

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

At December 31, 2015 and 2014

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

Years Ended December 31, 2015 and 2014

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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, 2015 and 2014, 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, 2015 and 2014, 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.

Changes in Accounting Principle

As described in Note 21 to the financial statements, in the year ended December 31, 2015, the District adopted new accounting guidance, GASB Statement No. 68, *Accounting and Financial Reporting for Pensions – an Amendment of GASB Statement No. 27* and GASB Statement No. 71 – *Pension Transition for Contributions Made Subsequent to the Measurement Date – an Amendment of GASB No. 68*. Our opinion is not modified with respect to this matter.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the Schedule of the District's Proportionate Share of the Net Pension Liability – County Employees Retirement System on page 23, and Schedule of the District's Contributions – County Employees Retirement System on page 24 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'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 Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated June 17, 2016, 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

June 17, 2016

HENRY COUNTY WATER DISTRICT #2
STATEMENT OF NET POSITION
December 31, 2015 and 2014

	2015	Restated 2014
ASSETS		
Current Assets:		
Cash, Including Time Deposits	\$ 158,954	\$ 178,833
Accrued Interest Receivable	122	83
Accounts Receivable (Net)	405,450	393,082
Other Receivables	78,272	-
Inventory	115,166	104,773
Prepaid Expense	30,092	30,014
Total Current Assets	<u>\$ 788,056</u>	<u>\$ 706,785</u>
Noncurrent Assets:		
Restricted Assets:		
Cash, Including Time Deposits	\$ 1,806,102	\$ 2,339,649
Accrued Interest Receivable	792	1,107
Capital Assets (Net)	15,227,669	15,232,458
Total Noncurrent Assets	<u>\$ 17,034,563</u>	<u>\$ 17,573,214</u>
Total Assets	<u>\$ 17,822,619</u>	<u>\$ 18,279,999</u>
DEFERRED OUTFLOWS OF RESOURCES		
Attributable to Employee Pension Plan	\$ 236,342	\$ 62,809
Deferred Loss - Early Debt Retirement	229,286	246,375
Total Deferred Outflows of Resources	<u>\$ 465,628</u>	<u>\$ 309,184</u>
LIABILITIES		
Current Liabilities:		
Accounts Payable	\$ 110,565	\$ 74,089
Accounts Payable - Construction	41,438	10,145
Accrued Compensated Absences	25,660	26,778
Accrued Salaries, Wages & Benefits	13,388	44,268
Accrued Payroll Taxes/Employee Withholding	31,499	26,903
Utility Tax Payable	6,786	6,745
Sales Tax Payable	538	520
Current Liabilities Payable from Restricted Assets:		
Accrued Interest Payable - Customer Deposits	152	184
Accrued Interest - Notes Payable	3,007	3,200
Revenue Bonds Payable	485,000	470,000
Notes Payable	159,086	156,827
Total Current Liabilities	<u>\$ 877,119</u>	<u>\$ 819,659</u>
Noncurrent Liabilities:		
Revenue Bonds Payable (Net of Unamortized Bond Discount & Premium of \$4,756 for 2015 and \$5,140 for 2014)	\$ 5,874,756	\$ 6,360,140
Notes Payable	2,031,653	2,190,739
Net Pension Liability	1,350,032	1,095,000
Noncurrent Liabilities Payable from Restricted Assets:		
Customer Deposits Payable	78,025	71,725
Total Noncurrent Liabilities	<u>\$ 9,334,466</u>	<u>\$ 9,717,604</u>
Total Liabilities	<u>\$ 10,211,585</u>	<u>\$ 10,537,263</u>
DEFERRED INFLOWS OF RESOURCES		
Attributable to Employee Pension Plan	\$ 158,525	\$ 122,000
Funds Held for Future Lines	4,340	31,400
Total Deferred Inflows of Resources	<u>\$ 162,865</u>	<u>\$ 153,400</u>
NET POSITION		
Net Investment in Capital Assets	\$ 6,865,022	\$ 6,490,983
Restricted for Capital Projects	377,281	823,909
Restricted for Debt Service	1,346,819	1,345,303
Unrestricted (deficit)	(675,325)	(761,675)
Total Net Position	<u>\$ 7,913,797</u>	<u>\$ 7,898,520</u>

See accompanying notes to the basic financial statements.

HENRY COUNTY WATER DISTRICT #2
STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN FUND NET POSITION
For the Years Ended December 31, 2015 and 2014

	2015	Restated 2014
Operating Revenues:		
Charges for Services:		
Water Charges (Net of Estimated Bad Debts)	\$ 2,990,999	\$ 2,949,020
Wholesale Water Charges	248,692	232,741
Total Charges for Services	<u>\$ 3,239,691</u>	<u>\$ 3,181,761</u>
Other Charges and Miscellaneous:		
Reconnect and Disconnect Charges	\$ 32,785	\$ 33,040
Forfeited Discounts	81,288	83,096
Miscellaneous	78,325	29,280
Total Other Charges and Miscellaneous	<u>\$ 192,398</u>	<u>\$ 145,416</u>
Total Operating Revenues	<u>\$ 3,432,089</u>	<u>\$ 3,327,177</u>
Operating Expenses:		
Accounting and Collecting Labor	\$ 116,458	\$ 108,702
Chemicals	62,189	79,449
Commissioner Salaries	33,900	32,700
Continuing Education	4,080	3,306
Contractual Services-Maintenance of Mains/Distribution System	39,790	22,281
Dues	5,103	4,031
Insurance	44,477	44,297
Maintenance of Mains/Distribution System Expenses	341,377	296,490
Miscellaneous	10,471	6,469
Office Supplies and Expense	69,619	64,416
Operating Labor	647,039	624,704
Other Interest Expense	36	345
Payroll Taxes	66,432	60,839
Professional Services	66,010	62,588
Purchased Power	408,656	411,664
Regulatory Fees	6,340	6,461
Retirement Expense & Employee Benefits	425,573	414,773
Transportation Expense	27,049	27,895
Utilities	23,461	26,610
Depreciation Expense	826,871	803,110
Total Operating Expenses	<u>\$ 3,224,931</u>	<u>\$ 3,101,130</u>
Net Operating Income	<u>\$ 207,158</u>	<u>\$ 226,047</u>
Nonoperating Revenue (Expense):		
Investment Income	\$ 8,077	\$ 10,492
Interest Expense	(306,190)	(291,032)
Penalties Paid	(7,290)	-
Gain (Loss) on Sale/Abandonment of Fixed Assets	-	(5,629)
Total Nonoperating Revenue (Expense)	<u>\$ (305,403)</u>	<u>\$ (286,169)</u>
Income (Loss) Before Contributions	<u>\$ (98,245)</u>	<u>\$ (60,122)</u>
Capital Contributions	<u>113,522</u>	<u>103,648</u>
Change in Net Position	<u>\$ 15,277</u>	<u>\$ 43,526</u>
Net Position--Beginning of Year	<u>7,898,520</u>	<u>7,854,994</u>
Net Position--End of Year	<u><u>\$ 7,913,797</u></u>	<u><u>\$ 7,898,520</u></u>

HENRY COUNTY WATER DISTRICT #2
STATEMENT OF CASH FLOWS
For the Years Ended December 31, 2015 and 2014

	2015	Restated 2014
CASH FLOWS FROM OPERATING ACTIVITIES		
Receipts from Customers	\$ 3,347,749	\$ 3,371,721
Payments to Suppliers	(1,472,522)	(1,461,827)
Payments to Employees	(829,395)	(781,091)
Other Receipts (Payments)	31,197	42,354
Net Cash Provided (Used) by Operating Activities	<u>\$ 1,077,029</u>	<u>\$ 1,171,157</u>
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Purchase of Capital Assets (Including Work In Process)	\$ (808,765)	\$ (2,511,671)
Principal Paid on Capital Debt	(626,827)	(460,475)
Interest Paid on Capital Debt	(289,678)	(271,125)
Note Proceeds	-	2,353,041
Capital Contributions	86,462	135,048
Proceeds Sale of Capital Asset	-	3,940
Net Cash Provided (Used) by Capital and Related Financing Activities	<u>\$ (1,638,808)</u>	<u>\$ (751,242)</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Interest Received	\$ 8,353	\$ 11,310
Net Cash Provided (Used) by Investing Activities	<u>\$ 8,353</u>	<u>\$ 11,310</u>
Net Increase (Decrease) in Cash and Cash Equivalents	\$ (553,426)	\$ 431,225
Balances-Beginning of the Year	<u>1,408,447</u>	<u>977,222</u>
Balances-End of the Year	<u><u>\$ 855,021</u></u>	<u><u>\$ 1,408,447</u></u>

	Balances Per December 31, 2015 Statement of Net Position	Balances Per December 31, 2015 Statement of Cash Flows
Cash	\$ 58,954	\$ 58,954
Certificates of Deposit	100,000	-
Restricted Cash	796,067	796,067
Restricted Certificates of Deposit	1,010,035	-
Total Cash and Cash Equivalents, End of Year	<u>\$ 1,965,056</u>	<u>\$ 855,021</u>

	Restated Balances Per December 31, 2014 Statement of Net Position	Restated 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>

(Continued)

HENRY COUNTY WATER DISTRICT #2
STATEMENT OF CASH FLOWS
For the Years Ended December 31, 2015 and 2014

	<u>2015</u>	<u>Restated 2014</u>
RECONCILIATION OF OPERATING INCOME (LOSS) TO NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES		
Operating Income (Loss)	\$ 207,158	\$ 226,047
Adjustments to Reconcile Operating Income to Net Cash		
Provided (Used) by Operating Activities:		
Cash Flows Reported in Other Categories:		
Depreciation Expense	826,871	803,110
Penalties Paid	(7,290)	-
Pension Expense	118,024	88,000
Change in Assets and Liabilities:		
Receivables, Net	(12,368)	46,369
Other Receivables	(78,272)	-
Inventories	(10,393)	13,551
Prepaid Expenses	(78)	(2,812)
Accounts Payable	54,452	3,703
Accrued Expenses	(27,343)	(4,867)
Customer Meter Deposits Payable	6,268	(1,944)
Net Cash Provided by Operating Activities	<u>\$ 1,077,029</u>	<u>\$ 1,171,157</u>

SCHEDULE OF NONCASH INVESTING, CAPITAL, AND FINANCING ACTIVITIES

At December 31, 2015 and 2014, Henry County Water District #2 had \$41,438 and \$10,145, respectively, of capitalized expenditures for construction in accounts payable and retainage payable on the Statement of Net Position. At December 31, 2015 and 2014, Henry County Water District #2 had \$24,392 and \$17,976, respectively, of capital assets in accounts payable on the Statement of Net Position.

Included in the \$41,438 of capitalized expenditures in 2015, increases of \$29,808 were added to the District's capital assets through the Focus on Core Mission and Infrastructure Project. The debt associated with financing (\$14,904) these improvements is included in the financial statements as Accounts Payable - Construction. The gross amount of the debt was reduced by the amounts provided for debt forgiveness due to federal and state funding (\$14,904). Henry County Water District #2 has included the debt reduction in capital contributions in its statement of revenues, expenses and changes in fund net position.

HENRY COUNTY WATER DISTRICT #2
NOTES TO BASIC FINANCIAL STATEMENTS
December 31, 2015 and 2014

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.

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.

HENRY COUNTY WATER DISTRICT #2
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
December 31, 2015 and 2014

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

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: Bond discount and premium are amortized over the life of the bond issue.

Debt Issuance Costs: Such costs are expensed as incurred.

Pension: 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 Commonwealth of Kentucky's County Employees' Retirement System (CERS), and additions to/deductions from CERS's fiduciary net position have been determined on the same basis as they are reported by CERS.

Compensated Absences: See Note 11 for the District's policy on vacation and sick pay.

Income Taxes: 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 \$78,960 and \$103,648 were received by the District for the years ended December 31, 2015 and 2014, respectively. Additional capital contributions of \$14,904 for debt forgiveness and \$19,658 from the Kentucky Department of Transportation were received by the District in the year ended December 31, 2015.

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.

HENRY COUNTY WATER DISTRICT #2
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
December 31, 2015 and 2014

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

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.

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, 2015 and 2014. During calendar year 2015 and 2014 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, 2015 and 2014, 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, 2015, and 2014 in accordance with District policy, \$1,525,302 and \$1,550,719 respectively, of the District's deposits were covered by federal depository insurance and \$1,035,811 and \$1,580,709, 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.

At December 31, 2015 and 2014, the District's deposits were as follows:

December 31, 2015

Type of Deposits	Total Bank Balance	Total Carrying Value
Demand Deposits	\$ 177,937	\$ 177,937
Time & Savings	2,383,176	1,786,619
Total Deposits	<u>\$ 2,561,113</u>	<u>\$ 1,964,556</u>

HENRY COUNTY WATER DISTRICT #2
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
December 31, 2015 and 2014

NOTE 3 – CASH AND INVESTMENTS (Continued)

Custodial Credit Risk (Continued)

December 31, 2014

<u>Type of Deposits</u>	<u>Total Bank Balance</u>	<u>Total Carrying Value</u>
Demand Deposits	\$ 200,028	\$ 200,028
Time & Savings	2,931,400	2,317,954
Total Deposits	<u>\$ 3,131,428</u>	<u>\$ 2,517,982</u>

Reconciliation to Statement of Net Position:

	<u>December 31, 2015</u>	<u>December 31, 2014</u>
Unrestricted Cash, Including Time Deposits	\$ 158,954	\$ 178,833
Restricted Cash, Including Time Deposits	1,806,102	2,339,649
Less Cash on Hand	(500)	(500)
	<u>\$ 1,964,556</u>	<u>\$ 2,517,982</u>

NOTE 4 – RESTRICTED ASSETS

Restricted cash and time deposits consist of the following:

	<u>December 31, 2015</u>	<u>December 31, 2014</u>
Bond and Interest Sinking Account	\$ 530,441	\$ 531,058
Debt Covenant	210,035	210,035
Depreciation Account	608,558	608,396
Customer Deposits & Impact Charge Escrow	79,787	166,251
Construction Account	377,281	823,909
Total	<u>\$ 1,806,102</u>	<u>\$ 2,339,649</u>

Restricted receivables consist of the following:

	<u>December 31, 2015</u>	<u>December 31, 2014</u>
Interest Receivable	\$ 792	\$ 1,107
	<u>\$ 792</u>	<u>\$ 1,107</u>

NOTE 5 – CUSTOMER ACCOUNTS RECEIVABLE

Customer Accounts Receivable has been netted with an Allowance for Bad Debts of \$61,402 and \$54,640 at December 31, 2015 and 2014, 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 \$125,501 and \$123,440 is included in accounts receivable at December 31, 2015 and 2014, respectively.

NOTE 6 – OTHER RECEIVABLES

At December 31, 2015 the District recorded other receivables of \$78,272. This amount consisted of \$51,151 receivable from the Federal Emergency Management Agency (FEMA) for amounts expended for repairs, \$19,658 receivable from Kentucky Department of Transportation for amounts expended, and \$7,463 from Kentucky Department of Revenue – Utility Gross Receipts License Tax for overpayment of Utility Gross Receipts License Tax.

HENRY COUNTY WATER DISTRICT #2
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
December 31, 2015 and 2014

NOTE 7 – CAPITAL ASSETS

Capital asset activity for the years ended December 31, 2015 and 2014, was as follows:

	Balance at January 1, 2015	Additions	Disposals	Balance at December 31, 2015
Land & Land Rights	\$ 176,617	\$ -	\$ -	\$ 176,617
Structures & Improvements	26,609,297	525,452	-	27,134,749
Distribution System	2,482,810	119,430	-	2,602,240
Machinery & Equipment	1,425,467	73,660	-	1,499,127
Construction in Process	75,052	605,868	(502,328)	178,592
Totals at Historical Cost	<u>\$ 30,769,243</u>	<u>\$ 1,324,410</u>	<u>\$ (502,328)</u>	<u>\$ 31,591,325</u>
Less: Accumulated Depreciation				
Structures & Improvements	\$ (13,224,843)	\$ (700,480)	\$ -	\$ (13,925,323)
Distribution System	(1,314,084)	(50,204)	-	(1,364,288)
Machinery & Equipment	(997,858)	(76,187)	-	(1,074,045)
Total Accumulated Depreciation	<u>\$ (15,536,785)</u>	<u>\$ (826,871)</u>	<u>\$ -</u>	<u>\$ (16,363,656)</u>
Capital Assets, Net	<u>\$ 15,232,458</u>	<u>\$ 497,539</u>	<u>\$ (502,328)</u>	<u>\$ 15,227,669</u>

	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 Costs	<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)
Totals 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>

Included under the District's capital assets were \$4,598,098 and \$4,433,513 of fully depreciated assets, at December 31, 2015 and 2014, respectively. Land and land rights and construction in process are capital assets not being depreciated.

Depreciation expense aggregated \$826,871 and \$803,110 in 2015 and 2014, respectively.

NOTE 8 – 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, 2015 and 2014

NOTE 9 – 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, 2015</u>	<u>December 31, 2014</u>
Difference between the reacquisition price and the net carrying amount of the old bond issues refunded.		
2010 Bond Issue	\$ 153,395	\$ 165,790
2013 Bond Issue	75,891	80,585
	<u>\$ 229,286</u>	<u>\$ 246,375</u>

Amounts reported as deferred outflows of resources due to the advance refunding of old bond issues will be amortized over the shorter of the life of the old or new debt and recognized in interest expense as follows:

Year Ended December 31, 2015:	<u>Deferred Outflows of Resources</u>
2016	\$ 17,089
2017	17,089
2018	17,089
2019	17,089
2020	17,089
2021-2025	85,447
2026-2030	52,916
2031-2032	5,478
	<u>\$ 229,286</u>
Year Ended December 31, 2014:	<u>Deferred Outflows of Resources</u>
2015	\$ 17,089
2016	17,089
2017	17,089
2018	17,089
2019	17,089
2020-2024	85,447
2025-2029	65,311
2030-2032	10,172
	<u>\$ 246,375</u>

The District's deferred outflows of resources attributable to the District's employee pension plan are detailed in Note 16.

HENRY COUNTY WATER DISTRICT #2
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
December 31, 2015 and 2014

NOTE 10 – LONG-TERM DEBT

As of December 31, 2015 and 2014, the long-term debt payable consisted of the following:

Notes Payable:

	<u>December 31, 2015</u>	<u>December 31, 2014</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.	\$ 2,062,270	\$ 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.	128,469	194,525
Total Notes Payable	\$ 2,190,739	\$ 2,347,566
Current Portion	\$ 159,086	\$ 156,827
Noncurrent Portion	2,031,653	2,190,739
Total Notes Payable	\$ 2,190,739	\$ 2,347,566

Bonds Payable:

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.	\$ 4,145,000	\$ 4,430,000
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.	2,210,000	2,395,000
Total Bonds Payable	\$ 6,355,000	\$ 6,825,000
Current Portion	\$ 485,000	\$ 470,000
Noncurrent Portion	5,870,000	6,355,000
Total Bonds Payable	\$ 6,355,000	\$ 6,825,000
Unamortized Bond Premium	4,756	5,140
Total Bonds Payable Net of Unamortized Bond Premium and Discount	\$ 6,359,756	\$ 6,830,140

Accrued Compensated Absences:

Accrued Compensated Absences (All Current)	\$ 25,660	\$ 26,778
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HENRY COUNTY WATER DISTRICT #2
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
December 31, 2015 and 2014

NOTE 10 – LONG-TERM DEBT (Continued)

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, 2015 was \$128,469.

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.

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 which were expensed when incurred.

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, 2015 and 2014.

December 31, 2015

	Balance at January 1, 2015	Additions	Retirements	Balance at December 31, 2015	Current Portion
Notes Payable	\$ 2,347,566	\$ -	\$ 156,827	\$ 2,190,739	\$ 159,086
Bonds Payable	6,825,000	-	470,000	6,355,000	485,000
Accrued Compensated Absences	26,778	-	1,118	25,660	25,660
Total Enterprise Fund Debt	<u>\$ 9,199,344</u>	<u>\$ -</u>	<u>\$ 627,945</u>	<u>\$ 8,571,399</u>	<u>\$ 669,746</u>

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>

HENRY COUNTY WATER DISTRICT #2
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
December 31, 2015 and 2014

NOTE 10 – LONG-TERM DEBT (Continued)

The annual requirements for all long-term debt outstanding at December 31, 2015, are as follows:

	Note Payable	Note Payable Interest	Service Fee	Bonds	Bond Interest	Trustee Fees	Total Principal, Interest, Trustee Fee and Servicing Fee
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	99,033	29,020	4,146	458,000	173,020	900	764,119
2021-2025	521,896	118,372	16,911	2,544,000	583,959	4,500	3,789,638
2026-2030	569,402	70,865	10,125	1,355,000	138,420	3,150	2,146,962
2031-2034	492,620	19,593	2,798	155,000	5,502	450	675,963
	<u>\$ 2,190,739</u>	<u>\$ 372,032</u>	<u>\$ 52,964</u>	<u>\$ 6,355,000</u>	<u>\$ 1,739,880</u>	<u>\$ 12,600</u>	<u>\$ 10,723,215</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>

NOTE 11 – 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, 2015 and 2014, a liability for accrued vacation was recorded in the amount of \$25,660 and \$26,778, 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, 2015 and 2014, the District had an unrecorded sick pay liability to its employees of \$140,633 and \$131,813, respectively. The estimated liabilities include required salary related payments.

HENRY COUNTY WATER DISTRICT #2
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
December 31, 2015 and 2014

NOTE 12 – FUND EQUITY- RESTRICTED NET POSITION

	<u>December 31, 2015</u>	<u>December 31, 2014</u>
Restricted for Capital Projects:		
Monies Reserved for Future System Improvements	\$ 377,281	\$ 823,909
Total Restricted for Capital Projects	<u>\$ 377,281</u>	<u>\$ 823,909</u>
Restricted for Debt Service:		
2010 and 2013 Bond Issues & KIA Note Payable		
Cash	\$ 1,349,034	\$ 1,347,396
Add: Accrued Interest Receivable	792	1,107
Less: Accrued Interest Payable	(3,007)	(3,200)
Total Restricted for Debt Service	<u>\$ 1,346,819</u>	<u>\$ 1,345,303</u>

NOTE 13 – BAD DEBT EXPENSE

Water revenue charges have been netted with an estimated bad debt expense of \$10,674 and \$7,934 at December 31, 2015 and 2014, respectively.

NOTE 14 – INTEREST EXPENSE

Interest expense incurred for the years ended December 31, 2015 and 2014 was \$306,226 and \$291,377, respectively. No interest was capitalized in 2015. Capitalized interest in 2014 was \$4,043.

NOTE 15 – 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 16 – COUNTY EMPLOYEES' RETIREMENT SYSTEM – NON-HAZARDOUS EMPLOYEES PENSION PLAN

Entry into the Commonwealth of Kentucky's County Employees' Retirement System (CERS) was authorized by the Commissioners. Electing employees and all new employees of the District may participate in the System.

Under the provision of Kentucky Revised Statute ("KRS") Section 61.645, the Board of Trustees of the Kentucky Retirement System administers CERS and has the authority to establish and amend benefit provisions. The Kentucky Retirement System issues a publicly available financial report that includes financial statements and required supplementary information for CERS. The most recent financial report, dated June 30, 2015, may be obtained from <https://kyret.ky.gov/Financial%20Statements/2015/Financial.pdf>. Additionally, the Kentucky Retirement System issues a publically available financial report that includes the Schedules of Employer Allocations and Pension amounts by Employer. The most recent report, dated June 30, 2015 may be obtained from <https://kyret.ky.gov/employers/GASB/pages/GASB-library.aspx>.

Plan Description – CERS is a cost-sharing multiple-employer defined benefit pension plan that covers all regular full-time members employed in non-hazardous duty positions 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, 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 12 months prior to the effective date of the COLA. If the recipient has been receiving a benefit for less than 12 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 12 months preceding the effective date of the COLA. The Kentucky General Assembly reserves the right to suspend or reduce the COLA if, in its judgment, the welfare of the Commonwealth so demands. No COLA has been granted since July 1, 2011.

HENRY COUNTY WATER DISTRICT #2
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
December 31, 2015 and 2014

**NOTE 16 – COUNTY EMPLOYEES' RETIREMENT SYSTEM – NON-HAZARDOUS EMPLOYEES PENSION PLAN
(CONTINUED)**

Basis of Accounting – CERS's financial statements are prepared using the accrual basis of accounting. Plan member contributions are recognized in the period in which contributions are due. Employer contributions to the plan are recognized when due and the employer has made a formal commitment to provide the contributions. Benefits and refunds are recognized when due and payable in accordance with terms of the plan. Premium payments are recognized when due and payable in accordance with the terms of the plan. Administrative and investment expenses are recognized when incurred.

Method Used to Value Investments – Investments of the plan are reported at fair value. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Short-term investments are reported at cost, which approximates fair value.

Benefits provided – 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
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

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.

Contributions - For the fiscal years ended June 30, 2015 and 2014, plan members who began participating prior to September 1, 2008, were required to contribute 5% of their annual creditable compensation. These members were classified in the Tier 1 structure of benefits. 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, 2015 and 2014, participating employers contributed 17.67% and 18.89%, respectively, of each employer's creditable compensation. The actuarially determined rates set by the Board for the fiscal years ended June 30, 2015 and 2014, were 17.67% and 18.89%, respectively. Administrative costs of KRS are financed through employer contributions and investment earnings.

Plan members who began participating on, or after, September 1, 2008, were required to contribute a total of 6% of their annual creditable compensation. These members were classified in the Tier 2 structure of benefits. 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

HENRY COUNTY WATER DISTRICT #2
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
December 31, 2015 and 2014

NOTE 16 – COUNTY EMPLOYEES' RETIREMENT SYSTEM – NON-HAZARDOUS EMPLOYEES PENSION PLAN
(Continued)

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.

Plan members who began participating on, or after, January 1, 2014, were required to contribute to the Cash Balance Plan. These members were classified in the Tier 3 structure of benefits. 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.

Actuarial Methods and Assumptions

The actuarially determined contribution rates are determined on a biennial basis beginning with the fiscal years ended 2016 and 2017, determined as of June 30, 2015. The amortization period of the unfunded liability has been reset as of July 1, 2013 to a closed 30 year period. The following actuarial methods and assumptions were used to determine contribution rates reported for all KRS Systems:

Actuarial Cost Method	Entry Age
Amortization Method	Level of Percentage of Payroll, closed
Remaining Amortization Period	28 years
Asset Valuation Method	5 year Smoothed Market
Inflation	3.25%
Salary Increase	4%, average, including Inflation
Investment Rate of Return	7.5%, Net of Pension Plan Investment Expense, including Inflation

There were no changes of benefit terms. However, the following changes in assumptions were adopted by the Board of Trustees and reflected in the valuation performed as of June 30, 2015:

- The assumed investment rate of return was decreased from 7.75% to 7.5%.
- The assumed rate of inflation was reduced from 3.5% to 3.25%.
- The assumed rate of wage inflation was reduced from 1% to .75%.
- Payroll growth assumption was reduced from 4.5% to 4%.
- The mortality table used for active members is 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 one year for females). For disabled members, the RP-2000 Combined Disabled Mortality Table projected with Scale BB to 2013 (set back four years for males) is used for the period after disability retirement. There is some margin in the current mortality tables for possible future improvement in mortality rates and that margin will be reviewed again when the next experience investigation is conducted.
- The assumed rates of retirement, withdrawal, and disability were updated to more accurately reflect experience.

The following table presents the net pension liability of CERS [as reported in its publicly available financial statements for the year ended June 30, 2015], calculated using the discount rate of 7.5%, as well as what CERS' net pension liability would be if it were calculated using a discount rate that is one percentage point lower (6.5%) or one percentage point higher (8.5%):

HENRY COUNTY WATER DISTRICT #2
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
December 31, 2015 and 2014

NOTE 16 – COUNTY EMPLOYEES' RETIREMENT SYSTEM – NON-HAZARDOUS EMPLOYEES PENSION PLAN
(Continued)

	1% Decrease [6.5%]	Current Discount [7.5%]	1% Increase [8.5%]
Net Pension Liability	\$ 54,888,780	\$ 42,995,250	\$ 32,809,500
District's Proportionate Share	1,723,484	1,350,032	1,030,204

Pension Liabilities, Pension Expense, and Deferred Outflows of Resources and Deferred Inflows of Resources Related to the County Employee Retirement System Pension

At December 31, 2015, and 2014 the District reported a liability of \$1,350,032 and \$1,095,000, respectively for its proportionate share of the net pension liability. The net pension liability for CERS was measured as of June 30, 2015, and 2014 and was based on the actual liability of the employees and former employees relative to the total liability of the system as determined by an actuarial valuation as of those dates. 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 employers, actuarially determined. At June 30, 2015, and 2014 the District's proportion was 0.031399 and 0.033750 percent, respectively. Data is not available for the change in its proportion from previous periods.

The District's total payroll for the fiscal year ended December 31, 2015 was \$884,650. Contributions to CERS were based on \$843,338 (eligible gross wages). The total employer contributions for the year ended December 31, 2015 were \$146,269.

The District's total payroll for the fiscal year ended December 31, 2014, was \$810,739. Contributions to CERS were based on \$766,921 (eligible gross wages). The total employer pension contributions for the year ended December 31, 2014, were \$140,535.

All contributions were made as required during these years.

The District's contribution for the County Employees' Retirement System's year(s) ended December 31, 2015, and 2014 was 0.03140 and 0.03376 percent, respectively, of the System's total contribution requirements for all employers.

For the year ended December 31, 2015, and December 31, 2014, the District recognized pension expense of \$264,293 and \$228,535, respectively. At December 31, 2015 and 2014 the District reported deferred outflows of resources and deferred inflows of resources related to CERS pensions from the following sources:

	December 31, 2015		December 31, 2014	
	Deferred Outflows of Resources	Deferred Inflows of Resources	Deferred Outflows of Resources	Deferred Inflows of Resources
Difference Between Expected and Actual Experience	\$ 11,219	\$ -	\$ -	\$ -
Change in Assumptions	136,136	-	-	-
Changes in Proportion and Differences Between Employer Contributions and Proportionate Share of Contributions	-	60,925	-	-
Net Difference Between Projected and Actual Investment Earnings on Pension Plan Investments	12,102	97,600	-	122,000
District Contributions Made Subsequent to the NPL Measurement Date	76,885	-	62,809	-
Total	<u>\$ 236,342</u>	<u>\$ 158,525</u>	<u>\$ 62,809</u>	<u>\$ 122,000</u>

HENRY COUNTY WATER DISTRICT #2
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
December 31, 2015 and 2014

NOTE 16 – COUNTY EMPLOYEES’ RETIREMENT SYSTEM – NON-HAZARDOUS EMPLOYEES PENSION PLAN
(Continued)

Pension Liabilities, Pension Expense, and Deferred Outflows of Resources and Deferred Inflows of Resources Related to the County Employee Retirement System Pension (Continued)

\$76,885 and \$62,809 reported as deferred outflows of resources related to pensions arising from District contributions made subsequent to the measurement date will be recognized as a reduction in the net pension liability in the years ended December 31, 2016 and 2015. Amounts reported as deferred inflows and outflows of resources due to the net difference between projected and actual investment earnings on pension plan investments will be amortized over five years and recognized in pension expense as follows:

		Deferred Outflows of Resources	Deferred Inflows of Resources
Year Ended December 31, 2015:			
	2016	\$ 2,420	\$ 24,400
	2017	2,420	24,400
	2018	2,420	24,400
	2019	2,420	24,400
	2020	2,422	-
		<u>\$ 12,102</u>	<u>\$ 97,600</u>
Year Ended December 31, 2014:			
	2015	\$ -	\$ 24,400
	2016	-	24,400
	2017	-	24,400
	2018	-	24,400
	2019	-	24,400
		<u>\$ -</u>	<u>\$ 122,000</u>

Amounts reported as deferred outflows of resources due to the difference between expected and actual experience, change of assumptions, and changes in proportion and differences between employer contributions and proportionate share of contributions will be amortized over the expected remaining service lives of all employees that are provided with pensions through the pension plan (twelve years) and recognized in pension expense as follows:

		Deferred Outflows of Resources	Deferred Inflows of Resources
Year Ended December 31, 2015:			
	2016	\$ 12,280	\$ 5,077
	2017	12,280	5,077
	2018	12,280	5,077
	2019	12,280	5,077
	2020	12,280	5,077
	2021-2025	61,400	25,385
	2026-2028	24,555	10,155
		<u>\$ 147,355</u>	<u>\$ 60,925</u>
Year Ended December 31, 2014:			
None		<u>\$ -</u>	<u>\$ -</u>

HENRY COUNTY WATER DISTRICT #2
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
December 31, 2015 and 2014

NOTE 17 – DEFICIT NET POSITION

An unrestricted net position deficit of \$675,325 and \$761,675 existed at December 31, 2015 and 2014, respectively. The deficit resulted from the recognition of net pension liability and related deferred outflows of resources and deferred inflows of resources due to the implementation GASB Statement No. 68.

NOTE 18 – 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 7.6% and 7.3% of the total water charges for services revenue was received from these cities for the years ended December 31, 2015 and 2014, 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 19 – 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 20 – 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. In March, 2016, the District accepted the bid of Caldwell Tanks, Inc. for \$2,197,000 to construct the tank.

At December 31, 2015, \$84,551 of construction costs and engineering fees relating to the Highway 42 water tank project had been expended. \$94,041 of the construction costs and engineering fees relating to line relocations had also been expended at December 31, 2015.

At December 31, 2014, \$15,130 of construction costs and engineering fees relating to the Highway 42 Water Tank project had been capitalized as construction in process. \$29,700 of engineering fees relating to the Wellfield project was capitalized as construction in process. The remaining \$30,222 was for line extensions.

NOTE 21 – FINANCIAL STATEMENTS RESTATEMENT

In June, 2012, the GASB issued Statement 68, *Accounting and Financial Reporting for Pensions – an Amendment of GASB Statement 27*. In November, 2013, the GASB issued Statement 71, *Pension Transition for Contributions Made Subsequent to the Measurement Date – An Amendment of GASB No. 68*. Both of these statements were adopted by the District for the fiscal year ended June 30, 2015. Under these statements, the District is required to report the net pension liability associated with its' employees' pensions as a liability. It is also required to report a deferred outflow of resources for its pension contributions made subsequent to the measurement date of the beginning net pension liability. These balances reflect the District's obligation to pay deferred benefits earned by its employees when the pension [plan's] liability exceeds the value of the pension plan's assets.

Retroactive application by restating financial statements for all periods presented is required. The effect of the reinstatement is as follows for the year ended December 31, 2014.

HENRY COUNTY WATER DISTRICT #2
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)
December 31, 2015 and 2014

NOTE 21 – FINANCIAL STATEMENTS RESTATEMENT (Continued)

Statement of Net Position:

Total Net Position as Originally Presented December 31, 2014	\$ 9,052,711
Less Net Pension Liability	(1,095,000)
Plus Deferred Outflows Employer Pension Contributions	62,809
Less Deferred Inflows of Resources - Difference Between Projected and Actual Earnings	<u>(122,000)</u>
Total Net Position December 31, 2014	<u><u>\$ 7,898,520</u></u>

The components of Net Position at December 31, 2014
after restatement are as follows:

Net Investment in Capital Assets	\$ 6,490,983
Restricted for Capital Projects	823,909
Restricted for Debt Service	1,345,303
Unrestricted (deficit)	<u>(761,675)</u>
Total Net Position	<u><u>\$ 7,898,520</u></u>

NOTE 22 – RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

In June 2015, the GASB issued Statement 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*, effective for fiscal years beginning after June 15, 2017. This statement requires the liability of employers to employees for defined benefit OPEB (net OPEB liability) to be measured as the portion of the present value of projected benefit payments to be provided to current active and inactive employees that is attributed to those employees' past periods of service (total OPEB liability), less the amount of the OPEB plan's fiduciary net position. The District is evaluating the requirements of this statement.

In June 2015, the GASB issued Statement No. 76, *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments*. The objective of this Statement is to identify (in the context of the current governmental financial reporting environment) the hierarchy of GAAP. The GAAP hierarchy consists of the sources of accounting principles used to prepare financial statements of state and local governmental entities in conformity with GAAP and the framework for selecting those principles. This Statement reduces the GAAP hierarchy to two categories of authoritative GAAP and addresses the use of authoritative and nonauthoritative literature in the event that the accounting treatment for a transaction of other event is not specified within a source of authoritative GAAP. This Statement becomes effective for the fiscal year beginning July 1, 2015. The District is evaluating the requirements of this Statement.

HENRY COUNTY WATER DISTRICT #2

SCHEDULE OF THE DISTRICT'S PROPORTIONATE SHARE OF THE NET PENSION LIABILITY
County Employees Retirement System

December 31, 2015*

	<u>2015</u>	<u>2014</u>
District's proportion of the net pension liability (asset)	0.031399%	0.033750%
District's proportionate share of the net pension liability (asset)	\$ 1,350,032	\$1,095,000
District's covered-employee payroll	\$ 843,338	\$766,921
District's proportionate share of the net pension liability (asset) as a percentage of its of its covered- employee payroll	160.08%	142.78%
Plan fiduciary net position as a percentage of the total pension liability	60.3%	62.6%

*Calculations based on June 30, 2015 and 2014, County Employees Retirement Systems' Schedules of Employer Allocations and Pension Amounts by Employer. District payroll is reported for its' covered calendar years ending December 31, 2015 and 2014.

GASB 68 requires the District to present the above information for 10 years. The information will be expanded annually until a full 10-year trend is compiled.

HENRY COUNTY WATER DISTRICT #2

SCHEDULE OF THE DISTRICT'S CONTRIBUTIONS

County Employees Retirement System

Last Ten (10) Fiscal Years Ended December 31

	2015	2014	2013	2012	2011	2010	2009	2008	2007	2006
Contractually required contributions	\$ 146,269	\$ 140,535	\$ 143,614	\$ 144,031	\$ 125,638	\$ 116,169	\$ 102,970	\$ 101,886	\$ 96,679	\$ 78,711
Contributions in relation to the contractually required contributions	146,269	140,535	143,614	144,031	125,638	116,169	102,970	101,886	96,679	78,711
Contribution deficiency (excess)	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
District's covered-employee payroll	\$ 843,338	\$ 766,921	\$ 746,795	\$ 746,906	\$ 701,585	\$ 702,431	\$ 696,367	\$ 686,735	\$ 658,215	\$ 653,742
Contributions as a percentage of covered-employee payroll	17.34%	18.32%	19.23%	19.28%	17.91%	16.54%	14.79%	14.84%	14.69%	12.04%

See accompanying notes to the basic financial statements

RAISOR, ZAPP & WOODS, PSC

Certified Public Accountants

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Susan A. Dukes, CPA

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, 2015, 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 June 17, 2016.

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.

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 certain deficiencies in internal control, described in the accompanying schedule of findings and responses that we consider to be material weaknesses (Items 2015-001 and 2015-002).

COMPLIANCE AND OTHER MATTERS

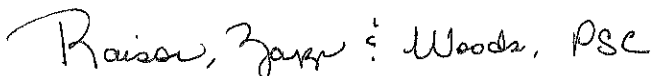
As part of obtaining reasonable assurance about whether Henry County Water District #2's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a 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 responses as Item 2015-003.

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 responses. 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 P.S.C
Certified Public Accountants
Carrollton, Kentucky

June 17, 2016

**HENRY COUNTY WATER DISTRICT #2
SCHEDULE OF FINDINGS AND RESPONSES
For the Year Ended December 31, 2015**

A. SUMMARY OF AUDITOR'S RESULTS

1. The auditors' report expresses an unmodified opinion on whether the financial statements of Henry County Water District #2 were prepared in accordance with GAAP.
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 2015-001 and 2015-002 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 2015-003.

B. FINDINGS - FINANCIAL STATEMENTS AUDIT

GOVERNMENT AUDITING STANDARDS

DEFICIENCIES IN INTERNAL CONTROL

2015-001 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 questioned costs for the year ended December 31, 2014 as Item 2014-001.

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.

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.

**HENRY COUNTY WATER DISTRICT #2
SCHEDULE OF FINDINGS AND RESPONSES (CONTINUED)
For the Year Ended December 31, 2015**

B. FINDINGS - FINANCIAL STATEMENTS AUDIT (Continued)

GOVERNMENT AUDITING STANDARDS (Continued)

DEFICIENCIES IN INTERNAL CONTROL (Continued)

2015-002 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 questioned costs for the year ended December 31, 2014 as Item 2014-002.

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's assistance 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.

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

2015-003 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, 2014 as item 2014-003.

CRITERIA:

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

**HENRY COUNTY WATER DISTRICT #2
SCHEDULE OF FINDINGS AND RESPONSES (CONTINUED)
For the Year Ended December 31, 2015**

B. FINDINGS - FINANCIAL STATEMENTS AUDIT (Continued)

GOVERNMENT AUDITING STANDARDS (Continued)

DEFICIENCIES IN INTERNAL CONTROL (Continued)

2015-003 VIOLATION OF KRS 424.260 (Continued)

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.