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**PUBLIC SERVICE
COMMISSION**

**U.S. 60 WATER DISTRICT
OF SHELBY AND FRANKLIN COUNTIES**

**BASIC FINANCIAL STATEMENTS
AND INDEPENDENT AUDITOR'S REPORTS**

At December 31, 2012 and 2011

RAISOR, ZAPP & WOODS, PSC
CERTIFIED PUBLIC ACCOUNTANTS

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AND INDEPENDENT AUDITOR'S REPORTS**

Years Ended December 31, 2012 and 2011

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To the Commissioners of the
U.S. 60 Water District of Shelby and Franklin Counties
Bagdad, Kentucky 40003

INDEPENDENT AUDITOR'S REPORT

Report on the Financial Statements

We have audited the accompanying financial statements of U.S. 60 Water District of Shelby and Franklin Counties as of and for the years ended December 31, 2012 and 2011, and the related notes to the financial statements, which collectively comprise the U.S. 60 Water District of Shelby and Franklin Counties' basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the U.S. 60 Water District of Shelby and Franklin Counties, as of December 31, 2012 and 2011, and the respective changes in financial position and cash flows thereof for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Management has omitted the management's discussion and analysis that accounting principles generally accepted in the United States of America require to be presented to supplement the basic financial statements. Such missing 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. Our opinion on the basic financial statements is not affected by this missing information.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated March 25, 2013, on our consideration of the U.S. 60 Water District of Shelby and Franklin Counties' 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 U.S. 60 Water District of Shelby and Franklin Counties' internal control over financial reporting and compliance.

Raisor, Zapp & Woods, PSC

RAISOR, ZAPP & WOODS, PSC
Certified Public Accountants
Carrollton, Kentucky

March 25, 2013

U.S. 60 WATER DISTRICT OF SHELBY AND FRANKLIN COUNTIES
STATEMENT OF NET POSITION
December 31, 2012 and 2011

	2012	2011
ASSETS		
Current Assets:		
Cash, Including Time Deposits	\$ 1,589,951	\$ 1,402,495
Accounts Receivable (Net)	117,745	112,197
Interest Receivable	528	535
Prepaid Insurance	6,017	4,896
Total Current Assets	\$ 1,714,241	\$ 1,520,123
Noncurrent Assets:		
Restricted Assets:		
Cash, Including Time Deposits	\$ 560,721	\$ 560,834
Interest Receivable	663	927
Bond and Note Payable Issuance Costs (Net)	5,470	10,378
Capital Assets (Net)	6,057,634	6,313,876
Total Noncurrent Assets	\$ 6,624,488	\$ 6,886,015
Total Assets	\$ 8,338,729	\$ 8,406,138
LIABILITIES		
Current Liabilities:		
Accounts Payable	\$ 72,118	\$ 87,419
Accounts Payable - Construction	-	36,589
Retainage Payable - Construction	-	5,946
Accrued Payroll Taxes/Employee Withholding	1,055	1,071
Utility Tax Payable	2,474	2,337
Sales Tax Payable	124	96
Current Liabilities Payable from Restricted Assets:		
Accrued Interest Payable - Customer Deposits	1,075	1,059
Accrued Interest Payable - Long Term Debt	35,901	36,792
Revenue Bonds Payable	32,700	30,900
Notes Payable	35,000	35,000
Total Current Liabilities	\$ 180,447	\$ 237,209
Noncurrent Liabilities:		
Revenue Bonds Payable	\$ 1,584,100	\$ 1,616,800
Notes Payable	17,500	52,500
Noncurrent Liabilities Payable from Restricted Assets:		
Customer Deposits Payable	117,019	115,733
Total Noncurrent Liabilities	\$ 1,718,619	\$ 1,785,033
Total Liabilities	\$ 1,899,066	\$ 2,022,242
NET POSITION		
Net Investment in Capital Assets	\$ 4,393,804	\$ 4,589,054
Restricted for Capital Projects	8,290	20,413
Restricted for Debt Service	400,174	346,287
Unrestricted	1,637,395	1,428,142
Total Net Position	\$ 6,439,663	\$ 6,383,896

U.S. 60 WATER DISTRICT OF SHELBY AND FRANKLIN COUNTIES
STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN FUND NET POSITION
For the Years Ended December 31, 2012 and 2011

	2012	2011
Operating Revenues:		
Charges for Services:		
Water Charges (Net of Estimated Bad Debts)	\$ 1,039,657	\$ 975,228
Total Charges for Services	\$ 1,039,657	\$ 975,228
Other Charges and Miscellaneous:		
Forfeited Discounts & Service Charges	\$ 33,768	\$ 33,063
Miscellaneous	7,500	244
Total Other Charges and Miscellaneous	\$ 41,268	\$ 33,307
Total Operating Revenues	\$ 1,080,925	\$ 1,008,535
Operating Expenses:		
Commissioner Fees	\$ 13,750	\$ 13,000
Contractual Service	161,121	165,062
Insurance	10,504	10,090
Maintenance of Mains	47,247	30,516
Miscellaneous	1,175	6,292
Office Supplies and Expense	21,052	16,799
Other Interest Expense	1,134	1,111
Payroll Taxes	1,373	1,304
Professional Services	22,819	27,534
Purchased Water	334,228	321,476
Purchased Power	27,224	27,224
Regulatory Fees	1,772	1,583
Rental of Building	24,000	24,000
Rental of Equipment	55,546	58,022
Depreciation Expense	236,231	235,259
Total Operating Expenses	\$ 959,176	\$ 939,272
Net Operating Income	\$ 121,749	\$ 69,263
Nonoperating Revenue (Expense):		
Investment Income	\$ 8,406	\$ 13,598
Interest Expense	(89,880)	(94,418)
Amortization Expense	(4,908)	(4,908)
Total Nonoperating Revenue (Expense)	\$ (86,382)	\$ (85,728)
Net Income Before Contributions	\$ 35,367	\$ (16,465)
Capital Contributions	20,400	180,728
Net Income	\$ 55,767	\$ 164,263
Net Position--Beginning of Year	6,383,896	6,219,633
Net Position--End of Year	\$ 6,439,663	\$ 6,383,896

U.S. 60 WATER DISTRICT OF SHELBY AND FRANKLIN COUNTIES
STATEMENT OF CASH FLOWS
For the Years Ended December 31, 2012 and 2011

	2012	2011
CASH FLOWS FROM OPERATING ACTIVITIES		
Receipts from Customers	\$ 1,075,377	\$ 1,020,175
Payments to Suppliers	(723,492)	(682,962)
Payments to Employees	(15,875)	(15,075)
Other Receipts (Payments)	1,451	950
Net Cash Provided (Used) by Operating Activities	\$ 337,461	\$ 323,088
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Grant Proceeds	\$ 10,000	\$ 169,913
Capital Contributions	10,400	10,815
Purchase of Capital Assets	(22,524)	(296,780)
Principal Paid on Long Term Debt	(65,900)	(104,200)
Interest Paid on Long Term Debt	(90,771)	(95,043)
Net Cash Provided (Used) by Capital and Related Financing Activities	\$ (158,795)	\$ (315,295)
CASH FLOWS FROM INVESTING ACTIVITIES		
Net Cash Invested in Certificates of Deposit	\$ (7,461)	\$ (12,392)
Interest Received	8,677	14,773
Net Cash Provided (Used) by Investing Activities	\$ 1,216	\$ 2,381
Net Increase (Decrease) in Cash and Cash Equivalents	\$ 179,882	\$ 10,174
Balances-Beginning of the Year	977,928	967,754
Balances-End of the Year	\$ 1,157,810	\$ 977,928

	Balances Per December 31, 2012 Statement of Net Position	Balances Per December 31, 2012 Statement of Cash Flows
Cash	\$ 1,021,708	\$ 1,021,708
Time Deposits	685,262	-
Restricted Cash	136,102	136,102
Restricted Time Deposits	307,600	-
Total Cash and Cash Equivalents, End of Year	\$ 2,150,672	\$ 1,157,810
	Balances Per December 31, 2011 Statement of Net Position	Balances Per December 31, 2011 Statement of Cash Flows
Cash	\$ 722,005	\$ 722,005
Time Deposits	680,490	-
Restricted Cash	255,923	255,923
Restricted Time Deposits	304,911	-
Total Cash and Cash Equivalents, End of Year	\$ 1,963,329	\$ 977,928

(Continued)

U.S. 60 WATER DISTRICT OF SHELBY AND FRANKLIN COUNTIES
STATEMENT OF CASH FLOWS
For the Years Ended December 31, 2012 and 2011

	2012	2011
RECONCILIATION OF OPERATING INCOME (LOSS) TO NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES		
Operating Income (Loss)	\$ 121,749	\$ 69,263
Adjustments to Reconcile Operating Income to Net Cash Provided (Used) by Operating Activities:		
Cash Flows Reported in Other Categories:		
Depreciation Expense	236,231	235,259
Change in Assets and Liabilities:		
Receivables, Net	(5,548)	11,640
Prepaid Expenses	(1,121)	(404)
Accounts and Other Payables	(15,301)	6,380
Accrued Expenses	165	(119)
Customer Meter Deposits Payable	1,286	1,069
	\$ 337,461	\$ 323,088
Net Cash Provided by Operating Activities		

SCHEDULE OF NONCASH INVESTING, CAPITAL, AND FINANCING ACTIVITIES

At December 31, 2011, U.S. 60 Water District of Shelby and Franklin Counties had \$42,535 of capitalized expenditures for the construction/acquisition of plant assets included in accounts payable on the Statement of Net assets.

U.S. 60 WATER DISTRICT OF SHELBY AND FRANKLIN COUNTIES
NOTES TO BASIC FINANCIAL STATEMENTS
December 31, 2012 and 2011

NOTE 1 – DESCRIPTION OF ENTITY AND SIGNIFICANT ACCOUNTING POLICIES

The U.S. 60 Water District of Shelby and Franklin Counties is a rural Water District serving customers in Anderson, Franklin, Shelby and Spencer Counties, Kentucky, and is regulated by the Public Service Commission of the Commonwealth of Kentucky. The Water District was formed under the laws of the above-mentioned counties through their Fiscal Courts and began operations in June, 1960.

In evaluating how to define U.S. 60 Water District of Shelby and Franklin Counties for financial reporting purposes, management has considered all potential component units. The decision to include a potential component unit in the reporting entity was made by applying the criteria set forth in GAAP. The basic -- but not the only -- criterion for including a potential component unit within the reporting entity is the governing body's ability to exercise oversight responsibility. The most significant manifestation of this ability is financial interdependency. Other manifestations of the ability to exercise oversight responsibility include, but are not limited to, the selection of governing authority, the designation of management, the ability to significantly influence operations and accountability for fiscal matters. The other criterion used to evaluate potential component units for inclusion or exclusion from the reporting entity is the existence of special financing relationships, regardless of whether the District is able to exercise oversight responsibilities. Based upon the application of these criteria, the District has no component units.

A summary of the District's significant accounting policies follows:

Basis of Presentation and Accounting: As stated in Kentucky Revised Statutes (KRS) 278.015, "any water district shall be a public utility and shall be subject to the jurisdiction of the Public Service Commission." In KRS 278.220, it is outlined that the Public Service Commission may establish a system of accounts to be kept by the utilities subject to its jurisdiction, and may prescribe the manner in which such accounts shall be kept. The financial statements of the District are prepared in accordance with generally accepted accounting principles (GAAP). The District applies all relevant Governmental Accounting Standards Board (GASB) pronouncements.

All activities of the District are accounted for within a single proprietary (enterprise) fund. Proprietary funds are used to account for operations that are (a) financed and operated in a manner similar to private business enterprises where the intent of the governing body is that the cost (expenses, including depreciation) of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges; or (b) where the governing body has decided that periodic determination of revenues earned, expenses incurred, and/or net income is appropriate for capital maintenance, public policy, management control, accountability, or other purposes.

Proprietary funds utilize the accrual basis of accounting. Under the accrual basis of accounting, revenues are recognized when earned and expenses are recorded when the liability is incurred or economic asset used.

The accounting and financial reporting treatment applied to the District is determined by its measurement focus. The transactions of the District are accounted for on a flow of economic resources measurement focus. The accounting objectives of this measurement focus are the determination of operating income, changes in net position (or cost recovery), financial position, and cash flows. With this measurement focus, all assets and all liabilities associated with the operations are included on the statement of net position. Net position (i.e., total assets net of total liabilities) are segregated into net investment in capital assets, restricted; and unrestricted components.

Revenues and Expenses: Operating revenues and expenses consist of those revenues and expenses that result from the ongoing principal operations of the District. Operating revenues consist primarily of charges for services. Non-operating revenues and expenses consist of those revenues and expenses that are related to financing and investing types of activities and result from nonexchange transactions or ancillary activities. The District adheres to the use restrictions established by debt agreements when expenses are incurred for which both restricted and unrestricted net assets are available. The District has no policy defining which resources (restricted or unrestricted) to use first.

U.S. 60 WATER DISTRICT OF SHELBY AND FRANKLIN COUNTIES
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
December 31, 2012 and 2011

NOTE 1 – DESCRIPTION OF ENTITY AND SIGNIFICANT ACCOUNTING POLICIES (Continued)

Property and Equipment: Property and equipment purchased or constructed is stated at cost. Interest related to costs, and major improvements, renewals and replacements is capitalized as a cost of the project. Costs associated with hook-up fees are capitalized as meters, installations, and services. Depreciation is computed on the straight-line basis over the estimated useful lives of the related assets. The range of estimated useful lives by type of asset is as follows:

- Distribution System	15-50 years
- Machinery & Equipment	5-50 years

Income Taxes: The U.S. 60 Water District of Shelby and Franklin Counties is not subject to income taxes.

Bond and Note Payable Issuance Costs: Such costs are amortized over the life of the respective bond issue or note payable using the straight line method.

Contributed Capital: Under the Governmental Accounting Standards Board's (GASB) Statement No. 33, *Accounting and Financial Reporting for Nonexchange Transactions*, the District recognizes capital contributions as revenues in the statement of revenues, expenses, and changes in fund net position. Grants of \$10,000 and \$169,913 were received by the District for the years ended December 31, 2012 and December 31, 2011, respectively. Tap-on fees of \$10,400 and \$10,815 were received by the District for the years ended December 31, 2012 and 2011, respectively.

Net Position: The District adopted Statement of Governmental Standards (GASB Statement) No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflow of Resources, and Net Position*, which requires the District to report net position and changes the title of the Statement of Net Assets to the Statement of Net Position (effective for periods beginning after December 15, 2011). Net position comprises the various net earnings from operating and non-operating revenues, expenses and contributions of capital. Net position is classified in the following three components: net investment in capital assets; restricted; and unrestricted net position. Net investment in capital assets consists of all capital assets, net of accumulated depreciation and reduced by outstanding debt that is attributable to the acquisition, construction and improvement of those assets; debt related to unspent proceeds or other restricted cash and investments is excluded from the determination. Restricted net position consists of net position for which constraints are placed thereon by external parties, such as lenders, grantors, contributors, laws, regulations and enabling legislation, including self-imposed legal mandates. Unrestricted net position consists of all other net position not included in the above categories.

Estimates: The preparation of financial statements 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.

Statement of Cash Flows: For the purpose of the Statement of Cash Flows, U.S. 60 Water District of Shelby and Franklin Counties considers all highly liquid investments (including restricted assets) with a maturity of three months or less when purchased to be cash equivalents.

NOTE 2 – DEBT RESTRICTIONS AND COVENANTS

A Bond and Interest Sinking Account was established with the original RECD bond issue, and is to be maintained as long as any of the 1992, 1998, 2008A or 2008B issues are outstanding. A minimum balance is to be maintained in this account as security to the bondholders. In order to attain the minimum balance, a monthly transfer must be made as follows:

	one sixth (1/6) of the next semiannual interest payment
+	<u>one twelfth (1/12) of the next annual principal payment</u>
=	monthly transfer

Transfers sufficient to meet the total obligation were made timely during the years ended December 31, 2012 and 2011.

U.S. 60 WATER DISTRICT OF SHELBY AND FRANKLIN COUNTIES
 NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
 December 31, 2012 and 2011

NOTE 2 – DEBT RESTRICTIONS AND COVENANTS (Continued)

Under the 1992, 1998, 2008A, and 2008B bond resolutions, a Depreciation Account is to be maintained as long as any of the bonds are outstanding to provide funds for extraordinary repairs and extensions to the system, and to make up any deficiency in the Bond and Interest Sinking Fund Account. The required minimum monthly transfers and balances are as follows:

	Monthly Requirements	Minimum Accumulated Balance
1992 Bond Issue	\$185/month	\$ 22,200
1998 Bond Issue	\$215/month	25,800
2008A & B Bond Issues	\$377/month	44,400
Total		\$ 92,400

When the required balance of \$92,400 is attained, the monthly transfers may be discontinued, but are subject to resumption if the depreciation account is depleted below the required balance. The depreciation account was fully funded for the years ended December 31, 2012 and 2011.

NOTE 3 – CASH AND INVESTMENTS

KRS 66.480 authorizes the District to invest in obligations of the United States and its agencies and instrumentalities including repurchase agreements, through sources including national and state banks chartered in Kentucky, obligations and contracts for future delivery backed by the full faith of the United States or its Agency, certificates of deposit and interest bearing accounts in institutions insured by the Federal Depository Insurance Corporation and other investments described therein provided that approved securities are pledged to secure those funds on deposit in an amount equal to the amount of those funds. The District may also invest in mutual funds meeting the requirements of the statute.

U.S. 60 Water District's policies regarding deposits of cash are discussed above. The table presented below is designed to disclose the level of custody credit risk assumed by the District based upon how its deposits were insured or secured with collateral at December 31, 2012 and 2011. The categories of credit risk are defined as follows:

Category 1 – Insured by FDIC Insurance or collateralized with a depository surety bond or securities held by the District (public trust) or by its agent in its name.

Category 2 – Uninsured but collateralized with securities held by the pledging financial institution's trust department or agent in the District's name.

Category 3 – Uninsured and uncollateralized; or collateralized with securities held by the pledging financial institution, or by its trust department or agent but not in the District's name; or collateralized with no written or approved collateral agreement.

December 31, 2012

Type of Deposits	Total Bank Balance	Custody Credit Risk Category			Total Carrying Value
		1	2	3	
Checking & Savings Deposits	\$ 1,158,518	\$ 307,727	\$ 850,791	\$ -	\$ 1,157,810
Certificates of Deposit	992,862	392,600	600,262	-	992,862
Total Deposits	\$ 2,151,380	\$ 700,327	\$ 1,451,053	\$ -	\$ 2,150,672

December 31, 2011

Type of Deposits	Total Bank Balance	Custody Credit Risk Category			Total Carrying Value
		1	2	3	
Checking & Savings Deposits	\$ 978,663	\$ 302,923	\$ 675,740	\$ -	\$ 977,928
Certificates of Deposit	985,401	407,501	577,900	-	985,401
Total Deposits	\$ 1,964,064	\$ 710,424	\$ 1,253,640	\$ -	\$ 1,963,329

U.S. 60 WATER DISTRICT OF SHELBY AND FRANKLIN COUNTIES
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
December 31, 2012 and 2011

NOTE 3 – CASH AND INVESTMENTS (Continued)

Reconciliation to Statement of Net Position:

	<u>December 31, 2012</u>	<u>December 31, 2011</u>
Unrestricted Cash, Including Time Deposits	\$ 1,589,951	\$ 1,402,495
Restricted Cash, Including Time Deposits	560,721	560,834
	<u>\$ 2,150,672</u>	<u>\$ 1,963,329</u>

NOTE 4 – RESTRICTED ASSETS

Restricted cash and time deposits consist of the following:

	<u>December 31, 2012</u>	<u>December 31, 2011</u>
Bond and Interest Sinking Accounts	\$ 192,037	\$ 190,010
Depreciation Accounts	243,375	234,677
Customer Deposits	117,019	115,733
Construction Accounts	8,290	20,414
	<u>\$ 560,721</u>	<u>\$ 560,834</u>

Restricted receivables consist of the following:

	<u>December 31, 2012</u>	<u>December 31, 2011</u>
Interest Receivable	\$ 663	\$ 927

NOTE 5 – CUSTOMER ACCOUNTS RECEIVABLE

Customer Accounts Receivable has been netted with an Allowance for Bad Debts of \$7,753 and \$7,554 at December 31, 2012 and 2011, respectively. The amount provided for bad debts represents the portion of the total amounts for which collection is unlikely, based on historical collection data.

Estimated unbilled water service of \$39,419 and \$38,722 is included in accounts receivable at December 31, 2012 and 2011, respectively.

NOTE 6 – CAPITAL ASSETS

Capital asset activity for the years ended December 31, 2012 and 2011, was as follows:

	<u>Balance at January 1, 2012</u>	<u>Additions</u>	<u>Disposals</u>	<u>Balance at December 31, 2012</u>
Structures & Improvements	\$ 24,234	\$ -	\$ -	\$ 24,234
Distribution System	9,103,285	10,400	(30,411)	9,083,274
Machinery & Equipment	306,959	-	-	306,959
Totals at Historical Cost	<u>\$ 9,434,478</u>	<u>\$ 10,400</u>	<u>\$ (30,411)</u>	<u>\$ 9,414,467</u>
Less: Accumulated Depreciation				
Structures & Improvements	\$ (22,097)	\$ (254)	\$ -	\$ (22,351)
Distribution System	(2,962,019)	(226,897)	-	(3,188,916)
Machinery & Equipment	(136,486)	(9,080)	-	(145,566)
Total Accumulated Depreciation	<u>\$ (3,120,602)</u>	<u>\$ (236,231)</u>	<u>\$ -</u>	<u>\$ (3,356,833)</u>
Capital Assets, Net	<u>\$ 6,313,876</u>	<u>\$ (225,831)</u>	<u>\$ (30,411)</u>	<u>\$ 6,057,634</u>

U.S. 60 WATER DISTRICT OF SHELBY AND FRANKLIN COUNTIES
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
December 31, 2012 and 2011

NOTE 6 – CAPITAL ASSETS (Continued)

	Balance at January 1, 2011	Additions	Disposals	Balance at December 31, 2011
Structures & Improvements	\$ 24,234	\$ -	\$ -	\$ 24,234
Distribution System	8,768,919	334,366	-	9,103,285
Machinery & Equipment	306,959	-	-	306,959
Totals at Historical Cost	<u>\$ 9,100,112</u>	<u>\$ 334,366</u>	<u>\$ -</u>	<u>\$ 9,434,478</u>
Less: Accumulated Depreciation				
Structures & Improvements	\$ (21,843)	\$ (254)	\$ -	\$ (22,097)
Distribution System	(2,736,094)	(225,925)	-	(2,962,019)
Machinery & Equipment	(127,406)	(9,080)	-	(136,486)
Total Accumulated Depreciation	<u>\$ (2,885,343)</u>	<u>\$ (235,259)</u>	<u>\$ -</u>	<u>\$ (3,120,602)</u>
Capital Assets, Net	<u>\$ 6,214,769</u>	<u>\$ 99,107</u>	<u>\$ -</u>	<u>\$ 6,313,876</u>

Included under the District's capital assets were \$531,302 and \$235,491 of fully depreciated assets at December 31, 2012 and 2011, respectively. Construction in process is not depreciated.

Depreciation expense for 2012 and 2011 was \$236,231 and \$235,259, respectively.

NOTE 7 – CUSTOMER DEPOSITS

Customer deposits are collected upon installation of water service. This amount is to be refunded to the customer upon discontinuation of service (after the customer's bill has been paid in full). Records are maintained which detail the accrued interest on each customer's deposit based on the current annual rate. Accrued interest is paid when the deposit is refunded or credited to the customer's account annually. At December 31, 2012 and 2011, accrued interest on customer deposits was \$1,075 and \$1,059 respectively. The District has not maintained a separate bank account specifically for cash collected and disbursed relating to customer deposits.

NOTE 8 – LONG-TERM DEBT

As of December 31, 2012 and 2011, long-term debt payable consisted of the following:

Bonds Payable:

	<u>December 31, 2012</u>	<u>December 31, 2011</u>
1986 Revenue Bonds, original issue amount of \$350,000, secured by water revenues. Interest is charged at the rate of 7.625% per annum. Final maturity is February, 2025.	\$ 257,000	\$ 266,000
1992 Revenue Bonds, original issue amount of \$294,000, secured by water revenues. Interest is charged at the rate of 6.125% per annum. Final maturity is February, 2032.	233,800	239,300

U.S. 60 WATER DISTRICT OF SHELBY AND FRANKLIN COUNTIES
 NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
 December 31, 2012 and 2011

NOTE 8 – LONG-TERM DEBT (Continued)

	December 31, 2012	December 31, 2011
1998 Revenue Bonds, original issue amount of \$460,700, secured by water revenues. Interest is charged at the rate of 4.5% per annum. Final maturity is February, 2038.	386,700	394,500
2008A Revenue Bonds, original issue amount of \$145,000, secured by water revenues. Interest is charged at the rate of 4.5% per annum. Final maturity is February, 2047.	140,300	141,900
2008B Revenue Bonds, original issue amount of \$619,000, secured by water revenues. Interest is charged at the rate 4.625% per annum. Final maturity is February, 2047.	599,000	606,000
Total Bonds Payable	\$ 1,616,800	\$ 1,647,700
Current Portion	\$ 32,700	\$ 30,900
Noncurrent Portion	1,584,100	1,616,800
Total Bonds Payable	\$ 1,616,800	\$ 1,647,700

The annual requirements for all bonds payable outstanding at December 31, 2012 are as follows:

	Principal	Interest	Total
2013	\$ 32,700	\$ 84,391	\$ 117,091
2014	36,600	82,380	118,980
2015	38,500	80,183	118,683
2016	41,400	77,826	119,226
2017	44,500	75,278	119,778
2018-2022	264,500	332,201	596,701
2023-2027	299,300	241,861	541,161
2028-2032	271,000	170,404	441,404
2033-2037	226,700	109,708	336,408
2038-2042	174,000	61,557	235,557
2043-2047	187,600	22,368	209,968
	\$ 1,616,800	\$ 1,338,157	\$ 2,954,957

The annual requirements for all bonds payable outstanding at December 31, 2011 are as follows:

	Principal	Interest	Total
2012	\$ 30,900	\$ 86,202	\$ 117,102
2013	32,700	84,391	117,091
2014	36,600	82,380	118,980
2015	38,500	80,183	118,683
2016	41,400	77,826	119,226
2017-2021	248,800	347,606	596,406
2022-2026	312,600	259,879	572,479
2027-2031	258,500	183,816	442,316
2032-2036	236,900	120,417	357,317
2037-2041	190,000	69,896	259,896
2042-2046	179,600	30,816	210,416
2047	41,200	947	42,147
	\$ 1,647,700	\$ 1,424,359	\$ 3,072,059

U.S. 60 WATER DISTRICT OF SHELBY AND FRANKLIN COUNTIES
 NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
 December 31, 2012 and 2011

NOTE 8 – LONG-TERM DEBT (Continued)

Notes Payable:

	December 31, 2012	December 31, 2011
1993 Kentucky Infrastructure note, original loan amount \$556,481, secured by water revenues. Interest is charged from 2.25% to 5.29% per annum. Final maturity is June, 2014.	\$ 52,500	\$ 87,500
Total Notes Payable	\$ 52,500	\$ 87,500
	December 31, 2012	December 31, 2011
Current Portion	\$ 35,000	\$ 35,000
Noncurrent Portion	17,500	52,500
Total Notes Payable	\$ 52,500	\$ 87,500

The annual requirements for all notes payable outstanding at December 31, 2012 are as follows:

	Principal	Interest	Service Fees	Total
2013	\$ 35,000	\$ 2,760	\$ 105	\$ 37,865
2014	17,500	926	35	18,461
	\$ 52,500	\$ 3,686	\$ 140	\$ 56,326

The annual requirements for all notes payable outstanding at December 31, 2011 are as follows:

	Principal	Interest	Service Fees	Total
2012	\$ 35,000	\$ 4,550	\$ 175	\$ 39,725
2013	35,000	2,760	105	37,865
2014	17,500	926	35	18,461
	\$ 87,500	\$ 8,236	\$ 315	\$ 96,051

Changes in Long-term Debt

The following is a summary of changes in long-term debt for the year ended December 31, 2012.

	Balance at January 1, 2012	Additions	Retirements	Balance at December 31, 2012	Current Portion
Revenue Bonds Payable	\$ 1,647,700	\$ -	\$ 30,900	\$ 1,616,800	\$ 32,700
Notes Payable	87,500	-	35,000	52,500	35,000
Total Long-Term Debt	\$ 1,735,200	\$ -	\$ 65,900	\$ 1,669,300	\$ 67,700

The following is a summary of changes in long-term debt for the year ended December 31, 2011.

	Balance at January 1, 2011	Additions	Retirements	Balance at December 31, 2011	Current Portion
Revenue Bonds Payable	\$ 1,676,900	\$ -	\$ 29,200	\$ 1,647,700	\$ 30,900
Notes Payable	127,500	-	40,000	87,500	35,000
Capital Lease Obligations	35,000	-	35,000	-	-
Total Long-Term Debt	\$ 1,839,400	\$ -	\$ 104,200	\$ 1,735,200	\$ 65,900

U.S. 60 WATER DISTRICT OF SHELBY AND FRANKLIN COUNTIES
 NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
 December 31, 2012 and 2011

NOTE 8 – LONG-TERM DEBT (Continued)

The annual requirements for all long-term debt outstanding at December 31, 2012 is as follows:

	Principal	Interest	Service Fees	Total
2013	\$ 67,700	\$ 87,151	\$ 105	\$ 154,956
2014	54,100	83,306	35	137,441
2015	38,500	80,183	-	118,683
2016	41,400	77,826	-	119,226
2017	44,500	75,278	-	119,778
2018-2022	264,500	332,201	-	596,701
2023-2027	299,300	241,861	-	541,161
2028-2032	271,000	170,404	-	441,404
2033-2037	226,700	109,708	-	336,408
2038-2042	174,000	61,557	-	235,557
2043-2047	187,600	22,368	-	209,968
	<u>\$ 1,669,300</u>	<u>\$ 1,341,843</u>	<u>\$ 140</u>	<u>\$ 3,011,283</u>

The annual requirements for all long-term debt outstanding, excluding interim financing, at December 31, 2011 is as follows:

	Principal	Interest	Service Fees	Total
2012	\$ 65,900	\$ 90,752	\$ 175	\$ 156,827
2013	67,700	87,151	105	154,956
2014	54,100	83,306	35	137,441
2015	38,500	80,183	-	118,683
2016	41,400	77,826	-	119,226
2017-2021	248,800	347,606	-	596,406
2022-2026	312,600	259,879	-	572,479
2027-2031	258,500	183,816	-	442,316
2032-2036	236,900	120,417	-	357,317
2037-2041	190,000	69,896	-	259,896
2042-2046	179,600	30,816	-	210,416
2047	41,200	947	-	42,147
	<u>\$ 1,735,200</u>	<u>\$ 1,432,595</u>	<u>\$ 315</u>	<u>\$ 3,168,110</u>

NOTE 9 – INTEREST EXPENSE

Interest expense incurred for the year ended December 31, 2012 and 2011 was \$91,014 and \$95,529, respectively. No interest was capitalized in 2012 or 2011.

NOTE 10 – FUND EQUITY – RESTRICTED NET POSITION

	December 31, 2012	December 31, 2011
Restricted for Capital Projects:		
Monies Restricted for Construction	\$ 8,290	\$ 20,413
Total Restricted for Capital Projects	<u>\$ 8,290</u>	<u>\$ 20,413</u>
Restricted for Debt Service:		
Revenue Bonds of 1992, 1998, 2008A & 2008B		
Cash	\$ 435,412	\$ 424,687
Add: Accrued Interest Receivable	663	927
Less: Accrued Interest Payable	(35,901)	(36,792)
Total Restricted for Debt Service	<u>\$ 400,174</u>	<u>\$ 388,822</u>

U.S. 60 WATER DISTRICT OF SHELBY AND FRANKLIN COUNTIES
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
December 31, 2012 and 2011

NOTE 11 – BAD DEBT EXPENSE

Water revenue charges have been netted with an estimated bad debt expense of \$1,892 and \$1,962 at December 31, 2012 and 2011, respectively.

NOTE 12 – INSURANCE AND RELATED ACTIVITIES

The District is exposed to various forms of loss of assets associated with the risks of fire, personal liability, theft, vehicular accidents, errors and omissions, fiduciary responsibility, etc. and is also subject to the risks associated with employee injury. Each of these risks is covered through the purchase of commercial insurance.

NOTE 13 – ECONOMIC DEPENDENCY

The District purchased 100.00% of the water it sold from Frankfort Electric and Water Plant Board for the years ended December 31, 2012 and 2011.

NOTE 14 – OPERATION AND MAINTENANCE CONTRACT

North Shelby Water Company furnishes managerial, meter reading, maintenance, meter installation, accounts receivable processing, and general office services to U.S. 60 Water District. The District paid \$266,731 and \$240,333 for the years ended December 31, 2012 and 2011, respectively. There is a payable due to North Shelby Water Company in the amount of \$10,990 and \$20,419 at December 31, 2012 and 2011, respectively.

NOTE 15 – COMMITMENTS, CONTINGENCIES AND SUBSEQUENT EVENTS

U.S. 60 Water District is considering a conversion of meters to auto-read meters along with construction of a new water tank. Preliminary estimated costs associated with these projects are \$1,800,000. The District is currently evaluating financing options. No formal actions or decisions have been made.

In February, 2013 the District refunded its outstanding 1985 Bonds and 1992 Bonds through the issuance of a \$490,000 loan from the Kentucky Rural Water Finance Corporation Public Properties Refunding Revenue Bonds (Flexible Term Program) Series 2013 B. It is estimated that this transaction will save the District \$166,686 in debt service payments and a Net Present Value Benefit of \$122,451.

To the Commissioners of the
U.S. 60 Water District of Shelby and Franklin Counties
Bagdad, KY 40003

**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***

INDEPENDENT AUDITOR'S REPORT

We have audited, 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, the financial statements of U.S. 60 Water District of Shelby and Franklin Counties as of and for the year ended December 31, 2012, and the related notes to the financial statements, which collectively comprise U.S. 60 Water District of Shelby and Franklin Counties' basic financial statements, and have issued our report thereon dated March 25, 2013.

INTERNAL CONTROL OVER FINANCIAL REPORTING

In planning and performing our audit of the financial statements, we considered U.S. 60 Water District of Shelby and Franklin Counties' 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 U.S. 60 Water District of Shelby and Franklin Counties' internal control. Accordingly, we do not express an opinion on the effectiveness of U.S. 60 Water District of Shelby and Franklin Counties' internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraph 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. However, as described in the accompanying schedule of findings and responses, we identified certain deficiencies in internal control that we consider to be material weaknesses and significant deficiencies.

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 (Items 12-1 and 12-2).

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. We consider the deficiency described in the accompanying schedule of findings and responses to be a significant deficiency (Item 12-3).

COMPLIANCE AND OTHER MATTERS

As part of obtaining reasonable assurance about whether U.S. 60 Water District of Shelby and Franklin Counties' 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*.

U.S. 60 WATER DISTRICT OF SHELBY AND FRANKLIN COUNTIES' RESPONSE TO FINDINGS

U.S. 60 Water District of Shelby and Franklin Counties' response to the findings identified in our audit are described in the accompanying schedule of findings and responses. U.S. 60 Water District of Shelby and Franklin Counties' response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

PURPOSE OF THIS REPORT

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the result 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.

Raisor, Zapp & Woods, PSC

RAISOR, ZAPP, & WOODS P.S.C
Certified Public Accountants
Carrollton, Kentucky

March 25, 2013

**U.S. 60 WATER DISTRICT OF SHELBY AND FRANKLIN COUNTIES
SCHEDULE OF FINDINGS AND RESPONSES
For the Year Ended December 31, 2012**

A. SUMMARY OF AUDIT RESULTS

1. The auditor's report expresses an unqualified opinion on the financial statements of U.S. 60 Water District of Shelby and Franklin Counties.
2. Three deficiencies in internal control related to the audit of the financial statements are reported in the 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*. Items 12-1 and 12-2 were reported as material weaknesses. Item 12-3 was reported as a significant deficiency.
3. No instances of noncompliance material to the financial statements of U.S. 60 Water District of Shelby and Franklin Counties, which would be required to be reported in accordance with *Government Auditing Standards*, were disclosed during the audit.

B. FINDINGS - FINANCIAL STATEMENTS AUDIT

GOVERNMENT AUDITING STANDARDS

DEFICIENCIES IN INTERNAL CONTROL

12-1 SIZE OF ENTITY, CROSS-TRAINING AND CHECKING PROCEDURES

CONDITION:

Due to the size of the entity, cross-training and checking procedures are not in place for certain administrative positions. This limits internal control. This condition was also cited as a material weakness in the schedule of findings and responses for the year ended December 31, 2011 as 11-1.

CRITERIA:

Internal controls should be in place to provide management with reasonable, but not absolute, assurance that assets are safeguarded against loss from unauthorized use or disposition, and allow timely preparation of financial data consistent with management assertions.

CAUSE:

Responsibilities associated with individual positions limit the availability of individuals to rotate duties and implement checking procedures.

EFFECT:

This limitation may affect the ability to timely record, process, summarize and report financial data.

RECOMMENDATION:

Management should strive to provide cross-training for administrative staff and implement checking processes.

RESPONSE:

We concur with the recommendation. Management believes adequate resources have been expended and control procedures implemented, that are commensurate with the staff size and responsibility of financial personnel.

U.S. 60 WATER DISTRICT OF SHELBY AND FRANKLIN COUNTIES
SCHEDULE OF FINDINGS AND RESPONSES (CONTINUED)
For the Year Ended December 31, 2012

B. FINDINGS - FINANCIAL STATEMENTS AUDIT (Continued)

GOVERNMENT AUDITING STANDARDS (Continued)

DEFICIENCIES IN INTERNAL CONTROL (Continued)

12-2 FAILURE TO PREPARE COMPLETE SET OF FINANCIAL STATEMENTS INCLUDING REQUIRED NOTE DISCLOSURES

CONDITION:

District financial statements, including the required disclosures, are prepared as part of the annual audit. This condition was also cited as a material weakness in the schedule of findings and responses for the year ended December 31, 2011 as 11-2.

CRITERIA:

Internal controls should be in place to provide management with reasonable, but not absolute, assurance that financial statements and required notes are prepared in accordance with generally accepted accounting principles.

CAUSE:

The draft accrual basis financial statements and disclosures are prepared during the audit process. The entries are entered into the District's general ledger/financial reports.

EFFECT:

Management engaged the auditor to prepare the draft of the financial statements, including the related notes to the financial statements. Management reviewed, approved, and accepted responsibility for the financial statements prior to their issuance.

RECOMMENDATION:

District management should continue to enhance its knowledge of reporting requirements in providing oversight of this service.

RESPONSE:

The outsourcing of this service is a result of management's cost benefit decision to use others' accounting expertise rather than incur internal resource costs. We concur with the recommendation and will continue to improve our overall accounting knowledge in performing our oversight responsibilities.

12-3 FAILURE TO DOCUMENT APPROVAL FOR CUSTOMER BAD DEBT WRITE OFFS

CONDITION:

Customer accounts were identified as uncollectible and subsequently written off. The write off as "bad debts" was not approved by District Commissioners and evidenced in Commission minutes. This condition was also cited as a significant deficiency in the schedule of findings and responses for the year ended December 31, 2011 as 11-4.

CRITERIA:

Customer accounts identified as uncollectible should be documented in District minutes.

U.S. 60 WATER DISTRICT OF SHELBY AND FRANKLIN COUNTIES
SCHEDULE OF FINDINGS AND RESPONSES (CONTINUED)
For the Year Ended December 31, 2012

B. FINDINGS - FINANCIAL STATEMENTS AUDIT (Continued)

GOVERNMENT AUDITING STANDARDS (Continued)

DEFICIENCIES IN INTERNAL CONTROL (Continued)

12-3 FAILURE TO DOCUMENT APPROVAL FOR CUSTOMER BAD DEBT WRITE OFFS (Continued)

CAUSE:

Customer bad debt write-offs were not approved by the Commission.

EFFECT:

Customer accounts were written off without proper authorization.

RECOMMENDATION:

Accounts identified as uncollectible should be approved for write-off and documented in Commission minutes.

RESPONSE:

We concur with the recommendation.

COMPLIANCE AND OTHER MATTERS

NONE