

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

**FINANCIAL STATEMENTS
December 31, 2015 and 2014**

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**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 Buffalo Trail Water Association, Inc. (the Association), as of and for the year ended December 31, 2015, 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 25, 2016.

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 (2015-001 and 2015-002).

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.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated March 25, 2016, 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.

RFH

RFH, PLLC
March 25, 2016

BUFFALO TRAIL WATER ASSOCIATION, INC.
STATEMENTS OF FINANCIAL POSITION
DECEMBER 31,

| ASSETS | 2015 | 2014 |
|---|-------------------------|-------------------------|
| Current assets | | |
| Cash and cash equivalents | \$ 331,292 | \$ 224,865 |
| Certificates of deposit | 1,006,883 | 1,001,944 |
| Accounts receivable, net | 60,465 | 48,733 |
| Accrued interest receivable | 628 | 625 |
| Inventory | <u>18,973</u> | <u>16,360</u> |
| Total current assets | <u>1,418,241</u> | <u>1,292,527</u> |
| Capital assets | | |
| Property, plant and equipment | 7,630,019 | 7,618,178 |
| Less accumulated depreciation | <u>(3,049,723)</u> | <u>(2,893,451)</u> |
| Total capital assets | <u>4,580,296</u> | <u>4,724,727</u> |
| Other assets | | |
| Note receivable - Mt. Olivet | 23,190 | 31,278 |
| Certificate of deposit | 36,024 | 36,024 |
| Unamortized bond costs | <u>1,743</u> | <u>1,823</u> |
| Total other assets | <u>60,957</u> | <u>69,125</u> |
| TOTAL ASSETS | <u>\$ 6,059,494</u> | <u>\$ 6,086,379</u> |
| LIABILITIES AND NET ASSETS | | |
| Current liabilities | | |
| Accounts payable | \$ 20,121 | \$ 29,791 |
| Taxes payable | 7,466 | 4,472 |
| Customer deposits | 22,440 | 20,190 |
| Accrued interest payable | 2,075 | 2,190 |
| Current portion of long-term debt | <u>32,090</u> | <u>30,605</u> |
| Total current liabilities | 84,192 | 87,248 |
| Long-term debt | | |
| Notes payable | <u>584,959</u> | <u>618,734</u> |
| Total liabilities | <u>669,151</u> | <u>705,982</u> |
| Net Assets | | |
| Unrestricted net assets-debt reserves | 36,024 | 36,024 |
| Unrestricted net assets-customer contributions | 3,220,151 | 3,209,351 |
| Unrestricted net assets-grants in aid of construction | 2,317,557 | 2,317,557 |
| Unrestricted net assets (deficit) | <u>(183,389)</u> | <u>(182,535)</u> |
| Total net assets | <u>5,390,343</u> | <u>5,380,397</u> |
| TOTAL LIABILITIES AND NET ASSETS | <u>\$ 6,059,494</u> | <u>\$ 6,086,379</u> |

The accompanying notes are an integral
part of the financial statements

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

| | 2015 | 2014 |
|--------------------------------------|----------------------------|----------------------------|
| OPERATING INCOME | | |
| Water sales | \$ 637,141 | \$ 620,430 |
| Other revenue | <u>14,814</u> | <u>13,670</u> |
| Total operating income | <u>651,955</u> | <u>634,100</u> |
| OPERATING EXPENSES | | |
| Purchased water | 205,567 | 213,484 |
| Contractual services | 121,502 | 147,378 |
| Salaries and wages | 79,274 | 59,313 |
| Regulatory commission expense | 1,547 | 2,380 |
| Materials and supplies | 11,687 | 13,100 |
| Utilities and telephone | 8,833 | 11,190 |
| Insurance | 9,218 | 9,600 |
| Bad debt expense | 601 | 802 |
| Miscellaneous | <u>41,744</u> | <u>8,631</u> |
| Total operating expense | <u>479,973</u> | <u>465,878</u> |
| Operating income before depreciation | 171,982 | 168,222 |
| Depreciation expense | <u>(156,272)</u> | <u>(156,155)</u> |
| OPERATING INCOME | <u>15,710</u> | <u>12,067</u> |
| Non-operating income (expense) | | |
| Interest income | 13,074 | 8,778 |
| Interest expense | <u>(29,638)</u> | <u>(30,964)</u> |
| Total non-operating income (expense) | <u>(16,564)</u> | <u>(22,186)</u> |
| NET (LOSS) | (854) | (10,119) |
| Net assets (deficit), beginning | <u>(182,535)</u> | <u>(172,416)</u> |
| NET ASSETS (DEFICIT), ENDING | <u><u>\$ (183,389)</u></u> | <u><u>\$ (182,535)</u></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,

| | 2015 | 2014 |
|--|-------------------|-------------------|
| CASH FLOWS FROM OPERATING ACTIVITIES | | |
| Receipts from customers | \$ 642,473 | \$ 640,521 |
| Payments to suppliers | (412,982) | (402,073) |
| Payments for employee services and benefits | <u>(76,280)</u> | <u>(58,141)</u> |
| Net cash provided by operating activities | <u>153,211</u> | <u>180,307</u> |
| CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES | | |
| Customer contributions | 10,765 | 90,541 |
| Purchases of capital assets | (11,841) | (82,141) |
| Interest paid | (29,638) | (31,082) |
| Principal paid | (32,290) | (30,766) |
| Receipts from note receivable | <u>8,088</u> | <u>6,432</u> |
| Net cash (used in) financing activities | <u>(54,916)</u> | <u>(47,016)</u> |
| CASH FLOWS FROM INVESTING ACTIVITIES | | |
| Purchase of certificates of deposit | (4,939) | (156,185) |
| Interest income | <u>13,071</u> | <u>8,781</u> |
| Net cash provided by (used in) investing activities | <u>8,132</u> | <u>(147,404)</u> |
| NET INCREASE (DECREASE) IN CASH | 106,427 | (14,113) |
| Cash and cash equivalents, beginning of year | <u>224,865</u> | <u>238,978</u> |
| CASH AND CASH EQUIVALENTS, END OF YEAR | <u>\$ 331,292</u> | <u>\$ 224,865</u> |
| Reconciliation of operating income (loss) to net cash provided by (used in) operating activities: | | |
| Operating income | \$ 15,710 | \$ 12,067 |
| Adjustments to reconcile operating income to net cash provided (used) by operating activities: | | |
| Depreciation expense | 156,272 | 156,155 |
| Change in assets and liabilities: | | |
| (Increase) decrease in accounts receivable | (11,732) | 5,581 |
| (Increase) decrease in inventory | (2,613) | (254) |
| Increase (decrease) in accounts payable | (9,670) | 4,746 |
| Increase (decrease) in taxes payable | 2,994 | 1,172 |
| Increase in customer deposits | <u>2,250</u> | <u>840</u> |
| Net cash provided by operating activities | <u>\$ 153,211</u> | <u>\$ 180,307</u> |

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

BUFFALO TRAIL WATER ASSOCIATION, INC.
NOTES TO FINANCIAL STATEMENTS
December 31, 2015 and 2014

1. ORGANIZATION AND ACCOUNTING POLICIES

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

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.

The Association files an income tax return in the U.S. federal jurisdiction and the state of Kentucky. The Association is no longer subject to income tax examinations by tax authorities for years before 2012. Association believes there are no tax positions that meet the more likely than not threshold for disclosure in these financial statements.

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 activities report all revenues and expenses as operating, except interest income, interest expense, and amortization.

Basis of Presentation

The Association is required to report information regarding its financial position and activities according to the three classes of net assets; unrestricted, temporarily restricted, and permanently restricted.

Unrestricted - These assets generally result from revenues from providing services, receiving unrestricted contributions and receiving dividends and interest from income-producing assets, less expense incurred in providing services, raising contributions and performing administrative functions. The only limits on unrestricted net assets are the board limits resulting from the nature of the Organization, the environment in which it operates and the purposes specified in its articles of incorporation.

Temporarily restricted - These assets result from receiving contributions that may be expended only for specific purposes or in specific future periods. There were no temporarily restricted net assets for the years ended December 31, 2015 or 2014.

Permanently restricted - These assets represent funds that are permanently restricted by the donor with income and appreciation available to support the general operations of the Association. There were no permanently restricted net assets for the years ended December 31, 2015 or 2014.

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, 2015 and 2014 totaled \$10,006 and \$12,631, respectively.

BUFFALO TRAIL WATER ASSOCIATION, INC.
NOTES TO FINANCIAL STATEMENTS
December 31, 2015 and 2014

1. ORGANIZATION AND ACCOUNTING POLICIES (CONTINUED)

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.

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 25, 2016; 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, 2015, have not been evaluated by the Association.

2. CASH AND CASH EQUIVALENTS

Custodial credit risk is the risk that, in the event of the failure of the counterparty, the Association will not be able to recover the value of the investment or collateral securities that are in the possession of an outside party. In order to anticipate market changes and provide a level of security for all funds, the collateralization level shall be one hundred percent of the market value of the principal, plus accrued interest.

The Association's deposits and investments at December 31, 2015 and 2014 were substantially covered by Federal Depository Insurance. These deposits totaled \$1,384,181 and \$1,371,489, respectively. There were uninsured deposits at December 31, 2015. There were no uninsured deposits at December 31, 2014.

| | |
|--------------------------------|---------------------|
| FDIC Insurance | \$ 1,270,425 |
| Uninsured and uncollateralized | <u>113,756</u> |
| Total | <u>\$ 1,384,181</u> |

BUFFALO TRAIL WATER ASSOCIATION, INC.
NOTES TO FINANCIAL STATEMENTS
December 31, 2015 and 2014

3. CAPITAL ASSETS

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

| | Balance 12/31/2014 | Additions | Disposals | Balance 12/31/2015 |
|--------------------------------------|-------------------------------|---------------------|------------------|-------------------------------|
| 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 | 7,608,400 | 11,841 | - | 7,620,241 |
| Less: accumulated depreciation | <u>(2,893,451)</u> | <u>(156,272)</u> | <u>-</u> | <u>(3,049,723)</u> |
| Total depreciated | <u>4,714,949</u> | <u>(144,431)</u> | <u>-</u> | <u>4,570,518</u> |
| Capital assets, net | <u>\$ 4,724,727</u> | <u>\$ (144,431)</u> | <u>\$ -</u> | <u>\$ 4,580,296</u> |

Depreciation expense totaled \$156,272 and \$156,155 for the years ended December 31, 2015 and 2014, respectively.

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 the Association \$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, 2015 totaled \$57,975, the receivable at December 31, 2015 totaled \$23,190. The debt at year end December 31, 2014 totaled \$76,577, the receivable December 31, 2014 totaled \$31,278.

5. LONG-TERM DEBT

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

| Notes-Farmers Home Administration | 2015 | 2014 |
|---|-------------------|-------------------|
| Loan - \$364,000, dated 5/12/80, payable in annual installments of \$21,588 through 2020, bearing interest at a rate of 5% | \$ 57,975 | \$ 76,577 |
| Loan - \$347,000, date 8/6/99, payable in annual installments of \$20,400 through 2040, bearing interest at a rate of 4.75% | 259,074 | 266,964 |
| Loan - \$347,000, dated 5/14/3, payable in annual installments of \$19,394 through 2040, bearing interest at a rate of 4.5% | <u>300,000</u> | <u>305,799</u> |
| Total debt | 617,049 | 649,340 |
| Less: current portion | <u>(32,090)</u> | <u>(30,605)</u> |
| Long-term portion | <u>\$ 584,959</u> | <u>\$ 618,734</u> |

BUFFALO TRAIL WATER ASSOCIATION, INC.
NOTES TO FINANCIAL STATEMENTS
December 31, 2015 and 2014

5. LONG-TERM DEBT (CONTINUED)

The annual requirements to amortize all bonds and loans outstanding at December 31, 2015, are as follows:

| Year Ending December 31 | Principal | Interest | Total |
|----------------------------|-------------------|-------------------|---------------------|
| 2016 | \$ 32,090 | \$ 28,786 | \$ 60,876 |
| 2017 | 33,646 | 27,230 | 60,876 |
| 2018 | 34,467 | 25,599 | 60,066 |
| 2019 | 15,402 | 23,886 | 39,288 |
| 2020 | 16,117 | 23,171 | 39,288 |
| 2021-2025 | 92,524 | 103,916 | 196,440 |
| 2026-2030 | 116,086 | 80,354 | 196,440 |
| 2031-2035 | 145,654 | 50,786 | 196,440 |
| 2036-2040 | 93,400 | 20,083 | 113,483 |
| 2041-2044 | <u>37,663</u> | <u>2,683</u> | <u>40,346</u> |
| | <u>\$ 617,049</u> | <u>\$ 386,494</u> | <u>\$ 1,003,543</u> |

| | December 31, 2014 | Additions | Retirements | December 31, 2015 | Due Within One Year |
|----------------|----------------------|-------------|--------------------|----------------------|---------------------------|
| Long-term debt | <u>\$ 649,339</u> | <u>\$ -</u> | <u>\$ (32,290)</u> | <u>\$ 617,049</u> | <u>\$ 32,090</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 NET ASSETS

The Association carried a deficit in net assets at December 31, 2015 and 2014 of \$183,389 and \$182,535, respectively. The deficit is primarily a result of user charges insufficient to provide for depreciation on contributed assets. Accumulated depreciation on contributed assets totaled \$3,049,724 and \$2,893,451 at December 31, 2015 and 2014, respectively.



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 Buffalo Trail Water Association, Inc. (the Association) as of and for the years ended December 31, 2015 and 2014, 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.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of Buffalo Trail Water Association, Inc., as of December 31, 2015 and 2014, 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.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether 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.

RFH

RFH, PLLC
March 25, 2015

BUFFALO TRAIL WATER ASSOCIATION, INC.
SCHEDULE OF FINDINGS AND RESPONSES
December 31, 2015

FINDING 2015-001 (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 2015-002 (recurring)

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.