

Monroe County Water District

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June 10, 2013

Public Service Commission
211 Sower Blvd.
P.O. Box 615
Frankfort, Kentucky 40602-0615

RE: 2012 annual audit report

To Whom It May Concern:

Enclosed you will find a copy of the Monroe County Water District annual audit. If you have any questions, please contact me at the office.

Sincerely,



Jana Dubree, Office Manager
Monroe County Water District

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COMMISSION**

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COMMISSION

Monroe County Water District

Financial Statements

December 31, 2012 and 2011

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Table of Contents

	<u>Page</u>
Independent Auditor's Report	1 - 3
Management's Discussion and Analysis	4 - 7
Statements of Net Assets	8 - 9
Statements of Revenues, Expenses and Changes in Net Assets	10
Statements of Cash Flows	11
Notes to Financial Statements	12 - 18
Supplemental Information	
Statement of Revenues, Expenditures and Changes in Equity – Budget and Actual	19
Schedule of Expenditures of Federal Awards	20
Notes to the Schedule of Expenditures of Federal Awards	21
Schedule of Findings and Questioned Costs	22
Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with <i>Government Auditing Standards</i>	23 – 24
Independent Auditor's Report on Compliance for Each Major Program and on Internal Control Over Compliance Required by OMB Circular A-133	25 - 26

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INDEPENDENT AUDITOR'S REPORT

Monroe County Water District
Tompkinsville, Kentucky

Report on the Financial Statements

We have audited the accompanying financial statements of Monroe County Water District, as of and for the years ended December 31, 2012 and 2011, and the related notes to the financial statements, which collectively comprise Monroe County Water District's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express opinions on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement on the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

Opinions

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

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and budgetary comparison information on pages 4 through 7 and page 19 be presented to supplement the basic financial statements. Such 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. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise Monroe County Water District's basic financial statements. The schedule of expenditures of federal awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is also not a required part of the basic financial statements.

The schedule of expenditures of federal awards is the responsibility of management and was derived from and relate directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America.

In our opinion, the schedule of expenditures of federal awards are fairly stated in all material respects in relation to the basic financial statements as a whole.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated May 1, 2013, on our consideration of the Monroe County Water District's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering Monroe County Water District's internal control over financial reporting and compliance.

Campbell, Myers & Ratledge, PLLC

Certified Public Accountants
Glasgow, Kentucky

May 1, 2013

MANAGEMENT'S DISCUSSION AND ANALYSIS

As management of the Monroe County Water District, we offer readers of the District's financial statements this narrative overview of the financial activities of the District for the fiscal years ending December 31, 2012 and 2011. We encourage readers to consider the information presented here in conjunction with the District's financial statements and notes to the basic financial statements to enhance their understanding of the District's financial performance.

Financial Highlights

For the year ending December 31, 2012, total operating and non-operating revenues (including capital contributions) totaled \$2,570,451. This represents a 32% increase in revenues from the prior year. This change was due to an increase of water rates and of grant proceeds received in 2012.

Total operating expenses amounted to \$1,395,128, an increase of \$382 from the prior year of \$1,394,746. This increase was primarily the result of an increase in depreciation expense and decrease in salary expense.

Total assets increased by \$1,138,357, and total liabilities increased by \$21,068. These changes resulted in an increase in net assets of \$1,117,289.

Overview of the Financial Statements

This report consists of this Management's Discussion and Analysis report, the Independent Auditor's Report, Financial Statements and Supplementary Information. The Financial Statements include notes which explain in detail some of the information included in the Financial Statements.

Required Financial Statements

The financial statements of Monroe County Water District report information of Monroe County Water District using accounting methods similar to those used by private sector companies. These statements offer short and long-term financial information about its activities. The Statement of Net Assets includes all of Monroe County Water District's assets and liabilities and provides information about the nature and amounts of investments in resources (assets) and the obligations to Monroe County Water District creditors (liabilities). It also provides the basis for evaluation of the capital structure of Monroe County Water District and assessing the liquidity and financial flexibility of Monroe County Water District.

All of the current year's revenues and expenses are accounted for in the Statement of Revenues, Expenses and Changes in Net Assets. This statement measures the success of Monroe County Water District's operations over the past year and can be used to determine whether Monroe County Water District has successfully recovered all its costs through its user fees and other charges, profitability and credit worthiness.

The final required financial statement is the Statement of Cash Flows. The statement reports cash receipts, cash payments, and net changes in cash resulting from operations, investing and financing activities and provides answers to such questions as where did cash come from, what was cash used for, and what was the change in the cash balance during the reporting period.

**Monroe County Water District
Summary of Net Assets
December 31, 2012 and 2011**

	<u>2012</u>	<u>2011</u>
Assets		
Total Current Assets	\$ 1,177,047	\$ 873,438
Total Restricted Assets	552,045	583,588
Net Capital Assets	<u>9,783,424</u>	<u>8,917,133</u>
Total Assets	<u>\$ 11,512,516</u>	<u>\$ 10,374,159</u>
Liabilities		
Total Current Liabilities	\$ 319,620	\$ 214,516
Total Liabilities Payable from Restricted Assets	206,681	203,717
Total Long-term Liabilities	<u>2,698,000</u>	<u>2,785,000</u>
Total Liabilities	<u>\$ 3,224,301</u>	<u>\$ 3,203,233</u>
Net Assets		
Invested in capital assets, net of related debt	\$ 6,989,127	\$ 6,038,336
Restricted for equipment replacement	344,031	341,682
Restricted for debt retirement	87,404	121,774
Restricted - other	929	915
Unrestricted	<u>866,724</u>	<u>668,219</u>
Total Net Assets	<u>\$ 8,288,215</u>	<u>\$ 7,170,926</u>

The largest portion (85%) of the District's net assets reflects its investment in capital assets, less any related debt used to acquire those assets still outstanding. This represents 1% percent increase from the prior year.

Restricted net assets (5%) represent resources that are subject to external restrictions on how they may be used.

The balance (10%) of unrestricted net assets may be used to meet the District's ongoing obligations to citizens, consumers and creditors.

**Monroe County Water District
Summary of Changes in Net Assets
For the Year Ended December 31, 2012 and 2011**

Total operating revenues	\$ 1,453,162	\$ 1,304,543
Total operating expenses	<u>1,395,128</u>	<u>1,394,746</u>
Operating Income	\$ 58,034	\$ (90,203)
Total non-operating revenue (expenses)	<u>(124,730)</u>	<u>(128,347)</u>
Income before capital contributions	\$ (66,696)	\$ (218,550)
Capital contributions	<u>1,183,985</u>	<u>859,725</u>
Increase in net assets	\$ 1,117,289	\$ 641,175
Beginning of year	<u>7,170,926</u>	<u>6,529,751</u>
End of year	<u>\$ 8,288,215</u>	<u>\$ 7,170,926</u>

Net assets increased by \$1,117,289, from the prior year.

Capital Asset Changes

At December 31, 2012, the District had invested \$9,783,424 in capital assets net of accumulated depreciation. This amount represents a net increase of \$866,291 or 10% more than the previous year. This increase is the result of continuing construction projects being implemented in 2012 by the District.

The Monroe County Water District completed several projects including 2.5 miles of water line extensions during the year of 2012. There were 41 new water connections set for service during the year of 2012. The Monroe County Water District has a very active meter testing program, having tested 504 meters during the year of 2012.

Monroe County Water District has worked diligently on the Monroe – Tompkinsville Regional Water Treatment Plant Project since 2006. The total project cost is \$16,800,000 which consists of the treatment plant, intake, transmission lines, storage tanks, land acquisition, engineering and administration. Preliminary design work was completed in 2012. There is hope of acquiring the location site in 2013 for the treatment plant and intake. The following three contracts were completed and in operation in 2012; Contract IIA - transmission lines, Contract IIIA - a 350,000 gallon storage tank (which replaced the current storage tank at Persimmon), and Contract IID - a new Pump Station on Capp Harlan Road. Funding applications have been filed. Grant funding has been appropriated from Kentucky General Assembly HB 380 (\$150,000 for design and \$1,200,000 for construction) and HB 608 (\$1,250,000 for construction). An Environmental Protection Agency Special Appropriations Projects grant has been designated for our project (\$1,350,000 for construction). Monroe County Water District was placed on the top priority list for the Kentucky Drinking Water State Revolving Fund (\$8,000,000 loan) for this project. Monroe County Water District has been fortunate to have the continued support from the Kentucky Legislators and the Kentucky Division of Water to help assist with moving our project forward. Monroe, Metcalfe and Cumberland Counties all share the need for a more abundant source and a higher quality of raw water. Health issues and restricted water use were continuing concerns in 2011. This is a major project for Monroe County Water District, but the need for upgrading and maintenance projects are also anticipated to help improve the distribution system and to better serve our customers.

Budgetary Highlights

The Monroe County Water District adopts an annual operating budget after careful considerations of prior year and anticipated current year operations. The operating budget includes proposed expenses and the means to finance them. The District's operating budget remains in effect the entire year and is not revised. A budget comparison and analysis is presented on page 19 of this report.

Debt Administration

At December 31, 2012, the District had \$2,785,000 bonds outstanding, a decrease of \$84,500 from the prior year's balance of \$2,869,500. The District incurred \$132,051 in interest expense associated with long term debt, a decrease of \$4,077 due to the increase amount paid on the principle.

Request for Information

This financial report is designed to provide our customers and creditors with a general overview of Monroe County Water District's finances and to demonstrate Monroe County Water District's accountability for the funds it receives. If you have any questions about this report or need any additional information, please contact the Monroe County Water District at 205 Capp Harlan Road, Tompkinsville, Kentucky 42167, or by phone (270) 487-8131.

MONROE COUNTY WATER DISTRICT
Statements of Net Assets
December 31, 2012 and 2011

Assets	<u>2012</u>	<u>2011</u>
Current Assets		
Cash	\$ 743,173	\$ 566,263
Accounts receivable	291,435	160,871
Inventory	142,439	146,304
Total Current Assets	<u>1,177,047</u>	<u>873,438</u>
Non-current Assets		
Restricted Assets		
Cash - Depreciation fund	344,031	341,682
Cash - Bond and interest redemption fund	153,431	189,839
Cash - Meter Deposits	54,583	52,067
Total Restricted Assets	<u>552,045</u>	<u>583,588</u>
Capital Assets		
Land and land rights	126,842	126,842
Utility plant in service	11,893,919	10,252,031
Furniture and equipment	1,080,059	769,626
Construction in progress	869,481	1,602,573
Accumulated depreciation and amortization	<u>(4,186,877)</u>	<u>(3,833,939)</u>
Net Capital Assets	<u>9,783,424</u>	<u>8,917,133</u>
Total Non-current Assets	<u>10,335,469</u>	<u>9,500,721</u>
 Total Assets	 <u>\$ 11,512,516</u>	 <u>\$ 10,374,159</u>

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

MONROE COUNTY WATER DISTRICT
Statements of Net Assets
December 31, 2012 and 2011

Liabilities	<u>2012</u>	<u>2011</u>
Current Liabilities		
Accounts payable	\$ 63,368	\$ 61,599
Construction accounts payable	172,860	50,086
Accrued liabilities	<u>83,392</u>	<u>102,831</u>
Total Current Liabilities	<u>319,620</u>	<u>214,516</u>
Liabilities Payable from Restricted Assets		
Current maturities of long-term debt	87,000	84,500
Customer deposits	53,654	51,152
Accrued interest	<u>66,027</u>	<u>68,065</u>
Total Liabilities Payable from Restricted Assets	<u>206,681</u>	<u>203,717</u>
Long-term Liabilities		
Long-term debt, less current maturities	<u>2,698,000</u>	<u>2,785,000</u>
Total Long-term Liabilities	<u>2,698,000</u>	<u>2,785,000</u>
Total Liabilities	<u>3,224,301</u>	<u>3,203,233</u>
Net Assets		
Net Assets		
Invested in capital assets, net of related debt	6,989,127	6,038,336
Restricted for equipment replacement	344,031	341,682
Restricted for debt retirement	87,404	121,774
Restricted - other	929	915
Unrestricted	<u>866,724</u>	<u>668,219</u>
Total Net Assets	<u>\$ 8,288,215</u>	<u>\$ 7,170,926</u>

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

MONROE COUNTY WATER DISTRICT
Statements of Revenues, Expenses and Changes in Net Assets
For the Years Ended December 31, 2012 and 2011

	<u>2012</u>	<u>2011</u>
Operating revenues:		
Residential water sales	\$ 1,318,202	\$ 1,135,946
Commerical water sales	83,790	80,456
Penalty collections	30,330	25,925
Miscellaneous	20,840	62,216
Total operating revenues	<u>1,453,162</u>	<u>1,304,543</u>
Operating expenses:		
Water purchases	405,726	430,385
Utilities	58,977	57,615
Repairs and maintenance	39,497	16,915
Meter readers	40,846	40,453
Office expense	33,116	36,865
Transportation expenses	27,846	25,796
Insurance	24,477	24,752
Commissioners' fees	6,000	6,000
Employees' salaries and wages	274,079	304,379
Employees' pensions and benefits	78,593	92,517
Depreciation	371,549	319,639
PSC tax assessment	2,288	1,885
Meter deposit interest expense	379	517
Bad debt expense	4,516	4,875
Professional fees	9,428	12,515
Miscellaneous	17,811	19,638
Total operating expenses	<u>1,395,128</u>	<u>1,394,746</u>
Operating income	<u>58,034</u>	<u>(90,203)</u>
Non-operating revenue (expenses):		
Interest income	7,321	7,781
Interest expense on bonds	<u>(132,051)</u>	<u>(136,128)</u>
Total non-operating revenue (expenses)	<u>(124,730)</u>	<u>(128,347)</u>
Income/(loss) before capital contributions	<u>(66,696)</u>	<u>(218,550)</u>
Capital contributions		
Grant proceeds	1,143,669	826,991
Tap fees	40,316	32,734
Total capital contributions	<u>1,183,985</u>	<u>859,725</u>
Increase in net assets	1,117,289	641,175
Net assets:		
Beginning of year	<u>7,170,926</u>	<u>6,529,751</u>
End of year	<u>\$ 8,288,215</u>	<u>\$ 7,170,926</u>

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

MONROE COUNTY WATER DISTRICT
Statements of Cash Flows
For the Years Ended December 31, 2012 and 2011

	<u>2012</u>	<u>2011</u>
Cash flows from operating activities:		
Cash receipts from customers	\$ 1,401,992	\$ 1,216,402
Cash payments to suppliers for goods and services	(591,984)	(524,288)
Cash payments to employees for services	(399,518)	(443,349)
Net cash provided (used) by operating activities	<u>410,490</u>	<u>248,765</u>
Cash flows from capital and related financing activities:		
Principal paid on long-term debt	(84,500)	(79,000)
Interest paid on long-term debt	(137,876)	(139,915)
Additions to capital assets	(1,234,053)	(917,447)
Capital contributions	1,183,985	859,725
Net cash provided (used) in financing activities	<u>(272,444)</u>	<u>(276,637)</u>
Cash flows from investing activities:		
Interest income	7,321	7,781
Net cash provided by (used) in investing activities	<u>7,321</u>	<u>7,781</u>
Net increase (decrease) in cash and cash equivalents	145,367	(20,091)
Cash and cash equivalents, beginning of year	<u>1,149,851</u>	<u>1,169,942</u>
Cash and cash equivalents, end of year	\$ <u>1,295,218</u>	\$ <u>1,149,851</u>
Reconciliation of operating income to		
net cash provided by operating activities:		
Operating income	\$ 58,034	\$ (90,203)
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation and amortization	371,549	319,639
Changes in assets and liabilities:		
(Increase) decrease in accounts receivable	(130,564)	(26,653)
(Increase) decrease in inventory	3,865	(9,182)
Increase (decrease) in accounts payable	124,543	24,015
Increase (decrease) in customer deposits	2,502	3,180
Increase (decrease) in accrued expenses	(19,439)	27,969
Net cash provided (used) by operating activities	<u>\$ 410,490</u>	<u>\$ 248,765</u>

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

MONROE COUNTY WATER DISTRICT
Notes to Financial Statements
December 31, 2012 and 2011

Note 1 – Description of Entity and Summary of Significant Accounting Policies

Organization

The Monroe County Water District was organized in 1975 under KRS 74.010 to provide water service to the residents of Monroe County, Kentucky. The District's commissioners are appointed by the Monroe County Judge-Executive.

The District grants credit to customers, substantially all of whom are local residents and commercial businesses in Monroe County, Kentucky.

Measurement Focus and Basis of Accounting

The term *measurement focus* is used to denote what is being measured and reported in the District's financial statements. The District is accounted for on the flow of economic resources measurement focus. Under this measurement focus, all assets and all liabilities associated with the operations are included in the Statement of Net Assets.

The term *basis of accounting* is used to determine when a transaction or event is recognized on the District's financial statements. The District uses the full accrual basis of accounting. Under this basis, revenues are recorded when earned and expenses are recorded when incurred, even though actual payment or receipt may not occur until after the period ends.

Financial Statement Presentation

The District has elected under GASB Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Activities That Use Proprietary Fund Accounting*, to apply all applicable GASB pronouncements as well as any applicable pronouncements of the Financial Accounting Standards Board, the Accounting Principles Board, or any Accounting Research Bulletins issued on or before November 30, 1989, unless these pronouncements conflict with or contradict GASB pronouncements.

The accounts of the District are organized on the basis of a proprietary fund type, specifically an enterprise fund. The activities of this fund are accounted for with a separate set of self-balancing accounts that comprise the District's assets, liabilities, net assets, revenues and expenses. Enterprise Funds account for activities; (i) that are financed with debt that is secured solely by a pledge of the net revenues from fees and charges of the activity, (ii) that are required by laws or regulations that the activity's costs of providing services, including capital costs (such as depreciation or debt service), be recovered with fees and charges, rather than with taxes or similar revenues, or (iii) that the pricing policies of the activity establish fees and charges designed to recover its costs, including capital costs (such as depreciation or debt service).

On January 1, 2004, the District adopted the provisions of Governmental Accounting Standards Board (GASB) No. 34 "*Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments.*" GASB 34 established standards for external financial reporting for all state and local governmental entities which includes a statement of net assets, a statement of activities and changes in net assets and a statement of cash flows. It requires the classification of net assets into three components: (i) invested in capital assets, net of related debt, (ii) restricted, and (iii) unrestricted.

MONROE COUNTY WATER DISTRICT
Notes to Financial Statements
December 31, 2012 and 2011

Note 1 – Description of Entity and Summary of Significant Accounting Policies, Continued

These classifications are defined as follows:

- *Invested in capital assets, net of related debt* - This component of net assets consists of capital assets, net of accumulated depreciation and reduced by the outstanding balances of any bonds, mortgages, notes or other borrowings that are attributable to the acquisition, construction or improvement of those assets.
- *Restricted* - This component of net assets consists of constraints imposed by creditors (such as through debt covenants), grantors, contributors, or laws or regulations of other governments or constraints imposed by law through constitutional provisions or enabling legislation.
- *Unrestricted net assets* - This component of net assets consists of net assets that do not meet the definition of "restricted" or "invested in capital assets, net of related debt."

Use of Restricted Funds

When both restricted and unrestricted resources are available for use, it is the Company's policy to use restricted resources first, then unrestricted resources as they are needed.

Receivables

The District uses the direct write-off method to account for bad debts. No allowance for bad debts has been provided, as no material write-offs are expected for receivables as of December 31, 2012. The direct write-off method does not significantly depart from generally accepted accounting principles.

Capital Assets

The utility plant in service is stated at cost. The cost of additions to the utility plant and major replacements of retired units of property is capitalized. Cost includes direct labor, outside services, materials and transportation, employee fringe benefits, overhead, and interest on funds borrowed to finance construction. The cost and accumulated depreciation of property sold or retired is deducted from capital assets, and any profit or loss resulting from the disposal is credited or charged in the nonoperating section of the statement of revenues, expenses and changes in net assets. The cost of current repairs, maintenance, and minor replacements is charged to expense as incurred. Depreciation has been provided over estimated useful lives of the assets using the straight-line method. Depreciation expense for the year ending December 31, 2012 and 2011 was \$371,549 and \$319,639, respectively.

The estimated useful lives of capital assets are as follows:

Utility plant	20-63 years
Equipment	7-13 years
Other	23 years

Cash and Investments

The District considers all highly liquid investments with maturities of three months or less when purchased to be cash equivalents. Investments are reported at fair market value.

Long-Term Obligations

Long-term debt and other obligations are reported as liabilities on the Statement of Net Assets. Bond premiums and discounts are deferred and amortized over the life of the bonds.

MONROE COUNTY WATER DISTRICT
Notes to Financial Statements
December 31, 2012 and 2011

Note 1 – Description of Entity and Summary of Significant Accounting Policies, Continued

Operating Revenues and Expenses

Operating revenues and expenses consists of those revenues that result from the ongoing principal operations of the District. Operating revenues consist primarily of charges for services. Nonoperating revenues and expenses consist of those revenues and expenses that are related to financing and investing type of activities and result from nonexchange transactions.

Capital Contributions

Transmission and distribution system assets contributed to the District by installers are capitalized at the installers' costs and recorded as capital contributions when received. Also included in capital contributions are various grants received for infrastructure and payments received from customers for tap fees.

Income Taxes

The District is exempt from federal and state income taxes.

Extraordinary and Special Items

Extraordinary items are transactions or other events that are both unusual in nature and infrequent in occurrence. Special items are significant transactions or other events within the control of management that are either unusual in nature or infrequent in occurrence. If such items exist during the reporting period, they are reported separately in the statement of revenues, expenses and changes in net assets.

Bond and Interest Redemption Fund

The ordinances authorizing the bond issues require monthly deposits of one-twelfth of the annual bond principal requirement and one-sixth of the semi-annual interest requirement. For the year ending December 31, 2012, the District had complied with this requirement.

Inventory

Inventory is valued at cost using the first in, first out method. Inventory in the Proprietary Funds consists of expendable supplies held for future consumption or capitalization. The cost is recorded as an expense or capital addition as inventory items are consumed.

Use of Estimates

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.

Compensated Absences

Accumulated unpaid vacation and sick pay amounts are accrued when benefits vest to employees and the unpaid liability is reflected in accrued liabilities.

Depreciation Fund

The ordinances authorizing the various bond issues of the District require monthly transfers into a depreciation fund until the maximum requirement of \$209,520 is reached. These funds can be used for capital improvements, expansions and extraordinary repairs. For the years ended December 31, 2012 and 2011, the District had a balance in excess of the required amount in the depreciation fund.

MONROE COUNTY WATER DISTRICT
Notes to Financial Statements
December 31, 2012 and 2011

Note 2 – Capital Assets

Capital asset activity for the year ended December 31, 2012 and 2011, was as follows:

	Balance 01/01/12	Additions	Deletions	Balance 12/31/12
<i>Capital Assets not being depreciated</i>				
Land & Rights	\$ 126,842	\$ -	\$ -	\$ 126,842
Construction In Progress	1,602,573	1,174,233	(1,907,324)	869,482
Total Non-Depreciable Capital Assets	<u>1,729,415</u>	<u>1,174,233</u>	<u>(1,907,324)</u>	<u>996,324</u>
<i>Capital Assets being depreciated</i>				
Structures and Improvements	420,126	7,652	-	427,778
Pumping Equipment	211,204	280,788	-	491,992
Distribution Reservoirs	1,293,293	706,432	-	1,999,725
Transmission and Distribution Mains	7,677,926	894,387	-	8,572,313
Services	120,774	-	-	120,774
Meters and Installations	739,912	33,416	-	773,328
Other Plant	32,370	-	-	32,370
Furniture and Equipment	98,249	-	-	98,249
Transportation Equipment	181,758	25,578	(18,611)	188,725
Power Operated Equipment	246,045	22,678	-	268,723
Total Depreciable Capital Assets	<u>11,021,657</u>	<u>1,970,931</u>	<u>(18,611)</u>	<u>12,973,977</u>
Less: Accumulated Depreciation and Amortization	<u>3,833,939</u>	<u>371,549</u>	<u>(18,611)</u>	<u>4,186,877</u>
Total Net Capital Assets	<u>\$ 8,917,133</u>			<u>\$ 9,783,424</u>
	Balance 01/01/11	Additions	Deletions	Balance 12/31/11
<i>Capital Assets not being depreciated</i>				
Land & Rights	\$ 126,842	\$ -	\$ -	\$ 126,842
Construction In Progress	850,010	752,563	-	1,602,573
Total Non-Depreciable Capital Assets	<u>976,852</u>	<u>752,563</u>	<u>-</u>	<u>1,729,415</u>
<i>Capital Assets being depreciated</i>				
Structures and Improvements	415,304	4,822	-	420,126
Pumping Equipment	208,835	2,369	-	211,204
Distribution Reservoirs	1,292,754	539	-	1,293,293
Transmission and Distribution Mains	7,624,519	53,407	-	7,677,926
Services	120,774	-	-	120,774
Meters and Installations	710,836	29,076	-	739,912
Other Plant	32,370	-	-	32,370
Furniture and Equipment	85,363	12,886	-	98,249
Transportation Equipment	181,758	-	-	181,758
Power Operated Equipment	184,260	61,785	-	246,045
Total Depreciable Capital Assets	<u>10,856,773</u>	<u>164,884</u>	<u>-</u>	<u>11,021,657</u>
Less: Accumulated Depreciation and Amortization	<u>3,514,300</u>	<u>319,639</u>	<u>-</u>	<u>3,833,939</u>
Total Net Capital Assets	<u>\$ 8,319,325</u>			<u>\$ 8,917,133</u>

MONROE COUNTY WATER DISTRICT
Notes to Financial Statements
December 31, 2012 and 2011

Note 3 – Long-Term Debt

Long-term debt consists of the following at December 31, 2012 and 2011:

	<u>2012</u>	<u>2011</u>
Series 1978 Water Revenue Bonds issued through the Rural Development of the USDA in the amount of \$277,000; due in annual installments on January 1 ranging from \$1,000 to \$15,000 through January 2018; interest rate of 5% due semi-annually on January 1 and July 1.	\$ 80,000	\$ 92,000
Series 1987 Water Revenue Bonds issued through the Rural Development of the USDA in the amount of \$391,000; due in annual installments on January 1 ranging from \$4,000 to \$21,000 through January 2027; interest rate of 5% due semi-annually on January 1 and July 1.	239,000	250,000
Series 1990 Water Revenue Bonds issued through the Rural Development of the USDA in the amount of \$811,000; due in annual installments on January 1 ranging from \$8,000 to \$45,000 through January 2031; interest rate of 5% due semi-annually on January 1 and July 1.	560,000	579,000
Series 1992 Water Revenue Bonds issued through the Rural Development of the USDA in the amount of \$490,000; due in annual installments on January 1 ranging from \$4,500 to \$27,000 through January 2031; interest rate of 5% due semi-annually on January 1 and July 1.	350,500	361,500
Series 1994 Water Revenue Bonds issued through the Rural Development of the USDA in the amount of \$570,000; due in annual installments on January 1 ranging from \$5,000 to \$32,000 through January 2033; interest rate of 4.5% due semi-annually on January 1 and July 1.	430,000	442,000
Series 1998 Water Revenue Bonds issued through the Rural Development of the USDA in the amount of \$500,000; due in annual installments on January 1 ranging from \$5,000 to \$26,500 through January 2038; interest rate of 4.5% due semi-annually on January 1 and July 1.	420,500	429,000
Series 1999 Water Revenue Bonds issued through the Rural Development of the USDA in the amount of \$270,000; due in annual installments on January 1 ranging from \$2,500 to \$15,500 through January 2038; interest rate of 4.75% due semi-annually on January 1 and July 1.	231,000	235,000
Series 2003 Water Revenue Bonds issued through the Rural Development of the USDA in the amount of \$517,000; due in annual installments on January 1 ranging from \$5,500 to \$27,500 through January 2043; interest rate of 4.5% due semi-annually on January 1 and July 1.	<u>474,000</u>	<u>481,000</u>
Total debt	<u>\$ 2,785,000</u>	<u>\$ 2,869,500</u>

MONROE COUNTY WATER DISTRICT
Notes to Financial Statements
December 31, 2012 and 2011

Note 3 – Long-Term Debt, Continued

Principal and interest maturities of long-term debt are as follows:

	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2013	\$ 87,000	\$ 132,050	\$ 219,050
2014	91,500	127,851	219,351
2015	95,000	123,438	218,438
2016	101,000	118,853	219,853
2017-21	534,000	518,740	1,052,740
2022-26	639,500	382,855	1,022,355
2027-31	656,500	221,580	878,080
2032-36	330,000	98,783	428,783
2037-41	197,000	33,706	230,706
2042-43	53,500	3,645	57,145
	<u>\$ 2,785,000</u>	<u>\$ 1,761,501</u>	<u>\$ 4,546,501</u>

Long-term debt activities for the year ended December 31, 2012 and 2011 are as follows:

	<u>Balance</u> <u>01/01/12</u>	<u>Additions</u>	<u>Debt Payments</u> <u>and Reductions</u>	<u>Balance</u> <u>12/31/12</u>	<u>Amount Due</u> <u>within One Year</u>
Series 1978	\$ 92,000	\$ -	\$ (12,000)	\$ 80,000	\$ 12,000
Series 1987	250,000	-	(11,000)	239,000	11,000
Series 1990	579,000	-	(19,000)	560,000	20,000
Series 1992	361,500	-	(11,000)	350,500	11,500
Series 1994	442,000	-	(12,000)	430,000	12,000
Series 1998	429,000	-	(8,500)	420,500	8,500
Series 1999	235,000	-	(4,000)	231,000	4,500
Series 2003	481,000	-	(7,000)	474,000	7,500
	<u>\$ 2,869,500</u>	<u>\$ -</u>	<u>\$ (84,500)</u>	<u>\$ 2,785,000</u>	<u>\$ 87,000</u>

	<u>Balance</u> <u>01/01/11</u>	<u>Additions</u>	<u>Debt Payments</u> <u>and Reductions</u>	<u>Balance</u> <u>12/31/11</u>	<u>Amount Due</u> <u>within One Year</u>
Series 1978	\$ 103,000	\$ -	\$ (11,000)	\$ 92,000	\$ 12,000
Series 1987	260,000	-	(10,000)	250,000	11,000
Series 1990	597,000	-	(18,000)	579,000	19,000
Series 1992	372,000	-	(10,500)	361,500	11,000
Series 1994	453,000	-	(11,000)	442,000	12,000
Series 1998	437,000	-	(8,000)	429,000	8,500
Series 1999	239,000	-	(4,000)	235,000	4,000
Series 2003	487,500	-	(6,500)	481,000	7,000
	<u>\$ 2,948,500</u>	<u>\$ -</u>	<u>\$ (79,000)</u>	<u>\$ 2,869,500</u>	<u>\$ 84,500</u>

MONROE COUNTY WATER DISTRICT
Notes to Financial Statements
December 31, 2012 and 2011

Note 3 – Long-Term Debt, Concluded

Arbitrage

The Tax Reform Act of 1986 instituted certain arbitrage restrictions with respect to the issuance of tax-exempt bonds after August 31, 1986. Arbitrage regulations deal with the investment of all tax-exempt bond proceeds at an interest yield greater than the interest yield paid to bondholders. Generally, all interest paid to bondholders can be retroactively rendered taxable if applicable rebates are not reported and paid to the Internal Revenue Service (IRS) at least every five years. During the current year, the District performed calculations of excess investment earnings on various bonds and at December 31, 2012 does not expect to incur a liability.

Note 4 – Cash and Investments

The carrying amount of the District's cash deposits was \$1,295,218 and \$1,149,851 for the years ending December 31, 2012 and 2011, respectively and the bank balances all at one institution, were \$1,322,403 and \$1,158,517. The difference between book and bank balances primarily represents checks that have been issued, but have not cleared the bank. The District's deposits included five certificates of deposit totaling approximately \$250,000 for 2012 and 2011 that matured annually. All were with the same financial institution at rates between .79% and 1.30% for the year ending December 31, 2012 and 2011, respectively. All of the District's deposits were either insured by FDIC or by collateral pledged by South Central Bank of Monroe County.

Note 5 – Pension Plan

The District provided a defined contribution plan, as of January 1, 2006, to its employees, who meet certain age and length of service requirements set forth by the Board of Commissioners. The plan is a deferred compensation plan as defined by the IRC 457(b). The District contributes 8% of covered payroll and each employee contributes 4% of their wages. For the years ended December 31, 2012 and 2011, employer contributions were \$22,790 and \$23,162 respectively and employee contributions were \$11,395 and \$11,581, respectively. Voluntary contributions were \$2,080 in 2012 and \$2,080 in 2011. Covered payroll was approximately \$274,000 and \$304,000 for years 2012 and 2011, respectively.

Note 6 – Commitments

The District has plans for a new regional water treatment facility to supply Monroe county and other water districts. The total cost of the project is projected to be \$16,800,000. The District has secured grant funds from KIA and EPA for approximately \$3,740,000. The District has also secured an additional grant and loan funds of \$12,808,000. As of December 31, 2012 the District has received \$2,614,629 of the above grant funds. Construction in Process balance of \$869,482 relates to engineering fees associated with the design of WTP.

Note 7- Subsequent Events

Management has evaluated subsequent events through May 1, 2013, the date which the financial statements were available to be issued.

Supplemental Information

MONROE COUNTY WATER DISTRICT
Statement of Revenues, Expenditures and
Change in Equity – Budget and Actual
For the Year Ended December 31, 2012

	Original and Final Budget	Actual	Variance Favorable (Unfavorable)
Operating revenues:			
Water sales	\$ 1,285,333	\$ 1,401,992	\$ 116,659
Penalties and other	<u>68,437</u>	<u>51,170</u>	<u>(17,267)</u>
Total operating revenues	<u>1,353,770</u>	<u>1,453,162</u>	<u>99,392</u>
Operating expenses:			
Water purchases	361,093	405,726	(44,633)
Utilities	51,642	58,977	(7,335)
Materials	59,158	39,497	19,661
Contractual	57,598	40,846	16,752
Insurance	48,856	24,477	24,379
Salaries and benefits	383,400	358,672	24,728
Depreciation	319,000	371,549	(52,549)
Other	<u>55,655</u>	<u>95,384</u>	<u>(39,729)</u>
Total operating expenses	<u>1,336,402</u>	<u>1,395,128</u>	<u>(58,726)</u>
Operating income	<u>17,368</u>	<u>58,034</u>	<u>40,666</u>
Non-operating revenue (expenses):			
Interest income and other	8,000	7,321	(679)
Interest expense on bonds	<u>(134,560)</u>	<u>(132,051)</u>	<u>2,509</u>
Total non-operating revenue (expenses)	<u>(126,560)</u>	<u>(124,730)</u>	<u>1,830</u>
Income before capital contributions	<u>(109,192)</u>	<u>(66,696)</u>	<u>42,496</u>
Capital contributions			
Grant proceeds	664,800	1,143,669	478,869
Tap fees	<u>33,000</u>	<u>40,316</u>	<u>7,316</u>
Total capital contributions	<u>697,800</u>	<u>1,183,985</u>	<u>486,185</u>
Increase/(Decrease) in net assets	<u>\$ 588,608</u>	<u>\$ 1,117,289</u>	<u>\$ 528,681</u>

MONROE COUNTY WATER DISTRICT
Schedule of Expenditures of Federal Awards
For the Year Ended December 31, 2012

<u>Federal Grantor/Pass-Through Grantor/Program Title</u>	<u>Federal CFDA Number</u>	<u>Pass-Through Grantor's Number</u>	<u>Federal Expenditures</u>
<u>U.S. Environmental Protection Agency:</u>			
Direct Programs			
Congressionally Mandated Projects	66.202	XP-95403510	\$ 537,615
Total Other Programs			<u>537,615</u>
Total Federal Assistance			<u>\$ 537,615</u>

MONROE COUNTY WATER DISTRICT
Notes to the Schedule of Expenditures of Federal Awards
For the Year Ended December 31, 2012

1. Basis of Presentation:

The accompanying schedule of expenditures of federal awards includes the federal grant activity of Monroe County Water District and is presented on the accrual basis of accounting. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations. Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of, the basic financial statements.

**MONROE COUNTY WATER DISTRICT
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
For the Year Ended December 31, 2012**

I. SUMMARY OF AUDITOR'S RESULTS

Financial Statements

Type of auditor's report issued (unqualified):

Internal control over financial reporting:

- Material weakness(es) identified? Yes No
- Significant deficiencies identified that are not considered to be material weaknesses? Yes None Reported

Noncompliance material to financial statements noted?

Yes No

Federal Awards

Internal control over major programs:

- Material weakness(es) identified? Yes No
- Significant deficiencies identified that are not considered to be material weaknesses? Yes None Reported

Type of auditor's report issued on compliance for major programs: Unqualified

Any audit findings disclosed that are required to be reported in accordance with section 510(a) of Circular A-133?

Yes No

Identification of major programs:

CFDA Number(s)

Name of Federal Program or Cluster

66.202

U. S. Environmental Protection Agency
Congressionally Mandated Projects

Dollar threshold used to distinguish Between type A and type B programs:

\$300,000

Auditee qualified as low-risk auditee?

Yes No.

II. FINANCIAL STATEMENTS FINDINGS
NONE REPORTED

III. FEDERAL AWARD FINDINGS AND QUESTIONED COSTS
NONE REPORTED

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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

Monroe County Water District
Tompkinsville, 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 Monroe County Water District, as of and for the years ended December 31, 2012 and 2011, and the related notes to the financial statements, which collectively comprise Monroe County Water District's basic financial statements, and have issued our report thereon dated May 1, 2013.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered Monroe County Water District'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 opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of Monroe County Water District's internal control. Accordingly, we do not express an opinion on the effectiveness of Monroe County Water District'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 entity's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control 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 were considered 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 Monroe County Water District'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.

This report is intended solely for the information and use of management and others within the entity, and is not intended to be and should not be used by anyone other than these specified parties.

Campbell, Myers & Rutledge, PLLC

Certified Public Accountants
Glasgow, Kentucky

May 1, 2013

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INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE FOR EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE REQUIRED BY OMB CIRCULAR A-133

Monroe County Water District
Glasgow, Kentucky

Report on Compliance for Each Major Federal Program

We have audited Monroe County Water District's compliance with the types of compliance requirements described in the *OMB Circular A-133 Compliance Supplement* that could have a direct and material effect on each of Monroe County Water District's major federal programs for the year ended December 31, 2012. Monroe County Water District's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs.

Management's Responsibility

Management is responsible for compliance with the requirements of laws, regulations, contracts, and grants applicable to its federal programs.

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for each of Monroe County Water District's major federal programs based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about Monroe County Water District's compliance with those requirements and performing such other procedures as were considered necessary in the circumstances.

We believe that our audit provides a reasonable basis for our opinion on compliance for each major federal program. However, our audit does not provide a legal determination of Monroe County Water District's Compliance.

Opinion on Each Major Federal Program

In our opinion, Monroe County Water District, complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year end December 31, 2012.

Report on Internal Control Over Compliance

Management of Monroe County Water District, is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered Monroe County Water District's internal control over compliance with the types of requirements that could have a direct and material effect on each major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of Monroe County Water District's internal control over compliance.

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

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of OMB Circular A-133. Accordingly, this report is not suitable for any other purpose.

Campbell, Myers & Rattledge, PLLC

Certified Public Accountants
Glasgow, Kentucky

May 1, 2013