

Laurel County Water District No. 2
London, Kentucky

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Independent Auditors' Report
And Financial Statements
For the Years Ended
December 31, 2014 and 2013

Laurel County Water District No. 2
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Independent Auditors' Report

To the Commissioners
Laurel County Water District No. 2
London, Kentucky

Report on the Financial Statements

We have audited the accompanying financial statements of the business-type activities of the Laurel County Water District No. 2, (the District), as of and for the years ended December 31, 2014 and 2013, and the related notes to the financial statements, which collectively comprise the District's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

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

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

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Laurel County Water District No. 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.

Correction of Error

As discussed in Note 9 to the financial statements, an error resulting in overstatement of the amount previously reported for inventories and understatement of the amount previously reported for operating expenses as of December 31, 2013, was discovered by management of the District during the current year. Accordingly, amounts reported for inventories and operating expenses have been restated in the 2013 financial statements now presented, and an adjustment has been made to retained earnings as of December 31, 2013 to correct the error. Our opinion is not modified with respect to that matter.

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 Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated April 29, 2015 on our consideration of the Laurel County Water District No. 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 the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Laurel County Water District No. 2's internal control over financial reporting and compliance.

Christian Sturgeon & Associates, PSC

Christian Sturgeon & Associates, PSC
London, Kentucky

April 29, 2015

Laurel County Water District No. 2
 Statements of Net Position
 December 31, 2014 and 2013

	<u>2014</u>	<u>2013</u>
Assets		
Current Assets		
Cash and cash equivalents	\$ 1,855,281	\$ 1,851,517
Receivables, less allowance	183,351	183,714
Unbilled accounts receivable	91,579	98,784
Grants receivable	37,935	121,082
Inventories	112,017	192,253
Prepaid expenses	4,459	4,375
Other current assets	38	46
Total Current Assets	<u>2,284,660</u>	<u>2,451,771</u>
Noncurrent Assets		
Restricted Assets		
Customer deposits	82,568	77,481
Grant monies	711	685
Depreciation reserves - cash	441,119	399,264
Depreciation reserves - certificates of deposit	125,100	125,100
Bond and interest funds	75,592	74,078
Plant escrow	<u>95,548</u>	<u>-</u>
Total Restricted Assets	<u>820,638</u>	<u>676,608</u>
Capital Assets		
Land and improvements	506,586	496,336
Buildings and improvements	592,657	490,637
Source of supply and pumping	3,560,392	3,560,392
Water treatment equipment	123,333	123,333
Transmission and distribution plant	14,404,695	14,087,712
Vehicles and other equipment	694,413	669,325
Construction in progress	5,500	-
Less: accumulated depreciation	<u>(6,073,025)</u>	<u>(5,555,529)</u>
Net Capital Assets	<u>13,814,551</u>	<u>13,872,206</u>
Other Assets		
Bond issuance costs, net of amortization	<u>11,245</u>	<u>13,263</u>
Total Noncurrent Assets	<u>14,646,434</u>	<u>14,562,077</u>
Total Assets	<u>16,931,094</u>	<u>17,013,848</u>

See accompanying notes to financial statements.

Laurel County Water District No. 2
 Statements of Net Position (Continued)
 December 31, 2014 and 2013

	<u>2014</u>	<u>2013</u>
Liabilities		
Current Liabilities		
Accounts payable	53,896	101,573
Accounts payable - construction	95,546	121,082
Accrued interest payable	873	1,180
Accrued salaries and taxes payable	21,372	22,943
Current portion of notes payable and long-term debt	310,336	223,545
Other current liabilities	26,651	24,740
Total Current Liabilities	<u>508,674</u>	<u>495,063</u>
Noncurrent Liabilities		
Customer deposits	81,909	77,890
Notes payable and long-term debt, less current portion	8,820,948	9,033,784
Total Noncurrent Liabilities	<u>8,902,857</u>	<u>9,111,674</u>
Total Liabilities	<u>9,411,531</u>	<u>9,606,737</u>
Net Position		
Net investment in capital assets	4,683,267	4,614,877
Restricted	820,638	676,608
Unrestricted	2,015,658	2,115,626
Total Net Position	<u>\$ 7,519,563</u>	<u>\$ 7,407,111</u>

Laurel County Water District No. 2
 Statements of Revenues, Expenses and Changes in Net Position
 For the Years Ended December 31, 2014 and 2013

	<u>2014</u>	<u>2013</u>
Operating Revenues		
Water sales	\$ 2,156,709	\$ 2,171,963
Service charges	91,762	92,221
Tap fees	26,325	19,950
Penalties	50,028	49,538
Other revenues	<u>27,229</u>	<u>9,381</u>
Total Operating Revenues	<u>2,352,053</u>	<u>2,343,053</u>
Operating Expenses		
Salaries and wages	608,065	553,621
Employee benefits	414,656	334,885
Purchased water	2,361	90
Purchased power	175,188	194,481
Utilities	23,167	21,578
Chemicals	64,847	79,895
Materials and supplies	59,145	54,675
Contracted services	57,210	64,513
Vehicle and equipment expenses	39,138	45,281
Insurance	19,560	29,482
Bad debt expense, net of recoveries	20,194	19,530
Depreciation	521,656	500,948
Amortization	2,018	2,018
Other operating expenses	<u>81,850</u>	<u>70,545</u>
Total Operating Expenses	<u>2,089,055</u>	<u>1,971,542</u>
Operating Income	<u>262,998</u>	<u>371,511</u>
Non-operating Revenues (Expenses)		
Interest income	2,044	1,998
Grant revenue	194,198	265,823
Rental income	6,000	6,000
Gain (loss) on disposition of equipment	2,588	6,367
Interest expense	<u>(355,376)</u>	<u>(362,887)</u>
Total Non-operating Revenues (Expenses)	<u>(150,546)</u>	<u>(82,699)</u>
Change in Net Position	112,452	288,812
Net Position, Beginning of Year	<u>7,407,111</u>	<u>7,118,299</u>
Net Position, End of Year	<u>\$ 7,519,563</u>	<u>\$ 7,407,111</u>

See accompanying notes to financial statements.

Laurel County Water District No. 2
Statements of Cash Flows
For the Years Ended December 31, 2014 and 2013

	<u>2014</u>	<u>2013</u>
Cash Flows From Operating Activities		
Receipts from customers	\$ 2,312,198	\$ 2,344,427
Receipts from other activities	27,229	8,349
Payments to employees	(617,841)	(543,845)
Payments to suppliers	(812,681)	(880,793)
Payments for other activities	<u>(81,850)</u>	<u>(37,611)</u>
Net Cash Provided by Operating Activities	<u>827,055</u>	<u>890,527</u>
Cash Flows From Capital and Related Financing Activities		
Purchases of property, plant and equipment	(485,937)	(999,713)
Proceeds from sales of property, plant and equipment	3,009	6,367
Principal payments on debt	(223,545)	(201,840)
Proceeds from debt	97,500	-
Interest payments on debt	(355,683)	(363,141)
Federal and state grants	277,345	851,690
Other receipts	<u>6,000</u>	<u>6,000</u>
Net Cash Used by Capital and Related Financing Activities	<u>(681,311)</u>	<u>(700,637)</u>
Cash Flows From Investing Activities		
Interest on certificates of deposits	<u>2,050</u>	<u>2,002</u>
Net Cash Provided by Investing Activities	<u>2,050</u>	<u>2,002</u>
Net Increase in Cash and Cash Equivalents	147,794	191,892
Cash and Cash Equivalents at Beginning of Year	<u>2,403,025</u>	<u>2,211,133</u>
Cash and Cash Equivalents at End of Year	<u>\$ 2,550,819</u>	<u>\$ 2,403,025</u>
Reconciliation of cash per Statements of Net Position to cash per Statements of Cash Flows:		
Cash and cash equivalents	\$ 1,855,281	\$ 1,851,517
Restricted cash and cash equivalents:		
Customer deposits	82,568	77,481
Grant monies	711	685
Depreciation reserves-cash	441,119	399,264
Plant escrow	95,548	-
Bond and interest funds	<u>75,592</u>	<u>74,078</u>
Cash and Equivalents per Statements of Cash Flows	<u>\$ 2,550,819</u>	<u>\$ 2,403,025</u>

See accompanying notes to financial statements.

Laurel County Water District No. 2
 Statements of Cash Flows (Continued)
 For the Years Ended December 31, 2014 and 2013

	<u>2014</u>	<u>2013</u>
Reconciliation of Operating Income to Net Cash Provided by		
Operating Activities:		
Operating income	\$ 262,998	\$ 371,511
Adjustments to reconcile operating income to net cash provided by operating activities		
Depreciation and amortization	523,674	502,966
Changes in operating assets and liabilities:		
Decrease (increase) in accounts receivable	7,568	29,253
Decrease (increase) in inventory	80,236	(86,636)
Increase in prepaid expenses	(84)	(4,375)
(Decrease) increase in accounts payable	(47,677)	60,358
Increase in accrued expenses	340	17,450
	<hr/>	<hr/>
Net Cash Provided by Operating Activities	<u>\$ 827,055</u>	<u>\$ 890,527</u>

Laurel County Water District No. 2
Notes to Financial Statements
December 31, 2014 and 2013

Note 1 – Summary of Significant Accounting Policies

Reporting Entity

Laurel County Water District No. 2, of Laurel County, Kentucky (“District”) was created in 1963 under Chapter 74 of the Kentucky Revised Statutes. The District is governed by a five person Board of Commissioners appointed by the Laurel County Fiscal Court. The District is regulated by the Kentucky Public Service Commission.

Laurel County Water District No. 2’s financial statements include the operations of all entities for which the District exercises oversight responsibility. Oversight responsibility includes, but is not limited to, financial interdependency, selection of the governing authority, designation of management, ability to significantly influence operations, and accountability for fiscal matters. There are no other entities that are subject to the District’s oversight responsibility as indicated above.

Basis of Accounting, Financial Presentation and Measurement Focus

The basic financial statements of the District have been prepared in accordance with accounting principles generally accepted in the United States of America (“GAAP”) as applied to governmental units. The Governmental Accounting Standards Board (“GASB”) is the standard-setting body for governmental accounting and financial reporting. The GASB periodically updates its codification of the existing Governmental Accounting and Financial Reporting Standards which, along with subsequent GASB pronouncements (Statements and Interpretations), constitutes GAAP for governmental units.

The Statement of Net Position and Statement of Revenues, Expenses and Changes in Net Position display information about the District as a whole. These statements include all funds of the District. The statements distinguish between governmental and business-type activities. The District does not have any governmental activities.

The financial statements are prepared using the accrual basis of accounting. Revenues are recognized when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows.

Operating income reported by the District includes revenues and expenses related to the continuing operation of water service for its customers. Principal operating revenues are charges to customers for services. Principal operating expenses are the costs of providing the services and include administrative expenses and depreciation of capital assets. Other revenues and expenses are classified as non-operating in the financial statements.

Cash and Cash Equivalents

The District considers demand deposits and certificates of deposits with maturities of 90 days or less to be cash equivalents.

Inventories and Prepaid Expenses

Inventories consist of expendable supplies held for consumption stated on a weighted average cost basis. They are reported at cost and are recorded as an expenditure at the time individual items are used. Prepaid expenses include payments to vendors that benefit future reporting periods and are reported on the consumption basis.

Laurel County Water District No. 2
Notes to Financial Statements (Continued)
December 31, 2014 and 2013

Note 1 - Summary of Significant Accounting Policies (Continued)

Capital Assets

The District's property, plant and equipment with useful lives of more than one year are stated at historical cost. The costs of normal maintenance and repairs that do not add to the asset value or materially extend useful lives are not capitalized. Capital assets are depreciated using the straight-line method. When assets are disposed, the cost and applicable accumulated depreciation are removed from the respective accounts, and the resulting gain or loss is recorded in operations.

Estimated useful lives for depreciable assets are as follows:

Asset Classification	Range of Lives
Structures and improvements	40 years
Transmission distribution mains	40 years
Plant equipment	25 years
Meters and services	20 years
Other equipment and vehicles	5-10 years

Accounts Receivable

Receivables include amounts due from customers for water services. These receivables are due at the time the services are billed. Billing is completed monthly and accounts are considered past due on the sixteenth day after the end of each billing period. Accounts receivable are presented net of uncollectible accounts. The allowance amount is estimated using a percentage of accounts past due more than 90 days. The balance of the allowance at December 31, 2014 and 2013 was \$10,000.

Unbilled Accounts Receivable

Estimated unbilled revenues from water sales are recognized at the end of each fiscal year on a pro rata basis. The estimated amount is based on billing during the month following the close of the fiscal year.

Net Position

Net position is comprised of the various net earnings from operating income, non-operating revenues and expenses, and capital contributions. Net position is classified in the following three components:

Net investment in capital assets – This component of net position consists of capital assets, net of accumulated depreciation, reduced by the outstanding balances of any bonds, mortgages, notes or other borrowings that are attributable to the acquisition, construction or improvement of those assets.

Restricted – This component of net position consists of restricted assets less liabilities and deferred inflows of resources related to those assets. Restricted assets are those with limits on their use that are externally imposed constraints imposed by creditors (such as through debt covenants), grantors, contributors, or laws or regulations of other governments or constraints imposed by law through constitutional provisions or enabling legislation.

Unrestricted – This component of net position consists of net amounts of the assets, deferred outflows of resources, liabilities, and deferred inflows of resources that are not included in the determination of the net investment in capital assets or the restricted component of net position.

Laurel County Water District No. 2
Notes to Financial Statements (Continued)
December 31, 2014 and 2013

Note 1 - Summary of Significant Accounting Policies (Continued)

Use of Estimates

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

Note 2 – Restricted Assets

Under the terms of all loan resolutions, the District is required to maintain certain accounts and funds for the benefit and protection of the creditors. In addition, the District is also required to collect reasonable and sufficient rates and charges for services rendered, prohibited from selling, leasing or mortgaging any part of the system without prior approval, required to maintain the operating system in good condition and to carry adequate insurance on all properties to protect against loss or damage.

The resolutions require the District to establish a depreciation fund or reserve to be used to finance the cost of unusual repairs, renewals and replacements not included in the annual budget and to pay for future system extensions. The balance of these accounts at December 31, 2014 and 2013 was \$737,359 and \$598,442, respectively. Restricted assets also include customer deposits of \$82,568 and \$77,481 held at December 31, 2014 and 2013, respectively and grant monies of \$711 and \$685 held at December 31, 2014 and 2013, respectively.

Note 3 – Kentucky Revised Statute

At December 31, 2014 and 2013, all of the cash of the District was covered by federal depository insurance and securities pledged as collateral on behalf of the District. In accordance with Kentucky Revised Statute (KRS) 91A.060, the deposits are to be insured by the Federal Depository Insurance Corporation or collateralized to the extent uninsured by any obligations permitted by KRS 41.240(4). According to KRS 41.240(4), financial institutions shall either pledge or provide as collateral securities or other obligations having an aggregate current face value or current quoted market value at least equal to the deposits. According to KRS 91A.060, the District is allowed to invest in obligations of the U.S. Treasury and U.S. agencies, repurchase agreements, obligations of the Commonwealth of Kentucky and its agencies, interest bearing deposits of insured savings and loans, or interest bearing deposits of insured national or state banks. For additional cash descriptive information, see Note 1.

Note 4 – Custodial Credit Risk - Deposits

Custodial credit risk is the risk that in the event of a bank failure, the District's deposits may not be returned to it. The District does not have a deposit policy for custodial credit risk. As of December 31, 2014 and 2013, \$2,605,348 and \$2,339,375, respectively, of the District's total deposits at banks of \$3,105,348 and \$2,839,375, respectively, were exposed to custodial credit risk as follows:

	<u>2014</u>	<u>2013</u>
Uninsured and uncollateralized	\$ -	\$ -
Uninsured and collateral held by pledging bank	2,605,348	2,339,375
Uninsured and collateral held by pledging bank's trust department not in the District's name	-	-
Total	<u>\$ 2,605,348</u>	<u>\$ 2,339,375</u>

Laurel County Water District No. 2
Notes to Financial Statements (Continued)
December 31, 2014 and 2013

Note 5 – Capital Assets

The following is a summary of capital asset transactions for the year ended December 31, 2014:

	Balance Dec. 31, 2013	Additions	Dispositions	Balance Dec. 31, 2014
Land and improvements	\$ 496,336	\$ 10,250	\$ -	\$ 506,586
Building and improvements	490,637	102,020	-	592,657
Source of supply and pumping	3,560,392	-	-	3,560,392
Water treatment equipment	123,333	-	-	123,333
Transmission and distribution plant	14,087,712	316,983	-	14,404,695
Vehicles and other equipment	669,325	29,670	4,582	694,413
Construction in progress	-	5,500	-	5,500
Totals at historical cost	<u>19,427,735</u>	<u>464,423</u>	<u>4,582</u>	<u>19,887,576</u>
Less accumulated depreciation for:				
Land and improvements	4,000	1,034	-	5,034
Building and improvements	416,483	10,399	-	426,882
Source of supply and pumping	392,390	87,017	-	479,407
Water treatment equipment	82,830	4,687	-	87,517
Transmission and distribution plant	4,160,867	383,816	-	4,544,683
Vehicles and other equipment	498,959	34,704	4,161	529,502
Total accumulated depreciation	<u>5,555,529</u>	<u>521,657</u>	<u>4,161</u>	<u>6,073,025</u>
Capital assets - net	<u>\$ 13,872,206</u>	<u>\$ (57,234)</u>	<u>\$ 421</u>	<u>\$ 13,814,551</u>

Laurel County Water District No. 2
Notes to Financial Statements (Continued)
December 31, 2014 and 2013

Note 5 – Capital Assets (Continued)

The following is a summary of capital asset transactions for the year ended December 31, 2013:

	Balance Dec. 31, 2012	Additions	Dispositions	Balance Dec. 31, 2013
Land and improvements	\$ 496,336	\$ -	\$ -	\$ 496,336
Building and improvements	485,153	5,484	-	490,637
Source of supply and pumping	3,503,559	56,833	-	3,560,392
Water treatment equipment	123,333	-	-	123,333
Transmission and distribution plant	13,150,021	937,691	-	14,087,712
Vehicles and other equipment	625,459	56,366	12,500	669,325
Construction in progress	642,509	309,707	952,216	-
Totals at historical cost	<u>19,026,370</u>	<u>1,366,081</u>	<u>964,716</u>	<u>19,427,735</u>
Less accumulated depreciation for:				
Land and improvements	3,000	1,000	-	4,000
Building and improvements	407,669	8,814	-	416,483
Source of supply and pumping	306,429	85,961	-	392,390
Water treatment equipment	78,144	4,686	-	82,830
Transmission and distribution plant	3,796,881	363,986	-	4,160,867
Vehicles and other equipment	474,958	36,501	12,500	498,959
Total accumulated depreciation	<u>5,067,081</u>	<u>500,948</u>	<u>12,500</u>	<u>5,555,529</u>
Capital assets - net	<u>\$ 13,959,289</u>	<u>\$ 865,133</u>	<u>\$ 952,216</u>	<u>\$ 13,872,206</u>

Note 6 – Notes Payable and Long-Term Debt

The following is a summary of long-term debt transactions for the year ended December 31, 2014:

	Balance Dec. 31, 2013	Additions	Payments	Balance Dec. 31, 2014	Due Within One Year
Loan payable to Kentucky Infrastructure Authority, principal and interest at the rate of 1.6%, payable on a semi-annual basis, with final payment due December 1, 2025.	\$ 213,870	\$ -	\$ 15,586	\$ 198,284	\$ 15,836
Loan payable to Kentucky Infrastructure Authority, payable monthly in varying principal amounts, with final payment due June 1, 2017; interest payable on semi-annual basis at rates graduated from 3.75% to 5.325% over the life of the loan.	202,500	-	55,000	147,500	57,500

Laurel County Water District No. 2
Notes to Financial Statements (Continued)
December 31, 2014 and 2013

Note 6 – Notes Payable and Long-Term Debt (Continued)

	<u>Balance</u> <u>Dec. 31, 2013</u>	<u>Additions</u>	<u>Payments</u>	<u>Balance</u> <u>Dec. 31, 2014</u>	<u>Due Within</u> <u>One Year</u>
Loan payable to GMAC Commercial Mortgage Corporation, payable annually in varying principal amounts, with final payment due January 1, 2019; interest payable on a semi-annual basis at the rate of 5.0%	104,000	-	24,000	80,000	25,000
Loan payable to United States Department of Agriculture, payable annually in varying principal amounts, with final payment due June 1, 2036; interest payable on a semi-annual basis at the rate of 4.5%	428,000	-	11,000	417,000	11,500
Line of credit payable to the First National Bank of London, payable monthly at a rate of 66% of the Wall Street prime rate, maturing March 15, 2015	18,959	97,500	18,959	97,500	97,500
Loan payable to United States Department of Agriculture, payable annually in varying principal amounts with final payment due January 1, 2051. Interest payable on semi-annual basis at the rate of 4.125%	6,002,000	-	66,000	5,936,000	69,000
Loan payable to United States Department of Agriculture, payable annually in varying principal amounts with final payment due January 1, 2051. Interest payable on semi-annual basis at the rate of 3.00%	2,288,000	-	33,000	2,255,000	34,000
	<u>\$ 9,257,329</u>	<u>\$ 97,500</u>	<u>\$ 223,545</u>	<u>\$ 9,131,284</u>	<u>\$ 310,336</u>

Laurel County Water District No. 2
Notes to Financial Statements (Continued)
December 31, 2014 and 2013

Note 6 – Notes Payable and Long-Term Debt (Continued)

The following is a summary of long-term debt transactions for the year ended December 31, 2013:

	<u>Dec. 31, 2012</u>	<u>Additions</u>	<u>Payments</u>	<u>Dec. 31, 2013</u>	<u>One Year</u>
Loan payable to Kentucky Infrastructure Authority, principal and interest, at the rate of 1.6%, payable on a semi-annual basis, with final payment due December 1, 2026	\$ 229,210	\$ -	\$ 15,340	\$ 213,870	\$ 15,586
Loan payable to Kentucky Infrastructure Authority, payable monthly in varying principal amounts, with final payment due June 1, 2017; interest payable on a semi-annual basis at rates graduated from 3.75% to 5.325% over the life of the loan	255,000	-	52,500	202,500	55,000
Loan payable to GMAC Commercial Mortgage Corporation, payable annually in varying principal amounts, with final payment due January 1, 2019; interest payable on a semi-annual basis at the rate of 5.0%	127,000	-	23,000	104,000	24,000
Loan payable to United States Department of Agriculture, payable annually in varying principal amounts, with final payment due June 1, 2036; interest payable on a semi-annual basis at the rate of 4.5%	438,500	-	10,500	428,000	11,000
Line of credit payable to the First National Bank of London, payable monthly at a rate of 66% of the Wall Street prime rate, maturing March 15, 2013	24,459	-	5,500	18,959	18,959

Laurel County Water District No. 2
Notes to Financial Statements (Continued)
December 31, 2014 and 2013

Note 6 – Notes Payable and Long-Term Debt (Continued)

	<u>Balance</u> <u>Dec. 31, 2012</u>	<u>Additions</u>	<u>Payments</u>	<u>Balance</u> <u>Dec. 31, 2013</u>	<u>Due Within</u> <u>One Year</u>
Loan payable to United States Department of Agriculture, payable annually in varying principal amounts with final payment due January 1, 2051. Interest payable on semi- annual basis at the rate of 4.125%	6,065,000	-	63,000	6,002,000	66,000
Loan payable to United States Department of Agriculture, payable annually in varying principal amounts with final payment due January 1, 2051. Interest payable on semi- annual basis at the rate of 3.00%	<u>2,320,000</u>	<u>-</u>	<u>32,000</u>	<u>2,288,000</u>	<u>33,000</u>
	<u>\$ 9,459,169</u>	<u>\$ -</u>	<u>\$ 201,840</u>	<u>\$ 9,257,329</u>	<u>\$ 223,545</u>

All revenues from water are pledged as collateral on the loans payable to the Kentucky Infrastructure Authority.

The aggregate annual principal repayments on long-term debt are summarized as follows:

<u>Due the year</u> <u>ending</u> <u>December 31,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2015	\$ 310,336	\$ 345,793	\$ 656,129
2016	222,090	337,421	559,511
2017	198,349	328,288	526,637
2018	145,612	320,200	465,812
2019	150,879	314,951	465,830
2020-2024	850,048	1,488,102	2,338,150
2025-2029	959,970	1,322,274	2,282,244
2030-2034	1,144,500	1,125,703	2,270,203
2035-2039	1,311,000	888,195	2,199,195
2040-2044	1,536,500	624,002	2,160,502
2045-2049	1,885,500	303,628	2,189,128
2050-2053	<u>416,500</u>	<u>16,050</u>	<u>432,550</u>
	<u>\$ 9,131,284</u>	<u>\$ 7,414,607</u>	<u>\$ 16,545,891</u>

Laurel County Water District No. 2
Notes to Financial Statements (Continued)
December 31, 2014 and 2013

Note 7 – Retirement Plan

The District's full time employees are covered under the County Employee's Retirement System (CERS), a cost sharing, multiple-employer, public employers retirement system. Funding for the plan is provided through payroll withholdings and contributions by the District. Employees hired before September 1, 2008 are withheld at the rate of 5% of the employee's total compensation subject to contribution. Employees hired on or after September 1, 2008 are withheld at the rate of 6% of the employee's total compensation subject to contribution. The District's contribution rate for the years ended December 31, 2014 and 2013 were 17.67% and 18.89%, respectively.

The District's payroll for the years ended December 31, 2014, 2013, and 2012 that was covered by CERS was \$625,357, \$548,699, and \$488,938, respectively.

The District's contribution requirement for CERS for the years ended December 31, 2014, 2013, and 2012 was \$109,297, \$98,374, and \$91,384, respectively.

Benefits under the plan will vary based on final compensation, years of service and other factors as fully described in the Plan documents.

The CERS issues a publicly available financial report that includes financial statements and required supplementary information. That report may be obtained by writing to Kentucky Retirement Systems, 1260 Louisville Road, Frankfort, Kentucky 40601.

Note 8 – Risk Management

The District is exposed to various risks of loss related to limited torts; theft of, damage to and destruction of assets; errors and omissions and natural disasters for which the District carries commercial insurance. There have been no significant reductions in coverage for the year and settlements have not exceeded coverage in the past three years.

Note 9 – Correction of Error

Due to a pricing error in the calculation of inventories, the amount reported for inventories at December 31, 2013 was overstated by \$36,015 and chemical expense for the year ended December 31, 2013 was understated by the same amount. The amounts reported in the 2013 financial statements have been restated to reflect the correct amounts.

Note 10 - Subsequent Events

Date of Management Evaluation

Management of the District has evaluated subsequent events through April 29, 2015, the date on which the financial statements were available to be issued.

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
Laurel County Water District No. 2
London, Kentucky

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Audit Standards* issued by the Comptroller General of the United States, the financial statements of the business-type activities of Laurel County Water District No. 2 as of and for the year ended December 31, 2014 and the related notes to the financial statements, which collectively comprise the Laurel County Water District No. 2's basic financial statements, and have issued our report thereon dated April 29, 2015.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered Laurel County Water District No. 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 Laurel County Water District No. 2's internal control. Accordingly, we do not express an opinion on the effectiveness of the District's internal control.

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

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

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Laurel County Water District No. 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 no instances of noncompliance and other matters that are required to be reported under *Government Auditing Standards*.

Purpose of this Report

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

Christian Sturgeon & Associates, PSC

Christian Sturgeon & Associates, PSC
London, Kentucky

April 29, 2015