

**MOUNTAIN WATER DISTRICT**

**REPORT OF AUDIT**

**DECEMBER 31, 2015**

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## **INDEPENDENT AUDITOR'S REPORT**

To the Board of Commissioners  
Mountain Water District  
Pikeville, Kentucky

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

I have audited the accompanying financial statements of the business-type activities of Mountain Water District, as of and for the year ended December 31, 2015, and the related notes to the financial statements, which collectively comprise the Mountain Water District's basic financial statement 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 opinions 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 statement are free from material misstatement.

An audit involves performing procedure to obtain audit evidence about the amounts and disclosures in the financial statements. The procedure selected depends 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 presentations 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, 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 evidence I obtained is sufficient and appropriate to provide a basis for my audit opinions.

### **Opinions**

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 Mountain Water District, as of December 31, 2015, and the respective changes in financial position and where applicable, cash flows thereof for the year ended in accordance with accounting principles generally accepted in the United States of America.

### **Emphasis of Matter**

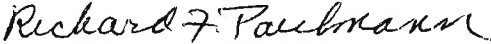
As discussed in Note 2 page 20 to the financial statements, effective December 1, 2014, Mountain Water District adopted Governmental Accounting Standards Board No. 68, Accounting and Financial Reporting for Pensions. My Opinion is not modified with respect to this matter.

### **Other Matters**

Accounting principles generally accepted in the United States of America require that management's discussion and analysis and budgetary comparison information on pages 3-5 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by Governmental Accounting Standards Board, who considers it to be an essential part of 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 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 me with sufficient evidence to express an opinion or provide assurance.

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

In accordance with Governmental Auditing Standards, I have also issued my report dated September 23, 2015, on my consideration of Mountain Water District's internal control over financial reporting and on 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 the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with Governmental Auditing Standards in considering Mountain Water District's internal control over financial reporting and compliance.

  
Richard F. Paulmann CPA, LLC  
Pewee Valley, KY  
September 19, 2016

**MOUNTAIN WATER DISTRICT**  
**MANAGEMENT'S DISCUSSION AND ANALYSIS**  
**ANNUAL FINANCIAL STATEMENTS**  
**FOR THE YEAR ENDED DECEMBER 31, 2015**

Our discussion and analysis of the Mountain Water District's financial performance provides an overview of the District's financial activities for the fiscal year ended December 31, 2015. Please read it in conjunction with the accompanying basic financial statements. It is our intent that this discussion provide all parties interested in the District's financial condition, especially the users of the facilities, a better understanding of the District's operations and financial status.

The District reports its financial statements in a required model format issued by the Governmental Accounting Standards Board.

**Financial Highlights**

- Net assets decreased this year by \$3,508,445 from operating activities and before capital contributions.
- The District's total long-term debt increased by \$1,055,576 with additional loan proceeds of \$1,609,292 and payment on the outstanding principal of \$772,464.
- The District acquired several vehicles through financing.
- The District was able to make the following purchases:
  1. Significant water and sewer line extensions to the outlying areas of Pike County.
  2. Assorted new equipment for treatment plant and distribution system to facilitate daily operations.

**Overview of the Financial Statements**

The District's basic financial statements include: (1) fund financial statements, and (2) notes to the financial statements. These financial statements present information about business-type activities, which consists principally of the fees the District charges its users to cover all or most of the cost of the services it provides.

**Fund Financial Statements**

The fund financial statements provide detailed information about the proprietary fund. When the District charges customers for services it provides, these services are generally reported in proprietary funds. Proprietary funds are reported in the same way that all activities are reported in the Statement of Net Assets and the Statement of Activities. In fact, the District's enterprise funds (a component of proprietary funds) are the same as the business-type activities we report in the government-wide statements but provide more detail and additional information, such as cash flows for proprietary funds.

**MOUNTAIN WATER DISTRICT**  
**MANAGEMENT'S DISCUSSION AND ANALYSIS**  
**ANNUAL FINANCIAL STATEMENTS**  
**FOR THE YEAR ENDED DECEMBER 31, 2015**  
**(CONTINUED)**

**Notes to the financial statements**

The accompanying notes to the financial statements provide information essential to a full understanding of the fund financial statements. The notes to the financial statements begin immediately following the basic financial statements.

**Reporting on the District as a Whole**

One of the most important questions asked about the District's finances is, "Is the District as a whole better off or worse off as a result of this year's activities?" The statements of Fund Net Assets and the Statement of Revenue, Expenses and Changes in Fund Net Assets report information about the District as a whole and about its activities in a way that helps answer this question.

Our discussion begins with an analysis of overall revenues and expenses and their treatment. An overwhelming majority of the District's revenue is received from charges for services.

The District's total revenues increased from a year ago by \$21,986 (.0024%). The increase was the result of a rate increase late in the year. Total cost of all programs and services (including depreciation) increased by \$417,205 (3.6%). Interest expense decreased by \$16,750, due in large part to the refinancing of bonds in 2012 at lower interest rates. This trend is expected to remain approximately the same through the next fiscal year end.

**Financial Analysis of the District's Proprietary Fund**

At year-end, the District's proprietary fund reported total net assets of \$74,076,396, which is a decrease of \$1,321,577 or (1.75%) from last year.

**Capital Assets**

As noted above, the District was able to make several capital asset purchases without additional debt.

**Debt/Advances in Construction**

At year-end, the District had various bond/notes payables to various lenders with a combined remaining balance of \$12,359,319 to be paid from utility revenues.

As of December 31, 2015, the District had received advances for construction towards projects not completed in the amount of \$3,966,360. During 2015, various construction projects were completed allowing the advances for construction from the prior year in the amount of \$2,323,091 to be transferred to capital contributions from government grants.

**MANAGEMENT'S DISCUSSION AND ANALYSIS**  
**ANNUAL FINANCIAL STATEMENTS**  
**FOR THE YEAR ENDED DECEMBER 31, 2015**  
**(CONTINUED)**

**Contacting the District's Financial Management**

This financial report is designed to provide our customers, creditors, and other users with a general overview of the District's finances and to show the District's accountability for the money it receives. If you have questions about this report or need additional financial information, contact the District's Treasurer, at the Mountain Water District, P. O. Box 3157, Pikeville, KY 41502, telephone number (606) 631-9162.

MOUNTAIN WATER DISTRICT  
STATEMENT OF FINANCIAL POSITION  
December 31, 2015  
(with prior year data for comparison purposes only)

	2015	2014
<b>ASSETS</b>		
<b>CURRENT ASSETS</b>		
Cash and Cash Equivalents	\$ 135,844	\$ 133,996
Accounts Receivable (Net of Allowance for Delinquencies of \$40,000 in 2015 and \$46,000 in 2014)	1,749,423	1,116,854
Prepaid expenses	-	37,294
Insurance refund receivable	-	13,279
	<b>TOTAL CURENT ASSETS</b>	<b>\$ 1,301,423</b>
<b>NONCURRENT ASSETS</b>		
<b>Restricted Assets</b>		
Cash-Depreciation Reserve	803,625	684,727
Cash-Construction	399,626	592,411
Cash-Customer Deposits	331,128	339,439
Cash-Recycling Account	2,893	2,853
Cash-Operation and Maintence Reserve	16,567	16,550
Cash-Wastewater Operation and Maintenance Reserve	827,723	690,883
Cash-Sinking Fund	461,566	415,598
	<b>TOTAL RESTRICTED CASH</b>	<b>2,742,461</b>
<b>Capital Assets</b>		
Supply & Pumping	3,547,281	3,668,064
Water Treatment Equipment	11,261,985	9,658,690
Transmission & Distribution	85,807,060	85,627,046
General Plant	4,176,916	4,327,092
Land and Land Rights	549,443	540,235
Sewer Utility Plant	29,345,539	29,598,405
Sewer General Plant	707,650	660,756
Total Capital Assets	135,395,874	134,080,288
Less: Accumulated Depreciation	(50,590,049)	(48,016,341)
Net Capital Assets	84,805,825	86,063,947
Construction in Progress	3,970,941	3,662,114
<b>OTHER ASSETS</b>		
Deposit on Leased Vehicles	625	625
Fema receivable	67,757	
Rate Case Cost-Net of Amortization	162,439	
Bond refinancing Cost-Net of Amortization	81,121	84,561
	<b>TOTAL OTHER ASSETS</b>	<b>85,186</b>
<b>TOTAL NONCURRENT ASSETS</b>	<b>91,931,836</b>	<b>92,553,708</b>
<b>TOTAL ASSETS</b>	<b>\$ 93,817,103</b>	<b>\$ 93,855,131</b>
<b>DEFERRED OUT FLOW OF RESOURCES</b>		
Defferred Pension Contributions	\$ 20,207	\$ 23,543

See Accompanying notes to the basic financial statements



MOUNTAIN WATER DISTRICT  
STATEMENT OF FINANCIAL POSITION  
, December 31, 2015  
(with prior year data for comparison purposes only)

	2015	2014
<b><u>LIABILITIES</u></b>		
<b><u>CURRENT LIABILITIES</u></b>		
Accounts Payable	\$ 154,898	\$ 122,005
Accounts Payable UMG	\$ 1,050,000	\$ 1,017,063
Other Accrued Liabilities	28,835	26,553
Accrued Interest	162,005	167,457
Customer Deposits	311,320	321,600
Line of Credit	93,790	31,235
Bonds Payable, Current	66,500	63,500
Notes Payable and Capital Leases, Current	820,758	714,056
<b>TOTAL CURRENT LIABILITIES</b>	2,688,106	2,463,469
<b><u>LONG-TERM LIABILITIES</u></b>		
Bonds Payable, long-Term	3,721,500	3,788,000
Notes Payable and Capital		
Net Pension Liability	162,933	167,879
Accounts Payable UMG	1,423,265	
Leases, Long-Term	7,750,561	8,365,030
Advances For Construction	3,996,360	3,678,134
<b>TOTAL LONG-TERM LIABILITES</b>	17,054,619	15,999,043
<b><u>TOTAL LIABILITIES</u></b>	19,742,725	18,462,512
<b><u>DEFERRED INFLOWS OF RESOURCES</u></b>		
Deferred Pension Investment Earnings	18,189	18,189
<b><u>NET POSITION</u></b>		
Invested in Capital Assets, Net of Related Debt	72,446,506	73,117,341
Restricted for:		
Construction	399,626	592,411
Depreciation, Maintenance and Replacement	1,824,054	1,521,133
Customer Deposits	19,808	17,839
Unrestricted	(613,598)	149,249
<b><u>TOTAL NET POSITION</u></b>	74,076,396	75,397,973

See Accompanying notes to the basic financial statements

MOUNTAIN WATER DISTRICT  
 STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET POSITION  
 FOR THE YEAR ENDED DECEMBER 31, 2015  
 (With prior year data for comparison purposes only)

	<u>2015</u>	<u>2014</u>
<b><u>OPERATING REVENUE</u></b>		
Metered Sales-Residential	\$6,482,561	\$6,343,302
Metered Sales-Commercial	597,841	607,330
Sewage Revenue	875,890	877,462
Metered Sales-Multi-Family	278,344	277,560
Metered Sales-Public Authorities	228,853	218,791
Customer Late Payment Charges	190,417	177,681
Other Water Service Revenue	188,093	302,193
Service Connection Fees	119,535	142,186
Metered Sales-Industrial	58,060	47,019
Misc Revenue		4,084
Fire Protection Revenue	1,200	1,200
	9,020,794	8,998,808
<b><u>TOTAL OPERATING REVENUE</u></b>		
 <b><u>OPERATING EXPENSES</u></b>		
Contract Service-Management	7,592,331	7,415,887
Depreciation	3,815,934	3,731,060
Material and Supplies	350,163	190,265
Wages	149,961	146,002
Contract Service-Accounting	61,877	67,189
Education, Dues and Meetings	14,542	13,204
Employee Benefits	14,857	15,076
Contract Service-Legal Engineering	52,352	43,903
Taxes & Licenses	16,951	17,865
Payroll Taxes	11,211	17,730
Retirement Expense	18,544	23,543
Settlement Fees	2,000	6,273
Rent Expense	1,200	5,300
Telephone Expense	4,200	3,841
Advertising	1,221	2,584
Amortization Expense	13,023	3,440
	12,120,367	11,703,162
<b><u>TOTAL OPERATING EXPENSE</u></b>		
	<u>(3,099,573)</u>	<u>(2,704,354)</u>
<b><u>OPERATING LOSS</u></b>		
 <b><u>NON-OPERATING REVENUE (EXPENSES)</u></b>		
Gain On Sale of Assets	(12,661)	14,818
Interest Income	2,774	3,031
Interest Expense	(398,985)	(415,735)
	(408,872)	(397,886)
<b><u>TOTAL NON-OPERATING REVENUE (EXPENSES)</u></b>		
 <b><u>LOSS BEFORE CAPITAL CONTRIBUTIONS AND OTHER CHANGES IN NET POSITION</u></b>		
	<u>(3,508,445)</u>	<u>(3,102,240)</u>

See Accompanying notes to the basic financial statements

MOUNTAIN WATER DISTRICT  
 STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN FUND NET POSITION  
 FOR THE YEAR ENDED DECEMBER 31, 2015  
 (With prior year data for comparison purposes only)

	<u>2015</u>	<u>2014</u>
<b><u>CAPITAL CONTRIBUTIONS AND OTHER CHANGES</u></b>		
<b><u>IN NET ASSETS</u></b>		
Capital Contributions from:		
Government Grants	2,095,459	3,802,668
Customers through Tap-on Fees	<u>91,409</u>	<u>116,972</u>
<b><u>TOTAL CAPITAL CONTRIBUTIONS AND</u></b>		
<b><u>OTHER CHANGES IN NET POSITION</u></b>	<u>2,186,868</u>	<u>3,919,640</u>
<b><u>CHANGE IN NET POSITION</u></b>	<u>(1,321,577)</u>	<u>817,400</u>
<b><u>NET POSITION, BEGINNING OF YEAR</u></b>	<u>75,397,973</u>	<u>74,580,573</u>
<b><u>NET POSITION, END OF YEAR</u></b>	<u>\$ 74,076,396</u>	<u>\$ 75,397,973</u>

See Accompanying notes to the basic financial statements

MOUNTAIN WATER DISTRICT  
STATEMENT OF CASH FLOWS  
FOR THE YEARS ENDED DECEMBER 31, 2015  
(with prior year data for comparison purposes only)

	<u>2015</u>	<u>2014</u>
<b><u>CASH FLOWS FROM OPERATING ACTIVITIES</u></b>		
Receipts from Customers	\$8,462,798	\$8,852,303
Payment to Suppliers	(8,123,739)	(7,239,900)
Payment to Employees	(164,818)	(163,173)
<b><u>NET CASH PROVIDED BY OPERATING ACTIVITIES</u></b>	<u>174,241</u>	<u>1,449,230</u>
<b><u>CASH FLOWS FROM NON-CAPITAL FINANCING ACTIVITIES</u></b>		
Increase (Decrease) In Customer Deposits	<u>(10,280)</u>	<u>50,423</u>
<b><u>CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES</u></b>		
Proceeds From Tap-On Fees	91,409	116,972
Payments for rate increase	(134,728)	(37,294)
Construction in Aid of Construction	2,095,459	3,802,668
(Decrease) Increase in Advances for Construction	318,226	(1,723,131)
Purchases of Equipment	(2,570,404)	(3,779,109)
Increase in Construction in Progress	(308,827)	1,346,756
Principal Payments	(772,464)	(911,226)
Interest Payments	(393,533)	(420,884)
Proceeds of Bank Loans & UMG	1,609,292	93,822
Proceeds from Sale of Vehicles	1,350	14,818
<b><u>NET CASH USED BY CAPITAL AND RELATED FINANCING ACTIVITIES</u></b>	<u>(64,220)</u>	<u>(1,496,608)</u>
<b><u>CASH FLOWS FROM INVESTING ACTIVITIES</u></b>		
Interest Income	<u>2,774</u>	<u>3,031</u>
<b><u>NET INCREASE IN CASH</u></b>	<u>102,515</u>	<u>6,076</u>
<b><u>CASH, BEGINNING OF YEAR</u></b>	2,876,457	2,870,381
<b><u>CASH, END OF YEAR</u></b>	<u>\$ 2,978,972</u>	<u>\$ 2,876,457</u>

See Accompanying notes to the basic financial statements

MOUNTAIN WATER DISTRICT  
STATEMENT OF CASH FLOWS  
PROPRIETARY FUND  
FOR THE YEARS ENDED DECEMBER 31, 2015 AND 2014  
(with prior year date for comparison purposes only)  
"Continued"

	2015	2014
<b><u>RECONCILIATION OF OPERATING LOSS</u></b>		
<b><u>TO NET CASH PROVIDED BY</u></b>		
<b><u>OPERATING ACTIVITIES</u></b>		
Operating Loss	\$ (3,099,523)	\$ (2,704,404)
Adjustments to Reconcile operating Loss to Net Cash Provided by Operating Activities		
Depreciation	3,815,934	3,731,060
Amortization	13,023	3,440
Cancelation of Debt Payments (Decrease) Increase in Provision for Uncollectible Accounts	(6,000)	
Decrease (Increase) In:		
Customer Accounts Receivable	(206,535)	(63,824)
Other Accounts Receivable	(426,331)	(82,682)
Prepaid Expenses	31,294	(50,572)
Increase (Decrease) In:		
Accounts Payable:		
Trade	32,893	612,355
Other Accrued Liabilities	19,486	3,857
<b>NET CASH PROVIDED BY OPERATING ACTIVITIES</b>	<b>\$ 174,241</b>	<b>\$ 1,449,230</b>
 <b>NON-CASH CAPITAL AND RELATED FINANCINGS ACTIVITIES</b>		
During the period the Company purchased Vehicles in exchange for long term debt.	\$ 29,119	\$ 62,316
During the period the Company Completed Certain construction projects that were transferred to capital assets.	\$ 2,323,091	\$ 2,976,564
Gain on Sale of Assets	\$ (12,661)	\$ 14,818

See Accompanying notes to the basic financial statements

**MOUNTAIN WATER DISTRICT**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**DECEMBER 31, 2015 AND 2014**

1. **SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

The accounting policies of Mountain Water District (“the District”) conform to generally accepted accounting principles as applicable to governmental units. The Governmental Accounting Standards Board (GASB) is accepted standard-setting body for establishing governmental accounting and financial reporting principles.

The following is a summary of the more significant policies:

**A. Organization**

Mountain Water District is a political subdivision of the Pike County Fiscal Court, organized under chapter 74 of the Kentucky Revised Statutes. It was formed from a merger of four existing water districts-Marrowbone Water District, Shelby Valley Water District, Pond Creek Water District, and John’s Creek Water District- on June 30, 1986 and at that time assumed all assets and liabilities of the existing water districts.

The territorial limits of Mountain Water District, set by the Pike County Judge/Executive on January 20, 1987, are all of Pike County except; (1) the territory of that portion of the Sandy Valley Water District located in Pike County (2) the water services area of the City of Pikeville, and (3) special financing relationships.

**B. Reporting Entity**

The District is the basic level of government which has financial accountability and control over all activities related to the District. The District is not included in any other governmental “reporting entity” as defined by GASB pronouncement. The Board of Commissioners have decision making authority, the power to designate management, the ability to influence operations, and the primary accountability for fiscal matters. There are no component units as defined in GASB Statement 14 which is included in the District’s reporting entity.

**C. Basis of Presentation-Fund Accounting**

The accounts of the District are organized on the basis of funds each of which is considered a separate accounting entity. The operations of each fund are accounted for with a separate set of self-balancing accounts that comprise its assets, liabilities, fund equity, revenues, and expenditures, or expenses, as appropriate.

**Proprietary Funds/Enterprises Funds**

Enterprise funds are used to account for operations (a) that are financed and operated in a manner similar to private business enterprises-where the intent of the governing body is that the costs (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 accountability, capital maintenance, public policy, management control, or other purposes.

**MOUNTAIN WATER DISTRICT**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**DECEMBER 31, 2015 AND 2014**

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

**D. Basis of Accounting**

All proprietary funds are accounted for using the accrual basis of accounting. Revenues are recognized when earned, and expenses are recognized when obligations are incurred.

**E. Encumbrance Accounting**

The District does not use encumbrance accounting. Since effective budgetary control and accountability and cash planning and control can be facilitated without encumbrance accounting, this is not considered departure from generally accepted accounting principles. There were no unperformed contracts in process at year end which otherwise might have resulted in the need to encumber estimated expenditures.

**F. Customer Accounts Receivable**

Customer accounts receivable are stated at face value, less allowance for uncollectible accounts. Changes in the allowance are charged to operating expenses.

**G. Capital Assets**

Capital Assets, which included property, plant and equipment, are reported in the fund financial statements at historical cost.

Depreciation is recorded as an allocated expense in the Statement of Revenues, Expenses and Changes in Fund Net Assets with accumulated depreciation reflected in the Statement of Fund Net Assets. Depreciation is computed using straight-line method over the estimated useful lives of the related assets. Estimated useful lives range from 3 to 40 years.

Capital additions improvements and major renewals are capitalized, whereas maintenance, repairs and minor renewals are charged to expenses when they are incurred. In the case of disposals, the assets and related reserves are removed from the accounts and the net amount less any proceeds from disposals, is charged or credited to revenues.

**H. Cash and Cash Equivalents**

For purpose of the statement of cash flows, the District considered all highly liquid investments (including restricted assets) with a maturity of three months or less when purchased to be cash equivalents.

As of December 31, 2015, cash consisted of the following:

Petty Cash	\$ 320
Cash in Bank	135,524
Restricted Cash	<u>2,900,213</u>
<b>Total Cash</b>	<b><u>\$ 3,036,057</u></b>

**MOUNTAIN WATER DISTRICT**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**DECEMBER 31, 2015 AND 2014**

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

**I. Bad Debts**

Bad debts are recognized using the reserve method of accounting for uncollectible accounts.

**J. Inventory**

Inventory is valued at lower of cost or market on a First-In, First-Out Basis. The management service company took over ownership of the inventory and its maintenance until the contract with them is completed.

**K. Investment Policy**

The District's policy is to invest available funds in the following:

1. Obligations of the U.S. and its agencies and Instrumentalities.
2. Obligations and contract for future delivery of purchases of obligations backed by the full faith and credit of the U.S. or a U.S. Government agency, including but not limited to"
  - a) United States Treasury
  - b) Export-Import Bank of the United States.
  - c) USDA-Rural Development
  - d) Government National Mortgage Corporation, and
  - e) Merchant Marine Bonds
3. Obligations of any corporation of the U.S. Government.
4. Certificate of Deposit issued by other interest bearing accounts of any bank or savings and loan institutions which are issued by the Federal Deposit Insurance Corporation or similar entity of which are collateralized, to the extent uninsured, by any obligation permitted by section 41.240(4) of the Kentucky revised statutes.
5. Uncollateralized certificates of deposits issued by any bank or savings and loans institution rated in one of the three highest categories by a national recognized rating agency.
6. Bankers' Acceptance for banks rated in one of three highest categories by a nationally recognized rating agency.
7. Commercial paper rated in the highest categories by a nationally recognized rated agency.
8. Bonds or certified of indebtedness of the Commonwealth of Kentucky and of its agencies or instrumentalities.
9. Securities issued by a state or local government, or any instrumentality or agency thereof, in the U.S. , and rated in one the three highest categories by a nationally recognized rating agency.
10. Shares of mutual funds, which contain certain characteristics.

Limits on investments transactions are limited in amount in one category to 20% of the total funds invested and no investment shall be purchased on a margin basis.

The District is currently invested only in interest bearing accounts of local federal insured financial institutions, including interest bearing checking accounts and certificates.



**MOUNTAIN WATER DISTRICT**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**DECEMBER 31, 2015 AND 2014**

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

**L. Leave Policy-Vacation/Leave Policy-Sick Leave**

The District allows full-time employees to accrue vacation leave as follows: (a) ten (10) days during the first year of employment. Employees can accrue vacation time up to a maximum of twice the annual entitlement. If an accrual of twice the annual vacation entitlement is attained, additional vacation days do not accrue. Upon termination of employment, an employee shall be paid for all accrued vacation leave.

Employees shall accrue sick leave at the rate of ten (10) days per year. Employees can accrue sick leave up to a maximum of 160 hours, after the maximum is obtained no additional sick leave is accrued. Upon termination, resignation, retirement or voluntary leave, the employee shall not be reimbursed for the accrued leave hours.

As of December 31, 2015 and December 31, 2014, the accrued liability for vacation leave was -0- and -0-, respectively.

**M. Advertising**

The company expenses advertising costs as incurred. Total advertising costs charged to expense for the years ended December 31, 2015 and 2014 are \$1,221 and \$2,584 respectively.

**N. Equity Classifications**

In the fund financial statements, equity classified as net assets and displayed in three components.

- Invested in capital assets, net of related debt-Consist of capital assets including restricted capital assets, net of accumulated depreciation and reduced by the outstanding balances of any bonds, mortgages, notes, or other borrowing that are attributable to the acquisition, construction, or improvement of those assets.
- Restricted net assets-Consist of net assets 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.
- Unrestricted net assets-All other net assets that do not meet the definition of "restricted" or "invested in capital assets, net of related debt".

**2. EMPLOYEE RETIREMENT SYSTEMS**

The District has elected to participate in the County Employee Retirement System (CERS) pursuant to KRS 78.530, administered by the Board of Trustees of the Kentucky Retirement System. This is a multiple employer public retirement system which covers all eligible full-time-employees. Benefit contributions and provisions are established by statute. Non-hazardous covered employees are required to contribute 5 percent of their salary to the Plan. The District's contribution rate for non-hazardous employees was 17.67 percent.

**MOUNTAIN WATER DISTRICT**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**DECEMBER 31, 2015 AND 2014**

**2. EMPLOYEE RETIREMENT SYSTEMS (Continued)**

(CERS) is a defined benefit plan created by the Kentucky General Assembly. (CERS) provides retirement and disability benefits, annual cost of living adjustments, and death benefits to plan members and beneficiaries.

The board of Trustees of the County Employee Retirement System (A division of Kentucky Retirement System), in consultation with the actuary, set the actuarial assumptions and methods used in the valuation. Once every five years the actuary conducts a thorough review of plan experience for the preceding five years, and then makes recommendations to the board.

CERS also provides postretirement health care coverage to age and service retirees with 20 or more years of qualifying CERS service credit. A portion of each employer's and employee's contribution to CERS is set aside for funding postretirement health care. The health care coverage provided by the retirement is considered another Post Employment Benefit as described in Governmental Accounting Board Statement 45. KRS provides statutory authority requiring public employers to fund post health care through contributions to (CERS).

The Schedule of Funding Progress for Pension Fund and the Schedule of Funding Progress for Health Fund, show the latest information for the past four fiscal years ending June 30, 2015 reported in Kentucky Retirement Systems audited financial statements for the fiscal year ended June 30, 2015 as follows:

Benefits fully vest on reaching five years of service for non-hazardous employees. Aspects of benefits for non-hazardous employees included retirement after 27 years of service or age 65.

The District's payroll for the year ended December 31, 2015 was \$149,961. The payroll for employees covered under CERS was \$116,364. The contributions required for CERS for the year was 26,380 which consisted of \$20,562 of District contributions and \$5,818 of employee contributions.

The District's payroll for the year ended December 31, 2014 was \$149,544. The payroll for employees covered under CERS was \$116,364. The contributions required for CERS for the year was \$26,380 which consisted of \$20,562 of District contributions and \$5,818 of employee contributions.

CERS issues a standalone financial report, which may be obtained from Kentucky Retirements Systems, 120 Louisville Road, Frankfort Kentucky, 40601.

**MOUNTAIN WATER DISTRICT**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**DECEMBER 31, 2015 AND 2014**

**2. EMPLOYEE RETIREMENT SYSTEM (Continued)**

FISCAL YEAR <u>FUNDING</u>	ANNUAL PENSION COST <u>(APC)</u>
12/31/13	\$21,829
12/31/14	\$20,562
12/31/15	\$20,562

Schedule of Nonhazardous Funding Progress – Pension Fund (CRES)

Actuarial Valuation <u>Date</u>	Actuarial Value <u>of Assets</u>	Actuarial Accrued Liability (AAL) Target <u>Rate</u>	Unfunded AAL (UAAL)	percent <u>Funded</u>	Covered <u>Payroll</u>	UAAL as a % of Cover <u>Payroll</u>
June 30, 2012	5,547,235,599	9,139,567,695	3,592,332,096	60.7	2,236,546,345	160.6
June 30, 2013	5,637,094,483	9,387,867,114	3,471,781,631	60.1	2,236,277,489	167.3
June 30, 2014	6,528,147,000	9,772,523,000	3,244,376,000	66.8	2,272,270,000	142.78
June 30, 2015	6,474,848,513	10,740,325,421	4,265,476,908	60.3	2,296,715,957	185.7

Schedule of Nonhazardous Funding Progress – Health Insurance Fund (CERS)

Actuarial Valuation <u>Date</u>	Actuarial Value <u>of Assets</u>	Actuarial Accrued Liability (AAL) Target <u>Rate</u>	Unfunded AAL (UAAL)	percent <u>Funded</u>	Covered <u>Payroll</u>	UAAL as a % of Cover <u>Payroll</u>
June 30, 2012	1,512,853,851	3,370,771,228	857,917,437	63.8	2,236,546,345	38.4
June 30, 2013	1,628,244,197	2,443,894,100	815,649,903	66.6	2,236,277,489	36.5
June 30, 2014	1,831,199,465	2,616,914,600	785,715,135	70.0	2,272,270,000	34.6
June 30, 2015	1,997,456,463	2,907,817,440	910,370,977	68.7	2,296,715,957	39.6

In accordance with Statement 68, cost sharing governmental employers, such as Mountain Water District are required to report a net pension liability, pension expense and pension related assets and liabilities based on their proportionate share of the collective amounts for all governments in the plan. For purpose of measuring the net pension liability, deferred outflows of resources and deferred inflows of resources related to pension, and pension expense, information about the fiduciary net position have been determined on the same basis as they are reported by CERS. For this purpose, benefit payments (Including refunds of employee contributions) are recognized when due and payable in accordance with the benefits terms. Investments are reported at fair value.

**MOUNTAIN WATER DISTRICT**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**DECEMBER 31, 2014 AND 2015**

**2. EMPLOYEE RETIREMENT SYSTEM (Continued)**

As of December 31, 2015 Mountain Water District reported a liability of \$162,933 for its proportionate share of the net pension liability. The net pension liability used to calculate the net pension liability was determined by an actuarial valuation as of that date. Mountain Water District proportion of the net pension liability was based on a projection of Mountain Water District's long term share of contributions of all to the pension relative to the projected contributions of all participating organizations, actuarially determined. At December 31, 2015, Mountain Water District proportion was 0.005022%.

At December 31, 2015 Mountain Water District reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

	Deferred Outflows of Resources	Deferred Inflows of Resources
Net difference between projected and Actual earnings on pension plan Investments	\$	\$ 18,189
Deferred pension contribution	<u>20,207</u>	<u>          </u>
Total	<u>\$ 20,207</u>	<u>\$ 18,189</u>

The deferred outflows of resources relate to Mountain Water District Contributions to the CERS plan subsequent to the measurement date and will be recognized as a reduction of net pension liability in the year ending December 31, 2017. Other amounts reported as deferred outflows of resources and deferred inflows of resources related to pension will be recognized in pension expense as follows:

Year ending December 31:	
2016	\$ 4,548
2017	4,547
2018	4,547
2019	<u>4,547</u>
Total	<u>\$ 18,189</u>

**MOUNTAIN WATER DISTRICT**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**DECEMBER 31, 2015 AND 2014**

2. **EMPLOYEE RETIREMENT SYSTEM (Continued)**

Actuarial assumption – The total pension liability in the actuarial valuation was determined using the following actuarial assumptions, applied to all periods included in the investments:

Inflation	3.5 percent
Salary increases	4.5 percent, average, including inflation
Investment rate – Of return	7.75 percent, net of pension plan investments Expense, including inflation

The rates of mortality for the period after service retirement are according to the 1983 Group Annuity Mortality Table for all retired members and beneficiaries as of June 30, 2006, And the 1194 Group Annuity Mortality Table for all other members. The Group Annuity Mortality Table set forward five years used for the period after disability retirement.

The actuarial assumptions used in the June 30, 2014 valuation were based on the results of an actuarial experience study for the period July 1, 2005 to June 2008.

The long term expected rate of return on pension plan investments was determined using a building block method in which best estimate ranges of expected future real rates of return (expressed returns, net of pension plan investment expenses and inflation) are developed for each major asset class. These ranges are combined to produce the long term expected future real rates of return by weighting the expected future rates of return by the target assets allocation percentage and by adding expected inflation. The target allocation and best estimates of arithmetic real rates of return for each major asset class are summarized in the following table:

Asset Class	<u>Target Allocation</u>	<u>Long Term Nominal Rate of Return</u>
Asset Class	30%	8.45%
Domestic Equity	22%	8.85%
International Equity	5%	10.50%
Emerging Market Equity	7%	11.25%
Private Equity	5%	7.00%
Real Estate	10%	5.25%
Core US Fixed Income	5%	7.25%
Non US Fixed Income	5%	5.50%
Commodities	5%	7.75%
TIPS	5%	5.00%
Cash	<u>1%</u>	3.25%
Total	100%	

**MOUNTAIN WATER DISTRICT**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**DECEMBER 31, 2015 AND 2014**

**2. EMPLOYEE RETIREMENT SYSTEM (Continued)**

Discount rate – The discount rate used to measure the total pension liability was 7.75%. The projection of cash flows used to determine the discount rate assumed that Contributions from plan members and employers will be made at statutory contribution rates. Based on those assumptions, the pension plan’s fiduciary net position was projected to be available to make all projected future benefit payments of current active and inactive employees. Therefore, the long term expected rate of return on pension plan investments was applied to all periods of projected benefit payments to determine the total pension liability.

Sensitivity of the Mountain Water District’s proportionate share of the net pension liability to changes in the discount rate – The following presents Mountain Water District’s share of the net pension liability calculated using the discount rate of 7.75%, as well as what the Mountain Water District’s proportionate share of the net pension would be if it were calculated using a discount rate that is 1 percentage point lower (6.75%) or 1 percentage point higher (8.75%) than the current rate.

	1% Decrease	Current Discount Rate	1%
Increase	<u>(6.75%)</u>	<u>(7.75%)</u>	<u>(8.75%)</u>
Mountain Water District Share Of the net pension liability	<u>\$ 214,442</u>	<u>\$ 162,933</u>	<u>\$ 117,471</u>

The beginning Net Position of the Public Utilities has been restated to record a prior period adjustment to implement GASB 68 .

	<u>Public Utilities</u>
Net Position as Previously Reported at December 31, 2014	\$ 311,774
Implementation of GASB 68: CERS Net Pension Liability (Measurement Date As of December 31, 2014)	(167,879)
Deferred Outflows – CERS Contributions made during Year ending December 31, 2014	<u>5,354</u>
Beginning Net Position, As restated	<u>\$149,249</u>

**MOUNTAIN WATER DISTRICT**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**DECEMBER 31, 2015 AND 2014**

**3. CUSTOMER DEPOSIT FUND**

Deposits required from customers when they sign up for the water service are deposited into the customer deposit escrow account. When services are terminated or a customer has paid in a timely fashion, a refund of the deposit plus interest is given after a year of water service. Customer deposits as of December 31, 2015 and December 31, 2014 were \$311,320 and \$321,600, respectively, and are currently held in escrow.

**4. COMMITMENTS AND CONTINGENCIES**

The District has been committed to several construction projects that have not been either started or completed as of the date of this report.

**5. FIXED ASSETS**

The following is a summary of changes in fixed asset:

<b>Description</b>	<b>Balance January 1 <u>2015</u></b>	<b>Additions</b>	<b>Dispositions</b>	<b>Balance December 31 <u>2015</u></b>
Supply & Pumping	\$3,668,064	\$244,729	\$365,532	\$3,547,281
Water Treatment Equipment	9,658,690	1,603,295	-0-	11,261,985
Transmission & Distribution	85,627,046	637,858	457,844	85,807,060
General Plant	4,327,092	28,400	178,576	4,176,916
Land and Land Rights	540,235	9,208	-0-	549,443
Sewer Utility Plant	29,598,405	-0-	252,866	29,345,539
Sewer General Plant	<u>660,756</u>	<u>46,894</u>	<u>-0-</u>	<u>707,650</u>
Totals	134,080,288	2,570,404	1,254,818	135,385,874
Accumulated Depreciation	<u>(48,016,341)</u>	<u>(3,815,934)</u>	<u>1,242,226</u>	<u>(50,590,049)</u>
Net Utility Plant	<u>\$86,063,947</u>	<u>\$(1,245,500)</u>	<u>\$ 12,592</u>	<u>\$84,805,825</u>
	<b>January 1</b>			<b>December 31</b>
<b>Description</b>	<b><u>2014</u></b>	<b>Additions</b>	<b>Dispositions</b>	<b><u>2014</u></b>
Supply & Pumping	\$3,372,662	\$295,402	\$ -0-	\$3,668,064
Water Treatment Equipment	9,231,954	426,736	-0-	9,658,690
Transmission & Distribution	84,751,581	975,830	100,365	85,627,046
General Plant	4,321,613	5,479	-0-	4,327,092
Land and Land Rights	534,875	5,360	-0-	540,235
Sewer Utility Plant	27,597,671	2,000,734	-0-	29,598,405
Sewer General Plant	<u>582,125</u>	<u>78,631</u>	<u>-0-</u>	<u>660,756</u>
Totals	130,392,481	3,788,172	100,365	134,080,288
Accumulated Depreciation	<u>(44,368,333)</u>	<u>(3,731,060)</u>	<u>83,052</u>	<u>(48,016,341)</u>
Net Utility Plant	<u>\$86,024,148</u>	<u>\$ 57,112</u>	<u>\$ 17,313</u>	<u>\$86,063,947</u>

Depreciation expense was \$3,815,934 and \$3,731,060 for the years ended December 31, 2015 and 2014, respectively.

**MOUNTAIN WATER DISTRICT**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**DECEMBER 31, 2015 AND 2014**

**6. SUBSEQUENT EVENTS**

In preparing these financial statements, the District has evaluated events and transactions for potential recognition or disclosure through September 23, 2015 the date the financial statements were available to be issued.

**7. RECLASSIFICATIONS**

Certain amounts in prior year financial statements have been reclassified for comparative purposes to conform with presentation in the current year financial statements.

**8. CONSTRUCTION IN PROGRESS**

Mountain Water District has overseen several construction projects. As of December 31, 2015, the following projects were in progress.

**Water Projects**

FEMA Mitigation Project	\$ 254,088
Tank Rehab Southern Corrosion	57,582
Jonican	901,889
Bad Fork	445,751
Pompey	47,488
Majesterial District 2	5,801
Phelps High School	52,000
Big creek Relocation	27,158
BPS Upgrage Caney	16,960
Various In House Projects	1,263,628

**Sewer Projects**

Phelps/Buskirk	67,038
Henry Clay	138,708
Belfry Pond Sewer	582,981
Douglas	109,842

**Total Construction in Progress** **\$ 3,970,914**

**9. RESTRICTED ASSETS AND RESERVE NET ASSETS**

Each of the proprietary funds has a portion of its net assets restricted in connection with assets restricted in uses, such as bond interest and redemption, depreciation, and customer deposits. Restricted net assets includes excess of restricted cash over liabilities payable from restricted cash.



**MOUNTAIN WATER DISTRICT**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**DECEMBER 31, 2015 AND 2014**

**10. DEPOSITS WITH FINANCIAL INSTITUTIONS**

At December 31, 2015, the carrying amount of the District's deposits with financial institutions was \$2,978,972 and the bank balance, per statements was \$3,905,738. The Bank balance is categorized as follows:

Amount insured by FDIC	\$ 750,000
Amount collateralized by securities held by third party trust company in the District's name	<u>2,491,879</u>
<b><u>Total Bank Balance</u></b>	<b><u>\$ 3,241,879</u></b>

Pledged collateral was obtained for amounts up to \$1,778,953 for money on deposit at Community Trust Bank in the name of Mountain Water District. Pledged Collateral was obtained for accounts up to \$712,926 for money on deposit with BB&T and Community Trust Bank in the name of Mountain Water District.

**11. CONSTRUCTION FUNDS**

Mountain Water District has several construction accounts used for the water projects. These are as follows:

	<u>2015</u>	<u>2014</u>
Big Creek Sewer Coal Settlement	\$5,401	\$18,934
District Wide Tap Fees	126,462	193,673
Misc. Line Extensions	4,968	15,069
MWD Special Projects	1,140	1,246
Phelps/Buskirk Waste Water	-0-	14,636
Shelby Waste Water	-0-	61,300
Penny Road Water and Sewer	29,973	44,868
Cowpen Waste Water Project	1,860	1,860
Elk Creek Project	2,272	2,279
Water Treatment Plant Upgrade	1	1
Water Treatment Raw Water Intake	25	25
LMI Service Contract	656	656
Various Short Line Extensions	191	175
Telemetry Project	100	100
Watson Hill Water Line	85	85
Long Fork Virgie Sewer Project	100	100
Belfry Pond Sewer Project	100	3,708
Smith Fork Waste Water Phase II	100	100
Pike County Fiscal Court Projects	173,606	187,360
Repair and Maintenance Reimbursement	2,200	3,413
MWD Rehabilitation Project	21,880	22,530
Sewer Customer Deposit	<u>28,506</u>	<u>20,293</u>
<b><u>Total Construction Funds</u></b>	<b><u>\$ 399,626</u></b>	<b><u>\$ 592,411</u></b>

**MOUNTAIN WATER DISTRICT**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**DECEMBER 31, 2015 AND 2014**

**11 RESTRICTED ASSETS AND RESERVE NET ASSETS Continued)**

As of December 31, 2015 and 2014 restricted cash were as follows:

	<u>2015</u>	<u>2014</u>
Depreciation Reserve	\$ 803,625	\$ 684,727
Sinking Fund	461,566	415,598
Customer Deposit Escrow Account	331,128	339,439
Operation & Maintenance reserve	16,567	16,550
Waste Water O & M Reserve	827,723	690,883
Recycling Account	2,893	2,853
Construction Account (Note 7)	<u>399,626</u>	<u>592,411</u>
<b><u>Total Restricted Cash</u></b>	<b><u>\$2,843,128</u></b>	<b><u>\$2,742,461</u></b>

The District is required by debt covenants to pay into and maintain a Depreciation Reserve Fund, a Repair and Maintenance Fund and Operation and Maintenance Fund. These Amounts may be used for extraordinary maintenance expenses related to the project or for costs of replacing worn obsolete portions of the project. If Amounts are withdrawn from said funds, the District must make required periodic deposits until the required balance is reinstated.

	<b>Maximum Required Balance</b>	<b>Required Balance at <u>12/31/15</u></b>	<b>Actual Balance At <u>12/31/15</u></b>
Depreciation Reserve Funds	\$851,400	\$ 814,980	\$ 803,625
Repairs and Maintenance Funds	866,168	<u>856,793</u>	<u>844,290</u>
<b>Total</b>		<b><u>\$1,671,773</u></b>	<b><u>\$1,647,915</u></b>

The Repair and Maintenance Funds required by Kentucky Infrastructure Authority (KIA) loan agreements are underfunded by \$12,503. This deficiency resulted from not making scheduled deposits to the reserve and from transfers to the operating account to make loan payments on several debt obligations. Such disbursements do not meet the criteria for appropriate withdrawals indicated by the (KIA) loan agreements.

The Depreciation Reserve Funds Required by USDA-Rural Development (RD) loan requirements are underfunded by \$11,355. This deficiency resulted from not making scheduled deposits to the reserve and from transfers to the operating account to make loan payments on several debt obligations. Such disbursements do not meet the criteria for appropriate withdrawals indicated by the (RD) loan agreements.

Mountain Water's management stated during the field work that there is verbal agreement to transfer \$11,000 to Kentucky Infrastructure Authority reserves and \$9,000 monthly to Rural Development Reserves until the deficit is made up. These payments were transferred during 2015.

**MOUNTAIN WATER DISTRICT**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**DECEMBER 31, 2015 AND 2014**

**11 RESTRICTED ASSETS AND RESERVE NET ASSETS Continued)**

The USDA-Rural Development (RD) loan agreements also include a requirement for an Operation and Maintenance Fund. The funding of this reserve is secondary to the Depreciation Reserve Funds.

**12. BONDS PAYABLE**

	<u>2015</u>	<u>2014</u>
Shelby Waste Water Project Fund The 4.125% sewer system revenue bonds issued July 22, 2005 in the original amount of \$740,000 are payable to USDA-Rural Development to the year 2045. The bonds are secured by a statutory Mortgage lien on the utility plant service and a pledge of all water revenues from the system	\$657,000	\$668,000
Phelps Waste Water Project Bond The 4.5% sewer system revenue bonds issued October 23, 2003 in the original amount of \$426,000 are payable to USDA-Rural Development to the year 2043. The bonds are secured by a statutory mortgage lien on the utility plant in service and a pledge of all water revenues from the system.	\$ 371,000	\$377,500
Feds creek Project The 3.5% revenue bonds issued July 2002 in the original amount of \$800,000 are payable to USDA-Rural Development to the year 2035. The bonds are secured by a secondary statutory mortgage lien on the utility plant in service and a pledge of all water revenues from the system.	\$658,000	\$673,000
Johns Creek The 4.125% revenue bonds issued November 2005 in the original amount of \$1,650,000 are payable to USDA-Rural Development to the year 2027. The bonds are secured by a secondary statutory mortgage lien on the utility plant in service and a pledge of all water revenues from the system.	\$1,489,000	\$1,512,000

**MOUNTAIN WATER DISTRICT**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**DECEMBER 31, 2015 AND 2014**

**12 BONDS PAYABLE (Continued)**

	<u>2014</u>	<u>2013</u>
Russell Fork Water Plant Project		
The 4.5% revenue bonds issued April 2009 in the original amount of \$650,000 are payable to USDA-Rural Development to the year 2047. The bonds are secured by a secondary statutory mortgage lien on the utility plant in service and pledge of all water revenue from the system.	\$ 613,000	\$ 621,000
Total bonds	\$3,788,000	\$ 3,851,500
Less current portion	(66,500)	(63,500)
Long Term Bonds Payable	<u>\$3,721,500</u>	<u>\$3,788,000</u>

Maturities of these long-term bonds are as follows:

	Principal	Interest
2016	66,500	153,038
2017	70,000	150,327
2018	73,000	147,461
2019	76,000	144,494
2020	78,500	141,293
2021-2025	447,000	657,076
2026-2030	548,500	562,686
2031-2035	676,000	430,810
2036-2040	832,000	282,536
2041-2045	821,500	103,548
2046-2050	99,000	9,000
	<u>\$3,788,000</u>	<u>\$2,782,269</u>

**13. NOTES PAYABLE AND CAPITAL LEASES**

	<u>2015</u>	<u>2014</u>
Kentucky Rural Water Finance Corporation		
The 3.14% note issued August 2012 in the original amount of \$6,270,000, payable in monthly installments, with payments through August 2039, secured by water revenues from the system.	\$ 5,400,000	\$ 5,755,000
Kentucky Infrastructure Authority-Multi-Area		
The 2.9% note issued June 1994 in the original Amount of \$5,165,093, payable in semi-annual Installments of \$129,479, with payments through the year 2023, secured by water revenues from the system.	1,837,105	2,038,399

**MOUNTAIN WATER DISTRICT**  
**NOTES TO THE FINANCIAL STATEMENT**  
**DECEMBER 31, 2015 AND 2014**

**13 NOTES PAYABLE AND CAPITAL LEASES (Continued)**

	<u>2015</u>	<u>2014</u>
Kentucky Infrastructure Authority-Indian Creek The 3% note issued June 1994 in the original amount of \$377,760, payable in semi-annual installments of \$8,577, with payments through the year 2023, secured by water revenue from the system.	121,202	134,422
Kentucky Infrastructure Authority-F01-07 The 1.8% note issued January 2002 in the original amount of \$1,197,072 payable in semi-annual of \$35,769, with payments through the year 20024 secured by water revenues from the system.	561,508	622,119
Kentucky Infrastructure Authority A03-06 The 1% note issued June 2004 in the original Amount of \$226,776, payable in semi-annual Installments of \$6,846 with payments through the year 2023, secured by water revenues from the system.	87,684	96,950
Kentucky Infrastructure Authority A209-32 The 1% note issued January 2010 in the original amount of \$750,000 with \$390,750 in principle forgiveness, payable in semi-annual installments of \$5,212, with payments through the year 2031, secured by water revenues from the system.	290,830	308,094
<u>US Bank</u> Loan to finance rate study, original balance \$149,956 at 2.9% interest; payments are \$6,441 for 24 months, maturing December 2017.	149,956	-0-
<u>Community Trust Bank</u> A purchase agreement, original balance \$20,710 at 3.36% interest, secured by vehicle; payments are \$462 for 48 months, maturing November 2015	-0-	4,818

**MOUNTAIN WATER DISTRICT**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**DECEMBER 31, 2015 AND 2014**

**13 NOTES PAYABLE AND CAPITAL LEASES (Continued)**

	<u>2015</u>	<u>2014</u>
<u>Community Trust Bank</u>		
A purchase agreement, original balance \$30,105 at 4.75% interest; secured by vehicle; payments are \$690 for 45 months maturing July 2015.	-0-	4,083
<u>Community Trust Bank</u>		
A purchase agreement, original balance \$30,105 at 4.75% interest; secured by vehicle; payments are \$690 for 48 months maturing July 2015	-0-	4,014
<u>US Bank</u>		
Loan to finance Big Fork Project, original balance \$272,145 at 3.1% interest; payments are \$4,153 beginning June 26, 2016 for 24 months, maturing December 2017.	27,428	-0-
<u>Community Trust Bank</u>		
A lease purchase agreement, original balance \$34,625; at 3.99% interest; secured by a vehicle; Payments are \$638 for 23 months and a final Balloon payment of \$22,246, maturing April 2014.	9,873	16,979
<u>Community Trust Bank</u>		
A lease purchase agreement, original balance \$29,119; at 2.01% interest; secured by a vehicle; Payments are \$658 for 48 months and a final maturing June 2020.	25,163	-0-
<u>Community Trust Bank</u>		
A lease purchase agreement, original balance \$20,772; at 3.035% interest; secured by a vehicle; Payments are \$460 for 48 months and a final Balloon payment of \$22,246, maturing June 2018.	13,276	18,312
<u>Community Trust Bank</u>		
A lease purchase agreement, original balance \$27,256; at 3.99% interest; secured by vehicle; payments are \$503 for 23 months with a final balloon payment of \$17,511, maturing May 2014.	8,269	13,840

**MOUNTAIN WATER DISTRICT**  
**NOTES TO THE FINANCIAL STATEMENT**  
**DECEMBER 31, 2015 AND 2014**

**13 NOTES PAYABLE AND CAPITAL LEASES (Continued)**

Community Trust Bank

A lease purchase agreement, original balance \$20,772; at 3.035% interest; secured by a vehicle; Payments are \$460 for 48 months and a final Balloon payment of \$22,246, maturing June 2018. 13,276      18,312

Community Trust Bank

A lease purchase agreement, original balance \$20,772; at 3.035% interest; secured by a vehicle; Payments are \$460 for 18 months and a final Balloon payment of \$22,246, maturing June 2018. 13,276      18,312

Community Trust Bank

A lease purchase agreement, original balance \$27,580; at 3.99% interest; secured by a vehicle; payments are \$623 for 23 months with a final balloon payment of \$14,970, maturing September 2014. 4,998      12,486

Community Trust Bank

A lease purchase agreement, original balance \$20,039; at 3.99% interest; secured by a vehicle; Payments are \$453 for 23 months with a final balloon payment of \$13,294, maturing May 2015. 7,475      12,946

Total Notes Payable	8,571,319	9,079,076
Less current portion	(820,758)	(714,056)
Total Line term Debt	<u>\$7,750,561</u>	<u>\$8,365,030</u>

Maturity of the long term debt and capital leases are as follows:

	Principal	Interest
2015	\$ 820,758	\$ 100,688
2016	795,283	88,814
2017	718,041	77,582
2018	722,991	67,524
2019	671,360	56,841
2020-2024	2,328,585	139,408
2025-2029	1,307,450	55,146
2030-2034	759,683	24,183
2035-2039	<u>447,168</u>	<u>5,701</u>
	<u>\$8,571,319</u>	<u>\$615,887</u>

**MOUNTAIN WATER DISTRICT**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**DECEMBER 31, 2015 AND 2014**

**14. ADVANCES FOR CONSTRUCTION**

**Water Projects**

Bad Fork	
Abandoned Mine Land	\$ 445,751
In House Projects	1,359,078
Pompey	47,488
PW220	18,315
Pump Booster	193,900
Phelps High	119,815
Big Creek	27,158
Tank Rehabilitation	
Coal Severance	901,889

**Sewer Projects**

Phelps Waste Water	
Kentucky Infrastructure Authority	57,110
Douglas WTP	
LGEDF Funds	104,842
Henry Clay Sewer Projects:	
COE Section 531	45,391
LGEDF Funds	92,641
Belfry Pond	
Coal Severance	<u>582,982</u>

<b><u>Total Advances for Construction</u></b>	<b><u>\$3,996,360</u></b>
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**MOUNTAIN WATER DISTRICT**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**DECEMBER 31, 2014 AND 2013**

**15. MANAGEMENT SERVICE AGREEMENT**

In January, 2011 the District entered into another five (5) year agreement with a management service company to manage the daily operations, water facilities and waste water facilities for the District. Each period during the term commencing January 1 and ending the following December 31 shall be referred to as an "Agreement Year". Either party shall have the right, without cause, to terminate the agreement at the end of the third agreement year. Notice of termination shall be given in writing no less than 120 days in advance of the effective date of termination. The management service company compensation under the agreement shall consist of an annual fee. The annual fee for the first year, which shall be the period January 1, 2011 through December 31, 2011, shall be \$7,632,000. The annual fee shall be adjusted annually to provide that management service company will be paid 70% of the increase in total operating revenue based on the District's two most recent prior year's audits. If the annual revenue decreases, there will likewise be a downward adjustment in the fee based on the same ratio. Included in the annual fee is the allowance for maintenance and repair, which shall initially be \$564,000. The maintenance and repair budget shall adjust annually in direct proportion with any adjustment in the annual fee.

On March 27, 2014 the District renewed another three (3) year agreement with a management service company to manage the daily operations, water facilities and waste water facilities for the District. Each period during the term commencing January 1 and ending the following December 31 shall be referred to as an "Agreement Year". Either party shall have the right, without cause, to terminate the agreement at the end of the third agreement year. Notice of termination shall be given in writing no less than 120 days in advance of the effective date of termination. The management service company compensation under the agreement shall consist of an annual fee. The annual fee for the first year, which shall be the period January 1, 2014 through December 31, 2014, shall be \$7,680,850. The annual fee for 2015 and 2016, shall be \$7,757,660.

Total management fees paid for this service for the year ended December 31, 2015 were \$7,750,896 less certain expenses assumed by the management service company totaling \$158,565, resulting in net payment of \$7,592,896.

In July 2016 Mountain Water District Board effectively terminated the contracts with the management service company. An agreement was made for Mountain Water to pay the management service Company \$50,000 per month through March 2016 then \$100,000 monthly until the balance is paid off. In these financial statements \$1,050,000 has been shown as short term with \$974,138 long term to paid during 2017 per agreement.

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**INDEPENDENT AUDITOR'S REPORT**

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

Board of Commissioners  
Mountain Water District  
Pikeville, KY

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 statement of the business type activities of Mountain Water District as of and for the year December 31, 2015, and the related notes to the financial statements, which collectively comprise Mountain Water District's basic financial statements and have issued my report thereon dated September 19, 2016.

**Internal Control Over Financial Reporting**

In planning and performing my audit of the financial statements, I considered Mountain Water 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 Mountain Water District's internal control.

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

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. 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.

### **Compliance and Other Matters**

As part of obtaining reasonable assurance about whether Mountain Water District's financial statements are free from material misstatement, I performed test 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.

### **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 to that testing; and not to provide an opinion on the effectiveness of the organization'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 organization's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.



Richard F. Paulmann, CPA, LLC.  
Pewee Valley, KY  
September 19, 2016