

PUBLIC SERVICE COMMISSION  
ANNUAL REPORT BRANCH  
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**CUMBERLAND FALLS HIGHWAY  
WATER DISTRICT**  
**AUDITED FINANCIAL STATEMENTS**  
**YEARS ENDED DECEMBER 31, 2011 AND 2010**

**CUMBERLAND FALLS HIGHWAY WATER DISTRICT  
DECEMBER 31, 2011 AND 2010**

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# SUMMERS, MCCRARY & SPARKS, P.S.C.

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## CERTIFIED PUBLIC ACCOUNTANTS

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---

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RYAN R. LASKI, CPA

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LAURENCE T. SUMMERS  
1961-1992

### INDEPENDENT AUDITORS' REPORT

To the Commissioners  
Cumberland Falls Highway Water District  
Corbin, KY

We have audited the accompanying financial statements of the business-type activities of the Cumberland Falls Highway Water District, as of and for the years ended December 31, 2011 and 2010, which collectively comprise the District's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the District's management. Our responsibility is to express opinions 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 and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and the significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the business-type activities of the Cumberland Falls Highway Water District, as of December 31, 2011 and 2010, and the respective changes in financial position, and cash flows, where applicable, thereof, for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated April 30, 2012, on our consideration of the District's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 3 through 6 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.

*Summers McCrary & Sparks PSC*

Summers, McCrary & Sparks, PSC  
Lexington, KY  
April 30, 2012

**CUMBERLAND FALLS HIGHWAY WATER DISTRICT  
MANAGEMENT'S DISCUSSION AND ANALYSIS  
DECEMBER 31, 2011**

This section of the Cumberland Falls Highway Water District's annual financial report presents an analysis of the District's financial performance during the fiscal years ended December 31, 2011 and 2010. This information is presented in conjunction with the audited basic financial statements, which follow this section.

**FINANCIAL HIGHLIGHTS FOR THE FISCAL YEAR 2011**

- The District's net assets decreased by \$114,956 or 2.6 percent from \$4,494,854 to \$4,379,898.
- Gross profit from operations decreased by \$32,899 or 3.6 percent from \$919,691 to \$886,792.
- Operating expenses increased by \$9,253 or 0.9 percent from \$980,080 to \$989,333.
- Capital contributions to the District increased by \$38,726 or 115 percent from \$33,611 to \$72,337.

**OVERVIEW OF THE FINANCIAL STATEMENTS**

This annual report consists of the following three parts: Management's Discussion and Analysis, Basic Financial Statements and Other Required Supplementary Information. The Financial Statements include notes which explain in detail some of the information included in the basic financial statements.

**REQUIRED FINANCIAL STATEMENTS**

The Financial Statements of the District report information utilizing the full accrual basis of accounting. The Financial Statements conform to accounting principles which are generally accepted in the United States of America. The Statements of Net Assets include information on the District's assets and liabilities and provide information about the nature and amounts of investments in resources (assets) and the obligations to District creditors (liabilities). The Statements of Revenues, Expenses and Changes in Net Assets identify the District's revenues and expenses for the fiscal years ended December 31, 2011 and 2010. This statement provides information on the District's operations over the past two fiscal years and can be used to determine whether the District has recovered all of its actual and projected costs through user fees and other charges. The third financial statement is the Statement of Cash Flows. This statement provides information on the District's cash receipts, cash payments and changes in cash resulting from operations, investments and financing activities. From the Statements of Cash Flows, the reader can obtain comparative information on the source and use of cash and the change in the cash and cash equivalents balance for each of the last two fiscal years.

**CUMBERLAND FALLS HIGHWAY WATER DISTRICT  
MANAGEMENT'S DISCUSSION AND ANALYSIS  
DECEMBER 31, 2011**

**FINANCIAL ANALYSIS OF THE DISTRICT**

The Statements of Net Assets and the Statements of Revenues, Expenses, and Changes in Net Assets provide an indication of the District's financial condition and also indicate the financial condition of the District during the last fiscal year. The District's net assets reflect the difference between assets and liabilities. An increase in net assets over time typically indicates an improvement in financial condition.

**Table 1  
Condensed Statement of Net Assets**

	2011	2010	\$ Change	% Change
Current and other assets	\$1,422,216	\$1,491,100	(\$68,884)	(5%)
Capital assets	5,404,214	5,505,822	(101,608)	(2%)
<b>Total Assets</b>	<b>6,826,430</b>	<b>6,996,922</b>	<b>(170,492)</b>	<b>(2%)</b>
Long-term debt	2,400,132	2,450,442	(50,310)	(2%)
Other liabilities	46,400	51,626	(5,226)	10%
<b>Total Liabilities</b>	<b>2,446,532</b>	<b>2,502,068</b>	<b>(55,536)</b>	<b>(2%)</b>
Net assets invested in capital assets	3,029,208	3,089,896	(60,688)	(2%)
Net assets restricted for debt service	388,974	369,540	19,434	5%
Unrestricted net assets	961,716	1,035,418	(73,702)	(7%)
<b>Total Net Assets</b>	<b>\$4,379,898</b>	<b>\$4,494,854</b>	<b>(\$114,956)</b>	<b>(3%)</b>

As the above table indicates, total assets decreased by \$170,492 from \$6,996,922 to \$6,826,430 during the fiscal year ended December 31, 2011. This decrease primarily resulted from a decrease in capital assets of \$101,608 resulting from depreciation of the assets and from a decrease in cash from operations.

Table 1 also indicates a decrease of \$114,956 in net assets, from \$4,494,854 to \$4,379,898 for fiscal year ending December 31, 2011. As indicated above, this was due to a decrease in capital assets.

The Statements of Revenues, Expenses and Changes in Net Assets identify the various revenue and expense items which affect the change in net assets. As the information in Table 2 indicates, income before capital contributions was a loss of \$187,293 and capital contributions were \$72,337, realizing a net change in assets of (\$114,956).

**CUMBERLAND FALLS HIGHWAY WATER DISTRICT  
MANAGEMENT'S DISCUSSION AND ANALYSIS  
DECEMBER 31, 2011**

**Table 2  
Condensed Statement of Revenues, Expenses  
and Changes in Net Assets**

	2011	2010	\$ Change	% Change
Gross Profit	\$886,792	\$919,691	(32,899)	(4%)
Nonoperating revenues	18,550	(40,812)	59,362	145%
<b>Total Revenues</b>	<b>905,342</b>	<b>878,879</b>	<b>26,463</b>	<b>3%</b>
Depreciation expense	246,324	251,617	(5,293)	(2%)
Other operating expenses	743,009	728,463	14,546	2%
Nonoperating expenses	103,302	105,063	(1,761)	(2%)
<b>Total Expenses</b>	<b>1,092,635</b>	<b>1,085,143</b>	<b>7,492</b>	<b>1%</b>
Income before capital contributions	(187,293)	(206,264)	18,971	(9%)
Capital contributions	72,337	33,611	38,726	115%
Changes in net assets	(114,956)	(172,653)	57,697	(33%)
Beginning net assets	4,494,854	4,667,507	(172,653)	(4%)
<b>Ending Net Assets</b>	<b>\$4,379,898</b>	<b>\$4,494,854</b>	<b>\$(114,956)</b>	<b>(3%)</b>

Table 2 indicates that the Districts total Gross Profit decreased by \$32,899 resulting from reduced water sales and increases in water purchases. Total expenses increased by \$7,492 due to an increase in operating expenses.

**CAPITAL ASSETS**

As of December 31, 2011, the District's investment in capital assets totaled \$5,404,214, a decrease of \$101,608. A comparison of the District's capital assets over the past two years is presented in Note 3 of the financial statements.

The district was awarded a \$50,000 grant from the Kentucky Infrastructure Authority for the construction of 16 miles of waterline to serve areas within its jurisdiction. There were approximately 8 miles of new lines and 8 miles of replacement lines installed, potentially servicing 40 new customers. The grant proceeds were received and expended in early 2011.

**CUMBERLAND FALLS HIGHWAY WATER DISTRICT  
MANAGEMENT'S DISCUSSION AND ANALYSIS  
DECEMBER 31, 2011**

**LONG TERM DEBT**

As of December 31, 2011, the District had \$2,375,006 in outstanding revenue bond debt. The reduction in long-term debt obligations of \$40,920 is from principal payments made during 2011.

Additional information on the District's long-term debt is provided in Note 4 of the financial statements.

**ADDITIONAL FINANCIAL INFORMATION**

This financial report is designed to provide the District's customers, investors, and other interested parties with an overview of the District's financial operations and financial condition. Should the reader have questions regarding the information included in this report or wish to request additional financial information, please contact the CFHWD at 6929 Cumberland Falls Highway, Corbin Ky.

**CUMBERLAND FALLS HIGHWAY WATER DISTRICT  
STATEMENTS OF NET ASSETS  
DECEMBER 31, 2011 AND 2010**

	2011	2010
<b>ASSETS</b>		
<b>CURRENT ASSETS</b>		
Cash and cash equivalents	\$ 147,066	\$ 244,460
Certificate of Deposits	672,950	665,223
Accounts receivable	147,478	140,440
Inventory - materials and supplies	50,485	56,037
Prepaid expenses	12,730	12,686
<b>Total Current Assets</b>	<b>1,030,709</b>	<b>1,118,846</b>
<b>RESTRICTED CASH AND CASH EQUIVALENTS</b>	<b>388,974</b>	<b>369,540</b>
<b>UTILITY PLANT</b>		
Nondepreciable capital assets	73,147	73,147
Depreciable capital assets, net of depreciation	5,331,067	5,432,675
<b>Net Utility Plant</b>	<b>5,404,214</b>	<b>5,505,822</b>
<b>OTHER ASSETS</b>		
Unamortized debt expense, net	2,533	2,714
<b>Total Other Assets</b>	<b>2,533</b>	<b>2,714</b>
<b>TOTAL ASSETS</b>	<b>\$ 6,826,430</b>	<b>\$ 6,996,922</b>
<b>LIABILITIES</b>		
<b>CURRENT LIABILITIES</b>		
Accounts payable	\$ -	\$ 7,446
Accrued taxes	4,900	4,680
Revenue bonds payable - due within one year	41,500	39,500
<b>Total Current Liabilities</b>	<b>46,400</b>	<b>51,626</b>
<b>NONCURRENT LIABILITIES</b>		
Revenue bonds payable - due in more than one year	2,333,506	2,376,426
Customer deposits	66,626	74,016
<b>Total Noncurrent Liabilities</b>	<b>2,400,132</b>	<b>2,450,442</b>
<b>TOTAL LIABILITIES</b>	<b>2,446,532</b>	<b>2,502,068</b>
<b>NET ASSETS</b>		
Invested in capital assets, net of related debt	3,029,208	3,089,896
Restricted for debt service	388,974	369,540
Unrestricted	961,716	1,035,418
<b>TOTAL NET ASSETS</b>	<b>4,379,898</b>	<b>4,494,854</b>
<b>TOTAL LIABILITIES AND NET ASSETS</b>	<b>\$ 6,826,430</b>	<b>\$ 6,996,922</b>

The Accompanying Notes Are An Integral Part Of These Financial Statements  
See Auditors' Report

**CUMBERLAND FALLS HIGHWAY WATER DISTRICT  
STATEMENTS OF REVENUE, EXPENSES  
AND CHANGES IN NET ASSETS  
FOR THE YEARS ENDED DECEMBER 31, 2011 AND 2010**

	<u>2011</u>	<u>2010</u>
<b>OPERATING REVENUES</b>		
Water sales	\$ 1,454,245	\$ 1,468,933
Other income	49,986	50,538
<b>Total Operating Revenues</b>	<u>1,504,231</u>	<u>1,519,471</u>
<b>COST OF SALES</b>		
Water purchases	<u>617,439</u>	<u>599,780</u>
<b>Gross Profit from Operations</b>	<b>886,792</b>	<b>919,691</b>
<b>OPERATING EXPENSES</b>		
Advertising	2,558	2,180
Commissioner fees	11,100	10,500
Contractual services:		
Maintenance	2,935	4,369
Operation supplies and materials	43,510	40,882
Office supplies and other expenses	41,574	41,685
Salaries and wages	333,584	336,171
Employee benefits	177,071	172,636
Professional services	38,598	29,572
Transportation expenses	24,242	28,786
Purchased power	30,237	28,122
Insurance	28,055	27,328
Depreciation	246,324	251,617
Bad debt expense	7,222	3,956
Other taxes	2,323	2,276
<b>Total Operating Expenses</b>	<u>989,333</u>	<u>980,080</u>
Operating Income (Loss)	(102,541)	(60,389)
<b>NONOPERATING REVENUE (EXPENSE)</b>		
Interest income	8,589	11,695
Interest expense	(103,121)	(104,882)
Loss on disposal of meters	9,961	(52,507)
Amortization of debt expense	<u>(181)</u>	<u>(181)</u>
Net Nonoperating Revenue (Expense)	<u>(84,752)</u>	<u>(145,875)</u>
Income (Loss) before Contributions	(187,293)	(206,264)
<b>CAPITAL CONTRIBUTIONS</b>	<u>72,337</u>	<u>33,611</u>
<b>CHANGE IN NET ASSETS</b>	<b>(114,956)</b>	<b>(172,653)</b>
<b>NET ASSETS</b>		
Beginning of year	4,494,854	4,667,507
End of year	<u>\$ 4,379,898</u>	<u>\$ 4,494,854</u>

The Accompanying Notes Are An Integral Part Of These Financial Statements  
See Auditors' Report

**CUMBERLAND FALLS HIGHWAY WATER DISTRICT  
STATEMENTS OF CASH FLOWS  
FOR THE YEARS ENDED DECEMBER 31, 2011 AND 2010**

	2011	2010
<b>Cash flows from operating activities:</b>		
Cash receipts from customers	\$ 1,497,193	\$ 1,519,908
Cash payments to employees for services	(333,584)	(336,171)
Cash payments to suppliers for goods and services	(1,028,582)	(995,821)
Net cash provided (used) by operating activities	135,027	187,916
<b>Cash flows from noncapital financing activities:</b>		
Change in customer deposits	(7,390)	5,180
<b>Cash flows from capital and related financing activities:</b>		
Additions to capital assets	(144,716)	(52,144)
Proceeds from asset disposals	9,961	-
Capital contributions	72,337	33,611
Principal paid on debt	(40,920)	(39,221)
Interest paid on debt	(103,121)	(104,882)
Net cash provided (used) in capital and related financing activities	(206,459)	(162,636)
<b>Cash flows from investing activities:</b>		
Interest received	8,589	11,695
<b>Net Increase (decrease) in cash and cash equivalents</b>	(70,233)	42,155
<b>Cash and cash equivalents, Beginning of Year</b>	1,279,223	1,237,068
<b>Cash and cash equivalents, End of Year</b>	\$ 1,208,990	\$ 1,279,223
<b>Reconciliation of operating income (loss) to net cash provided by operating activities:</b>		
Operating income (loss)	\$ (102,541)	\$ (60,389)
<b>Adjustments to reconcile net income (loss) to net cash provided (used) by operating activities:</b>		
Depreciation	246,324	251,617
(Increase) decrease in operating assets:		
Accounts receivable	(7,038)	437
Inventory	5,552	(6,665)
Prepaid expenses	(44)	677
Increase (decrease) in operating liabilities:		
Accounts payable	(7,446)	4,423
Accrued taxes	220	(892)
Accrued payroll taxes	-	(1,292)
Total cash provided (used) by operating activities	\$ 135,027	\$ 187,916
<b>Reconciliation of cash and cash equivalents:</b>		
Cash and cash equivalents	\$ 820,016	\$ 909,683
Restricted cash and cash equivalents	388,974	369,540
Total cash and cash equivalents	\$ 1,208,990	\$ 1,279,223
<b>Supplemental disclosure of cash flow information:</b>		
<b>Noncash capital and related activities:</b>		
Amortization of premium on issuance of debt	\$ 181	\$ 181

The Accompanying Notes Are An Integral Part Of These Financial Statements  
See Auditors' Report

**CUMBERLAND FALLS HIGHWAY WATER DISTRICT  
NOTES DISCLOSURES  
DECEMBER 31, 2011 AND 2010**

**NOTE 1 - NATURE OF ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES**

Nature of Organization

Cumberland Falls Highway Water District, a special district pursuant to KRS Chapter 74, was created by the Whitley County Fiscal Court on February 1, 1967, upon petition by area residents, to provide water services to the residents of the area specified in the petition. The District is accounted for as a governmental enterprise fund. It is financed and operated in a manner similar to a private business enterprise where the intent of the governing body is that costs (expenses, including depreciation) of providing goods or services to the general public on a continuing basis are financed primarily through user charges.

Basis of Presentation and Accounting, and Measurement Focus

The District's basic financial statements are presented on the full accrual basis of accounting and conform to accounting principles generally accepted in the United States of America. The District has elected under GASB Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Government Entities that Use Proprietary Fund Accounting*, to apply all applicable GASB pronouncements as well as any applicable pronouncements of the Financial Accounting Standards Board (FASB), the Accounting Principles Board, or any Accounting Research Bulletins issued on or before November 30, 1989, that do not conflict with or contradict GASB pronouncements.

The District follows the provisions of the GASB No. 34, *Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments*. The accompanying financial statements have been prepared using the economic resources measurement focus and the accrual basis of accounting and reflect transactions on behalf of the District. Operating revenues and expenses result from providing water services to customers. All other revenues and expenses are reported as nonoperating revenues and expenses. When both restricted and unrestricted resources are available for use, it is the District's policy to use restricted resources first, then unrestricted resources as they are needed.

Significant Accounting Policies

*Cash and Cash Equivalents:* Cash and cash equivalents are considered by the District to be highly liquid investments with a maturity of three months or less when purchased.

*Accounts Receivable:* The District uses the direct write-off method for accounting for bad debts, which management feels is not materially different from the allowance method. Accounts written off as uncollectible during the years ended December 31, 2011 and 2010 totaled \$7,222 and \$3,956, respectively. Receivables outstanding in excess of ninety days at December 31, 2011 and 2010 totaled \$8,198 and \$6,296, respectively.

**CUMBERLAND FALLS HIGHWAY WATER DISTRICT  
NOTES DISCLOSURES  
DECEMBER 31, 2011 AND 2010**

**NOTE 1 - NATURE OF ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES (Continued)**

*Inventory:* Inventories are stated at the lower of cost or market determined by the first-in, first-out method.

*Utility plant:* Utility plant and equipment are stated at cost and depreciated over their useful lives using the straight-line method. The estimated useful lives are as follows:

Structures, reservoirs, pumps and other improvements	10 - 40 years
Office furniture, fixtures and equipment	3-10 years
Motor Vehicles	5 years

*Restricted Cash and Cash Equivalents:* The District has designated bank accounts per the loan resolution covenants for debt service, depreciation fund and meter deposits.

*Amortization of Debt Expense:* Debt expense on the Waterworks Refunding and Improvement Revenue Bond of 1986, Series A and Series B, originally totaling \$13,799, is being amortized over the life of the outstanding bonds. Amortization expense was \$181 and \$181 for 2011 and 2010, respectively.

*Use of Estimates:* 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.

*Net Assets:* Net assets comprise the various net earnings from operating income, nonoperating revenues and expenses, and capital contributions. Net assets are classified in the following three components:

*Invested in capital assets, net of related debt* - This component of net assets consists of capital assets, net of accumulated depreciation and reduced by the outstanding balances of any bonds, mortgages, notes or other borrowings that are attributable to the acquisition, construction or improvement of those assets.

*Restricted* - This component of net assets consists of constraints imposed by creditors (such as through debt covenants), grantors, contributors, or laws or regulations of other governments.

*Unrestricted* - This component of net assets consists of net assets that do not meet the definitions of "restricted" or "invested in capital assets, net of related debt."

*Fair Value Measurements:* The carrying amount of cash and cash equivalents, accounts receivable, accounts payable, customer deposits and bonds approximates fair value because of the relative terms and short maturities of these financial instruments.

**CUMBERLAND FALLS HIGHWAY WATER DISTRICT  
NOTES DISCLOSURES  
DECEMBER 31, 2011 AND 2010**

**NOTE 2 - COMPOSITION OF CASH**

The District maintains its cash accounts with banks in Corbin, Kentucky. The balance of the accounts over Federal Deposit Insurance Corporation (FDIC) insured limit of \$250,000 is collateralized by securities held by the bank or by its agent in the name of the District and totaled \$417,934 and \$779,621 at December 31, 2011 and 2010 respectively. Following is an analysis of cash at December 31, 2011 and 2010.

	December 31, 2011		December 31, 2010	
	Bank Balance	Book Balance	Bank Balance	Book Balance
Unrestricted	\$848,356	\$820,016	\$908,672	\$909,683
Restricted	391,316	388,974	370,949	369,540
Total	<u>\$1,239,672</u>	<u>\$1,208,990</u>	<u>\$1,279,621</u>	<u>\$1,279,223</u>

**NOTE 3 – UTILITY PLANT**

Details of utility plant and related allowance for accumulated depreciation at December 31, 2011 and 2010 are as follows:

	Balance December 31, 2010	Additions	Deletions	Balance December 31, 2011
Nondepreciable Capital Assets:				
Land and Land Rights	\$73,147	\$0	\$0	\$73,147
Total Nondepreciable	<u>73,147</u>	<u>0</u>	<u>0</u>	<u>73,147</u>
Depreciable Capital Assets:				
Pumping Plant	112,564	0	0	112,564
Transmission and Distribution Plant	7,677,812	120,116	0	7,797,928
General Plant	445,185	24,600	(17,697)	452,088
Total Depreciable	<u>8,235,561</u>	<u>144,716</u>	<u>(17,697)</u>	<u>8,362,580</u>
Total Utility Plant	8,308,708	144,716	(17,697)	8,435,727
Less: Accumulated Depreciation	(2,802,886)	(246,324)	17,697	(3,031,513)
Net Utility Plant	<u>\$5,505,822</u>	<u>\$(101,608)</u>	<u>\$0</u>	<u>\$5,404,214</u>

**CUMBERLAND FALLS HIGHWAY WATER DISTRICT  
NOTES DISCLOSURES  
DECEMBER 31, 2011 AND 2010**

**NOTE 4 - BONDS PAYABLE**

The Waterworks Revenue Bonds, Series 1996, provide for the partial financing of the cost of construction of extension, additions, and improvements to the existing system. The interest rate of the Bonds is 4.50%. The maturity date is 01/01/35.

The Waterworks Revenue Bonds, Series 2001, provide for the partial financing of the cost of construction of extension, additions, and improvements to the existing waterworks system. The interest rate of the Bonds is 4.50%. The maturity date is 01/01/41.

The Waterworks Revenue Bonds, Series 2007, provide for the partial financing of the cost of construction of extension, additions, and improvements to the existing waterworks system. The interest rate of the Bonds is 4.125%. The maturity date is 01/01/44.

All bonds are secured by a lien on the gross income and revenues derived from the operation of the system sufficient to pay principal and interest on the bonds, as well as a statutory mortgage lien on the water utility plant and all properties therewith, pursuant to the Kentucky Revised Statutes, and also a first lien on all water purchase contracts owned by the District. The U.S. Department of Agriculture's Rural Economic Community Development (RECD), formerly Farmers Home Administration, requires the District to prepay monthly the required amounts of interest, due January 1 and July 1, and the required amounts of principal due January 1, according to bond redemption schedules.

The annual requirements for debt service as of December 31, 2011, are as follows:

Year Ending	Interest	Principal	Total
2012	102,004	41,500	143,504
2013	100,207	43,000	143,207
2014	98,347	45,000	143,347
2015	96,401	47,000	143,401
2016	94,366	49,000	143,366
2017-2021	438,208	278,500	716,708
2022-2026	372,247	346,500	718,747
2027-2031	290,303	430,000	720,303
2032-2036	189,379	473,903	663,282
2037-2041	96,233	411,240	507,473
2042-2045	17,508	209,363	226,871
<b>Total</b>	<b>\$1,895,203</b>	<b>\$2,375,006</b>	<b>\$4,270,209</b>

**CUMBERLAND FALLS HIGHWAY WATER DISTRICT  
NOTES DISCLOSURES  
DECEMBER 31, 2011 AND 2010**

**NOTE 4 - BONDS PAYABLE (Continued)**

The following is a summary of bonds payable for the year ended December 31, 2011:

	Beginning Balance	Additions	Reductions	Ending Balance	Amount due within one year
1996 Issue	613,438	0	15,035	598,403	15,000
2001 Issue	453,286	0	7,546	445,740	7,500
2007 Issue	1,349,202	0	18,339	1,330,863	19,000
Total Debt	<u>\$2,415,926</u>	<u>\$0</u>	<u>\$40,920</u>	<u>\$2,375,006</u>	<u>\$41,500</u>

Interest expense paid during 2011 and 2010 was \$103,121 and \$104,882, respectively.

**NOTE 5 – RETIREMENT PLAN**

The District adopted a Savings Incentive Match Plan for Employees of Small Employers (SIMPLE) effective October 1, 2006. The SIMPLE IRA is available to employees who are expected to receive at least \$5,000 in compensation during the year and who received at least \$5,000 in compensation during the prior year. The District matches participants' contributions to the Plan up to 3% of the participants' compensation. The District's contributions to the plan for 2011 and 2010 totaled \$13,686 and \$10,271, respectively.

**NOTE 6 – SUBSEQUENT EVENTS**

Due to an increase in water purchase rates, the District has applied with the Public Service Commission for both a water purchase adjustment and a general rate increase.

As required by FASB ASC 855-10-50-1, the Company has evaluated subsequent events through April 30, 2012, the date the financial statements were available to be issued.

**SUMMERS, MCCRARY & SPARKS, P.S.C.**  
**CERTIFIED PUBLIC ACCOUNTANTS**

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MEMBERS:

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DEBORAH L. MAYNARD, CPA  
RYAN R. LASKI, CPA

LAURENCE T. SUMMERS  
1961-1992

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

To the Commissioners  
Cumberland Falls Highway Water District  
Corbin, KY

We have audited the financial statements of the business-type activities of the Cumberland Falls Highway Water District as of and for the year ended December 31, 2011, which collectively comprise District's basic financial statements and have issued our report thereon dated April 30, 2012. 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.

**Internal Control Over Financial Reporting**

In planning and performing our audit, we considered the District's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the District's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the District's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over financial reporting that might be significant deficiencies, or material weaknesses and therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. However, as described in the accompanying schedule of findings and responses, we identified certain deficiencies in internal control over financial reporting that we consider to be material weaknesses.

*A deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or 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. We consider the deficiencies described in the accompanying schedule of findings and responses to be material weaknesses. (11-01 and 11-02)

### **Compliance and Other Matters**

As part of obtaining reasonable assurance about whether the District's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, 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*.

We noted certain other matters that we reported to management of Cumberland Falls Highway Water District in a separate letter dated April 30, 2012.

The District's response to the findings identified in our audit is described in the accompanying schedule of findings and responses. We did not audit the District's response and, accordingly, we express no opinion on it.

This report is intended solely for the information and use of management, Commissioners, others within the entity, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

*Summers, McCrary & Sparks, PSC*

Lexington, KY 40509  
April 30, 2012

**CUMBERLAND FALLS HIGHWAY WATER DISTRICT  
SCHEDULE OF FINDINGS AND RESPONSES  
DECEMBER 31, 2011**

**Finding 11-01:**

Condition: The financial statements were not adjusted to actual and not converted to full accrual in accordance with generally accepted accounting principles, GAAP, (capital assets, accounts payable, deposits, bonds, prior year adjustments).

Criteria: Financial statements must be prepared in accordance with GAAP.

Effect: Financial statements issued that are not in accordance with GAAP.

Cause: The organization's personnel lack the expertise specific to preparing the financial statements in accordance with GAAP.

Response: Due to the complexity of GAAP and audit standards, we rely on the audit for year-end adjustments that meet the required GAAP standards.

**Finding 11-02:**

Condition: The District lacks proper internal control over financing reporting of their year-end financial statements to be issued in accordance with generally accepted accounting principles.

Criteria: Financial statements must be prepared in accordance with GAAP.

Effect: Financial statements issued that are not in accordance with GAAP.

Cause: The organization's personnel lack the expertise specific to preparing the financial statements in accordance with GAAP.

Recommendation: The organization should consider electing a board member with the necessary knowledge to be able to prepare the financial statements in accordance with GAAP. Another alternative would be to contract with another CPA to take responsibility of the financial statements in accordance with GAAP.

Response: Due to the complexity of GAAP and audit standards this is not worth the effort required. The financial statements are more than adequate to reveal the financial stability of the organization and the reporting of operating results. We rely on the audit for year-end financial statements that meet the required GAAP standards.