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MARION COUNTY WATER DISTRICT
LEBANON, KENTUCKY

AUDIT REPORT

DECEMBER 31, 2012 AND 2011

MAR 25 2013

PUBLIC SERVICE
COMMISSION

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AUDIT REPORT
DECEMBER 31, 2012 AND 2011

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INDEPENDENT AUDITOR'S REPORT

January 25, 2013

To the Commissioners of the
Marion County Water District

Report on the Financial Statements

We have audited the accompanying general purpose financial statements of Marion County Water District, Lebanon, Kentucky, as of and for the years ended December 31, 2012 and 2011, and the related notes to the financial statements, which collectively comprise the District's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes 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 opinions on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the 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 opinions.

Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the general purpose financial statements of Marion County Water District, Lebanon, Kentucky, as of December 31, 2012 and 2011, and the respective changes in financial position, and, where applicable, cash flows thereof for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 4-6 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Government 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 opinions on the financial statements that collectively comprise the Marion County Water District, Lebanon, Kentucky's basic financial statements. The Schedules of Operating and Maintenance Expenses and Schedules of Bond Retirements are presented for purposes of additional analysis and are not a required part of the basic financial statements.

The Schedules of Operating and Maintenance Expenses and Schedules of Bond Retirements are the responsibility of management and were derived from and relate 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 Schedules of Operating and Maintenance Expenses and Schedules of Bond Retirements information are fairly stated in all material respects in relation to the basic financial statements taken as a whole.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated January 25, 2013, on our consideration of the Marion County Water District, Lebanon, Kentucky's internal control over financial reporting and on our test of its compliance with certain provision 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 Marion County Water District, Lebanon, Kentucky's internal control financial reporting and compliance.

Sincerely,

White and Company, P.S.C.

Certified Public Accountants

**MANAGEMENT'S DISCUSSION AND ANALYSIS
MARION COUNTY WATER DISTRICT
DECEMBER 31, 2012**

Within this section of the Marion County Water District's annual financial report, the District's management provides narrative discussion and analysis of the financial activities of the District for the fiscal year ended December 31, 2012. The District's financial performance is discussed and analyzed within the context of the accompanying financial statements and disclosure following this section.

Financial Highlights

- The District's assets and other debits exceeded its liabilities by \$11,897,832 (Net Position) for the fiscal year reported.
- Total net position comprised of the following:
 - (1) Appropriated retained earnings of \$806,058.
 - (2) Retained earnings from income before contributions of \$1,086,899.
 - (3) Donated capital of \$10,004,875.
- The District's general purpose financial statement's retained earnings from income before contributions increased by \$100,508 from the previous fiscal year.
- The District's general purpose financial statement's donated capital increased by \$95,492 from the previous fiscal year. Donated capital primarily consists of contributions in aid of construction from federal USDA grant funds, KY Legislature grant funds, and customers for water line construction and projects.

Overview of the Financial Statements

Management's Discussion and Analysis introduces the District's general purpose financial statements. The general purpose financial statements include: (1) Statements of Net Position, (2) Income Statements, (3) Statements of Changes in Net Position, (4) Statements of Cash Flows, and (5) Notes to the Financial Statements. The Statements of Net Position show the total assets, liabilities and net position as of December 31, 2012 and December 31, 2011. The Income Statements depict the difference between the revenues and expenses for the year 2012. The Statements of Changes in Net Position show the change in the appropriated retained earnings and retained earnings from income before contributions. The District includes in this report additional information to supplement the basic financial statements.

The District as a Whole

Statements of Net Position:

	<u>2012</u>	<u>2011</u>
Utility Plant	11,954,425	11,997,991
Certificates of Deposit	650,003	650,003
Cash	1,562,548	1,633,782
Net Customer Accounts Receivable	132,781	147,322
Other Current Assets	209,861	349,299
Construction in Progress	178	0
 Total Current & Accrued Assets	 1,905,368	 2,130,403
 Total Assets & Other Debits	 14,509,796	 14,778,397

	<u>2012</u>	<u>2011</u>
Net Position		
Appropriated Retained Earnings	806,058	817,991
Retained Earnings from Income before Contributions	1,086,899	986,391
Donated Capital	<u>10,004,875</u>	<u>9,909,383</u>
 Total Net Position	 11,897,832	 11,713,765
 Bonds Payable	 <u>2,289,800</u>	 <u>2,735,100</u>
Total Long-term Debt	2,289,800	2,735,100
Revenue Bonds Payable	45,300	62,600
Other Current and Accrued Liabilities	<u>276,864</u>	<u>266,932</u>
Total Current and Accrued Liabilities	322,164	329,532
 Total Net Position & Liabilities	 <u><u>14,509,796</u></u>	 <u><u>14,778,397</u></u>

Total assets and other debits decreased by \$268,601, a decrease of 1.82%. Major decreases include cash, which decreased \$71,234 (4.36%), net utility plant, which decreased \$43,566 (.36%) and other current assets, which decreased \$139,438 (39.92%) from the previous fiscal year. The primary reason for the decrease in other current assets is the result of a decrease in inventory due to the change out of several radio read meters on hand at the end of 2011.

Income Statement:

	<u>2012</u>	<u>2011</u>
Operating Revenue		
Water Revenue	2,426,824	2,407,665
Other Operating Revenue	<u>78,502</u>	<u>82,685</u>
Total Operating Revenue	2,505,326	2,490,350
Operating Expenses		
Purchased Water	1,315,096	1,289,191
Other Operation & Maintenance Expenses	686,010	624,331
Depreciation	<u>406,482</u>	<u>380,748</u>
Total Operating Expenses	<u>2,407,588</u>	<u>2,294,270</u>
Operating Income	97,738	196,080
Other Income	66,463	72,292
Other Expenses - Interest	<u>75,626</u>	<u>99,562</u>
Net Income Before Contributions	<u><u>88,575</u></u>	<u><u>168,810</u></u>
Retained Earnings From Income Before Contributions		
Beginning Balance	986,391	847,013
Transfer to/from Appropriated Retained Earnings	<u>11,933</u>	<u>(29,432)</u>
Ending Balance	<u><u>1,086,899</u></u>	<u><u>986,391</u></u>

Operating revenues budgeted for 2012 were \$2,539,600. Operating revenues for 2012 were \$2,505,326, which was \$34,274 less than the budgeted amount. Actual operating revenues increased \$14,976 from the prior year. Total operation and maintenance expenses budgeted for 2012 were \$2,013,975. Total operation and maintenance expenses for 2012 were \$2,001,106, which was \$12,869 less than the budgeted amount. Actual operating expenses increased \$113,318 from the prior year.

Net income before contributions decreased by \$80,235 as compared to 2011.

Utility Plant and Debt Administration

Additions to Utility Plant were \$380,618. Accumulated depreciation increased \$406,482 causing a total decrease in the District’s Utility Plant of \$25,864. Further, the District disposed of \$111,167 of assets and incurred \$17,702 of losses on these disposals. Overall, net utility plant decreased by \$43,566. For a detail of Utility Plant, see Note C.

	Utility Plant (Net of Accumulated Depreciation)
Land	\$ 59,708
Distribution Plant	11,617,030
General Plant	277,687
Total Utility Plan	<u>11,954,425</u>

At year-end, the District had \$2,335,100 in outstanding bonds payable versus \$2,797,700 the previous year, a decrease of \$462,600 (16.54%). For a breakdown of the District’s current and long-term debt, see Notes D, E, and F and the supplemental financial information provided within this report.

Future Projections

The projections for the District for 2013 will entail the continuation of the radio read meter change out program. As of January 1, 2013, the District has changed out approximately 3,370 meters in this program. The District currently has 675 radio read meters in inventory. All new purchases of meters will come from District funds, since all contingency funds from past projects have been depleted.

Going forward, the District will proceed to acquire funds to replace some of its aging infrastructure. The District has plans to start construction of the 23,500 feet of 6 inch main line upgrade on Highway 84 in February 2013. The funds for this project will be furnished through a loan from the Kentucky Infrastructure Authority (KIA) for \$548,180. Also, the District will begin the Stage II testing for THM’s and HAAS’s, that is mandated by the Division of Water (DOW), to start in October 2013. The District will also begin to comply with the Unregulated Contaminant Monitoring Rule (UCMR3), as required by the Environmental Protection Agency (EPA), in July 2013.

Marion County Water District
Lebanon, Kentucky

Statement of Net Position
December 31, 2012 and 2011

Assets and Other Debits

	<u>2012</u>	<u>2011</u>
Utility Plant (Notes A-3 and C)	11,954,425	11,997,991
Other Property and Investments		
Certificates of Deposit - Citizens National Bank	<u>650,003</u>	<u>650,003</u>
Total Other Property and Investments	650,003	650,003
Current and Accrued Assets		
Cash (Note B)	1,562,548	1,633,782
Customer Accounts Receivable, Net of Allowance of 4,840 and 5,383	132,781	147,322
Other Accounts Receivable	190	24,975
Materials and Supplies Inventory (Note A-2)	197,124	311,460
Prepaid Insurance	11,088	10,833
Accrued Interest Receivable	1,459	2,031
Construction in Progress - KIA Projects	<u>178</u>	<u>0</u>
Total Current and Accrued Assets	<u>1,905,368</u>	<u>2,130,403</u>
Total Assets and Other Debits	<u><u>14,509,796</u></u>	<u><u>14,778,397</u></u>

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

Marion County Water District
Lebanon, Kentucky

Statement of Net Position
December 31, 2012 and 2011

Equity Capital and Liabilities

	<u>2012</u>	<u>2011</u>
Net Position		
Appropriated Retained Earnings (Note G)	806,058	817,991
Retained Earnings from Income before Contributions	1,086,899	986,391
Donated Capital	<u>10,004,875</u>	<u>9,909,383</u>
Total Net Position	11,897,832	11,713,765
Long-Term Debt		
Revenue Bonds Payable (Note F)	<u>2,289,800</u>	<u>2,735,100</u>
Total Long-Term Debt	2,289,800	2,735,100
Current and Accrued Liabilities		
Revenue Bonds Payable (Note F)	45,300	62,600
Accounts Payable - Trade	114,125	103,062
Accrued County Retirement	4,901	4,995
Accrued Unemployment	482	443
Customer Deposits	30,173	28,226
Accrued Taxes	<u>127,183</u>	<u>130,206</u>
Total Current and Accrued Liabilities	<u>322,164</u>	<u>329,532</u>
Total Net Position and Liabilities	<u><u>14,509,796</u></u>	<u><u>14,778,397</u></u>

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

Marion County Water District
Lebanon, Kentucky

Statements of Income
Years Ended December 31, 2012 and 2011

	<u>2012</u>	<u>Percent of Revenue</u>	<u>2011</u>	<u>Percent of Revenue</u>
Operating Revenue				
Metered Sales Residential	1,967,471	78.5%	1,960,741	78.7%
Metered Sales Commercial	423,185	16.9%	410,078	16.5%
Metered Sales Schools	20,900	0.8%	20,343	0.8%
Metered Sales Multi-Family	15,268	0.6%	16,503	0.7%
Miscellaneous Service	37,643	1.5%	37,458	1.5%
Late Charges	40,859	1.6%	45,227	1.8%
	<u>2,505,326</u>		<u>2,490,350</u>	
Total Operating Revenue		100.0%		100.0%
Operating Expenses				
Operation & Maintenance Expense	2,001,106	79.9%	1,913,522	76.8%
Depreciation	406,482	16.2%	380,748	15.3%
	<u>2,407,588</u>		<u>2,294,270</u>	
Total Operating Expenses		96.1%		92.1%
Operating Income	97,738	3.9%	196,080	7.9%
Other Income				
Interest Income	6,706	0.3%	8,523	0.3%
Collection Fees	32,337	1.3%	32,071	1.3%
Gain (Loss) from Sale of Asset	(15,078)	-0.6%	0	0.0%
Misc. Non-Operating Income	42,498	1.7%	31,698	1.3%
Total Other Income	66,463	2.7%	72,292	2.9%
Other Expenses				
Interest on Long-Term Debt	75,378	3.0%	99,137	4.0%
Other Interest	248	0.0%	425	0.0%
	<u>75,626</u>		<u>99,562</u>	
Total Other Expenses		3.0%		4.0%
Net Income before Contributions	<u>88,575</u>	<u>3.5%</u>	<u>168,810</u>	<u>6.8%</u>

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

Marion County Water District
Lebanon, Kentucky

Statements of Changes in Net Position
Years Ended December 31, 2012 and 2011

	<u>2012</u>	<u>2011</u>
Appropriated Retained Earnings		
Balance - Beginning of Year	817,991	788,559
Transfer to/from Retained Earnings from Income before Contributions	<u>(11,933)</u>	<u>29,432</u>
Balance - End of Year	<u><u>806,058</u></u>	<u><u>817,991</u></u>
Retained Earnings from Income before Contributions		
Balance - Beginning of Year	986,391	847,013
Net Income for the Year	88,575	168,810
Transfer to/from Appropriated Retained Earnings	<u>11,933</u>	<u>(29,432)</u>
Balance - End of Year	<u><u>1,086,899</u></u>	<u><u>986,391</u></u>

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

Marion County Water District
Lebanon, Kentucky

Statements of Cash Flows
For the Years Ended December 31, 2012 and 2011

	<u>2012</u>	<u>2011</u>
Cash Flows from Operating Activities:		
Receipts from Users	2,576,989	2,510,205
Payments to Employees	(373,565)	(338,133)
Payments to Suppliers for Goods and Services	<u>(1,503,528)</u>	<u>(1,809,821)</u>
Net Cash Provided by Operating Activities	699,896	362,251
Cash Flows from Capital and Related Financing Activities:		
Capital Contributions	95,492	919,914
Proceeds from Sale of Fixed Assets	2,624	0
Principal Payments on Long-term Debt	(462,600)	(254,500)
Interest Payments	(75,626)	(99,562)
Payments for Capital Projects	<u>(380,796)</u>	<u>(765,768)</u>
Net Cash Used by Capital and Related Financing Activities	(820,906)	(199,916)
Cash Flows from Investing Activities:		
Interest Income Received	7,278	7,985
Rent Income	42,498	31,698
Investment Purchases: Certificates of Deposit	<u>0</u>	<u>(11,711)</u>
Net Cash Provided by Investing Activities	49,776	27,972
Cash and Investments, Beginning	<u>1,633,782</u>	<u>1,443,475</u>
Cash and Investments, Ending	<u><u>1,562,548</u></u>	<u><u>1,633,782</u></u>

Marion County Water District
Lebanon, Kentucky

Statements of Cash Flows - (Continued)
For the Years Ended December 31, 2012 and 2011

Reconciliation of Net Income to Net Cash Provided by Operating Activities

	<u>2012</u>	<u>2011</u>
Net Income	88,575	168,810
Adjustments to Reconcile Operating Income to Net Cash Provided by Operating Activities:		
Depreciation	406,482	380,748
Interest on Debt	75,626	99,562
Misc. Non-Operating Income	(42,498)	(31,698)
Interest Income	(6,706)	(8,523)
Loss on Sale of Fixed Assets	15,078	0
Changes in Current Assets & Liabilities:		
Accounts Receivable	39,326	(12,217)
Materials & Supplies Inventory	114,336	(173,050)
Other Assets	(255)	(279)
Accounts Payable	11,063	(66,993)
Other Liabilities	<u>(1,131)</u>	<u>5,891</u>
Net Cash Provided by Operating Activities	<u><u>699,896</u></u>	<u><u>362,251</u></u>

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

Notes to Financial Statements

Nature of Operations:

Marion County Water District is a special district of Marion County, Kentucky. It operates a water distribution system in Marion County and southern Nelson County. Water is purchased from the Lebanon Water Company and Campbellsville Water Company and resold to more than 5,000 customers in Marion and Nelson Counties.

Significant Accounting Policies:

- A. The following is a summary of the significant accounting policies of the Marion County Water District:
1. Assets and liabilities and revenues and expenses are recognized on the accrual basis of accounting.
 2. Inventory is recorded at cost.
 3. Utility plant is stated at cost less accumulated depreciation computed on a straight-line method. The distribution plant assets are depreciated mainly over 50 years. The general plant assets are depreciated over their estimated useful lives from four to ten years.
 4. Four funds are set up on the company's books: revenue fund, operation and maintenance fund, reserve fund, and sinking fund. All income is deposited to the revenue fund. Funds are transferred monthly from the revenue fund to the operation and maintenance fund sufficient to pay the general expenses of the water system. Transfers are made from the revenue fund to the reserve fund as stipulated by the bond agreements. Contributions in aid of construction are deposited directly to the reserve fund. Transfers from the revenue fund to the sinking fund are made to sufficiently meet the required bond and interest payments to the Farmers Home Administration.
 5. The District invests its reserves in short-term certificates of deposits with local financial institutions. All certificates of deposit are considered to be cash equivalents.
 6. Operating revenues include all utility service related revenues primarily derived from distributing water to Marion County and Nelson County residents. Non-operating revenues include revenues from rents, outside billings, interest, and other miscellaneous, non-operating revenues.
 7. When the District incurs an expense for which both restricted and unrestricted net assets are available, the District's policy is to expend restricted net assets to the extent available first and then to expend unrestricted net assets.

B. Cash:

At year end the carrying amount of the District's cash and cash equivalents was \$2,212,551. Of the total cash, \$1,000,000 was covered by Federal Depository Insurance, \$1,212,551 was covered by collateral agreements and collateral held by the pledging banks' trust departments in the District's name.

Notes to Financial Statements (Continued)

B. Cash (Continued):

Bond documents require the maintenance of certain accounts that are restricted as to withdrawal. Included in cash at December 31, 2012 and 2011, were the following restricted funds:

	<u>2012</u>	<u>2011</u>
Reserve Funds	57,317	85,217
Short-Lived Asset Account	<u>98,738</u>	<u>82,772</u>
Total	<u>156,055</u>	<u>167,989</u>

C. Utility Plant:

The following represents the amount of utility plant as of December 31, 2011 and 2012:

	Beginning Balance	Additions	Deletions	Ending Balance
Nondepreciable Assets:				
Land	52,205	7,503	0	59,708
Depreciable Assets:				
Distribution Plant	16,449,903	340,906	85,235	16,705,574
General Plant	<u>749,130</u>	<u>32,209</u>	<u>25,932</u>	<u>755,407</u>
	17,251,238	380,618	111,167	17,520,689
Less: Accumulated Depreciation	<u>(5,253,247)</u>	<u>(406,482)</u>	<u>93,465</u>	<u>(5,566,264)</u>
	<u>11,997,991</u>	<u>(25,864)</u>	<u>17,702</u>	<u>11,954,425</u>

No interest was capitalized during the years ended December 31, 2012 and 2011, respectively.

- D. The 2009 Series Revenue Bond Issue are Build America Bonds whereby the United States Treasury refunds to the Marion County Water District 35% of the interest paid on these bonds and thus reducing the effective rate of interest from 3.5% to 2.275% per annum.

E. Revenue Bonds Payable:

Water Revenue Bond Series of 1992A - Interest due semiannually January 1 and July 1 at 5% with varying principal payments due January 1 of each year through 2032	357,000
Water Revenue Bond Series of 1993 - Interest due semiannually January 1 and July 1 at 4.50% with varying principal payments due January 1 of each year through 2032	167,000
Water Revenue Bond Series of 1996 - Interest due semiannually January 1 and July 1 at 4.50% with varying principal payments due January 1 of each year through 2035	100,100

Notes to Financial Statements (Continued)

E. Revenue Bonds Payable (Continued):

Water Revenue Bond Series of 2000 - Interest due semiannually
January 1 and July 1 at 4.75% with varying principal payments
due January 1 of each year through 2039 296,000

Water Revenue Bond Series of 2009 - Interest due semiannually
January 1 and July 1 at 3.25% with varying principal payments
due January 1 of each year through 2050 1,415,000
2,335,100

Maturities for the next five years are as follows:

2014	45,300
2015	46,400
2016	48,500
2017	50,100
2018	52,800
Thereafter	<u>2,092,000</u>
	<u>2,335,100</u>

F. Long-term liability activity for the year ended December 31, 2012, was as follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Revenue Bonds Payable	<u>2,797,700</u>	<u>0</u>	<u>462,600</u>	<u>2,335,100</u>	<u>45,300</u>
Total	<u>2,797,700</u>	<u>0</u>	<u>462,600</u>	<u>2,335,100</u>	<u>45,300</u>

G. Appropriated Retained Earnings:

Appropriated retained earnings at December 31, 2012 and 2011, consist of restricted funds as follows:

	<u>2012</u>	<u>2011</u>
CDs - Reserve Fund	650,003	650,003
Cash - Reserve Fund	57,317	85,217
Cash - Short-Lived Asset Fund	<u>98,738</u>	<u>82,771</u>
	<u>806,058</u>	<u>817,991</u>

These funds are restricted in accordance with the provisions of the six outstanding bond issues. Reserve funds must be maintained at a level of \$285,900. The bond provisions allow the District to invest these funds in interest-bearing obligations maturing no later than three years after the date of investment.

Notes to Financial Statements (Continued)

- H. Marion County Water District began participating in the County Employees' Retirement System in January 2003, pursuant to KRS 78.530 administered by the Board of Trustees of the Kentucky Retirement Systems. This is a cost sharing, multiple-employer defined benefit pension plan, which covers all eligible full-time employees and provides for retirement, disability, and death benefits to plan members. Benefit contributions and provisions are established by statute.

All Marion County Water District employees are considered to be nonhazardous employees. Benefits fully vest on reaching five years of service. Aspects of benefits for nonhazardous employees include retirement after 27 years of service or age 65. Employees hired prior to September 15, 2008 are required to contribute 5% of their salary to the plan and employees hired after September 15, 2008 are required to contribute 6% of their salary to the plan.

Historical trend information showing the CERS' progress in accumulating sufficient assets to pay benefits when due is presented in the Kentucky Retirement Systems' annual financial report. This report may be obtained by writing the Kentucky Retirement System, 1260 Louisville Road, Frankfort, Kentucky, 40601-6124, or by telephone at (502) 564-4646.

The District contributed 18.96% of wages from January 1, 2012 through June 30, 2012 and 19.55% of wages from July 1, 2012 through December 31, 2012. The pension expense for 2012 was \$48,808, the pension expense for 2011 was \$40,653, and the pension expense for 2010 was \$39,045.

- I. Risk Management: The District insures against significant losses by commercial insurance. There have been no significant reductions in insurance coverage.
- J. The District generates approximately 96% of its revenues from water sales. Of the water sold, approximately, 99% is purchased from the Lebanon Water Works, a division of the City of Lebanon.
- K. Insurance Recovery: The District received \$10,800 of insurance proceeds due to vandalism of a water tank. These proceeds have been including in Statement of Income for 2012 as miscellaneous, non-operating income.
- L. Management has reviewed subsequent events through January 25, 2012. There are no material subsequent events that require disclosure.

Marion County Water District
Lebanon, Kentucky

Schedules of Operating and Maintenance Expenses
Years Ended December 31, 2012 and 2011

	<u>2012</u>	<u>Percent of Revenue</u>	<u>2011</u>	<u>Percent of Revenue</u>
Source of Supply Expense				
Purchased Water	1,315,096	52.5%	1,289,191	51.8%
Pumping Expense				
Fuel or Power Purchased for Pumping	40,633	1.6%	37,356	1.5%
Transmission & Distribution Expense				
Salaries	121,126	4.8%	106,835	4.3%
Operation Supplies & Expense	37,614	1.5%	35,716	1.4%
Maintenance	<u>85,789</u>	<u>3.4%</u>	<u>63,247</u>	<u>2.5%</u>
Total Transmission & Distribution Expense	244,529	9.8%	205,798	8.3%
Customer Accounts Expense				
Salaries	104,163	4.2%	99,789	4.0%
Contractual Services - Meter Reading	40,026	1.6%	48,026	1.9%
Supplies & Expense	34,692	1.4%	32,988	1.3%
Uncollectible Accounts	<u>9,745</u>	<u>0.4%</u>	<u>4,357</u>	<u>0.2%</u>
Total Customer Accounts Expense	188,626	7.5%	185,160	7.4%
Administrative & General Expense				
Administrative & General Salaries	35,693	1.4%	35,148	1.4%
Office Supplies & Other Expense	17,494	0.7%	20,482	0.8%
Outside Service Employed	11,435	0.5%	11,293	0.5%
Insurance	20,946	0.8%	21,449	0.9%
Employee Benefits	112,329	4.5%	96,226	3.9%
Regulatory Commission Expense	4,424	0.2%	3,858	0.2%
Miscellaneous	<u>9,901</u>	<u>0.4%</u>	<u>7,561</u>	<u>0.3%</u>
Total Administrative & General Expense	<u>212,222</u>	<u>8.5%</u>	<u>196,017</u>	<u>7.9%</u>
Total Operating & Maintenance Expense	<u><u>2,001,106</u></u>	<u><u>79.9%</u></u>	<u><u>1,913,522</u></u>	<u><u>76.8%</u></u>

See accompanying accountants' report.

DESIGNATION OF BOND: "Marion County Water District Water System Revenue Bonds, Series of 1992A," (Numbered R-1)

AMOUNT DUE: \$357,000

CHARACTER OF BOND: Single, non-negotiable bond in fully registered form, payable to the United States of America, Farmers Home Administration, as specifically provided in that certain Resolution adopted by the Commission of the Marion County Water District on August 20, 1992.

DATE: March 31, 1993

DENOMINATION: \$500,000

PAYABLE AS TO PRINCIPAL IN ANNUAL INSTALLMENTS ON JANUARY 1 OF THE RESPECTIVE YEARS AS FOLLOWS:

<u>YEAR</u>	<u>PRINCIPAL</u>	<u>YEAR</u>	<u>PRINCIPAL</u>
2014	12,000	2024	19,000
2015	12,000	2025	20,000
2016	13,000	2026	21,000
2017	14,000	2027	22,000
2018	14,000	2028	23,000
2019	15,000	2029	25,000
2020	16,000	2030	25,000
2021	16,000	2031	27,000
2022	18,000	2032	27,000
2023	18,000		

INTEREST RATE: Five percentum (5%) per annum, payable semiannually on each January 1 and July 1 to maturity of principal.

See accompanying accountant's report.

DESIGNATION OF BOND: "Marion County Water District Water System Revenue Bonds, Series of 1993," (Numbered R-1)

AMOUNT DUE: \$167,000

CHARACTER OF BOND: Single, non-negotiable bond in fully registered form, payable to the United States of America, Farmers Home Administration, as specifically provided in that certain Resolution adopted by the Commission of Marion County Water District on March 9, 1993.

DATE: June 20, 1994

DENOMINATION: \$235,000

PAYABLE AS TO PRINCIPAL IN ANNUAL INSTALLMENTS ON JANUARY 1 OF THE RESPECTIVE YEARS AS FOLLOWS:

<u>YEAR</u>	<u>PRINCIPAL</u>	<u>YEAR</u>	<u>PRINCIPAL</u>
2014	5,500	2024	9,000
2015	6,000	2025	9,500
2016	6,000	2026	10,000
2017	6,500	2027	10,000
2018	7,000	2028	10,500
2019	7,000	2029	11,000
2020	7,500	2030	11,500
2021	8,000	2031	12,000
2022	8,000	2032	13,000
2023	9,000		

INTEREST RATE: Four and one-half percentum (4-1/2%) per annum, payable semiannually on each January 1 and July 1, beginning July 1, 1994, to maturity of principal.

See accompanying accountant's report.

DESIGNATION OF BOND: "Marion County Water District Water System Revenue Bonds, Series of 1996," (Numbered R-1)

AMOUNT DUE: \$100,100

CHARACTER OF BOND: Single, non-negotiable bond in fully registered form, payable to the United States of America, Farmers Home Administration, as specifically provided in that certain Resolution adopted by the Commission of Marion County Water District on January 19, 1996.

DATE: January 19, 1996

DENOMINATION: \$131,000

PAYABLE AS TO PRINCIPAL IN ANNUAL INSTALLMENTS ON JANUARY 1 OF THE RESPECTIVE YEARS AS FOLLOWS:

<u>YEAR</u>	<u>PRINCIPAL</u>	<u>YEAR</u>	<u>PRINCIPAL</u>
2014	2,800	2025	4,500
2015	2,900	2026	4,700
2016	3,000	2027	4,900
2017	3,100	2028	5,100
2018	3,300	2029	5,300
2019	3,400	2030	5,600
2020	3,600	2031	5,800
2021	3,700	2032	6,100
2022	3,900	2033	6,300
2023	4,100	2034	6,700
2024	4,300	2035	7,000

INTEREST RATE: Four and one-half percentum (4-1/2%) per annum, payable semiannually on each January 1 and July 1, beginning July 1, 1997, to maturity of principal.

See accompanying accountant's report.

DESIGNATION OF BOND: "Marion County Water District Water System Revenue Bonds, Series of 2000," Numbered R-1

AMOUNT DUE: \$296,000

CHARACTER OF BOND: Single, non-negotiable bond in fully registered form, payable to the United States Department of Agriculture, Rural Development, as specifically provided in that certain Resolution adopted by the Commission of Marion County Water District on June 28, 2000.

DATE: June 28, 2000

DENOMINATION: \$350,000

PAYABLE AS TO PRINCIPAL IN ANNUAL INSTALLMENTS ON JANUARY 1 OF THE RESPECTIVE YEARS AS FOLLOWS:

<u>YEAR</u>	<u>PRINCIPAL</u>	<u>YEAR</u>	<u>PRINCIPAL</u>
2014	6,000	2027	11,000
2015	6,500	2028	11,500
2016	6,500	2029	12,000
2017	7,000	2030	12,500
2018	7,000	2031	13,500
2019	7,500	2032	13,500
2020	8,000	2033	14,500
2021	8,500	2034	15,000
2022	8,500	2035	16,000
2023	9,000	2036	16,500
2024	9,500	2037	17,500
2025	10,000	2038	18,500
2026	10,500	2039	19,500

INTEREST RATE: Four and seventy-five hundredths percentum (4.75%) per annum payable semiannually on each January 1 and July 1, beginning June 1, 2001, to maturity of principal.

See accompanying accountant's report.

DESIGNATION OF BOND: "Marion County Water District, Water System Revenue Bond, Taxable Series of 2009 (Build America Bonds-Direct Payment to Issuer)," Numbered R-1

AMOUNT DUE: \$1,415,000

CHARACTER OF BOND: Single, non-negotiable bond in fully registered form, payable to the United States Department of Agriculture, Rural Development, as specifically provided in that certain Resolutions adopted by the Commission of Marion County Water District on October 20, 2009, and May 11, 2010.

DATE: June 9, 2010

DENOMINATION: \$1,433,000

PAYABLE AS TO PRINCIPAL IN ANNUAL INSTALLMENTS ON JANUARY 1 OF THE RESPECTIVE YEARS AS FOLLOWS:

<u>YEAR</u>	<u>PRINCIPAL</u>	<u>YEAR</u>	<u>PRINCIPAL</u>
2014	19,000	2033	37,000
2015	19,000	2034	38,000
2016	20,000	2035	40,000
2017	21,000	2036	41,000
2018	22,000	2037	43,000
2019	22,000	2038	44,000
2020	23,000	2039	46,000
2021	24,000	2040	47,000
2022	25,000	2041	49,000
2023	26,000	2042	51,000
2024	27,000	2043	53,000
2025	28,000	2044	55,000
2026	29,000	2045	57,000
2027	30,000	2046	59,000
2028	31,000	2047	61,000
2029	32,000	2048	63,000
2030	33,000	2049	65,000
2031	34,000	2050	65,000
2032	36,000		

INTEREST RATE: Three and twenty-five hundredths percentum (3.25%) per annum payable semiannually on each January 1 and July 1, beginning June 1, 2013, to maturity of principal.

See accompanying accountant's report.

MARION COUNTY WATER DISTRICT
SCHEDULE OF PRIOR YEAR AUDIT FINDINGS AND RESPONSES
DECEMBER 31, 2012

2010-1 Lack of Controls Over Financial Reporting:

During the planning and performance of the audit, it was determined that there is not an effective system of controls over financial reporting. Financial reporting includes drafting the financial statements and notes to the financial statements. It was noted that the District does not have a person with the expertise to draft the financial statements and notes to the financial statements.

2010-1 Current Year Status:

The District was unable to correct this deficiency. Management feels that the costs of correcting this internal control matter outweigh the benefits.

WHITE AND COMPANY, P.S.C.

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Charles M. White, CPA

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

January 25, 2013

To the Commissioners of the
Marion County Water District

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 general purpose financial statements of Marion County Water District, Lebanon, Kentucky as of and for the years ended December 31, 2012 and 2011, and the related notes to the financial statements, which collectively comprise Marion County Water District, Lebanon, Kentucky's basic financial statements and have issued our report thereon dated January 25, 2013.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered Marion County Water District, Lebanon, Kentucky's internal control over financial reporting (*internal control*) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of Marion County Water District, Lebanon, Kentucky's internal control. Accordingly, we do not express an opinion on the effectiveness of Marion County Water District, Lebanon, Kentucky'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 combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. Given these limitations, during our audit we did not identify any deficiencies in internal control 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 schedules of findings and responses that we consider to be significant deficiencies. [2010-1].

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Marion County Water District, Lebanon, Kentucky'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*.

Marion County Water District, Lebanon, Kentucky's Response to Findings

Marion County Water District, Lebanon, Kentucky's response to the findings identified in our audit is described in the accompanying schedule of findings and responses. Marion County Water District, Lebanon, Kentucky's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

Purpose of this Report

This purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with Government Auditing Standards in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Sincerely,

White and Company, P.S.C.

Certified Public Accountants

WHITE AND COMPANY, P.S.C.
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Charles M. White, CPA

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January 25, 2013

To the Commissioners of the
Marion County Water District

We have audited the general purpose financial statements of the Marion County Water District, Lebanon, Kentucky as of and for the year ended December 31, 2012, and have issued our report thereon dated January 25, 2013. Professional standards require that we provide you with information about our responsibilities under generally accepted auditing standards (and, if applicable, *Government Auditing Standards* and OMB Circular A-133), as well as certain information related to the planned scope and timing of our audit. We have communicated such information in our letter to you dated November 27, 2012. Professional standards also require that we communicate to you the following information related to our audit.

Significant Auditing Findings

Qualitative Aspects of Accounting Practices

Management is responsible for the selection and use of appropriate accounting policies. The significant accounting polices used by Marion County Water District are described in Note 1 to the financial statements. No new accounting policies were adopted and the application of existing policies was not changed during 2012. We noted no transactions entered into by the governmental unit during the year for which there is a lack of authoritative guidance or consensus. All significant transactions have been recognized in the financial statements in the proper period.

Accounting estimates are an integral part of the financial statements prepared by management and are based on management's knowledge and experience about past and current events and assumptions about future events. Certain accounting estimates are particularly sensitive because of their significance to the financial statements and because of the possibility that future events affecting them may differ significantly from those expected. The most sensitive estimate affecting the financial statements was:

Management's estimate of the useful lives of capital assets for computation of depreciation. We evaluated the key factors and assumptions used to develop the computation of depreciation in determining that it is reasonable in relation to the financial statements taken as a whole.

Difficulties Encountered in Performing the Audit

We encountered no significant difficulties in dealing with management in performing and completing our audit.

Corrected and Uncorrected Misstatements

Professional standards require us to accumulate all known and likely misstatements identified during the audit, other than those that are clearly trivial, and communicate them to the appropriate level of management. Management has corrected all such misstatements. In addition, none of the misstatements detected as a result of audit procedures and corrected by management were material, either individually or in the aggregate, to the financial statements taken as a whole.

Disagreements with Management

For purposes of this letter, a disagreement with management as a financial accounting, reporting, or auditing matter, whether or not resolved to our satisfaction, that could be significant to the financial statements or the auditor's report. We are pleased to report that no such disagreements arose during the course of our audit.

Management Representations

We have requested certain representations from management that are included in the management representation letter dated January 17, 2013.

Management Consultations with Other Independent Accountants

In some cases, management may decide to consult with other accountants about auditing and accounting matters, similar to obtaining a "second opinion" on certain situations. If a consultation involves application of an accounting principle to the governmental unit's financial statements or a determination of the type of auditor's opinion that may be expressed on those statements, our professional standards require the consulting accountant to check with us to determine that the consultant has all the relevant facts. To our knowledge, there were not such consultations with other accountants.

Other Audit Findings or Issues

We generally discuss a variety of matters, including the application of accounting principles and auditing standards, with management each year prior to retention as the governmental unit's auditors. However, these discussions occurred in the normal course of our professional relationship and our responses were not a condition to our retention.

Other Matters

With respect to the supplementary information accompanying the financial statements, we made certain inquiries of management and evaluated the form, content, and methods of preparing the information to determine that the information complies with accounting principles generally accepted in the United States of America, the method of preparing it has not changed from the prior period, and the information is appropriate and complete in relation to the underlying accounting records used to prepare the financial statements or to the financial statements themselves.

This information is intended solely for the use of Marion County Water District's Commissioners and management of Marion County Water District and is not intended to be and should not be used by anyone other than these specified parties.

Sincerely,

White and Company, P.S.C.

Certified Public Accountants