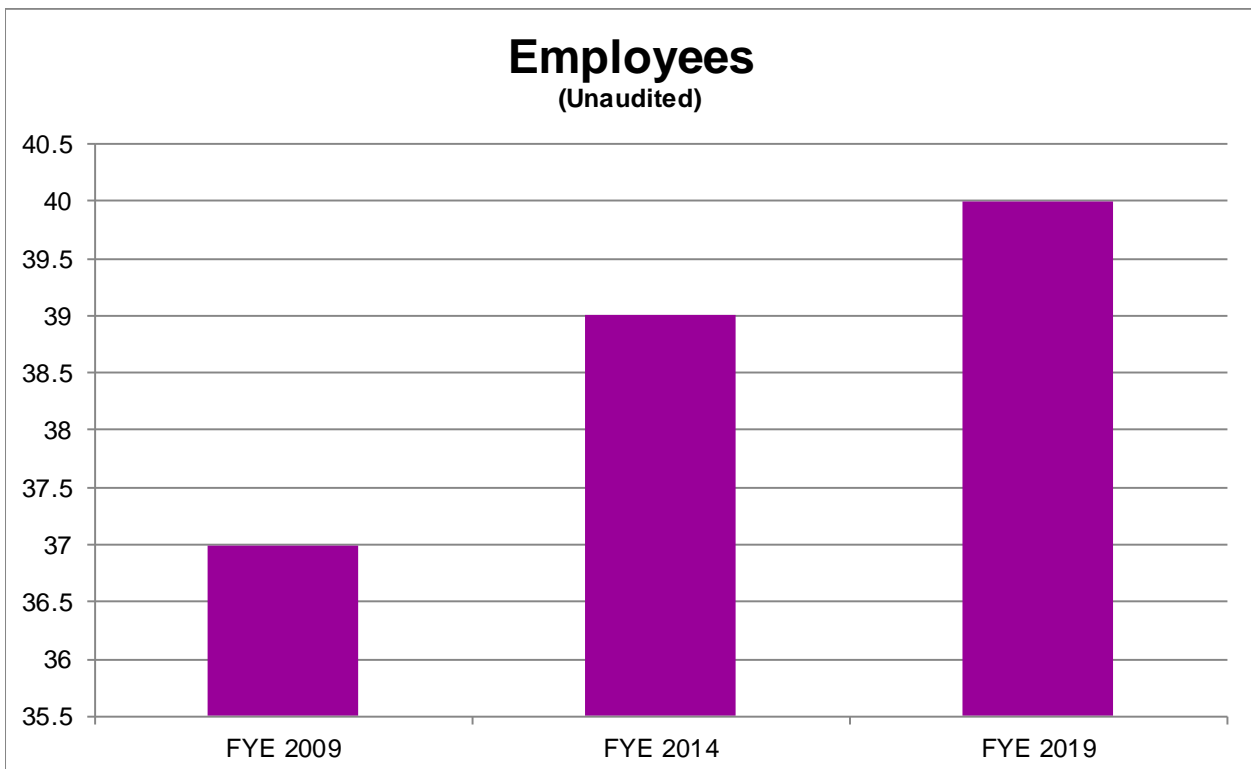
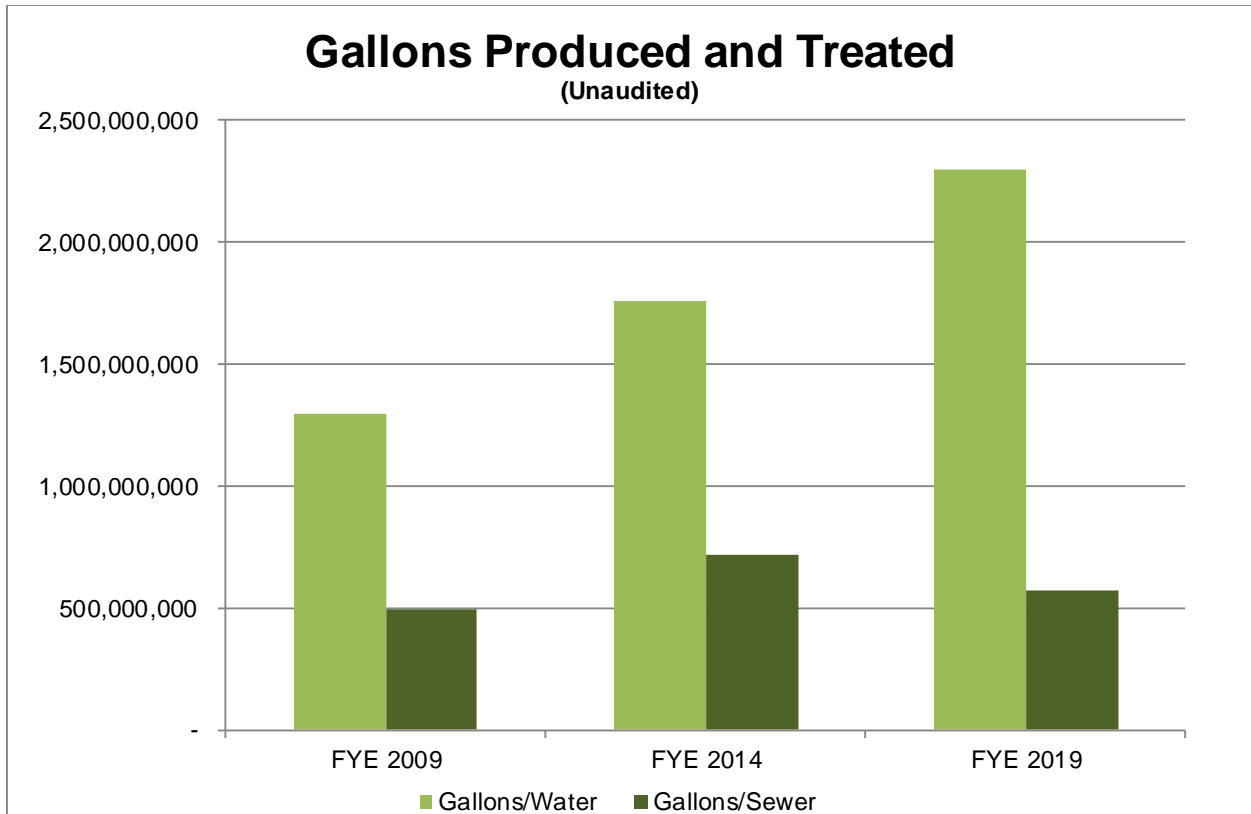
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**SOUTH WALTON UTILITY COMPANY, INC.
STATISTICAL INFORMATION – CONTINUED**



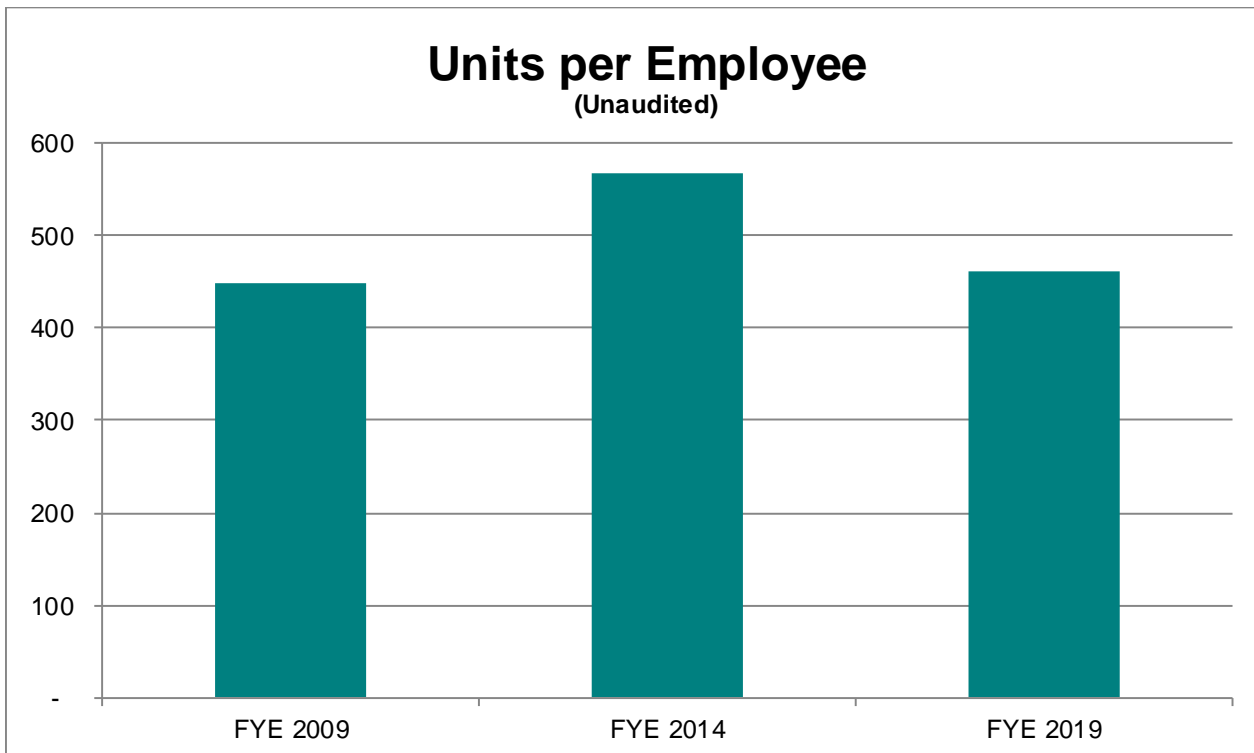
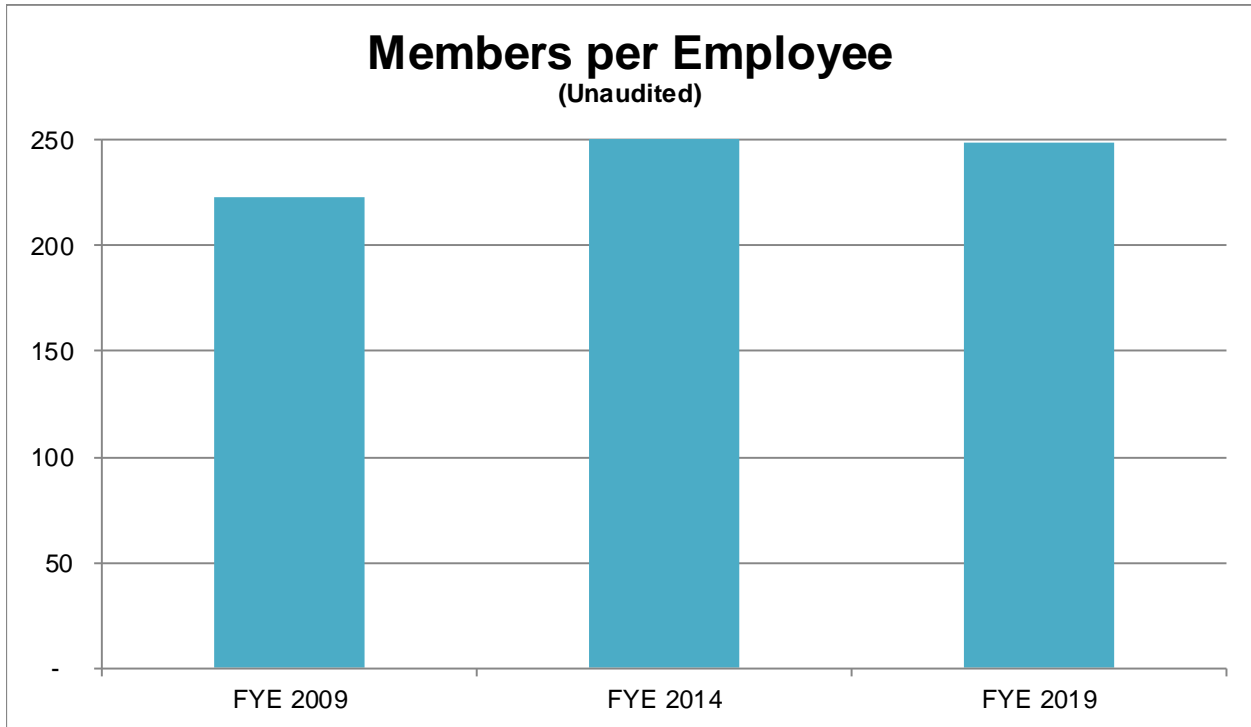
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**SOUTH WALTON UTILITY COMPANY, INC.
STATISTICAL INFORMATION – CONTINUED**



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**SOUTH WALTON UTILITY COMPANY, INC.
STATISTICAL INFORMATION – CONTINUED**



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