

**Butler County
Water System, Inc.**

Financial Statements

December 31, 2013 and 2012



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Independent Auditor's Report

Board of Directors
Butler County Water System, Inc.
Morgantown, Kentucky

Report on the Financial Statements

We have audited the accompanying financial statements of the Butler County Water System, Inc. (the "Utility") which comprise the balance sheets as of December 31, 2013 and 2012, and the related statements of operations, changes in members' equity and cash flows for the years then ended, and the related notes to the financial statements.

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 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 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 Butler County Water System, Inc. as of December 31, 2013 and 2012, and the changes in its financial position and cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Supplemental and Other Information

Our audits were conducted for the purpose of forming an opinion on the financial statements as a whole. The schedules of budgetary comparison on pages 26 and 27 are presented for purposes of additional analysis and are not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.

The financial and statistical highlights have not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we do not express an opinion or provide any assurance on them.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated April 3, 2014, on our consideration of the Butler County Water System, Inc.'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 Utility's internal control over financial reporting and compliance.

Carr, Riggs & Ingram, L.L.C.

Carr, Riggs & Ingram, LLC
Bowling Green, Kentucky
April 3, 2014

Other Information

Financial and Statistical Highlights

FINANCIAL & STATISCIAL HIGHLIGHTS

The following are financial and statistical highlights of Butler County Water System, Inc. for year ending December 31, 2013 and 2012.

- The System's total assets increased by \$12,054 to \$21,164,795 from \$21,152,741 in the prior year.
- Total operating revenue for the year decreased by \$62,332 from the prior year, a 3.5% decrease. Total operating expenses for the year decreased by \$24,641 from last year, a 1.5% decrease.
- Total water sales decreased by \$60,624 from the prior year, a 3.5% decrease. Residential sales decreased by \$52,694, or -3.5%; commercial sales decreased by \$7,930, or -3.8%. In year 2012 hot and dry weather conditions resulted in higher than normal water consumption compared to year 2013 when cool and wet weather conditions resulted in reduced water consumption.
- Total water sales were less than budgeted sales by \$162,249 due to the following: (1) a retail rate increase budgeted for July 2013 was expected to add \$80,120 in revenue was not implemented; and (2) the impact of a cool and wet year resulted in lower than budgeted water sales of \$82,129.
- The System uses Green River as a water source and produces water at its water treatment facility located on Middle Ferry Road in Morgantown, Kentucky. Total gallons produced for the year amounted to 297.8 million gallons compared to 318.2 million gallons in the prior year, a decrease of 6.4%. The peak production month was July 2013 which produced 27.2 million gallons.
- Total gallons sold to the System's customers during the year amounted to 241.5 million gallons compared to 256.7 million gallons in the prior year, a decrease of 5.9%. The peak demand month was July 2013 with 22.9 million gallons sold.
- The average monthly usage per residential customer was 3,818 gallons compared to 4,056 gallons in the prior year, a 5.9% decrease. The average monthly usage per commercial customer was 9,809 gallons compared to 10,601 gallons in the prior year, a 7.5% decrease.
- The number of customers at the end of the year totaled 4,813 consisting of 4,519 residential customers and 294 commercial customers.
- The System installed 25 new 5/8" size water meters during the year.
- The System has a total of 528 miles of distribution main serving an average of 9.1 customers per mile and 30 miles of service line.
- Project completed: *Highway 231 Water Line Relocation* – consisted of relocating approximately 6,800 linear feet of 4-, 8-, & 12-inch water line for a total project cost of \$419,800 which was 100% funded through the Kentucky Department of Transportation.

Financial Statements

Butler County Water System, Inc.
Balance Sheets

December 31,	2013	2012
Assets		
Current Assets		
Cash and cash equivalents	\$ 775,989	\$ 697,113
Short-term investments	500,000	-
Accounts receivable:		
Customer accounts receivable, net of allowance for uncollectibles of \$75,962 and \$72,672	59,235	61,068
Accounts receivable – WCWD	46,003	42,405
Accounts receivable – SCWD	19	1,778
Accounts receivable – other	549	106,314
Prepaid expenses	19,132	16,284
Total current assets	1,400,927	924,962
Property, Plant & Equipment		
Land and land rights	101,521	101,521
Utility plant in service	26,844,892	26,198,187
Construction in progress	172,498	494,421
Less: accumulated depreciation	(7,975,452)	(7,500,133)
Property, plant & equipment, net	19,143,459	19,293,996
Other Assets		
Restricted cash and cash equivalents	374,175	182,451
Restricted investments	125,749	125,372
Investments	-	500,000
Deferred charges	120,485	125,960
Total other assets	620,409	933,783
Total Assets	\$ 21,164,795	\$ 21,152,741

December 31,	2013	2012
Liabilities and Members' Equity		
Current Liabilities		
Accounts payable	\$ 7,802	\$ 78,072
Accounts payable – WCWD	96,751	102,162
Accrued interest payable	67,766	30,733
Other current liabilities	4,697	4,711
Current portion of long-term debt	184,273	60,740
Total current liabilities	361,289	276,418
Long-term Liabilities		
Rebates payable	14,625	14,625
Customer deposits	125,305	121,872
Loans payable	4,230,985	4,421,003
Total long-term liabilities	4,370,915	4,557,500
Total liabilities	4,732,204	4,833,918
Members' equity		
Capital investments	14,085,948	13,971,655
Retained earnings	2,346,643	2,347,168
Total members' equity	16,432,591	16,318,823
Total Liabilities and Members' Equity	\$ 21,164,795	\$ 21,152,741

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

Butler County Water System, Inc.
Statements of Operations

Years Ended December 31,	2013	2012
Operating Revenues		
Metered sales:		
Residential	\$ 1,462,847	\$ 1,515,541
Commercial	198,875	204,737
Resale	29	2,097
Total metered sales	1,661,751	1,722,375
Forfeited discounts	29,217	29,105
Miscellaneous service revenue	28,725	30,545
Total operating revenues	1,719,693	1,782,025
Operating Expenses		
Pumping expense:		
Purchased power	38,199	39,556
Salaries and benefits	-	33
Insurance	2,709	2,688
Miscellaneous	3,202	5,634
Professional services	754	718
Total pumping expense	44,864	48,629
Water treatment expense:		
Purchased power	79,719	82,182
Chemicals	39,612	48,830
Materials and supplies	12,779	12,619
Insurance	5,418	5,376
Salaries and benefits	88,966	94,868
Contractual services	3,209	2,612
Miscellaneous	5,758	7,051
Professional services	1,508	1,436
Total water treatment expense	236,969	254,974
General distribution expense:		
Purchased power	3,960	3,872
Salaries and benefits	109,820	114,144
Materials and supplies	21,198	30,758
Insurance	11,738	11,648
Miscellaneous	23,504	27,078
Contractual services	14,605	13,706
Professional services	755	719
Total general distribution expense	185,580	201,925

Years Ended December 31,	2013	2012
Customer accounts expense:		
Salaries and benefits	190,700	189,810
Contractual services	46,889	44,437
Uncollectible accounts	3,290	5,160
Materials and supplies	1,170	1,410
Insurance	1,354	1,344
Miscellaneous	27,229	30,337
Professional services	2,263	2,154
Total customer accounts expense	272,895	274,652
Maintenance expense:		
Pumping equipment and storage expense	18,447	20,843
Salaries and benefits	105,478	116,529
Contractual services	30,282	28,554
Professional services	1,509	1,437
Total maintenance expense	155,716	167,363
Administrative and general expense:		
Salaries and benefits	78,907	66,181
Materials and supplies	3,327	6,046
Insurance	2,323	2,350
Miscellaneous	3,048	2,533
Contractual services	26,215	25,058
Professional services	4,992	2,154
Total administrative and general expense	118,812	104,322
Depreciation and amortization expense	554,672	542,284
Total operating expenses	1,569,508	1,594,149
Operating income	150,185	187,876
Non-Operating Revenues (Expenses)		
Other income	14,545	13
Interest income	9,221	11,860
Interest expense on long-term debt	(171,087)	(218,790)
Interest expense on customer deposits	(208)	(697)
PSC taxes	(3,181)	(3,080)
Total non-operating revenues (expenses)	(150,710)	(210,694)
Net Loss	\$ (525)	\$ (22,818)

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

Butler County Water System, Inc.
Statements of Changes in Members' Equity

Years Ended December 31, 2013 and 2012	Retained Earnings	Contributions in Aid of Construction	Total
Balance, January 1, 2012	\$ 2,369,986	\$ 13,644,563	\$ 16,014,549
Net loss	(22,818)	-	(22,818)
Contributions in aid of construction	-	327,092	327,092
Balance, December 31, 2012	2,347,168	13,971,655	16,318,823
Net loss	(525)	-	(525)
Contributions in aid of construction	-	114,293	114,293
Balance, December 31, 2013	\$ 2,346,643	\$ 14,085,948	\$ 16,432,591

Butler County Water System, Inc.
Statements of Cash Flows

Years Ended December 31,	2013	2012
Cash Flows From Operating Activities		
Receipts from customers and agencies	\$ 1,719,687	\$ 1,657,600
Payments to suppliers for goods and services	(400,847)	(432,786)
Payments for contractual services	(573,871)	(581,565)
Net cash provided by operating activities	744,969	643,249
Cash Flows From Noncapital Financing Activities		
Interest paid on customer deposits	(208)	(697)
Net cash used in noncapital financing activities	(208)	(697)
Cash Flows From Capital and Related Financing Activities		
Principal repayment on long-term debt	(66,485)	(3,193,968)
Proceeds from issuance of long-term debt	-	3,045,000
Contributions in aid of construction	114,293	327,092
Purchases of capital assets	(396,759)	(653,137)
Debt issuance costs	-	(79,602)
Interest paid on long-term debt	(134,054)	(337,057)
Net cash used in capital and related financing activities	(483,005)	(891,672)
Cash Flows From Investing Activities		
Purchase of short-term investments	(377)	(625,372)
Maturity of short-term investments	-	119,635
Interest income	9,221	11,860
Net cash provided by (used in) investing activities	8,844	(493,877)
Net Increase (Decrease) in Cash and Cash Equivalents	270,600	(742,997)
Balances – Beginning of Year	879,564	1,622,561
Balances – End of Year	\$ 1,150,164	\$ 879,564

Years Ended December 31,	2013	2012
Reconciliation of Operating Income to Net Cash Provided		
By Operating Activities		
Operating income	\$ 150,185	\$ 187,876
Adjustment to reconcile net operating income to net cash provided by operating activities:		
Depreciation	547,296	542,184
Amortization	7,376	100
Non-utility income	14,545	13
Payment of PSC taxes	(3,181)	(3,080)
Changes in assets and liabilities:		
Net (increase) decrease in accounts receivable, net	105,759	(124,425)
Net increase in prepaid insurance	(2,848)	(125)
Net increase in deferred charges	(1,901)	(847)
Net increase (decrease) in accounts payable	(75,681)	38,536
Net increase (decrease) in other current liabilities	(14)	281
Net increase in customer deposits	3,433	2,736
Net Cash Provided By Operating Activities	\$ 744,969	\$ 643,249

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

Note 1: Summary of Significant Accounting Policies

• ***Nature of Business***

The Butler County Water System, Inc. (“Utility”) is a water association organized as a non-profit corporation under KRS 273 and is under the authority of the Public Service Commission of Kentucky. The Utility provides a public water system to primarily citizens located in Butler County, Kentucky.

The accounting policies of the Utility conform to generally accepted accounting principles as applicable to a non-profit membership association. The following is a summary of the more significant policies:

▶ **Reporting Entity**

The Utility is governed by a five-member board (the “Board”). The Board of Commissioners is elected by the members of the Utility. The Board has the power and authority to acquire, construct, maintain and operate the waterworks system.

▶ **Basis of Accounting**

Basis of accounting refers to the point at which revenues or expenses are recognized in the accounts and reported in the financial statements. It relates to the timing of the measurements made regardless of the measurement focus applied. The accompanying financial statements have been prepared on the accrual basis of accounting.

The Utility follows the practice of recording metered sales when billed to the customers and recording related expenses when billed to the water Utility. This results in a lag of recording revenue and related expenses. However, it does provide approximate matching of revenue and expenses and does not have a material effect between years. Operating revenues are revenues generated from general water operations (water sales, forfeited discounts and miscellaneous service revenue) and all other non-water revenues are considered non-operating revenues.

▶ **Use of 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 reporting period. Actual results could differ from those estimates.

Note 1: Summary of Significant Accounting Policies
(Continued)

▶ **Cash and Cash Equivalents**

The Utility has defined cash and cash equivalents to include all highly liquid investments (including restricted assets) with a maturity of three months or less when purchased to be cash equivalents.

▶ **Accounts Receivable**

Customer accounts receivable amounts arise from monthly water usage. Based on Utility policy, water meters are read monthly, with billings occurring approximately ten days subsequent to the reading. Once billed, the customer has 16 days to pay the amount due. If payment is not made by the due date, a two to four day grace period is granted. If payment is not made at the expiration of the grace period, a late penalty is assessed to water charges and delinquent notices are sent. Customers are given 14 days from the date of the delinquent notice to render payment. Customer service places calls to facilitate collection; if no payment is received, collection trips are made to the service location. If collection does not occur, the meter is shut off. If collection is considered unlikely, the balances are charged off as a bad debt expense in the period in which they were deemed uncollectible.

Management's periodic evaluation of the adequacy of the allowance for doubtful accounts is based on past loss experience, known and other risks inherent to the specific amount, adverse situations that may affect the customer's ability to render payment and current economic conditions. Management considers many factors in determining whether a receivable is impaired, such as payment history and changes in employment.

▶ **Concentration of Credit Risk**

The Utility extends credit to all citizens who live within the geographic location of the Utility and who utilize the utility system. Credit losses may be minimal and are generally within management's expectations.

▶ **Investments**

Investments consist of certificates of deposit and are recorded at cost. The cost of investments approximates their fair value.

Note 1: Summary of Significant Accounting Policies
(Continued)

▶ **Property, Plant and Equipment**

The Utility has an ongoing activity of assessing the feasibility of installing additional lines to new service areas. Once an extension is considered feasible, there are additional engineering studies, applications to various funding agencies and project administrative costs. The Utility defers the ongoing activity and capitalizes these costs as part of the utility plant upon completion of the project.

Management's capitalization policy is based upon the assets' estimated future benefit. Depreciation is computed using the straight-line method over the estimated useful lives of the utility plant. The estimated useful lives range from 5 to 50 years for utility plant assets. Upon retirement, the cost of the asset, less any proceeds, is charged to accumulated depreciation.

The Utility capitalizes construction period interest on loans that were obtained to finance construction.

▶ **Income Taxes**

The Utility has applied as a tax-exempt organization under Section 501(c)(12) of the Internal Revenue Code and, accordingly, the status is pending upon the Internal Revenue Service's approval. Management believes that the Utility is designed and is currently being operated in compliance with the applicable requirements of Section 501(c)(12) of the Internal Revenue Code and is, therefore, exempt from taxes.

● **Contributions in Aid of Construction**

Contributions in aid of construction consist of member fees, developer contributed utility systems, capital grants and other supplemental support by other utilities and industrial customers and federal, state and local grants in support of system improvements.

● **Uncertain Tax Positions**

The Utility follows accounting requirements associated with uncertainty in income taxes using the provisions of Financial Accounting Standards Board (FASB) ASC 740, *Income Taxes*. The guidance prescribed a minimum recognition threshold and measurement methodology that a tax position taken or expected to be taken in a tax return is required before being recognized in the financial statements. It also provides guidance for derecognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. As of December 31, 2013, the Utility has no uncertain tax positions that qualify for recognition; however, a disclosure in the financial statements of

Note 1: Summary of Significant Accounting Policies
(Continued)

an uncertain tax position is reflected in Note 1 under income taxes. With a few exceptions, the Utility is no longer subject to tax reporting examinations by the U.S. federal authorities for the years ended December 31, 2009 and prior.

• ***Subsequent Events***

The Utility has evaluated any recognized or unrecognized subsequent events for consideration in the accompanying financial statements through April 3, 2014 which was the date the financial statements were made available.

• ***Reclassifications***

Amounts in the 2012 financial statements have been reclassified to be comparable with the presentation of the 2013 financial statements. The reclassification had no impact on the net loss for 2012.

Note 2: Cash and Cash Equivalents and Investments

The Utility maintains its deposits with financial institutions insured by the Federal Deposit Insurance Corporation (FDIC). As of December 31, 2013 and 2012, the carrying amounts of the Utility's deposits were \$1,775,913 and \$1,504,936 and the bank balances were \$1,794,369 and \$1,572,620, respectively.

December 31,	2013	2012
Cash and cash equivalents	\$ 775,989	\$ 697,113
Restricted cash and cash equivalents	374,175	182,451
Short-term investments	500,000	-
Investments	-	500,000
Restricted investments	125,749	125,372
	\$ 1,775,913	\$ 1,504,936

Note 3: Restricted Cash and Investments

• **Cash Concentration Risk — Deposits**

Custodial credit risk is the risk that in the event of a bank failure, the Utility’s deposits may not be returned to it. The Utility’s formal deposit policy for custodial credit risk requires deposits in banks which are in excess of the FDIC insurance coverage to be secured by the bank pledging securities in direct obligations of the United States of America or by approved security bonds. As of December 31, 2013 and 2012, the Utility’s bank balance was not exposed to custodial credit risk.

The sinking funds are restricted to the payment of principal and interest on long-term debt.

The depreciation fund is restricted to payment for improvements and approved repairs.

The customer deposits fund is restricted to hold customer deposits until service is terminated.

December 31,	2013	2012
Sinking funds	\$ 186,268	\$ 3,044
Depreciation fund	187,907	174,407
Customer deposits	125,749	130,372
	\$ 499,924	\$ 307,823

Note 4: Property, Plant and Equipment

December 31,	2013	2012
Non-depreciable:		
Land and land rights	\$ 101,521	\$ 101,521
Construction in progress	172,498	494,421
Depreciable:		
Utility plant in service	26,844,892	26,198,187
Less: accumulated depreciation	(7,975,452)	(7,500,133)
Property, Plant and Equipment, Net	\$ 19,143,459	\$ 19,293,996

Butler County Water System, Inc.
Notes to the Financial Statements (Continued)

Note 4: Property, Plant and Equipment *(Continued)*

Depreciation expense was \$547,296 and \$542,184 for the years ended December 31, 2013 and 2012, respectively.

Note 5: Rebates Payable

These amounts are partially made up of private developers' unrecovered costs in installing water lines. Utility plant was increased for a like amount when the facilities were donated to the water Utility. As meters are placed in the development, the developer receives half of the new customers' contribution for meters connected directly to the extension over the next ten years or up to the value of facilities constructed. The remaining balance in this account was obtained from subscriptions of prospective users of the water Utility. When a meter is installed, the subscribed amount is transferred to contributions in aid of construction.

Note 6: Long-Term Debt

The loans below from Series 1973 through Series 1998 were issued through USDA, Rural Development (RD). The Series 2012 loan was issued through Kentucky Rural Water Finance Corporation (KRWFC). The following table shows loans outstanding:

Original Amount	Series of	Interest Rate	Balance as of December 31,	
			2013	2012
\$ 116,000	1973	5.00%	\$ -	\$ 2,666
117,400	1974	5.00%	-	11,744
191,400	1977	5.00%	39,801	48,715
152,000	1979	5.00%	36,697	43,637
950,000	1996	4.50%	737,061	755,195
40,013	1997	5.00%	8,968	11,696
197,214	1997	4.50%	147,908	152,105
545,000	1998	4.75%	399,823	410,985
3,045,000	2012	2.80% - 4.00%	3,045,000	3,045,000
			\$ 4,415,258	\$ 4,481,743

Butler County Water System, Inc.
Notes to the Financial Statements (Continued)

Note 6: Long-Term Debt (Continued)

All loans are secured by an exclusive pledge of a fixed portion of the income and revenues derived from the operation of the Utility's water distribution system. The RD loans each have a requirement for depreciation reserves. The KRWFC loan has requirements for a debt service sinking fund and a debt service coverage ratio, which were in compliance at December 31, 2013 and 2012.

Principal and interest of various amounts are due at least annually in each of the years through 2037. The principal and interest due for each of the next five years and thereafter is as follows:

Year	Principal Amount	Interest Amount
2014	\$ 184,273	\$ 167,696
2015	201,849	161,269
2016	209,489	154,439
2017	208,520	147,413
2018	186,828	140,610
Thereafter	3,424,299	1,214,687
	\$ 4,415,258	\$ 1,986,114

Note 7: Related Parties

The Warren County Water District (WCWD) provides management, engineering and repair and maintenance services to the Utility. Simpson County Water District shares common management with WCWD.

The following related party amounts were included in accounts receivable.

December 31,	2013	2012
Warren County Water District	\$ 46,003	\$ 42,405
Simpson County Water District	19	1,778

Butler County Water System, Inc.
Notes to the Financial Statements (Continued)

Note 7: Related Parties (Continued)

The following related party amounts were included in accounts payable.

<u>December 31,</u>	<u>2013</u>	<u>2012</u>
Warren County Water District	\$ 96,751	\$ 102,162

During 2013 and 2012, expenses from the WCWD amounted to \$907,404 and \$970,728, respectively, for the following expenses:

<u>Years Ended December 31,</u>	<u>2013</u>	<u>2012</u>
Wages and benefits:		
Operation	\$ 447,207	\$ 465,995
Administrative:		
Supervision and administration	111,192	108,110
Accounting	42,624	38,229
Customer service	74,974	73,394
Engineering	27,447	28,925
Operations - other	82,630	105,121
Additions to plant	59,966	47,946
Special projects	61,364	103,008
Totals	\$ 907,404	\$ 970,728

In the ordinary course of business, the Utility has and expects to continue to have transactions with WCWD. In the opinion of management, such transactions were on substantially the same terms as those prevailing at the time of comparable transactions with other persons and did not involve more than a normal risk of collectability or present any other unfavorable features to the Utility.

Note 8: Risks of Loss

The Utility's risks of loss are addressed by the purchase of commercial insurance. These areas include employee dishonesty bonds, property coverage, vehicle coverage and a public entity liability policy which includes errors and omission. Coverage is reviewed for adequacy by management and agents on an annual basis.

Note 9: Rochester Dam Regional Water Commission

The Rochester Dam Regional Water Commission (“RDRWC”) is a water commission which was created by an Order issued by the Ohio County Judge/Executive on June 13, 2013 pursuant to the provisions of KRS 74.440. Butler County Water System, Inc. participated in the creation of the RDRWC along with the City of Morgantown, Kentucky and the Ohio County Water District. The Board of Commissioners for the RDRWC is comprised of one representative from each of the three establishing entities plus two additional representatives appointed by the Ohio County Judge/Executive and approved by the Ohio County Fiscal Court.

The primary purpose of the RDRWC is to provide an adequate and dependable supply of water for the region which derives its water supply from Pool 3 of the Green River including, but not limited to, Butler, Muhlenberg, and Ohio Counties and all customers and entities served by the RDRWC members. RDRWC will endeavor to accomplish this purpose by: (1) acquiring an ownership interest, either by lease, easement, or deed, in the Rochester Dam on Pool 3 of the Green River; (2) repairing and stabilizing the Rochester Dam; and (3) maintaining the Rochester Dam.

The RDRWC is pursuing a lease on the Rochester Dam from the Corp of Engineers in order to obtain funding through the EDA or other agency grants to perform the necessary repairs for the dam. As of December 31, 2013, Butler County Water System has not incurred any charges for its participation in the RDRWC. Future payments to cover legal expenses of the RDRWC are estimated to be minimal and will be prorated between all participating entities.

Supplementary Information

Butler County Water System, Inc.
Schedules of Budgetary Comparison

Year Ended December 31, 2013

	<u>Budgeted Amounts</u>		Actual	Variances
	Original	Final		Favorable (Unfavorable) Final to Actual
Revenues				
Metered revenue	\$ 1,824,000	\$ 1,824,000	\$ 1,661,751	\$ (162,249)
Forfeited discounts	31,475	31,475	29,217	(2,258)
Miscellaneous service revenue	32,955	32,955	28,725	(4,230)
Interest income	10,790	10,790	9,221	(1,569)
Other income	-	-	14,545	14,545
Total revenues	1,899,220	1,899,220	1,743,459	(155,761)
Expenses				
Salaries and wages	369,325	369,325	351,410	17,915
Fringe benefits	222,975	222,975	222,461	514
Purchased power	135,310	135,310	121,878	13,432
Chemicals	43,275	43,275	39,612	3,663
Materials and supplies	55,490	55,490	40,607	14,883
Contractual services - Accounting	9,040	9,040	9,052	(12)
Contractual services - Legal	-	-	2,729	(2,729)
Contractual services - Other	118,740	118,740	121,200	(2,460)
Rental of building and utilities	15,135	15,135	14,969	166
Equipment expense	70,505	70,505	60,907	9,598
Insurance - general liability	22,300	22,300	22,461	(161)
Insurance - other	1,095	1,095	1,081	14
Regularly expense	2,870	2,870	3,181	(311)
Bad debt expense	4,125	4,125	3,290	835
Miscellaneous expense	3,095	3,095	3,179	(84)
Depreciation	543,960	543,960	547,296	(3,336)
Amortization	-	-	7,376	(7,376)
Interest expense	193,805	193,805	171,295	22,510
Total expenses	1,811,045	1,811,045	1,743,984	67,061
Net Income (Loss)	\$ 88,175	\$ 88,175	\$ (525)	\$ (88,700)

Year Ended December 31, 2012

	Budgeted Amounts		Actual	Variances
	Original	Final		Favorable (Unfavorable) Final to Actual
Revenues				
Metered revenue	\$ 1,722,000	\$ 1,722,000	\$ 1,722,375	\$ 375
Forfeited discounts	31,725	31,725	29,105	(2,620)
Miscellaneous service revenue	31,350	31,350	30,545	(805)
Other water revenue	-	-	13	13
Interest income	16,320	16,320	11,860	(4,460)
Total revenues	1,801,395	1,801,395	1,793,898	(7,497)
Expenses				
Salaries and wages	382,960	382,960	361,707	21,253
Fringe benefits	218,285	218,285	219,858	(1,573)
Purchased power	138,340	138,340	125,610	12,730
Chemicals	60,170	60,170	48,830	11,340
Materials and supplies	56,490	56,490	55,399	1,091
Contractual services - Accounting	5,750	5,750	8,618	(2,868)
Contractual services - Legal	-	-	-	-
Contractual services - Other	117,700	117,700	114,367	3,333
Rental of building and utilities	15,135	15,135	14,956	179
Equipment expense	75,825	75,825	71,704	4,121
Insurance - general liability	24,650	24,650	22,400	2,250
Insurance - other	915	915	1,006	(91)
Regularly expense	2,740	2,740	3,080	(340)
Bad debt expense	3,320	3,320	5,160	(1,840)
Miscellaneous expense	1,930	1,930	2,250	(320)
Depreciation	550,135	550,135	542,184	7,951
Amortization	-	-	100	(100)
Interest expense	226,250	226,250	219,487	6,763
Total expenses	1,880,595	1,880,595	1,816,716	63,879
Net Loss	\$ (79,200)	\$ (79,200)	\$ (22,818)	\$ 56,382



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Independent Auditor’s Report on Internal Control over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards*

Board of Directors
Butler County Water System, Inc.
Morgantown, 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 Butler County Water System, Inc. (the “Utility”) (a nonprofit organization), as of and for the year ended December 31, 2013, and the related notes to the financial statements, and have issued our report thereon dated April 3, 2014.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Utility’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 Utility’s internal control. Accordingly, we do not express an opinion on the effectiveness of the Utility’s internal control.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. *A material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the Utility’s financial statements will not be prevented, or detected and corrected on a timely basis. *A significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. 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.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Utility'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 Utility'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 Utility's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Carr, Riggs & Ingram, L.L.C.

Carr, Riggs & Ingram, LLC
Bowling Green, Kentucky
April 3, 2014