

PUBLIC SERVICE COMMISSION
ANNUAL REPORT BRANCH
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EXAMINED BY _____

REID VILLAGE
WATER DISTRICT

REPORT ON EXAMINATION OF BASIC FINANCIAL STATEMENTS
AND SUPPLEMENTAL INFORMATION
for the year ended December 31, 2011

CONTENTS

	Page
Independent Auditor's Report	1-2
Financial Statements	
Statement of Net Assets	3
Statement of Revenues, Expenses and Changes in Fund Net Assets	4
Statement of Cash Flows	5
Notes to the Financial Statements	6-11
Supplemental Information	
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	12-13
Comparative Statement of Revenues and Expenses	14
Schedule of Findings and Responses	15-16

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INDEPENDENT AUDITOR'S REPORT

Board of Commissioners
Reid Village Water District
Mt. Sterling, Kentucky

We have audited the accompanying financial statements listed in the Table of Contents of the business-type activities of the Reid Village Water District as of and for the year ended December 31, 2011 which comprises the District's basic financial statements. These financial statements are the responsibility of the District's management. 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 of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

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

In accordance with Government Auditing Standards, we have also issued our report dated April 26, 2012 on our consideration of the Reid Village Water District's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, 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 the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with Government Auditing Standards and should be read in conjunction with this report in considering the results of our audit.

Management has elected to omit the Management Discussion and Analysis which is supplemental information required by the Governmental Accounting Standards Board.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Reid Village Water District's basic financial statements. The schedules listed in the table of contents are presented for the purpose of additional analysis and are not a required part of the financial statements of the Reid Village Water District. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly presented in all material respects in relation to the basic financial statements taken as a whole.

John T. Lane & Associates, LLC

April 26, 2012

This report contains 16 pages.

Reid Village Water District
Statement of Net Assets
Proprietary Fund
December 31, 2011

ASSETS

Current Assets	
Cash and cash equivalents - unrestricted	\$ 364,206
Cash and cash equivalents - restricted	109,118
Accounts receivable - net of allowance for doubtful accounts	42,283
Prepaid expenses	<u>4,817</u>
Total Current Assets	<u>520,424</u>
Noncurrent Assets	
Capital assets:	
Land	7,000
Plant, equipment and lines	1,769,800
Less accumulated depreciation	<u>(522,867)</u>
Total Noncurrent Assets	<u>1,253,933</u>
Total Assets	<u><u>\$ 1,774,357</u></u>

LIABILITIES

Current Liabilities	
Accrued expenses	\$ 21,865
Bonds payable	12,000
Payable from restricted assets	<u>33,253</u>
Total Current Liabilities	<u>67,118</u>
Noncurrent Liabilities	
Bonds payable	<u>721,000</u>
Total Noncurrent Liabilities	<u>721,000</u>
Total Liabilities	<u>788,118</u>

NET ASSETS

Invested in capital assets, net of related debt	520,933
Restricted net assets	75,865
Unrestricted net assets	<u>389,441</u>
Total Net Assets	<u><u>\$ 986,239</u></u>

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

Reid Village Water District
Statement of Revenues, Expenses and Changes in Fund Net Assets
Proprietary Fund
December 31, 2011

Revenues	
User fees	\$ 438,317
Other water revenue	<u>15,856</u>
Total Revenues	<u>454,173</u>
Expenses	
Water purchased	148,062
Vehicle expense	14,023
Rent	6,000
Postage	3,709
Salaries	120,661
Office expense	32,635
Insurance	9,542
Water samples	1,600
Taxes and benefits	41,568
Maintenance	26,338
Miscellaneous	7,726
Bad debt expense	3,848
Depreciation	<u>35,267</u>
Total Operating Expenses	<u>450,979</u>
Operating Income (Loss)	<u>3,194</u>
Nonoperating Revenues (Expenses)	
Tap fees	2,510
Interest income	919
Interest expense	<u>(33,825)</u>
Net Nonoperating Revenues (Expenses)	<u>(30,396)</u>
Net Income (Loss)	(27,202)
Total Net Assets - beginning	<u>1,013,441</u>
Total Net Assets - ending	<u><u>\$ 986,239</u></u>

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

Reid Village Water District
Statement of Cash Flows
Proprietary Fund Type
December 31, 2011

CASH FLOWS FROM OPERATING ACTIVITIES:	
Operating revenues	\$ 458,256
Cash paid to employees	(120,661)
Cash paid for general and administrative expenses	<u>(294,411)</u>
Net Cash provided by operating activities	<u>43,184</u>
CASH FLOWS FROM INVESTING ACTIVITIES:	
Interest earned	919
Customer deposits	<u>2,404</u>
Net Cash provided by investing activities	<u>3,323</u>
CASH FLOWS FROM CAPITAL AND FINANCING ACTIVITIES:	
Bond payments	(11,300)
Purchase of fixed assets	(12,940)
Tap fees	2,510
Interest paid	<u>(34,088)</u>
Net Cash used in capital and financing activities	<u>(55,818)</u>
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(9,311)
CASH AND CASH EQUIVALENTS - BEGINNING OF YEAR	<u>482,635</u>
CASH AND CASH EQUIVALENTS - END OF THE YEAR	<u><u>\$ 473,324</u></u>
RECONCILIATION OF NET CASH PROVIDED BY OPERATING ACTIVITIES:	
Net Operating Income	\$ 3,194
Adjustments to Reconcile Net Income to Net Cash Provided by Operating Activities:	
Depreciation	35,267
(Increase)/Decrease in accounts receivable	1,790
(Increase)/Decrease in prepaid expenses	(217)
Increase/(Decrease) in accrued expenses	<u>3,150</u>
Net cash provided by operating activities	<u><u>\$ 43,184</u></u>

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

REID VILLAGE WATER DISTRICT
NOTES TO THE FINANCIAL STATEMENTS
December 31, 2011

The Reid Village Water District is a water utility which services areas of Montgomery County including Reid Village. Its sales are primarily to residential customers. The District is a corporate body set forth in Kentucky Revised Statutes (KRS) 74.070 which was created November, 1961. The District began operations in 1964. The District is subject to the regulatory District of the Kentucky Public Service Commission pursuant to KRS 278.040.

Note 1 - Summary of Significant Accounting Policies

The accounting policies of the District conform to accounting principles generally accepted in the United States of America as applicable to governments. The following is a summary of the more significant policies.

The Reporting Entity

The District, for financial purposes, includes all of the funds relevant to the operations of the District. The financial statements presented herein do not include agencies which have been formed under applicable state laws or separate and distinct units of government apart from the Reid Village Water District.

The financial statements of the District would include those of separately administered organizations that are controlled by or dependent on the District. Control or dependence is determined on the basis of financial interdependency, selection of governing District, designation of management, ability to significantly influence operations, accountability of fiscal matters, scope of public service, and financing relations.

Based on the foregoing criteria there are not other organizations included in these financial statements.

The District, presented as an enterprise fund, does not apply Financial Accounting Standards Board (FASB) pronouncements and Accounting Principles Board (APB) opinions issued on or after November 30, 1989.

Depreciation Reserve Fund - Monthly transfers are required to be made into this fund in the amount of \$395. Only expenditures for capital improvements or extraordinary expenses are permitted to be paid from this fund. The District had set aside \$46,358 into this fund at December 31, 2011. The required balance is \$36,300.

Bond and Interest Sinking Fund - Monthly transfers are required to be made into this account in an amount equal to one-sixth (1/6) of the interest becoming due on the next succeeding interest due date for all outstanding bonds and one-twelfth (1/12) of the principal of all such bonds maturing on the next succeeding due date. The required balance of the fund at December 31, 2010 was \$28,912. The District had set aside \$44,050.

Enterprise Funds

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

The accounting and financial reporting treatment applied to the District is determined by its measurement focus. The transactions of the District are accounted for on a flow of economic resources measurement focus. With this measurement focus, all assets and all liabilities associated with the operations are included on the balance sheet. Net assets (i.e., total assets net of total liabilities) are segmented into invested in capital assets, net of related debt, restricted and unrestricted components. When both restricted and unrestricted resources are available for use, it is the District's policy to use restricted resources first, and then unrestricted resources as they are needed.

An enterprise fund distinguishes 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 District's principal ongoing operations. The principal operating revenues of the Authority are operating grants and tenant rental revenue. Operating expenses of the District include the cost of producing the revenue and services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

Basis of Accounting

The records of the District are maintained and the budgetary process is based on the cash basis method of accounting. Adjustments have been made to properly reflect the fund balances.

Cash

At December 31, 2011, the carrying amount of the District's deposits was \$473,324 and the bank balance was \$475,250. Of the bank balance 100% was covered by federal deposit insurance or collateralized with securities held by the pledging financial institution's trust department or agent in the entity's name. The District considers all investments with a maturity date of three months or less from date of purchase to be cash equivalents. Certificates of deposit that are redeemable immediately with little or no penalty are considered cash equivalents

Fixed Assets

Fixed assets purchased are capitalized at the time of purchase. Such assets are recorded at cost. Donated assets are recorded at fair market value at the date of donation. Depreciation of property and equipment is computed by the straight-line method based upon the estimated useful lives of the assets as follows:

<u>Class</u>	<u>Life</u>
Water lines, tanks	50 years
Vehicle	5 years

The District's capitalization policy is as follows: expenditures costing more than \$1,000 with an estimated useful life greater than one year are capitalized: all others are expensed.

Budgets and Budgetary Accounting

The district follows these procedures in establishing the budgetary data reflected in the financial statements:

- a. Formal budgetary integration is employed as a management control device during the year for the enterprise funds. These budgets are prepared on the cash basis of accounting.
- b. Unused appropriations for all of the above annually budgeted funds lapse at the end of year.

For the year ending December 31, 2011 the above budgetary procedures were not followed.

Net Assets

Net assets represent the difference between assets and liabilities. Net assets invested in capital assets- net of related debt consists of capital assets, net of accumulated depreciation, reduced by the outstanding balance of any borrowing used for the acquisition, construction or improvement of those assets. Net assets are recorded as restricted when there are limitations imposed on their use by external restrictions.

Accounts Receivable

The receivable reflected in the statements in the amount of \$42,283 are net of allowance for uncollectibles in the amount of \$13,606.

Use of Estimates

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

Note 2 - Notes Payable

The amount shown in the accompanying financial statements as notes payable represents the District's future obligation to make loan payments from future revenues. At December 31, 2011, two separate loans had outstanding balances. Details of each of these issues are summarized as follows:

Note A

Lender – Rural Development

Balance of loan - \$351,000

Rate – 4.875%

Principal due January 1

Interest due January 1 and July 1

Prepayment provision - subject to payment prior to its stated maturity without penalty or premium, at any time upon ten (10) days notice.

Note B

Lender – Rural Development

Balance of loan - \$382,000

Rate – 4.375%

Principal due January 1

Interest due January 1 and July 1

Prepayment provision - subject to payment prior to its stated maturity without penalty or premium, at any time upon ten (10) days notice.

Five-Year Maturities

2012	12,000
2013	12,700
2014	13,900
2015	14,700
2016	15,500
Thereafter	<u>664,200</u>
	<u>\$733,000</u>

Schedule of Bonds Payable	balance <u>12/31/10</u>	<u>Additions</u>	<u>Payments</u>	balance Current <u>12/31/10</u>	Portion
USDA 91-05	\$357,500	\$-	\$6,500	\$351,000	\$7,000
USDA 91-06	<u>386,800</u>	<u>-</u>	<u>4,800</u>	<u>382,000</u>	<u>5,000</u>
	<u>744,300</u>	<u>-</u>	<u>11,300</u>	<u>733,000</u>	<u>12,000</u>

Note 3 - Pension Plan

The District's employees are not covered by any retirement plan.

Note 4 - Leave Policies

The District's employees with one year receive one week vacation, employees with two to five years receive two weeks vacation, employees with six to ten years receive three weeks vacation, employees with over ten years received four weeks vacation. Employees are not permitted to carryover vacation leave from one year to another. Sick leave is on an individual basis and decided by the commissioners. Employees with one year or less receive one-half personal day per month, while employees with over one year receive one personal day per month. Personal days are not carried over.

Note 5 - Changes in Fixed Assets

The following is a summary of changes in the fixed assets for the fiscal year:

	balance <u>12/31/10</u>	Transfer/ <u>Additions</u>	<u>Deletions</u>	balance <u>12/31/11</u>
Land	\$ 7,000	\$-	\$-	\$7,000
Property, plant & equipment	<u>1,756,860</u>	<u>12,940</u>	<u>-</u>	<u>1,769,800</u>
	<u>1,763,860</u>	<u>12,940</u>	<u>-</u>	<u>1,776,800</u>
Accumulated depreciation	<u>487,600</u>	<u>35,267</u>	<u>-</u>	<u>522,867</u>
Net fixed assets	<u>1,276,260</u>			<u>1,253,933</u>

Note 6 - Revenue Bonds

Water and Revenue Bonds constitute special obligations of the District solely secured by a lien on and pledge of the net revenues of the water system. The revenue bonds are collateralized by the revenue of the water system and the various special funds established by the bond ordinances. The ordinances provide that the revenue of the system is to be used first to pay operating and maintenance expenses of the system and second to establish and maintain the revenue bond funds. Any remaining revenues may then be used for any lawful purpose. The ordinances also contain certain provisions, which require the District to maintain pledged revenues. The District must transfer monthly 1/6 of the next succeeding interest payment and 1/12 of the next succeeding principal payment from the operations and maintenance account into the bond and interest sinking account. The District also must transfer \$395 per month into a depreciation fund.

Note 7 - Restricted Cash

Restricted cash is composed of the following:

Deposit account	\$18,710
Depreciation reserve fund	46,358
Debt reserve fund	<u>44,050</u>
	<u>\$109,118</u>

Note 8 – Contingencies

The District is subject to possible examinations made by Federal and State authorities who determine compliance with terms, conditions, laws, and regulations governing other grants given to the District in the current and prior years. There were no examinations for the year ended December 31, 2011. Areas of noncompliance, if any, as a result of examinations would be included as a part of the “Findings and Questioned Costs” section of this report.

Note 9 – Risk Management

The District is exposed to various risks of losses 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 coverage for the risks to the extent deemed prudent by District management.

SUPPLEMENTAL INFORMATION

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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

We have audited the financial statements of the Reid Village Water District as of and for the year ended December 31, 2011, and have issued our report thereon dated April 26, 2012. 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.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Reid Village Water District's internal control over financial reporting as a basis for designing our auditing procedures 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 Reid Village Water District's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Reid Village Water District's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses and therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. However, as described in the accompanying schedule of findings we identified certain deficiencies in internal control over financial reporting that we consider to be material weaknesses and other deficiencies that we consider to be significant deficiencies.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiencies described in the accompanying schedule of findings and questioned costs to be material weaknesses. (11-01 & 11-02)

A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider the deficiency described in the accompany schedule of findings and questioned costs to be a significant deficiency. (11-03)

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Reid Village 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 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*.

The Reid Village Water District's responses to the findings identified in our audit are described in the accompanying schedule of findings and responses. We did not audit the Reid Village Water District's responses and, accordingly, we express no opinion on them.

This report is intended solely for the information and use of the audit committee, management, others within the organization and Federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

John T. Lane & Associates, LLC

April 26, 2012

Reid Village Water District
 COMPARATIVE STATEMENT OF REVENUES AND EXPENSES
 for the years ended December 31, 2010 and 2011

	2010	2011
Revenues		
User fees	\$ 418,001	\$ 438,317
Other water revenue	29,680	15,856
Total Revenues	447,681	454,173
Expenses		
Water purchased	140,562	148,062
Vehicle expense	9,454	14,023
Rent	6,000	6,000
Postage	4,244	3,709
Salaries	88,851	120,661
Office expense	28,847	32,635
Insurance	8,165	9,542
Water samples	1,375	1,600
Taxes and benefits	40,971	41,568
Maintenance	26,995	26,338
Miscellaneous	16,973	7,726
Contract labor	884	-
Bad debt expense	1,964	3,848
Depreciation	34,863	35,267
Total Operating Expenses	410,148	450,979
Operating Income (Loss)	37,533	3,194
Nonoperating Revenues (Expenses)		
Tap fees	5,180	2,510
Interest income	931	919
Interest expense	(34,352)	(33,825)
Net Nonoperating Revenues (Expenses)	(28,241)	(30,396)
Net Income (Loss)	\$ 9,292	\$ (27,202)

REID VILLAGE WATER DISTRICT
Mt. Sterling, Kentucky
Schedule of Findings and Responses
December 31, 2011

Prior Findings

10-01, 10-02, 10-03 are repeated as 11-01, 11-02 and 11-03.

Current Findings

11-01 Lack of Segregation of Duties

Condition: The District has an inadequate segregation of duties within its internal control process.

Criteria: All governmental entities should design their internal control to provide an adequate segregation of duties.

Cause: The District does not have sufficient employees to adequately design its internal control.

Recommendation: The District should continue to design and implement its internal control policies to provide the maximum segregation of duties possible.

Response: The District has hired a part time employee for the office. She works 16-20 hours a week and in addition covers for the office managers during vacation or sick time off. This has provided us with the ability to segregate duties as recommended. As her training progresses she will be responsible for additional duties to help implement segregation of duties. She handles making deposits and customer service but does not adjust customer's accounts. Also we have hired a field supervisor who oversees and delegates the duties of our employees outside the office. He approves and signs time sheets for those employees. He also transports our starting cash and deposits to the bank in locked bags.

11-02 Lack of Understanding of GAAP

Condition: The District prepares its financial statements on the cash basis and lacks an understanding of generally accepted accounting principles.

Criteria: To prepare financial statements the entity's personnel should understand GAAP.

Cause: The entity's accounting personnel does not possess the necessary background in accounting.

Recommendation: The District cannot afford to hire personnel with adequate training.

Response: The District has purchased and is currently using Quick Books.(beginning January 2011) The office manager is currently working with a skilled Bookkeeper (also proficient in Quick Books) to better understand the accounting side of the business. We will continue to seek the assistance of a CPA to prepare financial statements.

11-03 Budget Process

Condition: The District's budget is prepared from actual results that are one year old.

Criteria: A budget should be prepared from information from the previous year's actual results to the extent possible.

Cause: Unknown.

Recommendation: The District should prepare monthly reports of cash receipts and disbursements compared to budgeted amounts, these statements should be presented to the board.

Response: With Quick Books in use, we can and will prepare monthly cash flow statements that will be presented to the board, usually quarterly, unless special meeting is called between quarterly meetings. It is our goal to eventually prepare our own budget from our previous years actual results. We intend to seek outside training on the procedures of preparing our budget. Until we feel confident in our abilities, we will seek professional help from our CPA.