EAST PENDLETON COUNTY
WATER DISTRICT
Falmouth, Kentucky

FINANCIAL STATEMENTS
December 31, 2016 and 2015

C O N T E N T S

Members American Institute of Certified Public Accountants
and Kentucky Society of Certified Public Accountants

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INDEPENDENT AUDITORS' REPORT

To the Board of Commissioners
East Pendleton County Water District
Falmouth, Kentucky

Report on the Financial Statements

We have audited the accompanying financial statements of the East Pendleton County Water District (the District) as of and for the years ended December 31, 2016 and 2015, 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 opinions on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

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

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

Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the East Pendleton County Water District as of December 31, 2016 and 2015, and the respective changes in financial position, and cash flows thereof for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the pension schedules on pages 15-16 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.

Management has omitted the Management Discussion and Analysis that accounting principles generally accepted in the United States of America require 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 Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated June 27, 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 27, 2017

EAST PENDLETON COUNTY WATER DISTRICT
STATEMENTS OF NET POSITION
December 31,

ASSETS	**2016**	**2015**
Current assets		
Cash	$ 429,564	$ 251,550
Customer accounts receivable, net	85,160	82,596
Inventory	23,096	16,827
Total current assets	537,820	350,973
Restricted assets		
Cash	323,810	222,914
Cash - construction	35,670	44,848
Certificates of deposit	255,353	254,620
Total restricted assets	614,833	522,382
Capital assets		
Property, plant and equipment - Water	7,230,477	7,184,181
Less: accumulated depreciation - Water	(3,412,760)	(3,301,700)
Property, plant and equipment - Sewer	34,952	34,952
Less: accumulated depreciation - Sewer	(27,987)	(27,361)
Total capital assets	3,824,682	3,890,072
Total assets	4,977,335	4,763,427
DEFERRED OUTFLOWS OF RESOURCES		
Deferred outflows - pension	87,010	77,185
Total assets and deferred outflows of resources	$ 5,064,345	$ 4,840,612
LIABILITIES		
Current liabilities		
Accounts payable	$ 26,631	$ 27,727
Taxes payable	3,923	4,266
Customer deposits	39,765	38,630
Accrued interest payable	13,797	1,456
Current portion of debt	83,917	91,138
Total current liabilities	168,033	163,217
Noncurrent liabilities		
Net pension liability	461,342	524,772
KIA notes payable	134,585	148,702
Bonds payable, net	1,016,300	1,021,100
Total noncurrent liabilities	1,612,227	1,694,574
Total liabilities	1,780,260	1,857,791
DEFERRED INFLOWS OF RESOURCES		
Defeasance on refunding	16,149	16,822
Deferred inflows - pension	87,430	19,031
Total deferred inflows of resources	103,579.00	35,853
NET POSITION		
Net investment in capital assets	2,589,880	2,629,132
Restricted for debt service	268,505	248,890
Restricted for depreciation	229,461	228,644
Unrestricted	92,660	(159,698)
Total net position	3,180,506	2,946,968
Total liabilities, deferred inflows of resources and net position	$ 5,064,345	$ 4,840,612

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

EAST PENDLETON COUNTY WATER DISTRICT
STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET POSITION
for the years ended December 31,

	2016	2015
OPERATING INCOME		
Water sales	$ 1,067,420	$ 1,062,411
Sewer sales	20,973	20,124
Other revenue	41,120	28,768
Total operating income	1,129,513	1,111,303
OPERATING EXPENSES		
Water purchases	209,746	216,873
Pumping	31,088	26,692
Operation	235,604	216,977
Maintenance	2,023	7,758
General and administrative	271,806	325,090
Sewer expenses	14,262	14,021
Total operating expense	764,529	807,411
Operating income before depreciation	364,984	303,892
Depreciation expense	(111,686)	(108,370)
OPERATING INCOME	253,298	195,522
Non-operating income (expense)		
Interest income	1,523	2,170
Interest expense	(39,841)	(81,499)
Total non-operating income (expense)	(38,318)	(79,329)
INCOME BEFORE CAPITAL CONTRIBUTIONS	214,980	116,193
Capital contributions		
Tap fees	18,558	14,223
Change in net position	233,538	130,416
Net position, beginning of year, as restated	2,946,968	2,816,552
NET POSITION, END OF YEAR	$ 3,180,506	$ 2,946,968

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

EAST PENDLETON COUNTY WATER DISTRICT
STATEMENTS OF CASH FLOWS
for the years ended December 31,

	2016	2015
CASH FLOWS FROM OPERATING ACTIVITIES		
Receipts from customers	$ 1,126,949	$ 1,106,459
Payments to suppliers	(388,994)	(360,115)
Payments for employee services and benefits	(386,423)	(408,033)
Net cash provided by operating activities	351,532	338,311
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Retirement of debt principal	(26,138)	(1,083,764)
Interest paid	(28,715)	(98,444)
Proceeds from issuance of bond	-	895,000
Purchase of capital assets	(46,295)	(121,488)
Tap fees	18,558	14,223
Net cash (used in) capital and related financing activities	(82,590)	(394,473)
CASH FLOWS FROM INVESTING ACTIVITIES		
Investment in certificates of deposit	(733)	(1,451)
Interest income	1,523	2,170
Net cash provided by investing activities	790	719
NET INCREASE (DECREASE) IN CASH	269,732	(55,443)
Cash, beginning of year	519,312	574,755
CASH, END OF YEAR	$ 789,044	$ 519,312
Reconciliation of operating income to net cash provided by operating activities:		
Operating income	$ 253,298	$ 195,522
Noncash items included in operating income		
Depreciation	111,686	108,370
Defeasance on refunding	-	17,403
Net change in pension liability	(4,856)	19,269
Changes in assets and liabilities		
(Increase) decrease in accounts receivables	(2,564)	(4,844)
(Increase) decrease in inventory	(6,269)	1,873
Increase (decrease) in accounts payable	(555)	(2,682)
Increase (decrease) in other payables	(343)	135
Increase (decrease) in customer deposits	1,135	3,265
Net cash provided by operating activities	$ 351,532	$ 338,311
Supplemental disclosure of cash flow information		
Non-cash capital and related financing information:		
Fixed asset additions accrued as accounts payable	$ -	$ 541
Defeasance on debt refunding	$ -	$ 17,403
Amortization of defeasance on refunding	$ 673	$ 581
Components of cash on the Statement of Net Position		
Cash	$ 429,564	$ 251,550
Restricted cash	323,810	222,914
Construction	35,670	44,848
	$ 789,044	$ 519,312

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

1. ORGANIZATION AND ACCOUNTING POLICIES

The East Pendleton County Water District (the District) was created and organized as a public body incorporated in Pendleton County, Kentucky, pursuant to Chapter 74 of the Kentucky Revised Statutes, by the Pendleton County Fiscal Court to operate a water distribution system.

Reporting Entity

The East Pendleton County Water District's financial statements include the operations of all entities for which the District exercises oversight responsibility. Oversight responsibility includes, but is not limited to, financial interdependency, selection of the governing authority, designation of management, ability to significantly influence operations, and accountability for fiscal matters.

There are no other entities that are subject to the District's oversight responsibility as indicated above.

Basis of Accounting

The net position of the District is classified into three categories; net investment in capital assets, restricted and unrestricted. The restricted net assets consist of reserves for bond retirement and depreciation costs relating to the construction, replacement, extension, additions and/or improvements to the system in addition to customer deposits. These reserves are discussed in Note 5.

When both restricted and unrestricted resources are available for use, the District's Board of Commissioners makes a determination as to which resource should be used first.

The accrual basis of accounting is utilized by the District. Under this method, revenues are recognized when earned and expenses are recognized when incurred.

The District reports all revenues and expenses as operating, except interest income, interest expense, amortization, gains and losses on disposal of assets, and capital contributions.

Cash and Cash Equivalents

For purposes of the statement of cash flows, the District defines cash as cash on hand, cash in bank, money market funds in both unrestricted and restricted accounts, and certificates of deposit with an initial maturity of less than 90 days.

Accounts Receivable

The District's accounts receivable reserve represents its estimate of all uncollectible accounts. The reserve at December 31, 2016 and 2015 totaled $3,500.

Inventory

The District's inventory is composed of chemicals, equipment and supply-type items used for routine maintenance, repairs and new water lines. The inventory is stated at the lower of cost (first-in, first-out method) or market.

Property and Equipment

Capital assets are recorded at cost. Depreciation has been provided using the straight-line method over the estimated useful life of the asset, which ranges from 7 - 62.5 years. Land and land rights are not subject to depreciation. Interest costs during construction of capital assets are capitalized as a part of the cost.

1. ORGANIZATION AND ACCOUNTING POLICIES (CONTINUED)

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.

Estimates

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

Management's Review of Subsequent Events

The District has evaluated and considered the need to recognize or disclose subsequent events through June 27, 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 INVESTMENTS

Under Kentucky Revised Statute 66.480 the District is allowed to invest in obligations of the U.S. Treasury and U.S. agencies, obligations of the Commonwealth of Kentucky and its agencies, insured savings and loans, or interest bearing deposits of insured national or state banks.

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. In order to anticipate market changes and provide a level of security for all funds, the collateralization level shall be one hundred percent of the market value of the principal, plus accrued interest.

The District's deposits and investments 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 table presented below is designed to disclose the level of custody credit risk assumed by the District, based upon how its deposits were insured or secured with collateral at December 31, 2016. The categories of credit risk are defined as follows:

(1) Insured or collateralized with securities held by the government or by its agent in the government's name.
(2) Collateralized with securities held by the pledging financial institution's trust department or agent in the government's name.
(3) Uncollateralized, including any bank balance that is collateralized with securities held by the pledging financial institution, or by its trust department or agent but not in the government's name.

2. CASH AND INVESTMENTS (CONTINUED)

Type of Deposit	Category 1	Category 2	Category 3	Total Bank Amount	Total Carrying Amount
Cash	$ 789,329	$ -	$ -	$ 789,329	$ 789,044
Certificates of deposit	255,353	-	-	255,353	255,353
	$ 1,044,682	$ -	$ -	$ 1,044,682	$ 1,044,397

3. CAPITAL ASSETS

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

	Balance 12/31/2015	Additions	Disposals	Balance 12/31/2016
Capital assets not depreciated:				
Organizational costs	$ 7,200	$ -	$ -	$ 7,200
Water land	16,157	-	-	16,157
Sewer land	1,168	-	-	1,168
Totals	24,525	-	-	24,525
Capital assets being depreciated:				
Water property and equipment	7,160,824	46,296	-	7,207,120
Sewer property and equipment	33,784	-	-	33,784
Totals	7,194,608	46,296	-	7,240,904
Less: accumulated depreciation	3,329,061	111,686	-	3,440,747
Net depreciable assets	3,865,547	(65,390)	-	3,800,157
Total capital assets, net	$ 3,890,072	$ (65,390)	$ -	$ 3,824,682

Depreciation expense totaled $111,686 and $108,370 for the years ended December 31, 2016 and 2015, respectively.

4. LONG-TERM DEBT

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

Bonds and Notes	**2016**	**2015**
Kentucky Infrastructure Authority Loan - $244,590 and restructured to $155,000, dated 4/28/98 and restructured 08/01/04 with payments through 2017, bearing interest at rates from 3.1% - 5.25%.	$ 7,500	$ 22,500
USDA, Rural Development Bond - $195,000, dated 2/22/07 with payments through 2042, bearing interest at a rate of 4.125%.	169,200	172,300
USDA, Rural Development Bond - $100,000, dated 2/22/07 with payments through 2044, bearing interest at a rate of 4.125%.	86,900	88,500
Kentucky Infrastructure Authority Loan - $160,000 Dated 2/22/07 with payments through 2044, bearing interest at a rate of 4.125%.	141,202	147,640
Kentucky Rural Water Finance Corp. Bond - $895,000, dated 2/19/15 with payments through 2041, bearing interest at 2.25 – 3.625%.	830,000	830,000
	1,234,802	1,260,940
Less: current portion of debt	(83,917)	(91,138)
Long-term debt	$ 1,150,885	$ 1,169,802

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

Year Ending December 31,	**Principle**	**Interest**	**Payment**
2017	$ 83,917	$ 37,460	$ 121,377
2018	76,900	36,245	113,145
2019	77,288	34,279	111,567
2020	82,781	32,348	115,129
2021	83,080	32,348	115,428
2022-2026	377,781	112,030	489,811
2027-2031	136,347	73,665	210,012
2032-2036	135,008	49,741	184,749
2037-2041	136,600	24,481	161,081
2042-2044	45,100	3,987	49,087
	$ 1,234,802	$ 436,584	$ 1,671,386

4. 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	$ 524,772	$ -	$ (63,430)	$ 461,342	$ -
Long-term debt	1,260,940	-	(26,138)	1,234,802	83,917
	$ 1,785,712	$ -	$ (89,568)	$ 1,696,144	$ 83,917

5. COMPLIANCE WITH BOND RESOLUTIONS

The bond resolution requires the District to maintain certain reserves as follows:

Reserve Fund – This reserve is to receive a monthly transfer of $483 until a balance of $58,000 is accumulated for all bond issues. In addition, this reserve is to receive all proceeds collected from potential customers to aid construction of extensions and any insurance proceeds from property damage. Funds may be used only for the purpose of paying the cost of unusual or extraordinary maintenance and repairs not included in the budget and cost of constructing extensions or improvements to the system. The Reserve Fund balance totaled $228,261 and $227,844 at December 31, 2016 and 2015.

Bond and Interest Sinking Fund – This reserve is to receive a monthly transfer of 1/12 of the next interest due and 1/12 of the next principal due. In addition, this reserve is to receive any excess revenues at the close of each year after provision of anticipated operating expenses for a two-month period. This reserve can only be used to pay debt service on the bond issues. The Bond and Interest Sinking Fund balances totaled $268,505 and $248,890 at December 31, 2016 and 2015.

Maintenance and Replacement Reserve – This reserve is to receive an amount equal to ten percent of the amount of loan payments until the amount on deposit is equal to five percent of the original principal amount of the loan. Funds may be used for extraordinary maintenance expenses related to the water tank painting project or for the costs of replacing worn or obsolete portions of the project. At December 31, 2016 and 2015 the required balance in this reserve was $1,200 and $800, and the Maintenance and Replacement Reserve totaled $1,200 and $800.

6. LEASE COMMITMENTS

The District leases office equipment under a non-cancellable operating lease agreement. Rental expense for the years ended December 31, 2016 and 2015 was $2,093 and $1,665. Future minimum lease payments including applicable taxes and fees for operating leases at December 31, 2016 are expected to total $258 in the year of 2017.

7. RETIREMENT PLAN

The East Pendleton County Water 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.

7. RETIREMENT PLAN (CONTINUED)

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 proved 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.

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 5.00% 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 $37,906 for the year ended December 31, 2016, or 100% of the required contribution. The contribution was allocated $28,028 to the CERS pension fund and $9,878 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	Before September 1, 2008
	Unreduced retirement	27 years service or 65 years old
	Reduced retirement	At least 5 years service and 55 years old or at least 25 years service and any age
Tier 2	Participation date	September 1, 2008 - December 31, 2013
	Unreduced retirement	At least 5 years service and 65 years old or age 57+ and sum of service years plus age equal 87
	Reduced retirement	At least 10 years service and 60 years old
Tier 3	Participation date	After December 31, 2013
	Unreduced retirement	At least 5 years service and 65 years old or age 57+ and sum of service years plus age equal 87
	Reduced retirement	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.

7. RETIREMENT PLAN (CONTINUED)

Pension Liabilities, Expense, Deferred Outflows of Resources and Deferred Inflows of Resources – At December 31, 2016, the District reported a liability of $461,342 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's 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 .009370%, which was a decrease of .002835% from its proportion measured as of June 30, 2015.

For the year ended December 31, 2016, the District recognized pension expense of $23,748. At December 31, 2016, the District reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

	Deferred Outflows of Resources	Deferred Inflows of Resources
Differences between expected and actual results	$ 2,014	$ -
Changes of assumptions	24,439	-
Net difference between projected and actual earnings on Plan investments	43,371	-
Changes in proportion and differences between Company contributions and proportionate share of contributions	-	87,430
Company contributions subsequent to the measurement date	17,186	-
Total	$ 87,010	$ 87,430

The $17,186 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:

Year ending December 31,	
2017	$ (12,081)
2018	(19,678)
2019	4,926
2020	9,227

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.

7. RETIREMENT PLAN (CONTINUED)

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.

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:

Asset Class	Target Allocation	Long-term Nominal Real Rate of Return
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	2%	-.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:

	Discount rate	District's proportionate share of net pension liability
1% decrease	6.50%	$ 363,999
Current discount rate	7.50%	$ 461,342
1% increase	8.50%	$ 574,915

7. RETIREMENT PLAN (CONTINUED)

Payable to the Pension Plan – At December 31, 2016 and 2015, the District reported a payable of $6,217 and $5,797 for the outstanding amount of contributions to the pension plan required for the year ended, respectively. 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.

REQUIRED SUPPLEMENTARY INFORMATION

EAST PENDLETON COUNTY WATER DISTRICT
REQUIRED SUPPLEMENTARY SCHEDULE OF
PROPORTIONATE SHARE OF THE NET PENSION LIABILITY
Last Three Fiscal Years

	2014	2015	2016
District's proportion of the net pension liability	0.012943%	0.012205%	0.009370%
District's proportionate share of the net pension liability (asset)	$ 420,000	$ 524,772	$ 461,342
District's covered employee payroll	$ 301,368	$ 239,531	$ 210,496
District's share of the net pension liability (asset) as a percentage of its covered employee payroll	139.36%	219.08%	219.17%
Plan fiduciary net position as a percentage of the total pension liability	66.80%	59.97%	55.50%

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.

EAST PENDLETON COUNTY WATER DISTRICT
REQUIRED SUPPLEMENTARY SCHEDULE OF CONTRIBUTIONS
Last Four Fiscal Years

	2013	2014	2015	2016
Contractually required employer contribution	$ 36,629	$ 40,040	$ 30,001	$ 28,028
Contributions relative to contractually required employer contribution	36,629	40,040	30,001	28,028
Contribution deficiency (excess)	$ -	$ -	$ -	$ -
District's covered employee payroll	$ 295,298	$ 301,368	$ 239,531	$ 210,496
Employer contributions as a percentage of covered-employee payroll	12.40%	13.29%	12.52%	13.32%

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.

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

To the Board of Commissioners
East Pendleton County Water District
Falmouth, 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 East Pendleton County Water 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, and have issued our report thereon dated June 27, 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 responses that we consider to be a material weakness (2016-001).

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the East Pendleton 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*.

East Pendleton County Water District's Response to Findings

The District's response to the findings identified in our audit is described in the accompanying schedule of findings and responses. The 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 27, 2017

FINDING 2016-001 (recurring)

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

CAUSE:
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.

RECOMMENDATION:
We recommend management review the costs and benefits involved to retain a consultant with the required expertise to prepare the financial statements and ensure compliance with generally accepted accounting principles.

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