

**RECEIVED**

JUN 14 2013

PUBLIC SERVICE  
COMMISSION

UNION COUNTY WATER DISTRICT

---

**REPORT ON AUDIT OF FINANCIAL STATEMENTS**

For the years ended December 31, 2012 and 2011

**McELROY, MITCHELL & ASSOCIATES, LLP**

CERTIFIED PUBLIC ACCOUNTANTS

**RECEIVED**

JUN 14 2013

PUBLIC SERVICE  
COMMISSION

**TABLE OF CONTENTS**

	<b>Page</b>
Independent Auditors' Report	1
Basic Financial Statements:	
Statement of Net Position	4
Statement of Revenues, Expenses and Changes in Fund Net Position	6
Statement of Cash Flows	7
Notes to Financial Statements	9
Report on Internal Control Over Financial Reporting and on Compliance And Other Matters Based on an Audit of Financial Statements Performed In Accordance with <i>Government Auditing Standards</i>	18

# M<sub>C</sub>ELROY, MITCHELL & ASSOCIATES, LLP

C E R T I F I E D      P U B L I C      A C C O U N T A N T S

B U S I N E S S      C O N S U L T A N T S

## INDEPENDENT AUDITORS' REPORT

### PARTNERS

S. MARTIN M<sub>C</sub>ELROY, JR., CPA  
ROBERT E. MITCHELL, CPA, CVA

### ASSOCIATES

ERICK SUDDOTH, CPA, CrFA  
LAURA MINOR, CPA  
TODD BOWLEY  
SHERRI BLACKBURN

Board of Commissioners  
Union County Water District  
Morganfield, Kentucky

### Report on the Financial Statements

We have audited the accompanying financial statements of the business-type activities of the Union County Water District as of and for the years ended December 31, 2012 and 2011 and the related notes to the financial statements, which 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 the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

### Auditors' Responsibility

Our responsibility is to express 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 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 opinions.

## **Opinions**

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the business-type activities of the Union County Water District as of December 31, 2012 and 2011 and the respective changes in financial position and cash flows thereof for the years then ended in conformity with accounting principles generally accepted in the United States of America.

## **Other Matters**

### *Required Supplementary Information*

Management has omitted 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 June 7, 2013, on our consideration of Union County Water District's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on 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 Union County Water District's internal control over financial reporting and compliance.

*M. E. Elroy, Mitchell & Associates, LLP*

Morganfield, Kentucky  
June 7, 2013

[This page intentionally left blank]

UNION COUNTY WATER DISTRICT  
Statement of Net Position  
December 31, 2012 and 2011

ASSETS

	<u>2012</u>	<u>2011</u>
Current assets:		
Cash and cash equivalents	\$ 226,329	\$ 187,484
Accounts receivable, consumers	120,933	115,109
Other receivables	-	3,336
Other assets	<u>78,920</u>	<u>78,387</u>
Total current assets	<u>426,182</u>	<u>384,316</u>
Restricted assets:		
Cash and cash equivalents	<u>65,839</u>	<u>48,530</u>
Capital assets:		
Non-depreciable	10,175	10,175
Depreciable	10,804,635	10,748,349
Less: accumulated depreciation	<u>(5,077,386)</u>	<u>(4,833,899)</u>
Total capital assets	<u>5,737,424</u>	<u>5,924,625</u>
Other assets	<u>324</u>	<u>1,656</u>
Total assets	<u>6,229,769</u>	<u>6,359,127</u>

## LIABILITIES

	<u>2012</u>	<u>2011</u>
Current liabilities:		
Current portion of long-term debt	55,000	80,000
Accounts payable	18,062	10,704
Deferred revenue	4,994	-
Other accrued liabilities	61,306	61,870
	<u>139,362</u>	<u>152,574</u>
Current liabilities payable from restricted assets:		
Accrued interest payable	3,433	4,750
Current portion of long-term debt	18,000	17,000
	<u>21,433</u>	<u>21,750</u>
Total current liabilities	<u>160,795</u>	<u>174,324</u>
Non-current liabilities:		
Long-term debt, net of current portion	116,000	189,000
Customer advances in aid of construction	1,081	980
Total non-current liabilities	<u>117,081</u>	<u>189,980</u>
Total liabilities	<u>277,876</u>	<u>364,304</u>

## NET POSITION

Net invested in capital assets	5,566,424	5,655,625
Restricted for debt service	44,406	26,780
Unrestricted	341,063	312,418
Total net position	<u>\$ 5,951,893</u>	<u>\$ 5,994,823</u>

The accompanying notes are an integral part of the financial statements

**UNION COUNTY WATER DISTRICT**  
**Statement of Revenues, Expenses, and Changes in Net Position**  
**For the years ended December 31, 2012 and 2011**

	<u>2012</u>	<u>2011</u>
<b>Operating revenues:</b>		
Water sales	\$ 1,334,507	\$ 1,271,090
Other revenues	79,863	87,167
	<u>1,414,370</u>	<u>1,358,257</u>
<b>Operating expenses:</b>		
Water purchased	508,330	491,165
Fuel and power purchased for pumping	54,560	58,501
Water transmission and distribution	103,403	121,310
Customer account expense	32,082	32,269
General and administrative	514,279	488,605
Depreciation and amortization	244,819	242,203
	<u>1,457,473</u>	<u>1,434,053</u>
Total operating expenses	<u>1,457,473</u>	<u>1,434,053</u>
Operating loss	<u>(43,103)</u>	<u>(75,796)</u>
<b>Non-operating revenues (expenses):</b>		
Interest income	41	405
Interest expense	(14,164)	(22,108)
	<u>(14,123)</u>	<u>(21,703)</u>
Total non-operating expenses	<u>(14,123)</u>	<u>(21,703)</u>
Loss before contributions	(57,226)	(97,499)
Capital contributions	14,296	67,949
	<u>(42,930)</u>	<u>(29,550)</u>
Change in net position	<u>(42,930)</u>	<u>(29,550)</u>
Total net position- beginning of year	<u>5,994,823</u>	<u>6,024,373</u>
Total net position- end of year	<u>\$ 5,951,893</u>	<u>\$ 5,994,823</u>

The accompanying notes are an integral part of the financial statements

**UNION COUNTY WATER DISTRICT**  
**Statement of Cash Flows**  
**For the years ended December 31, 2012 and 2011**

	<u>2012</u>	<u>2011</u>
<b>Cash flows from operating activities:</b>		
Receipts from customers	\$ 1,408,546	\$ 1,362,083
Payments to suppliers	(787,691)	(786,996)
Payments to employees	(413,693)	(401,267)
	<u>207,162</u>	<u>173,820</u>
<b>Cash flows from non-capital financing activities:</b>	<u>-</u>	<u>-</u>
<b>Cash flows from capital and related financing activities:</b>		
Acquisition and construction of capital assets	(56,286)	(102,050)
Principal payments on bond indebtedness	(97,000)	(277,500)
Principal payments on capital lease	-	(34,000)
Interest payments on bond indebtedness	(15,496)	(30,564)
Interest payments on capital lease	-	(118)
Proceeds from contributed capital	17,632	89,342
Proceeds (payments) on customer advances	101	(217)
	<u>(151,049)</u>	<u>(355,107)</u>
<b>Cash flows from investing activities:</b>		
Purchase of investment securities	-	(100,400)
Proceeds from sale and maturity of investment securities	-	275,400
Investment income	41	405
	<u>41</u>	<u>175,405</u>
Net increase(decrease) in cash and cash equivalents	56,154	(5,882)
Cash and cash equivalents, beginning of year	<u>236,014</u>	<u>241,896</u>
Cash and cash equivalents, end of year	<u>\$ 292,168</u>	<u>\$ 236,014</u>

The accompanying notes are an integral part of the financial statements

**UNION COUNTY WATER DISTRICT**  
**Statement of Cash Flows, Continued**  
**For the years ended December 31, 2012 and 2011**

	<u>2012</u>	<u>2011</u>
<b>Reconciliation of operating income to net cash provided by operating activities:</b>		
Operating loss	\$ (43,103)	\$ (75,796)
Items to reconcile net operating income to net cash provided by operations:		
Depreciation and amortization	244,819	242,203
Changes in operation assets and liabilities:		
Accounts receivable- consumers	(5,824)	3,826
Other assets	799	2,886
Accounts payable	7,358	2,538
Accrued interest payable	(1,317)	(8,596)
Deferred revenue	4,994	-
Other accrued liabilities	(564)	6,759
Net cash provided by operating activities	<u>207,162</u>	<u>173,820</u>
 <b>Reconciliation of cash and cash equivalents:</b>		
Unrestricted cash and cash equivalents	\$ 226,329	\$ 187,484
Restricted cash and cash equivalents	<u>65,839</u>	<u>48,530</u>
Total cash and cash equivalents	<u>\$ 292,168</u>	<u>\$ 236,014</u>

The accompanying notes are an integral part of the financial statements

UNION COUNTY WATER DISTRICT  
NOTES TO FINANCIAL STATEMENTS  
December 31, 2012 and 2011

1. Summary of Significant Accounting Policies

The Union County Water District's ("District") financial statements are prepared in accordance to generally accepted accounting principles (GAAP) applicable to governmental units. The Governmental Accounting Standards Board (GASB) is responsible for establishing GAAP for state and local governments through its pronouncements. The following summary of the more significant accounting policies is presented to assist the reader in interpreting the financial statements and other data in this report. These policies should be viewed as an integral part of the accompanying financial statements.

a. Reporting Entity

In evaluating how to define the entity for financial reporting purposes, management considered whether the District is a component unit of another primary government and all potential component units of the District. The District is a special-purpose district organized to construct, operate, and maintain water service facilities and supply water to customers in Union County, Kentucky. The District is governed by three appointed Commissioners who are nominated and approved by the Union County Fiscal Court. The District purchases its water supply from the City of Morganfield, Kentucky. All of the water purchased by the District has been filtered and treated. The District operates and maintains the distribution system that supplies its end users. The District's basic financial statements include the financial position and the results of operations of the District. A review of other units of local government, using the criteria set forth in generally accepted accounting principles, indicates there are no additional entities or funds for which the District has reporting responsibilities. Management has determined the District should not be considered a part of any unit of local government for reporting purposes for the following reasons:

1. The District has separate legal standing from all other units of government.
2. A primary government appoints the voting majority of the District's Board of Commissioners. However, the primary government is not able to impose its will on the District and there is no potential for the District to provide benefits to or burdens on the primary government.
3. The District is fiscally independent of all other units of local government. The District's Board of Commissioners has the sole authority to determine financial programs, establish rates (subject to Public Service Commission approval) and issue bonded debt.
4. The financial statements of other units of local government would not be misleading or incomplete without the inclusion of the District's financial statements.

b. Basis of Accounting and Presentation

The District is a single-enterprise proprietary fund and uses the accrual basis of accounting. Proprietary funds are used to account for activities that are operated and financed in a manner similar to private business enterprise and that a periodic determination of revenues earned, expenses incurred and/or change in position is appropriate for capital maintenance, public policy, management control, accountability or other purposes. Under the accrual method, revenues are recognized when earned, and expenses are recognized as soon as they result in liabilities for the benefits provided.

1. **Summary of Significant Accounting Policies, Continued**

b. **Basis of Accounting and Presentation, Continued**

Proprietary funds distinguish operating revenues and expenses from non-operating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with the proprietary funds principle ongoing operations. The principle operating revenues of the District are charges to customers for water usage. Operating expenses include the cost of providing water service, administrative expenses and depreciation on capital assets. Other revenues and expenses are reported as non-operating in the financial statements.

Charges for services include revenues based on exchange or exchange-like transactions, namely water and sewer use. Program-specific grants and contributions (operating and capital), include revenues arising from mandatory and voluntary nonexchange transactions with other governments, organizations, or individuals that are restricted for use in a particular program, are accrued when all related eligibility requirements have been met.

c. **Measurement Focus**

The District's enterprise fund is accounted for on an "economic resources" measurement focus. Accordingly, determination of operating income, changes in net position, financial position and cash flows are the primary focus of fund measurement.

d. **Cash and Cash Equivalents**

The District considers all highly liquid investments with an original maturity of ninety days or less to be cash equivalents.

e. **Investments**

KRS 66.480 permits the District to invest in U.S. Treasury obligations, U.S. Agency obligations, certain Federal instruments, repurchase agreements, commercial bank certificates of deposit, savings and loan deposits, and the Commonwealth of Kentucky investment pool. Investments are recorded at fair market value. Certificates of deposit are reported at cost since the redemption terms do not consider market rates. These investments are required to be fully collateralized in accordance with provisions of KRS 66.480.

f. **Accounts Receivable**

The District's receivable balances are expected to be fully collectible; therefore an allowance for uncollectible accounts has not been recorded.

g. **Restricted Assets**

Restricted assets are cash and cash equivalents whose use is limited by legal requirements. Restricted cash and cash equivalents represent amounts required by debt covenants to be segregated for future debt payments and accrued interest on long-term debt obligations.

UNION COUNTY WATER DISTRICT  
 NOTES TO FINANCIAL STATEMENTS  
 December 31, 2012 and 2011

1. Summary of Significant Accounting Policies, Continued

h. Capital Assets

Capital assets represent the cumulative amount of capital assets owned by the District. Capital assets purchased or acquired are reported at historical cost. Contributed assets are reported at fair value as of the date received. Additions, improvements and other capital outlays that significantly extend the useful life of an asset are capitalized. Other costs incurred for repairs and maintenance are expensed as incurred. All capital assets except land and construction in progress are depreciated. Depreciation is provided for by using the straight-line method over the following estimated useful lives of the assets:

Structures, lines, mains and accessories, and system improvements	50 years
Equipment, including hydrants, pumps and meters	5-30 years
Transportation equipment	5 years

i. Debt Issue Cost

Issue costs on bonds payable are being amortized using the outstanding bonds method.

j. Deferred Revenues

The District reports deferred revenue on its statement of net position. Deferred revenues arise when potential revenue does not meet both the “measurable” and “available” criteria for recognition in the current period. Deferred revenues also arise when resources are received by the District before it has legal claim to them, as when grant monies are received prior to the incurrence of qualifying expenditures. In subsequent periods, when both revenue recognition criteria are met, or when the District has a legal claim to the resources, the liability for deferred revenue is removed from the statement of net position and revenue is recognized.

k. Compensated Absences

Compensated absences are absences for which employees will be paid, such as vacation and sick leave. A liability for compensated absences that are attributable to services already rendered and that are not contingent on a specific event that is outside the control of the District and its employees is accrued as employees earn the rights to the benefits. The District’s policy is to accrue up to 30 days of unused vacation, which is payable upon termination of employment. Employees can accrue up to 60 days of sick leave, which upon termination of employment has no monetary value. Compensated absence activity for the year ended December 31, 2012 was as follows:

	<u>Balance</u> <u>January 1, 2012</u>	<u>Additions</u>	<u>Deductions</u>	<u>Balance</u> <u>Dec. 31, 2012</u>
Compensated absences	\$ 4,391	12,260	(10,163)	\$ 6,488

1. **Summary of Significant Accounting Policies, Continued**

**l. Net Position**

Net position presents the difference between assets and liabilities in the statement of net position. Proprietary fund net position is divided into three components:

- Net investment in capital assets- consist of the historical cost of capital assets less accumulated depreciation and less any debt that remains outstanding that was used to finance those assets plus deferred outflows of resources less deferred inflows of resources related to those assets.
- Restricted- consist of net position that is restricted by the District's creditors (for example, through debt covenants), by state enabling legislation (through restrictions on shared revenues), by grantors (both federal and state), and by other contributors less related liabilities and deferred inflows of resources.
- Unrestricted- all other net position is reported in this category.

**m. Use of Restricted Resources**

When an expense is incurred for purposes for which both restricted and unrestricted resources (net position) are available, the District's policy is to first apply the expense toward restricted resources and then toward unrestricted resources.

**n. New Accounting Pronouncements**

The District implemented GASB 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements* which incorporates into the GASB's authoritative literature certain accounting and financial reporting guidance that is included in the following pronouncements issued on or before November 30, 1989 which does not conflict with or contradict GASB pronouncements: Financial Accounting Standards Board (FASB) Statements and Interpretations, Accounting Principles Board Opinions and Accounting Research Bulletins of the American Institute of Certified Public Accountants' (AICPA) Committee on Accounting Procedure. The adoption of GASB 62 did not have any impact on the District's financial statements.

The District implemented GASB 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*, which provides financial reporting guidance for deferred outflows and inflows of resources and net position in a statement of financial position and related disclosures. The Statement of Net Assets is renamed the Statement of Net Position and includes four components: assets, deferred outflows of resources, liabilities, and deferred inflows of resources. The District has determined they have no deferred outflows or inflows as defined by this standard. The implementation of this pronouncement did not cause a restatement of any beginning balances.

2. **Deposits**

At December 31, 2012, the Union County Water District maintained deposits of \$298,010 at two financial institutions. All of these bank balances were covered by federal depository insurance.

UNION COUNTY WATER DISTRICT  
NOTES TO FINANCIAL STATEMENTS  
December 31, 2012 and 2011

3. **Restricted Assets**

The Union County Water District had certain assets and corresponding net position reserved for debt service which were restricted due to its outstanding debt. These consisted of a cash reserve and sinking fund for the United States Department of Agriculture note.

<b><u>Restricted Assets:</u></b>	<b><u>2012</u></b>	<b><u>2011</u></b>
Sinking Fund	\$ 39,040	\$ 28,455
Reserve Fund	26,799	20,075
Total restricted assets	<u>65,839</u>	<u>48,530</u>
Less: Accrued current liabilities payable from restricted assets:		
Principal	18,000	17,000
Interest	3,433	4,750
	<u>21,433</u>	<u>21,750</u>
Net assets restricted for debt service	<u>\$ 44,406</u>	<u>\$ 26,780</u>

4. **Capital Assets**

Capital asset activity consisted of the following for the year ended December 31, 2012:

	<b><u>December 31,</u></b> <b><u>2011</u></b>	<b><u>Additions</u></b>	<b><u>Disposals</u></b>	<b><u>December 31,</u></b> <b><u>2012</u></b>
Capital assets not depreciated:				
Land and land rights	\$ 10,175	\$ -	\$ -	\$ 10,175
Capital assets depreciated:				
Transport and distribution mains	4,115,405	9,455	-	4,124,860
Other transport and distribution plant	25,354	-	-	25,354
Distribution reservoirs and standpipe	4,602,808	20,909	-	4,623,717
Meters	1,044,705	25,672	-	1,070,377
Hydrants	34,523	-	-	34,523
Electric pumping equipment	688,553	-	-	688,553
Structures and improvements	20,202	-	-	20,202
Equipment	119,250	-	-	119,250
Transportation equipment	64,795	-	-	64,795
Office equipment and software	21,854	250	-	22,104
Other tangible property	10,900	-	-	10,900
	<u>10,748,349</u>	<u>56,286</u>	<u>-</u>	<u>10,804,635</u>
Total assets at historical cost	10,758,524	56,286	-	10,814,810
Less accumulated depreciation	<u>(4,833,899)</u>	<u>(243,487)</u>	<u>-</u>	<u>(5,077,386)</u>
Total capital assets, net	<u>\$ 5,924,625</u>	<u>\$ (187,201)</u>	<u>\$ -</u>	<u>\$ 5,737,424</u>

Continued

UNION COUNTY WATER DISTRICT  
NOTES TO FINANCIAL STATEMENTS  
December 31, 2012 and 2011

4. Capital Assets, Continued

Depreciation expense amounted to \$243,487 and \$240,871 for the years ended December 31, 2012 and 2011, respectively. Amortization expense amounted to \$1,332 for each of the years ended December 31, 2012 and 2011.

5. Long-Term Debt

Long-term debt of the District consisted of the following as of December 31, 2012 and 2011:

	December 31, 2012			Balance Dec. 31, 2012	Due Within One Year
	Balance Dec. 31, 2011	Additions	Deductions		
USDA Loan	\$ 151,000	\$ -	\$ 17,000	\$ 134,000	\$ 18,000
KIA Assistance Agreement	135,000	-	80,000	55,000	55,000
Total long-term debt	<u>286,000</u>	<u>-</u>	<u>97,000</u>	<u>189,000</u>	<u>\$ 73,000</u>

Presented on the balance sheet under the following captions:

Current portion long-term debt	\$ 55,000
Current portion long-term debt payable from restricted assets	18,000
Long-term debt, net of current portion	<u>116,000</u>
	<u>\$ 189,000</u>

Principal and interest requirements to retire the District's long-term obligations at December 31, 2012 were as follows:

	Principal	Interest	Total
2013	\$ 73,000	\$ 9,404	\$ 82,404
2014	18,000	5,484	23,484
2015	20,000	4,510	24,510
2016	20,000	3,485	23,485
2017	22,000	2,409	24,409
2018-2019	<u>36,000</u>	<u>1,589</u>	<u>37,589</u>
	<u>\$ 189,000</u>	<u>\$ 26,881</u>	<u>\$ 215,881</u>

Other information on the District's long-term indebtedness is summarized below:

	Interest Rate	Final Maturity	Principal Balance	Security
USDA Loan	5.125%	1/1/2019	\$ 134,000	Utility Revenues
KIA Assistance Agreement	2.5%-5.25%	6/1/2013	\$ 55,000	Utility Revenues

UNION COUNTY WATER DISTRICT  
 NOTES TO FINANCIAL STATEMENTS  
 December 31, 2012 and 2011

5. Long-Term Debt, Continued

December 31, 2011					
	Balance Dec. 31, 2010	Additions	Deductions	Balance Dec. 31, 2011	Due Within One Year
USDA Loan	\$ 381,000	\$ -	\$ 230,000	\$ 151,000	\$ 17,000
KIA Assistance Agreement	182,500	-	47,500	135,000	80,000
Total long-term debt	<u>563,500</u>	<u>-</u>	<u>277,500</u>	<u>286,000</u>	<u>\$ 97,000</u>

6. Line of Credit

During the year ended December 31, 2012, the District had a line of credit in the amount of \$300,000 with United Community Bank. The line of credit bears interest at the prime rate minus 0.43% and is unsecured. The outstanding balance was zero at December 31, 2012 and 2011, respectively.

7. Operating Lease

The Union County Water District entered into a lease agreement with the Union County Fiscal Court to lease office space. The original lease was for a term of twenty-eight months expiring December 31, 2011 with an option for three annual renewals. The District is in the final year of annual renewal. The monthly rent expense is \$500.

8. County Employees Retirement System (CERS)

The District has elected to participate in the County Employee Retirement System (CERS), 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.

Covered employees are required to contribute 5 percent of their salary to the plan. Covered employees who began participation on or after September 1, 2008 are required to contribute 6 percent of their salary to the plan. The District's contribution rate for employees was 19.55 percent.

The District's contributions for the fiscal years ending December 31 were as follows:

Year	Amount
2012	\$ 42,360
2011	36,761
2010	32,642

Benefits fully vest on reaching five years of service for employees. Aspects of benefits for covered employees include retirement after 27 years of service or age 65. Employees who began participation on or after September 1, 2008 must meet the rule of 87 (members age plus years of service credit must equal 87, and the member must be a minimum of 57 years of age) or the member is age 65, with a minimum of 60 months of service credit.

**UNION COUNTY WATER DISTRICT  
 NOTES TO FINANCIAL STATEMENTS  
 December 31, 2012 and 2011**

**8. County Employees Retirement System (CERS), Continued**

CERS also provides post-retirement health care coverage as follows:

<u>Years of Service</u>	<u>% Paid by Insurance Fund</u>	<u>% Paid by Member through Payroll Deduction</u>
20 or more	100%	0%
15 - 19	75%	25%
10 - 14	50%	50%
4 - 9	25%	75%
Less than 4	0%	100%

As a result of House Bill 290 (2004 General Assembly), medical insurance benefits are calculated differently for members who began participation on or after July 1, 2003. Once members reach a minimum vesting period of ten years, nonhazardous employees whose participation began on or after July 1, 2003, earn ten dollars per month for insurance benefits at retirement for every year of earned service without regard to maximum dollar amount.

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 Systems, 1260 Louisville Road, Frankfort, KY 40601-6124, or by telephone at (502)564-4646.

**9. Deferred Compensation**

The District allows all eligible employees to participate in deferred compensation plans administered by the Kentucky Public Employees' Deferred Compensation Authority. The Kentucky Public Employees' Deferred Compensation Authority is authorized under KRS 18A.230 to 18A.275 to provide administration of tax sheltered supplemental retirement plans for all state, public school and university employees and employees of local political subdivisions that have elected to participate. These deferred compensation plans permit all full-time employees to defer a portion of their salary until future years. The deferred compensation is not available to employees until termination, retirement, death, or unforeseeable emergency. Participation by eligible employees in the deferred compensation plans is voluntary.

Historical trend information showing the Kentucky Public Employees' Deferred Compensation Authority's progress in accumulating sufficient assets to pay benefits when due is presented in the Kentucky Public Employees' Deferred Compensation Authority's annual financial report. This report may be obtained by writing the Kentucky Public Employees' Deferred Compensation Authority at 101 Sea Hero Road, Suite 110, Frankfort, KY 40601-8862, or by telephone at (502) 573-7925.

**10. Concentrations of Sales**

For the year ended December 31, 2012, three industrial customers in the coal mining industry accounted for \$542,304 in sales and surcharges for approximately 38% of the District's total operating revenues. For the year ended December 31, 2011, sales attributable to these companies were \$419,570 or approximately 31% of total operating revenues.

**UNION COUNTY WATER DISTRICT  
NOTES TO FINANCIAL STATEMENTS  
December 31, 2012 and 2011**

**11. Commitments**

The District entered into an agreement dated December 19, 1986 with the City of Morganfield, Kentucky whereby the City agrees to sell and deliver to the District and the District agrees to purchase and receive from the City all of the water required by the District up to a maximum of 1,000,000 gallons per day. The District can purchase water from other suppliers only in the event of an emergency. The agreement outlines a specific method of determining the City's cost of water produced during the previous fiscal year which is the rate charged to the District for the next year. The agreement covers a period of 42 years which expires December 19, 2028.

The City of Morganfield Council approved a motion on April 22, 2010 to amend the contract with the District to increase the maximum amount of water which the City must furnish to the District during any twenty-four (24) hour period by 1,000,000 gallons to a maximum of 2,000,000 gallons per day. As of the date of this report, no contract amendment had been signed by the two parties.

**12. Risk Management**

The District is exposed to various risks of loss related to torts, theft of, damage to, and destruction of assets; errors and omissions; injuries to employees, and natural disasters. The District carries commercial insurance for these types of risk of loss, including workers compensation. Settled claims resulting from these risks have not exceeded commercial insurance coverage in any of the past three fiscal years.

**13. Subsequent Events**

In preparing these financial statements, the District has evaluated events and transactions for potential recognition or disclosure through June 7, 2013, the date the financial statements were available to be issued.

# McELROY, MITCHELL & ASSOCIATES, LLP

CERTIFIED PUBLIC ACCOUNTANTS

BUSINESS CONSULTANTS

## Independent Auditors' 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*

### PARTNERS

S. MARTIN McELROY, JR., CPA  
ROBERT E. MITCHELL, CPA, CVA

### ASSOCIATES

ERICK SUDDOTH, CPA, CRFA  
LAURA MINOR, CPA  
TODD BOWLEY  
SHERRI BLACKBURN

To the Commissioners  
Union County Water District  
Morganfield, Kentucky

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to the financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the business-type activities of the Union County Water District as of and for the year ended December 31, 2012 and the related notes to the financial statements, which collectively comprise the District's basic financial statements and have issued our report thereon dated June 7, 2013.

### **Internal Control over Financial Reporting**

In planning and performing our audit of the financial statements, we considered Union County Water District's internal control over financial reporting (internal control) to determine the auditing 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 the District's internal control. Accordingly, we do not express an opinion on the effectiveness of the District's internal control over financial reporting.

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 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 over financial reporting 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 schedule of findings and responses that we consider to be significant deficiencies. [A-1 and A-2]

### **Compliance and Other Matters**

As part of obtaining reasonable assurance about whether the Union County Water District's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with such 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*.

### **Union County Water District's Response to Findings**

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

### **Purpose of the Report**

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the 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.

*McElroy, Mitchell & Associates, LLP*

Morganfield, Kentucky  
June 7, 2013

## **Schedule of Findings & Responses**

### **A-1 Control Risk Related To Lack Of Segregation Of Duties:**

Due to a limited number of personnel employed at the District, incompatible work functions are often performed by the same individual and a high degree of trust is necessitated.

**Criteria:** Each key step of an accounting system should be segregated among employees. 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.

**Effect:** The staff size of the District limits the ability to rotate duties and implement some checking procedures. This limitation may affect the ability to record, process, summarize and report financial data.

**Recommendation:** We recommend that management always be mindful of key functions assigned to employees and provide oversight in all steps of the accounting system.

**Response:** Management concurs with the recommendation and has taken steps to separate functions and provide oversight where needed.

### **A-2 Control Risk Due to Lack of Qualifications to Fulfill Assigned Functions**

The auditor, from the District's books of original entry, prepares the financial statements and notes for the Union County Water District.

**Criteria:** Internal controls should be put in place for the District to review and approve generally accepted accounting principles (GAAP) financial statements and notes. The District is to accept full responsibility for the accuracy of the GAAP financial statements and notes.

**Effect:** Based upon the entity's present financial statements, the client's auditor is currently preparing the audit financial statements and disclosures.

**Recommendation:** Procedures should be implemented to allow the District to prepare their own GAAP financial statements and notes.

**Response:** Management is aware of the situation regarding the preparation of GAAP financial statements and is continuing to determine the best way to handle the situation.