

**BUFFALO TRAIL
WATER ASSOCIATION, INC.
Sardis, Kentucky**

**FINANCIAL STATEMENTS
December 31, 2013 and 2012**

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INDEPENDENT AUDITORS' REPORT

To the Board of Directors
Buffalo Trail Water Association, Inc.
Sardis, Kentucky

Report on the Financial Statements

We have audited the accompanying financial statements of the Buffalo Trail Water Association, Inc. (the Association) as of and for the years ended December 31, 2013 and 2012, and the related notes to the financial statements, which collectively comprise the Association'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 an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in **Government Auditing Standards**, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free 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 auditors' 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.

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Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the Buffalo Trail Water Association, Inc., as of December 31, 2013 and 2012, 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

Required Supplementary Information

Management has omitted the Management 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 26, 2014, on our consideration of the Association's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with **Government Auditing Standards** in considering the Association's internal control over financial reporting and compliance.

Ray, Foley, Hensley & Company

Ray, Foley, Hensley & Company, PLLC
March 26, 2014

BUFFALO TRAIL WATER ASSOCIATION, INC.
BALANCE SHEETS
DECEMBER 31,

ASSETS	2013	2012
Current assets		
Cash and cash equivalents	\$ 238,978	\$ 203,227
Certificates of deposit	845,759	739,691
Accounts receivable, net	54,314	47,244
Accrued interest receivable	628	628
Inventory	<u>16,106</u>	<u>15,624</u>
Total current assets	<u>1,155,785</u>	<u>1,006,414</u>
Restricted assets		
Cash and cash equivalents	-	115,561
Investments	36,024	36,024
Note receivable - Mt. Olivet	<u>37,710</u>	<u>44,514</u>
Total restricted assets	<u>73,734</u>	<u>196,099</u>
Capital assets		
Property, plant and equipment	7,536,037	7,482,902
Less accumulated depreciation	<u>(2,737,296)</u>	<u>(2,570,040)</u>
Total plant, property and equipment	<u>4,798,741</u>	<u>4,912,862</u>
Other assets		
Unamortized bond costs	<u>1,903</u>	<u>3,191</u>
TOTAL ASSETS	<u>\$ 6,030,163</u>	<u>\$ 6,118,566</u>
LIABILITIES AND EQUITY		
Current liabilities		
Accounts payable	\$ 25,045	\$ 18,721
Taxes payable	3,300	2,971
Customer deposits	19,350	18,780
Accrued interest payable	2,388	2,492
Current portion of long-term debt	<u>29,114</u>	<u>44,693</u>
Total current liabilities	79,197	87,657
Long-term debt		
Notes payable	<u>650,991</u>	<u>681,724</u>
Total liabilities	<u>730,188</u>	<u>769,381</u>
Equity		
Contributed capital		
Customer contributions	3,118,810	3,108,010
Federal and state grants in aid of construction	2,317,557	2,317,557
Retained earnings (deficit)	<u>(136,392)</u>	<u>(76,382)</u>
Total equity	<u>5,299,975</u>	<u>5,349,185</u>
TOTAL LIABILITIES AND EQUITY	<u>\$ 6,030,163</u>	<u>\$ 6,118,566</u>

The accompanying notes are an integral
part of the financial statements

BUFFALO TRAIL WATER ASSOCIATION, INC.
STATEMENTS OF REVENUES, EXPENSES AND CHANGES
IN RETAINED EARNINGS
for the years ended December 31,

	2013	2012
OPERATING INCOME		
Water sales	\$ 609,798	\$ 607,378
Other revenue	<u>6,399</u>	<u>9,691</u>
Total operating income	<u>616,197</u>	<u>617,069</u>
OPERATING EXPENSES		
Purchased water	192,024	186,052
Contractual services	160,003	146,850
Salaries and wages	65,789	78,764
Regulatory commission expenses	2,440	1,167
Materials and supplies	9,862	12,414
Utilities and telephone	7,419	6,107
Insurance	9,145	8,022
Bad debt expense	730	737
Miscellaneous	<u>7,091</u>	<u>2,833</u>
Total operating expense	<u>454,503</u>	<u>442,946</u>
Operating income before depreciation	161,694	174,123
Depreciation expense	<u>(167,256)</u>	<u>(168,330)</u>
OPERATING INCOME (LOSS)	(5,562)	5,793
Non-operating income (expenses)		
Interest income	8,712	11,782
Interest expense	<u>(63,160)</u>	<u>(39,075)</u>
NET (LOSS)	(60,010)	(21,500)
Retained earnings (deficit), beginning	<u>(76,382)</u>	<u>(54,882)</u>
RETAINED EARNINGS (DEFICIT), ENDING	<u>\$ (136,392)</u>	<u>\$ (76,382)</u>

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

BUFFALO TRAIL WATER ASSOCIATION, INC.
STATEMENTS OF CASH FLOWS
for the years ended December 31,

	2013	2012
CASH FLOWS FROM OPERATING ACTIVITIES		
Receipts from customers	\$ 609,697	\$ 620,037
Payments to suppliers	(382,872)	(367,328)
Payments for employee services and benefits	<u>(65,460)</u>	<u>(78,798)</u>
Net cash provided by operating activities	<u>161,365</u>	<u>173,911</u>
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Customer contributions	10,800	150,900
Purchases of capital assets	(53,135)	(95,425)
Interest paid	(61,976)	(38,081)
Principal paid	(46,312)	(67,927)
Receipts from note receivable	<u>6,804</u>	<u>5,922</u>
Net cash (used in) financing activities	<u>(143,819)</u>	<u>(44,611)</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchase of certificates of deposit	(106,068)	(106,972)
Interest income	<u>8,712</u>	<u>12,304</u>
Net cash (used in) investing activities	<u>(97,356)</u>	<u>(94,668)</u>
NET INCREASE (DECREASE) IN CASH	(79,810)	34,632
Cash and cash equivalents, beginning of year	<u>318,788</u>	<u>284,156</u>
CASH AND CASH EQUIVALENTS, END OF YEAR	<u>\$ 238,978</u>	<u>\$ 318,788</u>
Reconciliation of operating income (loss) to net cash provided by (used in) operating activities:		
Operating income (loss)	\$ (5,562)	\$ 5,793
Adjustments to reconcile operating income to net cash provided (used) by operating activities:		
Depreciation expense	167,256	168,330
Change in assets and liabilities:		
(Increase) in accounts receivable	(7,070)	(812)
(Increase) in inventory	(482)	(1,718)
Increase (decrease) in accounts payable	6,324	(1,428)
Increase (decrease) in taxes payable	329	(34)
Increase in customer deposits	<u>570</u>	<u>3,780</u>
Net cash provided by operating activities	<u>\$ 161,365</u>	<u>\$ 173,911</u>

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

BUFFALO TRAIL WATER ASSOCIATION, INC.
NOTES TO FINANCIAL STATEMENTS
December 31, 2013 and 2012

1. ORGANIZATION AND ACCOUNTING POLICIES

The Buffalo Trail Water Association, Inc. (the Association) distributes and sells water to approximately 1,500 members. The Association primarily serves Bracken, Harrison, Mason, Nicholas, Pendleton, and Robertson Counties. Its suppliers of water are Maysville Utilities and the Western Fleming Water District.

Reporting Entity

The Buffalo Trail Water Association, Inc. was created and organized as a non-profit association and is exempt from income tax under Section 501(c)12 of the Internal Revenue Code.

Basis of Accounting

The Association maintains its accounting records on the cash basis during the year. Adjustments are made to convert to the accrual basis from memorandum records at year end.

The Association records revenue as billed to its customers based upon monthly meter reading cycles. At the end of each year, water service which has been rendered from the latest date of each meter reading to December 31, is unbilled.

The statements of revenues, expenses and changes in retained earnings reports all revenues and expenses as operating, except interest income, interest expense, and amortization.

Cash and Cash Equivalents

For purposes of the statements of cash flows, the Association defines cash and cash equivalents to include cash on hand, cash in bank, and certificates of deposit with original maturities of 90 days or less.

Accounts Receivable

The reserve for accounts receivable represents accounts past due in excess of thirty days that are thought to be uncollectible. The reserve for accounts receivable at December 31, 2013 and 2012 totaled \$14,294 and \$9,489, respectively.

Inventory

The Association's inventory is maintained at lower of cost (first-in, first-out method) or market.

Property and Equipment

Fixed assets are stated at cost. Interest costs incurred during construction are capitalized as a cost of the project. Depreciation has been provided using the straight-line method with the economic lives determined using the following guidelines:

Asset Class	Life
Vehicles and Equipment	5-10
Meters and Pipes	25
Buildings	40
Water and Sewer Systems	50

Restricted Funds

The Board of Directors makes a determination whether to first apply restricted or unrestricted resources when an expense is incurred for purposes for which both restricted and unrestricted net assets are available.

BUFFALO TRAIL WATER ASSOCIATION, INC.
NOTES TO FINANCIAL STATEMENTS
December 31, 2013 and 2012

1. ORGANIZATION AND ACCOUNTING POLICIES (CONTINUED)

Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the period. Actual results could differ from those estimates.

Management's Review of Subsequent Events

The Association has evaluated and considered the need to recognize or disclose subsequent events through March 26, 2013; which represents the date that these financial statements were available for issuance. Subsequent events past this date, as they pertain to the fiscal year ended December 31, 2013, have not been evaluated by the Association.

2. CASH AND CASH EQUIVALENTS

The Association's deposits and investments at December 31, 2013 and 2012 were entirely covered by either Federal Depository Insurance or by collateral held by the custodial banks in the Association's name. These deposits totaled \$1,228,160 and \$952,859, respectively. There were no uninsured deposits at December 31, 2013 and 2012.

Statements of Cash Flows

The statements of cash flows include the following as cash and cash equivalents:

	2013	2012
Cash	\$ 238,978	\$ 203,227
Cash - restricted	<u> -</u>	<u>115,561</u>
Total	<u>\$ 238,978</u>	<u>\$ 318,788</u>

3. CAPITAL ASSETS

The following is a summary of capital asset activity during the year:

	Balance 12/31/2012	Additions	Disposals	Balance 12/31/2013
Capital assets not depreciated:				
Land and land rights	\$ 9,778	\$ -	\$ -	\$ 9,778
Construction in process	<u> -</u>	<u> -</u>	<u> -</u>	<u> -</u>
Total not depreciated	<u>9,778</u>	<u> -</u>	<u> -</u>	<u>9,778</u>
Capital assets that are depreciated:				
Plant and equipment	7,473,124	53,135	-	7,526,259
Less: accumulated depreciation	<u>(2,570,040)</u>	<u>(167,256)</u>	<u> -</u>	<u>(2,737,296)</u>
Total depreciated	<u>4,903,084</u>	<u>(114,121)</u>	<u> -</u>	<u>4,788,963</u>
Capital assets, net	<u>\$ 4,912,862</u>	<u>\$ (114,121)</u>	<u>\$ -</u>	<u>\$ 4,798,741</u>

BUFFALO TRAIL WATER ASSOCIATION, INC.
NOTES TO FINANCIAL STATEMENTS
December 31, 2013 and 2012

4. NOTE RECEIVABLE

The Association entered into an agreement with the City of Mt. Olivet to help pay a debt incurred in 1980 to connect to the West Fleming Water District. The City of Mt. Olivet agreed to pay \$648 per month for a total of \$7,772 per year. This represents 35% of the annual payment of \$22,008 due on the Farmers Home Loan. The receivable represents 40% of the outstanding debt at year end. The debt at December 31, 2013 totaled \$94,274, the receivable at December 31, 2013 totaled \$37,710. The debt at year end December 31, 2012 totaled \$111,110, the receivable December 31, 2012 totaled \$44,514.

5. LONG-TERM DEBT

The following is a summary of the notes outstanding for the Association for the years ended December 31:

	Outstanding 2013	Outstanding 2012
Notes-Farmers Home Administration		
Loan - \$364,000, dated 5/12/80, payable in annual installments of \$21,588 through 2020, bearing interest at a rate of 5%	\$ 94,274	\$ 111,110
Loan - \$347,000, date 8/6/99, payable in annual installments of \$20,400 through 2040, bearing interest at a rate of 4.75%	274,489	281,665
Loan - \$347,000, dated 5/14/3, payable in annual installments of \$19,394 through 2040, bearing interest at a rate of 4.5%	311,342	316,642
Bonds- Robertson County - \$540,000 dated 12/01/93, payable in variable annual installments through 2013, bearing interest at rates of 4% to 6.4%	-	17,000
Total debt	680,105	726,417
Less: current portion	<u>(29,114)</u>	<u>(44,693)</u>
Long-term portion	<u>\$ 650,991</u>	<u>\$ 681,724</u>

The annual requirements to amortize all bonds and loans outstanding at December 31, 2013, are as follows:

Year Ending December 31	Principal	Interest	Total
2014	\$ 29,114	\$ 31,762	\$ 60,876
2015	30,525	30,351	60,876
2016	32,005	28,871	60,876
2017	33,558	27,318	60,876
2018	35,185	25,691	60,876
2019-2023	85,273	112,251	197,524
2024-2028	105,691	90,749	196,440
2029-2033	132,608	63,832	196,440
2034-2038	124,725	31,081	155,806
2039-2043	<u>71,421</u>	<u>8,453</u>	<u>79,874</u>
	<u>\$ 680,105</u>	<u>\$ 450,359</u>	<u>\$ 1,130,464</u>

BUFFALO TRAIL WATER ASSOCIATION, INC.
NOTES TO FINANCIAL STATEMENTS
December 31, 2013 and 2012

5. LONG-TERM DEBT (CONTINUED)

	December 31, 2012	Additions	Retirements	December 31, 2013	Due Within One Year
Long-term debt	<u>\$ 726,417</u>	<u>\$ -</u>	<u>\$ (46,312)</u>	<u>\$ 680,105</u>	<u>\$ 29,114</u>

6. RISK MANAGEMENT

The Association is exposed to various risks of loss related torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. In addition to its general liability insurance, the Association also carries commercial insurance for all other risks of loss such as worker's compensation and employee health and accident coverage. Settled claims resulting from these risks have not exceeded commercial insurance coverage in any of the past three fiscal years.

7. DEFICIT RETAINED EARNINGS

The Association carried a deficit in retained earnings at December 31, 2013 and 2012 of \$138,295 and \$79,573, respectively. The deficit is primarily a result of user charges insufficient to provide for depreciation on contributed assets. Accumulated depreciation on contributed assets totaled \$2,737,296 and \$2,570,040 at December 31, 2013 and 2012, respectively.

**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**

To the Board of Directors
Buffalo Trail Water Association, Inc.
Sardis, Kentucky

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the Buffalo Trail Water Association, Inc. (the Association), as of and for the year ended December 31, 2013, and the related notes to the financial statements, which collectively comprise the Association's basic financial statements, and have issued our report thereon dated March 26, 2014.

Internal Control Over Financial Reporting

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

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. 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.

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 (2013-1, 2013-2, and 2013-3).

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 to those charged with governance.

**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
(CONTINUED)**

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Buffalo Trail Water Association Inc.'s financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under **Government Auditing Standards**.

Purpose of this Report

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

Ray, Foley, Hensley & Company
Ray, Foley, Hensley & Company, PLLC
March 26, 2014

BUFFALO TRAIL WATER ASSOCIATION, INC.
SCHEDULE OF FINDINGS AND RESPONSES
DECEMBER 31, 2013

FINDING 2013-1 (recurring)

The Association is required to have internal controls in place that enable it to prepare complete financial statements, including note disclosures, in compliance with generally accepted accounting principles.

The Association lacks personnel with the expertise to apply generally accepted accounting principles in preparing its financial statements including note disclosures.

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

We recommend management review the costs and benefits involved to retain a consultant with the required expertise to prepare the financial statements and ensure compliance with generally accepted accounting principles.

RESPONSE:

This is an ongoing finding. Management has determined that it is more cost effective to continue to engage the auditor to draft the financial statements and related notes.

FINDING 2013-2

The Association is required to have internal controls in place that enable it to identify discrepancies in cash accounts between book balances and bank balances.

Management is charged with performing monthly bank reconciliations to help identify these discrepancies. Our audit revealed that the cash accounts were not being reconciled to the bank statements.

We recommend management perform monthly bank reconciliations on a timely basis and that the Board of Directors review the bank reconciliations at the monthly board meetings.

RESPONSE:

Management has agreed to start reconciling cash accounts monthly, on a timely basis. The Board of Directors has agreed to review management's monthly bank reconciliations at the board meetings.

FINDING 2013-3

The Association is required to have internal controls in place that enable it to collect on accounts receivable, including following account cutoff procedures that are in compliance with PSC regulations.

Management has allowed customers to receive services, while previous balances are past due, and not attempting to remedy the default.

We recommend the Board of Directors implement cutoff policies, conforming to PSC regulations, which will give management the proper guidance to follow when applying account cutoff procedures.

RESPONSE:

The Board of Directors has agreed to implement account cutoff procedures that conform to PSC regulations.