

**NORTH SHELBY WATER COMPANY**  
**BASIC FINANCIAL STATEMENTS,**  
**SUPPLEMENTARY INFORMATION,**  
**AND INDEPENDENT AUDITOR'S REPORTS**

**At December 31, 2018 and 2017**

**NORTH SHELBY WATER COMPANY  
BASIC FINANCIAL STATEMENTS,  
SUPPLEMENTARY INFORMATION,  
AND INDEPENDENT AUDITOR'S REPORTS**

**Years Ended December 31, 2018 and 2017**

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# RAISOR, ZAPP & WOODS, PSC

## Certified Public Accountants

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### INDEPENDENT AUDITOR'S REPORT

To the Board of Directors of the  
North Shelby Water Company  
Bagdad, Kentucky 40003

#### Report on the Financial Statements

We have audited the accompanying financial statements of North Shelby Water Company as of and for the years ended December 31, 2018 and 2017, and the related notes to the financial statements, which collectively comprise the North Shelby Water Company's basic financial statements as listed in the table of contents.

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

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

#### *Auditor's Responsibility*

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

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

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

#### *Opinion*

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the North Shelby Water Company, as of December 31, 2018 and 2017, 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.

#### *Change in Accounting Principle*

As discussed in Note 20 to the financial statements, in 2018 the Water Company adopted new accounting guidance, GASBS No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*. Our opinion is not modified with respect to this matter.

**Other Matters**

*Required Supplementary Information*

Accounting principles generally accepted in the United States of America require that the required supplementary information listed in the Table of Contents on pages 29 through 32 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Management has omitted the management's discussion and analysis that accounting principles generally accepted in the United States of America require to be presented to supplement the basic financial statements. Such missing information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. Our opinion on the basic financial statements is not affected by this missing information.

*Other Information*

Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise the North Shelby Water Company's basic financial statements. The schedule of expenditures of federal awards as required by Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards*, is presented for purposes of additional analysis and is not a required part of the basic financial statements.

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

**Other Reporting Required by Government Auditing Standards**

In accordance with *Government Auditing Standards*, we have also issued our report dated June 28, 2019, on our consideration of the North Shelby Water Company'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 solely 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 effectiveness of the North Shelby Water Company's 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 North Shelby Water Company's internal control over financial reporting and compliance.

*Raisor, Zapp & Woods, PSC*

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

June 28, 2019

**NORTH SHELBY WATER COMPANY**  
**STATEMENT OF NET POSITION**  
**December 31, 2018 and 2017**

	<u>2018</u>	<u>Restated 2017</u>
<b>ASSETS</b>		
<b>Current Assets:</b>		
Cash	\$ 3,045,139	\$ 2,362,486
Accounts Receivable (Net)	251,421	255,566
Other Receivables	59,218	25,005
Inventory	156,205	135,801
Prepaid Expenses	54,435	42,849
Total Current Assets	<u>\$ 3,566,418</u>	<u>\$ 2,821,707</u>
<b>Noncurrent Assets:</b>		
Restricted Assets:		
Cash, Including Time Deposits	\$ 1,736,034	\$ 1,007,972
Capital Assets (Net)	17,002,691	15,441,550
Total Noncurrent Assets	<u>\$ 18,738,725</u>	<u>\$ 16,449,522</u>
Total Assets	<u>\$ 22,305,143</u>	<u>\$ 19,271,229</u>
<b>DEFERRED OUTFLOWS OF RESOURCES</b>		
Attributable to Employee Pension Plan	\$ 237,483	\$ 335,042
Attributable to OPEB Plan	77,422	93,176
Total Deferred Outflows of Resources	<u>\$ 314,905</u>	<u>\$ 428,218</u>
<b>LIABILITIES</b>		
<b>Current Liabilities:</b>		
Accounts Payable	\$ 194,121	\$ 156,172
Accounts Payable - Construction	270,676	-
Retainage Payable - Construction	81,353	-
Funds Held for Future Lines	692,438	-
Accrued Compensated Absences	9,962	9,435
Accrued Employee Benefits	7,704	6,214
Accrued Payroll Taxes/Employee Withholding	7,064	6,574
Utility Tax Payable	6,823	6,376
Sales Tax Payable	312	226
Current Liabilities Payable from Restricted Assets:		
Accrued Interest Payable - Customer Deposits	5,251	2,671
Accrued Interest Payable - Notes Payable	66,054	59,449
Notes Payable	168,609	83,741
Total Current Liabilities	<u>\$ 1,510,367</u>	<u>\$ 330,858</u>
<b>Noncurrent Liabilities:</b>		
Notes Payable	\$ 7,806,541	\$ 6,450,165
Customer Deposits Payable	296,135	287,337
Net Pension Liability	1,104,599	1,093,398
Net OPEB Liability	322,001	375,532
Total Noncurrent Liabilities	<u>\$ 9,529,276</u>	<u>\$ 8,206,432</u>
Total Liabilities	<u>\$ 11,039,643</u>	<u>\$ 8,537,290</u>
<b>DEFERRED INFLOWS OF RESOURCES</b>		
Attributable to Employee Pension Plan	\$ 101,622	\$ 104,598
Attributable to OPEB Plan	70,054	19,662
Total Deferred Inflows of Resources	<u>\$ 171,676</u>	<u>\$ 124,260</u>
<b>NET POSITION</b>		
Net Investment in Capital Assets	\$ 8,675,512	\$ 8,907,644
Restricted for Capital Projects	1,041,898	129,332
Restricted for Debt Service	628,082	819,191
Unrestricted	1,063,237	1,181,730
Total Net Position	<u>\$ 11,408,729</u>	<u>\$ 11,037,897</u>

**NORTH SHELBY WATER COMPANY**  
**STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN FUND NET POSITION**  
**For the Years Ended December 31, 2018 and 2017**

	<u>2018</u>	<u>Restated 2017</u>
<b>Operating Revenues:</b>		
<b>Charges for Services:</b>		
Water Charges (Net of Estimated Bad Debts)	\$ 2,967,492	\$ 2,767,490
Total Charges for Services	<u>\$ 2,967,492</u>	<u>\$ 2,767,490</u>
<b>Other Charges and Miscellaneous:</b>		
Forfeited Discounts & Service Charges	\$ 69,620	\$ 71,368
Building Rental Income	30,000	28,000
Equipment Rental Income	45,427	38,192
Contractual Services	134,226	130,761
Miscellaneous	16,310	29,980
Total Other Charges and Miscellaneous	<u>\$ 295,583</u>	<u>\$ 298,301</u>
Total Operating Revenues	<u>\$ 3,263,075</u>	<u>\$ 3,065,791</u>
<b>Operating Expenses:</b>		
Accounting and Collecting Labor	\$ 311,241	\$ 303,507
Commissioner Fees	37,400	34,200
Contractual Service	90,420	95,518
Employee Benefits	189,972	189,622
Employee Retirement Expense	172,959	216,843
Insurance	50,068	52,442
Maintenance of Mains	88,039	79,679
Miscellaneous	21,905	12,750
Office Supplies and Expense	84,353	63,171
Operating Labor	72,200	65,709
Other Interest Expense	5,822	3,945
Payroll Taxes	37,379	36,759
Professional Services	42,368	46,282
Purchased Water	1,068,534	1,006,961
Purchased Power	67,807	72,798
Regulatory Fees	6,152	5,681
Transportation Expense	36,799	31,114
Utilities	23,812	26,893
Depreciation Expense	602,180	553,270
Total Operating Expenses	<u>\$ 3,009,410</u>	<u>\$ 2,897,144</u>
Operating Income (Loss)	<u>\$ 253,665</u>	<u>\$ 168,647</u>
<b>Nonoperating Revenue (Expense):</b>		
Investment Income	\$ 6,782	\$ 5,286
Interest Expense	(201,562)	(152,582)
Gain (Loss) on Disposition of Fixed Assets	3,560	(98,667)
Total Nonoperating Revenues (Expense)	<u>\$ (191,220)</u>	<u>\$ (245,963)</u>
Income (Loss) Before Contributions	\$ 62,445	\$ (77,316)
Capital Contributions	308,387	97,825
Change in Net Position	<u>\$ 370,832</u>	<u>\$ 20,509</u>
Net Position - (As Previously Stated)	\$ 11,037,897	\$ 11,288,076
Restatement - (GASB Statement 75)	<u>-</u>	<u>(270,688)</u>
Net Position - As Restated	<u>\$ 11,037,897</u>	<u>\$ 11,017,388</u>
Net Position	<u><u>\$ 11,408,729</u></u>	<u><u>\$ 11,037,897</u></u>

**NORTH SHELBY WATER COMPANY**  
**STATEMENT OF CASH FLOWS**  
For the Years Ended December 31, 2018 and 2017

	<b>2018</b>	<b>2017</b>
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Receipts from Customers	\$ 3,242,338	\$ 3,060,439
Payments to Suppliers	(1,836,015)	(1,742,596)
Payments to Employees	(439,018)	(434,724)
Other Receipts (Payments)	(2,752)	(1,230)
Net Cash Provided (Used) by Operating Activities	<u>\$ 964,553</u>	<u>\$ 881,889</u>
<b>CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES</b>		
Capital Contributions	\$ 1,000,825	\$ 97,825
Purchases of Capital Assets	(1,789,538)	(1,964,308)
Proceeds from Rural Development Note	1,588,720	1,381,441
Proceeds Sale of Capital Assets	3,560	14,572
Principal Paid on Capital Debt	(147,476)	(80,543)
Interest Paid on Capital Debt (Including Capitalized Interest)	(216,711)	(189,486)
Net Cash Provided (Used) by Capital and Related Financing Activities	<u>\$ 439,380</u>	<u>\$ (740,499)</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Net Cash Received (Invested) in Certificates of Deposits	\$ (2,657)	\$ (67,301)
Interest Received	6,782	5,286
Net Cash Provided (Used) by Investing Activities	<u>\$ 4,125</u>	<u>\$ (62,015)</u>
Net Increase (Decrease) in Cash and Cash Equivalents	\$ 1,408,058	\$ 79,375
Balances-Beginning of the Year	<u>3,046,031</u>	<u>2,966,656</u>
Balances-End of the Year	<u><u>\$ 4,454,089</u></u>	<u><u>\$ 3,046,031</u></u>

	<b>Balances Per December 31, 2018 Statement of Net Position</b>	<b>Balances Per December 31, 2018 Statement of Cash Flows</b>
Unrestricted Cash	\$ 3,045,139	\$ 3,045,139
Restricted Cash	1,408,950	1,408,950
Restricted Certificates of Deposit	327,084	-
Total Cash and Cash Equivalents, End of Year	<u><u>\$ 4,781,173</u></u>	<u><u>\$ 4,454,089</u></u>

	<b>Balances Per December 31, 2017 Statement of Net Position</b>	<b>Balances Per December 31, 2017 Statement of Cash Flows</b>
Unrestricted Cash	\$ 2,362,486	\$ 2,362,486
Restricted Cash	683,545	683,545
Restricted Certificates of Deposit	324,427	-
Total Cash and Cash Equivalents, End of Year	<u><u>\$ 3,370,458</u></u>	<u><u>\$ 3,046,031</u></u>

(Continued)

**NORTH SHELBY WATER COMPANY**  
**STATEMENT OF CASH FLOWS**  
For the Years Ended December 31, 2018 and 2017

	<u>2018</u>	<u>Restated 2017</u>
<b>RECONCILIATION OF OPERATING INCOME (LOSS) TO NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES</b>		
Operating Income (Loss)	\$ 253,665	\$ 168,647
<b>Adjustments to Reconcile Operating Income to Net Cash Provided (Used) by Operating Activities:</b>		
<b>Cash Flows Reported in Other Categories:</b>		
Depreciation Expense	602,180	553,270
Pension & OPEB Expense	118,399	172,831
<b>Change in Assets and Liabilities:</b>		
Receivables, Net	4,145	6,585
Other Receivables	(34,213)	(21,692)
Inventories	(20,404)	(14,668)
Prepaid Expenses	(11,586)	279
Accounts Payable	37,949	5,914
Accrued Expenses	5,620	799
Customer Meter Deposits Payable	8,798	9,924
Net Cash Provided by Operating Activities	<u>\$ 964,553</u>	<u>\$ 881,889</u>

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

North Shelby Water Company had \$352,029 and \$0 outstanding construction accounts payable and retainage payable related to capital projects in process at December 31, 2018 and 2017, respectively.



**NORTH SHELBY WATER COMPANY**  
**NOTES TO BASIC FINANCIAL STATEMENTS**  
**December 31, 2018 and 2017**

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

The North Shelby Water Company is a rural water company serving customers in Franklin, Henry, Oldham and Shelby Counties, Kentucky, and is regulated by the Public Service Commission of the Commonwealth of Kentucky. The Water Company was formed as a 501(c)12 nonprofit organization in August 1972. Eight directors are elected from the members to manage the affairs of the corporation.

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

A summary of the Water Company's significant accounting policies follows:

**Basis of presentation and accounting:** As stated in Kentucky Revised Statutes (KRS) 278.012, "any water association formed for the purpose of furnishing water services to the general public pursuant to KRS Chapter 273 is deemed to be and shall be a public utility and shall be subject to the jurisdiction of the Public Service Commission." In KRS 278.220, it is outlined that the Public Service Commission may establish a system of accounts to be kept by the utilities subject to its jurisdiction, and may prescribe the manner in which such accounts shall be kept. The financial statements of the Water Company are prepared in accordance with generally accepted accounting principles (GAAP). The Water Company applies all relevant Governmental Accounting Standards Board (GASB) pronouncements.

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

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

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

**Revenues and expenses:** Operating revenues and expenses consist of those revenues and expenses that result from the ongoing principal operations of the Water Company. Operating revenues consist primarily of charges for services. Non-operating revenues and expenses consist of those revenues and expenses that are related to financing and investing types of activities and result from nonexchange transactions or ancillary activities. The Water Company adheres to the use restrictions established by note agreements when expenses are incurred for which both restricted and unrestricted net position is available. The Water Company has no policy defining which resources (restricted or unrestricted) to use first.

**NORTH SHELBY WATER COMPANY**  
**NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)**  
**December 31, 2018 and 2017**

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

**Property and equipment:** Property and equipment purchased or constructed is stated at cost. Interest related to costs, and major improvements, renewals and replacements is capitalized as a cost of the project. Costs associated with hook-up fees are capitalized as meters, installations, and services. Depreciation is computed on the straight-line basis over the estimated useful lives of the related assets. The range of estimated useful lives by type of asset is as follows:

- Buildings & Improvements	10-30 years
- Distribution System	5-50 years
- Machinery & Equipment	3-30 years

**Inventory:** Inventories are stated at cost based on first in – first out.

**Compensated Absences:** See Note 15 for the Water Company's policy on vacation and sick pay.

**Pension:** For purposes of measuring the net pension liability, deferred outflows of resources and deferred inflows of resources related to pensions, and pension expense, information about the fiduciary net position of the Commonwealth of Kentucky's County Employees' Retirement System (CERS), and additions to/deductions from CERS's fiduciary net position have been determined on the same basis as they are reported by CERS.

**Post Employment Benefits Other Than Pensions:** For purposes of measuring the net liability, deferred outflows of resources and deferred inflows of resources related to OPEB and OPEB expense, information about the fiduciary net position of the Commonwealth of Kentucky's County Employees' Retirement System (CERS), and additions to/deductions from CERS's fiduciary net position have been determined on the same basis as they are reported by CERS.

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

**Income Taxes:** The corporation is a nonprofit organization and is exempt from income taxes under Section 501(c)12 of the Internal Revenue Code.

**Contributed Capital:** Under the Governmental Accounting Standards Board's (GASB) Statement No. 33, *Accounting and Financial Reporting for Nonexchange Transactions*, the Water Company recognizes capital contributions as revenues in the statement of revenues, expenses and changes in fund net position. Tap-on fees of \$75,825 and \$97,825 were received by the Water Company for the years ended December 31, 2018 and 2017. Customer contributions of \$232,562 and \$0 were received by the Water Company for the years ended December 31, 2018 and 2017, respectively, for hydrants and line extensions.

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

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

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

**NORTH SHELBY WATER COMPANY**  
**NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)**  
**December 31, 2018 and 2017**

**NOTE 2 – DEBT RESTRICTIONS AND COVENANTS**

The Debt Service Account was established with the original RECD note payable, and is to be continued to be maintained as long as any of the notes are outstanding. Under the loan agreement which established this account, it was provided that a minimum balance be maintained in this account as security to the creditor. In order to attain the minimum balance, a monthly transfer must be made in the sum equal to at least 1/12 of the annual installment next becoming due.

Transfers sufficient to meet the total obligation outstanding on all notes were made timely during the year ended December 31, 2018. Sufficient transfers were not made during the year ended December 31, 2017, however the balance in the account was sufficient to make debt service payments.

Under the loan agreements of the original 1971 (2 notes) and 1972 (1 note) notes, a Depreciation Account was to be established to provide funds for extraordinary repairs and extensions to the system, and to make up any deficiency in the Debt Service Account. The monthly transfer required to be made to the Depreciation Account would be a minimum of \$741 each month until a balance of \$88,920 is accumulated. The 1979 note required an additional \$113 each month until a balance of \$13,560 is accumulated. The 1993 note required an additional \$185 each month until a balance of \$22,200 is accumulated. The 1998 note required an additional \$135 each month until a balance of \$16,200 is accumulated. The 2000 note required an additional \$260 each month until a balance of \$31,200 is accumulated. The 2012 note required an additional \$515 each month until a balance of \$61,800 is accumulated. The 2013 note required an additional \$840 each month until a balance of \$100,800 is accumulated. The 2014 note required an additional \$1,345 each month until the account reaches \$161,000. The 2015 note required an additional \$875 each month until the account reaches \$105,000. The monthly deposits are to commence with the first month of the first full year after the facility becomes operational. The Depreciation Account is to be maintained as long as any of the above notes are outstanding. Sufficient funds were maintained in the depreciation accounts for the years ended December 31, 2018 and 2017.

A funded short lived asset account is required under the letter of conditions establishing funding for the 2012, 2013, 2014, and 2015 Rural Development notes. A short lived asset account must be funded at the beginning of the next calendar year following the completion and operational startup of the asset. Under the 2012 Note agreement, the Company must deposit \$1,667 monthly into the account. Under the 2013 Note agreement, the Company must deposit \$3,335 monthly into the account. Under the 2014 note agreement, the Company must deposit \$3,333 monthly into the account. Under the 2015 note agreement the Company must deposit \$4,153 monthly into the account once the project is operational. This account may be used as needed to replace and add short lived assets in the Company's water system. A short lived asset account had not been created as of December 31, 2018.

**NOTE 3 – CASH AND INVESTMENTS**

North Shelby Water Company invests in obligations of the United States and its agencies and instrumentalities through sources including national and state banks chartered in Kentucky, obligations and contracts for future delivery backed by the full faith of the United States or its Agency, certificates of deposit and interest bearing accounts in institutions insured by the Federal Depository Insurance Corporation and other investments described therein.

Custodial credit risk for deposits is the risk that in the event of a bank failure, the Company's deposits may not be returned to it. As of December 31, 2018, and 2017, \$758,994 and \$757,803, respectively, of the Company's deposits were covered by federal depository insurance and \$4,028,961 and \$2,616,766 were collateralized by securities held by the pledging financial institution's agent or trust department in the Company's name. As of December 31, 2018 and 2017, all of the Company's deposits were collateralized by securities and therefore not exposed to custodial risk.

At December 31, 2018 and 2017, the Water Company's deposits were as follows:

**December 31, 2018**

<u>Type of Deposits</u>	<u>Total Bank Balance</u>	<u>Total Carrying Value</u>
Demand Deposits	\$ 4,093,819	\$ 4,086,537
Time and Savings	694,136	694,136
Total Deposits	<u>\$ 4,787,955</u>	<u>\$ 4,780,673</u>

**NORTH SHELBY WATER COMPANY**  
**NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)**  
**December 31, 2018 and 2017**

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

**December 31, 2017**

<u>Type of Deposits</u>	<u>Total Bank Balance</u>	<u>Total Carrying Value</u>
Demand Deposits	\$ 2,495,929	\$ 2,491,318
Time and Savings	878,640	878,640
Total Deposits	<u>\$ 3,374,569</u>	<u>\$ 3,369,958</u>

Reconciliation to Statement of Net Position:

	<u>December 31, 2018</u>	<u>December 31, 2017</u>
Unrestricted Cash,	\$ 3,045,139	\$ 2,362,486
Restricted Cash, Including Time Deposits	1,736,034	1,007,972
Less Cash on Hand	(500)	(500)
	<u>\$ 4,780,673</u>	<u>\$ 3,369,958</u>

**NOTE 4 – RESTRICTED ASSETS**

Restricted cash and time deposits consist of the following:

	<u>December 31, 2018</u>	<u>December 31, 2017</u>
Debt Service Accounts	\$ 215,836	\$ 429,437
Depreciation Accounts	478,299	449,203
Construction Accounts	<u>1,041,899</u>	<u>129,332</u>
Total	<u>\$ 1,736,034</u>	<u>\$ 1,007,972</u>

**NOTE 5 – CUSTOMER ACCOUNTS RECEIVABLE**

Customer Accounts Receivable has been netted with an Allowance for Bad Debts of \$22,277 and \$21,592 at December 31, 2018 and 2017, respectively. The amount provided for bad debts represents the portion of the total amounts for which collection is unlikely, based on historical collection data.

Estimated unbilled water service revenue of \$184,534 and \$196,980 is included in accounts receivable at December 31, 2018 and 2017, respectively.

**NOTE 6 – OTHER RECEIVABLES**

Other receivables at December 31, 2018 and 2017, respectively, included \$59,218 and \$25,005 receivable for the joint operations contract between North Shelby Water Company and U.S. 60 Water Company of Shelby and Franklin Counties, respectively. See Note 17 for details.

**NORTH SHELBY WATER COMPANY**  
**NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)**  
**December 31, 2018 and 2017**

**NOTE 7 – CAPITAL ASSETS**

Capital asset activity for the years ended December 31, 2018 and 2017, was as follows:

	<u>Balance at January 1, 2018</u>	<u>Additions</u>	<u>Disposals</u>	<u>Balance at December 31, 2018</u>
Land & Land Rights	\$ 142,226	\$ -	\$ -	\$ 142,226
Structures & Improvements	735,149	-	-	735,149
Distribution System	19,932,483	117,078	(13,292)	20,036,269
Machinery & Equipment	3,046,630	71,306	(16,679)	3,101,257
Construction in Process	8,195	1,974,937	-	1,983,132
Totals at Historical Cost	<u>\$ 23,864,683</u>	<u>\$ 2,163,321</u>	<u>\$ (29,971)</u>	<u>\$ 25,998,033</u>
Less: Accumulated Depreciation				
Structures & Improvements	\$ (137,259)	\$ (13,355)	\$ -	\$ (150,614)
Distribution System	(6,821,270)	(398,339)	13,292	(7,206,317)
Machinery & Equipment	(1,464,604)	(190,486)	16,679	(1,638,411)
Total Accumulated Depreciation	<u>\$ (8,423,133)</u>	<u>\$ (602,180)</u>	<u>\$ 29,971</u>	<u>\$ (8,995,342)</u>
Capital Assets, Net	<u>\$ 15,441,550</u>	<u>\$ 1,561,141</u>	<u>\$ -</u>	<u>\$ 17,002,691</u>
	<u>Balance at January 1, 2017</u>	<u>Additions</u>	<u>Disposals</u>	<u>Balance at December 31, 2017</u>
Land & Land Rights	\$ 89,526	\$ 52,700	\$ -	\$ 142,226
Structures & Improvements	385,725	349,424	-	735,149
Distribution System	17,809,682	2,328,531	(205,730)	19,932,483
Machinery & Equipment	2,952,064	190,329	(95,763)	3,046,630
Construction in Process	1,485,742	1,119,846	(2,597,393)	8,195
Totals at Historical Cost	<u>\$ 22,722,739</u>	<u>\$ 4,040,830</u>	<u>\$ (2,898,886)</u>	<u>\$ 23,864,683</u>
Less: Accumulated Depreciation				
Structures & Improvements	\$ (124,065)	\$ (13,194)	\$ -	\$ (137,259)
Distribution System	(6,571,367)	(375,242)	125,339	(6,821,270)
Machinery & Equipment	(1,385,685)	(164,834)	85,915	(1,464,604)
Total Accumulated Depreciation	<u>\$ (8,081,117)</u>	<u>\$ (553,270)</u>	<u>\$ 211,254</u>	<u>\$ (8,423,133)</u>
Capital Assets, Net	<u>\$ 14,641,622</u>	<u>\$ 3,487,560</u>	<u>\$ (2,687,632)</u>	<u>\$ 15,441,550</u>

Included under the Water Company's capital assets at December 31, 2018 and 2017, were \$1,422,669 and \$1,339,090 of fully depreciated assets, respectively. Land and land rights, and construction in process are capital assets not being depreciated.

Depreciation expense aggregated \$602,180 and \$553,270 in 2018 and 2017, respectively.

**NOTE 8 – CUSTOMER DEPOSITS**

Customer deposits are collected upon installation of water service. This amount is to be refunded to the customer upon discontinuation of service (after the customer's bill has been paid in full). Records are maintained which detail the accrued interest on each customer's deposit based on the current annual rate. Interest accrued is refunded to the customer or credited to the customer's bill on an annual basis. At December 31, 2018 and 2017, accrued interest on customer deposits was \$5,251 and \$2,671, respectively.

North Shelby Water Company has not maintained a separate bank account specifically for cash collected and disbursed relating to customer deposits.

**NORTH SHELBY WATER COMPANY**  
**NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)**  
**December 31, 2018 and 2017**

**NOTE 9 – LONG TERM DEBT**

As of December 31, 2018 and 2017, the long-term debt payable consisted of the following:

**Notes Payable:**

	<u>December 31, 2018</u>	<u>December 31, 2017</u>
1979 RECD note, original loan amount of \$230,000, secured by water revenues. Interest is charged 5.00% per annum. Final maturity is July, 2019.	\$ 19,750	\$ 31,725
1993 RECD note, original loan amount of \$300,600, secured by water revenues. Interest is charged 5.625% per annum. Final maturity is April, 2033.	188,755	196,733
1998 RECD note, original loan amount of \$288,500, secured by water revenues. Interest is charged 4.5% per annum. Final maturity is October, 2038.	207,181	213,557
2000 RECD note, original loan amount of \$568,000, secured by water revenues. Interest is charged 4.375% per annum. Final maturity is May, 2040.	431,061	442,623
2012 RECD note, original loan amount of \$1,069,758, secured by water revenues. Interest is charged at 3.5% per annum. Final maturity is November, 2052.	1,013,002	1,028,359
2013 RECD note, original loan amount of \$2,100,000, secured by water revenues. Interest is charged at 3.125% per annum. Final maturity is September, 2054.	2,039,940	2,070,432
2014 RECD note, approved for \$2,755,000, secured by water revenues. Interest is charged at 2.375% per annum. Final maturity is October, 2056. Total draws through December 31, 2018 are \$2,550,477.	2,550,477	2,550,477
2015 RECD note, approved for \$1,988,000, secured by water revenues. Interest is charged at 2.375% per annum. Final maturity is October, 2057. Total draws through December 31, 2018 are \$1,524,984.	1,524,984	-
Total Notes Payable	<u>\$ 7,975,150</u>	<u>\$ 6,533,906</u>
Current Portion	\$ 168,609	\$ 83,741
Noncurrent Portion	7,806,541	6,450,165
Total Notes Payable	<u>\$ 7,975,150</u>	<u>\$ 6,533,906</u>

**Accrued Compensated Absences:**

All Classified as Current	<u>\$ 9,962</u>	<u>\$ 9,435</u>
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**NORTH SHELBY WATER COMPANY**  
**NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)**  
December 31, 2018 and 2017

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

**Changes in Long-term Debt**

The following is a summary of changes in long-term debt for the years ended December 31, 2018 and 2017.

**December 31, 2018**

	Balance at January 1, 2018	Additions	Repayments	Balance at December 31, 2018	Current Portion
Notes Payable	\$ 6,533,906	\$ 1,588,720	\$ (147,476)	\$ 7,975,150	\$ 168,609
Accrued Compensated Absences	9,435	527	-	9,962	9,962
Total Long-Term Debt	<u>\$ 6,543,341</u>	<u>\$ 1,589,247</u>	<u>\$ (147,476)</u>	<u>\$ 7,985,112</u>	<u>\$ 178,571</u>

**December 31, 2017**

	Balance at January 1, 2017	Additions	Repayments	Balance at December 31, 2017	Current Portion
Notes Payable	\$ 5,233,008	\$ 1,381,440	\$ 80,542	\$ 6,533,906	\$ 83,741
Accrued Compensated Absences	9,383	52	-	9,435	9,435
Total Long-Term Debt	<u>\$ 5,242,391</u>	<u>\$ 1,381,492</u>	<u>\$ 80,542</u>	<u>\$ 6,543,341</u>	<u>\$ 93,176</u>

The annual requirements for all notes payable outstanding at December 31, 2018 are as follows:

<u>Due</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2019	\$ 168,609	\$ 236,227	\$ 404,836
2020	153,372	230,723	384,095
2021	158,238	225,857	384,095
2022	163,169	220,927	384,096
2023	168,269	215,826	384,095
2024-2028	923,935	996,540	1,920,475
2029-2033	1,077,639	839,967	1,917,606
2034-2038	1,157,376	666,038	1,823,414
2039-2043	1,161,220	490,595	1,651,815
2044-2048	1,265,273	325,412	1,590,685
2049-2053	1,257,246	140,308	1,397,554
2054-2057	320,804	16,799	337,603
	<u>\$ 7,975,150</u>	<u>\$ 4,605,219</u>	<u>\$ 12,580,369</u>

The annual requirements for all notes payable outstanding at December 31, 2017 are as follows:

<u>Due</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2018	\$ 83,741	\$ 202,894	\$ 286,635
2019	144,556	199,574	344,130
2020	128,841	194,549	323,390
2021	133,018	190,372	323,390
2022	137,343	186,048	323,391
2023-2027	757,149	859,801	1,616,950
2028-2032	890,899	726,051	1,616,950
2033-2037	964,557	573,348	1,537,905
2038-2042	974,306	419,054	1,393,360
2043-2047	1,008,200	278,960	1,287,160
2048-2052	1,129,792	126,476	1,256,268
2053-2057	181,504	8,547	190,051
	<u>\$ 6,533,906</u>	<u>\$ 3,965,674</u>	<u>\$ 10,499,580</u>

**NORTH SHELBY WATER COMPANY**  
**NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)**  
**December 31, 2018 and 2017**

**NOTE 10 – INTEREST EXPENSE**

Interest expense incurred for the years ended December 31, 2018 and 2017 was \$229,138 and \$200,496, respectively. \$21,754 and \$43,968 of construction related interest expense was capitalized in 2018 and 2017, respectively.

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

	<u>December 31, 2018</u>	<u>December 31, 2017</u>
<b>Restricted for Capital Projects:</b>		
Monies Restricted for Construction	\$ 1,041,898	\$ 129,332
Total Restricted for Capital Projects	<u>\$ 1,041,898</u>	<u>\$ 129,332</u>
<b>Restricted for Debt Service:</b>		
RECD Notes Payable		
Cash	\$ 694,136	\$ 878,640
Less: Accrued Interest Payable	(66,054)	(59,449)
Total Restricted for Debt Service	<u>\$ 628,082</u>	<u>\$ 819,191</u>

**NOTE 12 – BAD DEBT EXPENSE**

Water revenue charges have been netted with an estimated bad debt expense of \$6,843 and \$10,105 at December 31, 2018 and 2017, respectively.

**NOTE 13 – INSURANCE AND RELATED ACTIVITIES**

The Water Company is exposed to various forms of loss of assets associated with the risks of fire, personal liability, theft, vehicular accidents, errors and omissions, fiduciary responsibility, etc. and is also subject to the risks associated with employee injury. Each of these risks is covered through the purchase of commercial insurance.

**NOTE 14 – COUNTY EMPLOYEES' RETIREMENT SYSTEM – NON-HAZARDOUS EMPLOYEES PENSION PLAN AND POST-EMPLOYMENT HEALTHCARE BENEFIT (INSURANCE PLAN)**

The North Shelby Water Company participates in the Commonwealth of Kentucky's County Employees' Retirement System (CERS) for non-hazardous employees.

Under the provision of Kentucky Revised Statute ("KRS") Section 61.645, the Board of Trustees of the Kentucky Retirement System administers CERS and has the authority to establish and amend benefit provisions. Under the provisions of Kentucky Revised Statute ("KRS") Section 61.701, the KRS Board administers the Kentucky Retirement Systems Insurance Fund. The statutes provide for an insurance fund to provide group hospital and medical benefits to retirees drawing a benefit from the pension funds administered by KRS, which includes CERS.

The Kentucky Retirement System issues a publicly available financial report that includes financial statements and required supplementary information for CERS's pension and insurance funds. Additionally, the Kentucky Retirement System issues publicly available financial reports that include the Schedules of Employer Allocations and Pension amounts, and the Schedules of Employer Allocations of Post Employment Benefits Other Than Pension amounts, by employer. The most recent financial reports, dated June 30, 2018, may be obtained on-line as follows:

- Kentucky Retirement Systems Audit Report – 2018  
[https://apps.auditor.ky.gov/Public/Audit\\_Reports/Archive/2018KRSfinancialaudit.pdf](https://apps.auditor.ky.gov/Public/Audit_Reports/Archive/2018KRSfinancialaudit.pdf)
- Kentucky Retirement Systems Schedule of Employer Allocations and Pension Amounts – Audit Report 2018 – GASB 68  
<https://kyret.ky.gov/Employers/GASB/2018%20Audited%20Reports/2018KRSEmployerAllocationPensionAudit.pdf>
- Kentucky CERS GASB 68 Actuarial Report  
[https://kyret.ky.gov/Employers/GASB/2018%20GASB%2068%20and%2075%20Actuary%20Reports/GASB68\\_Actuarial\\_Information\\_CERS\\_FY2018.pdf](https://kyret.ky.gov/Employers/GASB/2018%20GASB%2068%20and%2075%20Actuary%20Reports/GASB68_Actuarial_Information_CERS_FY2018.pdf)



**NORTH SHELBY WATER COMPANY**  
**NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)**  
**December 31, 2018 and 2017**

**NOTE 14 – COUNTY EMPLOYEES' RETIREMENT SYSTEM – NON-HAZARDOUS EMPLOYEES PENSION PLAN AND POST-EMPLOYMENT HEALTHCARE BENEFIT (INSURANCE PLAN) (Continued)**

- Kentucky Retirement Systems Schedules of Employer Allocations and OPEB Amounts by Employer – Audit Report 2018 – GASB 75  
<https://kyret.ky.gov/Employers/GASB/2018%20Audited%20Reports/2018KRS-OPEBAudit.pdf>
- Kentucky CERS GASB 75 Actuarial Report  
[https://kyret.ky.gov/Employers/GASB/2018%20GASB%2068%20and%2075%20Actuary%20Reports/GASB75\\_Actuarial\\_Information\\_CERS\\_FY2018.pdf](https://kyret.ky.gov/Employers/GASB/2018%20GASB%2068%20and%2075%20Actuary%20Reports/GASB75_Actuarial_Information_CERS_FY2018.pdf)

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

**Method Used to Value Investments/Investment Objectives** – Investments of the plan are reported at fair value. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Short-term investments are reported at cost, which approximates fair value. Purchases and sales of securities are recorded on a trade-date basis. Interest income is recorded on the accrual basis. Dividends are recorded on the dividend date. Gain (loss) on investments includes KRS' gains and losses on investments bought and sold as well as held during the fiscal year. Investment returns are recorded net of investment fees.

The investment objectives of the portfolios are to produce results that exceed the stated goals over both short-term and long-term periods.

- **Shorter-Term (5 years and less):** The returns of the particular asset classes of the managed funds of the Systems, measured on an annual basis, should exceed the return achieved by a policy benchmark portfolio composed of comparable unmanaged market indices.
- **Medium-Term (5 to 30 years):** The returns of the particular asset classes of the managed funds of the Systems, measured on a rolling year basis should exceed the returns achieved by a policy benchmark portfolio composed of comparable unmanaged market indices and perform above the median of an appropriate peer universe, if there is one.
- **Longer-Term:** The total assets of the Systems should achieve a return of 6.25% for CERS pension and insurance plans. This is measured over 30 to 40 years which exceeds the actuarially required rate of return while also exceeding the return achieved by its total fund benchmark.

Target Asset Allocation Board Policy as of June 30, 2018 and 2017 was as follows:

	2018	2017
Combined Equity	35.00%	50.80%
Combined Fixed Income	24.00%	14.00%
Private Equity	10.00%	10.00%
Absolute Return	10.00%	10.00%
Real Return	10.00%	8.00%
Real Estate	5.00%	5.00%
Global Bonds	4.00%	0.00%
Cash	2.00%	2.20%
	<u>100.00%</u>	<u>100.00%</u>

Total fund return for the years ended June 30, 2018 and 2017 was 8.57% and 13.47% respectively.

**NORTH SHELBY WATER COMPANY**  
**NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)**  
**December 31, 2018 and 2017**

**NOTE 14 – COUNTY EMPLOYEES' RETIREMENT SYSTEM – NON-HAZARDOUS EMPLOYEES PENSION PLAN AND POST-EMPLOYMENT HEALTHCARE BENEFIT (INSURANCE PLAN) (Continued)**

**Pension Plan Description** – CERS is a cost-sharing multiple-employer defined benefit pension plan that covers all regular full-time members employed in non-hazardous and hazardous positions of each participating county, city, and school board, and any additional eligible local agencies electing to participate in CERS along with hazardous duty position of each participating county, city, or school board, any additional eligible local agencies electing to participate in CERS. The plan provides for retirement, disability, and death benefits to plan members. Retirement benefits may be extended to beneficiaries of plan members under certain circumstances. Prior to July 1, 2009, COLAs were provided annually equal to the percentage increase in the annual average of the consumer price index for all urban consumers for the most recent calendar year, not to exceed 5% in any plan year. After July 1, 2009, the COLAs were limited to 1.5%. No COLA has been granted since July 1, 2011. The North Shelby Water Company participates in the non-hazardous plan.

**Benefits provided** – CERS provides retirement, health insurance, death and disability benefits to Plan employees and beneficiaries. Employees are vested in the plan after five years' service. For retirement purposes, employees are grouped into three tiers, based on hire date:

Tier 1	Participation date	Before September 1, 2008
	Unreduced retirement	27 years service or 65 years old
	Reduced retirement	At least 5 years service and 55 years old
Tier 2	Participation date	September 1, 2008 – December 31, 2013
	Unreduced retirement	At least 5 years service and 65 years old or age 57+ and sum of service years plus age equal 87
	Reduced retirement	At least 10 years service and 60 years old
Tier 3	Participation date	After December 31, 2013
	Unreduced retirement	At least 5 years service and 65 years old or age 57+ and sum of service years plus age equal 87
	Reduced retirement	Not available

Retirement is based on a factor of the number of years' service and hire date multiplied by the average of the highest five years' earnings. Reduced benefits are based on factors of both of these components. Participating employees become eligible to receive the health insurance benefit after at least 180 months of service. Death benefits are provided for both death after retirement and death prior to retirement. Death benefits after retirement are \$5,000 in lump sum. Five years' service is required for death benefits prior to retirement and the employee must have suffered a duty-related death. The decedent's beneficiary will receive the higher of the normal death benefit and \$10,000 plus 25% of the decedent's monthly final rate of pay and any dependent child will receive 10% of the decedent's monthly final rate of pay up to 40% for all dependent children. Five years' service is required for nonservice-related disability benefits.

During the 2018 legislative session, House Bill 185 was enacted, which updated the benefit provisions for active members who die in the line of duty. Benefits paid to the spouses of deceased members have been increased from 25% of the member's final rate of pay to 75% of the member's average pay. If the member does not have a surviving spouse, benefits paid to surviving dependent children have been increased from 10% of the member's final pay rate to 50% of average pay for one child, 65% of average pay for two children, or 75% of average pay for three children.

There were no changes in benefit terms during the year ended June 30, 2017.

**Contributions** - Participating employers are required to contribute at an actuarially determined rate. Per Kentucky Revised Statute Section 78.545(33), normal contribution and past service contribution rates shall be determined by the Board on the basis of an annual valuation last preceding the July 1 of a new biennium. The Board may amend contribution rates as of the first day of July of the second year of a biennium, if it is determined on the basis of a subsequent actuarial valuation that amended contribution rates are necessary to satisfy requirements determined in accordance with actuarial bases adopted by the Board. For the fiscal years ended June 30, 2018 and 2017 participating non-hazardous employers contributed 19.18% and 18.68%, respectively, of each employee's creditable compensation. The actuarially determined rates set by the Board for the fiscal years ended June 30, 2018 and 2017 were 19.18% and 18.88%, respectively. Administrative costs of KRS are financed through employer contributions and investment earnings.

**NORTH SHELBY WATER COMPANY**  
**NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)**  
**December 31, 2018 and 2017**

**NOTE 14 – COUNTY EMPLOYEES' RETIREMENT SYSTEM – NON-HAZARDOUS EMPLOYEES PENSION PLAN AND POST-EMPLOYMENT HEALTHCARE BENEFIT (INSURANCE PLAN) (Continued)**

Non-hazardous employer contributions for the year ended June 30, 2018, of \$19.18% were allocated 14.48% to CERS's pension fund and 4.70% to CERS's (health insurance). Non-hazardous employer contributions for the year ended June 30, 2017, of 18.68% were allocated 13.95% to CERS's pension fund and 4.73% to CERS' OPEB (health insurance) fund, respectively.

For the fiscal year ended June 30, 2018 and 2017, plan members who began participating prior to September 1, 2008, were required to contribute 5% non-hazardous, of their annual creditable compensation. These members were classified in the Tier 1 structure of benefits. Plan members who began participating on, or after, September 1, 2008 and before January 1, 2014, were required to contribute a total of 6% non-hazardous, of their annual creditable compensation. These members were classified in the Tier 2 structure of benefits. Five percent of the contribution was deposited to the member's account while the 1% was deposited to an account created for the payment of health insurance benefits under 26 USC Section 401(h) in the Pension Fund (see Kentucky Administrative Regulation 105 KAR 1:420E). Interest is paid each June 30 on members' accounts at a rate of 2.5%.

If a member terminates employment and applies to take a refund, the member is entitled to a full refund of contributions and interest; however, for plan members who began participating on, or after, September 1, 2008, the 1% contribution to the 401(h) account is non-refundable and is forfeited.

Plan members who began participating on, or after, January 1, 2014, were required to contribute to the Cash Balance Plan. These members were classified in the Tier 3 structure of benefits. The Cash Balance Plan is known as a hybrid plan because it has characteristics of both a defined benefit plan and a defined contribution plan. Members in the plan contribute a set percentage of their salary each month to their own account. Non-hazardous members contribute 5%, of their annual creditable compensation and an additional 1% to the health insurance fund which is not credited to the member's account and is not refundable. The employer contribution rate is set annually by the Board based on an actuarial valuation. The employer contributes a set percentage of the member's salary. Each month, when employer contributions are received, an employer pay credit is deposited to the member's account. A member's account is credited with a 4% (non-hazardous) and employer pay credit. The employer pay credit represents a portion of the employer contribution.

Interest is paid into the Tier 3 member's account. The account currently earns 4% interest credit on the member's account balance as of June 30<sup>th</sup> of the previous year. The member's account may be credited with additional interest if the system's five-year Geometric Average Net Investment Return (GANIR) exceeded 4%. If the member was actively employed and participating in the fiscal year, and if the systems' GANIR for the previous five years exceeds 4%, then the member's account will be credited with 75% of the amount of the returns over 4% on the account balance as of June 30<sup>th</sup> of the previous year (Upside Sharing Interest). It is possible that one system in KRS may get an Upside Sharing Interest, while one may not.

***Methods and Assumptions Used in Calculation of Actuarially Determined Contributions (Pension Plan)***

Per the Kentucky Retirement System's 2018 Comprehensive Annual Financial Report, the actuarially determined contribution rates effective for fiscal year ending 2018 are calculated as of June 30, 2017. Based on the June 30, 2017 actuarial valuation report, the actuarial methods and assumptions used to calculate these contribution rates are as follows:

**NORTH SHELBY WATER COMPANY**  
**NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)**  
**December 31, 2018 and 2017**

**NOTE 14 – COUNTY EMPLOYEES’ RETIREMENT SYSTEM – NON-HAZARDOUS EMPLOYEES PENSION PLAN AND POST-EMPLOYMENT HEALTHCARE BENEFIT (INSURANCE PLAN) (Continued)**

Item	CERS June 30, 2018 Non-Hazardous/Hazardous	CERS June 30, 2017 Non-Hazardous/Hazardous
Determined by the Actuarial Valuation as of:	June 30, 2016	June 30, 2016
Actuarial Cost Method:	Entry Age Normal	Entry Age Normal
Asset Valuation Method:	20% of the difference between the market value of assets and the expected actuarial value of assets is recognized.	20% of the difference between the market value of assets and the expected actuarial value of assets is recognized.
Amortization Method:	Level Percent of Pay	Level Percent of Pay
Amortization Period:	27 Years, Closed	28 Years, Closed
Investment Return:	7.50%	7.50%
Inflation:	3.25%	3.25%
Payroll Growth:	4.00%, average	4.00%, average
Mortality:	RP-2000 Combined Mortality Table, projected to 2013 with Scale BB (set back 1 year for females)	RP-2000 Combined Mortality Table, projected to 2013 with Scale BB (set back 1 year for females)

***Actuarial Methods and Assumptions Used in Calculation of the Actuarially Determined Total Pension Liability and Net Pension Liability***

The total pension liability is based on the actuarial valuation as of June 30, 2018 performed by Gabriel Roeder Smith (GRS). The total pension liability, net pension liability, and sensitivity information as of June 30, 2018 were based on an actuarial valuation date of June 30, 2017. The total pension liability was rolled-forward from the valuation date (June 30, 2017) to the plan’s fiscal year ending June 30, 2018, using generally accepted actuarial principles.

There have been no changes in actuarial assumptions since June 30, 2017. The actuarial assumptions are:

Inflation	2.30%
Salary Increases	3.05%
Investment Rate of Return	6.25%

However, during the 2018 legislative session, House Bill 185 was enacted, which updated the benefit provisions for active members who die in the line of duty. Benefits paid to the spouses of deceased members have been increased from 25% of the member’s final rate of pay to 75% of the member’s average pay. If the member does not have a surviving spouse, benefits paid to surviving dependent children have been increased from 10% of the member’s final pay rate to 50% of average pay for one child, 65% of average pay for two children, or 75% of average pay for three children. The Total Pension Liability as of June 30, 2018 is determined using these updated benefit provisions.

**NORTH SHELBY WATER COMPANY  
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)  
December 31, 2018 and 2017**

**NOTE 14 – COUNTY EMPLOYEES’ RETIREMENT SYSTEM – NON-HAZARDOUS EMPLOYEES PENSION PLAN AND POST-EMPLOYMENT HEALTHCARE BENEFIT (INSURANCE PLAN) (Continued)**

***Actuarial Methods and Assumptions Used in Calculation of the Actuarially Determined Total Pension Liability and Net Pension Liability (Continued)***

The mortality table used for active members is RP-2000 Combined Mortality Table projected with Scale BB to 2013 (multiplied by 50% for males and 30% for females). For healthy retired members and beneficiaries, the mortality table used is the RP-2000 Combined Mortality Table projected with Scale BB to 2013 (set-back for one year for females). For disabled members, the RP-2000 Combined Disabled Mortality Table projected with Scale BB to 2013 (set-back four years for males) is used for the period after disability retirement.

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

At December 31, 2018, and 2017 the Water Company reported a liability of \$1,104,599 and \$1,093,398, respectively for its proportionate share of the net pension liability. The net pension liability for CERS was measured as of June 30, 2018, and 2017 and was based on the actual liability of the employees and former employees relative to the total liability of the system as determined by an actuarial valuation as of those dates. The Water Company's proportion of the net pension liability was based on a projection of the Water Company's long-term share of contributions to the pension plan relative to the projected contributions of all participating employers, actuarially determined. At June 30, 2018, and 2017 the Water Company's proportion was 0.018137 and 0.018680 percent, respectively, which is a decrease of 0.000543% and 0.000154% for the years ended June 30, 2018 and June 30, 2017, respectively.

The Water Company's total payroll for the calendar year ended December 31, 2018 was \$478,435. Contributions to the CERS were based on \$457,698 (eligible gross wages). The total employer pension contributions for the calendar year ended December 31, 2018 were \$70,327.

The Water Company's total payroll for the calendar year ended December 31, 2017 was \$467,177. Contributions to the CERS were based on \$458,377 (eligible gross wages). The total employer pension contributions for the calendar year ended December 31, 2017 were \$64,826.

All contributions were made as required.

The Water Company's contribution for the County Employees' Retirement System's year(s) ended December 31, 2018, and 2017 was 0.018137 and 0.018680 percent, respectively, of the System's total contribution requirements for all employers.

For the years ended December 31, 2018, and December 31, 2017, the Water Company recognized pension expense of \$172,959 and \$216,843, respectively. At December 31, 2018 and 2017 the Water Company reported deferred outflows of resources and deferred inflows of resources related to CERS pensions from the following sources:

	<b>December 31, 2018</b>		<b>December 31, 2017</b>	
	<b>Deferred Outflows of Resources</b>	<b>Deferred Inflows of Resources</b>	<b>Deferred Outflows of Resources</b>	<b>Deferred Inflows of Resources</b>
Difference Between Expected and Actual Experience	\$ 36,029	\$ 16,169	\$ 1,356	\$ 27,755
Change in Assumptions	107,951	-	201,762	-
Changes in Proportion and Differences Between Employer Contributions and Proportionate Share of Contributions	2,797	20,844	11,520	3,771
Difference Between Projected and Actual Investment Earnings on Pension Plan Investments	51,365	64,609	86,596	73,072
Water Company Contributions Made Subsequent to the NPL Measurement Date	39,341	-	33,808	-
<b>Total</b>	<b>\$ 237,483</b>	<b>\$ 101,622</b>	<b>\$ 335,042</b>	<b>\$ 104,598</b>

**NORTH SHELBY WATER COMPANY**  
**NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)**  
December 31, 2018 and 2017

**NOTE 14 – COUNTY EMPLOYEES' RETIREMENT SYSTEM – NON-HAZARDOUS EMPLOYEES PENSION PLAN AND POST-EMPLOYMENT HEALTHCARE BENEFIT (INSURANCE PLAN) (Continued)**

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

In the Water Company's 2017 audit report deferred outflows and inflows attributable to the net difference between projected and actual investment earnings on pension plan assets were netted. They are shown at gross above.

\$39,341 and \$33,808 reported as deferred outflows of resources related to pensions arising from Water Company contributions made subsequent to the measurement date will be recognized as a reduction in the net pension liability in the years ended December 31, 2019 and 2018. Amounts reported as deferred inflows and outflows of resources due to the net difference between projected and actual investment earnings on pension plan investments will be netted and amortized over five years and recognized in pension expense. Amounts reported as deferred outflows of resources due to the difference between expected and actual experience, change of assumptions, and changes in proportion and differences between employer contributions and proportionate share of contributions will be amortized and recognized in pension expense over the expected remaining service lives of all employees. Total amortization to be recognized in pension expense is presented below as follows:

		Increase (Decrease) to Pension Expense
<b>Year Ended December 31, 2018:</b>		
	2019	\$ 46,138
	2020	22,450
	2021	(7,425)
	2022	(3,288)
		<u>\$ 57,875</u>
		Increase (Decrease) to Pension Expense
<b>Year Ended December 31, 2017:</b>		
	2018	\$ 44,086
	2019	42,469
	2020	17,621
	2021	(7,578)
		<u>\$ 96,598</u>

***Sensitivity of the Water Company's Proportionate Share of the Net Pension Liability to Changes in the Discount Rate***

The following table presents the net pension liability of CERS [as reported in its publicly available financial statements for the years ended June 30, 2018 and 2017], calculated using the discount rates of 6.25% and 6.25% for the years ended June 30, 2018 and 2017, respectively, as well as what CERS' net pension liability would be if it were calculated using a discount rate that is one percentage point lower or one percentage point higher than the approved rate:

	1% Decrease [5.25%]	Current Discount [6.25%]	1% Increase [7.25%]
<b>As of June 30, 2018</b>			
Net Pension Liability	\$ 7,667,062,949	\$ 6,090,304,793	\$ 4,769,257,576
Water Company's Proportionate Share	1,390,576	1,104,599	865,001
	1% Decrease [5.25%]	Current Discount [6.25%]	1% Increase [7.25%]
<b>As of June 30, 2017</b>			
Net Pension Liability	\$ 7,382,285,860	\$ 5,853,307,449	\$ 4,574,328,530
Water Company's Proportionate Share	1,379,011	1,093,398	854,485

**NORTH SHELBY WATER COMPANY  
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)  
December 31, 2018 and 2017**

**NOTE 14 – COUNTY EMPLOYEES' RETIREMENT SYSTEM – NON-HAZARDOUS EMPLOYEES PENSION PLAN AND POST-EMPLOYMENT HEALTHCARE BENEFIT (INSURANCE PLAN) (Continued)**

***Payable to the Pension Plan***

At December 31, 2018 and 2017, the Water Company reported a payable of \$7,225 and \$5,886 for the outstanding amount of contributions required for the years then ended. The amount represents the employee withholding and employer match for the last month of the years then ended.

**Insurance (OPEB) Plan Description** – The Kentucky Retirement Systems' Insurance Fund (Insurance Fund) was established to provide hospital and medical insurance for eligible members receiving benefits from KERS, CERS, and SPRS. The eligible non-Medicare retirees are covered by the Department of Employee Insurance (DEI) plans. KRS submits the premium payments to DEI. The Board contracts with Humana to provide health care benefits to the eligible Medicare retirees through a Medicare Advantage Plan. The Insurance Fund pays a prescribed contribution for whole or partial payment of required premiums to purchase hospital and medical insurance. A portion of the insurance premiums are withheld from benefit payments for members including those of the CERS Non-Hazardous system.

***Contributions***

As a result of House Bill 290 (2004 Kentucky General Assembly), medical insurance benefits are calculated differently for members who began participating on, or after, July 1, 2003. Once members reach a minimum vesting period of 10 years, non-hazardous employees whose participation began on, or after, July 1, 2003, earn \$10 per month for insurance benefits at retirement for every year of earned service without regard to a maximum dollar amount. This dollar amount is subject to adjustment annually, which is currently 1.5%, based upon Kentucky Revised Statutes. This benefit is not protected under the inviolable contract provisions of Kentucky Revised Statute 78.852. The Kentucky General Assembly reserves the right to suspend or reduce this benefit if, in its judgment, the welfare of the Commonwealth so demands.

The amount of contribution paid by the Insurance Fund is based on years of service. For members participating prior to July 1, 2003, years of service and respective percentages of the maximum contribution are as follows:

Portion Paid by Insurance Fund	
Years of Service	Paid by Insurance Fund (%)
20+ years	100.00%
15-19 years	75.00%
10-14 years	50.00%
4-9 years	25.00%
Less than 4 years	0.00%

For members participating on or after July 1, 2003, for CERS Non-Hazardous members, the dollar contribution for fiscal years 2018 and 2017 was \$13.38 and \$13.18, respectively.

For the fiscal years ended June 30, 2018 and 2017, plan members who began on, or after, September 1, 2008 (classified in the Tier 2 or Tier 3 structure of benefits) were required to contribute 1% of their annual creditable compensation to an account created for the payment of health insurance benefits under 26 USC Section 401(h) in the Pension Fund (see Kentucky Administrative Regulation 105 KAR 1:420E).

If a member terminates employment the 1% contribution to the 401(h) account is non-refundable and is forfeited.

Participating employers are required to contribute at an actuarially determined rate as described previously.

***Methods and Assumptions Used in Calculation of Actuarially Determined Contributions (OPEB)***

Per the GASB Statement No. 75, *Report for Postemployment Benefits Other than Pensions* for the Kentucky County Employees Retirement System prepared as of June 30, 2018 and 2017, the actuarially determined contribution rates effective for fiscal year ending 2018 are calculated as of June 30, 2017. The actuarial methods and assumptions used to calculate the actuarially determined contributions are as follows:

**NORTH SHELBY WATER COMPANY**  
**NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)**  
**December 31, 2018 and 2017**

**NOTE 14 – COUNTY EMPLOYEES’ RETIREMENT SYSTEM – NON-HAZARDOUS EMPLOYEES PENSION PLAN AND POST-EMPLOYMENT HEALTHCARE BENEFIT (INSURANCE PLAN) (Continued)**

***Methods and Assumptions Used in Calculation of Actuarially Determined Contributions (OPEB) (Continued)***

Item	CERS June 30, 2018 Non-Hazardous/Hazardous	CERS June 30, 2017 Non-Hazardous/Hazardous
Determined by the Actuarial Valuation as of:	June 30, 2016	June 30, 2015
Experience Study	July 1, 2008 - June 30, 2013	July 1, 2008 - June 30, 2013
Actuarial Cost Method:	Entry Age Normal	Entry Age Normal
Asset Valuation Method:	20% of the difference between the market value of assets and the expected actuarial value of assets is recognized.	20% of the difference between the market value of assets and the expected actuarial value of assets is recognized.
Amortization Method:	Level Percent of Pay	Level Percent of Pay
Remaining Amortization Period:	27 Years, Closed	28 Years, Closed
Payroll Growth:	4.00%, average	4.00%, average
Investment Return:	7.50%	7.50%
Inflation:	3.25%	3.25%
Salary Increases:	4.00%, average	4.00%, average
Mortality:	The mortality table used for active members is RP-2000 Combined Mortality Table projected with Scale BB to 2013 (multiplied by 50% for males and 30% for females). For healthy retired members and beneficiaries, the mortality table used is the RP-2000 Combined Mortality Table projected with Scale BB to 2013 (set-back for one year for females). For disabled members, the RP-2000 Combined Disabled Mortality Table projected with Scale BB to 2013 (set-back four years for males) is used for the period after disability retirement.	The mortality table used for active members is RP-2000 Combined Mortality Table projected with Scale BB to 2013 (multiplied by 50% for males and 30% for females). For healthy retired members and beneficiaries, the mortality table used is the RP-2000 Combined Mortality Table projected with Scale BB to 2013 (set-back for one year for females). For disabled members, the RP-2000 Combined Disabled Mortality Table projected with Scale BB to 2013 (set-back four years for males) is used for the period after disability retirement.
<i>Healthcare Trend Rates:</i>		
Pre-65	Initial trend starting at 7.50% and gradually decreasing to an ultimate trend rate of 5.00% over a period of 5 years.	Initial trend starting at 7.50% and gradually decreasing to an ultimate trend rate of 5.00% over a period of 5 years.
Post-65	Initial trend starting at 5.50% and gradually decreasing to an ultimate trend rate of 5.0% over a period of 2 years.	Initial trend starting at 5.50% and gradually decreasing to an ultimate trend rate of 5.0% over a period of 2 years.



**NORTH SHELBY WATER COMPANY  
NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)  
December 31, 2018 and 2017**

**NOTE 14 – COUNTY EMPLOYEES' RETIREMENT SYSTEM – NON-HAZARDOUS EMPLOYEES PENSION PLAN AND POST-EMPLOYMENT HEALTHCARE BENEFIT (INSURANCE PLAN) (Continued)**

***Actuarial Methods and Assumptions to Determine the Total OPEB Liability and Net OPEB Liability***

For financial reporting the actuarial valuation as of June 30, 2018, was performed by Gabriel Roeder Smith (GRS). The total OPEB liability, net OPEB liability, and sensitivity information as of June 30, 2018, were based on an actuarial valuation date of June 30, 2017. The total OPEB liability was rolled-forward from the valuation date (June 30, 2017) to the plan's fiscal year ending June 30, 2018, using generally accepted actuarial principles. The total OPEB liability at June 30, 2017 was rolled from the June 30, 2016 valuation date using generally accepted accounting principles. There have been no changes in actuarial assumptions since June 30, 2017 (other than the blended discount rate used to calculate the total OPEB liability). However, during the 2018 legislative session, House Bill 185 was enacted, which updated the benefit provisions for active members who die in the line of duty. The system shall now pay 100% of the insurance premium for spouses and children for all active members who die in the line of duty. The total OPEB liability as of June 30, 2018, is determined using these updated benefit provisions.

The actuarial assumptions are:

Inflation	2.30%
Payroll Growth Rate	2.0% for CERS Non-hazardous and hazardous
Salary Increases	3.05%, average
Investment Rate of Return	6.25%
Healthcare Trend Rates	
Pre – 65	Initial trend starting at 7.00% at January 1, 2020, and gradually decreasing to an ultimate trend rate of 4.05% over a period of 12 years.
Post – 65	Initial trend starting at 5.00% at January 1, 2020, and gradually decreasing to an ultimate trend rate of 4.05% over a period of 10 years.

The mortality table used for active members is RP-2000 Combined Mortality Table projected with Scale BB to 2013 (multiplied by 50% for males and 30% for females). For healthy retired members and beneficiaries, the mortality table used is the RP-2000 Combined Mortality Table projected with Scale BB to 2013 (set-back for one year for females). For disabled members, the RP-2000 Combined Disabled Mortality Table projected with Scale BB to 2013 (set-back four years for males) is used for the period after disability retirement.

***Long-Term Expected Rate of Return***

The long-term expected rate of return was determined by using a building-block method in which best-estimate ranges of expected future real rate of returns are developed for each asset class. The ranges are combined by weighting the expected future real rate of return by the target asset allocation percentage.

The long-term expected real rate of return was 6.09% and 6.25% at June 30, 2018 and 2017.

***Discount Rate***

The projection of cash flows used to determine the June 30, 2018 discount rate of 5.85% for CERS Non-hazardous, assumed that local employers would contribute the actuarially determined contribution rate of projected compensation over the remaining 25 years (closed) amortization period of the unfunded actuarial accrued liability. The discount rate determination used an expected rate of return of 6.25%, and a municipal bond rate of 3.62%, as reported in Fidelity Index's "20-Year Municipal GO AA Index" as of June 30, 2018.

The discount rates used to measure the total OPEB liability as of June 30, 2017 for the CERS Non-Hazardous group were based on the expected rate of return on OPEB plan investments of 6.25% and a municipal bond rate of 3.56%, as reported in Fidelity Index's "20-year Municipal GO AA Index" as of June 30, 2017.

The fully-insured premiums KRS pays for the CERS Plan are blended rates based on the combined experience of active and retired members. Because the average cost of providing health care benefits to retirees under age 65 is higher than

**NORTH SHELBY WATER COMPANY**  
**NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)**  
**December 31, 2018 and 2017**

**NOTE 14 – COUNTY EMPLOYEES' RETIREMENT SYSTEM – NON-HAZARDOUS EMPLOYEES PENSION PLAN AND POST-EMPLOYMENT HEALTHCARE BENEFIT (INSURANCE PLAN) (Continued)**

***Discount Rate (Continued)***

the average cost of providing health care benefits to active employees, there is an implicit employer subsidy for the non-Medicare eligible retirees. The liability associated with this implicit subsidy is included in the calculation of the total OPEB liability.

However, the cost associated with the implicit employer subsidy was not included in the calculation of the System's actuarial determined contributions, and any cost associated with the implicit subsidy will not be paid out of the System's trusts. Therefore, the municipal bond rate was applied to future expected benefit payments associated with the implicit subsidy. The target asset allocation and best estimates of arithmetic nominal rates of return for each major asset class are summarized in the Kentucky Retirement System's CAFR.

***OPEB Liabilities, OPEB Expense, and Deferred Outflows of Resources and Deferred Inflows of Resources related to the County Employee Retirement System Insurance Plan***

At December 31, 2018 and 2017 the Water Company reported a liability of \$322,001 and \$375,532, respectively.

The Water Company's total payroll for the calendar year ended December 31, 2018 was \$478,435. Contributions were based on \$457,698 (eligible gross wages). The total employer contributions to the Health Insurance Fund for the year ended June 30, 2018 were \$22,821.

The Water Company's total payroll for the calendar year ended December 31, 2017 was \$252,449. Contributions were based on \$458,377 (eligible gross wages). The total employer contributions to the Health Insurance Fund for the year ended June 30, 2017 were \$21,979.

All contributions were made as required.

The Water Company's contribution for the County Employee's Retirement System's (Insurance Plan) for the years ended June 30, 2018 and 2017 was 0.018137 percent and 0.018680 percent, respectively, of the System's total contribution requirements for all employers.

The implicit employer subsidy for the non-Medicare eligible retirees for the years ended June 30, 2018 and 2017 was \$3,843 and \$2,356, respectively.

For the years ended December 31, 2018 and 2017, the Water Company recognized OPEB expense of \$38,915 and \$42,793, respectively. At December 31, 2018 and 2017 the Water Company reported deferred outflows of resources and deferred inflows of resources related to CERS OPEB from the following sources:

	<b>December 31, 2018</b>		<b>December 31, 2017</b>	
	<b>Deferred Outflows of Resources</b>	<b>Deferred Inflows of Resources</b>	<b>Deferred Outflows of Resources</b>	<b>Deferred Inflows of Resources</b>
Difference Between Expected and Actual Experience	\$ -	\$ 37,525	\$ -	\$ 1,043
Change in Assumptions	64,308	744	81,713	-
Changes in Proportion and Differences Between Employer Contributions and Proportionate Share of Contributions	-	9,605	-	872
Difference Between Projected and Actual Investment Earnings on Insurance Plan Investments	-	22,180	-	17,747
Water Company Contributions Made Subsequent to the Net OPEB Measurement Date	13,114	-	11,463	-
<b>Total</b>	<b>\$ 77,422</b>	<b>\$ 70,054</b>	<b>\$ 93,176</b>	<b>\$ 19,662</b>

**NORTH SHELBY WATER COMPANY**  
**NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)**  
**December 31, 2018 and 2017**

**NOTE 14 – COUNTY EMPLOYEES' RETIREMENT SYSTEM – NON-HAZARDOUS EMPLOYEES PENSION PLAN AND POST-EMPLOYMENT HEALTHCARE BENEFIT (INSURANCE PLAN) (Continued)**

***OPEB Liabilities, OPEB Expense, and Deferred Outflows of Resources and Deferred Inflows of Resources related to the County Employee Retirement System Insurance Plan (Continued)***

\$13,114 and \$11,463 reported as deferred outflows of resources related to OPEB arising from Water Company contributions made subsequent to the measurement date will be recognized as a reduction in the net OPEB liability in the years ended December 31, 2019 and 2018 respectively. Amounts reported as deferred inflows and outflows of resources due to the net difference between projected and actual investment earnings on OPEB plan investments will be netted and amortized over five years and recognized in OPEB expense. Amounts reported as deferred outflows of resources and deferred inflows of resources due to the difference between expected and actual experience, change of assumptions, and changes in proportion and differences between employer contributions and proportionate share of contributions will be amortized and recognized in OPEB expense over the expected remaining service lives of all employees. Total amortization to be recognized in OPEB expense is presented below as follows:

		Increase (Decrease) to OPEB Expense
<b>Year Ended December 31, 2018:</b>		
	2019	\$ 281
	2020	281
	2021	281
	2022	2,670
	2023	(1,905)
	Thereafter	(1,254)
		<u>\$ 354</u>
		Increase (Decrease) to OPEB Expense
<b>Year Ended December 31, 2017:</b>		
	2018	\$ 5,776
	2019	5,776
	2020	5,776
	2021	5,776
	2022	8,178
	Thereafter	2,289
		<u>\$ 33,571</u>

***Payable to the OPEB Health Insurance Plan***

At December 31, 2018 and 2017, the Water Company reported a payable of \$2,344 and \$1,995, respectively for the outstanding amount of contributions required for the years then ended. This amount represents the employee withholding and employer match for the last month of the years then ended.

***Sensitivity of the Water Company's Proportionate Share of the Net Other Post Employment Benefit (OPEB) Liability to Changes in the Discount Rate and Healthcare Trend Rate***

The following table presents the net other post-employment benefit liability of CERS [as reported in its publicly available financial statements for the years ended June 30, 2018 and 2017, calculated using the single discount rates of 5.85% and 5.84%, respectively as well as what CERS' net OPEB liability would be if it were calculated using a single discount rate that is one percentage point lower or one percentage point higher than the approved rate:

**NORTH SHELBY WATER COMPANY**  
**NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)**  
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**NOTE 14 – COUNTY EMPLOYEES' RETIREMENT SYSTEM – NON-HAZARDOUS EMPLOYEES PENSION PLAN AND POST-EMPLOYMENT HEALTHCARE BENEFIT (INSURANCE PLAN) (Continued)**

***Sensitivity of the Water Company's Proportionate Share of the Net Other Post Employment Benefit (OPEB) Liability to Changes in the Discount Rate and Healthcare Trend Rate (Continued)***

As of June 30, 2018	1% Decrease [4.85%]	Current Discount [5.85%]	1% Increase [6.85%]
Net OPEB Liability	\$ 2,306,064,041	\$ 1,775,480,122	\$ 1,323,519,582
Water Company's Proportionate Share	418,228	322,001	240,033

The following table presents the net other post-employment benefit liability of CERS [as reported in its publicly available financial statements for the year ended June 30, 2018, calculated using the healthcare cost trend rate for the year ended June 30, 2018 as well as what CERS' net OPEB liability would be if it were calculated using a healthcare cost trend rate that is one percentage point lower or one percentage point higher than the approved rate:

As of June 30, 2018	1% Decrease	Current Healthcare Cost Trend Rate	1% Increase
Net OPEB Liability	\$ 1,321,862,520	\$ 1,775,480,122	\$ 2,310,164,647
Water Company's Proportionate Share	239,733	322,001	418,971

The following table presents the net other post-employment benefit liability of CERS [as reported in its publicly available financial statements for the year ended June 30, 2017, calculated using the single discount rates of 5.84% for the year ended June 30, 2017 as well as what CERS' net OPEB liability would be if it were calculated using a single discount rate that is one percentage point lower or one percentage point higher than the approved rate:

As of June 30, 2017	1% Decrease [4.84%]	Current Discount [5.84%]	1% Increase [6.84%]
Net OPEB Liability	\$ 2,558,048,813	\$ 2,010,342,058	\$ 1,554,563,974
Water Company's Proportionate Share	477,844	375,532	290,393

The following table presents the net other post-employment benefit liability of CERS [as reported in its publicly available financial statements for the year ended June 30, 2017, calculated using the healthcare cost trend rate for the year ended June 30, 2017 as well as what CERS' net OPEB liability would be if it were calculated using a healthcare cost trend rate that is one percentage point lower or one percentage point higher than the approved rate:

As of June 30, 2017	1% Decrease	Current Healthcare Cost Trend Rate	1% Increase
Net OPEB Liability	\$ 1,542,035,808	\$ 2,010,342,058	\$ 2,619,112,629
Water Company's Proportionate Share	288,052	375,532	489,250

**NOTE 15 – COMPENSATED ABSENCES**

**Vacation Days**

Vacation is earned at rates varying one to twenty-four days per year depending on the length of service. A maximum of five vacation days may be carried over to the next year. At December 31, 2018, and 2017, the Water Company had accrued compensated absence liabilities of \$9,962 and \$9,435, respectively.

**Sick Days**

Sick leave accrues at the rate of twelve days per year and shall accumulate without limit. If and when the employee retires and resigns, there will be no pay for unused sick leave. At December 31, 2018, the Water Company had an unrecorded sick pay liability of \$126,899. At December 31, 2017, the Water Company had an unrecorded sick pay liability of \$116,685.

**NORTH SHELBY WATER COMPANY**  
**NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)**  
**December 31, 2018 and 2017**

**NOTE 16 – ECONOMIC DEPENDENCY**

The Water Company purchases 100% of the water it sells from the following entities: Shelbyville Municipal Water, Frankfort Electric & Water Plant Board, and Louisville Water Company.

**NOTE 17 – OPERATION AND MAINTENANCE CONTRACT**

The Water Company furnishes managerial, meter reading, maintenance, meter installation, accounts receivable processing, and general office services for U.S. 60 Water District. The Company received \$342,397 and \$289,148 for these services for the years ended December 31, 2018 and 2017, respectively. There was a receivable due from U.S. 60 Water District in the amount of \$59,218 and \$25,005 at December 31, 2018 and 2017, respectively. The December 2018 receivable included \$26,284 for December 2018 and \$27,260 for November 2018 and was increased by \$5,674 for an underbilling. The December 2017 receivable from U.S. 60 Water District of \$19,832 was increased by \$5,173 for an undercharge by the Water Company during the year. The operation and maintenance agreement was updated in 2017.

**NOTE 18 – FUNDS HELD FOR FUTURE LINES AND CONTRIBUTED CAPITAL**

The Water Company collects funds from developers for their allocable cost of line extensions. The amount is calculated based on the size of the line and cost of construction. The Water Company held \$692,438 and \$0 for future lines at December 31, 2018 and 2017, respectively.

**NOTE 19 – COMMITMENTS, CONTINGENCIES AND SUBSEQUENT EVENTS**

North Shelby Water Company continues work on the East-West Connector project. North Shelby Water Company is constructing an East-West Connector line which will transport water purchased from Louisville Water Company. The first phase of this project consisted of the construction of the new Long Run Pump Station. A second, dual purpose pump station to pump water from Louisville Water Company eastward through the new East-West Connector and/or westward to North Central and Northwestern Shelby County was constructed during the second phase of the project. The third phase of the project consisted of a line and booster pump station, the construction of a 400,000 gallon elevated storage tank at Todd's Point, and the Jacksonville water storage tank rehabilitation. The fourth phase of the project entails construction of a new 750,000 gallon elevated water storage tank. North Shelby Water Company completed Phase III of the project during calendar year 2017. The fourth phase was completed in May 2019.

The East West Connector Project was financed by USDA. Phase III has \$204,523 available funding remaining. The Water Company plans to combine the remaining funds from Phase III and any remaining available funds after completion of Phase IV to rehab a storage tank.

North Shelby Water Company is constructing an 8 inch main on Benson Pike for an industrial customer. The estimated cost of the project \$925,000 is being funded by customer contribution.

During the 2018 Kentucky Legislature Session, House bill 362 passed which caps CERS Employer Contribution rate increases up to 12% per year over the prior fiscal year for the period July 1, 2018 to June 30, 2028. The CERS Employer rates, beginning July 1, 2018 and 2019 have been set at 21.48% and 24.06% respectively.

**NOTE 20 – RECENTLY ADOPTED ACCOUNTING PRONOUNCEMENTS**

In June 2015, the GASB issued Statement 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*, effective for fiscal years beginning after June 15, 2017 [Water Company year beginning January 1, 2018]. This statement requires the liability of employers to employees for defined benefit OPEB (net OPEB liability) to be measured as the portion of the present value of projected benefit payments to be provided to current active and inactive employees that is attributed to those employees' past periods of service (total OPEB liability), less the amount of the OPEB plan's fiduciary net position. Under this statement, the Water Company is required to report in its financial statement(s), the net other postemployment benefit liability associated with its' employees' benefits as a liability. It is also required to report a deferred outflow of resources for its benefit, contributions made subsequent to the measurement date of the beginning net OPEB liability. These balances reflect the government's obligation to pay deferred benefits earned by its employees when the benefit [plan's] liability exceeds the value of the benefit plan's assets.

Retroactive application by restating financial statements for all periods presented is required. The effect of the reinstatement is as follows for the year ended December 31, 2017.

**NORTH SHELBY WATER COMPANY**  
**NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)**  
**December 31, 2018 and 2017**

**NOTE 20 – RECENTLY ADOPTED ACCOUNTING PRONOUNCEMENTS (Continued)**

**Statement of Net Position:**

Total Net Position as Originally Presented December 31, 2017	\$ 11,351,378
Less: Net OPEB Liability	(375,532)
Plus: Deferred Outflows - Change in Assumptions	81,713
Less: Deferred Inflows -	
* Difference Between Expected & Actual Experience	(1,043)
* Change in Proportion & Difference Between Employer Contributions & Proportionate Share of Contributions	(872)
* Net Difference Between Projected and Actual Investment Earnings on Pension Plan Investments	(17,747)
Total Net Position as Restated at December 31, 2017	<u>\$ 11,037,897</u>

**The components of Net Position at December 31, 2017:  
after restatement are as follows:**

Net Investment in Capital Assets	\$ 8,907,644
Restricted for Capital Projects	129,332
Restricted for Debt Service	819,191
Unrestricted	1,181,730
Total Net Position as Restated at December 31, 2017	<u>\$ 11,037,897</u>

**Statement of Revenues, Expenses and Changes in Fund Net Position:**

Change in Net Position as Originally Presented in the [Comparative] Statement for the Year Ended December 31, 2017	\$ 63,302
GASB 75 Adjustments for OPEB Liability	(42,793)
Change in Net Position as Restated for the Year Ended December 31, 2017	<u>\$ 20,509</u>

**NORTH SHELBY WATER COMPANY**  
**SCHEDULE OF THE WATER COMPANY'S PROPORTIONATE SHARE OF THE NET PENSION LIABILITY**  
**COUNTY EMPLOYEES RETIREMENT SYSTEM**  
**Years Ended December 31**

	<u>2018</u>	<u>2017</u>	<u>2016</u>	<u>2015</u>	<u>2014</u>
Water Company's proportion of the net pension liability (asset) %	0.018370%	0.018680%	0.018834%	0.018220%	0.017846%
Water Company's proportionate share of the net pension liability (asset)	\$ 1,104,599	\$ 1,093,398	\$ 927,293	\$ 783,379	\$579,000
Water Company's covered payroll (Calendar Year)	\$ 457,698	\$458,377	\$ 448,684	\$ 433,851	\$426,930
Water Company's proportionate share of the net pension liability (asset) as a percentage of its covered payroll	241.34%	238.54%	206.67%	180.56%	135.62%
Plan fiduciary net position as a percentage of the total pension liability	53.54%	53.3%	55.5%	59.97%	62.60%

Calculations of the Water Company's proportion of the net pension liability (%) and proportionate share of the net pension liability (\$) are based on reports of the Kentucky Retirement Systems', County Employees Retirement Systems' Schedule of Employer Allocations and Pension Amounts by Employer for the fiscal years ended June 30, shown.

Water Company payroll is reported for its' covered calendar years ending December 31, 2014 through 2018.

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

During the 2018 legislative session, House Bill 185 was enacted, which updated the benefit provisions for active members who die in the line of duty. Benefits paid to the spouses of deceased members have been increased from 25% of the member's final rate of pay to 75% of the member's average pay. If the member does not have a surviving spouse, benefits paid to surviving dependent children have been increased from 10% of the member's final pay rate to 50% of average pay for one child, 65% of average pay for two children, or 75% of average pay for three children.

There have been no changes in the actuarial assumptions since June 30, 2017. Actuarial Methods and Assumptions for Determining Net Pension Liability:

	<u>2018</u>	<u>2017</u>	<u>2016</u>	<u>2015</u>	<u>2014</u>
Inflation	2.30%	2.30%	3.25%	3.25%	3.50%
Salary Increases	3.05%	3.05%	4.00%	4.00%	4.50%
Investment Rate of Return	6.25%	6.25%	7.50%	7.50%	7.75%

The mortality table used for active members is RP-2000 Combined Mortality Table projected with Scale BB to 2013 (multiplied by 50% for males and 30% for females). For healthy retired members and beneficiaries, the mortality table used is the RP-2000 Combined Mortality Table projected with Scale BB to 2013 (set-back for one year for females). For disabled members, the RP-2000 Combined Disabled Mortality Table projected with Scale BB to 2013 (set-back four years for males) is used for the period after disability retirement.

The assumed rates of retirement, withdrawal, and disability were based on an actuarial valuation performed as of June 30, 2017.

**NORTH SHELBY WATER COMPAY  
SCHEDULE OF THE WATER COMPANY'S CONTRIBUTIONS (PENSION)  
COUNTY EMPLOYEES RETIREMENT SYSTEM**

**Years Ended December 31**

	<u>2018</u>	<u>2017</u>	<u>2016</u>	<u>2015</u>
Contractually required contributions	\$ 70,519	\$ 64,825	\$ 59,977	\$ 56,189
Contributions in relation to the contractually required contributions	70,519	64,825	59,977	56,189
Contribution deficiency (excess)	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>
Water Company's covered payroll (calendar year)	\$ 457,698	\$ 458,377	\$ 448,684	\$ 433,851
Contributions as a percentage of covered payroll	14.48%	13.95%	12.42%	12.75%

The Water Company's contributions above include only contributions to the County Employees Retirement System Pension Fund. GASB 68 requires the Water Company to present the above information for the CERS pension for 10 years. The information will be expanded annually until a full 10-year trend is compiled.



**NORTH SHELBY WATER COMPANY  
SCHEDULE OF THE WATER COMPANY'S PROPORTIONATE SHARE OF THE NET OPEB LIABILITY  
COUNTY EMPLOYEES RETIREMENT SYSTEM**

**Years Ended December 31**

	<b>2018</b>	<b>2017</b>
Water Company's proportion of the net OPEB liability (asset) %	0.018137%	0.018680%
Water Company's proportionate share of the net OPEB liability (asset)	\$ 322,001	\$375,532
Water Company's covered payroll (Calendar Year)	\$ 457,698	\$458,377
Water Company's proportionate share of the net OPEB liability (asset) as a percentage of its covered payroll	70.35%	81.93%
Plan fiduciary net position as a percentage of the total OPEB liability	57.62%	52.4%

Calculations of the Water Company's proportion of the net OPEB liability (%) and proportionate share of the net OPEB liability (\$) are based on reports of the Kentucky Retirement Systems', County Employees Retirement Systems' Schedule of Employer Allocations and OPEB Amounts by Employer for the fiscal years ended June 30, shown.

Water Company covered payroll is reported for its calendar year.

GASB 75 requires the Water Company to present the above information for 10 years. The information will be expanded annually until a full 10-year trend is compiled.

During the 2018 legislative session, House Bill 185 was enacted, which updated the benefit provisions for active members who die in the line of duty. The system shall now pay 100% of the insurance premium for spouses and children of all active members who die in the line of duty.

Actuarial Methods and Assumptions for Determining Net OPEB Liability:

There were no changes in actuarial assumptions since June 30, 2017.

	<b>2018</b>	<b>2017</b>
Payroll Growth Rate	2.0%	2.0%
Salary Increases	3.05% Average	3.05% Average
Investment Rate of Return	6.25%	6.25%
Investment Rate of Return	7.50%	7.75%
Inflation	2.3%	2.3%
Healthcare Trend Rates: Pre-65	Initial trend at 7.00% at January 1, 2020, and gradually decreasing to an ultimate trend rate of 4.05% over a period of 12 years.	Initial trend at 7.00% at January 1, 2020, and gradually decreasing to an ultimate trend rate of 4.05% over a period of 12 years.
Healthcare Trend Rates: Post-65	Initial trend starting at 5.00% at January 1, 2020, and gradually decreasing to an ultimate trend rate of 4.05% over a period of 10 years.	Initial trend starting at 5.00% at January 1, 2020, and gradually decreasing to an ultimate trend rate of 4.05% over a period of 10 years.
Healthcare Trend Rates: Mortality:	The mortality table used for active members is RP-2000 Combined Mortality Table projected with Scale BB to 2013 (multiplied by 50% for males and 30% for females). For healthy retired members and beneficiaries, the mortality table used is the RP-2000 Combined Mortality Table projected with Scale BB to 2013 (set-back for one year for females). For disabled members, the RP-2000 Combined Disabled Mortality Table projected with Scale BB to 2013 (set-back four years for males) is used for the period after disability retirement.	The mortality table used for active members is RP-2000 Combined Mortality Table projected with Scale BB to 2013 (multiplied by 50% for males and 30% for females). For healthy retired members and beneficiaries, the mortality table used is the RP-2000 Combined Mortality Table projected with Scale BB to 2013 (set-back for one year for females). For disabled members, the RP-2000 Combined Disabled Mortality Table projected with Scale BB to 2013 (set-back four years for males) is used for the period after disability retirement.

**NORTH SHELBY WATER COMPANY  
SCHEDULE OF THE WATER COMPANY'S CONTRIBUTIONS (OPEB)  
COUNTY EMPLOYEES RETIREMENT SYSTEM**

**Years Ended December 31**

	<u>2018</u>	<u>2017</u>	<u>2016</u>	<u>2015</u>
Contractually (Employer) required contributions	\$ 22,884	\$ 21,980	\$ 20,335	\$ 19,051
Contributions in relation to the contractually required contributions	22,884	21,980	20,335	19,051
Contribution deficiency (excess)	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>
Water Company's covered payroll	\$ 457,698	\$ 458,377	\$ 448,684	\$ 433,851
Contributions as a percentage of covered payroll	4.70%	4.73%	4.64%	4.92%

The Water Company's contributions above include only the contributions to the County Employees Retirement System Insurance Fund.

GASB 75 requires the Water Company to present the above information for the CERS OPEB Plan for 10 years. The information will be expanded annually until a full 10-year trend is compiled.

# RAISOR, ZAPP & WOODS, PSC

## Certified Public Accountants

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Susan A. Dukes, CPA

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

To the Board of Directors of the  
North Shelby Water Company  
Bagdad, Kentucky 40003

We have audited in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of North Shelby Water Company as of and for the year ended December 31, 2018, and the related notes to the financial statements, which collectively comprise North Shelby Water Company's basic financial statements, and have issued our report thereon dated June 28, 2019.

#### **INTERNAL CONTROL OVER FINANCIAL REPORTING**

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

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

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that have not been identified. We did identify certain deficiencies in internal control, described in the accompanying schedule of findings and questioned costs as Items 2018-001 and 2018-002 that we consider to be material weaknesses.

## **COMPLIANCE AND OTHER MATTERS**

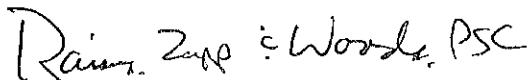
As part of obtaining reasonable assurance about whether North Shelby Water Company's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct 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*.

## **NORTH SHELBY WATER COMPANY'S RESPONSE TO FINDINGS**

North Shelby Water Company's response to the findings identified in our audit is described in the accompanying schedule of findings and questioned costs. North Shelby Water Company's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

## **PURPOSE OF THIS REPORT**

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



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

June 28, 2019

# RAISOR, ZAPP & WOODS, PSC

## Certified Public Accountants

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### INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE FOR EACH MAJOR FEDERAL PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE REQUIRED BY THE UNIFORM GUIDANCE

To the Board of Directors of  
North Shelby Water Company  
Bagdad, Kentucky 40003

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

We have audited North Shelby Water Company's compliance with the types of compliance requirements described in the *OMB Compliance Supplement* that could have a direct and material effect on each of North Shelby Water Company's major federal programs for the year ended December 31, 2018. North Shelby Water Company's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs.

#### *Management's Responsibility*

Management is responsible for compliance with federal statutes, regulations and the terms and conditions of its federal awards applicable to its federal programs.

#### *Auditor's Responsibility*

Our responsibility is to express an opinion on compliance for each of North Shelby Water Company's major federal programs based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and the audit requirements of Title 2 U.S. *Code of Federal Regulations* Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance). Those standards and the Uniform Guidance require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about North Shelby Water Company's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

We believe that our audit provides a reasonable basis for our opinion on compliance for each major federal program. However, our audit does not provide a legal determination of North Shelby Water Company's compliance.

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

In our opinion, North Shelby Water Company complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended December 31, 2018.

### Report on Internal Control Over Compliance

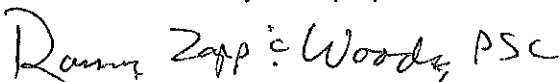
Management of North Shelby Water Company is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered North Shelby Water Company's internal control over compliance with the types of requirements that could have a direct and material effect on each major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major federal program and to test and report on internal control over compliance in accordance with the Uniform Guidance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of North Shelby Water Company's internal control over compliance.

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

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that have not been identified. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, we identified a deficiency in internal control over compliance, described in the accompanying schedule of findings and questioned costs as Item 2018-003 that we consider to be a significant deficiency.

North Shelby Water Company's response to the internal control over compliance finding identified in our audit is described in the accompanying schedule of findings and questioned costs and corrective action plan. North Shelby Water Company's response was not subjected to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on the response.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of the Uniform Guidance. Accordingly, this report is not suitable for any other purpose.



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

June 28, 2019

**NORTH SHELBY WATER COMPANY  
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS  
For the Year Ended December 31, 2018**

<u>Federal Grantor/Pass-through Grantor/Program or Cluster Title</u>	<u>Federal CFDA Number</u>	<u>Federal Expenditures</u>
<b><u>United States Department of Agriculture</u></b>		
Rural Development		
Direct Program		
Water and Waste Disposal Systems for Rural Communities	10.760	\$ 1,704,347
Total United States Department of Agriculture		\$ 1,704,347
Total Expenditures of Federal Awards		\$ 1,704,347

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

**Note A: Basis of Presentation**

The accompanying schedule of expenditures of federal awards (the Schedule) includes the federal award activity of North Shelby Water Company under programs of the federal government for the year ended December 31, 2018. The information in this Schedule is presented in accordance with the requirements of Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance). Because the Schedule presents only a selected portion of the operations of the North Shelby Water Company, it is not intended to and does not present the financial position, changes in net position, or cash flows of North Shelby Water Company.

**Note B: Summary of Significant Accounting Policies**

Expenditures reported on the Schedule are reported on the accrual basis of accounting. Such expenditures are recognized following the cost principles contained in the Uniform Guidance, wherein certain types of expenditures are not allowable or are limited as to reimbursement.

**Note C: Non Cash Awards**

The North Shelby Water Company did not receive any other federal awards in the form of non-cash assistance, insurance contracts, or loan guarantees for the year ended December 31, 2018.

**Note D: Notes Payable**

At December 31, 2018, including the above total expenditures, North Shelby Water Company had loans outstanding and payable to the USDA Rural Development in the amount of \$7,975,150. These loans impose no continuing compliance requirements other than to repay the loans.

**Note E: Passed Through to Sub-Recipients**

There were no awards passed through to sub-recipients.

**Note F: Indirect Cost Rate**

North Shelby Water Company has not elected to use the 10% de minimis indirect cost rate. North Shelby Water has not included indirect costs in the schedule.

**NORTH SHELBY WATER COMPANY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
For the Year Ended December 31, 2018**

**A. SUMMARY OF AUDIT RESULTS**

1. The auditor's report expresses an unmodified opinion on whether the financial statements of North Shelby Water Company were prepared in accordance with GAAP.
2. Two deficiencies in internal control disclosed during the audit of the financial statements are reported in the Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards*. Items 2018-001 and 2018-002 were reported as material weaknesses.
3. No instances of noncompliance material to the financial statements of North Shelby Water Company, which would be required to be reported in accordance with *Government Auditing Standards*, were disclosed during the audit.
4. One significant deficiency in internal control over the major federal award program was disclosed during the audit and is reported in the Report on Compliance for Each Major Federal Program and on Internal Control over Compliance Required by the Uniform Guidance. Item 2018-003 was reported as a significant deficiency.
5. The auditor's report on compliance for the major federal award program for the North Shelby Water Company expresses an unmodified opinion.
6. Audit findings that are required to be reported in accordance with 2 CFR Section 200.516(a) are reported in this Schedule.
7. The program tested as a major program was:

United States Department of Agriculture:  
Water and Waste Disposal Systems  
for Rural Communities

CFDA No.

10.760

8. The threshold used for distinguishing between Type A and Type B programs was \$750,000.
9. The North Shelby Water Company did not qualify as a low risk auditee.

**B. FINDINGS - FINANCIAL STATEMENTS AUDIT**

**GOVERNMENT AUDITING STANDARDS**

**DEFICIENCIES IN INTERNAL CONTROL**

**2018-001 SIZE OF ENTITY, CROSS-TRAINING, CHECKING PROCEDURES AND DOCUMENTATION**

**CRITERIA:**

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



**NORTH SHELBY WATER COMPANY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)  
For the Year Ended December 31, 2018**

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

**GOVERNMENT AUDITING STANDARDS (Continued)**

**DEFICIENCIES IN INTERNAL CONTROL (Continued)**

**2018-001 SIZE OF ENTITY, CROSS-TRAINING, CHECKING PROCEDURES AND DOCUMENTATION  
(Continued)**

**CONDITION:**

Due to the size of the entity, cross-training and checking procedures are not in place for certain administrative functions. This condition was also cited as a material weakness in the schedule of findings and questioned costs for the year ended December 31, 2017 as Item 2017-001.

**CAUSE:**

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

**EFFECT:**

These limitations may affect the ability to timely record, process, summarize and report financial data. Debt service and depreciation transfers were not reviewed timely. Inconsistencies were viewed in joint maintenance agreement calculations.

**RECOMMENDATION:**

Management should strive to provide cross-training for administrative staff, implement checking processes and increase review procedures. Management should periodically review invoice and expenditures processes and documentation to help employees maintain good practices. Periodic reviews of debt service requirements should also occur.

**VIEW OF RESPONSIBLE OFFICIALS AND PLANNED CORRECTIVE ACTION:**

We concur with the recommendation. Efforts have been made to cross train employees and improve transaction documentation. The Company will continue its efforts to improve training and review associated procedures.

**2018-002 FAILURE TO PREPARE COMPLETE SET OF FINANCIAL STATEMENTS INCLUDING REQUIRED  
NOTE DISCLOSURES**

**CRITERIA:**

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

**CONDITION:**

Company financial statements, including the required disclosures, are prepared as part of the annual audit. This condition was also cited as a material weakness in the schedule of findings and questioned costs for the year ended December 31, 2017 as Item 2017-002.

**CAUSE:**

The draft accrual basis financial statements and disclosures are prepared during the audit process. The entries are entered into the Company's general ledger/financial reports.

**NORTH SHELBY WATER COMPANY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)  
For the Year Ended December 31, 2018**

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

**GOVERNMENT AUDITING STANDARDS (Continued)**

**DEFICIENCIES IN INTERNAL CONTROL (Continued)**

**2018-002 FAILURE TO PREPARE COMPLETE SET OF FINANCIAL STATEMENTS INCLUDING REQUIRED NOTE DISCLOSURES**

**EFFECT:**

Management engaged auditor assistance to prepare the draft of the financial statements, including the related notes to the financial statements. Management reviewed, approved, and accepted responsibility for the financial statements prior to their issuance.

**RECOMMENDATION:**

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

**VIEWS OF RESPONSIBLE OFFICIALS AND PLANNED CORRECTIVE ACTION:**

The outsourcing of this service is a result of management's cost benefit decision to use others' accounting expertise rather than incur internal resource costs. We concur with the recommendation and will continue to improve our overall accounting knowledge in performing our oversight responsibilities.

**COMPLIANCE**

None

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

**SIGNIFICANT DEFICIENCIES**

**2018-003 Checking and Review Procedures**

**U.S. Department of Agriculture: Direct Program, Water and Waste Disposal Systems for Rural Communities - CFDA #10.760; loan dated October 12, 2017.**

**CRITERIA:**

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

**CONDITION:**

Checking procedures and rotation of duties are limited due to the size of the administrative staff and responsibilities associated with individual positions. Training for managerial and staff responsibilities associated with the federal program are limited. Administrative review procedures have not been executed fully in oversight. Managerial staff depends on external parties for federal program oversight.

**CAUSE:**

Responsibilities of the Water Company staff for federal program requirements have not been clearly defined and communicated. Funds were received from Rural Development, but payment was not made to the contractor within 30 days in two instances. Short lived asset accounts have not been established. Sufficient debt service transfers were not made timely as required by note agreements.

**NORTH SHELBY WATER COMPANY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)  
For the Year Ended December 31, 2018**

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

**SIGNIFICANT DEFICIENCIES (Continued)**

**2018-003 Checking and Review Procedures (Continued)**

**U.S. Department of Agriculture: Direct Program, Water and Waste Disposal Systems for Rural Communities  
- CFDA #10.760; loan dated October 12, 2017 (Continued)**

**EFFECT:**

Specific requirements of the Rural Development financing as set forth in its letter of conditions were not communicated to all appropriate Water Company staff. Lack of communication could cause a failure to adhere to federally mandated rules and regulations.

**QUESTIONED COSTS:**

None

**CONTEXT:**

A review of controls over federal expenditures and the Company's reliance on outside entities in its oversight of federal program expenditures was performed.

**IDENTIFICATION OF A REPEAT FINDING**

The Water Company Staff's reliance on other parties continues to limit availability of formally executed documents. The Water Company should maintain all completed documents on site.

**RECOMMENDATION:**

Employees should be fully trained on compliance requirements associated with the federal programs and responsibility should be assigned. Management should continue to contract with parties knowledgeable of federal program compliance, but should be aware that the Company, itself, is the entity with ultimate responsibility. Staff should annually review all debt and depreciation reserves timely to determine appropriate transfers and balances as required by the loans. Contractor payments should be made timely once properly approved.

**VIEWS OF RESPONSIBLE OFFICIALS AND PLANNED CORRECTIVE ACTION:**

The Water Company will clearly define the job requirements and responsibilities of Water Company staff. North Shelby Water Company will implement review and checking procedures to determine that all requirements and board approvals are communicated and implemented properly.

**COMPLIANCE**

None

**NORTH SHELBY WATER COMPANY  
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS  
For the Year Ended December 31, 2018**

**Finding 2017-001: Size of Entity, Cross-Training, Checking Procedures and Documentation**

**Condition:** This finding was a material weakness stating that due to the size of the entity, cross-training and checking procedures were not in place for certain administrative functions. This lack of checking procedures could affect the Company's ability to timely record, process, summarize and report financial data.

**Recommendation:** It was recommended that procedures be implemented to ensure cross training and checking procedures are in place to allow proper wording of transactions.

**Current Status:** Management continues to implement checking and review procedures. Finding 2018-001 has identified a continued need for checking and review procedures.

**Finding 2017-002: Failure to Prepare a Complete Set of Financial Statements Including Required Note Disclosures**

**Condition:** This finding was a material weakness indicating that the Company's financial statements, including the required note disclosures, are prepared as part of the annual audit.

**Recommendation:** Company management should continue to enhance its knowledge of reporting requirements in providing oversight of this service.

**Current Status:** As indicated in Finding 2018-002, the Water Company continues to outsource this service as a result of management's cost benefit decision.

**U.S. Department of Agriculture**

**Finding 2017-003: U.S. Department of Agriculture: Direct Program, Water and Waste Disposal Systems for Rural Communities – CFDA #10.760: Checking and Review Procedures**

**Condition:** The finding was a significant deficiency stating that administrative review procedures were not executed fully in oversight.

**Recommendation:** It was recommended that employees be fully trained on compliance requirements associated with the federal programs.

**Current Status:** Finding 2018-003 has identified a continued need for checking procedures and federal program requirement training.

## North Shelby Water Company

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Jerry Ruble, President

Bryan Franklin, Vice President

Tom McGinnis, Secretary/Treasurer

Kevin Armstrong, Director  
James Anglin, Director  
Herb McCoun, Director  
Lloyd Eades, Director  
Jim Smith, Director

### U. S. Department of Agriculture

North Shelby Water Company respectfully submits the following corrective action plan for the year ended December 31, 2018.

Name and Address of the independent public accounting firm: Ralsor, Zapp & Woods, PSC, 513 Highland Avenue, P. O. Box 354, Carrollton, KY 41008.

Audit Period: As of and for the year ended December 31, 2018.

The findings from the December 31, 2018 schedule of findings and questioned costs are discussed below. The findings are numbered consistently with the numbers assigned in the schedule.

### FINDINGS-FINANCIAL STATEMENT AUDIT

#### **Material Weakness 2018-001 - Size of Entity, Cross-training, Checking Procedures and Documentation**

In response to this item, the Water Company will do its best to address this issue through enhanced management oversight and checking procedures. We believe that we have an office staff commensurate with the size and needs of the Water Company. Financial considerations have been taken into consideration in meeting those needs. We will continue to cross train office staff members to protect the Water Company from unforeseen circumstances.

#### **Material Weakness 2018-002 - Failure to Prepare a Complete Set of Financial Statements Including Required Note Disclosures**

In response to this item, the Water Company's decision to outsource the preparation of the complete set of financial statements and required note disclosures is a cost-benefit decision. The Water Company is aware of its role in oversight of this process and is conscientious in its efforts to review the reporting package. It is anticipated that the Water Company will continue to outsource this procedure.

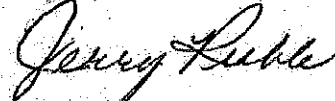
## FINDINGS-FEDERAL AWARD PROGRAM AUDITS

### Significant Deficiency in Internal Controls Over Compliance – 2018-003 –Checking & Review Procedures

In response to this item, the Water Company is aware of its responsibility to comply with the specific requirements of the Rural Development financing as set forth in its letter of conditions. The Water Company will seek to implement further review procedures for all compliance requirements. The Water Company will annually review debt and depreciation reserve accounts to determine appropriate transfers and balances. The Water Company will remit payment to all contractors once an approved pay estimate is received.

If the U. S. Department of Agriculture has questions regarding this plan, please call Jerry Ruble at (502) 747-8942.

Sincerely-



Jerry Ruble

Chairman

June 27, 2019