

**PADUCAH WATER WORKS**

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**FINANCIAL STATEMENTS  
YEARS ENDED JUNE 30, 2014 AND 2013**

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## Independent Auditor's Report

The Board of Directors  
Paducah Water Works  
Paducah, Kentucky

We have audited the accompanying financial statements of Paducah Water Works, a component unit of the City of Paducah, Kentucky, as of and for the years ended June 30, 2014 and 2013, and the related notes to the financial statements, which collectively comprise Paducah Water Works' 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 *Governmental 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 upon 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 respective financial position of Paducah Water Works, as of June 30, 2014 and 2013, and the respective changes in financial position and cash flows thereof for the years then ended in accordance with accounting principles generally accepted in the United States of America.

## Other Matters

### *Required Supplementary Information*

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 3 through 7 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the 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. 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.

## Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated September 24, 2014, on our consideration of Paducah Water Works' internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering Paducah Water Works' internal control over financial reporting and compliance.

Handwritten signature in black ink that reads "William F. Zengler". The signature is written in a cursive style.

September 24, 2014

**REQUIRED SUPPLEMENTARY INFORMATION**

## MANAGEMENT'S DISCUSSION AND ANALYSIS

Management's discussion and analysis of Paducah Water Works' financial performance provides an overview of the financial activities for the fiscal year ended June 30, 2014. Please read it in conjunction with the financial statements, which begin on page 8.

### **Financial Highlights**

- PWW's net position increased by \$1.914 million (4.0%) as a result of this year's operations.
- Net income before capital contributions decreased by \$851.9 thousand to \$1.484 million.
- Operating revenues decreased by \$284.6 thousand (2.7%) to \$10.388 million, due mainly to a decrease in water sales revenue of approximately \$268.5 thousand.
- Operating expenses excluding depreciation increased by \$466.8 thousand (7.1%) to \$7.072 million.

### **Using This Annual Report**

This annual report consists of a series of financial statements: The Statements of Net Position, The Statements of Revenues, Expenses and Changes in Net Position and The Statements of Cash Flows. These statements provide information about the activities of PWW and present a long-term view of the finances.

#### **The Statements of Net Position**

The Statements of Net Position includes all of PWW's assets and liabilities and provides information about the nature and amounts of investments in resources (assets) and the obligations to creditors (liabilities). The difference between assets and liabilities is reported as net position. Over time increases or decreases in net position may serve as a useful indicator of whether the financial position of PWW is improving or deteriorating.

#### **The Statements of Revenues, Expenses and Changes in Net Position**

The Statements of Revenues, Expenses and Changes in Net Position identifies the revenues generated, expenses incurred and net position change during the period reported. This statement measures the success of PWW's operations over the reporting period and can be used to determine whether PWW has successfully recovered all its costs through its water rates and other charges.

#### **The Statements of Cash Flows**

The Statements of Cash Flows provides information relating to PWW's cash receipts and cash disbursements during the fiscal year. The statement reports net changes in cash resulting from operations, investing and financing activities, and helps the user assess where cash came from, what cash was used for, and what changes occurred in cash balances during the reporting period.

## Financial Analysis

### Net Position

Net position may serve over time as a useful indicator of PWW's financial position. Net position was \$49.37 million at June 30, 2014 compared to \$47.45 at June 30, 2013, an increase of \$1.91 million or 4.0%.

#### Condensed Statements of Net Position (amounts expressed in thousands)

	As of June 30, 2014	2013	Increase (Decrease)	Percent Change
Current and other assets	\$ 9,115	\$ 9,088	\$ 27	0%
Capital assets, net	48,544	46,829	1,715	4%
Total assets	<u>57,659</u>	<u>55,917</u>	<u>1,742</u>	3%
Current liabilities	2,344	2,175	169	8%
Long-term liabilities	<u>5,948</u>	<u>6,289</u>	<u>(341)</u>	-5%
Total liabilities	<u>8,292</u>	<u>8,464</u>	<u>(172)</u>	-2%
<u>Net assets:</u>				
Invested in capital assets	42,254	40,202	2,052	5%
Restricted	0	0	0	0%
Unrestricted	<u>7,113</u>	<u>7,251</u>	<u>(138)</u>	-2%
Total net position	<u>\$ 49,367</u>	<u>\$ 47,453</u>	<u>\$ 1,914</u>	4%

By far, the largest portion of PWW's net position reflects its investment in capital assets (i.e., utility plant), less any related debt used to acquire those assets that is still outstanding. Although PWW's investment in its capital assets is reported net of related debt, it should be noted that the resources to repay this debt must be provided from other sources, since the capital assets themselves are not intended to be used to liquidate these liabilities.

The remaining balance of net position represents unrestricted net position and may be used to meet PWW's ongoing obligations to creditors.

The increase in net position during the current fiscal year indicates an improved financial position.

### Change in Net Position

While the statements of net position show the make-up of PWW's assets, liabilities and net position at year-end, the statements of revenues, expenses and changes in net position provide information on the source of the change during the year. The two sources of the increase in net position of \$1.914 million were income before capital contributions (formerly net revenue) of \$1.484 million and capital contributions of \$430 thousand.

## **Condensed Statements of Revenues, Expenses and Changes in Net Position**

(amounts expressed in thousands)

	Years ended June 30, 2014	2013	Increase (Decrease)	Percent Change
Operating revenues	\$ 10,388	\$ 10,673	\$ (285)	-3%
Nonoperating revenues	16	17	(1)	-6%
Total revenues	<u>10,404</u>	<u>10,690</u>	<u>(286)</u>	-3%
Operating expenses	7,072	6,606	466	7%
Nonoperating expenses	1,848	1,748	100	6%
Total expenses	<u>8,920</u>	<u>8,354</u>	<u>566</u>	7%
Income before capital contributions (formerly net revenue)	1,484	2,336	(852)	-36%
Contributions	<u>430</u>	<u>812</u>	<u>(382)</u>	-47%
Increase in net position	1,914	3,148	(1,234)	-39%
Beginning net position	47,453	42,665	4,788	11%
Hendron merger	-	1,640	(1,640)	
Ending net position	<u>\$ 49,367</u>	<u>\$ 47,453</u>	<u>\$ 1,914</u>	4%

Income before capital contributions decreased by \$852 thousand from the previous year mainly due to decreased water sales revenue of \$269 thousand and an increase in operating expenses of \$466 thousand. The increase in operating expenses was due mainly to increased power costs, increased customer service costs and increased administrative salary and benefit costs.

### **Capital Assets and Long-Term Debt**

PWW's net investment in plant, lines, and other facilities increased by \$1.715 million in FY 2014. Major additions included a main replacement on Old Mayfield Road (\$594 thousand), a main extension on Madison and Monroe streets (\$442 thousand), the final phase of a main extension on Blandville Road (\$288 thousand), and an upgrade to the Sedimentation Basin (\$209 thousand).

During FY 2014, long-term debt decreased by \$341 thousand due to principal payments that were made on notes payable. Total long-term debt as of June 30, 2014 is \$5.948 million. This consists entirely of KIA debt that was assumed in order to connect the Paducah system with the Reidland system as well as improvements to the Reidland area system.

### **Budgetary Controls**

PWW operates its general activities in accordance with a budget adopted by its Board. As demonstrated by the statements included in the financial section of this report, PWW continues to meet its responsibility for sound financial management.

Total operating revenues for the period were \$10.388 million compared to a budget of \$10.666 million. Total operating expense was over the budgeted amount for the fiscal year by 3.0%. Actual operating expense was \$7.072 million compared to a budget of \$6.863 million. Net Revenue before capital contributions ended \$469 thousand under budget for the period.

### **Currently Known Facts, Decisions or Conditions**

This section discusses currently known facts, decisions or conditions as of the date of the auditor's report that are expected to have a significant effect on PWW's financial position (net position) or results of operations (revenues, expenses, and other changes in net position).

PWW has a significant percentage of water mains that are aging. Over the next twenty-five years, these water mains will need to begin to be replaced at what will be a significant expense to the rate payers. Management estimates that nearly \$100 million will need to be spent over the next fifty to sixty years replacing aging water mains. In FY2010, a Capital Replacement and Expansion fee was instituted for all customers based on meter size that will add additional revenue of approximately \$2 million per year. This fee partnered with other operating revenue will begin to allow Paducah Water Works to address this issue.

### **Requests for Additional Information**

This financial report is designed to provide a general overview of PWW's finances for all those with an interest in PWW's finances. Questions concerning any of the information provided in this report or requests for additional information should be addressed to:

Controller  
Paducah Water Works  
P.O. Box 2377  
Paducah, Ky 42002-2377

**Statement of Income and Expense**  
**For the twelve months ended June 30, 2014**  
(amounts expressed in thousands)

	Actual	Budget	Increase (Decrease)	Percent Difference
<b>Operating revenue</b>	\$ 10,388	\$ 10,666	\$ (278)	-3%
<b>Operating expenses</b>				
Pumping & purification	2,466	2,322	144	6%
Distribution & engineering	1,874	1,873	1	0%
Office & administrative	1,926	1,821	105	6%
Other	<u>807</u>	<u>848</u>	<u>(41)</u>	-5%
Total expenses	<u>7,073</u>	<u>6,864</u>	<u>209</u>	3%
<b>Net operating income</b>	<u>3,315</u>	<u>3,802</u>	<u>(487)</u>	-13%
<b>Other income (expenses)</b>				
Interest income	16	16	-	0%
Other	64	0	64	0%
Depreciation	(1,829)	(1,800)	(29)	2%
Interest on funded debt	<u>(82)</u>	<u>(65)</u>	<u>(17)</u>	26%
	<u>(1,831)</u>	<u>(1,849)</u>	<u>18</u>	-1%
<b>Net Revenue</b>	<u>\$ 1,484</u>	<u>\$ 1,953</u>	<u>\$ (469)</u>	-24%

**BASIC FINANCIAL STATEMENTS**

**PADUCAH WATER WORKS**  
**STATEMENTS OF NET POSITION**  
**JUNE 30**

**ASSETS**

<b>Current Assets:</b>	<b>2014</b>	<b>2013</b>
Cash and cash equivalents	\$ 1,254,787	\$ 1,478,634
Accounts receivable	591,627	513,212
Material and supplies inventory	630,723	770,605
Accrued unbilled revenue	1,099,201	1,030,255
Other current assets	977,486	916,063
<b>Total current assets</b>	<b>4,553,824</b>	<b>4,708,769</b>
<b>Capital Assets:</b>		
Utility plant in service	80,793,963	78,230,189
Construction in progress	2,685,360	2,093,776
<b>Totals</b>	<b>83,479,323</b>	<b>80,323,965</b>
Less accumulated depreciation	34,935,540	33,495,229
<b>Total capital assets</b>	<b>48,543,783</b>	<b>46,828,736</b>
<b>Other Assets:</b>		
KIA replacement reserve	56,250	37,500
Cash, designated	3,163,760	3,007,803
Certificates of deposit, designated	1,341,651	1,334,448
<b>Total other assets</b>	<b>4,561,661</b>	<b>4,379,751</b>
<b>Total assets</b>	<b>57,659,268</b>	<b>55,917,256</b>

**LIABILITIES**

<b>Current Liabilities:</b>		
Notes payable, KIA	341,179	337,793
Accounts payable, trade	747,382	758,698
Other accrued expenses and current liabilities	1,255,287	1,078,585
<b>Total current liabilities</b>	<b>2,343,848</b>	<b>2,175,076</b>
<b>Long-Term Debt:</b>		
Notes payable, KIA	5,948,187	6,289,366
<b>Total long-term debt</b>	<b>5,948,187</b>	<b>6,289,366</b>
<b>Total liabilities</b>	<b>8,292,035</b>	<b>8,464,442</b>

**NET POSITION**

Net invested in capital assets	42,254,417	40,201,577
Unrestricted	7,112,816	7,251,237
<b>TOTAL NET POSITION</b>	<b>\$49,367,233</b>	<b>\$47,452,814</b>

See notes to financial statements.

**PADUCAH WATER WORKS**  
**STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN NET POSITION**  
**YEARS ENDED JUNE 30**

	<u>2014</u>	<u>2013</u>
<b>Operating Revenues:</b>		
Metered water sales	\$ 7,396,452	\$ 7,664,985
Fire protection fees	128,897	127,727
Municipal water sales	39,578	52,937
Collection fees and late payment charges	339,825	340,952
Capital replacement fee	2,204,735	2,259,138
Miscellaneous	278,479	226,834
	<u>10,387,966</u>	<u>10,672,573</u>
<b>Operating Expenses:</b>		
Pumping and purification	2,465,513	2,276,932
Transmission and distribution	1,874,320	1,916,729
Office and administrative	1,925,572	1,636,364
Other	806,937	775,483
	<u>7,072,342</u>	<u>6,605,508</u>
Total operating expenses	<u>7,072,342</u>	<u>6,605,508</u>
Operating income	<u>3,315,624</u>	<u>4,067,065</u>
<b>Nonoperating Revenues (Expenses):</b>		
Interest income	15,849	17,221
Amortization	-	(2,154)
Other interest	(82,160)	(91,837)
Depreciation	(1,828,770)	(1,727,924)
Gain (loss) on disposal of capital asset	60,017	39,405
Other	3,759	34,404
	<u>(1,831,305)</u>	<u>(1,730,885)</u>
Net nonoperating revenues (expenses)	<u>(1,831,305)</u>	<u>(1,730,885)</u>
Income before capital contributions	<u>1,484,319</u>	<u>2,336,180</u>
<b>Capital Contributions:</b>		
Connection fees	202,700	179,099
Donated surplus	64,400	486,699
Line grant	-	145,847
Saferoom grant	163,000	-
	<u>430,100</u>	<u>811,645</u>
Total capital contributions	<u>430,100</u>	<u>811,645</u>
Increase in net position	1,914,419	3,147,825
Net position, beginning of year	47,452,814	42,665,176
Net position of merged Hendron Water District Operation	<u>-</u>	<u>1,639,813</u>
<b>NET POSITION, END OF YEAR</b>	<u><u>\$49,367,233</u></u>	<u><u>\$47,452,814</u></u>

See notes to financial statements.

**PADUCAH WATER WORKS**  
**STATEMENTS OF CASH FLOWS**  
**YEARS ENDED JUNE 30**

	<u>2014</u>	<u>2013</u>
<b>Cash Flows from Operating Activities:</b>		
Receipts from customers	\$ 10,240,605	\$ 10,701,089
Payments to suppliers	(4,003,134)	(4,213,830)
Payments to employees	(2,844,112)	(2,676,689)
Net cash provided by operating activities	<u>3,393,359</u>	<u>3,810,570</u>
<b>Cash Flows from Capital and Related Financing Activities:</b>		
Capital contributions	202,700	179,099
Acquisitions of capital assets	(3,532,376)	(3,670,266)
Proceeds from sale of assets	279,737	131,432
Principal paid on capital debt	(337,793)	(418,422)
Interest paid on capital debt	(82,160)	(91,837)
Net cash used by capital and related financing activities	<u>(3,469,892)</u>	<u>(3,869,994)</u>
<b>Cash Flows from Investing Activities:</b>		
Purchase of investments	(7,203)	(7,339)
Interest on investments	15,846	17,253
Net cash provided by investing activities	<u>8,643</u>	<u>9,914</u>
Net decrease in cash and cash equivalents	(67,890)	(49,510)
Cash and cash equivalents, beginning of year	4,486,437	4,478,405
Cash transferred from merger with Hendron Water District Operations	-	57,542
<b>CASH AND CASH EQUIVALENTS, END OF YEAR</b>	<u><u>\$ 4,418,547</u></u>	<u><u>\$ 4,486,437</u></u>
Reconciliation of operating income to net cash provided by operating activities:		
Operating income	\$ 3,315,624	\$ 4,067,065
Adjustments to reconcile operating income to net cash provided by operating activities:		
Changes in assets and liabilities:		
(Increase) decrease in accounts receivable	(78,415)	(6,129)
(Increase) decrease in accrued unbilled revenue	(68,946)	34,645
(Increase) decrease in inventory	139,882	(242,253)
(Increase) decrease in other current assets	(61,423)	(133,298)
Increase (decrease) in accounts payable	(11,316)	36,284
Increase (decrease) in accrued payroll	5,933	14,755
Increase (decrease) in other current liabilities	152,020	39,501
<b>NET CASH PROVIDED BY OPERATING ACTIVITIES</b>	<u><u>\$ 3,393,359</u></u>	<u><u>\$ 3,810,570</u></u>

See notes to financial statements.

**PADUCAH WATER WORKS**  
**NOTES TO FINANCIAL STATEMENTS**  
**YEARS ENDED JUNE 30, 2014 AND 2013**

**Note 1 - Summary of Significant Accounting Policies:**

**Reporting Entity**

Paducah Water Works is a municipal utility, purchased by the City of Paducah in 1930. The area served is virtually all of McCracken County, including a separate water district, as well as a small portion of Marshall County and Graves County. Effective July 18, 2012, the Hendron Water District merged with Paducah Water Works. Paducah Water Works assumed control of Hendron Water District on August 1, 2012.

Paducah Water Works serves 26,600 customers with 14,600 of these in the City of Paducah and the remainder in the areas previously described.

**Basis of Accounting**

Paducah Water Works' financial statements are prepared in accordance with generally accepted accounting principles (GAAP) as applied to governmental units. This requires the accrual basis of accounting for proprietary entities. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles.

Paducah Water Works is a single fund government and a component unit of the City of Paducah with the Board of Directors appointed by the Mayor. Paducah Water Works has no oversight responsibility for any other entity since control or dependence is determined on the basis of budget adoption, taxing authority, funding, and appointment of the respective governing board.

**Basic Financial Statements**

Paducah Water Works' basic financial statements include the Statement of Net Position; the Statement of Revenues, Expenses, and Changes in Net Position; and the Statement of Cash Flows. Paducah Water Works has only one fund that uses a set of self-balancing accounts comprised of its assets, liabilities, net position, revenues, and expenses.

The statements are prepared on a full accrual, economic resource basis, which recognizes all long-term assets and receivables as well as long-term debt and obligations.

**Cash and Cash Equivalents**

For purposes of reporting cash flows, Paducah Water Works does not consider certificates of deposit, regardless of maturity, as cash equivalents.

**Materials and Supplies Inventory**

Materials and supplies inventory is valued at weighted average cost.

**Depreciation**

Depreciation is computed on the straight-line basis over the estimated useful lives of various classes of assets. It is Paducah Water Works' policy to include amortization expense on assets acquired under capital leases with depreciation expense on owned assets.

Distribution mains, service lines, standpipes, and tanks	60 years
Booster station, raw water intake, and treatment plant equipment	40 years
Meters	25 years
Hydrants	40 years
Buildings	40-60 years
Other equipment	5-15 years

(Continued)

**PADUCAH WATER WORKS**  
**NOTES TO FINANCIAL STATEMENTS**  
**YEARS ENDED JUNE 30, 2014 AND 2013**

**Note 1 - Summary of Significant Accounting Policies:**

**Net Position**

Net assets are displayed in three components:

- a. Net invested in capital assets - Consists of capital assets including restricted capital assets, net of accumulated depreciation, and unpaid debt financing.
- b. Restricted net position - Consists of net position with constraints placed on the use either by (1) external groups such as creditors, grantors, contributors, or laws or regulations of other governments; or (2) law through constitutional provisions or enabling legislation.
- c. Unrestricted net position - All other net position that does not meet the definition of "restricted" or "invested in capital assets."

**Capital Contributions**

Capital contributions are derived from three main sources: 1) customers, in the form of tap fees; 2) developers, when they construct and pay for water lines and then donate these additions to Paducah Water Works; and 3) other governments, in the form of grant contributions for capital assets. Developer contributions are recorded at the developer's cost and are depreciated over their estimated useful lives using the straight-line method.

**Employee Compensated Absences**

Employees of Paducah Water Works are entitled to paid vacations and sick days depending on job classification, length of service, and other factors and, accordingly, Paducah Water Works has recorded the accrual in the accompanying financial statements.

**Operating Revenues and Expenses**

Operating revenues consist primarily of charges to customers for the sale of water. Operating expenses consist of the cost of providing water, including administrative expenses. All other revenues and expenses are classified as non-operating.

Accrued unbilled revenue represents the portion of water service provided that was unbilled as of the end of the year.

**Bad Debts**

The Company uses the direct write-off method in recognizing bad debts expense. Generally accepted accounting principles require that the allowance method be used to reflect bad debts. However, the effect of the use of the direct write-off method is not materially different from the results that would have been obtained had the allowance method been followed. The Company expensed \$44,685 and \$24,905 in bad debts during the years ended June 30, 2014 and 2013, respectively.

**Use of Estimates**

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that effect certain amounts and disclosures. Accordingly, actual results could differ from those estimates.

(Continued)

**PADUCAH WATER WORKS**  
**NOTES TO FINANCIAL STATEMENTS**  
**YEARS ENDED JUNE 30, 2014 AND 2013**

**Note 1 - Summary of Significant Accounting Policies:**

**Subsequent Events**

Subsequent events were evaluated through September 24, 2014, which is the date the financial statements were available to be issued.

**Note 2 - Deposits:**

The investment policies of Paducah Water Works are governed by the State statute. In general, this requires that all deposits and investments, not covered by FDIC insurance, are to be collateralized. For the years ended June 30, 2014 and 2013, Paducah Water Works' financial institution balances were fully collateralized as required by State statute.

Deposits consist of savings and checking accounts and certificates of deposit that mature in twelve months or less. The financial institution balances of Paducah Water Works' deposits were \$5,868,334 for the year ended June 30, 2014. The book balance was \$5,761,300. Of the various financial institution balances at June 30, 2014, \$538,791 was insured by federal depository insurance, and the remaining balance was subject to custodial credit risk. Custodial credit risk is the risk that in the event of a bank failure, the Utility's deposits may not be returned to it. The remaining balance of \$5,329,543 was uninsured and collateralized with securities held by the pledging bank's agent not in Paducah Water Works' name.

**Note 3 - Reserve Fund:**

As required by the Note Agreement with the Kentucky Infrastructure Authority, Paducah Water Works is required on December 1 each year beginning December 1, 2011 to transfer \$18,750 into replacement reserve until the account balance reaches \$187,500. At June 30, 2014, \$56,250 had been transferred into a replacement reserve account.

**Note 4 - Capital Assets:**

A summary of capital asset activity for the year ended June 30, 2014, is as follows:

	<u>Balance</u> <u>June 30, 2013</u>	<u>Increases</u>	<u>Decreases</u>	<u>Balance</u> <u>June 30, 2014</u>
Capital assets	\$ 80,323,965	\$ 3,759,775	\$ (604,417)	\$ 83,479,323
Accumulated depreciation	<u>(33,495,229)</u>	<u>(1,828,770)</u>	<u>388,459</u>	<u>(34,935,540)</u>
 CAPITAL ASSETS, NET	 <u>\$ 46,828,736</u>	 <u>\$ 1,931,005</u>	 <u>\$ (215,958)</u>	 <u>\$ 48,543,783</u>

**Note 5 - Notes Payable, KIA:**

Notes payable, KIA represents financing from the Kentucky Infrastructure Authority. Interest rate is 1.00% with a .25% annual service fee.

(Continued)

**PADUCAH WATER WORKS**  
**NOTES TO FINANCIAL STATEMENTS**  
**YEARS ENDED JUNE 30, 2014 AND 2013**

**Note 5 - Notes Payable, KIA:**

The annual requirements to amortize the outstanding debt as of June 30, 2014, are as follows:

<b>Year Ending June 30</b>	<b>Principal</b>	<b>Interest</b>	<b>.25% Service Fee</b>	<b>R &amp; M Reserve</b>	<b>Total</b>
2015	\$ 341,179	\$ 62,043	\$ 15,511	\$ 18,750	\$ 437,483
2016	344,600	58,623	14,656	18,750	436,629
2017	348,054	55,168	13,792	18,750	435,764
2018	351,543	51,679	12,920	18,750	434,892
2019	355,068	48,155	12,039	18,750	434,012
2020-2024	1,829,450	186,660	46,665	37,500	2,100,275
2025-2029	1,923,008	93,102	23,275	-	2,039,385
2030-2031	796,464	9,980	2,495	-	808,939
<b>TOTALS</b>	<b><u>\$6,289,366</u></b>	<b><u>\$ 565,410</u></b>	<b><u>\$141,353</u></b>	<b><u>\$131,250</u></b>	<b><u>\$7,127,379</u></b>

**Note 6 - Change in Long-Term Liability:**

	<b>Balance June 30, 2013</b>	<b>Increases</b>	<b>Decreases</b>	<b>Balance June 30, 2014</b>
Notes payable, KIA Reidland Interchange	\$6,627,159	\$ -	\$ 337,793	\$6,289,366
<b>TOTALS</b>	<b><u>\$6,627,159</u></b>	<b><u>\$ -</u></b>	<b><u>\$ 337,793</u></b>	<b><u>\$6,289,366</u></b>

**Note 7 - Employee Benefits:**

**Pension Plan**

*Plan Description.* Paducah Water Works contributes to the County Employees Retirement System (CERS), a cost-sharing multiple-employer defined benefit pension plan administered by the Kentucky Retirement Systems. CERS provides retirement, disability benefits, and death benefits to plan members. Retirement benefits may be extended to beneficiaries of plan members under certain circumstances. Cost of living (COLA) adjustments are provided at the discretion of the State legislature. Under the provisions of Kentucky Revised Section 61.645, the Board of Trustees of Kentucky Retirement Systems administers the CERS. The Kentucky Retirement Systems issues a publicly available financial report that includes writing to Kentucky Retirement Systems, Perimeter Park West, 1260 Louisville Road, Frankfort, KY 40601-6124 or by calling (502) 564-4646.

*Funding Policy.* Plan members hired before January 2009 are required to contribute 5% of their annual covered salary. Plan members hired after January 2009 are required to contribute 6% of their annual covered salary, and Paducah Water Works is required to contribute at an actuarially determined rate. The current rate is 18.89% of annual covered payroll. The contribution requirements of plan members and Paducah Water Works are established and may be amended by the KRS Board of Trustees. The Paducah Water Works contributions to CERS for the years ended June 2014, 2013, and 2012, were \$509,758, \$504,070, and \$436,993, respectively, equal to the required contribution for each year.

(Continued)

**PADUCAH WATER WORKS**  
**NOTES TO FINANCIAL STATEMENTS**  
**YEARS ENDED JUNE 30, 2014 AND 2013**

**Note 7 - Employee Benefits:**

**Health Insurance**

Paducah Water Works no longer has a self-insured health plan but rather a traditional health insurance plan through Anthem. A majority of the cost of the plan is borne by Paducah Water Works. Health insurance expense was \$590,502 and \$546,310 for years ended June 30, 2014 and 2013, respectively.

**Note 8 - Disclosures Regarding the Statement of Cash Flows:**

For purposes of the Statement of Cash Flows, the composition of cash and cash equivalents at June 30, 2014 and 2013, is as follows:

	<u>2014</u>	<u>2013</u>
Cash and cash equivalents	\$1,254,787	\$1,478,634
Cash, designated	<u>3,163,760</u>	<u>3,007,803</u>
<b>TOTAL CASH AND CASH EQUIVALENTS</b>	<b><u>\$4,418,547</u></b>	<b><u>\$4,486,437</u></b>
Noncash capital and related financing activities:		
	<u>2014</u>	<u>2013</u>
<b>NONCASH CAPITAL CONTRIBUTIONS</b>	<b><u>\$ 227,400</u></b>	<b><u>\$ 632,546</u></b>
Noncash transactions with Hendron merger:		
Net capital assets	\$ -	\$1,686,726
Inventory	-	8,241
Notes payable	-	88,386
Other liabilities	-	62,487

**Note 9 - Other Current Assets:**

Other Current Assets consisted of the following:

	<u>2014</u>	<u>2013</u>
Miscellaneous receivable	\$ 787,134	\$ 674,093
Accrued interest receivable	31	28
Prepaid insurance	104,397	143,270
Health insurance premium receivable	33,718	42,686
Flex advance receivable	19,832	16,707
Other	<u>32,374</u>	<u>39,279</u>
<b>TOTAL OTHER CURRENT ASSETS</b>	<b><u>\$ 977,486</u></b>	<b><u>\$ 916,063</u></b>

(Continued)

**PADUCAH WATER WORKS**  
**NOTES TO FINANCIAL STATEMENTS**  
**YEARS ENDED JUNE 30, 2014 AND 2013**

**Note 10 - Other Accrued Expenses and Current Liabilities:**

Other accrued expenses and current liabilities consisted of the following:

	<u>2014</u>	<u>2013</u>
Accrued payroll and payroll withholdings	\$ 82,947	\$ 97,172
Accrued sales tax	23,803	30,723
City refuse and dumpster payable	172,943	116,981
Sewer service collections payable	503,253	460,695
Deposit collections payable	54,738	17,513
Accrued sick and vacation time	239,106	236,567
Customer advances	38,828	38,828
Other	<u>139,669</u>	<u>80,106</u>
<b>TOTAL ACCRUED EXPENSES AND CURRENT LIABILITIES</b>	<b><u>\$1,255,287</u></b>	<b><u>\$1,078,585</u></b>

**Note 11 - Miscellaneous Revenues:**

Miscellaneous revenues consisted of the following:

	<u>2014</u>	<u>2013</u>
Returned checks	\$ 9,519	\$ 6,595
Re-established service	114,679	84,862
Meter replacement	15,455	13,135
Service calls	17,624	5,063
New service	118,624	88,112
Miscellaneous fees	<u>2,578</u>	<u>29,067</u>
<b>TOTAL MISCELLANEOUS REVENUE</b>	<b><u>\$278,479</u></b>	<b><u>\$226,834</u></b>

**Note 12 - Other Operating Expenses:**

Other operating expenses consisted of the following:

	<u>2014</u>	<u>2013</u>
Legal and professional expenses	\$ 31,214	\$ 38,426
Insurance expense	767,535	730,453
Wellness Program	<u>8,188</u>	<u>6,604</u>
<b>TOTAL OTHER OPERATING EXPENSES</b>	<b><u>\$806,937</u></b>	<b><u>\$775,483</u></b>

(Continued)

**PADUCAH WATER WORKS**  
**NOTES TO FINANCIAL STATEMENTS**  
**YEARS ENDED JUNE 30, 2014 AND 2013**

**Note 13 - Gain (Loss) on Disposal of Capital Asset:**

Gain (loss) on Disposal of Capital Asset as of June 30, 2014 consisted of:

Gain on sale of office building	\$ 38,430
Gain on sale of SCADA equipment	12,111
Gain on sale of old vac unit	8,000
Sale of other assets	<u>1,476</u>

TOTAL GAIN ON DISPOSAL OF CAPITAL ASSET \$ 60,017

Gain (loss) on Disposal of Capital Asset as of June 30, 2013 consisted of:

Auction proceeds Hendron Water Equipment	\$ 70,169
Loss on sale of Reidland property	(35,594)
Gain on sale of Truck	<u>4,830</u>

TOTAL GAIN ON DISPOSAL OF CAPITAL ASSET \$ 39,405

**Note 14 - Hendron Water District:**

Paducah Water Works assumed control of all Hendron's assets, inventory, equipment, etc. through a merger on August 1, 2012. The assets acquired from Hendron Water District consisted of the following:

	<b><u>August 1,</u></b> <b><u>2012</u></b>
<b><u>Assets:</u></b>	
Cash	\$ 57,542
Certificate of deposit	38,177
Inventory	8,241
Capital assets	3,731,595
Accumulated depreciation	<u>(2,044,869)</u>
Total assets	<u>1,790,686</u>
<b><u>Liabilities:</u></b>	
Accounts payable	31,076
Customer advances	31,411
Notes payable	<u>88,386</u>
Total liabilities	<u>150,873</u>
<b><u>Net Position:</u></b>	
Invested in capital assets	1,598,340
Unrestricted	<u>41,473</u>
TOTAL NET POSITION	<u>\$1,639,813</u>

(Continued)

**PADUCAH WATER WORKS**  
**NOTES TO FINANCIAL STATEMENTS**  
**YEARS ENDED JUNE 30, 2014 AND 2013**

**Note 15 - Reclassification:**

Paducah Water Works assumed control of all Hendron's assets, inventory, equipment, etc. through a merger on August 1, 2012. The assets acquired from Hendron Water District included a certificate of deposit in the amount of \$38,177. This certificate of deposit was included as part of cash and cash equivalents on the Statement of Net Position dated June 30, 2013. It should have been included in certificates of deposit, designated. The certificate of deposit was restated on the comparative Statement of Net Position for the years ended June 30, 2014 and 2013.

Cash and cash equivalents, as previously stated	
June 30, 2013	\$1,516,811
Certificate of deposit	<u>(38,177)</u>
Cash and cash equivalents, as restated	
June 30, 2013	<u>\$1,478,634</u>
Certificates of deposit, designated, as previously	
stated June 30, 2013	\$1,296,271
Certificate of deposit	<u>38,177</u>
Certificates of deposit, designated, as restated	
June 30, 2013	<u>\$1,334,448</u>

**Note 16 - Change in Accounting Standards:**

In June 2012, the GASB issued Statement No. 68, *Accounting and Financial Reporting for Pensions*, which amends GASB statement No. 27. It addresses several issues regarding public pension plans, liabilities reported pertaining to unfunded portions of those plans, and the disclosure requirements. GASB Statement No. 68 will be effective for Paducah Water Works for the calendar year beginning January 1, 2014. The effects it will have on Paducah Water Works have yet to be determined.

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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***

The Board of Directors  
Paducah Water Works  
Paducah, Kentucky

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to the financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of Paducah Water Works as of and for the years ended June 30, 2014 and 2013, and the related notes to the financial statements, which collectively comprise Paducah Water Works' basic financial statements, and have issued our report thereon dated September 24, 2014.

**Internal Control Over Financial Reporting**

In planning and performing our audit of the financial statements, we considered Paducah Water Works' internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of Paducah Water Works' internal control. Accordingly, we do not express an opinion on the effectiveness of Paducah Water Works' 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. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

**Compliance and Other Matters**

As part of obtaining reasonable assurance about whether Paducah Water Works' financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

**Purpose of this Report**

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the result 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.

*Williams, Williams & Zengler*

September 24, 2014