

**BUTLER COUNTY  
WATER SYSTEM, INC.**

**FINANCIAL STATEMENTS**

**DECEMBER 31, 2017 AND 2016**

**BUTLER COUNTY WATER SYSTEM, INC.**

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DECEMBER 31, 2017 AND 2016**

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## INDEPENDENT AUDITORS' REPORT

Board of Directors  
Butler County Water System, Inc.  
Morgantown, Kentucky

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

We have audited the accompanying financial statements of the Butler County Water System, Inc. (the "Utility") which comprise the balance sheet as of December 31, 2017 and 2016, and the related statements of operations, changes in members' equity and cash flows for the years then ended, and the related notes to the financial statements.

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

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

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

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

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

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

## ***Opinion***

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Butler County Water System, Inc. as of December 31, 2017 and 2016, and the changes in its financial position and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

## **Other Matters**

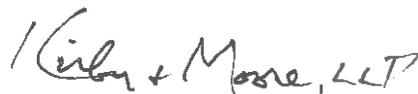
### ***Supplemental and Other Information***

Our audit was conducted for the purpose of forming an opinion on the financial statements as a whole. The schedules of budgetary comparison on pages 19 and 20 are presented for purposes of additional analysis and are not a required part of the basic financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated, in all material respects, in relation to the financial statements as a whole.

The financial and statistical highlights have not been subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we do not express an opinion or provide any assurance on them.

### **Other Reporting Required by *Government Auditing Standards***

In accordance with *Government Auditing Standards*, we have also issued our report dated April 9, 2018, on our consideration of the Utility's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Utility's internal control over financial reporting and compliance.



Kirby & Moore, LLP  
Bowling Green, Kentucky  
April 9, 2018

**BUTLER COUNTY WATER SYSTEM, INC.**  
**FINANCIAL AND STATISTICAL HIGHLIGHTS**

The following are financial and statistical highlights of Butler County Water System, Inc. for year ending December 31, 2017 and 2016.

- The System's assets totaled \$21,308,828 and decreased by \$107,925, or -0.5% from the prior year. The decrease in assets reflects the reduction in property, plant, and equipment by accumulated depreciation recorded throughout the year.
- Operating revenue for the year totaled \$1,948,135 and increased by \$31,853 from the prior year, a 1.7% increase. Operating expenses totaled \$1,766,195 for the year and increased by \$35,601 from last year, a 2.1% increase. Operating revenues increased due to weather driven customer demand which increased metered sales, and operating expenses which increased due to repairs and the System's contribution to the Rochester Dam Rural Water Commission.
- Metered sales totaled \$1,890,640 and increased by \$32,957 from the prior year, a 1.8% increase. Residential sales increased by \$14,951, or 0.9%; commercial, agricultural, fire protection and other sales increased by \$18,006, or 8.2%.
- Total revenues were greater than budgeted revenue by \$58,227 and total expenses were greater than budgeted expenses by \$31,584. Net income of \$30,043 exceeded budget by \$26,643.
- The System uses Green River as a water source and produces water at its water treatment facility located on Middle Ferry Road in Morgantown, Kentucky. Total gallons produced for the year amounted to 309.4 million gallons compared to 307.7 million gallons in the prior year, an increase of 1.7 million gallons, or 0.55%. The peak production month was September 2017 which produced 29.4 million gallons and the peak production day was in July 2017 which produced 1.1 million gallons.
- Total gallons sold to the System's customers during the year amounted to 253.5 million gallons compared to 247.3 million gallons in the prior year, an increase of 6.2 million gallons, or 2.5%. The peak demand month was September 2017 with 24.3 million gallons sold.
- The average monthly usage per residential customer was 3,990 gallons compared to 3,961 gallons in the prior year, a 0.7% increase. The average monthly usage per commercial customer was 9,438 gallons compared to 8,711 gallons in the prior year, a 8.3% increase.
- The number of customers at the end of the year totaled 4,854 consisting of 4,545 residential customers and 309 commercial and other class customers.
- The System received 43 new meter applications throughout the year.
- The System has a total of 515 miles of distribution main serving an average of 9.4 customers per mile and 31 miles of service line.

## **FINANCIAL STATEMENTS**

**BUTLER COUNTY WATER SYSTEM, INC.**

**BALANCE SHEETS**  
**December 31, 2017 and 2016**

|  | 2017                 | 2016                 |
|--|----------------------|----------------------|
| <b>ASSETS</b>  |                      |                      |
| Current assets   |                      |                      |
| Cash and cash equivalents  | \$ 1,056,799         | \$ 859,293           |
| Short-term investments   | 500,000              | 500,000              |
| Accounts receivable  |                      |                      |
| Customer accounts receivable, net of allowance for uncollectibles of \$87,131 and \$86,003 | 72,847               | 67,320               |
| Accounts receivable - WCWD   | 57,441               | 61,099               |
| Accounts receivable - SCWD   | —                    | 27                   |
| Prepaid expenses   | <u>17,801</u>        | <u>18,837</u>        |
| Total current assets   | <u>1,704,888</u>     | <u>1,506,576</u>     |
| <b>PROPERTY, PLANT AND EQUIPMENT</b>   |                      |                      |
| Land and land rights   | 101,521              | 101,521              |
| Utility plant in service   | 28,783,326           | 28,606,234           |
| Construction in progress   | 379,427              | 256,683              |
| Less: accumulated depreciation   | <u>( 10,261,545)</u> | <u>( 9,645,211)</u>  |
| Property, plant and equipment, net   | <u>19,002,729</u>    | <u>19,319,227</u>    |
| <b>OTHER ASSETS</b>  |                      |                      |
| Restricted cash and cash equivalents   | 316,834              | 335,233              |
| Restricted investments   | 146,444              | 140,815              |
| Deferred charges   | <u>137,933</u>       | <u>114,902</u>       |
| Total other assets   | <u>601,211</u>       | <u>590,950</u>       |
| Total assets   | <u>\$ 21,308,828</u> | <u>\$ 21,416,753</u> |

See Notes to Financial Statements

|  | 2017                 | 2016                 |
|--|----------------------|----------------------|
| <b>LIABILITIES AND MEMBERS' EQUITY</b> |                      |                      |
| <b>Liabilities</b>                     |                      |                      |
| <b>Current liabilities</b>             |                      |                      |
| Accounts payable                       | \$ 52,870            | \$ 31,112            |
| Accounts payable - WCWD                | 105,468              | 80,542               |
| Accrued interest payable               | 58,725               | 61,408               |
| Other current liabilities              | 6,573                | 5,364                |
| Current portion of long-term debt      | <u>193,658</u>       | <u>215,186</u>       |
| Total current liabilities              | <u>417,294</u>       | <u>393,612</u>       |
| <b>Long-term liabilities</b>           |                      |                      |
| Rebates payable                        | 9,450                | 9,450                |
| Customer deposits                      | 147,634              | 139,885              |
| Loan payable                           | <u>3,846,628</u>     | <u>4,040,603</u>     |
| Total long-term liabilities            | <u>4,003,712</u>     | <u>4,189,938</u>     |
| Total liabilities                      | <u>4,421,006</u>     | <u>4,583,550</u>     |
| <b>MEMBERS' EQUITY</b>                 |                      |                      |
| Capital investments                    | 14,409,037           | 14,384,463           |
| Retained earnings                      | <u>2,478,785</u>     | <u>2,448,740</u>     |
| Total members' equity                  | <u>16,887,822</u>    | <u>16,833,203</u>    |
| Total liabilities and members' equity  | <u>\$ 21,308,828</u> | <u>\$ 21,416,753</u> |

**BUTLER COUNTY WATER SYSTEM, INC.**

**STATEMENTS OF OPERATIONS**  
**December 31, 2017 and 2016**

|                                    | <b>2017</b>      | <b>2016</b>      |
|------------------------------------|------------------|------------------|
| <b>Operating revenues</b>          |                  |                  |
| Metered sales                      |                  |                  |
| Residential                        | \$ 1,652,687     | \$ 1,637,736     |
| Commercial                         | <u>237,953</u>   | <u>219,947</u>   |
| Total metered sales                | 1,890,640        | 1,857,683        |
| Forfeited discounts                | 30,311           | 31,715           |
| Miscellaneous service revenue      | <u>27,184</u>    | <u>26,884</u>    |
| Total operating revenues           | <u>1,948,135</u> | <u>1,916,282</u> |
| <b>Operating expenses</b>          |                  |                  |
| Pumping expense                    |                  |                  |
| Purchased power                    | 42,045           | 41,774           |
| Materials and supplies             | —                | 135              |
| Insurance                          | 2,869            | 2,914            |
| Miscellaneous                      | 2,812            | 2,145            |
| Professional services              | <u>708</u>       | <u>794</u>       |
| Total pumping expense              | <u>48,434</u>    | <u>47,762</u>    |
| Water treatment expense            |                  |                  |
| Purchased power                    | 87,716           | 85,908           |
| Purchased water                    | 4                | —                |
| Chemicals                          | 56,437           | 58,168           |
| Materials and supplies             | 16,279           | 16,637           |
| Insurance                          | 5,737            | 5,828            |
| Salaries and benefits              | 97,170           | 87,466           |
| Contractual services               | 675              | 3,103            |
| Miscellaneous                      | 4,842            | 4,717            |
| Professional services              | <u>1,416</u>     | <u>1,587</u>     |
| Total water treatment expense      | <u>270,276</u>   | <u>263,414</u>   |
| General distribution expense       |                  |                  |
| Purchased power                    | 4,265            | 4,252            |
| Salaries and benefits              | 101,805          | 109,312          |
| Materials and supplies             | 26,017           | 18,865           |
| Insurance                          | 12,430           | 12,627           |
| Miscellaneous                      | 17,888           | 20,945           |
| Contractual services               | 24,304           | 17,351           |
| Professional services              | <u>709</u>       | <u>795</u>       |
| Total general distribution expense | <u>187,418</u>   | <u>184,147</u>   |

See Notes to Financial Statements

**BUTLER COUNTY WATER SYSTEM, INC.**

**STATEMENTS OF OPERATIONS (Continued)**  
**December 31, 2017 and 2016**

|  | 2017              | 2016              |
|--|-------------------|-------------------|
| Customer accounts expense                |                   |                   |
| Salaries and benefits                    | \$ 211,929        | \$ 229,652        |
| Contractual services                     | 53,353            | 53,595            |
| Uncollectible accounts                   | 2,885             | 2,337             |
| Materials and supplies                   | 904               | 2,461             |
| Insurance                                | 1,434             | 1,457             |
| Miscellaneous                            | 27,749            | 27,387            |
| Professional services                    | <u>2,125</u>      | <u>2,382</u>      |
| Total customer accounts expense          | <u>300,379</u>    | <u>318,271</u>    |
| Maintenance expense                      |                   |                   |
| Pumping equipment and storage expense    | 18,508            | 18,019            |
| Materials and supplies                   | 539               | —                 |
| Salaries and benefits                    | 126,335           | 116,289           |
| Contractual services                     | 35,021            | 33,740            |
| Professional services                    | <u>1,417</u>      | <u>1,588</u>      |
| Total maintenance expense                | <u>181,820</u>    | <u>169,636</u>    |
| Administrative and general expense       |                   |                   |
| Salaries and benefits                    | 90,480            | 86,292            |
| Other post-employment benefits           | 8,542             | —                 |
| Materials and supplies                   | 6,506             | 4,934             |
| Insurance                                | 2,499             | 2,522             |
| Miscellaneous                            | 3,197             | 3,073             |
| Contractual services                     | 35,971            | 42,477            |
| Professional services                    | <u>2,125</u>      | <u>2,382</u>      |
| Total administrative and general expense | <u>149,320</u>    | <u>141,680</u>    |
| Depreciation and amortization expense    | <u>628,548</u>    | <u>605,684</u>    |
| Total operating expenses                 | <u>1,766,195</u>  | <u>1,730,594</u>  |
| Operating income                         | <u>181,940</u>    | <u>185,688</u>    |
| Non-operating revenues (expenses)        |                   |                   |
| Non-utility income                       | 164               | 21                |
| Interest income                          | 9,227             | 7,757             |
| Interest expense on long-term debt       | ( 156,434)        | ( 163,576)        |
| Interest expense on customer deposits    | ( 937)            | ( 486)            |
| Gain on disposition of assets            | —                 | 3,875             |
| PSC taxes                                | <u>( 3,915)</u>   | <u>( 3,743)</u>   |
| Total non-operating revenues (expenses)  | <u>( 151,895)</u> | <u>( 156,152)</u> |
| Net income                               | <u>\$ 30,045</u>  | <u>\$ 29,536</u>  |

See Notes to Financial Statements

**BUTLER COUNTY WATER SYSTEM, INC.**

**STATEMENTS OF CHANGES IN MEMBERS' EQUITY**  
**Years Ended December 31, 2017 and 2016**

|                                      | <u>Retained Earnings</u> | <u>Contributions<br/>in Aid of<br/>Construction</u> | <u>Total</u>        |
|--------------------------------------|--------------------------|---|---------------------|
| Balance, December 31, 2015           | \$ 2,419,204             | \$14,364,177  | \$16,783,381        |
| Net income                           | 29,536                   | —   | 29,536              |
| Contributions in aid of construction | <u>—</u>                 | <u>20,286</u>                                       | <u>20,286</u>       |
| Balance, December 31, 2016           | 2,448,740                | 14,384,463  | 16,833,203          |
| Net income                           | 30,045                   | —   | 30,045              |
| Contributions in aid of construction | <u>—</u>                 | <u>24,574</u>                                       | <u>24,574</u>       |
| Balance, December 31, 2017           | <u>\$ 2,478,785</u>      | <u>\$14,409,037</u>                                 | <u>\$16,887,822</u> |

See Notes to Financial Statements

**BUTLER COUNTY WATER SYSTEM, INC.**

**STATEMENTS OF CASH FLOWS**  
**Years Ended December 31, 2017 and 2016**

|   | 2017                | 2016                |
|---|---------------------|---------------------|
| <b>CASH FLOWS FROM OPERATING ACTIVITIES</b>                     |                     |                     |
| Receipts from customers and agencies                            | \$ 1,946,293        | \$ 1,908,978        |
| Payments to suppliers for goods and services                    | ( 502,357)          | ( 508,358)          |
| Payments for contractual services                               | ( 611,377)          | ( 611,034)          |
| Net cash provided by operating activities                       | <u>832,559</u>      | <u>789,586</u>      |
| <b>CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES</b>          |                     |                     |
| Interest paid on customer deposits                              | ( 937)              | ( 486)              |
| Net cash used in noncapital financial activities                | ( 937)              | ( 486)              |
| <b>CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES</b> |                     |                     |
| Proceeds from capital asset disposals                           | —                   | 3,875               |
| Principal repayment on long-term debt                           | ( 215,503)          | ( 209,789)          |
| Contributions in aid of construction                            | 24,574              | 20,286              |
| Purchases of capital assets                                     | ( 306,067)          | ( 567,329)          |
| Interest paid on long-term debt                                 | ( 159,117)          | ( 166,217)          |
| Net cash used in capital and related financing activities       | ( 656,113)          | ( 919,174)          |
| <b>CASH FLOWS FROM INVESTING ACTIVITIES</b>                     |                     |                     |
| Purchase of short-term investments                              | ( 5,629)            | ( 8,733)            |
| Interest income   | <u>9,227</u>        | <u>7,757</u>        |
| Net cash provided by (used in) investing activities             | <u>3,598</u>        | ( 976)              |
| Net increase (decrease) in cash and cash equivalents            | 179,107             | ( 131,050)          |
| Cash and cash equivalents, beginning of year                    | <u>1,194,526</u>    | <u>1,325,576</u>    |
| Cash and cash equivalents, end of year                          | <u>\$ 1,373,633</u> | <u>\$ 1,194,526</u> |

See Notes to Financial Statements

**BUTLER COUNTY WATER SYSTEM, INC.**

**STATEMENTS OF CASH FLOWS**  
**Years Ended December 31, 2017 and 2016**

|   | 2017               | 2016              |
|---|--------------------|-------------------|
| Reconciliation of operating income to net cash provided by operating activities           |                    |                   |
| Operating income  | \$ 181,940         | \$ 185,688        |
| Adjustment to reconcile net operating income to net cash provided by operating activities |                    |                   |
| Depreciation  | 622,565            | 599,337           |
| Amortization  | 5,983              | 6,347             |
| Non-utility income  | 164                | 21                |
| Payment of PSC taxes  | ( 3,915)           | ( 3,743)          |
| Changes in assets and liabilities   |                    |                   |
| Net increase in accounts receivable, net  | ( 1,842)           | ( 7,304)          |
| Net decrease in prepaid insurance   | 1,036              | 162               |
| Net (increase) decrease in deferred charges   | ( 29,014)          | 11,982            |
| Net increase (decrease) in accounts payable   | 46,684             | ( 7,701)          |
| Net increase in other current liabilities   | 1,209              | 254               |
| Net increase in customer deposits   | 7,749              | 7,243             |
| Net decrease in rebates payable   | <u>          —</u> | <u>( 2,700)</u>   |
| Net cash provided by operating activities   | <u>\$ 832,559</u>  | <u>\$ 789,586</u> |

See Notes to Financial Statements

**BUTLER COUNTY WATER SYSTEM, INC.**

**NOTES TO FINANCIAL STATEMENTS**

**December 31, 2017 and 2016**

**NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**Nature of Business**

The Butler County Water System, Inc. (the "Utility") is a water association organized as a non-profit corporation under KRS 273 and is under the authority of the Public Service Commission of Kentucky. The Utility provides a public water system to primarily citizens located in Butler County, Kentucky.

The accounting policies of the Utility conform to generally accepted accounting principles as applicable to a non-profit membership association. The following is a summary of the more significant policies:

**Reporting Entity**

The Utility is governed by a five-member board (the "Board"). The Board of Directors are elected by the members of the Utility. The Board has the power and authority to acquire, construct, maintain and operate the waterworks system.

**Basis of Accounting**

Basis of accounting refers to the point at which revenues or expenses are recognized in the accounts and reported in the financial statements. It relates to the timing of the measurements made regardless of the measurement focus applied. The accompanying financial statements have been prepared on the accrual basis of accounting.

The Utility follows the practice of recording metered sales when billed to the customers and recording related expenses when billed to the water utility. This results in a lag of recording revenue and related expenses. However, it does provide approximate matching of revenues and expenses and does not have a material effect between years. Operating revenues are revenues generated from general water operations (water sales, forfeited discounts and miscellaneous service revenue) and all other non-water revenues are considered non-operating revenues.

**BUTLER COUNTY WATER SYSTEM, INC.**

**NOTES TO FINANCIAL STATEMENTS**

**December 31, 2017 and 2016**

**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.

**Cash and Cash Equivalents**

The Utility has defined cash and cash equivalents to include all highly liquid investments (including restricted assets) with a maturity of three months or less when purchased to be cash equivalents.

**Accounts Receivable**

Customer accounts receivable amounts arise from monthly water usage. Based on Utility policy, water meters are read monthly, with billings occurring approximately ten days subsequent to the reading. Once billed, the customer has 16 days to pay the amount due. If payment is not made by the due date, a two to four day grace period is granted. If payment is not made at the expiration of the grace period, a late penalty is assessed to water charges and delinquent notices are sent. Customers are given 14 days from the date of the delinquent notice to render payment. Customer service places calls to facilitate collection; if no payment is received, collection trips are made to the service location. If collection does not occur, the meter is shut off. If collection is considered unlikely, the balances are charged off as a bad debt expense in the period in which they were deemed uncollectible.

Management's periodic evaluation of the adequacy of the allowance for doubtful accounts is based on past loss experience, known and other risks inherent to the specific amount, adverse situations that may affect the customer's ability to render payment and current economic conditions. Management considers many factors in determining whether a receivable is impaired, such as payment history and changes in employment.

**Concentration of Credit Risk**

The Utility extends credit to all citizens who live within the geographic location of the Utility and who utilize the utility system. Credit losses may be minimal and are generally within management's expectations.

**BUTLER COUNTY WATER SYSTEM, INC.**

**NOTES TO FINANCIAL STATEMENTS**

**December 31, 2017 and 2016**

**NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

**Investments**

Investments consist of certificates of deposit and are recorded at cost. The cost of investments approximates their fair value.

**Property, Plant and Equipment**

The Utility has an ongoing activity of assessing the feasibility of installing additional lines to new service areas. Once an extension is considered feasible, there are additional engineering studies, applications to various funding agencies and project administrative costs. The Utility defers the ongoing activity and capitalizes these costs as part of the utility plant upon completion of the project.

Management's capitalization policy is based upon the assets' estimated future benefit. Depreciation is computed using the straight-line method over the estimated useful lives of the utility plant. The estimated useful lives range from 5 to 50 years for utility plant assets. Upon retirement, the cost of the asset, less any proceeds, is charged to accumulated depreciation.

The Utility capitalizes construction period interest on loans that were obtained to finance construction.

**Income Taxes**

The Utility is a tax-exempt organization under Section 501(c)(12) of the Internal Revenue Code. Therefore, no provision for income taxes is made in the accompanying financial statements.

**Contributions in Aid of Construction**

Contributions in aid of construction consist of member fees, developer contributed utility systems, capital grants and other supplemental support by other utilities and industrial customers, and federal, state and local grants in support of system improvements.

**Uncertain Tax Positions**

The Utility follows accounting requirements associated with uncertainty in income taxes using the provisions of Financial Accounting Standards Board (FASB) ASC 740, *Income Taxes*. The guidance prescribed a minimum recognition threshold and measurement methodology that a tax position taken or expected to be taken in a tax

**BUTLER COUNTY WATER SYSTEM, INC.**

**NOTES TO FINANCIAL STATEMENTS**

**December 31, 2017 and 2016**

**NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

return is required before being recognized in the financial statements. It also provides guidance for derecognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. As of December 31, 2017, the Utility has no uncertain tax positions that qualify for recognition.

**Subsequent Events**

The Utility has evaluated any recognized or unrecognized subsequent events for consideration in the accompanying financial statements through April 9, 2018, which was the date the financial statements were made available.

**NOTE 2. CASH AND CASH EQUIVALENTS AND INVESTMENTS**

The Utility maintains its deposits with financial institutions insured by the Federal Deposit Insurance Corporation (FDIC). As of December 31, 2017 and 2016, the carrying amounts of the Utility's deposits were \$2,020,077 and \$1,835,341 and the bank balances were \$2,029,682 and \$1,949,591, respectively.

|                                      | 2017                | 2016                |
|--------------------------------------|---------------------|---------------------|
| Cash and cash equivalents            | \$ 1,056,799        | \$ 859,293          |
| Restricted cash and cash equivalents | 316,834             | 335,233             |
| Short-term investments               | 500,000             | 500,000             |
| Restricted investments               | <u>146,444</u>      | <u>140,815</u>      |
|                                      | <u>\$ 2,020,077</u> | <u>\$ 1,835,341</u> |

**Cash Concentration Risk - Deposits**

Custodial credit risk is the risk that in the event of a bank failure, the Utility's deposits may not be returned to it. The Utility's formal deposit policy for custodial credit risk requires deposits in banks which are in excess of the FDIC insurance coverage to be secured by the bank pledging securities in direct obligations of the United States of America or by approved security bonds. As of December 31, 2017 and 2016, the Utility's bank balance was not exposed to custodial credit risk.

**Restricted Cash and Cash Equivalents and Investments**

The sinking funds are restricted to the payment of principal and interest on long-term debt. The depreciation fund is restricted to payment for improvements and approved repairs. The customer deposits fund is restricted to hold customer deposits until

**BUTLER COUNTY WATER SYSTEM, INC.**

**NOTES TO FINANCIAL STATEMENTS**

**December 31, 2017 and 2016**

**NOTE 2. CASH AND CASH EQUIVALENTS AND INVESTMENTS (Continued)**

service is terminated. The construction fund is restricted by USDA Rural Development for Project 18 receipts and disbursements.

Restricted cash and cash equivalents and investments consist of the following as of December 31, 2017 and 2016:

|                   | <b>2017</b>       | <b>2016</b>       |
|-------------------|-------------------|-------------------|
| Sinking funds     | \$ 189,199        | \$ 200,748        |
| Depreciation fund | 123,135           | 134,485           |
| Customer deposits | 146,444           | 140,815           |
| Construction fund | <u>4,500</u>      | <u>—</u>          |
|                   | <u>\$ 463,278</u> | <u>\$ 476,048</u> |

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

Property, plant and equipment consists of the following as of December 31, 2017 and 2016:

|                                    | <b>2017</b>          | <b>2016</b>          |
|------------------------------------|----------------------|----------------------|
| <b>Non-depreciable</b>             |                      |                      |
| Land and land rights               | \$ 101,521           | \$ 101,521           |
| Construction in progress           | 379,427              | 256,683              |
| <b>Depreciable</b>                 |                      |                      |
| Utility plant in service           | 28,783,326           | 28,606,234           |
| Less: accumulated depreciation     | <u>( 10,261,545)</u> | <u>( 9,645,211)</u>  |
| Property, plant and equipment, net | <u>\$ 19,002,729</u> | <u>\$ 19,319,227</u> |

Depreciation expense was \$622,565 and \$599,337 for the years ended December 31, 2017 and 2016, respectively.

**NOTE 4. REBATES PAYABLE**

These amounts are partially made up of private developers' unrecovered costs in installing water lines. Utility plant was increased for a like amount when the facilities were donated to the Utility. As meters are placed in the development, the developer receives half of the new customers' contribution for meters connected directly to the extension over the next ten years or up to the value of facilities constructed. The remaining balance in this account was obtained from subscriptions of prospective users of the Utility. When a meter is installed, the subscribed amount is transferred to contributions in aid of construction.

**BUTLER COUNTY WATER SYSTEM, INC.**

**NOTES TO FINANCIAL STATEMENTS**

**December 31, 2017 and 2016**

**NOTE 5. LONG-TERM DEBT**

The loans below from Series 1977 through Series 2014 were issued through USDA Rural Development (RD). The Series 2012 loan was issued through Kentucky Rural Water Finance Corporation (KRWFC). Loans outstanding as of December 31, 2017 and 2016 consist of the following:

| <u>Original Amount</u> | <u>Series of</u> | <u>Interest Rate</u> | <u>2017</u>         | <u>2016</u>         |
|------------------------|------------------|----------------------|---------------------|---------------------|
| \$ 191,400             | 1977             | 5.00%                | \$ —                | \$ 10,297           |
| 152,000                | 1979             | 5.00%                | 5,200               | 13,673              |
| 950,000                | 1996             | 4.50%                | 655,993             | 677,617             |
| 197,214                | 1997             | 4.50%                | 129,143             | 134,148             |
| 545,000                | 1998             | 4.75%                | 349,615             | 363,054             |
| 3,045,000              | 2012             | 2.80%-4.00%          | 2,770,000           | 2,620,000           |
| 437,000                | 2014             | 2.75%                | 430,335             | 437,000             |
|                        |                  |                      | <u>\$ 4,040,286</u> | <u>\$ 4,255,789</u> |

All loans are secured by an exclusive pledge of a fixed portion of the income and revenues derived from the operation of the Utility's water distribution system. The RD loans each have a requirement for depreciation reserves. The KRWFC loan has requirements for a debt service sinking fund and a debt service coverage ratio. The Utility was in compliance with the depreciation reserve, debt service sinking fund and debt service coverage ratio requirements as of December 31, 2017 and 2016.

Principal and interest of various amounts are due at least annually in each of the years through 2054. The principal and interest due for each of the next five years and thereafter is as follows:

| <u>Year</u> | <u>Principal Amount</u> | <u>Interest Amount</u> |
|-------------|-------------------------|------------------------|
| 2018        | \$ 193,658              | \$ 152,628             |
| 2019        | 190,532                 | 146,521                |
| 2020        | 192,719                 | 140,420                |
| 2021        | 200,003                 | 134,150                |
| 2022        | 207,390                 | 127,639                |
| Thereafter  | <u>3,055,984</u>        | <u>926,270</u>         |
|             | <u>\$ 4,040,286</u>     | <u>\$ 1,627,628</u>    |

**BUTLER COUNTY WATER SYSTEM, INC.**

**NOTES TO FINANCIAL STATEMENTS**

**December 31, 2017 and 2016**

**NOTE 6. RELATED PARTIES**

The Warren County Water District (WCWD) provides management, engineering and repair and maintenance services to the Utility. Butler County Water System, Inc. shares common management with WCWD.

The following related party amounts were included in accounts receivable at December 31, 2017 and 2016:

|                               | 2017      | 2016      |
|-------------------------------|-----------|-----------|
| Warren County Water District  | \$ 57,441 | \$ 61,099 |
| Simpson County Water District | —         | 27        |

The following related party amounts were included in accounts payable at December 31, 2017 and 2016:

|                              | 2017       | 2016      |
|------------------------------|------------|-----------|
| Warren County Water District | \$ 105,468 | \$ 80,542 |

During 2017 and 2016, expenses from the WCWD amounted to \$1,051,332 and \$1,052,705, respectively, for the following:

|                                | 2017              | 2016                |
|--------------------------------|-------------------|---------------------|
| Wages and benefits:            |                   |                     |
| Operation                      | \$ 473,817        | \$ 500,479          |
| Administrative:                |                   |                     |
| Supervision and administration | 118,804           | 105,695             |
| Accounting                     | 40,638            | 45,036              |
| Customer service               | 91,954            | 89,666              |
| Engineering                    | 6,826             | 22,730              |
| Operations - other             | 125,867           | 135,243             |
| Additions to plant             | 117,548           | 116,175             |
| Special projects               | <u>15,172</u>     | <u>36,308</u>       |
| Totals                         | <u>\$ 990,626</u> | <u>\$ 1,051,332</u> |

In addition to the above expenses from WCWD totaling \$990,626 and \$1,051,332 for the years ending December 31, 2017 and 2016, respectively, the Utility also recognized other post-employment benefits (OPEB) expense of \$8,542 in 2017. WCWD accrues the projected value of retiree healthcare benefits earned during its

**BUTLER COUNTY WATER SYSTEM, INC.**

**NOTES TO FINANCIAL STATEMENTS  
December 31, 2017 and 2016**

**NOTE 6. RELATED PARTIES (Continued)**

employees' working lifetime. The OPEB expense of \$8,542 reflected in administrative and general expense in the statement of operations for 2017 is the Utility's proportionate share of annual OPEB costs (expense) recorded by WCWD.

In the ordinary course of business, the Utility has and expects to continue to have transactions with WCWD. In the opinion of management, such transactions were on substantially the same terms as those prevailing at the time of comparable transactions with other persons and did not involve more than a normal risk of collectability or present any other unfavorable features to the Utility.

**NOTE 7. RISKS OF LOSS**

The Utility's risks of loss are addressed by the purchase of commercial insurance. These areas include employee dishonesty bonds, property coverage, vehicle coverage and a public entity liability policy which includes errors and omission. Coverage is reviewed for adequacy by management and agents on an annual basis.

**NOTE 8. ROCHESTER DAM REGIONAL WATER COMMISSION**

The Rochester Dam Regional Water Commission ("RDRWC") is a water commission which was created by an Order issued by the Ohio County Judge/Executive on June 13, 2013 pursuant to the provision of KRS 74.440. Butler County Water System, Inc. participated in the creation of the RDRWC along with the City of Morgantown, Kentucky and the Ohio County Water District. The Board of Commissioners for the RDRWC is comprised of one representative from each of the three establishing entities plus two additional representatives appointed by the Ohio County Judge/Executive and approved by the Ohio County Fiscal Court.

The primary purpose of the RDRWC is to provide an adequate and dependable supply of water for the region which derives its water supply from Pool 3 of the Green River including, but not limited to, Butler, Muhlenberg, and Ohio Counties and all customers and entities served by the RDRWC members. RDRWC will endeavor to accomplish this purpose by (1) acquiring an ownership interest, either by lease, easement, or deed, in the Rochester Dam on Pool 3 of the Green River, (2) repairing and stabilizing the Rochester Dam; and (3) maintaining the Rochester Dam.

**BUTLER COUNTY WATER SYSTEM, INC.**

**NOTES TO FINANCIAL STATEMENTS  
December 31, 2017 and 2016**

**NOTE 8. ROCHESTER DAM REGIONAL WATER COMMISSION (Continued)**

In 2015, the RDRWC obtained a lease on the Rochester Dam from the Corp of Engineers in order to obtain funding through the EDA or other agency grants to perform the necessary repairs for the dam. Congress passed, and the President signed legislation in December, 2016 to permanently transfer the dam and associated property to RDRWC. In October, 2017, the RDRWC was awarded a \$3,000,000 grant from the U.S. Economic Development Administration towards the estimated \$4,000,000 dam repair cost. The RDRWC has issued bonds for the remaining cost and each facility withdrawing water from the pool will pay \$0.10 per 1,000 gallons withdrawn beginning January 1, 2018. As of December 31, 2017 and 2016, Butler County Water System, Inc. has incurred cumulative costs totaling \$33,030 and \$13,320, respectively, for its participation in the RDRWC.

**NOTE 9. COMMITMENTS**

**Project 18 Line Extension & AMR System**

Project 18 includes the construction of water main extensions and the installation of an automated meter reading (AMR) system. The water main extension portion of the project consists of five separate lines that will provide service to ten households which currently do not have access to an adequate supply of potable water. The total length of 4-inch water main to be installed is 22,860 feet. The mains will be installed on G. Sutherland Road, Tarvin Embry Road, Ruby Road, Whalen Cemetery Road, and Doc Hampton Road. The AMR portion of the project consists of a radio based meter reading system that will collect consumption data from the Utility's 4,854 customers using a drive-by system that will eliminate the need to physically read meters each month. The AMR system will include acoustic leak detection capabilities that continuously monitor mains and service lines for water leaks and provide notification during the data collection process. The estimated cost of the project is \$1,734,500 which will be funded by loan and grant proceeds from USDA—Rural Development of \$1,422,000 and \$250,000, respectively, and Utility funds of \$62,500. The project is expected to start installation in April, 2018 and be completed in May, 2019.

**BUTLER COUNTY WATER SYSTEM, INC.**

**SCHEDULE OF BUDGETARY COMPARISON  
Year Ended December 31, 2017**

|                                   | <u>Budgeted Amounts</u> |                  | <u>Actual</u>    | <u>Variances</u>                                       |
|-----------------------------------|-------------------------|------------------|------------------|--|
|                                   | <u>Original</u>         | <u>Final</u>     |                  | <u>Favorable<br/>(Unfavorable)<br/>Final to Actual</u> |
| <b>Revenues</b>                   |                         |                  |                  |  |
| Metered revenue                   | \$ 1,835,000            | \$ 1,835,000     | \$ 1,890,640     | \$ 55,640  |
| Forfeited discounts               | 31,340                  | 31,340           | 30,311           | ( 1,029)   |
| Miscellaneous service revenue     | 25,370                  | 25,370           | 27,091           | 1,721  |
| Interest income                   | 7,590                   | 7,590            | 9,227            | 1,637  |
| Other income                      | <u>—</u>                | <u>—</u>         | <u>258</u>       | <u>258</u>   |
| Total revenues                    | <u>1,899,300</u>        | <u>1,899,300</u> | <u>1,957,527</u> | <u>58,227</u>  |
| <b>Expenses</b>                   |                         |                  |                  |  |
| Salaries and wages                | 365,000                 | 365,000          | 363,634          | 1,366  |
| Commissioner fees                 | 18,000                  | 18,000           | 18,000           | —  |
| Fringe benefits                   | 240,780                 | 240,780          | 247,743          | ( 6,963)   |
| Purchased water                   | —                       | —                | 4                | ( 4)   |
| Purchased power                   | 137,000                 | 137,000          | 134,027          | 2,973  |
| Chemicals                         | 57,610                  | 57,610           | 56,437           | 1,173  |
| Materials and supplies            | 40,000                  | 40,000           | 50,245           | ( 10,245)  |
| Contractual services - Accounting | 8,500                   | 8,500            | 8,500            | —  |
| Contractual services - Other      | 136,400                 | 136,400          | 149,324          | ( 12,924)  |
| Rental of building and utilities  | 16,410                  | 16,410           | 16,155           | 255  |
| Equipment expense                 | 59,460                  | 59,460           | 52,781           | 6,679  |
| Insurance - general liability     | 25,200                  | 25,200           | 23,905           | 1,295  |
| Insurance - other                 | 1,060                   | 1,060            | 1,065            | ( 5)   |
| Regulatory expense                | 3,400                   | 3,400            | 3,915            | ( 515)   |
| Bad debt expense                  | 2,250                   | 2,250            | 2,885            | ( 635)   |
| Miscellaneous expense             | 3,120                   | 3,120            | 4,403            | ( 1,283)   |
| Depreciation                      | 615,450                 | 615,450          | 622,565          | ( 7,115)   |
| Amortization                      | 6,000                   | 6,000            | 5,983            | 17   |
| Interest expense                  | 160,260                 | 160,260          | 157,371          | 2,889  |
| OPEB expense                      | <u>—</u>                | <u>—</u>         | <u>8,542</u>     | <u>( 8,542)</u>  |
| Total expenses                    | <u>1,895,900</u>        | <u>1,895,900</u> | <u>1,927,484</u> | <u>( 31,584)</u>                                       |
| Net income                        | <u>\$ 3,400</u>         | <u>\$ 3,400</u>  | <u>\$ 30,043</u> | <u>\$ 26,643</u>                                       |

**BUTLER COUNTY WATER SYSTEM, INC.**

**SCHEDULE OF BUDGETARY COMPARISON  
Year Ended December 31, 2016**

|                                   | <u>Budgeted Amounts</u> |                  | <u>Actual</u>    | <u>Variances</u>                                       |
|-----------------------------------|-------------------------|------------------|------------------|--|
|                                   | <u>Original</u>         | <u>Final</u>     |                  | <u>Favorable<br/>(Unfavorable)<br/>Final to Actual</u> |
| <b>Revenues</b>                   |                         |                  |                  |  |
| Metered revenue                   | \$ 1,894,000            | \$ 1,894,000     | \$ 1,857,683     | (\$ 36,317)  |
| Forfeited discounts               | 31,500                  | 31,500           | 31,715           | 215  |
| Miscellaneous service revenue     | 29,700                  | 29,700           | 26,850           | ( 2,850)   |
| Interest income                   | 7,730                   | 7,730            | 7,757            | 27   |
| Other income                      | —                       | —                | 55               | 55   |
| Disposition gains (losses)        | —                       | —                | 3,875            | 3,875  |
| <b>Total revenues</b>             | <u>1,962,930</u>        | <u>1,962,930</u> | <u>1,927,935</u> | <u>( 34,995)</u>                                       |
| <b>Expenses</b>                   |                         |                  |                  |  |
| Salaries and wages                | 381,970                 | 381,970          | 366,533          | 15,437   |
| Commissioner fees                 | 18,000                  | 18,000           | 18,000           | —  |
| Fringe benefits                   | 272,360                 | 272,360          | 244,501          | 27,859   |
| Purchased power                   | 135,460                 | 135,460          | 131,935          | 3,525  |
| Chemicals                         | 56,000                  | 56,000           | 58,168           | ( 2,168)   |
| Materials and supplies            | 49,520                  | 49,520           | 43,032           | 6,488  |
| Contractual services - Accounting | 9,500                   | 9,500            | 9,527            | ( 27)  |
| Contractual services - Other      | 138,170                 | 138,170          | 150,267          | ( 12,097)  |
| Rental of building and utilities  | 15,780                  | 15,780           | 15,689           | 91   |
| Equipment expense                 | 70,960                  | 70,960           | 56,423           | 14,537   |
| Insurance - general liability     | 25,000                  | 25,000           | 24,282           | 718  |
| Insurance - other                 | 1,070                   | 1,070            | 1,065            | 5  |
| Regulatory expense                | 3,500                   | 3,500            | 3,743            | ( 243)   |
| Bad debt expense                  | 4,500                   | 4,500            | 2,337            | 2,163  |
| Miscellaneous expense             | 5,000                   | 5,000            | 3,151            | 1,849  |
| Depreciation                      | 591,380                 | 591,380          | 599,337          | ( 7,957)   |
| Amortization                      | 6,350                   | 6,350            | 6,347            | 3  |
| Interest expense                  | <u>165,670</u>          | <u>165,670</u>   | <u>164,062</u>   | <u>1,608</u>   |
| <b>Total expenses</b>             | <u>1,950,190</u>        | <u>1,950,190</u> | <u>1,898,399</u> | <u>51,791</u>  |
| <b>Net income</b>                 | <u>\$ 12,740</u>        | <u>\$ 12,740</u> | <u>\$ 29,536</u> | <u>\$ 16,796</u>                                       |



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

Board of Directors  
Butler County Water System, Inc.  
Morgantown, Kentucky

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the Butler County Water System, Inc. (the "Utility") (a nonprofit organization), which comprise the balance sheet as of December 31, 2017, and the related statements of operations and cash flows for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated April 9, 2018.

**Internal Control Over Financial Reporting**

In planning and performing our audit of the financial statements, we considered the Utility'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 the Utility's internal control. Accordingly, we do not express an opinion on the effectiveness of the Utility'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 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.

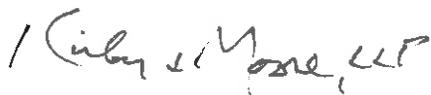
Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not 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 the Utility's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

### **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 Utility's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.



Kirby & Moore, LLP  
Bowling Green, Kentucky  
April 9, 2018