



DOWNINGTOWN MUNICIPAL WATER AUTHORITY
(A Component Unit of the Borough of Downingtown)
DOWNINGTOWN, PENNSYLVANIA

BASIC FINANCIAL STATEMENTS
AND SUPPLEMENTARY INFORMATION

DECEMBER 31, 2018

DOWNTOWN MUNICIPAL WATER AUTHORITY
DOWNTOWN, PENNSYLVANIA
(A Component Unit of Borough of Downingtown)

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INDEPENDENT AUDITOR'S REPORT

June 27, 2019

To the Board of Directors
Downingtown Municipal Water Authority
Downingtown, Pennsylvania

Report on the Financial Statements

We have audited the accompanying financial statements of the Downingtown Municipal Water Authority ("the Authority"), a component unit of Borough of Downingtown, Downingtown, Pennsylvania, as of and for the year ended December 31, 2018, and the related notes to the financial statements, which collectively comprise the Authority'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.

To the Board of Directors
Downingtown Municipal Water Authority

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 the Downingtown Municipal Water Authority, Downingtown, Pennsylvania, as of December 31, 2018, and the respective changes in financial position and cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 4 through 8 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 Information

Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise the Authority's financial statements. The combining schedule of net position; combining schedule of revenues, expenses, and changes in net position; and schedule of operating revenues and expenses - budget to actual are presented for purposes of additional analysis and are not a required part of the basic financial statements. The combining schedule of net position; combining schedule of revenues, expenses and changes in net position; and schedule of operating revenues and expenses - budget to actual are the responsibility of management and were derived from and relate

To the Board of Directors
Downingtown Municipal Water Authority

directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the combining schedule of net position; combining schedule of revenues, expenses, and changes in net position; and schedule of operating revenues and expenses - budget to actual are fairly stated, in all material respects, in relation to the basic financial statements as a whole.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated June 27, 2019, on our consideration of the Authority's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Authority's internal control over financial reporting and compliance.

Barbacane, Thornton & Company LLP
BARBACANE, THORNTON & COMPANY LLP

DOWNINGTOWN MUNICIPAL WATER AUTHORITY
(A Component Unit of the Borough of Downingtown)
MANAGEMENT'S DISCUSSION AND ANALYSIS – UNAUDITED
DECEMBER 31, 2018

Our discussion and analysis of the Downingtown Municipal Water Authority's ("the Authority") financial performance provides an overview of the Authority's financial activities for the year ended December 31, 2018. Please read it in conjunction with the Authority's financial statements that begin on page 9 and the accompanying notes to those statements. Responsibility for both the accuracy of the presented data and the thoroughness of the presentation rests with the Authority. We believe that the data, as presented herein, is accurate in all material respects and presented in a manner designed to fairly set forth the financial position and results of operations of the Authority. We believe that all disclosures necessary to enable the reader to gain the maximum understanding of the Authority's financial affairs have been included.

Profile of the Downingtown Municipal Water Authority

The Downingtown Municipal Water Authority, a component unit of the Borough of Downingtown, is a water authority incorporated on July 13, 1987, under the provisions of the Pennsylvania Municipality Authorities Act of 1945, as amended, pursuant to the ordinance of the Council of the Borough of Downingtown, Chester County, Pennsylvania. The Authority was formed principally to acquire, hold, construct, improve, maintain, own, and operate a water system for the Borough of Downingtown and other territories it may be authorized to serve. The Authority's Board is empowered with legislative functions that include enacting ordinances and resolutions, adopting a budget, and establishing water rates.

FINANCIAL HIGHLIGHTS

- The net position (assets minus liabilities) of the Authority as of December 31, 2018 was \$8,017,178. Of this amount, \$4,304,388 is unrestricted and is available to meet the Authority's ongoing obligations in accordance with the Authority's policies. In comparison, the Authority's net position at December 31, 2017 was \$6,345,491.
- The Authority's net position increased by \$1,671,951 or 26.3 percent in 2018, compared to \$1,047,322 or 19.8 percent for the year ended December 31, 2017.
- The Authority's total assets were \$15,005,525 at December 31, 2018, compared to \$14,355,126 at December 31, 2017.
- The Authority's total liabilities were \$6,988,347 at December 31, 2018, compared to \$8,009,635 at December 31, 2017.
- Revenue for the year ended December 31, 2018 totaled \$4,796,976 compared to \$4,389,077 for the year ended December 31, 2017. The major sources of revenue for the Authority were water revenue charges, penalties, and fees.

DOWNINGTOWN MUNICIPAL WATER AUTHORITY
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MANAGEMENT'S DISCUSSION AND ANALYSIS – UNAUDITED (CONT'D)
DECEMBER 31, 2018

- Expenses for the year ended December 31, 2018 totaled \$3,125,025, compared to \$3,341,755 for the year ended December 31, 2017. The major expenses for the Authority were chemical supplies, insurance, repairs and maintenance, salaries, utilities, depreciation, and interest.
- The Authority's long-term debt outstanding at December 31, 2018 was \$6,661,650, compared to \$7,648,085 at December 31, 2017.

OVERVIEW OF THE FINANCIAL STATEMENTS

The financial statements are designed to provide readers with a broad overview of the Authority's finances in a manner similar to private-sector businesses. The following statements are included:

Statement of Net Position: This statement reports all financial and capital resources for the Authority. The statement is presented in the format wherein assets equal liabilities and net position. Assets and liabilities are presented in order of liquidity and are classified as "current" (convertible into cash within one year) and "noncurrent" (long-term). The focus of the statement of net position is the "unrestricted net position" that is designed to represent the net available liquid (noncapital) assets, net of liabilities, for the entire Authority. Net position is reported in three broad categories:

- **Net Investment in Capital Assets:** This component of net position consists of all capital assets, reduced by the outstanding balances of any bonds, mortgages, notes, or other borrowings that are attributed to the acquisition, construction, or improvement of those assets.
- **Restricted Net Position:** This component of net position consists of restricted assets when constraints are placed on the asset by creditors (such as debt covenants), grantors, contributors, laws, regulations, etc. The Authority has no restricted net position.
- **Unrestricted Net Position:** This component of net position consists of net position that does not meet the definition of "net investment in capital assets," or "restricted net position."

Statement of Revenues, Expenses, and Changes in Net Position: This statement reports the Authority's operating and non-operating revenue, by major sources, along with operating and non-operating expenses.

Statement of Cash Flows: This statement discloses net cash provided by and used for the operating activities, investing activities, and from capital and related financing activities.

Notes to the Financial Statements: The notes to the financial statements provide additional information that is essential to a full understanding of the data provided in the financial statements.

Supplementary Information: The Authority presents a combining schedule of net position, combining schedule of revenues, expenses, and changes in net position, and schedule of operating revenues and expenses - budget to actual for additional information.

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MANAGEMENT'S DISCUSSION AND ANALYSIS – UNAUDITED (CONT'D)
DECEMBER 31, 2018

FINANCIAL ANALYSIS OF THE AUTHORITY AS A WHOLE

Condensed Comparative Financial Statements

Analysis of Statement of Net Position

Total Net Position for the year ended December 31, 2018 was \$8,017,178 and for the year ended December 31, 2017, the amount was \$6,345,491. This represents an overall net increase of \$1,671,687 or 26.3 percent.

Current Assets increased by \$461,275, or 11.1 percent, during 2018 primarily due to an increase in cash and cash equivalents and accounts receivable.

Capital Assets decreased by \$189,388, or 1.9 percent, during 2018. This decrease is primarily due to current year additions exceeding depreciation expense.

Current Liabilities decreased by \$166,169, or 13.3 percent, during 2018. This is primarily due to a decrease in the current portion of long-term debt.

Noncurrent Liabilities decreased by \$855,119, or 12.7 percent, during 2018. This was mainly due to the payments made on long-term debt.

The table below illustrates our analysis:

	<u>2018</u>	<u>2017</u>
Current assets	\$ 4,631,349	\$ 4,170,074
Capital assets, net	<u>10,374,440</u>	<u>10,185,052</u>
Total Assets	<u>15,005,789</u>	<u>14,355,126</u>
Current liabilities	1,087,631	1,253,800
Noncurrent liabilities	<u>5,900,716</u>	<u>6,755,835</u>
Total Liabilities	<u>6,988,347</u>	<u>8,009,635</u>
Net Position:		
Net position invested in capital assets	3,712,790	2,536,967
Unrestricted	<u>4,304,652</u>	<u>3,808,524</u>
Total Net Position	<u>\$ 8,017,442</u>	<u>\$ 6,345,491</u>

DOWNINGTOWN MUNICIPAL WATER AUTHORITY
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MANAGEMENT'S DISCUSSION AND ANALYSIS – UNAUDITED (CONT'D)
DECEMBER 31, 2018

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

Total revenues increased by \$407,899 when comparing 2018 to 2017. Operating revenues totaled \$4,781,201, representing an increase of \$399,513, or 9.12 percent, compared to 2017. Water revenues, which is the primary source of revenue for the Authority, represents \$4,722,157 or 99 percent of operating revenues. The remaining year 2018 operating revenue is comprised of penalties and miscellaneous fees of \$59,044. Non-operating revenues totaled \$15,775, an increase of \$8,386 from 2017.

Total expenses decreased by \$216,730 when comparing 2018 to 2017. Operating expenses totaled \$2,844,001, a decrease of \$219,486 or 7.2 percent, compared to 2017. Water system expenses of \$2,255,070 represents 72 percent of total operating expenses. Non-operating expenses, which consists of entirely interest expense, totaled \$281,024, an increase of \$2,756 from 2017.

The table below illustrates our analysis:

	<u>2018</u>	<u>2017</u>
Operating revenues	\$ 4,781,201	\$ 4,381,688
Non-operating revenues	15,775	7,389
Total Revenues	<u>4,796,976</u>	<u>4,389,077</u>
Operating expenses	2,844,001	3,063,487
Non-operating expenses	281,024	278,268
Total Expenses	<u>3,125,025</u>	<u>3,341,755</u>
Change in Net Position	<u>\$ 1,671,951</u>	<u>\$ 1,047,322</u>

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets

The Authority's investment in capital assets as of December 31, 2018 amounted to \$10,374,440 (net of accumulated depreciation). This is an increase of \$189,388, or 1.9 percent, from 2017. This investment in capital assets includes land, land improvements, construction-in-progress, furniture and equipment, water system, and water plant assets. Capital acquisitions are valued at historical cost or estimated historical cost if actual cost is not available. Donated capital assets are valued at their estimated fair value on the date of donation.

Major capital asset transactions/events during the year ended December 31, 2018 included upgrades to the Authority's control system in the amount of \$472,970.

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MANAGEMENT'S DISCUSSION AND ANALYSIS – UNAUDITED (CONT'D)
DECEMBER 31, 2018

Additional information on capital assets can be found in Note 4 to the financial statements.

Debt Administration

At December 31, 2018, the Authority's total amount of outstanding debt was \$6,661,650 compared to \$7,648,085 in 2017.

Additional information about the Authority's long-term debt can be found in Note 5 of this report.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES

The 2019 budget, as adopted by the Authority Board, provides the necessary resources for the Authority to achieve its goals and priorities. The Authority expects to see similar revenue to last year in the upcoming year. Operating expenses are expected to decrease by approximately \$209,000, or twenty-one percent, due to decreased maintenance costs. The Authority's budget maintained accustomed service levels and represents an accurate estimate in dollar terms of its commitment to deliver quality services to its customers. Economic conditions of the Authority are expected to remain stable, and the Authority continues to work on its capital improvement plan.

REQUESTS FOR INFORMATION

This financial report is designed to provide our citizens, customers, investors, and creditors with a general overview of the Authority's finances and to show the Authority's accountability for the funds it receives and disburses. If you have any questions about this report or need additional information, please contact the Authority's Executive Director at the Downingtown Municipal Water Authority, 100 Water Plant Way, Downingtown, PA 19335.

DOWNINGTOWN MUNICIPAL WATER AUTHORITY
(A Component Unit of the Borough of Downingtown)
STATEMENT OF NET POSITION
DECEMBER 31, 2018

ASSETS	
Current Assets:	
Cash and cash equivalents	\$ 2,370,857
Investments	164,320
Accounts receivable	1,991,595
Prepaid expenses	43,633
Inventory	60,944
Total Current Assets	<u>4,631,349</u>
Noncurrent Assets:	
Land	468,785
Construction-in-progress	712,695
Capital assets, net of depreciation	9,192,960
Total Noncurrent Assets	<u>10,374,440</u>
TOTAL ASSETS	<u>\$ 15,005,789</u>
LIABILITIES AND NET POSITION	
LIABILITIES	
Current Liabilities:	
Accounts payable	\$ 80,529
Accrued payroll liabilities	38,970
Accrued interest	57,195
Pension payable	17,916
Escrows	132,087
Bond and notes payable, net	760,934
Total Current Liabilities	<u>1,087,631</u>
Noncurrent Liabilities:	
Bond and notes payable, net	<u>5,900,716</u>
Total Noncurrent Liabilities	<u>5,900,716</u>
TOTAL LIABILITIES	<u>6,988,347</u>
NET POSITION	
Net investment in capital assets	3,712,790
Unrestricted	4,304,652
TOTAL NET POSITION	<u>8,017,442</u>
TOTAL LIABILITIES AND NET POSITION	<u>\$ 15,005,789</u>

The accompanying notes are an integral part of these financial statements.

DOWNINGTOWN MUNICIPAL WATER AUTHORITY
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STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET POSITION
FOR THE YEAR ENDED DECEMBER 31, 2018

OPERATING REVENUES	
Water revenues	\$ 4,722,157
Penalties and miscellaneous	59,044
TOTAL OPERATING REVENUES	<u>4,781,201</u>
OPERATING EXPENSES	
Water system	2,255,070
Administrative	588,931
TOTAL OPERATING EXPENSES	<u>2,844,001</u>
NET OPERATING INCOME	<u>1,937,200</u>
NONOPERATING REVENUES (EXPENSES)	
Interest income	15,775
Interest expense	<u>(281,024)</u>
TOTAL NONOPERATING EXPENSES	<u>(265,249)</u>
CHANGE IN NET POSITION	1,671,951
NET POSITION, BEGINNING OF YEAR	<u>6,345,491</u>
NET POSITION, END OF YEAR	<u><u>\$ 8,017,442</u></u>

The accompanying notes are an integral part of these financial statements.

DOWNINGTOWN MUNICIPAL WATER AUTHORITY
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STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED DECEMBER 31, 2018

CASH FLOWS FROM OPERATING ACTIVITIES:	
Cash receipts from customers	\$ 4,248,151
Cash paid to suppliers	(2,425,545)
NET CASH PROVIDED BY OPERATING ACTIVITIES	<u>1,822,606</u>
 CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES:	
Purchase of capital assets	(612,296)
Proceeds from long-term debt	5,525,000
Principal payment on long-term debt	(6,450,918)
Interest paid on long-term debt	(372,955)
NET CASH USED BY CAPITAL AND RELATED FINANCING ACTIVITIES	<u>(1,911,169)</u>
 CASH FLOWS FROM INVESTING ACTIVITIES:	
Interest income	15,775
NET CASH PROVIDED FROM INVESTING ACTIVITIES	<u>15,775</u>
 NET DECREASE IN CASH AND CASH EQUIVALENTS	 (72,788)
 CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR	 <u>2,443,645</u>
 CASH AND CASH EQUIVALENTS, END OF YEAR	 <u><u>\$ 2,370,857</u></u>
 RECONCILIATION OF OPERATING INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES:	
Operating income	\$ 1,937,200
Adjustments to reconcile operating income to net cash provided by operating activities:	
Depreciation expense	439,729
Decrease (Increase) in assets:	
Accounts receivable	(533,050)
Prepaid expenses	1,635
Inventory	(1,102)
Increase (Decrease) in liabilities:	
Accounts payable	(24,653)
Accrued payroll liabilities	2,581
Pension payable	(24,234)
Escrows	24,500
NET CASH PROVIDED BY OPERATING ACTIVITIES	<u><u>\$ 1,822,606</u></u>
 NONCASH CAPITAL AND RELATED FINANCING ACTIVITIES:	
Capital asset additions in accounts payable	<u><u>\$ 16,821</u></u>

The accompanying notes are an integral part of these financial statements.

DOWNTOWN MUNICIPAL WATER AUTHORITY
(A Component Unit of Borough of Downingtown)

NOTES TO FINANCIAL STATEMENTS

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The financial statements of the Downingtown Municipal Water Authority ("the Authority") have been prepared in conformity with generally accepted accounting principles ("GAAP") as applied to government units. The Governmental Accounting Standards Board ("GASB") is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. The significant accounting principles and policies utilized by the Authority are described below.

Reporting Entity

The Authority, a component unit of the Borough of Downingtown, is a water authority incorporated on July 13, 1987 under the provisions of the Pennsylvania Municipality Authorities Act of 1945, as amended, pursuant to the ordinance of the Council of the Borough of Downingtown, Chester County, Pennsylvania. The Authority was formed principally to acquire, hold, construct, improve, maintain, own, and operate a water system for the Borough of Downingtown and other territories it may be authorized to serve. The Authority's revenue base consists of residential and commercial customers in the Downingtown area.

Measurement Focus and Basis of Accounting and Financial Statement Presentation

The term "measurement focus" is used to denote what is being measured and reported in the Authority's operating statement. The Authority is accounted for on the flow of economic resources measurement focus. The fundamental objective of this focus is to measure whether the Authority is better or worse off economically as a result of events and transactions of the period.

The term "basis of accounting" is used to determine when a transaction or event is recognized on the Authority's operating statement. The Authority uses the accrual basis of accounting. Under this basis, revenues are recorded when earned and expenses are recorded when incurred, even though actual payment or receipt may not occur until after the period ends.

The Authority adheres to the provisions of the *GASB Codification of Governmental Accounting and Financial Reporting Standards* ("GASB Codification"). The Codification established standards for external financial reporting for all state and local governmental entities, which includes a statement of net position; a statement of revenues, expenses, and changes in net position; and a statement of cash flows. It requires the classification of net position into three components: net investment in capital assets, restricted, and unrestricted. These classifications are defined as follows:

Net investment in capital assets – This component of net position 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

DOWNTOWN MUNICIPAL WATER AUTHORITY
(A Component Unit of Borough of Downingtown)

NOTES TO FINANCIAL STATEMENTS

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont'd)

to the acquisition, construction, or improvement of those assets. If there are significant unspent related debt proceeds at year end, the portion of the debt attributable to the unspent proceeds is not included in the calculation of net investment in capital assets. Rather, that portion of the debt is included in the same net position component as the unspent proceeds.

Restricted – This component of net position consists of constraints placed on net position use through external constraints imposed by creditors (such as through debt covenants), grantors, contributors, or laws or regulations of other governments or constraints imposed by law through constitutional provisions or enabling legislation. It is comprised of assets, net of related liabilities, that are required to be set aside by revenue bond covenants for operations, maintenance, and renewal and replacements.

Unrestricted – This component of net position consists of net position that does not meet the definition of "restricted" or "net investment in capital assets." Administrative expenses are paid with the use of unrestricted resources.

All water revenues received must be disbursed as provided in the Trust Indenture, dated June 15, 2008, the First Supplemental Trust Indenture, dated July 20, 2016, securing the Promissory Note, Series of 2016, and the Second Supplemental Trust Indenture, dated September 4, 2018, securing the Guaranteed Water Revenue Note, Series of 2018. The Trust Indenture and First Supplemental Trust Indenture provide, among other things, for the creation of various subfunds which restrict financial activities to the following:

Operating Fund – Receipt of transfers from the Revenue Fund and Construction Fund to pay for the operating expenses incurred in connection with the water system.

Revenue Fund – Receipt of revenues from the water system to be disbursed for both debt service and operations and maintenance.

Debt Service Fund – Payment of bond principal and interest on the water revenue bonds.

Construction Fund – Funds set aside for use in construction projects.

Use of Estimates in the Preparation of Financial Statements

The preparation of financial statements in conformity with generally accepted accounting principles 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 revenues and expenses during the reporting period. Actual results could differ from those estimates.

DOWNTOWN MUNICIPAL WATER AUTHORITY
(A Component Unit of Borough of Downingtown)

NOTES TO FINANCIAL STATEMENTS

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont'd)

Cash and Cash Equivalents

Cash deposits consist of demand and time deposits and money market funds with financial institutions and are carried at cost. For purposes of the statement of cash flows, all cash deposits and highly liquid investments with an original maturity of three months or less when acquired are considered to be cash equivalents.

Investments

Investments consist of nonnegotiable certificates of deposit. The investments are recorded at amortized cost. Nonnegotiable certificates of deposit are nonparticipating interest earning investment contracts which are exempt from measurement at fair value.

Accounts Receivable

Accounts receivable are stated at the amount the Authority expects to collect. No provision has been made for uncollectible accounts since the Authority has the ability to lien customer properties for unpaid fees.

Revenues and Expenses

Revenues and expenses are distinguished between operating and nonoperating items. Operating revenues generally result from providing services in connection with the Authority's principal ongoing operations. The principal operating revenues of the Authority are lease rentals from the Borough of Downingtown and tapping fees.

Operating expenses include the costs associated with the engineering, administrative expenses, professional fees, and depreciation on capital assets. All revenues and expenses not meeting these definitions are reported as nonoperating revenues and expenses.

Use of Restricted/Unrestricted Net Position

When an expense is incurred for purposes for which both restricted and unrestricted net position is available, the Authority's policy is to apply restricted net position first.

Capital Assets

The Authority defines capital assets as assets with an estimated useful life in excess of one year. Capital assets of the Authority are recorded at either their actual cost or estimated historical cost. Donated assets are valued at their estimated fair value on the date donated. Depreciation of all exhaustible capital assets is charged as an expense against their operations. Depreciation is computed using the straight-line method over estimated asset lives as follows:

DOWNTOWN MUNICIPAL WATER AUTHORITY
(A Component Unit of Borough of Downingtown)

NOTES TO FINANCIAL STATEMENTS

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont'd)

Water system	20 - 40 years
Water plant	20 - 40 years
Land improvements	10 - 20 years
Furniture and equipment	5 - 20 years

NOTE 2 DEPOSITS AND INVESTMENTS

Major additions and betterments are capitalized while expenses for maintenance and repairs that do not add value to the asset or materially extend asset lives are charged to operations as incurred.

Deposits

Custodial Credit Risk

Custodial credit risk is the risk that in the event of a bank failure, the Authority's deposits may not be returned. The Authority does not have a policy for custodial credit risk on deposits. At December 31, 2018, the carrying amount of the Authority's deposits was \$2,370,857, and the bank balance was \$2,372,238. Of the bank balance, \$587,525 was covered by federal depository insurance, and the remaining \$1,784,713 was subject to custodial credit risk because it was fully collateralized by the banks holding the funds but not in the Authority's name.

Investments

Statutes authorize the Authority to invest in obligations of the U.S. Treasury; agencies and instrumentalities; deposits in savings accounts or time deposits or share accounts of institutions insured by the Federal Deposit Insurance Corporation ("FDIC"), the Federal Savings and Loan Insurance Corporation ("FSLIC"), or the National Credit Union Share Insurance Fund ("NCUSIF"). The Authority also is authorized to invest in obligations of the United States of America or any of its agencies or instrumentalities backed by the full faith and credit of the United States of America, or the Commonwealth of Pennsylvania or any of its agencies or instrumentalities.

As of December 31, 2018, the Authority had \$164,320 invested in certificates of deposit due within one year.

Interest Rate Risk

The Authority does not have an investment policy that limits investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates. At December 31, 2018, all of the Authority's investments had maturity dates of one year or less.

DOWNTOWN MUNICIPAL WATER AUTHORITY
(A Component Unit of Borough of Downingtown)

NOTES TO FINANCIAL STATEMENTS

NOTE 2 DEPOSITS AND INVESTMENTS (cont'd)

Custodial Credit Risk

For an investment, custodial credit risk is the risk that, in the event of the failure of the counterparty, the Authority will not be able to recover the value of its investments or collateral security that are in the possession of an outside party. As of December 31, 2018, none of the Authority's investments were subject to custodial credit risk.

Concentration and Credit Risk

The Authority does not have a policy that would limit the amount it may invest in any one issuer. As of December 31, 2018, all of the Authority's investments were in the form of certificates of deposit held by DNB First Bank and Citadel Federal Credit Union.

NOTE 3 ACCOUNTS RECEIVABLE

Accounts receivable consist of the following at December 31, 2018:

Utility billing	\$ 1,338,617
Escrow	11,588
Other	21,346
Unbilled revenue	620,044
	\$ 1,991,595

NOTE 4 CAPITAL ASSETS

The changes in capital assets for the year ended December 31, 2018 are as follows:

	Beginning Balance 01/01/18	Additions	Deletions	Reclass- ification	Ending Balance 12/31/18
Capital assets not being depreciated:					
Land	\$ 468,785	\$ -	\$ -	\$ -	\$ 468,785
Construction-in-progress	261,613	557,600	-	(106,518)	712,695
Total capital assets not being depreciated	730,398	557,600	-	(106,518)	1,181,480

DOWNTOWN MUNICIPAL WATER AUTHORITY
(A Component Unit of Borough of Downingtown)

NOTES TO FINANCIAL STATEMENTS

NOTE 4 CAPITAL ASSETS (cont'd)

	Beginning Balance 01/01/18	Additions	Deletions	Reclass- ification	Ending Balance 12/31/18
Capital assets being depreciated:					
Water plant	12,388,656	-	-	106,518	12,495,174
Water system	6,072,933	38,619	-	-	6,111,552
Land improvements	11,536	-	-	-	11,536
Furniture and equipment	617,387	32,898	-	-	650,285
Total capital assets being depreciated	19,090,512	71,517	-	106,518	19,268,547
Accumulated depreciation	(9,635,858)	(439,729)	-	-	(10,075,587)
Capital assets being depreciated, net	9,454,654	(368,212)	-	106,518	9,192,960
CAPITAL ASSETS, NET	\$10,185,052	\$ 189,388	\$ -	\$ -	\$10,374,440

NOTE 5 LONG-TERM DEBT

In June 2008, the Authority issued \$10,705,000 of term bonds which refinanced the outstanding Series A of 1998 Bonds and a construction loan. The bonds matured through 2026 with interest rates ranging from 3.00 percent to 4.75 percent. The bonds are guaranteed by the Borough of Downingtown. During the current year, the bonds were refunded with the issuance of the Guaranteed Water Revenue Note, Series of 2018.

In July 2016, the Authority obtained a \$2,000,000 Promissory Note for the purpose of financing a capital project. The Promissory Note, Series of 2016, with a maximum draw amount of \$2,000,000, calls for quarterly payments of principal and interest at 2.46 percent and matures July 2023. The note is collateralized by the security interest in the revenue of the Authority.

In September 2018, the Authority issued the \$5,525,000 Guaranteed Water Revenue Note, Series of 2018 to refund the outstanding Series of 2008 bonds. The bonds mature through 2026 with interest of 2.74 percent. The bonds are guaranteed by the Borough of Downingtown. The refunding of the bond resulted in a cash flow savings of \$227,131.

The Authority's Guaranteed Water Revenue Note and Promissory Note are secured by all assets of the Authority and the water revenue consumer base.

DOWNTOWN MUNICIPAL WATER AUTHORITY
(A Component Unit of Borough of Downingtown)

NOTES TO FINANCIAL STATEMENTS

NOTE 5 LONG-TERM DEBT (cont'd)

The following summarizes the changes in general long-term debt for the year ended December 31, 2018:

	Outstanding 01/01/18	Additions	Retirements	Outstanding 12/31/18	Amounts Due in One Year
Guaranteed Water Revenue Bonds, Series of 2008	\$ 6,125,000	\$ -	\$6,125,000	\$ -	\$ -
Promissory Note, Series of 2016	1,462,568	-	325,918	1,136,650	225,844
Bond premium	60,517	-	60,517	-	-
Guaranteed Water Revenue Note, Series of 2018	-	5,525,000	-	5,525,000	535,090
	<u>\$ 7,648,085</u>	<u>\$5,525,000</u>	<u>\$6,511,435</u>	<u>\$ 6,661,650</u>	<u>\$ 760,934</u>

Future scheduled maturities is as follows:

<u>Year Ending December 31,</u>	<u>Principal</u>	<u>Interest</u>
2019	\$ 760,934	\$ 203,302
2020	1,010,123	178,654
2021	1,039,511	145,665
2022	1,068,968	111,606
2023	982,714	76,462
2024-2026	1,799,400	78,807
Totals	<u>\$ 6,661,650</u>	<u>\$ 794,496</u>

The Authority is required to meet certain financial and non-financial covenants on an annual basis in accordance with the Promissory Note, Series of 2016 and Guaranteed Water Revenue Note, Series of 2018. The covenants include, among other items, a minimum debt service coverage ratio. At December 31, 2018, the Authority was in compliance with the minimum debt service coverage ratio for both Notes.

NOTE 6 PENSION PLAN

The Authority provides pension benefits for its employees through a single employer defined contribution pension plan. All full-time employees are eligible to participate in the plan. Full-

DOWNINGTOWN MUNICIPAL WATER AUTHORITY
(A Component Unit of Borough of Downingtown)

NOTES TO FINANCIAL STATEMENTS

NOTE 6 PENSION PLAN (cont'd)

time employment is defined as no less than 35 hours per week. Contributions are made by the Authority based upon a fixed percentage of each qualified employee's gross wages. The Authority contributes 7.0 percent to the plan. Employees do not contribute to the plan. The Authority's Board of Directors is responsible for establishing plan benefits, contributions, and other provisions, and for approving all plan amendments. The annual contribution to the plan for 2018 totaled \$51,166.

The following is a brief description of the plan:

Death Benefits – When a member dies prior to the commencement of his pension benefits, he is deemed fully vested, and his designated beneficiary shall be entitled to the entire vested interest. If a member dies after commencement of his benefits, the member's entire interest will be distributed to his beneficiaries under the member's selected distribution method.

Forfeitures – Forfeitures will remain assets of the plan to reduce future contributions by the Authority.

Vesting – Contributions vest after five years of service. Upon termination of employment, the employee receives a distribution of his entire vested interest at the end of the quarter during which termination occurs.

NOTE 7 DEFERRED COMPENSATION PLAN

Employees of the Authority may participate in a deferred compensation plan adopted under the provisions of the Internal Revenue Code. The deferred compensation plan is available to all employees of the Authority. Under the plan, employees may elect to defer a portion of their salaries and avoid paying federal taxes on the deferred portion until the withdrawal date. The deferred compensation amount is not available for withdrawal by employees until termination, retirement, death, or plan-defined unforeseeable emergency. Upon Board approval, the Authority may contribute to the employees' deferred compensation accounts. There were no contributions made in 2018.

NOTE 8 CAPITAL IMPROVEMENTS COMMITMENTS

The Authority has incurred costs totaling \$712,695 for project costs that are not under a formal contract as of December 31, 2018.

DOWNINGTOWN MUNICIPAL WATER AUTHORITY
(A Component Unit of Borough of Downingtown)

NOTES TO FINANCIAL STATEMENTS

NOTE 9 RESERVATION OF NET POSITION

As of December 31, 2018, the Authority has \$79,702 in unrestricted net position which the Authority Board has set aside for debt payments. In addition, the Authority Board has also set aside \$130,222 in unrestricted net position for construction projects.

NOTE 10 SUBSEQUENT EVENTS

The Authority has evaluated all subsequent events through June 27, 2019, the date the financial statements were available to be issued.

SUPPLEMENTARY INFORMATION

DOWNINGTOWN MUNICIPAL WATER AUTHORITY
(A Component Unit of the Borough of Downingtown)
COMBINING SCHEDULE OF NET POSITION
DECEMBER 31, 2018

	Operating Fund	Revenue Fund	Debt Service Fund	Construction Fund	Totals
ASSETS					
Current Assets:					
Cash and cash equivalents	\$ 529,480	\$ 1,631,453	\$ 79,702	\$ 130,222	\$ 2,370,857
Investments	164,320	-	-	-	164,320
Accounts receivable	-	1,991,595	-	-	1,991,595
Prepaid expenditures	43,633	-	-	-	43,633
Inventory	60,944	-	-	-	60,944
Total Current Assets	<u>798,377</u>	<u>3,623,048</u>	<u>79,702</u>	<u>130,222</u>	<u>4,631,349</u>
Noncurrent Assets:					
Land	468,785	-	-	-	468,785
Construction-in-progress	712,695	-	-	-	712,695
Capital assets, net of depreciation	9,192,960	-	-	-	9,192,960
Total Noncurrent Assets	<u>10,374,440</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>10,374,440</u>
TOTAL ASSETS	<u>\$ 11,172,817</u>	<u>\$ 3,623,048</u>	<u>\$ 79,702</u>	<u>\$ 130,222</u>	<u>\$ 15,005,789</u>
LIABILITIES					
Current Liabilities:					
Accounts payable	\$ 80,529	\$ -	\$ -	\$ -	\$ 80,529
Accrued payroll liabilities	38,970	-	-	-	38,970
Accrued interest	57,195	-	-	-	57,195
Pension payable	17,916	-	-	-	17,916
Escrows	-	132,087	-	-	132,087
Note payable	760,934	-	-	-	760,934
Total Current Liabilities	<u>955,544</u>	<u>132,087</u>	<u>-</u>	<u>-</u>	<u>1,087,631</u>
Noncurrent Liabilities:					
Note payable	5,900,716	-	-	-	5,900,716
Total Noncurrent Liabilities	<u>5,900,716</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>5,900,716</u>
TOTAL LIABILITIES	<u>6,856,260</u>	<u>132,087</u>	<u>-</u>	<u>-</u>	<u>6,988,347</u>
NET POSITION					
Net investment in capital assets	3,712,790	-	-	-	3,712,790
Unrestricted	603,767	3,490,961	79,702	130,222	4,304,652
TOTAL NET POSITION	<u>4,316,557</u>	<u>3,490,961</u>	<u>79,702</u>	<u>130,222</u>	<u>8,017,442</u>
TOTAL LIABILITIES AND NET POSITION	<u>\$ 11,172,817</u>	<u>\$ 3,623,048</u>	<u>\$ 79,702</u>	<u>\$ 130,222</u>	<u>\$ 15,005,789</u>

DOWNINGTOWN MUNICIPAL WATER AUTHORITY
(A Component Unit of the Borough of Downingtown)
COMBINING SCHEDULE OF REVENUES, EXPENSES, AND CHANGES IN NET POSITION
FOR THE YEAR ENDED DECEMBER 31, 2018

	Operating Fund	Revenue Fund	Debt Service Fund	Construction Fund	Totals
OPERATING REVENUES					
Water revenues	\$ -	\$ 4,722,157	\$ -	\$ -	\$ 4,722,157
Penalties and miscellaneous	-	59,044	-	-	59,044
TOTAL OPERATING REVENUES	-	4,781,201	-	-	4,781,201
OPERATING EXPENSES					
Water system:					
Chemical supplies	118,319	-	-	-	118,319
Depreciation expense	439,729	-	-	-	439,729
Insurance	146,697	-	-	-	146,697
Laboratory supplies	59,527	-	-	-	59,527
Distribution system	449	-	-	-	449
Miscellaneous expenses	7,523	-	-	-	7,523
Operating supplies	86,894	-	-	-	86,894
Payroll taxes	56,989	-	-	-	56,989
Pension	76,988	-	-	-	76,988
Regulatory expense	24,049	-	-	-	24,049
Repairs and maintenance	361,255	-	-	-	361,255
Salaries	730,899	-	-	-	730,899
Sludge removal	7,595	-	-	-	7,595
Utilities	130,500	-	-	-	130,500
Training	7,657	-	-	-	7,657
Total Water System Expenses	2,255,070	-	-	-	2,255,070
Administrative:					
Board members' fees	7,125	-	-	-	7,125
Engineers' fees	51,198	-	-	-	51,198
Insurance	77,644	-	-	-	77,644
Miscellaneous	17,454	-	-	-	17,454
Office expenses	57,716	-	-	-	57,716
Payroll taxes	14,836	-	-	-	14,836
Professional fees	172,675	-	-	-	172,675
Salaries	190,283	-	-	-	190,283
Total Administrative	588,931	-	-	-	588,931
TOTAL OPERATING EXPENSES	2,844,001	-	-	-	2,844,001
NET OPERATING INCOME (LOSS)	(2,844,001)	4,781,201	-	-	1,937,200
NONOPERATING REVENUES (EXPENSES)					
Investment income	-	9,156	6,619	-	15,775
Interest expense	-	-	(281,024)	-	(281,024)
TOTAL NONOPERATING REVENUES (EXPENSES)	-	9,156	(274,405)	-	(265,249)
Transfers In (Out)	4,203,517	(4,214,359)	(32,419)	43,261	-
CHANGE IN NET POSITION	1,359,516	575,998	(306,824)	43,261	1,671,951
NET POSITION, BEGINNING OF YEAR	2,957,041	2,914,963	386,526	86,961	6,345,491
NET POSITION, END OF YEAR	\$ 4,316,557	\$ 3,490,961	\$ 79,702	\$ 130,222	\$ 8,017,442

DOWNTOWN MUNICIPAL WATER AUTHORITY
(A Component Unit of the Borough of Downingtown)
SCHEDULE OF OPERATING REVENUES AND EXPENSES - BUDGET TO ACTUAL
FOR THE YEAR ENDED DECEMBER 31, 2018

	<u>Original and Final Budget</u>	<u>Actual</u>	<u>Variance with Final Budget</u>
OPERATING REVENUES			
Water revenues	\$ 4,262,500	\$ 4,722,157	\$ 459,657
Penalties and miscellaneous	60,000	59,044	(956)
TOTAL OPERATING REVENUES	<u>4,322,500</u>	<u>4,781,201</u>	<u>458,701</u>
 OPERATING EXPENSES			
Water system	2,078,437	2,255,070	176,633
Administrative	643,220	588,931	(54,289)
TOTAL OPERATING EXPENSES	<u>2,721,657</u>	<u>2,844,001</u>	<u>122,344</u>
 OPERATING INCOME	 <u>\$ 1,600,843</u>	 <u>\$ 1,937,200</u>	 <u>\$ 336,357</u>



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

June 27, 2019

To the Board of Directors
Downingtown Municipal Water Authority
Downingtown, Pennsylvania

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the Downingtown Municipal Water Authority ("the Authority"), Downingtown, Pennsylvania, 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, and have issued our report thereon dated June 27, 2019.

Internal Control Over Financial Reporting

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

To the Board of Directors
Downingtown Municipal Water Authority

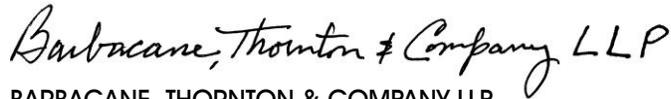
Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and, therefore, material weaknesses or significant deficiencies may exist that were not identified. Given these limitations, during our audit we did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified. We did identify certain deficiencies in internal control, described in the accompanying schedule of findings and recommendations as items #2017-001 and #2017-002, that we consider to be significant deficiencies.

Compliance and Other Matters

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

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 Authority'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 Authority's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.


BARBACANE, THORNTON & COMPANY LLP

SCHEDULE OF FINDINGS AND RECOMMENDATIONS

DOWNTOWN MUNICIPAL WATER AUTHORITY
(A Component Unit of the Borough of Downingtown)

SCHEDULE OF FINDINGS AND RECOMMENDATIONS

STATUS OF PRIOR YEAR FINDINGS AND RECOMMENDATIONS

2017-001 – LACK OF CONTROLS SURROUNDING CASH RECEIPTS

During our prior year audit, we noted the lack of proper controls surrounding the cash receipts cycle. There was a lack of segregation of duties, as the same employee substantially had complete control over all components of the receipts cycle. The same employee performed duties such as creating invoices, receiving payments, recording payments in the accounting software, depositing of cash, and preparation of bank reconciliations. Segregation of duties is critical to reduce the risk of errors, misappropriations, fraud, and to maintain a strong financial transaction control environment.

We recommended that the Authority develop and implement policies and procedures surrounding cash receipts that will provide for strong internal controls, keeping in mind the importance of proper segregation of duties.

Status

During our current year audit, we did not note any changes made to the entity's internal controls surrounding cash receipts. As a result, this finding is still applicable for the current year.

2017-002 – LACK OF CONTROLS SURROUNDING PAYROLL PROCESSING

During our prior year audit, we noted the lack of proper controls surrounding the payroll cycle. There was a lack of segregation of duties, as the same employee substantially had complete control over all components of the receipts cycle. The same employee performed duties such as signing off on employee timesheets, submitting payroll to the Authority's payroll service organization, preparing bank reconciliations, as well as other payroll functions. Segregation of duties is critical to reduce the risk of errors, misappropriations, fraud, and to maintain a strong financial transaction control environment.

We recommended that the Authority develop and implement policies and procedures surrounding payroll that will provide for strong internal controls, keeping in mind the importance of proper segregation of duties.

Status

During our current year audit, we did not note any changes made to the entity's internal controls surrounding payroll processing. As a result, this finding is still applicable for the current year.

CURRENT YEAR FINDINGS AND RECOMMENDATIONS

None.