

**HENRY COUNTY WATER DISTRICT #2**  
**BASIC FINANCIAL STATEMENTS**  
**AND INDEPENDENT AUDITOR'S REPORTS**  
**At December 31, 2014 and 2013**

**HENRY COUNTY WATER DISTRICT #2  
BASIC FINANCIAL STATEMENTS  
AND INDEPENDENT AUDITOR'S REPORTS**

**Years Ended December 31, 2014 and 2013**

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# RAISOR, ZAPP & WOODS, PSC

## Certified Public Accountants

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### INDEPENDENT AUDITOR'S REPORT

To the Commissioners of the  
Henry County Water District #2  
Campbellsburg, Kentucky 40011

#### Report on the Financial Statements

We have audited the accompanying financial statements of Henry County Water District #2 as of and for the years ended December 31, 2014 and 2013, and the related notes to the financial statements, which collectively comprise the Henry County Water District #2's basic financial statements as listed in the table of contents.

#### *Management's Responsibility for the Financial Statements*

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

#### *Auditor's Responsibility*

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

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

#### *Opinion*

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Henry County Water District #2, as of December 31, 2014 and 2013, 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*

Management has omitted the management's 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 Information*

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Henry County Water District #2's basic financial statements. The *schedule of expenditures of federal awards* is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is not a required part of the basic financial statements.

The schedule of expenditures of federal awards is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the schedule of expenditures of federal awards is fairly stated in all material respects in relation to the basic financial statements as a whole.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated March 9, 2015, on our consideration of the Henry County Water District #2'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 Henry County Water District #2's internal control over financial reporting and compliance.

*Raisor, Zapp & Woods, PSC*

RAISOR, ZAPP & WOODS, PSC  
Certified Public Accountants  
Carrollton, Kentucky

March 9, 2015

HENRY COUNTY WATER DISTRICT #2  
STATEMENT OF NET POSITION  
December 31, 2014 and 2013

ASSETS	2014	2013
<b>Current Assets:</b>		
Cash, Including Time Deposits	\$ 178,833	\$ 364,933
Accrued Interest Receivable	83	93
Accounts Receivable (Net)	393,082	439,451
Inventory	104,773	118,324
Prepaid Expense	30,014	27,202
Total Current Assets	<u>\$ 706,785</u>	<u>\$ 950,003</u>
<b>Noncurrent Assets:</b>		
<b>Restricted Assets:</b>		
Cash, Including Time Deposits	\$ 2,339,649	\$ 1,722,324
Accrued Interest Receivable	1,107	1,915
Capital Assets (Net)	15,232,458	13,820,445
Total Noncurrent Assets	<u>\$ 17,573,214</u>	<u>\$ 15,544,684</u>
<b>Total Assets</b>	<u>\$ 18,279,999</u>	<u>\$ 16,494,687</u>
<b>DEFERRED OUTFLOWS OF RESOURCES</b>		
Deferred Loss - Early Debt Retirement	<u>\$ 246,375</u>	<u>\$ 263,465</u>
<b>LIABILITIES</b>		
<b>Current Liabilities:</b>		
Accounts Payable	\$ 74,089	\$ 52,410
Accounts Payable - Construction	10,145	31,510
Retainage Payable	-	283,589
Accrued Compensated Absences	26,778	45,656
Accrued Salaries, Wages & Benefits	44,268	40,375
Accrued Payroll Taxes/Employee Withholding	26,903	16,059
Utility Tax Payable	6,745	7,556
Sales Tax Payable	520	435
<b>Current Liabilities Payable from Restricted Assets:</b>		
Accrued Interest Payable - Customer Deposits	184	303
Accrued Interest - Notes Payable	3,200	-
Revenue Bonds Payable	470,000	455,000
Notes Payable	156,827	-
Total Current Liabilities	<u>\$ 819,659</u>	<u>\$ 932,893</u>
<b>Noncurrent Liabilities:</b>		
Revenue Bonds Payable (Net of Unamortized Bond Discount & Premium of \$5,140 for 2014 and \$5,524 for 2013)	\$ 6,360,140	\$ 6,830,524
Notes Payable	2,190,739	-
<b>Noncurrent Liabilities Payable from Restricted Assets:</b>		
Customer Deposits Payable	71,725	73,550
Total Noncurrent Liabilities	<u>\$ 8,622,604</u>	<u>\$ 6,904,074</u>
<b>Total Liabilities</b>	<u>\$ 9,442,263</u>	<u>\$ 7,836,967</u>
<b>DEFERRED INFLOWS OF RESOURCES</b>		
Funds Held for Future Lines	<u>\$ 31,400</u>	<u>\$ -</u>
<b>NET POSITION</b>		
Net Investment in Capital Assets	\$ 6,490,983	\$ 6,483,287
Restricted for Capital Projects	823,909	451,876
Restricted for Debt Service	1,347,396	1,133,113
Unrestricted	390,423	852,909
<b>Total Net Position</b>	<u>\$ 9,052,711</u>	<u>\$ 8,921,185</u>

HENRY COUNTY WATER DISTRICT #2  
STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN FUND NET POSITION  
For the Years Ended December 31, 2014 and 2013

Operating Revenues:	2014	2013
Charges for Services:		
Water Charges (Net of Estimated Bad Debts)	\$ 2,949,020	\$ 2,939,215
Wholesale Water Charges	232,741	230,355
Total Charges for Services	<u>\$ 3,181,761</u>	<u>\$ 3,169,570</u>
Other Charges and Miscellaneous:		
Reconnect and Disconnect Charges	\$ 33,040	\$ 28,297
Forfeited Discounts	83,096	84,993
Miscellaneous	29,280	18,907
Total Other Charges and Miscellaneous	<u>\$ 145,416</u>	<u>\$ 132,197</u>
Total Operating Revenues	<u>\$ 3,327,177</u>	<u>\$ 3,301,767</u>
Operating Expenses:		
Accounting and Collecting Labor	\$ 108,702	\$ 121,004
Chemicals	79,449	70,169
Commissioner Salaries	32,700	24,525
Continuing Education	3,306	5,431
Contractual Services-Maintenance of Mains/Distribution System	22,281	46,009
Dues	4,031	4,532
Insurance	44,297	46,136
Maintenance of Mains/Distribution System Expenses	296,490	196,158
Miscellaneous	6,469	5,285
Office Supplies and Expense	64,416	79,225
Operating Labor	624,704	595,743
Other Interest Expense	345	549
Payroll Taxes	60,839	60,104
Professional Services	62,588	50,681
Purchased Power	411,664	400,068
Regulatory Fees	6,461	6,557
Retirement Expense & Employee Benefits	326,773	315,376
Transportation Expense	27,895	23,093
Utilities	26,610	28,495
Depreciation Expense	803,110	791,267
Total Operating Expenses	<u>\$ 3,013,130</u>	<u>\$ 2,870,407</u>
Net Operating Income	<u>\$ 314,047</u>	<u>\$ 431,360</u>
Nonoperating Revenue (Expense):		
Investment Income	\$ 10,492	\$ 14,514
Interest Expense	(291,032)	(290,925)
Bond Issuance Costs	-	(61,389)
Gain (Loss) on Sale/Abandonment of Fixed Assets	(5,629)	(366)
Total Nonoperating Revenue (Expense)	<u>\$ (286,169)</u>	<u>\$ (338,166)</u>
Income (Loss) Before Contributions	\$ 27,878	\$ 93,194
Capital Contributions	<u>103,648</u>	<u>73,460</u>
Change in Net Position	\$ 131,526	\$ 166,654
Net Position--Beginning of Year	<u>8,921,185</u>	<u>8,754,531</u>
Net Position--End of Year	<u>\$ 9,052,711</u>	<u>\$ 8,921,185</u>

See accompanying notes to the basic financial statements.

**HENRY COUNTY WATER DISTRICT #2**  
**STATEMENT OF CASH FLOWS**  
For the Years Ended December 31, 2014 and 2013

	<u>2014</u>	<u>2013</u>
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Receipts from Customers	\$ 3,371,721	\$ 3,317,962
Payments to Suppliers	(1,461,827)	(1,240,250)
Payments to Employees	(781,091)	(721,389)
Other Receipts (Payments)	42,354	2,362
Net Cash Provided (Used) by Operating Activities	<u>\$ 1,171,157</u>	<u>\$ 1,358,685</u>
<b>CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES</b>		
Purchase of Capital Assets (Including Work In Process)	\$ (2,511,671)	\$ (653,715)
Principal Paid on Capital Debt	(460,475)	(3,158,000)
Interest Paid on Capital Debt	(271,125)	(291,309)
Note Proceeds	2,353,041	-
Bond Proceeds	-	2,749,277
Capital Contributions	135,048	66,460
Proceeds Sale of Capital Asset	3,940	13,751
Bond Issuance Costs	-	(61,389)
Net Cash Provided (Used) by Capital and Related Financing Activities	<u>\$ (751,242)</u>	<u>\$ (1,334,925)</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Interest Received	\$ 11,310	\$ 17,513
Net Cash Provided (Used) by Investing Activities	<u>\$ 11,310</u>	<u>\$ 17,513</u>
 Net Increase (Decrease) in Cash and Cash Equivalents	 \$ 431,225	 \$ 41,273
 Balances-Beginning of the Year	 <u>977,222</u>	 <u>935,949</u>
 Balances-End of the Year	 <u><u>\$ 1,408,447</u></u>	 <u><u>\$ 977,222</u></u>

	Balances Per December 31, 2014 Statement of Net Position	Balances Per December 31, 2014 Statement of Cash Flows
Cash	\$ 78,833	\$ 78,833
Certificates of Deposit	100,000	-
Restricted Cash	1,329,614	1,329,614
Restricted Certificates of Deposit	1,010,035	-
Total Cash and Cash Equivalents, End of Year	<u>\$ 2,518,482</u>	<u>\$ 1,408,447</u>

	Restated Balances Per December 31, 2013 Statement of Net Position	Restated Balances Per December 31, 2013 Statement of Cash Flows
Cash	\$ 54,898	\$ 54,898
Certificates of Deposit	310,035	-
Restricted Cash	922,324	922,324
Restricted Certificates of Deposit	800,000	-
Total Cash and Cash Equivalents, End of Year	<u>\$ 2,087,257</u>	<u>\$ 977,222</u>

(Continued)

**HENRY COUNTY WATER DISTRICT #2**  
**STATEMENT OF CASH FLOWS**  
For the Years Ended December 31, 2014 and 2013

	<u>2014</u>	<u>2013</u>
<b>RECONCILIATION OF OPERATING INCOME (LOSS) TO NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES</b>		
Operating Income (Loss)	\$ 314,047	\$ 431,360
Adjustments to Reconcile Operating Income to Net Cash Provided (Used) by Operating Activities:		
Cash Flows Reported in Other Categories:		
Depreciation Expense	803,110	791,267
Change in Assets and Liabilities:		
Receivables, Net	46,369	9,131
Other Receivables	-	774
Inventories	13,551	117,385
Prepaid Expenses	(2,812)	3,488
Accounts Payable	3,703	721
Accrued Expenses	(4,867)	(1,852)
Customer Meter Deposits Payable	(1,944)	6,411
<b>Net Cash Provided by Operating Activities</b>	<u><u>\$ 1,171,157</u></u>	<u><u>\$ 1,358,685</u></u>

**SCHEDULE OF NONCASH INVESTING, CAPITAL, AND FINANCING ACTIVITIES**

At December 31, 2014 and 2013, Henry County Water District #2 had \$10,145 and \$315,099 of capitalized expenditures for construction in accounts payable and retainage payable on the Statement of Net Position. At December 31, 2014, Henry County Water District #2 had \$17,976 of capital assets in accounts payable on the Statement of Net Position.



**HENRY COUNTY WATER DISTRICT #2**  
**NOTES TO BASIC FINANCIAL STATEMENTS**  
**December 31, 2014 and 2013**

**NOTE 1 – DESCRIPTION OF ENTITY AND SIGNIFICANT ACCOUNTING POLICIES**

Description of entity: Henry County Water District #2 is a rural water company serving approximately 6,300 customers in the Kentucky counties of Henry, Trimble, Carroll, Oldham and Shelby, and is regulated by the Public Service Commission of the Commonwealth of Kentucky. The water district was formed under the laws of Henry County through its Fiscal Court and began operations in 1965.

In evaluating how to define Henry County Water District #2 for financial reporting purposes, management has considered all potential component units. The decision to include a potential component unit in the reporting entity was made by applying the criteria set forth in GAAP. The basic – but not the only – criterion for including a potential component unit within the reporting entity is the governing body's ability to exercise oversight responsibility. The most significant manifestation of this ability is financial interdependency. Other manifestations of the ability to exercise oversight responsibility include, but are not limited to, the selection of governing authority, the designation of management, the ability to significantly influence operations and accountability for fiscal matters. The other criterion used to evaluate potential component units for inclusion or exclusion from the reporting entity is the existence of special financing relationships, regardless of whether the District is able to exercise oversight responsibilities. Based upon the application of these criteria, the District has no component units.

A summary of the District's significant accounting policies follows:

**Basis of presentation and accounting:** As stated in Kentucky Revised Statutes (KRS) 278.015, "any water district shall be a public utility and shall be subject to the jurisdiction of the Public Service Commission." In KRS 278.220, it is outlined that the Public Service Commission may establish a system of accounts to be kept by the utilities subject to its jurisdiction, and may prescribe the manner in which such accounts shall be kept. The financial statements of the District are prepared in accordance with generally accepted accounting principles (GAAP). The District applies all relevant Governmental Accounting Standards Board (GASB) pronouncements.

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

Proprietary funds utilize the accrual basis of accounting. Under the accrual basis of accounting, revenues are recognized when earned and expenses are recorded when the liability is incurred or economic asset used.

The accounting and financial reporting treatment applied to the District is determined by its measurement focus. The transactions of the District are accounted for on a flow of economic resources measurement focus. The accounting objectives of this measurement focus are the determination of operating income, changes in net position (or cost recovery), financial position, and cash flows. With this measurement focus, all assets and all liabilities associated with the operations are included on the statement of net position. Net position (total assets plus deferred outflows net of total liabilities and deferred inflows) is segregated into net investment in capital assets, restricted; and unrestricted components.

**Revenues and expenses:** Operating revenues and expenses consist of those revenues and expenses that result from the ongoing principal operations of the District. Operating revenues consist primarily of charges for services. Non-operating revenues and expenses consist of those revenues and expenses that are related to financing and investing types of activities and result from nonexchange transactions or ancillary activities.

**Debt Issuance Costs:** Debt issuance Costs are expensed when incurred.

HENRY COUNTY WATER DISTRICT #2  
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)  
December 31, 2014 and 2013

**NOTE 1 – DESCRIPTION OF ENTITY AND SIGNIFICANT ACCOUNTING POLICIES (Continued)**

The District adheres to the use restrictions established by Bond Agreements when expenses are incurred for which both restricted and unrestricted net position is available. The District has no policy defining which resources (restricted or unrestricted) to use first.

**Property and equipment:** Property and equipment purchased or constructed is stated at cost. The District's policy is to capitalize asset purchases exceeding \$500 for office equipment and \$1,000 for service equipment. The cost of meters, including installation, is recorded at the Public Service Commission approved charge of \$1,120. Interest related to costs, and major improvements, renewals and replacements is capitalized as a cost of the project. Depreciation is computed on the straight-line basis over the estimated useful lives of the related assets. The range of estimated useful lives by type of asset is as follows:

- Structures & Improvements	7-60 years
- Distribution System	7-40 years
- Machinery & Equipment	3-25 years

Construction in process represents costs related to various water line extensions being installed by District employees, as well as system improvements. Expenses for maintenance and repairs that do not increase the useful life of the asset are charged to operations as they are incurred.

**Inventory:** Inventories of supplies are valued at the lower of cost or market on a first-in, first-out basis.

**Bond Discount and Premium:** The bond discount and premium are amortized over the life of the bonds.

**Debt Issuance Costs:** Such costs are expensed as incurred.

**Compensated Absences:** See Note 10 for the District's policy on vacation and sick pay.

**Income Taxes:** The Henry County Water District #2 is not subject to income taxes.

**Contributed Capital:** Under the Governmental Accounting Standards Board's (GASB) Statement No. 33, *Accounting and Financial Reporting for Nonexchange Transactions*, the District recognizes capital contributions as revenues, in the statement of revenues, expenses, and changes in fund net position. Capital contributions include donated property, impact fees, tap on fees and grants. Tap on fees and impact fees of \$103,468 and \$73,460 were received by the District for the years ended December 31, 2014 and 2013, respectively.

**Net Position:** Net position comprises the various net earnings from operating and non-operating revenues, expenses, and contributions of capital. Net position is classified in the following three components: net investment in capital assets, restricted, and unrestricted net position. Net investment in capital assets consists of all capital assets, net of accumulated depreciation and reduced by outstanding debt that is attributable to the acquisition, construction and improvement of those assets; debt related to unspent proceeds or other restricted cash and investments is excluded from the determination. Restricted net position consists of net position for which constraints are placed thereon by external parties, such as lenders, grantors, contributors, laws, regulations and enabling legislation, including self-imposed legal mandates. Unrestricted net position consists of all other net position not included in the above categories.

**Deferred Outflows and Deferred Inflows:** Deferred Outflows of Resources and Deferred Inflows of Resources are not assets or liabilities; revenues or expenses. Rather, they represent resources or the use of resources related to future periods.

**Estimates:** The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

**Statement of Cash Flows:** For the purpose of the Statement of Cash Flows, Henry County Water District #2 considers all highly liquid investments (including restricted assets) with a maturity of three months or less when purchased to be cash equivalents.

**HENRY COUNTY WATER DISTRICT #2**  
**NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)**  
**December 31, 2014 and 2013**

**NOTE 2 – DEBT RESTRICTIONS AND COVENANTS**

The Bond and Interest Sinking Account was established with the original bond issue. Under the bond resolution which established this account, it was provided that a minimum balance be maintained in this account as security to the bondholders. In order to attain the minimum balance, the monthly transfer to be made into the account for the outstanding bond issues is as follows:

	one sixth (1/6) of the next semiannual interest payment
+	one twelfth (1/12) of next annual principal payment
=	monthly transfer

The transfers and/or segregated deposits were sufficient to meet the total obligation outstanding on all issues at December 31, 2014 and 2013. During calendar year 2014 and 2013 all transfers were made timely as appropriate.

Upon the issuance of the original bonds, a Depreciation Account was established to provide funds for extraordinary repairs and extensions to the system and/or make up any deficiency in the Bond and Interest Sinking Account. After monthly deposits are made into the Bond and Interest Account, monthly transfers are required to be made to the Depreciation Account. The 1996 Bond Resolution (which was refinanced with the 2003 Bond Issue) required a monthly transfer of \$3,845 to accumulate to a balance of \$461,400. The 2001, 2003, 2010 and 2013 Bond Resolutions ratify and confirm the creation of the 1996 Depreciation Fund. The Kentucky Infrastructure Authority Note requires the establishment of a replacement reserve account. The KIA note requires an annual transfer of \$7,100 to accumulate to a balance of \$71,000. At December 31, 2014 and 2013, the Depreciation Account was fully funded.

**NOTE 3 – CASH AND INVESTMENTS**

KRS 66.480 authorizes the District to invest in obligations of the United States and its agencies and instrumentalities including repurchase agreements, through sources including national and state banks chartered in Kentucky, obligations and contracts for future delivery backed by the full faith of the United States or its Agency, certificates of deposit and interest bearing accounts in institutions insured by the Federal Depository Insurance Corporation and other investments described therein provided that approved securities are pledged to secure those funds on deposit in an amount equal to the amount of those funds. The District may also invest in mutual funds meeting the requirements of the statute.

**Custodial Credit Risk**

Custodial credit risk for deposits is the risk that in the event of a bank failure, the District's deposits may not be returned to it. As of December 31, 2014, and 2013 in accordance with District policy, \$1,550,719 and \$1,350,625 respectively, of the District's deposits were covered by federal depository insurance and \$1,580,709 and \$1,333,808, respectively, were collateralized by securities held by the pledging financial institution's agent or trust department in the District's name. Thus, the district had no deposits that were exposed to custodial credit risk.

Henry County Water District #2's policies regarding deposits of cash are discussed above. 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, 2014 and 2013. The categories of credit risk are defined as follows:

Category 1 – Insured by FDIC or collateralized with a depository surety bond or securities held by the District (public trust) or by its agent in its name.

Category 2 – Uninsured but collateralized with securities held by the pledging financial institution's trust department or agent in the District's name.

Category 3 – Uninsured and uncollateralized; or collateralized with securities held by the pledging financial institution, or by its trust department or agent but not in the District's name; or collateralized with no written or approved collateral agreement.

**HENRY COUNTY WATER DISTRICT #2**  
**NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)**  
December 31, 2014 and 2013

**NOTE 3 – CASH AND INVESTMENTS (Continued)**

**December 31, 2014**

Type of Deposits	Total Bank Balance	Custody Credit Risk Category			Total Carrying Value
		1	2	3	
Demand Deposits	\$ 200,028	\$ 200,028	\$ -	\$ -	\$ 200,028
Time & Savings	2,931,400	1,350,691	1,580,709	-	2,317,954
Total Deposits	<u>\$ 3,131,428</u>	<u>\$ 1,550,719</u>	<u>\$ 1,580,709</u>	<u>\$ -</u>	<u>\$ 2,517,982</u>

**December 31, 2013**

Type of Deposits	Total Bank Balance	Custody Credit Risk Category			Total Carrying Value
		1	2	3	
Demand Deposits	\$ 65	\$ 65	\$ -	\$ -	\$ 65
Time & Savings	2,684,368	1,350,560	1,333,808	-	2,086,692
Total Deposits	<u>\$ 2,684,433</u>	<u>\$ 1,350,625</u>	<u>\$ 1,333,808</u>	<u>\$ -</u>	<u>\$ 2,086,757</u>

**Reconciliation to Statement of Net Position:**

	<u>December 31, 2014</u>	<u>December 31, 2013</u>
Unrestricted Cash, Including Time Deposits	\$ 178,833	\$ 364,933
Restricted Cash, Including Time Deposits	2,339,649	1,722,324
Less Cash on Hand	(500)	(500)
	<u>\$ 2,517,982</u>	<u>\$ 2,086,757</u>

**NOTE 4 – RESTRICTED ASSETS**

Restricted cash and time deposits consist of the following:

	<u>December 31, 2014</u>	<u>December 31, 2013</u>
Bond and Interest Sinking Account	\$ 531,058	\$ 524,480
Debt Covenant	210,035	-
Depreciation Account	608,396	606,718
Customer Deposits & Impact Charge Escrow	166,251	139,250
Construction Account	823,909	451,876
Total	<u>\$ 2,339,649</u>	<u>\$ 1,722,324</u>

Restricted receivables consist of the following:

	<u>December 31, 2014</u>	<u>December 31, 2013</u>
Interest Receivable	\$ 1,107	\$ 1,915
	<u>\$ 1,107</u>	<u>\$ 1,915</u>

**NOTE 5 – CUSTOMER ACCOUNTS RECEIVABLE**

Customer Accounts Receivable has been netted with an Allowance for Bad Debts of \$54,640 and \$48,096 at December 31, 2014 and 2013, respectively. The amount provided for bad debts represents the portion of the total amounts for which collection is unlikely, based on historical collection data.

Estimated unbilled water service revenue of \$123,440 and \$159,938 is included in accounts receivable at December 31, 2014 and 2013, respectively.

**HENRY COUNTY WATER DISTRICT #2**  
**NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)**  
**December 31, 2014 and 2013**

**NOTE 6 – CAPITAL ASSETS**

Capital asset activity for the years ended December 31, 2014 and 2013, was as follows:

	Balance at January 1, 2014	Additions	Disposals	Balance at December 31, 2014
Land & Land Rights	\$ 176,617	\$ -	\$ -	\$ 176,617
Structures & Improvements	24,207,319	2,401,978	-	26,609,297
Distribution System	2,484,196	34,235	(35,621)	2,482,810
Machinery & Equipment	1,253,797	171,670	-	1,425,467
Construction in Process	458,243	2,018,787	(2,401,978)	75,052
Totals at Historical Cost	<u>\$ 28,580,172</u>	<u>\$ 4,626,670</u>	<u>\$ (2,437,599)</u>	<u>\$ 30,769,243</u>
Less: Accumulated Depreciation				
Structures & Improvements	\$ (12,549,873)	\$ (674,970)	\$ -	\$ (13,224,843)
Distribution System	(1,286,184)	(53,952)	26,052	(1,314,084)
Machinery & Equipment	(923,670)	(74,188)	-	(997,858)
Total Accumulated Depreciation	<u>\$ (14,759,727)</u>	<u>\$ (803,110)</u>	<u>\$ 26,052</u>	<u>\$ (15,536,785)</u>
Capital Assets, Net	<u>\$ 13,820,445</u>	<u>\$ 3,823,560</u>	<u>\$ (2,411,547)</u>	<u>\$ 15,232,458</u>

  

	Balance at January 1, 2013	Additions	Disposals	Balance at December 31, 2013
Land & Land Rights	\$ 176,617	\$ -	\$ -	\$ 176,617
Structures & Improvements	24,125,763	81,556	-	24,207,319
Distribution System	2,754,831	341,251	(611,886)	2,484,196
Machinery & Equipment	1,132,599	121,198	-	1,253,797
Construction in Process	35,434	504,365	(81,556)	458,243
Totals at Historical Costs	<u>\$ 28,225,244</u>	<u>\$ 1,048,370</u>	<u>\$ (693,442)</u>	<u>\$ 28,580,172</u>
Less: Accumulated Depreciation				
Structures & Improvements	\$ (11,874,963)	\$ (674,910)	\$ -	\$ (12,549,873)
Distribution System	(1,828,317)	(55,636)	597,769	(1,286,184)
Machinery & Equipment	(862,949)	(60,721)	-	(923,670)
Totals Accumulated Depreciation	<u>\$ (14,566,229)</u>	<u>\$ (791,267)</u>	<u>\$ 597,769</u>	<u>\$ (14,759,727)</u>
Capital Assets, Net	<u>\$ 13,659,015</u>	<u>\$ 257,103</u>	<u>\$ (95,673)</u>	<u>\$ 13,820,445</u>

Included under the District's capital assets were \$4,433,513 and \$4,104,621 of fully depreciated assets, at December 31, 2014 and 2013, respectively. Land and land rights and construction in process are capital assets not being depreciated.

Depreciation expense aggregated \$803,110 and \$791,267 in 2014 and 2013, respectively.

**NOTE 7 – CUSTOMER DEPOSITS/ESCROW**

Customer deposits are collected upon installation of water service. This amount is to be refunded to the customer upon discontinuation of service (after the customer's bill has been paid in full) or one year pending a satisfactory payment record. Deposits received from customers are held in an interest bearing account (which is included in the financial statements as restricted cash). Records are maintained which detail the accrued interest on each customer's deposit based on the current annual rate. Accrued interest is paid annually and when the deposit is refunded.

HENRY COUNTY WATER DISTRICT #2  
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)  
December 31, 2014 and 2013

**NOTE 8 – DEFERRED OUTFLOWS OF RESOURCES**

In 2013, Henry County Water District adopted GASB 65, *Items Previously Reported as Assets and Liabilities*. Under GASBS No. 65 a consumption of net position by the District that is applicable to a future period is reported as a deferred outflow of resources.

The following is a summary of the District's deferred outflows of resources:

	<u>December 31, 2014</u>	<u>December 31, 2013</u>
Difference between the reacquisition price and the net carrying amount of the old bond issues refunded.		
2010 Bond Issue	\$ 165,790	\$ 178,185
2013 Bond Issue	80,585	85,280
	<u>\$ 246,375</u>	<u>\$ 263,465</u>

**NOTE 9 – LONG-TERM DEBT**

As of December 31, 2014 and 2013, the long-term debt payable consisted of the following:

Notes Payable:

	<u>December 31, 2014</u>	<u>December 31, 2013</u>
Kentucky Infrastructure Authority represents a 20 year loan secured by water revenues. Interest is charged at 1.75% per annum. In addition, a loan servicing fee of 0.25% of the annual outstanding loan balance will be payable to the authority as part of each interest payment. Total draws on the loan were \$2,153,041. Semi-annual payments with final maturity December 1, 2034.	\$ 2,153,041	\$ -
2014 Shelby Energy Electric Cooperative Corporation Note, original loan amount of \$200,000, secured by two certificates of deposit owned by the District. Interest is charged at the rate of 1% per annum. Monthly payments with initial maturity at September 5, 2016 and automatic renewal through September 5, 2017.	194,525	-
Total Notes Payable	<u>\$ 2,347,566</u>	<u>\$ -</u>
Current Portion	\$ 156,827	\$ -
Noncurrent Portion	2,190,739	-
Total Notes Payable	<u>\$ 2,347,566</u>	<u>\$ -</u>

**HENRY COUNTY WATER DISTRICT #2**  
**NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)**  
December 31, 2014 and 2013

**NOTE 9 – LONG-TERM DEBT (Continued)**

**Bonds Payable:**

	<u>December 31, 2014</u>	<u>December 31, 2013</u>
2010 B Bond Issue, original issue amount of \$5,663,000, secured by water revenues. Interest is charged 3.20% to 4.33% per annum. Final maturity is January 1, 2028.	\$ 4,430,000	\$ 4,705,000
Kentucky Rural Water Finance Corporation Public Projects Refunding Revenue Bonds (Flexible Term Program) Series 2013B, original issue (District Share) \$2,760,000, secured by water revenues. Interest is charged at the rates of 2.30% - 3.5% per annum. Final maturity is February 1, 2032.	<u>2,395,000</u>	<u>2,575,000</u>
Total Bonds Payable	<u>\$ 6,825,000</u>	<u>\$ 7,280,000</u>
Current Portion	\$ 470,000	\$ 455,000
Noncurrent Portion	<u>6,355,000</u>	<u>6,825,000</u>
Total Bonds Payable	\$ 6,825,000	\$ 7,280,000
Unamortized Bond Premium	<u>5,140</u>	<u>5,524</u>
Total Bonds Payable Net of Unamortized Bond Premium and Discount	<u>\$ 6,830,140</u>	<u>\$ 7,285,524</u>

**Accrued Compensated Absences:**

Accrued Compensated Absences (All Current)	<u>\$ 26,778</u>	<u>\$ 45,656</u>
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**Kentucky Infrastructure Authority – Federally Assisted Drinking Water Revolving Loan Fund**

On October 6, 2014 Henry County Water District closed a loan in the amount of \$2,153,041 with Kentucky Infrastructure Authority secured by water revenues. Interest is charged at 1.75% per annum. In addition a loan servicing fee of 0.25% of the annual outstanding loan balance will be payable to the authority as part of each interest payment. Proceeds from this loan were used to install approximately 24,000 linear feet of water main. Final maturity is December 1, 2034.

**2014 Shelby Energy Electric Cooperative Corporation Note Payable**

The original balance of the Shelby Energy Electric Cooperative Corporation note payable was \$200,000. The note is payable in monthly installments of \$5,642 through September 5, 2016. The note shall, on September 5, 2016 be automatically renewed for an additional one year term ending on September 7, 2017. In the event the note is not renewed the entire unpaid balance shall be immediately due and owing on September 5, 2016. Interest is charged at 1% per annum. Also, Shelby Energy may charge on annual loan servicing charge that does not exceed 1% of the unpaid balance on the loan at the beginning of the year. The principal balance outstanding at December 31, 2014 was \$194,525.

**Kentucky Rural Water Finance Corporation Public Projects Revenue Bonds, Series 2010 B**

On May 13, 2010 Henry County Water District entered into a \$5,663,000 bond agreement with Kentucky Rural Water Finance Corporation. The proceeds of the bonds were used to refund the District's then outstanding Refunding Revenue Bonds, Series 1998 (principal, interest, and 1% redemption premium as required). Final maturity on the 2010 issue is January 1, 2028.

**HENRY COUNTY WATER DISTRICT #2**  
**NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)**  
**December 31, 2014 and 2013**

**NOTE 9 – LONG-TERM DEBT (Continued)**

**Bonds Payable Kentucky Rural Water Finance Corporation Flexible Term Finance Program Series 2013B**

On February 27, 2013, Henry County Water District #2 issued \$2,760,000, Series 2013B Kentucky Rural Water Finance Corporation Public Projects Refunding Revenue Bonds with interest rates of 2.30% - 3.55% to advance refund \$370,000 Series 2001D and \$2,333,000 Series 2003 revenue bonds outstanding. The 2001D Series was originally issued at 2.4% to 4.75% per annum. The 2003 Series was issued at 4.06% to 4.81% per annum. The refunded bonds were redeemed on February 27, 2013 at a price equal to 100% of the principal amounts of the refunded bonds outstanding at that date. Bond issuance costs were \$61,389.

As a result of the advance refunding, the District reduced its total debt service requirements by \$476,674, which resulted in an economic gain (difference between the present value of the debt service payments on the old and new debts) of \$356,023. Final maturity on the 2013 issue is February 1, 2032.

**Changes in Long-term Debt**

The following is a summary of changes in long-term debt for the years ended December 31, 2014 and 2013.

**December 31, 2014**

	Balance at January 1, 2014	Additions	Retirements	Balance at December 31, 2014	Current Portion
Notes Payable	\$ -	\$ 2,353,041	\$ 5,475	\$ 2,347,566	\$ 156,827
Bonds Payable	7,280,000	-	455,000	6,825,000	470,000
Accrued Compensated Absences	45,656	-	18,878	26,778	26,778
Total Enterprise Fund Debt	<u>\$ 7,325,656</u>	<u>\$ 2,353,041</u>	<u>\$ 479,353</u>	<u>\$ 9,199,344</u>	<u>\$ 653,605</u>

**December 31, 2013**

	Balance at January 1, 2013	Additions	Retirements	Balance at December 31, 2013	Current Portion
Bonds Payable	\$ 7,678,000	\$ 2,760,000	\$ 3,158,000	\$ 7,280,000	\$ 455,000
Accrued Compensated Absences	28,603	17,053	-	45,656	45,656
Total Enterprise Fund Debt	<u>\$ 7,706,603</u>	<u>\$ 2,777,053</u>	<u>\$ 3,158,000</u>	<u>\$ 7,325,656</u>	<u>\$ 500,656</u>

The annual requirements for all long-term debt outstanding at December 31, 2014, are as follows:

	Note Payable	Note Payable Interest	Service Fee	Bonds	Bond Interest	Trustee Fees	Total Principal, Interest, Trustee Fee and Servicing Fee
2015	\$ 156,827	\$ 38,926	\$ 5,326	\$ 470,000	\$ 244,526	\$ 900	\$ 916,505
2016	159,086	36,666	5,098	485,000	231,152	900	917,902
2017	155,739	34,373	4,866	495,000	217,342	900	908,220
2018	95,641	32,412	4,630	421,000	202,296	900	756,879
2019	97,322	30,731	4,390	442,000	188,189	900	763,532
2020-2024	512,881	127,386	18,199	2,495,000	680,690	4,500	3,838,656
2025-2029	559,567	80,701	11,530	1,712,000	204,069	3,600	2,571,467
2030-2034	610,503	29,763	4,251	305,000	16,142	900	966,559
	<u>\$ 2,347,566</u>	<u>\$ 410,958</u>	<u>\$ 58,290</u>	<u>\$ 6,825,000</u>	<u>\$ 1,984,406</u>	<u>\$ 13,500</u>	<u>\$ 11,639,720</u>



**HENRY COUNTY WATER DISTRICT #2**  
**NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)**  
**December 31, 2014 and 2013**

**NOTE 9 – LONG-TERM DEBT (Continued)**

The annual requirements for all long-term debt outstanding at December 31, 2013, are as follows:

Due	Bonds	Bond Interest	Total Principal and Interest
2014	\$ 455,000	\$ 258,366	\$ 713,366
2015	470,000	245,426	715,426
2016	485,000	232,052	717,052
2017	495,000	218,242	713,242
2018	421,000	203,196	624,196
2019-2023	2,394,000	775,779	3,169,779
2024-2028	2,110,000	290,294	2,400,294
2029-2032	450,000	32,917	482,917
	<u>\$ 7,280,000</u>	<u>\$ 2,256,272</u>	<u>\$ 9,536,272</u>

**NOTE 10 – COMPENSATED ABSENCES**

Vacation and sick pay are considered expenditures in the year earned.

**Vacation Days**

All full time employees earn one week of vacation time at the beginning of the first whole calendar year of employment and one additional day per year up to the maximum of four weeks. Only two weeks of unused vacation time may be carried over to the next year. If there is still any vacation leave remaining, the employee will be paid straight time for that portion not carried over in January of the following year. If an employee has accumulated vacation leave at time of retirement or resigning, he may have the option to use the leave time or receive payment at his/her regular rate. A terminated employee will be compensated for any accrued vacation time.

At December 31, 2014 and 2013, a liability for accrued vacation was recorded in the amount of \$26,778 and \$45,656, respectively.

**Sick and Personal Days**

All full time employees earn 1 sick day per month. An employee may carry over any sick leave accrued during the year that was not used, without limit. If and when the employee retires or resigns, there will be no pay for unused sick leave. Full time personnel earn 4 personal days per year with no carry-over or pay for any unused time.

At December 31, 2014 and 2013, the District had an unrecorded sick pay liability to its employees of \$131,813 and \$129,129, respectively. The estimated liabilities include required salary related payments.

**NOTE 11 – FUND EQUITY- RESTRICTED NET POSITION**

	December 31, 2014	December 31, 2013
Restricted for Capital Projects:		
Monies Reserved for Future System Improvements	\$ 823,909	\$ 451,876
Total Restricted for Capital Projects	<u>\$ 823,909</u>	<u>\$ 451,876</u>
Restricted for Debt Service:		
2010 and 2013 Bond Issues & KIA Note Payable		
Cash	\$ 1,139,454	\$ 1,131,198
Add: Accrued Interest Receivable	1,107	1,915
Less: Accrued Interest Payable	(3,200)	-
Total Restricted for Debt Service	<u>\$ 1,137,361</u>	<u>\$ 1,133,113</u>

**HENRY COUNTY WATER DISTRICT #2**  
**NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)**  
**December 31, 2014 and 2013**

**NOTE 12 – BAD DEBT EXPENSE**

Water revenue charges have been netted with an estimated bad debt expense of \$7,934 and \$7,916 at December 31, 2014 and 2013, respectively.

**NOTE 13 – INTEREST EXPENSE**

Interest expense incurred for the years ended December 31, 2014 and 2013 was \$291,377 and \$291,474, respectively. Capitalized interest in 2014 was \$4,043. No interest was capitalized in 2013.

**NOTE 14 – INSURANCE AND RELATED ACTIVITIES**

The District is exposed to various forms of loss of assets associated with the risks of fire, personal liability, theft, vehicular accidents, errors and omissions, fiduciary responsibility, etc. Each of these risks is covered through the purchase of commercial insurance. The District is also subject to the risks associated with employee injury. These risks are covered through premiums paid to Kentucky Employers' Mutual Insurance, a commercial insurance company.

**NOTE 15 – THE COUNTY EMPLOYEES' RETIREMENT SYSTEM**

Henry County Water District #2 participates in the Commonwealth of Kentucky's County Employees' Retirement System (CERS). Electing employees and all new employees of the District may participate in the System. The most recent financial report on CERS is included in the Kentucky Retirement System's annual report, June 30, 2014. The most recent financial report on CERS is included in the Kentucky Retirement System's annual report, June 30, 2014. Copies of this report will be distributed to each participating employer in the Kentucky Employees Retirement System, County Employees Retirement System, and State Police Retirement System. Copies will also be available to Legislative personnel and state libraries.

**Plan Description** – CERS is a cost-sharing multiple-employer defined benefit pension plan that covers substantially all regular full-time members employed in non-hazardous duty position of each participating county, city and school board, and any additional eligible local agencies electing to participate in CERS. 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. Prior to July 1, 2009, cost-of-living adjustments (COLAs) were provided annually equal to the percentage increase in the annual average of the consumer price index for all urban consumers for the most recent calendar year, not to exceed 5% in any plan year.

Effective July 1, 2009, and on July 1 of each year thereafter, the COLA is limited to 1.5% provided the recipient has been receiving a benefit for at least twelve months prior to the effective date of the COLA. If the recipient has been receiving a benefit for less than twelve months prior to the effective date of the COLA, the increase shall be reduced on a pro-rata basis for each month the recipient has not been receiving benefits in the twelve months preceding the effective date of the COLA. The Kentucky General Assembly reserves the right to suspend or reduce cost-of-living adjustments if, in its judgment, the welfare of the Commonwealth so demands. On July 1, 2013, the COLA was not granted.

**Contributions** - For the fiscal years ended June 30, 2014 and 2013, plan members who began participating prior to September 1, 2008, were required to contribute 5% of their annual creditable compensation. 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 preceding 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 bases adopted by the Board. For the fiscal years ended June 30, 2014 and 2013, participating employers contributed 18.89% and 19.55%, respectively, of each employer's creditable compensation. The actuarially determined rates set by the Board for the fiscal years ended June 30, 2014 and 2013, were 18.89% and 19.55%, respectively. Administrative costs of KRS are financed through employer contributions and investment earnings.

**HENRY COUNTY WATER DISTRICT #2**  
**NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)**  
**December 31, 2014 and 2013**

**NOTE 15 – THE COUNTY EMPLOYEES' RETIREMENT SYSTEM (Continued)**

In accordance with House Bill 1, signed by the Governor on June 27, 2008, plan members who began participating on, or after, September 1, 2008, were required to contribute a total of 6% of their annual creditable compensation. Five percent of the contribution was deposited to the member's account while the 1% was deposited to an account created for the payment of health insurance benefits under 26 USC Section 401(h) in the Pension Fund (see Kentucky Administrative Regulation 105 KAR 1:420E). Interest is paid each June 30 on members' accounts at a rate of 2.5%. If a member terminates employment and applies to take a refund, the member is entitled to a full refund of contributions and interest; however, the 1% contribution to the 401(h) account is non-refundable and is forfeited. For plan members who began participating prior to September 1, 2008, their contributions remain at 5% of their annual creditable compensation.

In accordance with Senate Bill 2, signed by the Governor on April 4, 2013, 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. Non-hazardous members contribute 5% of their annual creditable compensation and 1% to the health insurance fund which is not credited to the member's account and is not refundable. The employer contribution rate is set annually by the Board based on an actuarial valuation. The employer contributes a set percentage of the 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's total payroll for the year ended December 31, 2014 was \$810,739. Contributions were based on \$766,921 (eligible gross wages). The total pension expense for the year ended December 31, 2014 was \$140,535 and \$39,189 for the employer and employees, respectively. All contributions were made as required during the year ended December 31, 2014.

The District's total payroll for the year ended December 31, 2013 was \$776,894. Contributions were based on \$746,795 (eligible gross wages). The total pension expense for the year ended December 31, 2013 was \$143,614 and \$37,653 for the employer and employees, respectively. All contributions were made as required during this year. There have been no changes in the plan since inception.

The District's contribution for the year ended June 30, 2014 and 2013, was .037% and .039%, respectively, of the System's total contribution requirements for all employers.

For non-hazardous duty, the required contributions to the plan for all participating employees were as follows (\$ in thousands):

**County Employees Retirement System (CERS) – Pension Funds**

	<u>Annual Required Contributions</u>	<u>Actual Contributions</u>	<u>Actual Contributions as a Percentage of Covered Employee Payroll</u>
June 30, 2014	324,231	324,231	14.27%
June 30, 2013	294,914	294,914	13.19%
June 30, 2012	261,764	275,736	12.33%

**County Employees Retirement System (CERS) – Insurance Funds**

	<u>Annual Required Contributions</u>	<u>Actual Contributions</u>	<u>Actual Contributions as a Percentage of Covered Employee Payroll</u>
June 30, 2014	130,652	123,278	94.40%
June 30, 2013	195,561	159,993	81.80%
June 30, 2012	214,421	171,925	80.20%

**HENRY COUNTY WATER DISTRICT #2**  
**NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)**  
**December 31, 2014 and 2013**

**NOTE 15 – THE COUNTY EMPLOYEES' RETIREMENT SYSTEM (Continued)**

The Kentucky Retirement Systems Insurance Fund (Fund) was established to provide hospital and medical insurance for members receiving benefits from CERS. The Fund pays a prescribed contribution for whole or partial payment of required premiums to purchase hospital and medical insurance for current beneficiaries.

**NOTE 16 – ECONOMIC DEPENDENCY**

Henry County Water District #2 provides water services to residential and commercial customers in the Kentucky counties of Henry, Trimble, Carroll, Oldham and Shelby. The District also supplies water for resale to the cities of Eminence and New Castle located in Henry County. It should be noted that 7.3% and 7.1% of the total water charges for services revenue was received from these cities for the years ended December 31, 2014 and 2013, respectively. The wholesale rate is \$2.58 per 1,000 gallons. Also, the District supplies water for resale to West Carroll Water District at the same wholesale rate.

**NOTE 17 – FUNDS HELD FOR FUTURE LINES AND CONTRIBUTED CAPITAL – IMPACT FEES**

The District collects funds from developers for their allocable cost of line extensions. The amount is calculated based on the size of the line and the number of estimated hook-ups. As others pay to hook-up to the line, portions of these funds are refunded to the developer. Once a line has been completed, the developer's cost of the line is recorded as capital contributions from customers.

**NOTE 18 – COMMITMENTS, CONTINGENCIES AND SUBSEQUENT EVENTS**

The District has been approved for financing for a \$3.25 million water project. The U.S. Highway 42 Water Tank project involves constructing a new 1 million gallon composite storage tank on U.S. Highway 42 financed through Kentucky Infrastructure Authority, the State Revolving Fund, Shelby Energy Electric Cooperative Corporation, and local funds. TetraTech has been selected as the engineer for this project.

\$15,130 of construction costs and engineering fees relating to the Highway 42 Water Tank project have been capitalized as construction in process. \$29,700 of engineering fees relating to the Wellfield project have been capitalized as construction in process. The remaining \$30,222 is for line extensions.

**NOTE 20 – RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS**

In June 2012, the GASB issued Statement 68, *Accounting and Financial Reporting for Pensions – an Amendment of GASB Statement 27*. GASB 68 is effective for periods beginning after June 15, 2014. Under this statement governments will be required to report the net pension liability associated with its' employee's pension as a liability in their accrual-based financial statements (for example, the government-wide Statement of Net Position). A government has a present obligation to pay deferred benefits earned by its employees. "*Net Position Liability*" represents the government's obligation to pay deferred benefits when the total pension [plan's] liability exceeds the pension plan's net assets. This reporting requirement is an important change that will more clearly depict the government's financial position. While this information will, in some cases give the appearance that a government is financially weaker than it was previously, the financial reality of the government's situation will not have changed. Management is currently evaluating the impact of the adoption of this statement on the District's financial statements.

# RAISOR, ZAPP & WOODS, PSC

## Certified Public Accountants

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

To the Commissioners of the  
Henry County Water District #2  
Campbellsburg, KY 40011

We have audited, 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, the financial statements of Henry County Water District #2 as of and for the year ended December 31, 2014, and the related notes to the financial statements, which collectively comprise Henry County Water District No. 2's basis financial statements, and have issued our report thereon dated March 9, 2015.

#### INTERNAL CONTROL OVER FINANCIAL REPORTING

In planning and performing our audit of the financial statements, we considered Henry County Water District #2's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of Henry County Water District #2's internal control. Accordingly, we do not express an opinion on the effectiveness of Henry County Water District #2's internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraph 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. However, as described in the accompanying schedule of findings and questioned costs, we identified certain deficiencies in internal control that we consider to be material weaknesses.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiencies described in the accompanying schedule of findings and questioned costs to be material weaknesses (Items 2014-001 and 2014-002).

#### COMPLIANCE AND OTHER MATTERS

As part of obtaining reasonable assurance about whether Henry County Water District #2'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 an instance of noncompliance or other matters that is required to be reported under *Government Auditing Standards* and which is described in the accompanying schedule of findings and questioned costs as Item 2014-003.

#### HENRY COUNTY WATER DISTRICT #2'S RESPONSE TO FINDINGS

Henry County Water District #2's response to the findings identified in our audit is described in the accompanying schedule of findings and questioned costs. Henry County Water District #2'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.

*Raisor, Zapp & Woods, PSC*

RAISOR, ZAPP, & WOODS P.S.C  
Certified Public Accountants  
Carrollton, Kentucky

March 9, 2015

# RAISOR, ZAPP & WOODS, PSC

## Certified Public Accountants

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

To the Commissioners of the  
Henry County Water District #2  
Campbellsburg, Kentucky 40011

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

We have audited Henry County Water District #2's compliance with the types of compliance requirements described in the *OMB Circular A-133 Compliance Supplement* that could have a direct and material effect on each of Henry County Water District #2's major federal programs for the year ended December 31, 2014. Henry County Water District #2's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs.

#### *Management's Responsibility*

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

#### *Auditor's Responsibility*

Our responsibility is to express an opinion on compliance for each of Henry County Water District #2's major federal programs based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about Henry County Water District #2'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 Henry County Water District #2's compliance.

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

In our opinion, Henry County Water District #2, 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, 2014.

## Report on Internal Control over Compliance

Management of Henry County Water District #2, 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 Henry County Water District #2'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 OMB Circular A-133, 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 Henry County Water District #2'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 OMB Circular A-133. Accordingly, this report is not suitable for any other purpose.

*Raisor, Zapp & Woods, PSC*

RAISOR, ZAPP & WOODS, PSC  
Certified Public Accountants  
Carrollton, Kentucky

March 9, 2015



**HENRY COUNTY WATER DISTRICT #2**  
**SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS**  
**For the Year Ended December 31, 2014**

<u>Federal Grant/Pass-through Grantor/Program or Cluster Title</u>	<u>Federal CFDA Number</u>	<u>Pass-through Entity Identifying Number</u>	<u>Federal Expenditures</u>
<b><u>Environmental Protection Agency</u></b>			
Pass-through Kentucky Infrastructure Authority			
Capitalization Grants for Clean Water State Revolving Funds	66.458	F13-039	\$ 1,163,423
Total Pass-through the Kentucky infrastructure Authority			\$ 1,163,423
Total Environmental Protection Agency			\$ 1,163,423
Total Expenditures of Federal Awards			\$ 1,163,423

**NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS**

**Note A: Basis of Presentation**

The accompanying schedule of expenditures of federal awards (the Schedule) includes the federal grant activity of Henry County Water District #2 under programs of the federal government for the year ended December 31, 2014, and is presented on the accrual basis of accounting. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Because the Schedule presents only a selected portion of the operations of the Henry County Water District #2, it is not intended to and does not present the financial position, changes in net position, or cash flows of Henry County Water District #2.

**Note B: Insurance**

The Henry County Water District #2 did not receive any other federal awards in the form of non-cash assistance, insurance contracts, or loan guarantees for the year ended December 31, 2014.

**HENRY COUNTY WATER DISTRICT #2  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
For the Year Ended December 31, 2014**

**A. SUMMARY OF AUDITOR'S RESULTS**

1. The auditors' report expresses an unmodified opinion on the financial statements of Henry County Water District #2.
2. Two deficiencies in internal control related to the audit of the financial statements are reported in the 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. Items 2014-001 and 2014-002 were reported as material weaknesses.
3. One instance of noncompliance material to the financial statements of Henry County Water District #2, which would be required to be reported in accordance with Government Auditing Standards, was disclosed during the audit as Item 2014-003.
4. No significant deficiencies in internal control over the major federal award program were disclosed during the audit or reported in the Report on Compliance for Each Major Program and on Internal Control over Compliance required by OMB Circular A-133.
5. The auditor's report on compliance for the major federal award program for the Henry County Water District #2 expresses an unmodified opinion on the major federal program.
6. Audit findings that are required to be reported in accordance with Section 510(a) of OMB Circular A-133 are reported in this Schedule.
7. The program tested as a major program was:

	<u>CFDA No.</u>
Environmental Protection Agency:	
Capitalization Grants for Clean Water	
State Revolving Funds	66.458

8. The threshold used for distinguishing between Type A and Type B programs was \$300,000.
9. The Henry County Water District #2 did not qualify as a low risk auditee.

**B. FINDINGS - FINANCIAL STATEMENTS AUDIT**

**GOVERNMENT AUDITING STANDARDS**

**DEFICIENCIES IN INTERNAL CONTROL**

**2014-001 SIZE OF ENTITY, CROSS-TRAINING, CHECKING PROCEDURES AND DOCUMENTATION**

**CONDITION:**

Due to the size of the entity, cross-training and checking procedures are not in place for certain administrative positions. This limits internal control. This condition was also cited as a material weakness in the schedule of findings and responses for the year ended December 31, 2013 as Item 2013-001.

**CRITERIA:**

Internal controls should be in place to provide management with reasonable, but not absolute, assurance that assets are safeguarded against loss from unauthorized use or disposition, and allow timely preparation of financial data consistent with management assertions.

**HENRY COUNTY WATER DISTRICT #2  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)  
For the Year Ended December 31, 2014**

**B. FINDINGS - FINANCIAL STATEMENTS AUDIT (Continued)**

**GOVERNMENT AUDITING STANDARDS (Continued)**

**DEFICIENCIES IN INTERNAL CONTROL (Continued)**

**2014-001 SIZE OF ENTITY, CROSS-TRAINING, CHECKING PROCEDURES AND DOCUMENTATION  
(Continued)**

**CAUSE:**

Responsibilities associated with individual positions limit the availability of individuals to rotate duties and implement checking procedures.

**EFFECT:**

This limitation may affect the ability to timely and effectively record, process, summarize and report financial data.

**RECOMMENDATION:**

Management should strive to provide cross-training for administrative staff and implement checking processes.

**RESPONSE:**

We concur with the recommendation. Management believes adequate resources have been expended and control procedures implemented, that are commensurate with the staff size and responsibility of financial personnel.

**2014-002 FAILURE TO PREPARE COMPLETE SET OF FINANCIAL STATEMENTS INCLUDING REQUIRED  
NOTE DISCLOSURES**

**CONDITION:**

District financial statements, including the required disclosures, are prepared as part of the annual audit. This condition was also cited as a material weakness in the schedule of findings and responses for the year ended December 31, 2013 as Item 2013-002.

**CRITERIA:**

Internal controls should be in place to provide management with reasonable, but not absolute, assurance that financial statements and required notes are prepared in accordance with generally accepted accounting principles.

**CAUSE:**

The draft financial statements and disclosures are prepared during the audit process.

**EFFECT:**

Management engaged the auditor to prepare the draft of the 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:**

District management should continue to enhance its knowledge of reporting requirements in providing oversight of this service.

**HENRY COUNTY WATER DISTRICT #2  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)  
For the Year Ended December 31, 2014**

**B. FINDINGS - FINANCIAL STATEMENTS AUDIT (Continued)**

**GOVERNMENT AUDITING STANDARDS (Continued)**

**DEFICIENCIES IN INTERNAL CONTROL (Continued)**

**2014-002 FAILURE TO PREPARE COMPLETE SET OF FINANCIAL STATEMENTS INCLUDING REQUIRED  
NOTE DISCLOSURES (Continued)**

**RESPONSE:**

The outsourcing of this service is a result of management's cost benefit decision to avoid incurring internal resource costs. We concur with the recommendation and will continue to improve our overall accounting knowledge in performing our oversight responsibilities. We are aware of our responsibilities for the financial statements. We have reviewed and approved the financial statements as presented.

**COMPLIANCE AND OTHER MATTERS**

**2014-003 VIOLATION OF KRS 424.260**

**CONDITION:**

The Henry County Water District #2 did not advertise for bidS on certain materials, supplies, equipment, or services. This condition was also cited as an instance of noncompliance material to the financial statements for the year ended December 31, 2013 as item 2013-003.

**CRITERIA:**

KRS 424.260 requires districts to implement procedures to ascertain that any qualified purchase greater than \$20,000 is properly bid.

**CAUSE:**

Procedures were not followed regarding Kentucky Revised Statutes.

**EFFECT:**

Goods and services may not be purchased at the most competitive price.

**RECOMMENDATION:**

The District's management should review purchases for any bid requirements.

**RESPONSE:**

The purchase that was determined as not following KRS 424.260 was considered by the Commissioners to be an emergency purchase but was not documented as such. We will strive to properly document purchases deemed emergency purchases and therefore not subject to advertisement for bid in the future.

**C. FINDINGS AND QUESTIONED COSTS – MAJOR FEDERAL AWARD PROGRAMS AUDIT**

**SIGNIFICANT DEFICIENCIES**

None

Compliance

None

**HENRY COUNTY WATER DISTRICT #2  
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS  
For the Year Ended December 31, 2014**

**There were no prior year audit findings to report.**