

NORTHERN MADISON COUNTY SANITATION DISTRICT
AUDITED FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2013

**NORTHERN MADISON COUNTY SANITATION DISTRICT
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FOR THE YEAR ENDED JUNE 30, 2013**

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INDEPENDENT AUDITOR'S REPORT

To the Chairman and Board of Directors
Northern Madison County Sanitation District
Richmond, Kentucky 40475

Report on the Financial Statements

I have audited the accompanying financial statements of the business-type activities of Northern Madison County Sanitation District as of and for the year ended June 30, 2013, and the related notes to the financial statements, which collectively comprise the District's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

My responsibility is to express an opinion on these financial statements based on my audit. I conducted my 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 I 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 District'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 opinions on the effectiveness of the District's internal control. Accordingly, I 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.

I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my audit opinion.

Opinion

In my opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the business-type activities of the District as of June 30, 2013, and the respective changes in financial position, and where applicable, cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Management has omitted the Management Discussion and Analysis that accounting principles generally accepted in the United States of America required 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. My opinion on the basic financial statements is not affected by the missing information.

Accounting principles generally accepted in the United States of America require that the budgetary comparison to be presented to supplement the basic financial statements. Such information, although not part of the basic financial statements, is required by Government 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. I 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 I obtained during my audit of the basic financial statements. I 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.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, I have also issued my report dated December 10, 2013, on my consideration of the District's internal control over financial reporting and my tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of my testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the District's internal control over financial reporting.

Sammy K. Lee, P.S.C.

Berea, Kentucky
December 10, 2013

**NORTHERN MADISON COUNTY SANITATION DISTRICT
STATEMENT OF NET POSITION
JUNE 30, 2013**

ASSETS

Current Assets

| | |
|--|-----------------------|
| Cash and cash equivalents | \$ 390,429 |
| Accounts receivable less allowance for doubtful accounts of \$ 11,739 | 319,114 |
| Accounts receivable - tap on fees | 133,797 |
| Total Current Assets | <u>843,340</u> |

Non-Current Assets

| | |
|--|--------------------------|
| Restricted cash | 399,513 |
| Capital assets, net of accumulated depreciation of \$ 3,044,298 | 19,081,756 |
| Total Non-Current Assets | <u>19,481,269</u> |

TOTAL ASSETS **\$ 20,324,609**

LIABILITIES AND NET POSITION

Current Liabilities

| | |
|--|-----------------------|
| Accounts payable and accrued liabilities | \$ 40,383 |
| Notes payable - current portion | 406,521 |
| Interest payable | 7,500 |
| Total Current Liabilities | <u>454,404</u> |

Non-Current Liabilities

| | |
|--------------------------------------|-------------------------|
| Other non-current liabilities | 34,479 |
| Notes payable | 7,033,216 |
| Total Non-Current Liabilities | <u>7,067,695</u> |

Total Liabilities **7,522,099**

Net Position

| | |
|----------------------------------|--------------------------|
| Net investment in capital assets | 12,041,532 |
| Unrestricted | 361,465 |
| Restricted | 399,513 |
| Total Net Position | <u>12,802,510</u> |

TOTAL LIABILITIES AND NET POSITION **\$ 20,324,609**

**NORTHERN MADISON COUNTY SANITATION DISTRICT
STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED JUNE 30, 2013**

| | |
|--|----------------------|
| OPERATING REVENUES | |
| Charges for services | \$ 1,192,905 |
| Miscellaneous | 23,669 |
| | <hr/> |
| TOTAL OPERATING REVENUES | 1,216,574 |
| | <hr/> |
| OPERATING EXPENSES | |
| Personnel costs | 140,655 |
| Contractual services | 66,150 |
| Utilities & telephone | 236,750 |
| Repairs & maintenance | 86,806 |
| Auto expense & travel | 19,362 |
| Office expense | 1,230 |
| Laboratory services | 14,028 |
| Supplies | 54,431 |
| Rent | 3,000 |
| Insurance | 19,044 |
| Depreciation | 587,036 |
| Bad debt expense | 11,153 |
| Miscellaneous | 4,143 |
| | <hr/> |
| TOTAL OPERATING EXPENSES | 1,243,788 |
| | <hr/> |
| Operating loss | (27,214) |
| NON-OPERATING REVENUES (EXPENSES) | |
| Interest income | 2,328 |
| Development fees (Tap & Grinder Fees) | 41,557 |
| Interest expense | (79,897) |
| | <hr/> |
| TOTAL NON-OPERATING REVENUES (EXPENSES) | (36,012) |
| | <hr/> |
| LOSS BEFORE CONTRIBUTIONS AND TRANSFERS | (36,012) |
| | <hr/> |
| CHANGE IN NET POSITION | (63,226) |
| | <hr/> |
| NET POSITION AT BEGINNING OF YEAR | 12,865,736 |
| | <hr/> |
| NET POSITION AT END OF YEAR | \$ 12,802,510 |
| | <hr/> <hr/> |

The accompanying notes are an integral part of the financial statements.

**NORTHERN MADISON COUNTY SANITATION DISTRICT
STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED JUNE 30, 2013**

CASH FLOWS FROM OPERATING ACTIVITIES

| | |
|--|-----------------------|
| Receipts from customers | \$ 1,165,746 |
| Other receipts | 23,669 |
| Payments to suppliers | (524,653) |
| Payments to employees | (144,776) |
| Net cash provided by operating activities | <u>519,986</u> |

CASH FLOWS FROM NONCAPITAL

FINANCING ACTIVITIES

| | |
|---|---------------------|
| Interest income | 2,328 |
| Net cash provided by noncapital financing activities | <u>2,328</u> |

CASH FLOWS FROM CAPITAL AND

RELATED FINANCING ACTIVITIES

| | |
|---|-------------------------|
| Proceeds from development fees | 41,557 |
| Principal paid on capital debt | (400,403) |
| Purchase of capital assets | (137,472) |
| Interest paid on capital debt | (79,116) |
| Net cash used by noncapital financing activities | <u>(575,434)</u> |

| | |
|--|--------------------------|
| Net decrease in cash and cash equivalents | (53,120) |
| Cash and cash equivalents - beginning of year | 843,062 |
| Cash and cash equivalents - end of year | <u>\$ 789,942</u> |

Reconciliation of operating loss to net cash provided by operating activities:

| | |
|---|--------------------------|
| Operating loss | \$ (27,214) |
| Adjustments to reconcile operating loss to net cash provided by operating activities: | |
| Bad debt expense | 11,153 |
| Depreciation expense | 587,036 |
| Change in assets and liabilities | |
| Receivables, net | (38,312) |
| Accounts and other payables | (12,677) |
| Net cash provided by operating activities | <u>\$ 519,986</u> |

**NORTHERN MADISON COUNTY SANITATION DISTRICT
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2013**

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A summary of the District's significant accounting policies applied in the preparation of the accompanying financial statements follows:

Nature of Organization and Activities

The District was established by Madison County Fiscal Court Ordinance #96.07. The original directors were appointed by the Madison County Judge Executive to operate the sanitation district at that time. The officers adopted by-laws dated January 7, 1997. The by-laws state that succeeding directors will also be appointed by the Madison County Judge Executive. The Board of Directors are commissioned by the by-laws to control and manage the affairs of the District and shall have all powers authorized by KRS Chapter 220 for directors of sanitation districts.

Reporting Entity

The Northern Madison County Sanitation District's financial statements include the operations of all entities for which the Board of Directors exercises oversight responsibility. Oversight responsibility includes, but is not limited to financial interdependency, selection of the governing authority, designation of management, ability to significantly influence operations, and accountability for fiscal matters. The District has no identifiable component units.

Measurement Focus and Basis of Accounting

The proprietary fund financial statements use a flow of economic resources measurement focus to determine net income and financial position. The accounting principles used are similar to those applicable to businesses in the private sector and, thus, these funds are maintained on the accrual basis of accounting. Revenues are recognized when earned and expenses are recognized when incurred.

GASB Statement No. 20 Election

Pursuant to the election option made available by GASB Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*, pronouncements of the Financial Accounting Standards Board (FASB) issued after November 30, 1989, are not applied in the preparation of the business-type activities and the enterprise fund financial statements.

Financial Statement Presentation

The financial statements of the District have been prepared in conformity with U.S. Generally Accepted Accounting Principles (GAAP) as applied to government units. The Government Accounting Standards Board (GASB) is the accepted standard setting body for establishing governmental accounting and financial reporting principles.

Generally accepted accounting principles for state and local governments requires that resources be classified for accounting and reporting purposes into the following three net position categories:

Net investment in capital assets – Capital Assets, net of accumulated depreciation and outstanding principal balances of debt attributable to the acquisition, construction or improvement of those assets.

Restricted – Net positions whose use by the District is subject to externally imposed stipulations that can be fulfilled by actions of the District pursuant to those stipulations or that expire by the passage of time. Such assets include assets restricted for capital acquisitions and debt service.

Unrestricted – Net position that is not subject to externally imposed stipulations. Unrestricted net assets may be designated for specific purposes by action of management or the District's Board or may otherwise be limited by contractual agreements with outside parties.

**NORTHERN MADISON COUNTY SANITATION DISTRICT
NOTES TO FINANCIAL STATEMENTS - CONTINUED
JUNE 30, 2013**

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

Cash and Cash Equivalents

The District considers all checking and savings accounts with an original maturity of three months or less when purchased to be cash equivalents. Cash deposits are reported at their carrying amount.

Deposits and Investments

It is the District's policy for deposits to be 100% secured.

Accounts Receivable and Allowance for Doubtful Accounts

Receivable represent charges due at year-end and are considered fully collectible by the District with an allowance for doubtful amounts taken into consideration. The receivables are reviewed periodically to establish or update the provision for uncollectible amounts. These provisions are estimated based on an analysis of the age of the various accounts. The District records the amount of earned but unbilled service revenues as revenue.

Capital Assets

Constructed or purchased assets are recorded at historical cost or estimated historical cost. Donated assets are recorded at the estimated fair market value on the date of donation. The thresholds for capitalization of assets range from \$500 to \$1,000, depending on the asset class. Costs of maintenance and repairs that do not add value to the assets or extend their useful lives are not capitalized and are expensed in the current period. Depreciation expense for 2013 is \$ 587,036.

Depreciation of Capital Assets is computed using the straight-line method over the following estimated useful lives of the assets.

| | <u>Asset Class</u> | <u>Estimated Useful Life</u> |
|------------------------------|--------------------|------------------------------|
| Buildings | | 40 Years |
| Building & land improvements | | 20 – 40 Years |
| Vehicles | | 5 Years |
| Equipment | | 3 – 10 Years |

Compensated Absences

Compensated absences are those absences for which employees will be paid, such as vacation and sick leave. A liability for compensated absences that is attributable to services already rendered and that are not contingent on a specific event that is outside the control of the District and its employees, is accrued as employees earn the rights to the benefits.

Compensated absences that relate to future services or that are contingent on a specific event that is outside the control of the District and its employees are accounted for in the period in which such services are rendered or in which such events take place.

Use of Estimates

The preparation of the financial statements in conformity with Generally Accepted Accounting Principles in the United States requires management to make estimates and assumptions that affect certain 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.

Operating Revenues and Expenses

Operating revenues and expenses generally result from providing and producing goods and/or services in connection with sanitation services. Operating expenses include services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

**NORTHERN MADISON COUNTY SANITATION DISTRICT
NOTES TO FINANCIAL STATEMENTS - CONTINUED
JUNE 30, 2013**

NOTE 2 – UTILITY REVENUE BOND CASH MANAGEMENT AND CASH RESTRICTIONS

The District loan covenants requires certain funds be maintained in order to meet the debt service requirements and to provide for unusual repairs and maintenance to the present system.

Operation and Maintenance Fund: An Operation and Maintenance Fund must be maintained, from which all costs of operating, maintaining, and insuring District's project shall be paid.

NOTE 3 – DEPOSITS WITH FINANCIAL INSTITUTIONS

Cash and Investments, Both Restricted and Unrestricted:

At June 30, 2013, the carrying amount of the District's cash accounts (including certificates of deposit) both restricted and unrestricted was \$789,942 and the bank balance was \$793,503. All of the bank balance was fully collateralized by FDIC insurance, or by securities pledged at market.

Interest Rate Risk: Is the risk that changes in interest rates will adversely affect the fair value of an investment. The District does not have a formal investment policy that limits investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates. Management believes the District is not exposed to significant interest rate risk on investments.

Credit Risk: Is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. The District does not have a policy regarding the types of authorized investments that would ensure preservation of the assets, only certificates of deposit and money market accounts are permitted. Management believes the District is not exposed to a significant credit risk.

Custodial Credit Risk: Is the risk that the District's deposits may not be returned in the event of bank failure. The District maintains its deposits with a financial institution insured by Federal Deposit Insurance Corporation (FDIC) or by securities pledged at market. As of June 30, 2013, all of the bank balances were fully collateralized by FDIC insurance, or by securities pledged at market.

Concentration of Credit Risk: Is the risk of loss attributed to the magnitude of investment in a single issuer. Management does not believe the District is exposed to a significant concentration of credit risk.

Cash, both restricted and unrestricted, at June 30, 2013, consisted of the following:

| <u>Account</u> | <u>Interest Bearing</u> | <u>Restricted</u> | <u>June 30, 2013 Balance</u> |
|----------------------------|-----------------------------|-------------------|----------------------------------|
| Operating | | | \$ 68,421 |
| Savings | √ | √ | 307,970 |
| Savings - Tap on Fees | √ | √ | 7,275 |
| Savings - Development Fees | √ | √ | 6,764 |
| Construction Account RD | | √ | 240 |
| KIA Loan | √ | √ | 68,231 |
| KIA Boones Trace | √ | √ | 48,846 |
| CD - North Project | √ | √ | 157,623 |
| CD - Terrill Project | √ | √ | 105,082 |
| CD - Clays Ferry | √ | √ | 19,490 |
| Total | | | <u>\$ 789,942</u> |

**NORTHERN MADISON COUNTY SANITATION DISTRICT
NOTES TO FINANCIAL STATEMENTS - CONTINUED
JUNE 30, 2013**

NOTE 4 – ACCOUNTS RECEIVABLE AND ALLOWANCE FOR DOUBTFUL ACCOUNTS

Accounts receivable are stated at the amount management expects to collect from outstanding balances. Management provides for probable uncollectable amounts through a provision for bad debt expense and an adjustment to a valuation allowance based on its assessment for the current status of individual accounts. Balances that are still outstanding after management has used reasonable collection efforts are written off through a charge to the valuation allowance and credit to receivable. At June 30, 2013, accounts receivable was \$464,650 and the allowance for doubtful accounts was \$11,739. Based on the consistency of the amounts with prior years and no significant change in the customer base or local economic conditions, in my opinion, the allowance at year end appears adequate for any potential losses.

NOTE 5 – CHANGES IN CAPITAL ASSETS

The following is a summary of changes in capital assets for the year ended June 30, 2013:

| Changes in Capital Assets | | | | |
|--|----------------------|------------|-------------|----------------------|
| | Balance 6/30/2012 | Additions | Retirements | Balance 6/30/2013 |
| Capital Assets | | | | |
| Land | \$ - | \$ 45,000 | \$ - | \$ 45,000 |
| Collection systems and equipment | 21,865,963 | 21,107 | - | 21,887,070 |
| Vehicles | 86,752 | - | - | 86,752 |
| Construction in progress | 35,867 | 90,821 | 19,456 | 107,232 |
| Total | \$ 21,988,582 | \$ 156,928 | \$ 19,456 | \$ 22,126,054 |
| Changes in Accumulated Depreciation | | | | |
| | Balance 6/30/2012 | Additions | Retirements | Balance 6/30/2013 |
| Accumulated Depreciation | | | | |
| Collection systems and equipment | \$ 2,370,509 | \$ 587,036 | \$ - | \$ 2,957,545 |
| Vehicles | 86,753 | - | - | 86,753 |
| Construction in progress | - | - | - | - |
| Total | \$ 2,457,262 | \$ 587,036 | \$ - | \$ 3,044,298 |
| Capital Assets, Net | | | | \$ 19,081,756 |

NOTE 6 – COMPENSATED ABENCES

It is the policy of the District to permit employees to accumulate a limited amount of earned but unused leave benefits which will be paid to employees upon separation from service. Unpaid compensated absences are recorded as a liability when the benefits are earned in the proprietary fund financial statements. Upon termination, up to 240 hours of accumulated vacation leave and 960 hours accumulated sick leave will be paid to the employee.

As of June 30, 2013, the current liability for accrued compensated absences totaled \$3,831.

Non-current liabilities at June 30, 2013 consisted of the following:

| | <u>6/30/12</u> | <u>Additions</u> | <u>Deletions</u> | <u>6/30/13</u> |
|------------------------------|----------------|------------------|------------------|----------------|
| Accrued Compensated Absences | \$30,192 | \$4,287 | \$0 | \$34,479 |

**NORTHERN MADISON COUNTY SANITATION DISTRICT
NOTES TO FINANCIAL STATEMENTS - CONTINUED
JUNE 30, 2013**

NOTE 7 – LONG-TERM NOTES PAYABLE – KENTUCKY INFRASTRUCTURE AUTHORITY

Terrill Sewer Project – Note payable due in semi-annual payments of \$8,513 at one percent interest plus a one-tenth percent service fee.

Regional Plant and US 25 Improvements – Note payable due in semi-annual payments of \$224,056 at one percent interest plus a one-tenth percent service fee.

Clays Ferry Project – Note payable due in semi-annual payments of \$7,424 at two percent interest plus a one-tenth percent service fee.

Annual debt service requirements are as follows:

| <u>Year Ending June 30,</u> | <u>Principal</u> | <u>Interest</u> | <u>Total</u> |
|---------------------------------|---------------------|-------------------|---------------------|
| 2014 | \$ 406,521 | \$ 75,465 | \$ 481,986 |
| 2015 | 408,685 | 71,301 | 479,986 |
| 2016 | 409,417 | 67,105 | 476,522 |
| 2017 | 412,881 | 62,909 | 475,790 |
| 2018 | 421,438 | 58,581 | 480,019 |
| 2019-2023 | 2,173,237 | 226,867 | 2,400,104 |
| 2024-2028 | 2,307,765 | 112,445 | 2,420,210 |
| 2029-2030 | 899,793 | 11,821 | 911,614 |
| Totals | <u>\$ 7,439,737</u> | <u>\$ 686,494</u> | <u>\$ 8,126,231</u> |

NOTE 8 – RETIREMENT PLAN

The District participates in a retirement plan through Kentucky Deferred Compensation Program. If an employee chooses to participate in this program, the District will match the employees' contribution. The District will contribute up to 6%.

The retirement expense for the years ended June 30, 2013, 2012, and 2011 respectively were:

| | <u>2013</u> | <u>2012</u> | <u>2011</u> |
|--------------------------|-------------|-------------|-------------|
| Employer's contributions | \$ 3,071 | \$ 3,188 | \$ 3,245 |
| Employee contribution | \$ 4,550 | \$ 3,661 | \$ 4,200 |

NOTE 9 – RECLASSIFICATION AND RESTATEMENTS

Certain reclassifications have been made to the June 30, 2013 information.

NOTE 10 – COMMITMENTS AND CONTINGENCIES

The District receives funding from Federal, State and Local government agencies. These funds are to be used for designated purposes only. For government agency grants, if based on the grantor's review, the funds are considered not to have been used properly for the intended purpose, the grantors may request a refund of monies advanced, or refuse to reimburse the District for its disbursements. The amount of such future refunds and unreimbursed disbursements, if any, is not expected to be significant. Continuation of the District's grant programs is predicated upon the grantor's satisfaction that the funds provided are being spent as intended and the grantor's intent to continue their program.

**NORTHERN MADISON COUNTY SANITATION DISTRICT
NOTES TO FINANCIAL STATEMENTS - CONTINUED
JUNE 30, 2013**

NOTE 11 – RISK MANAGEMENT

The District is exposed to various risks of loss related to torts; theft of damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. The District purchases commercial insurance for liability, property, and crime damage and for risks related to injuries to employees. Amounts of settlements have not exceeded insurance coverage in the past three years. There have been no significant reductions in insurance coverage.

NOTE 12 – EVALUATION OF SUBSEQUENT EVENTS

The District has evaluated subsequent events through December 10, 2013, which is the date the financial statements were available to be issued.

SAMMY K. LEE, P.S.C.
Certified Public Accountant

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

To the Chairman and Board of Directors
Northern Madison County Sanitation District
Richmond, Kentucky 40475

I have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the business-type activities of Northern Madison County Sanitation District, as of and for the year ended June 30, 2013, and the related notes to the financial statements, which collectively comprise the District's basic financial statements and have issued my report thereon dated December 10, 2013.

Internal Control Over Financial Reporting

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

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect and correct misstatements on a timely basis. *A material weakness* is a deficiency, or 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.

My consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies, and therefore, material weaknesses or significant deficiencies may exist that were not identified. Given these limitations, during my audit I did not identify any deficiencies in internal control that I consider to be material weaknesses. However, material weaknesses may exist that have not been identified. I did identify a certain deficiency in internal control, described in the accompanying Schedule of Findings and Responses that I consider to be a significant deficiency as item 2013-01.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the District's financial statements are free from material misstatement, I 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 my audit, and accordingly, I do not express such an opinion. The results of my tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Response to Findings

The District's response to the findings identified in my audit as described in the accompanying Schedule of Findings and Responses. The District's response was not subjected to the auditing procedures applied in the audit of the financial statements, and accordingly, I express no opinion on it.

Purpose of this Report

The purpose of this report is solely to describe the scope of my testing of internal control and compliance and the results of testing, and not to provide an opinion on the effectiveness of the District'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 District's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Sammy K. Lee, P.S.C.

Berea, Kentucky
December 10, 2013

**NORTHERN MADISON COUNTY SANITATION DISTRICT
SCHEDULE OF FINDINGS AND RESPONSES
FOR THE YEAR ENDED JUNE 30, 2013**

Section I - Summary of Auditor's Results

1. The auditor's report expresses an unqualified opinion on the basic financial statements of Northern Madison County Sanitation District
2. The results of my audit procedures disclosed one significant deficiency in internal control over financial reporting for the fiscal year ended June 30, 2013. The significant deficiency identified is not deemed to be material weaknesses.
3. The results of my audit procedures disclosed no instances of noncompliance.

Section II - Financial Statement Findings

Finding 2013-01 Internal Control Over Financial Reporting

Criteria:

A key component of internal control is to ensure the responsibility of management to establish and maintain internal controls in the financial reporting system and for the fair presentation of the financial position, results of operations, cash flows, and disclosures in the financial statements, in conformity with U.S. Generally Accepted Accounting Principles (GAAP).

Condition:

While conducting my audit procedures to gain an understanding of internal controls over financial reporting, I noted the absence of internal control in the following areas:

- The District's internal control system does not reliably and consistently produce adjustments to bring the accounting records into alignment with generally accepted accounting principles in the United States of America.
- The District does not have a system of internal controls that would enable management to conclude that the financial statements and the related disclosures are complete and presented in accordance with generally accepted accounting principles in the United States of America.

Cause:

Due to the small number of administrative and clerical employees at the District, there is an inherent limitation in its ability to prepare financial statements in accordance with Generally Accepted Accounting Principles of the United States.

Effect:

The lack of internal controls increases the risk that an error, either intentional or unintentional, will go undetected and the financial statements will contain material misstatements

**NORTHERN MADISON COUNTY SANITATION DISTRICT
SCHEDULE OF FINDINGS AND RESPONSES - CONTINUED
FOR THE YEAR ENDED JUNE 30, 2013**

Recommendation:

Specific recommendations are:

1. Management should consult with their current fee accountant for financial statement and notes disclosure preparation services.

Views of Responsible Officials:

Management concurs with recommendations. The District will strive to implement controls and procedures to correct the deficiency as noted in the finding. We understand these limitations, and we are responsible for any outcomes.