

**KNOTT COUNTY WATER AND SEWER DISTRICT  
Vicco, Kentucky**

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**FINANCIAL STATEMENTS  
December 31, 2016**

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## INDEPENDENT AUDITORS' REPORT

To the Board of Commissioners  
Knott County Water and Sewer District  
Vicco, Kentucky

### **Report on the Financial Statements**

We have audited the accompanying financial statements of the Knott County Water and Sewer District (the District) as of and for the year ended December 31, 2016, and the related notes to the financial statements, which collectively comprise the 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.

### ***Auditors' Responsibility***

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

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

### ***Opinion***

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Knott County Water and Sewer District, as of December 31, 2016, and the changes in financial position, and cash flows thereof for the year then 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 pension schedules on pages 16-17 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 and other auditors 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.

Management has omitted the Management Discussion and Analysis that accounting principles generally accepted in the United States of America requires to be presented to supplement the basic financial statements. Such missing information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. Our opinion on the basic financial statements is not affected by this missing information.

### *Other Information*

Our audit was conducted for the purpose of forming an opinion on the financial statements as a whole. The accompanying schedule of expenditures of federal awards, as required by Title 2 U.S. *Code of Federal Regulations* (CFR) Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* and the budgetary comparison schedule are presented for the purpose 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 schedule of expenditures of federal awards and the budgetary comparison schedule are fairly stated, in all material respects, in relation to the 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 June 19, 2017, on our consideration of the 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 the District's internal control over financial reporting and compliance.

**RFH**

RFH, PLLC  
Lexington, Kentucky  
June 19, 2017

**KNOTT COUNTY WATER AND SEWER DISTRICT**  
**STATEMENT OF NET POSITION**  
**December 31, 2016**

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**ASSETS**

Current assets	
Cash and cash equivalents	\$ 242,084
Customer accounts receivable, net	256,373
Grant receivable	<u>405,725</u>
Total current assets	<u>904,182</u>
Restricted assets	
Cash and cash equivalents	<u>463,603</u>
Capital assets	
Property, plant and equipment, net	48,604,922
Land	150,585
Construction-in-progress	<u>1,896,952</u>
Net capital assets	<u>50,652,459</u>
Total assets	<u>52,020,244</u>

**DEFERRED OUTFLOWS OF RESOURCES**

Deferred outflows - pension	<u>191,128</u>
Total assets and deferred outflows of resources	<u>\$ 52,211,372</u>

**LIABILITIES**

Current liabilities	
Accounts payable	\$ 49,805
Accrued compensation	21,091
Payroll liabilities	21,134
Accrued interest	1,545
Other current liabilities	501,507
Current portion of long-term debt	<u>63,788</u>
Total current liabilities	<u>658,870</u>
Noncurrent liabilities	
Net pension liability (CERS)	823,295
Notes payable	263,046
Bonds payable	<u>241,000</u>
Total long-term liabilities	<u>1,327,341</u>
Total liabilities	<u>1,986,211</u>

**DEFERRED INFLOWS OF RESOURCES**

Deferred inflows - pension	<u>45,630</u>
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**NET POSITION**

Net investment in capital assets	49,934,040
Restricted	463,603
Unrestricted	<u>(218,112)</u>
Total net position	<u>50,179,531</u>
Total liabilities, deferred inflows of resources and net position	<u>\$ 52,211,372</u>

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

**KNOTT COUNTY WATER AND SEWER DISTRICT**  
**STATEMENT OF REVENUES, EXPENSES AND CHANGES**  
**IN NET POSITION**  
for the year ended December 31, 2016

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<b>OPERATING INCOME</b>	
Water service	\$ 1,893,265
Sewer service	66,855
Penalties	20,238
Miscellaneous income	51,376
Reconnection and collection fees	<u>6,965</u>
Total operating income	<u>2,038,699</u>
<b>OPERATING EXPENSES</b>	
Salaries and fringe benefits	710,626
Commissioner fee	27,800
Office and advertising expense	1,182
Water consumption	65,705
Electricity	370,062
Telephone	10,453
Travel and training	4,088
Rents	13,707
Contractual fees	204,752
Vehicle expense	34,596
Operating supplies and maintenance	236,506
Licenses, permits, dues, and fees	7,080
Bad debt expense	73,862
Insurance and bonds	<u>54,308</u>
Total operating expense	<u>1,814,727</u>
Operating income before depreciation	223,972
Depreciation expense	<u>1,204,014</u>
<b>OPERATING (LOSS)</b>	(980,042)
Non-operating income (expenses)	
Interest income	740
Loss on disposal of asset	(459)
Interest expense	<u>(34,162)</u>
<b>(LOSS) BEFORE CAPITAL CONTRIBUTIONS</b>	(1,013,923)
Capital contributions	
Tap fees	24,300
Contributed capital	<u>9,352,552</u>
<b>CHANGE IN NET POSITION</b>	8,362,929
Net position, beginning of year, as restated	<u>41,816,602</u>
<b>NET POSITION, END OF YEAR</b>	<u>\$ 50,179,531</u>

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

**KNOTT COUNTY WATER AND SEWER DISTRICT**  
**STATEMENT OF CASH FLOWS**  
for the year ended December 31, 2016

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**CASH FLOWS FROM OPERATING ACTIVITIES**

Receipts from customers	\$ 2,285,534
Payment to suppliers	(1,131,368)
Payment for employee services and benefits	(697,167)
Other receipts	<u>51,376</u>
 Net cash provided by operating activities	 <u>508,375</u>

**CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES**

Purchase of capital assets	(4,650,535)
Contributed capital	4,673,473
Proceeds on sale of capital assets	2,918
Principal paid on capital debt	(63,739)
Interest paid on capital debt	<u>(32,617)</u>
 Net cash (used) by financing activities	 <u>(70,500)</u>

**CASH FLOWS FROM INVESTING ACTIVITIES**

Interest income	<u>740</u>
 Net cash provided by investing activities	 <u>740</u>

**NET INCREASE IN CASH AND CASH EQUIVALENTS**

438,615

Cash and cash equivalents at beginning of year

267,072

**CASH AND CASH EQUIVALENTS AT END OF YEAR**

\$ 705,687

**Reconciliation of operating (loss) to net cash provided by operating activities:**

Operating (loss)	\$ (980,042)
Adjustments to reconcile operating income to net cash provided by operating activities	
Depreciation	1,204,014
Net change in pension liability	58,800
Changes in assets and liabilities	
(Increase) decrease in receivables	298,211
Increase (decrease) in accounts payable	(44,493)
Increase (decrease) in payroll and other liabilities	(17,541)
Increase (decrease) in other current liabilities	<u>(10,574)</u>

Net cash provided by operating activities \$ 508,375

Supplemental disclosure of cash flow information:

Non-cash capital and related financing information:

Capital asset additions accrued as other current liabilities	<u>\$ 378,710</u>
Fair value of contributed capital assets	<u>\$ 4,297,654</u>

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

**KNOTT COUNTY WATER AND SEWER DISTRICT  
NOTES TO FINANCIAL STATEMENTS  
December 31, 2016**

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**1. ORGANIZATION AND ACCOUNTING POLICIES**

**Nature of Activities**

Knott County Water and Sewer District (the District) was created by the Knott County Fiscal Court on February 10, 1999 to be governed and operated under rules and procedures established under Kentucky Revised Statutes (KRS) Chapter 74, relating to water districts and KRS Chapter 220 relating to sanitation districts. The entity's plans are to expand its operating activities into parts of Knott County not presently served with water and sewer utility services.

**Cash and cash equivalents**

The District's cash and cash equivalents are considered to be cash on hand, demand deposits, certificates of deposit, and short-term investments with original maturities of three months or less from the date of acquisition.

**Capital Assets and Depreciation**

Property, plant and equipment are stated at historical cost. Donated assets are valued at their fair market value on the date of donation. Capital assets costing over \$1,500 are recorded and depreciated using the straight-line method of accounting over the respective assets useful lives as follows:

Equipment	5-20	years
Transmission Lines	30-63	years
Water Wells, Structures and Improvements	15-63	years

**Allowance for Doubtful Accounts**

Knott County Water and Sewer District's financial statements reflect an allowance account for its customer accounts receivable based on management's estimates of probable losses. The allowance for doubtful accounts was estimated at \$50,000 as of December 31, 2016.

**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 and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

**Basis of Presentation**

The GASB Codification creates basic financial statements for reporting on the government's financial activities. Financial statements include government-wide financial statements prepared on an accrual basis of accounting and fund financial statements which present information for individual major funds rather than by fund type. Knott County Water and Sewer District is considered a special purpose government engaged in a business-type activity. No governmental type funds are recognized.

The accounting and reporting treatment applied to a fund is determined by its measurement focus. Proprietary funds are reported using the economic resources measurement focus. The statement of cash flows provides information about how the District finances and meets the cash flow needs of its proprietary activities.



**KNOTT COUNTY WATER AND SEWER DISTRICT**  
**NOTES TO FINANCIAL STATEMENTS**  
**December 31, 2016**

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**1. ORGANIZATION AND ACCOUNTING POLICIES (CONTINUED)**

**Basis of Accounting**

The basis of accounting determines when transactions are recorded in the financial records and reported on the financial statements. For its water and sewer enterprise operations, the District uses the full-accrual basis of accounting where revenues are recorded when earned and expenses are recognized when incurred.

Revenues resulting from exchange transactions, in which each party receives essentially equal value, is recorded on the accrual basis when the exchange takes place.

Unearned revenue arises when assets are recognized before revenue recognition criteria have been satisfied. Grants and entitlements received before the eligibility requirements are met are recorded as unearned revenue.

**Net Position**

The District's financial statements incorporate the concepts of net position, deferred outflows of resources and deferred inflows of resources. Net position represents the difference between assets and deferred outflows and liabilities and deferred inflows. The net position component "net investment in capital assets", consists of capital assets, net of accumulated depreciation, reduced by the outstanding balances of any borrowing used for acquisition, construction or improvement of those assets. Deferred outflows of resources and deferred inflows of resources that are attributable to the acquisition, construction or improvement of those assets or related debt also should be included in this component of net position. Net position is reported as restricted when there are limitations on its use either through enabling legislation adopted by the District or through external restrictions imposed by creditors, grantors or laws or regulations of other governments.

**Operating Revenues and Expenses**

Operating revenues are those revenues that are generated directly from the primary activity of the proprietary funds. For the District, those revenues are primarily charges for utility services provided. Non-operating includes interest income/expense and gain/loss on disposal of assets.

**Materials and Supplies**

Purchases of materials and supplies are expensed when purchased and are not inventoried and reflected in the balance sheet. Generally, supplies are purchased as needed. This departure from GAAP is not considered material to the financial statements.

**Restricted Net Position**

Restricted net position reflect funds held in various reserve accounts to meet the covenants as may be specified and defined in the bond and note indentures, restrictions imposed by grantors or as deemed appropriate by management.

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

**Pensions**

For purposes of measuring the net pension liability, deferred outflows of resources and deferred inflows of resources related to pensions, and pension expense, information about the fiduciary net position of the County Employees' Retirement System (CERS) and additions to/deductions from CERS' fiduciary net position have been determined on the same basis as they are reported by CERS. For this purpose, benefit payments, (including refunds of employee contributions) are recognized when due and payable in accordance with benefit terms. Investments are reported at fair value.

**KNOTT COUNTY WATER AND SEWER DISTRICT**  
**NOTES TO FINANCIAL STATEMENTS**  
**December 31, 2016**

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**1. ORGANIZATION AND ACCOUNTING POLICIES (CONTINUED)**

**Advertising Expense**

The District expenses advertising costs as they are incurred. Advertising costs were \$428 for the year ended December 31, 2016.

**Management's Review of Subsequent Events**

The District has evaluated and considered the need to recognize or disclose subsequent events through June 19, 2017; which represents the date that these financial statements were available to be issued. Subsequent events past this date, as they pertain to the year ended December 31, 2016, have not been evaluated by the District.

**2. CASH AND CASH EQUIVALENTS**

KRS 66.480 authorizes the District to invest in the following, including but not limited to, obligations of the United States and of its agencies and instrumentalities, obligations and contracts for future delivery or purchase of obligations backed by the full faith and credit of the United States, obligations of any corporation of the United States government, bonds or certificates of indebtedness of this state, and certificates of deposit issued by or other interest-bearing accounts of any bank or savings and loan institution which are insured by the Federal Deposit Insurance Corporation (FDIC) or which are collateralized, to the extent uninsured, by any obligation permitted by KRS 41.240(4).

Custodial credit risk is the risk that, in the event of the failure of the counterparty, the District will not be able to recover the value of the investment or collateral securities that are in the possession of an outside party.

The District's deposits at December 31, 2016, were entirely covered by Federal Depository Insurance or by collateral held by the custodial banks in the District's name. The bank balances of the District's deposits were \$996,424 at December 31, 2016. As of December 31, 2016, \$746,424 of the District's deposits were covered by collateral held by the custodial banks in the District's name.

**Statement of Cash Flows**

The Statement of Cash Flows for the year ended December 31, 2016, includes as cash and cash equivalents the following:

Cash	\$ 242,084
Restricted cash	<u>463,603</u>
	<u>\$ 705,687</u>

**3. PROPERTY, PLANT, AND EQUIPMENT**

During 2016, the District determined that it would be necessary to modify the estimated useful lives of their capital assets. The change in the estimated useful lives of capital assets required a restatement of beginning accumulated depreciation. See Note 10 for the effect of the restatement of accumulated depreciation on net position. The change in estimated useful lives results in a decreased depreciation expense being recognized on an annual basis, over an increased period of time. Therefore, total depreciation expense recognized by the District over the assets' useful life remains unchanged.

During 2016, the District assumed ownership of the Ball Creek Sewer Plant in a non-monetary transaction with the Troublesome Creek Environmental Authority. The District recorded contributed capital at the estimated fair value of the plant of approximately \$4,300,000.

**KNOTT COUNTY WATER AND SEWER DISTRICT  
NOTES TO FINANCIAL STATEMENTS  
December 31, 2016**

**3. PROPERTY, PLANT, AND EQUIPMENT (CONTINUED)**

The following is a summary of changes in capital assets for the District at December 31, 2016:

	<b>Balance 12/31/15 (as restated)</b>	<b>Additions</b>	<b>Deductions</b>	<b>Balance 12/31/16</b>
<b><u>Capital Assets – Water</u></b>				
Land and land rights	\$ 117,294	\$ -	\$ -	\$ 117,294
Construction in Progress	1,553,722	5,025,035	(4,681,805)	1,896,952
Water plant and transmission lines	46,990,411	4,651,337	-	51,641,748
Vehicles	379,849	-	(39,029)	340,820
Operating equipment	182,310	-	-	182,310
Office furniture and equipment	177,713	-	-	177,713
Subtotal	<u>49,401,299</u>	<u>9,676,372</u>	<u>(4,720,834)</u>	<u>54,356,837</u>
<b><u>Accumulated depreciation – Water</u></b>				
Water plant and transmission lines	6,780,258	1,021,593	-	7,801,851
Vehicles	233,987	38,628	(35,651)	236,964
Operating equipment	123,960	6,915	-	130,875
Office furniture and equipment	72,340	11,087	-	83,427
Subtotal	<u>7,210,545</u>	<u>1,078,223</u>	<u>(35,651)</u>	<u>8,253,117</u>
Total - Water	<u>42,190,754</u>	<u>8,598,149</u>	<u>(4,685,183)</u>	<u>46,103,720</u>
<b><u>Capital Assets – Sewer</u></b>				
Land and land rights	2,790	30,501	-	33,291
WWTPs & collection systems	621,104	4,301,829	-	4,922,933
Operating equipment	68,811	-	-	68,811
Subtotal	<u>692,705</u>	<u>4,332,330</u>	<u>-</u>	<u>5,025,035</u>
<b><u>Accumulated depreciation – Sewer</u></b>				
Vehicles	318,499	121,303	-	439,802
Operating equipment	32,006	4,488	-	36,494
Subtotal	<u>350,505</u>	<u>125,791</u>	<u>-</u>	<u>476,296</u>
Total - Sewer	<u>342,200</u>	<u>4,206,539</u>	<u>-</u>	<u>4,548,739</u>
<b>Total net property and equipment</b>	<b><u>\$ 42,532,954</u></b>	<b><u>\$ 12,804,688</u></b>	<b><u>\$ (4,685,183)</u></b>	<b><u>\$ 50,652,459</u></b>

Total depreciation expense for the year ended December 31, 2016 is allocated as follows:

Water operations	\$ 1,078,223
Sewer operations	<u>125,791</u>
	<u>\$ 1,204,014</u>

**4. OTHER CURRENT LIABILITIES**

Other current liabilities consisted of the following at December 31, 2016:

Construction contractors payable	\$ 378,710
Customer deposit payable	117,370
Utility tax payable	3,649
Engineering contract payable	1,100
Sales tax payable	<u>678</u>
Total other current liabilities	<u>\$ 501,507</u>

**KNOTT COUNTY WATER AND SEWER DISTRICT  
NOTES TO FINANCIAL STATEMENTS  
December 31, 2016**

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**5. LONG-TERM DEBT**

The following is a summary of the bonds and notes outstanding for the District for the year ended December 31, 2016:

**Bonds and Notes**

Rural Utilities Service Bond - \$185,000, dated 12/19/03, was issued to pay off prior debt of the District, with payments through 2043, bearing interest at a rate of 4.5%.	\$ 155,500
Kentucky Infrastructure Authority Loan - \$547,000, dated 1/1/04, was issued to pay for expenditures related to the Highway 899/Mallie Waterworks improvement project, with payments through 2022, bearing interest at a rate of 4.05%.	315,280
Rural Utilities Service Bond - \$100,000, dated 1/26/07, was issued to finance a portion of the Water Treatment Plant project, with payments through 2046, bearing interest at a rate of 4.125%.	89,900
Government Obligation Contract - \$27,250, dated 11/1/14, to finance the purchase of a pickup truck with payments through 2017, bearing interest at 2.25 – 3.625%.	<u>7,154</u>
	567,834
Less: current portion of debt	<u>(63,788)</u>
Long-term debt	<u>\$ 504,046</u>

The annual requirements to amortize all bonds and notes outstanding as of December 31, 2016 are as follows:

Year Ending December 31,	Principle	Interest and Fees	Payment
2017	\$ 63,788	\$ 23,856	\$ 87,644
2018	59,390	20,853	80,243
2019	61,634	18,609	80,243
2020	64,072	15,932	80,004
2021	66,604	13,149	79,753
2022-2026	62,246	48,484	110,730
2027-2031	39,000	40,503	79,503
2032-2036	48,000	30,936	78,936
2037-2041	59,700	20,468	80,168
2042-2046	39,600	5,808	45,408
2047	<u>3,800</u>	<u>252</u>	<u>4,052</u>
	<u>\$ 567,834</u>	<u>\$ 238,850</u>	<u>\$ 806,684</u>

**KNOTT COUNTY WATER AND SEWER DISTRICT  
NOTES TO FINANCIAL STATEMENTS  
December 31, 2016**

**5. LONG-TERM DEBT (CONTINUED)**

The following is a summary of changes in long-term debt and net pension liability:

	December 31, 2015	Additions	Retirements	December 31, 2016	Due Within One Year
Net pension liability	\$ 792,152	\$ 31,143	\$ -	\$ 823,295	\$ -
Bonds payable	249,900	-	(4,500)	245,400	4,400
Notes payable	<u>381,673</u>	<u>-</u>	<u>(59,239)</u>	<u>322,434</u>	<u>59,388</u>
	<u>\$ 1,423,725</u>	<u>\$ 31,143</u>	<u>\$ (63,739)</u>	<u>\$ 1,391,129</u>	<u>\$ 63,788</u>

The District's is required to maintain debt service and depreciation reserves in accordance with their various debt agreements. The District has fully funded its debt service and depreciation reserves at December 31, 2016.

**6. LEASE COMMITMENTS**

The District leases office equipment under a non-cancellable operating lease agreement. Rental expense for the year ended December 31, 2016 was \$6,127. Future minimum lease payments including applicable taxes and fees for operating leases at December 31, 2016 are as follows:

<b>December 31,</b>	
2017	\$ 4,394
2018	<u>732</u>
Total lease payments	<u>\$ 5,126</u>

**7. RETIREMENT PLAN**

The Knott County Water and Sewer District is a participating employer of the County Employees' Retirement System (CERS). Under the provisions of Kentucky Revised Statute 61.645, the Board of Trustees of Kentucky Retirement Systems administers the CERS. The plan issues publicly available financial statements which may be downloaded from the Kentucky Retirement Systems website.

*Plan Description* – CERS is a cost-sharing multiple-employer defined benefit pension plan that covers substantially all regular full-time members employed in positions of each participating county, city, and school board, and any additional eligible local agencies electing to participate in the System. The plan provides for retirement, disability, and death benefits to plan members. Retirement benefits may be extended to beneficiaries of plan members under certain circumstances. Cost-of-living (COLA) adjustments are provided at the discretion of state legislature.

*Contributions* – For the year ended December 31, 2016, plan members were required to contribute 5.00% of wages for non-hazardous job classifications. Employees hired after September 2008 were required to contribute an additional 1% to cover the cost of medical insurance that is provided through CERS. Participating employers were required to contribute at an actuarially determined rate. Per Kentucky Revised Statute Section 78.545(33), normal contribution and past service contribution rates shall be determined by the Board on the basis of an annual valuation last proceeding the July 1 of a new biennium. The Board may amend contribution rates as of the first day of July of the second year of a biennium, if it is determined on the basis of a subsequent actuarial valuation that amended contribution rates are necessary to satisfy requirements determined in accordance with actuarial basis adopted by the Board. For the year ended December 31, 2016, participating employers contributed 17.06% through June 30 and 18.68% thereafter, of each non-hazardous employee's wages, which is equal to the actuarially determined rate set by the Board. Administrative costs of Kentucky Retirement System are financed through employer contributions and investment earnings.

**KNOTT COUNTY WATER AND SEWER DISTRICT  
NOTES TO FINANCIAL STATEMENTS  
December 31, 2016**

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**7. RETIREMENT PLAN (CONTINUED)**

Plan members who began participating on, or after, January 1, 2014, were required to contribute to the Cash Balance Plan. The Cash Balance Plan is known as a hybrid plan because it has characteristics of both a defined benefit plan and a defined contribution plan. Members in the plan contribute a set percentage of their salary each month to their own account. Plan members contribute 5% of wages to their own account and 1% to the health insurance fund. The employer contribution rate is set annually by the Board based on an actuarial valuation. The employer contributes a set percentage of each member's salary. Each month, when employer contributions are received, an employer pay credit is deposited to the member's account. For non-hazardous members, their account is credited with a 4% employer pay credit. The employer pay credit represents a portion of the employer contribution.

The District contributed \$82,187 for the year ended December 31, 2016, or 100% of the required contribution. The contribution was allocated \$60,741 to the CERS pension fund and \$21,446 to the CERS insurance fund.

*Benefits* – CERS provides retirement, health insurance, death and disability benefits to Plan employees and beneficiaries. Employees are vested in the plan after five years' service.

For retirement purposes, employees are grouped into three tiers based on hire date:

Tier 1	Participation date Unreduced retirement Reduced retirement	Before September 1, 2008 27 years service or 65 years old At least 5 years service and 55 years old or At least 25 years service and any age
Tier 2	Participation date Unreduced retirement  Reduced retirement	September 1, 2008 - December 31, 2013 At least 5 years service and 65 years old or age 57+ and sum of service years plus age equal 87 At least 10 years service and 60 years old
Tier 3	Participation date Unreduced retirement  Reduced retirement	After December 31, 2013 At least 5 years service and 65 years old or age 57+ and sum of service years plus age equal 87 Not available

Cost of living adjustments are provided at the discretion of the General Assembly. Retirement is based on a factor of the number of years' service and hire date multiplied by the average of the highest five years' earnings. Reduced benefits are based on factors of both of these components. Participating employees become eligible to receive the health insurance benefit after at least 180 months of service. Death benefits are provided for both death after retirement and death prior to retirement. Death benefits after retirement are \$5,000 in lump sum. Five years' service is required for death benefits prior to retirement and the employee must have suffered a duty-related death. The decedent's beneficiary will receive the higher of the normal death benefit and \$10,000 plus 25% of the decedent's monthly final rate of pay and any dependent child will receive 10% of the decedent's monthly final rate of pay up to 40% for all dependent children. Five years' service is required for nonservice-related disability benefits.

*Pension Liabilities, Expense, Deferred Outflows of Resources and Deferred Inflows of Resources* – At December 31, 2016, the District reported a liability of \$823,295 or its proportionate share of the net pension liability. The net pension liability was measured as of June 30, 2016, and the total pension liability used to calculate the net pension liability was determined by an actuarial valuation as of that date. The District proportion of the net pension liability was based on a projection of the District's long-term share of contributions to the pension plan relative to the projected contributions of all participating entities, actuarially determined. At June 30, 2016, the District's proportion was .01672 percent, which was a decrease of 0.0017 percent from its proportion measured as of June 30, 2015.

**KNOTT COUNTY WATER AND SEWER DISTRICT  
NOTES TO FINANCIAL STATEMENTS  
December 31, 2016**

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**7. RETIREMENT PLAN (CONTINUED)**

For the year ended December 31, 2016, the District recognized pension expense of \$113,380. At December 31, 2016, the District reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

	<b>Deferred Outflows of Resources</b>	<b>Deferred Inflows of Resources</b>
Differences between expected and actual results	\$ 3,594	\$ -
Changes of assumptions	43,614	-
Net difference between projected and actual earnings on Plan investments	77,398	-
Changes in proportion and differences between Company contributions and proportionate share of contributions	30,412	45,630
Company contributions subsequent to the measurement date	36,110	-
 Total	 \$ 191,128	 \$ 45,630

The \$36,110 of deferred outflows of resources resulting from the District's contributions subsequent to the measurement date will be recognized as a reduction of the net pension liability in the year ending December 31, 2017. Other amounts reported as deferred outflows of resources and deferred inflows of resources will be recognized in pension expense as follows:

<b>Year ending December 31,</b>	
2017	\$ 48,810
2018	\$ 21,961
2019	\$ 21,439
2020	\$ 17,178

*Actuarial Assumptions* – The total pension liability in the June 30, 2016 actuarial valuation was determined using the following actuarial assumptions, applied to all periods included in the measurement:

Inflation	3.25%
Salary increases	4.00%, average, including inflation
Investment rate of return	7.50%, net of Plan investment expense, including inflation

Mortality rates were based on the RP-2000 Combined Mortality Table projected with Scale BB to 2013 (multiplied by 50% for males and 30% for females). For healthy retired members and beneficiaries, the mortality table used is the RP-2000 Combined Mortality Table projected with Scale BB to 2013 (set back 1 year for females). For disabled members, the RP-2000 Combined Disabled Mortality Table projected with Scale BB to 2013 (set back 4 years for males) is used for the period after disability retirement.

The actuarial assumptions used in the June 30, 2016 valuation were based on the results of an actuarial experience study for the period July 1, 2008 - June 30, 2013.

**KNOTT COUNTY WATER AND SEWER DISTRICT  
NOTES TO FINANCIAL STATEMENTS  
December 31, 2016**

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**7. RETIREMENT PLAN (CONTINUED)**

The long-term expected return on plan assets is reviewed as part of the regular experience studies prepared every five years. Several factors are considered in evaluating the long-term rate of return assumptions including long-term historical data, estimates inherent in current market data, and a log-normal distribution analysis in which best-estimate ranges of expected future real rates of return (expected return, net of investment expense and inflation) were developed by the investment consultant for each major asset class. These ranges were combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and then adding expected inflation. The capital market assumptions developed by the investment consultant are intended for use over a 10-year horizon and may not be useful in setting the long-term rate of return for funding pension plans which covers a longer time frame. The assumption is intended to be a long-term assumption and is not expected to change absent a significant change in the asset allocation, a change in the inflation assumption, or a fundamental change in the market that alters expected returns in future years.

The target allocation and best estimates of nominal real rates of return for each major asset class are summarized in the following table:

<b>Asset Class</b>	<b>Target Allocation</b>	<b>Long-term Nominal Real Rate of Return</b>
Combined Equity	44%	5.4%
Combined Fixed Income	19%	1.5%
Real Return (Diversified Inflation Strategies)	10%	3.5%
Real Estate	5%	4.5%
Absolute Return (Diversified Hedge Funds)	10%	4.25%
Private Equity	10%	8.5%
Cash Equivalent	<u>2%</u>	-.25%
Total	100%	

*Discount Rate* – The discount rate used to measure the total pension liability was 7.50 percent. The projection of cash flows used to determine the discount rate assumed that local employers would contribute the actuarially determined contribution rate of projected compensation over the remaining 27 year amortization period of the unfunded actuarial accrued liability. The actuarial determined contribution rate is adjusted to reflect the phase in of anticipated gains on actuarial value of assets over the first four years of the projection period. The discount rate does not use a municipal bond rate.

*Sensitivity of the District's Proportionate Share of the Net Pension Liability to Changes in the Discount Rate* – The following presents the District's proportionate share of the net pension liability calculated using the discount rate of 7.50 percent, as well as what the District's proportionate share of the net pension liability would be if it were calculated using a discount rate that is 1-percentage-point lower (6.50 percent) or 1-percentage-point higher (8.50 percent) than the current rate:

	<b>Discount rate</b>	<b>District's proportionate share of net pension liability</b>
1% decrease	6.50%	\$ 649,568
Current discount rate	7.50%	\$ 823,295
1% increase	8.50%	\$ 1,025,953



**KNOTT COUNTY WATER AND SEWER DISTRICT**  
**NOTES TO FINANCIAL STATEMENTS**  
**December 31, 2016**

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**7. RETIREMENT PLAN (CONTINUED)**

*Payable to the Pension Plan* – At December 31, 2016, the District reported a payable of \$10,418 for the outstanding amount of contributions to the pension plan required for the year ended December 31, 2016. The payable includes both the pension and insurance contribution allocation.

**8. RISK MANAGEMENT**

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

**9. CONSTRUCTION COMMITMENTS**

The District regularly engages in construction projects to expand water lines and access throughout its service area. The District generally applies for grant money to fund these projects. As of December 31, 2016, the District had construction in progress of \$1,869,952 related to a water line project that it has committed to completing.

**10. RESTATEMENT OF NET POSITION**

The following table summarizes restatements in net position of the District as previously reported:

Net position, as previously reported	\$ 39,030,298
Deferred inflows and outflows - pension	173,153
Net pension liability	(257,999)
Customer accounts receivable	93,758
Accounts payable	10,590
Prepaid expenses	(20,046)
Other current liabilities	30,151
Accumulated depreciation	<u>2,756,697</u>
Net position, as restated	<u>\$ 41,816,602</u>

The reason for the District's restatement of net position related to accumulated depreciation is described in Note 3. The restatement related to the net pension liability and the deferred inflows and outflows – pension, was primarily due to the December 31, 2015 financial statements of the District reporting these balances as measured on June 30, 2014. The restatement was made to adjust to the balances, as measured on June 30, 2015, as required by GASB standards. The remaining restatements shown in the above table related to accruals that had been paid or received in prior years but not removed from the District's statement of net position.

**REQUIRED SUPPLEMENTARY INFORMATION**

**KNOTT COUNTY WATER AND SEWER DISTRICT  
 REQUIRED SUPPLEMENTARY SCHEDULE OF  
 PROPORTIONATE SHARE OF THE NET PENSION LIABILITY  
 Current Fiscal Year**

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	<b>2016</b>
District's proportion of the net pension liability	0.01672%
District's proportionate share of the net pension liability (asset)	\$ 823,295
District's covered employee payroll	\$ 435,595
District's share of the net pension liability (asset) as a percentage of its covered employee payroll	189.00%
Plan fiduciary net position as a percentage of the total pension liability	59.97%

Notes:

There were no changes in benefit terms, size or composition of the population covered by the benefit terms, or the assumptions used in the current fiscal year.

Prior year information is not available. In future audit periods this schedule will be updated to include available prior period information.

**KNOTT COUNTY WATER AND SEWER DISTRICT  
REQUIRED SUPPLEMENTARY SCHEDULE OF CONTRIBUTIONS  
Current Fiscal Year**

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	<b>2016</b>
Contractually required employer contribution	\$ 60,741
Contributions relative to contractually required employer contribution	<u>60,741</u>
Contribution deficiency (excess)	<u>\$ -</u>
District's covered employee payroll	\$ 435,595
Employer contributions as a percentage of covered-employee payroll	13.94%

Notes:

There were no changes in benefit terms, size or composition of the population covered by the benefit terms, or the assumptions used in the current fiscal year.

Contractually required employer contributions exclude the portion of contributions paid to CERS but allocated to the insurance fund of the CERS. The above contributions only include those contributions allocated directly to the CERS pension fund.

Prior year information is not available. In future audit periods this schedule will be updated to include available prior period information.

## **SUPPLEMENTARY INFORMATION**

**KNOTT COUNTY WATER AND SEWER DISTRICT  
BUDGETARY COMPARISON SCHEDULE  
for the year ended December 31, 2016**

	Original Budget	Appropriated Budget	Actual Amount	Variance with Final Budget Favorable (Unfavorable)
<b>OPERATING INCOME</b>				
Water service	\$ 2,294,850	\$ 2,294,850	\$ 1,893,265	\$ (401,585)
Sewer service	-	-	66,855	66,855
Penalties	-	-	20,238	20,238
Miscellaneous income	34,423	34,423	51,376	16,953
Reconnection and collection fees	-	-	6,965	6,965
	<u>2,329,273</u>	<u>2,329,273</u>	<u>2,038,699</u>	<u>(290,574)</u>
<b>OPERATING EXPENSES</b>				
Salaries and fringe benefits	721,364	721,364	710,626	10,738
Commissioner fee	30,200	30,200	27,800	2,400
Office and advertising expense	1,500	1,500	1,182	318
Water consumption	96,268	96,268	65,705	30,563
Electricity	348,559	348,559	370,062	(21,503)
Telephone	11,108	11,108	10,453	655
Travel and training	3,117	3,117	4,088	(971)
Rents	14,145	14,145	13,707	438
Contractual fees	187,084	187,084	204,752	(17,668)
Vehicle expense	34,708	34,708	34,596	112
Operating supplies and maintenance	250,839	250,839	236,506	14,333
Licenses, permits, dues, and fees	6,296	6,296	7,080	(784)
Bad debt expense	-	-	73,862	(73,862)
Insurance and bonds	53,569	53,569	54,308	(739)
	<u>1,758,757</u>	<u>1,758,757</u>	<u>1,814,727</u>	<u>(55,970)</u>
Total operating expense				
Operating income before depreciation	570,516	570,516	223,972	(346,544)
Depreciation expense	1,632,662	1,632,662	1,204,014	428,648
	<u>(1,062,146)</u>	<u>(1,062,146)</u>	<u>(980,042)</u>	<u>82,104</u>
<b>OPERATING (LOSS)</b>				
Non-operating income (expenses)				
Interest income	-	-	740	740
Loss on disposal of asset	-	-	(459)	(459)
Interest expense	(26,206)	(26,206)	(34,162)	(7,956)
	<u>(1,088,352)</u>	<u>(1,088,352)</u>	<u>(1,013,923)</u>	<u>74,429</u>
<b>(LOSS) BEFORE CAPITAL CONTRIBUTIONS</b>				
Capital contributions				
Tap fees	-	-	24,300	24,300
Contributed capital	-	-	9,352,552	9,352,552
	<u>-\$ (1,088,352)</u>	<u>-\$ (1,088,352)</u>	<u>\$ 8,362,929</u>	<u>\$ 9,451,281</u>
<b>CHANGE IN NET POSITION</b>				



**INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL OVER  
FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS  
BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED  
IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS**

To the Board of Commissioners  
Knott County Water and Sewer District  
Vicco, 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 Knott County Water and Sewer District (the "District") as of and for the year ended December 31, 2016, and the related notes to the financial statements, which collectively comprise the Knott County Water and Sewer District's basic financial statements and have issued our report thereon dated June 19, 2017.

**Internal Control over Financial Reporting**

In planning and performing our audit of the financial statements, we considered the 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 the District's internal control. Accordingly, we do not express an opinion on the effectiveness of the 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 and therefore, material weaknesses or significant deficiencies may exist that were not identified. We did identify a certain deficiency in internal control, described in the accompanying schedule of findings and questioned costs that we consider to be a material weakness (2016-001).

**Compliance and Other Matters**

As part of obtaining reasonable assurance about whether Knott County Water and Sewer 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*.

### **Knott County Water and Sewer District's Response to Findings**

Knott County Water and Sewer District's response to the findings identified in our audit is described in the accompanying schedule of findings and questioned costs. Knott County Water and Sewer District's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

### **Purpose of this Report**

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

**RFH**

RFH, PLLC  
Lexington, Kentucky  
June 19, 2017





**INDEPENDENT AUDITORS' REPORT ON COMPLIANCE  
FOR EACH MAJOR PROGRAM AND ON INTERNAL CONTROL  
OVER COMPLIANCE REQUIRED BY THE UNIFORM GUIDANCE**

To the Board of Commissioners  
Knott County Water and Sewer District  
Vicco, Kentucky

**Report on Compliance for Each Major Federal Program**

We have audited Knott County Water and Sewer District's compliance with the types of compliance requirements described in the *OMB Compliance Supplement* that could have a direct and material effect on each of Knott County Water and Sewer District's major federal programs for the year ended December 31, 2016. Knott County Water and Sewer District's major federal programs are identified in the summary of auditors' results section of the accompanying schedule of findings and questioned costs.

***Management's Responsibility***

Management is responsible for compliance with federal statutes, regulations, and the terms and conditions of its federal awards applicable to its federal programs.

***Auditors' Responsibility***

Our responsibility is to express an opinion on compliance for each of Knott County Water and Sewer 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 the audit requirements of Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance). Those standards and the Uniform Guidance 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 Knott County Water and Sewer District's compliance with those requirements and performing such other procedures as we 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 Knott County Water and Sewer District's compliance.

***Opinion on Each Major Federal Program***

In our opinion, Knott County Water and Sewer 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 ended December 31, 2016.

## Report on Internal Control over Compliance

Management of Knott County Water and Sewer 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 Knott County Water and Sewer 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 compliance for each major federal program and to test and report on internal control over compliance in accordance with Uniform Guidance, but not 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 Knott County Water and Sewer 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 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 Uniform Guidance. Accordingly, this report is not suitable for any other purpose.

**RFH**

RFH, PLLC  
Lexington, Kentucky  
June 19, 2017

**KNOTT COUNTY WATER AND SEWER DISTRICT  
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS  
for the year ended December 31, 2016**

Federal Grant/Pass Through Grantor/Program Title	Federal CFDA Number	Grantor Number	Grant Award Period	Expenditures
<b><u>U.S. Department of the Interior:</u></b>				
<b>Passed through from Kentucky Department for Natural Resources</b>				
Abandoned Mine Land Reclamation	15.252	PO2 128 1400005591	04/01/15-06/30/17	\$ 1,077,493
	15.252	PO2 128 1500003937	04/01/15-06/30/17	526,340
	15.252	PO2 128 1400006848	07/01/14-06/30/17	<u>3,430,885</u>
		<b>Total Department of the Interior</b>		<u>5,034,718</u>
<b><u>U.S. Department of Homeland Security:</u></b>				
<b>Passed through from Kentucky Emergency Management</b>				
Disaster Grants - Public Assistance	97.036	PO2 095 1500004734	02/15/15-06/30/16	25,376
	97.036	PO2 095 1600000757	07/11/15-06/30/18	<u>16,132</u>
		<b>Total Department of Homeland Security</b>		<u>41,508</u>
<b>TOTAL FEDERAL AWARDS (INCLUDED IN CONTRIBUTED CAPITAL)</b>				<b><u>\$ 5,076,226</u></b>

The Organization did not pass through any funds to subrecipients.

**Note 1 - Basis of Presentation**

This schedule is presented on the accrual basis of accounting. The information in this schedule is presented in accordance with the requirements of Title 2 U.S. Code of Federal Regulations (CFR) Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance). Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of the basic financial statements.

**Note 2 - Loans and Loan Guarantees**

The auditee had no loans or loan guarantees during or at the end of the year, except for the loans payable to USDA Rural Development, Kentucky Infrastructure Authority and to banks, which are indicated in the Notes to the basic financial statements of the District.

**Note 3 - Indirect Cost Rates**

The Organization did not elect to use the 10 percent de minimis cost rate as allowed under the Uniform Guidance.

**KNOTT COUNTY WATER AND SEWER DISTRICT  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
for the year ended December 31, 2016**

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**I. SUMMARY OF AUDITORS' RESULTS**

Financial Statements:

Type of auditors' report issued: Unmodified

Internal control over financial reporting:

Material weaknesses identified	<input checked="" type="checkbox"/> Yes	<input type="checkbox"/> No
Significant deficiencies identified that are not considered to be material weaknesses	<input type="checkbox"/> Yes	<input checked="" type="checkbox"/> None reported

Non-compliance material to financial statements noted	<input type="checkbox"/> Yes	<input checked="" type="checkbox"/> No
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Federal Awards:

Internal control over major programs:

Material weaknesses identified	<input type="checkbox"/> Yes	<input checked="" type="checkbox"/> No
Significant deficiencies identified that are not considered to be material weaknesses	<input type="checkbox"/> Yes	<input checked="" type="checkbox"/> None reported

Type of auditors' report issued on compliance for major programs:  
Unmodified for all major programs.

Any audit findings disclosed that are required to be reported in accordance with 2 CFR 200.516(a)?	<input checked="" type="checkbox"/> Yes	<input type="checkbox"/> No
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**Major Programs:**

CFDA Number	Name of Federal Program or Cluster
15.252	Abandoned Mine Land Reclamation

Dollar threshold used to distinguish between type A and type B programs:	\$ 750,000
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Auditee qualified as a low-risk auditee?	<input type="checkbox"/> Yes	<input checked="" type="checkbox"/> No
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**II. FINDINGS RELATED TO FINANCIAL STATEMENTS**

**2016-001 – Internal Control over Financial Reporting**

**Criteria:**

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

**Condition:**

The District does not have the internal control procedures required to draft the financial statements in conformity with generally accepted accounting principles.

**Cause:**

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

**Effect:**

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

**II. FINDINGS RELATED TO FINANCIAL STATEMENTS (CONTINUED)**

**2016-001 – Internal Control over Financial Reporting (CONTINUED)**

**Recommendation:**

We recommend management review the costs and benefits involved to retain a consultant with the required expertise to prepare the financial statements or review the financial statements as prepared by the auditor for compliance with generally accepted accounting principles.

**RESPONSE:**

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

**III. FINDINGS AND QUESTIONED COSTS FOR FEDERAL AWARDS**

NONE

**IV. PRIOR AUDIT FINDINGS**

NONE