HARDIN COUNTY WATER DISTRICT NO. 2

INDEPENDENT AUDITOR'S REPORT
ON FINANCIAL STATEMENTS
AND SUPPLEMENTARY INFORMATION

YEARS ENDED DECEMBER 31, 2017 AND 2016

HARDIN COUNTY WATER DISTRICT NO. 2

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YEARS ENDED DECEMBER 31, 2017 AND 2016

HARDIN COUNTY WATER DISTRICT NO. 2

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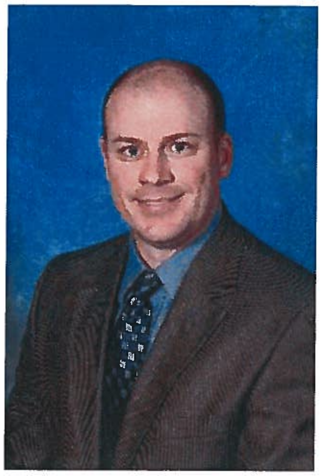
YEARS ENDED DECEMBER 31, 2017 AND 2016

LETTER OF TRANSMITTAL

A Message from the General Manager



I am pleased to submit the Annual Report for Hardin County Water District No. 2 for the year ending December 31, 2017. Years of long range planning have come to fruition and 2017 was the year of successful completions.

At our water treatment plants, the secondary disinfectant conversion was put to the test and the District celebrated one full year of chloramine treatment on November 30, 2016. The time since has been marked by fewer taste and odor complaints, and disinfectant by-products measuring at half of historic levels. In addition, the District continues its long tradition of "Best Tasting Water" championships. We claimed the 2017 AWWA "Best Tasting Water" title and placed second at the KRWA competition. These results confirm the District's commitment to providing the best product for our customers, before and after the chloramine conversion.

The successful chloramine conversion paved the way for the connection with Louisville Water Company and the purchase of supplemental water supplies. The pipeline and pump station project were completed in May 2017, and Hardin County began purchasing water from Louisville Water Company that month. For 2017, we will receive about 8% of our water supply from this source, and it will grow to about 18% by 2021. This completes the supplemental water supply project that began in 2008. We have plenty of water to supply the next generation.

The District still enjoys some of the best business metrics in the state. As the second largest water district in Kentucky, we still have water rates that are approximately 25% below the Kentucky Public Service Commission average. We maintain a Moody's Bond Rating of Aa2; also the best in the state for the same class; and managed a record $14 million operations budget.

The District's first wastewater project reached a major mile stone during 2017. After years of procurement, the District was successful in obtaining all required approvals to proceed with construction of the $12.2M wastewater collection system that will service the community of Glendale, Glendale Junction, and the Industrial Park. The contracts have a 14-month completion target, and the District could be offering wastewater services to the public as early as 2019.

The year was also marked by very aggressive advances in the District's general administration. In 2017, the company moved from fully insured health insurance to a partially self-funded health care plan for the employee base. This implementation was coupled with a wellness plan that became effective January 1 of 2018. Additional advances were made in payroll software, asset management, and accounting software. As the District grows, we see more opportunities to leverage our size in order to control costs for our customers.

Also in this report, the auditor's financial statements will reflect an increase in revenue of 4.1%. This increase is driven by the final rate increase for the Elizabethtown customer base that saw its last transition to District rates on July 1, 2017. The operational margin of the District came in at a healthy 23% compared to 25% the previous year. Given that our wholesale water purchase for the first year of the contract entered the expense column at over $300,000, the fiscal management of the District remains under tight control. Our operation margin is still one of the best in Kentucky.

At the close of each passing year, I reflect on the accomplishments of the company and wonder if it's possible for Hardin County Water District No. 2 to experience any higher levels of success. Each year, the news seems to top the year before. I contribute the success of 2017 to the unwavering spirit and zeal of the professionals who run the company each and every day. Hardin County Water District No. 2 has the best employees servicing our community.

The future still looks bright.

James R. Jeffries

James R. Jeffries
General Manager

INDEPENDENT AUDITOR'S REPORT

CHRIS R. CARTER, CPA
ANN M. FISHER, CPA
SCOTT KISSELBAUGH, CPA
PHILIP A. LOGSDON, CPA
BRIAN S. WOOSLEY, CPA

STILES, CARTER & ASSOCIATES
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INDEPENDENT AUDITOR'S REPORT

Board of Commissioners
Hardin County Water District No. 2
Elizabethtown, Kentucky

Report on the Financial Statements

We have audited the accompanying financial statements of Hardin County Water District No. 2 as of and for the years ended December 31, 2017 and 2016, and the related notes to the financial statements, which collectively comprise the District's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

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

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

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Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of Hardin County Water District No. 2, as of December 31, 2017 and 2016, and the respective changes in financial position and cash flows, thereof for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Emphasis of a Matter

As discussed in Note 1 to the financial statements, during the year ended December 31, 2017, the District adopted Governmental Accounting Standards Board Statement 73, *Accounting and Financial Reporting for Pensions and Related Assets That Are Not Within the Scope of GASB Statement 68, and Amendments to Certain Provisions of GASB Statements 67 and 68,* Statement 80, *Blending Requirements for Certain Component Units – An Amendment of GASB Statement 14,* Statement 81, *Irrevocable Split-Interest Agreements* and Statement 82, *Pension Issues – An Amendment of GASB Statements No. 67, No. 68 and No. 72.* Our opinion is not modified with respect to this matter.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 5 to 9, schedule of proportionate share of the net pension liability on page 32 and schedule of contributions on page 33 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information

Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise the Hardin County Water District No. 2's basic financial statements. Schedules I, II, IV, V, VI and VII are presented for purposes of additional analysis and are not a required part of the basic financial statements. The schedule of expenditures of federal awards is presented for purposes of additional analysis as required by Title 2 U.S. *Code of Federal Regulations (CFR) Part 200, Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards*, and is also not a required part of the basic financial statements.

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

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

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated June 12, 2018, on our consideration of Hardin County Water District No. 2's 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 Hardin County Water District No. 2's internal control over financial reporting and compliance.

Stiles, Carter & Associates
Certified Public Accountants
Elizabethtown, Kentucky
June 12, 2018

REQUIRED SUPPLEMENTARY INFORMATION

HARDIN COUNTY WATER DISTRICT NO. 2
MANAGEMENT'S DISCUSSION AND ANALYSIS (MD&A)
YEAR ENDED DECEMBER 31, 2017

The discussion and analysis of Hardin County Water District No. 2's financial performance provides an overall review of the District's financial activities for the year ended December 31, 2017. The intent of this discussion and analysis is to review the District's financial performance as a whole. Readers should also review the basic financial statements and notes to the basic financial statements to enhance their understanding of the District's financial performance.

FINANCIAL HIGHLIGHTS

- The ending cash and investment balance for the District was $22.6 million. The balance at December 31, 2016, was $20.4 million. This reflects an increase in cash and investments during the year of $2.2 million.

- The District continued capital construction projects to improve the water system and ensure the future water supply.

- The District created a Sewer Division to develop and construct a sewer service in the Glendale area.

- The District invested approximately $4.7 million in capital assets during the year.

USING THIS ANNUAL REPORT

The basic financial statements report information about the District using full accrual accounting methods as utilized by similar business activities in the private sector. The basic financial statements include a statement of net position; a statement of revenues, expenses, and changes in fund net position; a statement of cash flows; and notes to the basic financial statements.

The ***statement of net position*** presents the financial position of the District on a full accrual historical cost basis. The statement presents information on all of the District's assets, deferred outflows of resources and liabilities and deferred inflows of resources, with the difference reported as net position. Over time, increases and decreases in net position are one indicator of whether the financial position of the District is improving or deteriorating.

While the statement of net position provides information about the nature and amount of resources and obligations at year-end, the ***statement of revenues, expenses, and changes in fund net position*** presents the results of the District's activities over the course of the fiscal year and information as to how the net position changed during the year. All changes in net position are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of the related cash flows. This statement also provides certain information about the District's recovery of its costs. Rate setting policies use different methods of cost recovery not fully provided for by generally accepted accounting principles. The primary objectives of the rate model are to improve equity among customer classes and to ensure that capital costs are allocated on the basis of long-term capacity needs, ensuring that growth pays for growth.

The ***statement of cash flows*** presents changes in cash and cash equivalents, resulting from operational, financing, and investing activities. This statement presents cash receipts and cash disbursement information, without consideration of the earnings event, when an obligation arises, or depreciation of capital assets.

The ***notes to the basic financial statements*** provide required disclosures and other information that are essential to a full understanding of material data provided in the statements. The notes present information about the District's accounting policies, significant account balances and activities, material risks, obligations, commitments, contingencies and subsequent events, if any.

ENTITY-WIDE FINANCIAL ANAYLSIS

Net position may serve over time as a useful indicator of a government's financial position. In the case of the District, assets and deferred outflows exceeded liabilities and deferred inflows by $77.1 million and $73.1 million as of December 31, 2017 and 2016.

The largest portion of the District's net position reflects its investment in infrastructure and capital assets (e.g., land, buildings, vehicles, equipment, transmission and distribution systems and construction in progress), less any related debt used to acquire those assets that is outstanding. The District uses these capital assets to provide services to its customers; consequently, these assets are not available for future spending. Although the District's investment in its capital assets is reported net of related debt, it should be noted that the resources needed to repay this debt must be provided from other sources, since the capital assets themselves cannot be used to liquidate these liabilities.

The District's financial position is the product of several financial transactions including the net results of activities, the acquisition and payment of debt, the acquisition and disposal of capital assets, and the depreciation of capital assets.

(Table 1)
Summary of Net Position
as of December 31, 2017 and 2016

	2017	2016
Assets		
Current and Other Assets	$ 30,341,529	$ 27,192,922
Capital Assets	73,379,493	71,638,003
Total Assets	103,721,022	98,830,925
Deferred Outflows of Resources	2,961,747	1,947,965
Liabilities		
Long-term liabilities	25,833,444	25,241,978
Other Liabilities	3,074,597	2,437,404
Total Liabilities	28,908,041	27,679,382
Deferred Inflows of Resources	697,071	-
Net Position		
Net investment in capital assets	54,007,148	51,753,510
Restricted	5,941,474	4,266,820
Unrestricted	17,129,035	17,079,178
Total Net Position	$ 77,077,657	$ 73,099,508

Unrestricted net position, the portion of net position that can be used to finance day-to-day operations (without constraints established by debt covenants, enabling legislation or other legal requirements), increased $50 thousand (.29%) at December 31, 2017. Restricted net position increased $1.7 million (39.25%). Net investment in capital assets increased by $2.3 million (4.35%).

(Table 2)
Changes in Net Position
Years Ended December 31, 2017 and 2016

	2017	2016
OPERATING REVENUES:		
Water sales	$ 13,040,102	$ 12,512,174
Other operating income	838,780	820,005
Total operating revenues	13,878,882	13,332,179
OPERATING EXPENSES:		
Power purchased	808,028	822,983
Purchased water	302,321.00	-
Pumping and treatment labor	1,291,392	1,007,379
Purification supplies and expense	336,357	556,493
Transmission and distribution labor	1,690,446	1,525,723
Transmission and distribution supplies and expense	224,722	242,028
Transmission and distribution maintenance and repairs	72,390	54,476
Equipment rental	5,014	5,131
Transportation expense	151,224	154,429
Water treatment maintenance and expense	176,574	152,360
General and administrative expenses	2,674,988	2,711,567
Depreciation	2,935,452	2,768,074
Total operating expenses	10,668,908	10,000,643
OPERATING INCOME	3,209,974	3,331,536
NON-OPERATING REVENUES (EXPENSES):		
Investment income	558,735	384,592
Other income	146,768	179,376
Gain (loss) on disposal of capital assets	33,075	8,607
Bond issuance costs	-	(120,614)
Interest expense on long-term debt	(573,693)	(706,250)
Interest expense on customer deposits	-	(295)
Amortization of bond discount and utility acquisition	(27,938)	(31,855)
TOTAL NON-OPERATING REVENUES (EXPENSES)	136,947	(286,439)
Capital contributions	631,228	6,326,795
Increase in net position	3,978,149	9,371,892
Net position, beginning	73,099,508	63,727,616
Net position, ending	$ 77,077,657	$ 73,099,508

Operating revenue increased 4% as compared to the prior year as new customers were added. Total operating expenses increased 6.7%, which was due to increased depreciation expense and operating costs for personnel. Interest expense on long-term debt declined 18.8 percent due to the bond refunding in calendar year 2016. The District continues to receive capital contributions through the State of Kentucky, the Federal government, other governments and individual developers.

Capital Assets and Debt Administration

Capital Assets

At December 31, 2017 and 2016, the District had $73.4 million and $71.6 million invested in a variety of capital assets, as reflected in the following table:

(Table 3)
Capital Assets (Net of Depreciation)
as of December 31, 2017 and 2016

	2017	2016
Non-Depreciable Assets:		
Land and land rights	$ 2,171,632	$ 2,137,632
Depreciable Assets:		
Structures and improvements	6,413,261	7,574,490
Property held for future use	1,143,284	1,173,044
Supply mains	592,263	706,168
Water treatment plant	9,611,628	7,082,438
Standpipes, tanks and foundations	7,667,662	7,755,219
Transmission and distribution mains	35,523,040	28,565,091
Services and meters	5,995,030	6,200,302
Hydrants	36,123	44,972
Office furniture and fixtures	139,949	133,532
Transportation equipment	671,562	618,310
Other property and equipment	217,759	202,798
Capital assets in service	70,183,193	62,193,996
Construction in progress	3,196,300	9,444,007
Total capital assets, net of depreciation	$ 73,379,493	$ 71,638,003

(Table 4)
Changes in Capital Assets
Years Ended December 31, 2017 and 2016

	2017	2016
Beginning balance	$ 71,638,003	$ 62,638,515
Additions	14,632,991	12,678,743
Retirements	(9,956,049)	(911,181)
Depreciation	(2,935,452)	(2,768,074)
Ending balance	$ 73,379,493	$ 71,638,003

Debt

At December 31, 2017 and 2016, the District had $13.5 million and $14.3 million, in revenue bonds outstanding and $5.4 million and $5.6 million of notes payable. A total of $1.1 million is due within the 2018 calendar year.

(Table 5)
Outstanding Debt
as of December 31, 2017 and 2016

	2017	2016
Revenue bonds	$ 13,465,000	$ 14,320,000
Notes payable	5,376,227	5,621,906
Unamortized discount/premium	133,969	146,786
	$ 18,975,196	$ 20,088,692

District Challenges for the Future

The District continues to be financially sound. However, the current state and national financial climate requires the District to remain prudent.

The District will continue to use careful planning and monitoring of finances to provide quality services to its customers.

Contacting the District's Financial Management

This financial report is designed to provide our customers, investors and creditors with a general overview of the District's finances and to show the District's accountability for the money it receives and spends. If you have questions about this report or need additional financial information, contact James Jeffries, General Manager, 360 Ring Road, Elizabethtown, Kentucky 42701, (270) 737-1056.

BASIC FINANCIAL STATEMENTS

HARDIN COUNTY WATER DISTRICT NO. 2

STATEMENTS OF NET POSITION

DECEMBER 31, 2017 AND 2016

	2017	2016
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	$ 3,183,375	$ 3,320,204
Investments	13,264,952	12,805,317
Accounts receivable, net	1,568,803	1,433,412
State grants receivable	136,805	476,002
Materials and supplies	427,034	511,382
TOTAL CURRENT ASSETS	18,580,969	18,546,317
NONCURRENT ASSETS:		
Restricted cash and cash equivalents	4,905,847	3,089,426
Restricted investments	1,207,394	1,207,394
Regulatory asset on CERS pension	5,647,319	4,349,785
Non-depreciable capital assets	5,367,932	11,581,639
Depreciable capital assets, net of accumulated depreciation	68,011,561	60,056,364
TOTAL NONCURRENT ASSETS	85,140,053	80,284,608
TOTAL ASSETS	103,721,022	98,830,925
DEFERRED OUTFLOWS OF RESOURCES		
Deferred amount on debt refundings	187,324	218,350
Deferred amount on CERS pension	2,609,006	1,554,468
Utility acquisition adjustments	165,417	175,147
TOTAL DEFERRED OUTFLOWS OF RESOURCES	2,961,747	1,947,965
LIABILITIES		
CURRENT LIABILITIES:		
Accounts payable	166,419	158,753
Construction projects payable	584,473	14,149
Elizabethtown sewer payable	749,478	720,357
Accrued taxes	62,754	54,703
Accrued liabilities	87,939	75,898
Accrued vacation	178,148	155,245
Customer deposits	45,713	43,008
Customer advances for construction	87,250	77,250
Bonds payable	860,000	855,000
Notes payable	252,423	283,041
TOTAL CURRENT LIABILITIES	3,074,597	2,437,404
NONCURRENT LIABILITIES:		
Customer deposits	411,417	387,072
Net pension liability - CERS	7,559,254	5,904,253
Bonds payable	12,738,969	13,611,788
Notes payable	5,123,804	5,338,865
TOTAL NONCURRENT LIABILITIES	25,833,444	25,241,978
TOTAL LIABILITIES	28,908,041	27,679,382
DEFERRED INFLOWS OF RESOURCES		
Deferred amount on CERS pension	697,071	-
TOTAL DEFERRED INFLOWS OF RESOURCES	697,071	-
NET POSITION		
Net investment in capital assets	54,007,148	51,753,510
Restricted for debt service	2,408,756	2,397,776
Restricted for capital projects	3,100,525	1,370,549
Restricted for customers	432,193	498,495
Unrestricted	17,129,035	17,079,178
TOTAL NET POSITION	$ 77,077,657	$ 73,099,508

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

HARDIN COUNTY WATER DISTRICT NO. 2

STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN FUND NET POSITION

YEARS ENDED DECEMBER 31, 2017 AND 2016

	2017	2016
OPERATING REVENUES:		
Water sales	13,040,102	$ 12,512,174
Other operating income	838,780	820,005
TOTAL OPERATING REVENUES	13,878,882	13,332,179
OPERATING EXPENSES:		
Power purchased	808,028	822,983
Purchased water	302,321.00	-
Pumping and treatment labor	1,291,392	1,007,379
Purification supplies and expense	336,357	556,493
Transmission and distribution labor	1,690,446	1,525,723
Transmission and distribution supplies and expense	224,722	242,028
Transmission and distribution maintenance and repairs	72,390	54,476
Equipment rental	5,014	5,131
Transportation expense	151,224	154,429
Water treatment maintenance and expense	176,574	152,360
General and administrative expenses	2,674,988	2,711,567
Depreciation	2,935,452	2,768,074
TOTAL OPERATING EXPENSES	10,668,908	10,000,643
OPERATING INCOME	3,209,974	3,331,536
NON-OPERATING REVENUES (EXPENSES):		
Investment income	558,735	384,592
Other income	146,768	179,376
Gain on disposal of capital assets	33,075	8,607
Bond issuance costs	-	(120,614)
Interest expense on long-term debt	(573,693)	(706,250)
Interest expense on customer deposits	-	(295)
Amortization of bond discount and utility acquisition	(27,938)	(31,855)
TOTAL NON-OPERATING REVENUES (EXPENSES)	136,947	(286,439)
CAPITAL CONTRIBUTIONS	631,228	6,326,795
CHANGE IN NET POSITION	3,978,149	9,371,892
NET POSITION, beginning of year, as restated	73,099,508	63,727,616
NET POSITION, end of year	$ 77,077,657	$ 73,099,508

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

HARDIN COUNTY WATER DISTRICT NO. 2

STATEMENTS OF CASH FLOWS

YEARS ENDED DECEMBER 31, 2017 AND 2016

	2017	2016
CASH FLOWS FROM OPERATING ACTIVITIES:		
Receipts from customers	$ 13,743,491	$ 13,038,302
Payments to suppliers	(3,641,076)	(3,288,324)
Payments to employees	(3,937,542)	(3,182,601)
NET CASH PROVIDED BY OPERATING ACTIVITIES	6,164,873	6,567,377
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES:		
Principal payments on bonds	(855,000)	(5,633,000)
Proceeds from bonds	-	4,805,917
Principal payments on notes	(245,679)	(239,115)
Acquisition of capital assets	(4,072,151)	(12,082,942)
Contributions in aid of construction	980,425	5,850,793
Interest on long-term debt	(573,693)	(706,250)
Sale of capital assets	34,949	8,607
Customer deposit interest	-	(295)
NET CASH USED BY CAPITAL AND RELATED FINANCING ACTIVITIES	(4,731,149)	(7,996,285)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Sale (purchase) of investments	(454,762)	1,931,397
Other income	146,768	179,376
Investment income	553,862	557,511
NET CASH PROVIDED BY INVESTING ACTIVITIES	245,868	2,668,284
NET INCREASE IN CASH AND CASH EQUIVALENTS	1,679,592	1,239,376
CASH AND CASH EQUIVALENTS, beginning of year	6,409,630	5,170,254
CASH AND CASH EQUIVALENTS, end of year	$ 8,089,222	$ 6,409,630
RECONCILIATION OF OPERATING INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES:		
Operating income	$ 3,209,974	$ 3,331,536
Adjustments to reconcile net operating income to net cash provided by operating activities:		
Depreciation	2,935,452	2,768,074
Provision for bad debts	48,006	37,690
(Increase) in accounts receivable	(135,391)	(293,877)
(Increase) in prepaids	-	50,000
Increase (decrease) in accounts payable	7,666	(2,132)
Increase in Elizabethtown sewer payable	29,121	720,357
Increase (decrease) in customer deposits	27,050	(66,631)
Increase (decrease) in accrued taxes payable	8,051	(18,664)
Increase in accrued liabilities	12,041	9,047
Increase in accrued vacation	22,903	31,977
NET CASH PROVIDED BY OPERATING ACTIVITIES	$ 6,164,873	$ 6,567,377

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

NOTES TO BASIC FINANCIAL STATEMENTS

HARDIN COUNTY WATER DISTRICT NO. 2

NOTES TO FINANCIAL STATEMENTS

DECEMBER 31, 2017 AND 2016

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Brief history - The Hardin County Water District No. 2 was organized pursuant to the provisions of Kentucky Revised Statutes KRS 74.010 and KRS 44.020 in order to provide a water supply for the residents of Hardin County, Kentucky. During the year ended December 31, 2017, the District established a sewer division. The anticipation is that the District will supply sewer service by the end of 2018.

The District's financial statements are prepared in accordance with generally accepted accounting principles (GAAP). The Governmental Accounting Standards Board (GASB) is responsible for establishing GAAP for state and local governments through its pronouncements (Statements and Interpretations). The District follows the accounting policies and procedures set forth by the National Association of Regulatory Utility Commissioners and the guidance provided by the American Water Works Association in *Water Utility Accounting* and is regulated by the Kentucky Public Service Commission. The more significant accounting policies established in GAAP and used by the District are discussed below.

A. REPORTING ENTITY

These financial statements present the District's financial activities. As defined by GASB No. 14, *The Financial Reporting Entity,* as amended by GASB No. 39, *Determining Whether Certain Organizations Are Component Units* the criteria for inclusion in the reporting entity involve those cases where the District or its officials appoint a voting majority of an organization's governing body, and is either able to impose its will on the organization or there is a potential for the organization to provide specific financial benefits to or to impose specific financial burdens on the District or the nature and significance of the relationship between the District and the organization is such that exclusion would cause the District's financial statements to be incomplete. Applying this definition, the District does not include any component units in its reporting entity.

B. BASIC FINANCIAL STATEMENTS

All activities of the District are accounted for within a single proprietary (enterprise) fund. The focus of proprietary fund measurement is upon determination of operating income, changes in net position, financial position, and cash flows. The GAAP applicable are those similar to businesses in the private sector. Enterprise funds are required to be used to account for operations for which a fee is charged to external users for goods or services and the activity is financed with debt that is solely secured by a pledge of the net revenues.

C. BASIS OF ACCOUNTING

Basis of accounting refers to the point at which revenues or expenses are recognized in the accounts and reported in the financial statements. It relates to the timing of the measurements made regardless of the measurement focus applied. The proprietary fund financial statements are presented on the accrual basis of accounting. Nonexchange revenues, including intergovernmental revenues and grants, are reported when all eligibility requirements have been met. Fees and charges and other exchange revenues are recognized when earned and expenses are recognized when incurred. Because the District's rates are regulated by the Kentucky Public Service Commission the District accounts for the financial effects of regulation in accordance with

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Governmental Accounting Standards Board (GASB) Statement No. 62, Paragraphs 476-500, Regulated Operations. Accordingly, certain costs and income may be capitalized as a regulatory asset or liability that would otherwise be charged to expense or revenues. Regulatory assets and liabilities are recorded when it is probable that future rates will permit recovery.

D. FINANCIAL STATEMENT AMOUNTS

1. Cash and investments – The District's cash balances are held at multiple financial institutions. Investments are stated at fair value based on quoted market prices.

2. Cash and cash equivalents – The District has defined cash and cash equivalents to include cash on hand and demand deposits. The District considers all highly liquid debt instruments (including restricted assets) purchased with a maturity of three months or less to be cash equivalents.

3. Restricted Assets – Restricted assets consist of demand deposit savings accounts and certificates of deposit. The cost basis approximates market value.

4. Materials and supplies – Materials and supplies is composed of items used in the capital construction process.

5. Accounts Receivable - The allowance method is used to record uncollectible accounts.- At December 31, 2017 and 2016, accounts receivable was stated net of an allowance for uncollectible accounts of $80,000 and $70,000. Bad debt expense for 2017 was $48,006 and 2016 was $37,960. The District does not believe there is any credit risk associated with these receivables due to the large customer base and small individual account balances.

6. Capital Assets – Capital assets in service and construction in progress with an original cost of $5,000 or more are recorded at historical cost, if purchased or constructed. Assets acquired through contributions from developers or other customers are capitalized at their estimated fair market value, if available, or at engineers' estimated fair market value or cost to construct at the date of the contribution. Maintenance and repairs, which do not significantly extend the value or life of property, plant and equipment, are expensed as incurred. Assets are depreciated on the straight-line method. Depreciation is calculated using the following estimated useful lives:

	Years
Source of supply equipment	15-50
Water treatment plant	10-40
Transmission and distribution systems	10-50
Equipment	3-20
Structures and improvements, including buildings	10-50
Office furniture, equipment and vehicles	3-20
Meters	10-20

7. Compensated absences – The District accrues unpaid vacation when earned by the employee.

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HARDIN COUNTY WATER DISTRICT NO. 2

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8. Defining Operating Revenues and Expenses – The District distinguishes between operating and non-operating revenue and expenses. Operating revenues and expenses consist of charges for services and the costs of providing those services, including depreciation and excluding interest cost. All other revenues and expenses are reported as non-operating.

9. Net Position – Net position is divided into three components:

    a. Net investment in capital assets – consist of the historical cost of capital assets less accumulated depreciation and less any debt that remains outstanding that was used to finance those assets.
    b. Restricted net position – consist of net position that is restricted by the District's creditors (for example, through debt covenants), by grantors (federal, state and local) and by other contributors.
    c. Unrestricted – all other net position is reported in this category.

10. Use of Restricted Resources – When an expense is incurred that can be paid using either restricted or unrestricted resources (net position), the District's policy is to first apply the expense toward restricted resources and then toward unrestricted resources.

11. Amortization – Bond discounts/premiums and deferred amounts on refundings are being amortized using the interest method over the life of each respective bond issue.

12. Capital Contributions – Contributions are recognized in the Statement of Revenues, Expenses and Changes in Fund Net Position when earned. Contributions include capacity fees, capital grants, and other supplemental support by other utilities and industrial customers and federal, state and local grants in support of system improvements.

13. Long-term Obligations – Long-term obligations are reported at face value, net of applicable premiums and discounts.

14. Use of Estimates - Preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

15. Restatement – Change in Accounting Principle – During the year ended December 31, 2016, the District adopted the provisions of GASB Statement No. 62, Paragraphs 476-500, Regulated Operations with respect to its participation in the County Employees Retirement System. The District presents comparative financial statements so the restatement was made through the December 31, 2015 amounts. The effect of the restatement was to record a regulatory asset of $3,121,693, a change to beginning net position of $3,050,465 and an increase in pension expense of $107,955 which was reflected through the change in net position.

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16. Pensions – For purposes of measuring the net pension liability, deferred outflows/inflows of resources, and pension expense, information about the fiduciary net position of the County Employees Retirement System (CERS) and additions to/deductions from CERS's fiduciary net position have been determined on the same basis as they are reported by CERS except that CERS's fiscal year end is June 30. For this purpose, plan contributions are recognized as of employer payroll paid dates and benefit payments and refunds are recognized when due and payable in accordance with the benefit terms. Investments are reported at fair value.

    The District's rates are regulated by the Kentucky Public Service Commission. In accordance with GASB Statement No. 62, Paragraphs 476-500, Regulated Operations, which requires that the effects of the rate-making process be recorded in the financial statements, the District has elected to record a regulatory asset for the net pension liability, deferred outflows of resources and deferred inflows of resources related to pensions. Accordingly, the District recognizes the actuarially determined contribution as the current year pension expense.

17. Impact Of Recently Issued Accounting Principles

    Recently Issued And Adopted Accounting Principles

    In June 2015, the GASB issued Statement 73, *Accounting and Financial Reporting for Pensions and Related Assets That Are Not Within the Scope of GASB Statement 68, and Amendments to Certain Provisions of GASB Statements 67 and 68*. This statement is effective for periods beginning after June 15, 2016. This statement was adopted during the year ended December 31, 2017 and did not have an impact on the District's financial statements.

    In January 2016, the GASB issued Statement 80, *Blending Requirements for Certain Component Units – An Amendment of GASB Statement 14.* This statement is effective for periods beginning after June 15, 2016. This statement was adopted during the year ended December 31, 2017 and did not have an impact on the District's financial statements.

    In March 2016, the GASB issued Statement 81, *Irrevocable Split-Interest Agreements*. This statement is effective for periods beginning after December 15, 2016. This statement was adopted during the year ended December 31, 2017 and did not have an impact on the District's financial statements.

    In March 2016, the GASB issued Statement 82, *Pension Issues – An Amendment of GASB Statements No. 67, No. 68 and No. 72*. This statement is effective for periods beginning after June 15, 2016 except for the requirements of the Statement for the selection of assumptions in a circumstance in which an employer's pension liability is measured as of a date other than the employer's most recent fiscal year-end. In that circumstance, the requirements for the selection of assumptions are effective for that employer in the first reporting period in which the measurement date of the pension liability is on or after June 15, 2017. This statement was adopted during the year ended December 31, 2017 and did not have an impact on the District's financial statements.

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Recently Issued Accounting Pronouncements

In June 2015, the GASB issued Statement 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*. This statement is effective for periods beginning after June 15, 2017. Management is currently evaluating the impact of the adoption of this statement on the District's financial statements.

In November 2016, the GASB issued Statement 83, *Certain Asset Retirement Obligations*. This statement is effective for periods beginning after June 15, 2018. Management is currently evaluating the impact of the adoption of this statement on the District's financial statements.

In January 2017, the GASB issued Statement 84, *Fiduciary Activities*. This statement is effective for periods beginning after December 15, 2018. Management is currently evaluating the impact of the adoption of this statement on the District's financial statements.

In March 2017, the GASB issued Statement 85, *Omnibus 2017*. This statement is effective for periods beginning after June 15, 2017. Management is currently evaluating the impact of the adoption of this statement on the District's financial statements.

In May 2017, the GASB issued Statement 86, *Certain Debt Extinguishment Issues*. This statement is effective for periods beginning after June 15, 2017. Management is currently evaluating the impact of the adoption of this statement on the District's financial statements.

In June 2017, the GASB issued Statement 87, *Leases*. This statement is effective for periods beginning after December 15, 2019. Management is currently evaluating the impact of the adoption of this statement on the District's financial statements.

In April 2018, the GASB issued Statement 88, *Certain Disclosures Related to Debt, including Direct Borrowings and Direct Placements*. This statement is effective for periods beginning after June 15, 2018. Management is currently evaluating the impact of the adoption of this statement on the District's financial statements.

NOTE 2 – ELIZABETHTOWN WATER SYSTEM ACQUISITION

On October 23, 2014, the Kentucky Public Service Commission approved an asset purchase agreement between the District and the City of Elizabethtown, Kentucky, for the District's purchase of certain water system assets of the City. The transaction closed on October 31, 2014. The agreement requires the District to pay a note to the City of $8,000,000 in twenty annual installments of $400,000 beginning in 2015. The note carries no specified interest rate, but interest was imputed at a rate of 2.745 percent resulting in a net principal amount of $6,093,748 and a resulting interest amount of $1,906,252 over the life of the note (See note 5). The assets acquired were recorded at cost as well as the corresponding accumulated depreciation (See note 4). The transaction resulted in a $1,000,000 capital contribution from the City and a utility acquisition adjustment of $194,608 which is presented as a deferred outflow of resources in the Statement of Net Position. This amount is being amortized over 20 years at $9,730 per year. The unamortized amount at December 31, 2017 and 2016 was $165,417 and $175,147.

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NOTE 3 – DEPOSITS AND INVESTMENTS

DEPOSITS

Custodial Credit Risk—Deposits. Custodial credit risk is the risk that in the event of a bank failure, the District's deposits may not be returned or that the District will not be able to recover collateral securities in the possession of an outside party. As of December 31, 2017 and 2016, $9,010,424 and $7,930,584 of the District's bank balance of $9,703,422 and $8,430,584 was exposed to custodial credit risk. For 2017 and 2016, of the amount exposed to custodial credit risk, the entire amount was collateralized by securities held by the pledging financial institution.

INVESTMENTS

At December 31, 2017 and 2016, the District had the following investments and maturities:

	12/31/2017 Fair Value	Average Credit Quality/Ratings	Maturities
Bond Mutual Funds	$ 4,921,888	Unrated	7.5 years average
Bond Mutual Funds	4,712,267	Unrated	5.3 years average
Bond Mutual Funds	3,630,796	Unrated	6.7 years average
Total Investments	$ 13,264,951		

	12/31/2016 Fair Value	Average Credit Quality/Ratings	Maturities
Bond Mutual Funds	$ 4,826,954	Unrated	7.5 years average
Bond Mutual Funds	4,524,211	Unrated	5.1 years average
Bond Mutual Funds	3,454,152	Unrated	7.6 years average
Total Investments	$ 12,805,317		

The funds listed above are not rated. The individual investments within the funds are rated no lower than BBB.

Investment Policies

Credit Risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. Generally, the District's investing activities are under the custody of the District Commissioners. Investing policies comply with the State Statutes. Kentucky Revised Statute 66.480 defines the following items as permissible investments:

- Obligations of the United States and of its agencies and instrumentalities;
- Obligations of any corporation of the United States Government;
- Obligations and contracts for future delivery or purchase of obligations backed by the full faith and credit of the United States or a United States government agency;
- Uncollateralized certificates of deposit issued by any bank or savings and loan institution rated in one (1) of the three (3) highest categories by a nationally recognized rating agency;
- Bankers' acceptances for banks rated in one (1) of the three (3) highest categories by a nationally recognized rating agency;

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- Certificates of deposit issued by or other interest-bearing accounts of any bank or savings and loan institution which are insured by the Federal Deposit Insurance Corporation or similar entity or which are collateralized, to the extent uninsured, by any obligations, including surety bonds, permitted by KRS 41.240(4)
- Commercial paper rated in the highest category by a nationally recognized rating agency;
- Bonds or certificates of indebtedness of this state and of its agencies and instrumentalities;
- Securities issued by a state or local government, or any instrumentality of agency thereof, in the United States, and rated in one (1) of the three (3) highest categories by a nationally recognized rating agency; and
- Shares of mutual funds, each of which shall have the following characteristics:
    1. The mutual fund shall be an open-end diversified investment company registered under the Federal Investment Company Act of 1940, as amended;
    2. The management company of the investment company shall have been in operation for at least five (5) years; and
    3. All of the securities in the mutual fund shall be eligible investments pursuant to this section.

Interest Rate Risk is the risk that changes in interest rates will adversely affect the fair value of an investment. Investments held for longer periods are subject to increased risk of adverse interest rate changes. The District policy provides that, to the extent practicable, investments are matched with anticipated cash flows. Investments are diversified to minimize the risk of loss resulting from over-concentration of assets in a specific maturity period, a single issuer, or an individual class of securities. **Concentration of Credit Risk** is the risk of loss attributed to the magnitude of the District's investment in a single issuer. U.S. Government securities and investments in mutual funds are excluded from this risk. The District does not have more than 5% or more of investments subject to the concentration of credit risk disclosure in any one issuer. **Custodial Credit Risk** is the risk that, in the event of the failure of the counterparty, the District will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. No investments are reported at amortized cost. The District categorizes its fair value measurements within the fair value hierarchy established by generally accepted accounting principles. The hierarchy is based on the valuation inputs used to measure the fair value of the asset. Level 1 inputs are quoted prices in active markets for identical assets; Level 2 inputs are significant other observable inputs; Level 3 inputs are significant unobservable inputs. The District's investments are level 1 inputs.

NOTE 4 - RESTRICTED CASH

The District has restricted cash for various purposes at December 31, 2017 and 2016 as follows:

Restricted For	December 31, 2017	December 31, 2016
Debt service	$ 2,408,756	$ 2,397,776
Depreciation fund	1,526,305	831,166
Escrow	77,132	65,306
Construction	1,497,088	474,077
Health plan	171,767	40,000
Customer deposits	432,193	488,495
	$ 6,113,241	$ 4,296,820

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HARDIN COUNTY WATER DISTRICT NO. 2

NOTES TO FINANCIAL STATEMENTS

DECEMBER 31, 2017 AND 2016

NOTE 5 – CAPITAL ASSETS

Capital asset activity for the year ended December 31, 2017 follows.

	Balance at December 31, 2016	Additions	Relassifications/ Retirements	Balance at December 31, 2017
Non-Depreciable Assets:				
Land and land rights	$ 2,137,632	$ 34,000	$ -	$ 2,171,632
Construction in progress	9,444,007	3,706,468	(9,954,175)	3,196,300
Total Capital Assets Not Being Depreciated	11,581,639	3,740,468	(9,954,175)	5,367,932
Capital Assets Being Depreciated:				
Structures and improvements	10,884,254	1,745,265	-	12,629,519
Property held for future use	1,190,404	-	-	1,190,404
Supply mains	1,763,965	31,194	-	1,795,159
Water treatment plant	11,603,601	110,951	-	11,714,552
Standpipes, tanks and foundations	11,238,627	202,806	-	11,441,433
Transmission and distribution mains	43,731,894	7,999,764	-	51,731,658
Services and meters	10,109,523	421,569	(90,190)	10,440,902
Hydrants	284,920	246	-	285,166
Office furniture and fixtures	506,817	62,600	-	569,417
Transportation equipment	1,785,106	250,725	(89,590)	1,946,241
Other property and equipment	606,185	67,403	-	673,588
Total Capital Assets Being Depreciated at historical cost	93,705,296	10,892,523	(179,780)	104,418,039
Less accumulated depreciation:				
Structures and improvements	3,309,764	341,006	2,565,488	6,216,258
Property held for future use	17,360	29,760	-	47,120
Supply mains	1,057,797	44,234	100,865	1,202,896
Water treatment plant	4,521,163	248,114	(2,666,353)	2,102,924
Standpipes, tanks and foundations	3,483,408	290,363	-	3,773,771
Transmission and distribution mains	15,166,803	1,041,815	-	16,208,618
Services and meters	3,909,221	624,967	(88,316)	4,445,872
Hydrants	239,948	9,095	-	249,043
Office furniture and fixtures	373,285	56,183	-	429,468
Transportation equipment	1,166,796	197,473	(89,590)	1,274,679
Other property and equipment	403,387	52,442	-	455,829
Total accumulated depreciation	33,648,932	2,935,452	(177,906)	36,406,478
Total other capital assets, net	60,056,364	7,957,071	(1,874)	68,011,561
Capital assets, net	$ 71,638,003	$ 11,697,539	$ (9,956,049)	$ 73,379,493

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HARDIN COUNTY WATER DISTRICT NO. 2

NOTES TO FINANCIAL STATEMENTS

DECEMBER 31, 2017 AND 2016

Capital asset activity for the year ended December 31, 2016 follows.

	Balance at December 31, 2015	Additions	Retirements	Balance at December 31, 2016
Non-Depreciable Assets:				
Land and land rights	$ 687,483	$1,450,149	$ -	$ 2,137,632
Construction in progress	3,054,092	7,301,096	(911,181)	9,444,007
Total Capital Assets Not Being Depreciated	3,741,575	8,751,245	(911,181)	11,581,639
Capital Assets Being Depreciated:				
Structures and improvements	10,834,554	49,700	-	10,884,254
Property held for future use	-	1,190,404	-	1,190,404
Supply mains	1,763,965	-	-	1,763,965
Water treatment plant	11,113,289	490,312	-	11,603,601
Standpipes, tanks and foundations	10,900,431	338,196	-	11,238,627
Transmission and distribution mains	43,672,916	58,978	-	43,731,894
Services and meters	8,663,459	1,562,688	(116,624)	10,109,523
Hydrants	261,775	23,145	-	284,920
Office furniture and fixtures	479,702	27,115	-	506,817
Transportation equipment	1,667,751	186,960	(69,605)	1,785,106
Other property and equipment	606,185	-	-	606,185
Total Capital Assets Being Depreciated at historical cost	89,964,027	3,927,498	(186,229)	93,705,296
Less accumulated depreciation:				
Structures and improvements	3,000,077	309,687	-	3,309,764
Property held for future use	-	17,360	-	17,360
Supply mains	1,013,698	44,099	-	1,057,797
Water treatment plant	4,286,796	234,367	-	4,521,163
Standpipes, tanks and foundations	3,203,781	279,627	-	3,483,408
Transmission and distribution mains	14,203,119	963,684	-	15,166,803
Services and meters	3,397,268	628,577	(116,624)	3,909,221
Hydrants	230,857	9,091	-	239,948
Office furniture and fixtures	320,749	52,536	-	373,285
Transportation equipment	1,055,689	180,712	(69,605)	1,166,796
Other property and equipment	355,053	48,334	-	403,387
Total accumulated depreciation	31,067,087	2,768,074	(186,229)	33,648,932
Total other capital assets, net	58,896,940	1,159,424	-	60,056,364
Capital assets, net	$ 62,638,515	$9,910,669	$ (911,181)	$ 71,638,003

During the years ended December 31, 2017 and 2016, the District capitalized no interest in either year and expensed $573,693 and $706,545 of interest.

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HARDIN COUNTY WATER DISTRICT NO. 2

NOTES TO FINANCIAL STATEMENTS

DECEMBER 31, 2017 AND 2016

NOTE 6 – LONG-TERM OBLIGATIONS

The construction costs of the District's water facilities have been financed by issuance of revenue bonds authorized under Kentucky Revised. All assets of the District are pledged as collateral for these bonds. Information relating to the outstanding bond issues is summarized below:

Issue	Interest Rate	Face Amount	Bonds Due 12/31/2017	Bonds Due 12/31/2016
2010 Series A	2.0% - 4.125%	5,625,000	$ 4,180,000	$ 4,410,000
2012 Series	1.0% - 3.75%	6,070,000	5,105,000	5,300,000
2016 Series B	2.0% - 3.0%	2,180,000	1,980,000	2,180,000
2016 Series C	2.0% - 3.0%	2,430,000	2,200,000	2,430,000
			$ 13,465,000	$ 14,320,000

On July 7, 2016, the District issued $2,180,000 in Series 2016B Water System Refunding Revenue Bonds with an average interest rate of 2.8 percent and $2,430,000 in Series 2016C Water System Refunding Revenue Bonds with an average interest rate of 2.8 percent to advance refund $4,964,000 of outstanding 2004A, 2005A and 2007 Series Bonds. The refunding was an advance refunding. The net proceeds of $4,814,439 (after $120,614 in cost of issuance, $316,530 in bond premium, and $8,523 in accrued interest) in combination with $174,600 from the District were used to call the bonds ($4,964,000 of principal and $25,039 of interest).

The District completed the refunding to reduce its total debt service payments over the next 10 years by $1,984,658 and to obtain an economic gain (difference between the present values of the old and new debt service payments) of $1,172,766.

The District requires new customers to provide a $60 deposit for initial water service. Current customers in good standing who add additional service locations are not required to pay an additional deposit.

Long-term liability activity for the year ended December 31, 2017, was as follows:

	Balance at December 31, 2016	Additions	Reductions	Balance at December 31, 2017	Amount Due Within One Year
Bonds and notes payable:					
Revenue bonds	$ 14,320,000	$ -	$ (855,000)	$ 13,465,000	$ 860,000
Notes	5,621,906	-	(245,679)	5,376,227	252,423
Unamortized bond premium/discount	146,786	-	(12,817)	133,969	-
Total bonds and notes payable	20,088,692	-	(1,113,496)	18,975,196	1,112,423
Other liabilities:					
Customer deposits	430,080	56,750	(29,700)	457,130	45,713
Accrued vacation	155,245	178,148	(155,245)	178,148	178,148
Customer advances for construction	77,250	40,000	(30,000)	87,250	87,250
Total other liabilities	662,575	274,898	(214,945)	722,528	311,111
Long-term liabilities	$ 20,751,267	$ 274,898	$ (1,328,441)	$ 19,697,724	$ 1,423,534

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HARDIN COUNTY WATER DISTRICT NO. 2

NOTES TO FINANCIAL STATEMENTS

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Long-term liability activity for the year ended December 31, 2016, was as follows:

	Balance at December 31, 2015	Additions	Reductions	Balance at December 31, 2016	Amount Due Within One Year
Bonds and notes payable:					
Revenue bonds	$ 15,343,000	$ 4,610,000	$ (5,633,000)	$ 14,320,000	$ 855,000
Notes	5,861,021	-	(239,115)	5,621,906	283,041
Unamortized bond premium/discount	(158,455)	316,530	(11,289)	146,786	
Total bonds and notes payable	21,045,566	4,926,530	(5,883,404)	20,088,692	1,138,041
Other liabilities:					
Customer deposits	496,711	176,520	(243,151)	430,080	43,008
Accrued vacation	123,268	155,245	(123,268)	155,245	155,245
Customer advances for construction	34,250	47,000	(4,000)	77,250	77,250
Total other liabilities	654,229	378,765	(370,419)	662,575	275,503
Long-term liabilities	$ 21,699,795	$ 5,305,295	$ (6,253,823)	$ 20,751,267	$ 1,413,544

Bond and note maturities and Sinking Fund requirements in each of the next five years and in five year increments thereafter are as follows at December 31, 2017:

	Revenue Bonds			Notes		
Year	Principal	Interest	Totals	Principal	Interest	Totals
2018	$ 860,000	$ 414,169	$ 1,274,169	$ 252,423	$ 147,577	$ 400,000
2019	890,000	392,337	1,282,337	259,352	140,648	400,000
2020	910,000	366,922	1,276,922	266,471	133,529	400,000
2021	950,000	339,906	1,289,906	273,785	126,215	400,000
2022	980,000	311,431	1,291,431	281,301	118,699	400,000
2023-2027	4,545,000	1,099,734	5,644,734	1,526,657	473,343	2,000,000
2028-2032	2,790,000	507,669	3,297,669	1,748,014	251,986	2,000,000
2033-2037	1,195,000	170,056	1,365,056	768,224	31,776	800,000
2038-2042	345,000	10,406	355,406	-	-	-
Total	$ 13,465,000	$ 3,612,630	$ 17,077,630	$ 5,376,227	$ 1,423,773	$ 6,800,000

Year	Sinking Fund Requirements
2018	$ 1,674,169
2019	1,682,337
2020	1,676,922
2021	1,689,906
2022	1,691,431
2023-2027	7,644,734
2028-2032	5,297,669
2033-2037	2,165,056
2038-2042	355,406
Total	$ 23,877,630

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Under covenants of the bond ordinances, certain funds have been established. These funds and their current financial requirements are presented as follows:

Revenue Fund
All receipts for services are deposited into this fund and, subsequently, disbursed into the following required funds:

Bond and Interest Redemption Funds
There is to be a monthly deposit of an amount equal to 1/12 of the next ensuing principal payment due and 1/6 of the next ensuing interest payment due for the 2010 Series A, 2012 Series, 2016 Series B and 2016 Series C and 1/12 of the next ensuing principal and interest payment on the note payable.

Depreciation Fund
This fund receives, on a monthly basis, $150,000. This fund also receives the proceeds from the sale of any property or equipment. This fund may be used to purchase new or replacement property and equipment.

Operation and Maintenance Fund
This fund receives, on a monthly basis, sufficient amounts to pay current expenses from the Revenue Fund after the above transfers have been made. This fund is used to pay operating expenditures. This account is funded until it reaches 2 months of forecasted operating expenses. Any surplus left may be added to the Bond and Interest Redemption Fund.

NOTE 7 - RETIREMENT PLAN

Plan Description
The District participates in the County Employees' Retirement System (CERS), a component unit of the Commonwealth of Kentucky which is a cost-sharing multiple-employer defined benefit plan. CERS provides retirement and disability benefits, annual cost-of-living adjustments, and death benefits to plan members and beneficiaries. Under the provisions of KRS Section 61.645, the Board of Trustees of Kentucky Retirement Systems (KRS) administers the CERS. The CERS issues a publicly available financial report that includes financial statements, required supplementary information and detailed information about CERS' fiduciary net position. CERS' report may be obtained at www.kyret.ky.gov.

Benefits Provided
The system provides for retirement, disability, and death benefits to system members. Retirement benefits may be extended to beneficiaries of members under certain circumstances. Prior to July 1, 2009, cost-of-living adjustments (COLA) were provided annually equal to the percentage increase in the annual average of the consumer price index for all urban consumers for the most recent calendar year, not to exceed 5% in any plan year. Effective July 1, 2009, and on July 1 of each year thereafter, the COLA is limited to 1.5% provided the recipient has been receiving a benefit for at least 12 months prior to the effective date of the COLA. If the recipient has been receiving a benefit for less than 12 months prior to the effective date of the COLA, the increase shall be reduced on a pro-rata basis for each month the recipient has not been receiving benefits in the 12 months preceding the effective date of the COLA. The Kentucky General Assembly has the authority to

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increase, suspend or reduce COLAs. Senate Bill 2 of 2013 eliminated all future COLAs unless the State Legislature so authorizes on a biennial basis and either (1) the system is over 100% funded or (2) the Legislature appropriates sufficient funds to pay the increased liability for the COLA. No COLA has been granted since July 1, 2011.

Contributions

For the calendar year ended December 31, 2017, plan members who began participating prior to, or, or after September 1, 2008, were required to contribute 5% of their annual creditable compensation. Participating employers were required to contribute at an actuarially determined rate. Per Kentucky Revised Statute Section 78.545(33), normal contribution and past service contribution rates shall be determined by the Board on the basis of an annual valuation last preceding July 1 of a new biennium. The Board may amend contribution rates as of the first day of July of the second year of a biennium, if it is determined on the basis of a subsequent actuarial valuation that amended contribution rates are necessary to satisfy requirements determined in accordance with actuarial bases adopted by the Board. Plan members who began participating prior to September 1, 2008 are considered in the Tier 1 structure of benefits and plan members who began participating September 1, 2008 through December 31, 2013 are considered in the Tier 2 structure of benefits.

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

The District's contractually required contribution rate for the calendar year ended December 31, 2017, was 13.95 percent of creditable compensation from January 1 to June 30 and 14.48 percent of creditable compensation from July 1 to December 31. The District's contractually required contribution rate for the calendar year ended December 31, 2016, was 12.42 percent of creditable compensation from January 1 to June 30 and 13.95 percent of creditable compensation from July 1 to December 31. Contributions to the pension plan for the years ended December 31, 2017 and 2016 from the District were $456,294 and $412,832. At December 31, 2017 and 2016, the District owed $85,054 and $75,898 to the plan for employer and member contributions for December.

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HARDIN COUNTY WATER DISTRICT NO. 2

NOTES TO FINANCIAL STATEMENTS

DECEMBER 31, 2017 AND 2016

Pension Liabilities, Pension Expense, and Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions

At December 31, 2017, the District reported a liability of $7,559,254 for its proportionate share of the net pension liability. The net pension liability was measured as of June 30, 2017, and the total pension liability used to calculate the net pension liability was determined by an actuarial valuation as of June 30, 2016 using standard roll-forward techniques. The District's proportion of the net pension liability was based on a projection of the District's long-term share of contributions to the pension plan relative to the projected contributions of all, actuarially determined. At June 30, 2017, the District's proportion was 0.129145 percent, which was an increase of .009228 percent from its proportion measured as of June 30, 2016.

For the years ended December 31, 2017 and 2016, the District recognized pension expense of $456,294 and $412,832. At December 31, 2017 and 2016, the District reported its proportionate share of the CERS deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

	2017	
	Deferred Outflows of Resources	Deferred Inflows of Resources
Differences between expected and actual economic experience	$ 9,376	$ 191,886
Changes in actuarial assumptions	1,394,887	-
Difference between projected and actual investment earnings	598,684	505,185
Changes in proportion and proportionate share of contributions	606,059	-
	$ 2,609,006	$ 697,071

	2016	
	Deferred Outflows of Resources	Deferred Inflows of Resources
Differences between expected and actual economic experience	$ 25,776	$ -
Changes in actuarial assumptions	312,776	-
Difference between projected and actual investment earnings	555,060	-
Changes in proportion and proportionate share of contributions	660,856	-
	$ 1,554,468	$ -

(Continued next page)

HARDIN COUNTY WATER DISTRICT NO. 2

NOTES TO FINANCIAL STATEMENTS

DECEMBER 31, 2017 AND 2016

Amounts reported as deferred outflows of resources related to pensions will be recognized in pension expense as follows:

Year Ending December 31	Amortization Amount
2018	$ 945,185
2019	754,022
2020	309,795
2021	(97,067)
2022	-
	$ 1,911,935

The total pension liability in the June 30, 2017 actuarial valuation using standard roll-forward techniques was determined using the following actuarial assumptions, applied to all periods included in the measurement:

Valuation Date	June 30, 2016
Actuarial Cost Method	Entry Age Normal

Actuarial Assumptions:

Discount Rate	6.25 percent
Inflation	2.30 percent
Salary increases	3.05 percent, average, including inflation
Investment rate of return	6.25 percent, net of pension plan investment expense, including inflation

The mortality table used for active members is RP-2000 Combined Mortality Table projected with Scale BB to 2013 (multiplied by 50% for males and 30% for females). For healthy retired members and beneficiaries, the mortality table used is the RP-2000 Combined Mortality Table projected with Scale BB to 2013 (set back for one year for females). For disabled members, the RP-2000 Combined Disabled Mortality Table projected with Scale BB to 2013 (set back four years for males) is used for the period after disability retirement. There is some margin in the current mortality tables for possible future improvement in mortality rates and that margin will be reviewed again when the next experience investigation is conducted.

The actuarial assumptions used in the June 30, 2016 valuation were based on the results of an actuarial experience study for the period July 1, 2008 – June 30, 2013.

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The long-term expected return on plan assets is reviewed as part of the regular experience studies prepared every five years for the Systems. The most recent analysis, performed for the period covering fiscal years 2008 through 2013, is outlined in a report dated April 30, 2014. Several factors are considered in evaluating the long-term historical data, estimates inherent in current market data, and a log-normal distribution analysis in which best-estimate ranges of expected future real rates of return (expected return, net of investment expense and inflation) were developed by the investment consultant for each major asset class. These ranges were combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and then adding expected inflation. The capital market assumptions developed by the investment consultant are intended for use over a 10-year horizon and may not be useful in setting the long-term rate of return for funding pension plans which covers a longer timeframe. The assumption is intended to be a long-term assumption and is not expected to change absent a significant change in the asset allocation, a change in the inflation assumption, or a fundamental change in the market that alters expected returns in future years.

Asset Class	Target Allocation	Long-term Expected Real Rate of Return
US Equity	17.50%	5.97%
International Equity	17.50%	7.85%
Global Bonds	4.00%	2.63%
Global Credit	2.00%	3.63%
High Yiewld	7.00%	5.75%
Emerging Market Debt	5.00%	5.50%
Private Credit	10.00%	8.75%
Real Estate	5.00%	7.63%
Absolute Return	10.00%	5.63%
Real Return	10.00%	6.13%
Private Equity	10.00%	8.25%
Cash	2.00%	1.88%
Total	100.00%	

Discount Rate

The discount rate used to measure the total pension liability as of the Measurement Date was 6.25%. The projection of cash flows used to determine the discount rate assumed that local employers would contribute the actuarially determined contribution rate of projected compensation over the remaining 26 year (closed) amortization period of the unfunded actuarial accrued liability. The actuarial determined contribution rate is adjusted to reflect the phase in of anticipated gains on actuarial value of assets over the first four years of the projection period. Projected inflows from investment earnings were calculated using the long-term assumed investment return of 6.25%. The long-term assumed investment rate of return was applied to all periods of projected benefit payments to determine the total pension liability.

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Sensitivity Of The District's Proportionate Share Of The Net Pension Liability To Changes In The Discount Rate

The following presents the District's proportionate share of the net pension liability calculated using the discount rate of 6.25 percent, as well as what the District's proportionate share of the net pension liability would be if it were calculated using a discount rate that is 1-percentage-point lower (5.25 percent) or 1-percentage-point higher (7.25 percent) than the current rate:

	1% Decrease (5.25%)	Current Discount Rate (6.25%)	1% Increase (7.25%)
District's proportionate share of the net pension liability	$ 9,533,853	$ 7,559,254	$ 5,907,517

Pension Plan Fiduciary Net Position

Detailed information about the pension plan's fiduciary net position is available in the separately issued CERS financial report.

CERS also provides post-retirement health care coverage as follows:

For members participating prior to July 1, 2003, years of service and respective percentages of the maximum contribution are as follows:

Years of Service	% paid by Insurance Fund	% Paid by Member through
20 or more	10	0%
15-19	7	25%
10-14	5	50%
4-9	2	75%
Less than 4	0	100%

As a result of House Bill 290 (2004 General Assembly), medical insurance benefits are calculated differently for members who began participation on or after July 1, 2003. Once members reach a minimum vesting period of ten years, non-hazardous employees whose participation began on or after July 1, 2003, earn ten dollars per month for insurance benefits at retirement for every year of earned service without regard to a maximum dollar amount.

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HARDIN COUNTY WATER DISTRICT NO. 2

NOTES TO FINANCIAL STATEMENTS

DECEMBER 31, 2017 AND 2016

NOTE 8 - SELF-INSURANCE

In January 2017, the District implemented a self-insured health insurance plan. Revenues are recognized from payroll deductions for employee dependent coverage and from City contributions for employee coverage. Liabilities for unpaid claims are estimated based on a review of claims incurred during the fiscal year but not paid until the following fiscal year. Changes in claims liability during the year ended December 31, 2017, were as follows:

Year Ended December 31,	Balance at beginning of year	Current-year claims and changes in estimates	Claim payments and transfers	Balance at end year
2017	$ -	$ 578,881	$ 574,924	$ 3,957

Claims due within one year at December 31, 2017 were $114,397. The health care coverage program maintains a policy with a commercial insurance company that covers any claims greater than $250,000 per year per employee and also covers any aggregate claims greater than $594,040 per year. For the year ending December 31, 2017 no settlements exceeded insurance coverage.

NOTE 9 – INTERDIVISION ACTIVITIES

During the year ended December 31, 2017, the Water Division transferred $2,218,669 of capital asset construction in progress to the Sewer Division. Also, on October 17, 2017, the Water Division loaned the Sewer Division $500,000 at no interest. The amount is due October 1, 2019.

NOTE 10 – CAPITAL CONTRIBUTIONS

The following schedule details the sources of capital contributions for the years ended December 31, 2017 and 2016:

Source	2017	2016
State of Kentucky	$ 240,006	$ 5,952,907
Relocation	108,031	150,748
Tap Fees	277,098	219,518
Developers	6,093	3,622
	$ 631,228	$ 6,326,795

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HARDIN COUNTY WATER DISTRICT NO. 2

NOTES TO FINANCIAL STATEMENTS

DECEMBER 31, 2017 AND 2016

NOTE 11 – RENTAL AGREEMENTS

The District has entered into agreements to lease space on its water towers to various customers. Rental income during the years ended December 31, 2017 and 2016 was $101,210 and $81,940. The following schedule represents future payments to be received. Each agreement provides for optional renewals. The schedule below reflects payments to be received under current agreements and does not include renewals after the current term.

2018	$ 89,850
2019	61,284
2020	61,284
2021	61,284
2022	61,284
Total	$ 334,986

NOTE 12 – COMMITMENTS AND CONTINGENCIES

The District is subject to various legal actions in various stages of litigation, the outcome of which is not determinable at this time. Management of the District and its legal counsel do not anticipate that there will be any material effect on the basic financial statements as a result of the cases presently in progress.

The District has construction commitments for ongoing projects.

Under COBRA, employers are mandated to notify terminated employees of available continuing insurance coverage. Failure to comply with this requirement may put the District at risk for a substantial loss.

NOTE 13 – RISK MANAGEMENT

The District is exposed to various risks of loss related to torts; theft of, damage to and destruction of assets; errors and omissions; and natural disasters. The District was insured for workers' compensation, general liability and automobile liability coverage under a retrospectively rated commercial policy.

REQUIRED SUPPLEMENTARY INFORMATION

HARDIN COUNTY WATER DISTRICT NO. 2

SCHEDULE OF THE DISTRICT'S PROPORTIONATE SHARE OF THE CERS NET PENSION LIABILITY

December 31, 2017

Last 10 Years *

	2017	2016	2015
Proportion of the net pension liability	0.129145%	0.119917%	0.104554%
Proportionate share of the net pension liability	$ 7,559,254	$ 5,904,253	$ 4,495,343
Covered - employee payroll	$ 3,233,237	$ 2,993,522	$ 2,638,530
Proportionate share of the net pension liability as percentage of covered payroll	233.8%	197.2%	170.4%
Plan fiduciary net position as a percentage of the total pension liability	53.30%	55.50%	59.97%

* Calendar year 2015 was the first year of implementation, therefore, only three years are shown.

HARDIN COUNTY WATER DISTRICT NO. 2

SCHEDULE OF CONTRIBUTIONS TO CERS

December 31, 2017

Last 10 Years *

	2017	2016	2015
Contractually required contribution (actuarially determined)	$ 456,294	$ 412,832	$ 312,163
Contribution in relation to the actuarially determined contributions	456,294	412,832	312,163
Contribution deficiency (excess)	$ -	$ -	$ -
Covered employee payroll	$ 3,208,084	$ 3,117,060	$ 2,939,133
Contributions as a percentage of covered employee payroll	14.22%	13.24%	10.62%

* Calendar year 2015 was the first year of implementation, therefore, only three years are shown.

HARDIN COUNTY WATER DISTRICT NO. 2

NOTES TO REQUIRED SUPPLEMENTARY INFORMATION

FOR THE YEAR ENDED DECEMBER 31, 2017

Changes of benefit terms. There were no changes in benefit terms.

Changes of assumptions:

1. Decrease the price inflation assumption to 3.25 % to 2.30%
2. Decrease the assumed rate of return from 7.50% to 6.25%;
3. Decrease the payroll growth assumption from 4.00% to 2.00%

OTHER SUPPLEMENTARY INFORMATION

HARDIN COUNTY WATER DISTRICT NO. 2

SCHEDULE I - BOND AND INTEREST REQUIREMENTS

DECEMBER 31, 2017

	$ 5,625,000 2010 SERIES A		$ 6,070,000 2012 SERIES	
	BOND	INTEREST	BOND	INTEREST
2018	$ 235,000	$ 149,894	$ 195,000	$ 147,475
2019	245,000	142,987	200,000	143,525
2020	250,000	135,250	205,000	139,347
2021	260,000	126,800	210,000	134,806
2022	265,000	117,940	215,000	129,891
2023	275,000	108,656	220,000	124,725
2024	290,000	98,588	230,000	119,238
2025	300,000	87,707	235,000	113,425
2026	310,000	76,075	245,000	107,119
2027	325,000	63,772	245,000	100,381
2028	340,000	50,676	255,000	93,506
2029	345,000	36,976	265,000	86,356
2030	360,000	22,876	270,000	78,663
2031	380,000	7,833	280,000	70,063
2032			295,000	60,719
2033			300,000	50,675
2034			210,000	41,750
2035			220,000	34,225
2036			230,000	26,063
2037			235,000	17,344
2038			250,000	8,250
2039			85,000	1,969
2040			10,000	188
	$ 4,180,000	$ 1,226,030	$ 5,105,000	$ 1,829,703

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HARDIN COUNTY WATER DISTRICT NO. 2

SCHEDULE I - BOND AND INTEREST REQUIREMENTS

DECEMBER 31, 2017

(CONTINUED)

	$ 2,180,000 2016 SERIES B		$ 2,430,000 2016 SERIES C	
	BOND	INTEREST	BOND	INTEREST
2018	195,000	55,500	$ 235,000	$ 61,300
2019	200,000	50,550	245,000	55,275
2020	205,000	44,475	250,000	47,850
2021	215,000	38,175	265,000	40,125
2022	220,000	31,650	280,000	31,950
2023	225,000	24,975	295,000	23,325
2024	235,000	18,075	310,000	14,250
2025	240,000	10,950	320,000	4,800
2026	245,000	3,675		
2027				
2028				
2029				
2030				
2031				
2032				
2033				
2034				
2035				
2036				
2037				
2038				
2039				
2040				
	$ 1,980,000	$ 278,025	$ 2,200,000	$ 278,875

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HARDIN COUNTY WATER DISTRICT NO. 2

SCHEDULE I - BOND AND INTEREST REQUIREMENTS

DECEMBER 31, 2017

(CONTINUED)

TOTAL ALL ISSUES	
BOND	INTEREST
$ 860,000	$ 414,169
890,000	392,337
910,000	366,922
950,000	339,906
980,000	311,431
1,015,000	281,681
1,065,000	250,151
1,095,000	216,882
800,000	186,869
570,000	164,153
595,000	144,182
610,000	123,332
630,000	101,539
660,000	77,896
295,000	60,719
300,000	50,675
210,000	41,750
220,000	34,225
230,000	26,063
235,000	17,344
250,000	8,250
85,000	1,969
10,000	188
$ 13,465,000	$ 3,612,633

HARDIN COUNTY WATER DISTRICT NO. 2

SCHEDULE II - GENERAL AND ADMINISTRATIVE EXPENSES

YEARS ENDED DECEMBER 31, 2017 AND 2016

	2017	2016
Salaries	$ 1,258,773	$ 1,203,525
Commissioner's salaries	30,324	30,314
Employee benefits	611,072	542,871
Materials and supplies	85,416	90,687
Professional fees and contractual services	108,302	221,428
Insurance	144,931	138,909
Advertising	4,476	7,853
Provision for bad debts	48,006	37,690
Other general and administrative	383,688	438,290
	$ 2,674,988	$ 2,711,567

HARDIN COUNTY WATER DISTRICT NO. 2

SCHEDULE III - ORGANIZATION DATA

DECEMBER 31, 2017

WATER COMMISSIONERS

Michael Bell - Chairman
Morris Miller - Secretary/Treasurer
Cordell Tabb - Member
John Effinger - Member
Tim Davis - Member

ATTORNEY

Stoll, Keenon, Ogden, PLLC

GENERAL MANAGER

James Jeffries

CALENDAR YEAR

January 1 to December 31

HARDIN COUNTY WATER DISTRICT NO. 2

SCHEDULE IV - SCHEDULE OF NET POSITION - WATER DIVISION

DECEMBER 31, 2017 AND 2016

	2017	2016
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	$ 3,183,242	$ 3,320,204
Investments	13,264,952	12,805,317
Accounts receivable, net	1,568,803	1,433,412
State grants receivable	-	476,002
Materials and supplies	427,034	511,382
TOTAL CURRENT ASSETS	18,444,031	18,546,317
NONCURRENT ASSETS:		
Restricted cash and cash equivalents	4,404,937	3,089,426
Restricted investments	1,207,394	1,207,394
Regulatory asset on CERS pension	5,647,319	4,349,785
Due from sewer division	500,000	-
Non-depreciable capital assets	3,149,263	11,581,639
Depreciable capital assets, net of accumulated depreciation	68,011,561	60,056,364
TOTAL NONCURRENT ASSETS	82,920,474	80,284,608
TOTAL ASSETS	101,364,505	98,830,925
DEFERRED OUTFLOWS OF RESOURCES		
Deferred amount on debt refundings	187,324	218,350
Deferred amount on CERS pension	2,609,006	1,554,468
Utility acquisition adjustments	165,417	175,147
TOTAL DEFERRED OUTFLOWS OF RESOURCES	2,961,747	1,947,965
LIABILITIES		
CURRENT LIABILITIES:		
Accounts payable	166,419	158,753
Construction projects payable	584,473	14,149
Due to sewer division	191	-
Elizabethtown sewer payable	749,478	720,357
Accrued taxes	62,754	54,703
Accrued liabilities	87,939	75,898
Accrued vacation	178,148	155,245
Customer deposits	45,713	43,008
Customer advances for construction	87,250	77,250
Bonds payable	860,000	855,000
Notes payable	252,423	283,041
TOTAL CURRENT LIABILITIES	3,074,788	2,437,404
NONCURRENT LIABILITIES:		
Customer deposits	411,417	387,072
Net pension liability - CERS	7,559,254	5,904,253
Bonds payable	12,738,969	13,611,788
Notes payable	5,123,804	5,338,865
TOTAL NONCURRENT LIABILITIES	25,833,444	25,241,978
TOTAL LIABILITIES	28,908,232	27,679,382
DEFERRED INFLOWS OF RESOURCES		
Deferred amount on CERS pension	697,071	-
TOTAL DEFERRED INFLOWS OF RESOURCES	697,071	-
NET POSITION		
Net investment in capital assets	51,788,479	51,753,510
Restricted for debt service	2,408,756	2,397,776
Restricted for capital projects	2,963,720	1,370,549
Restricted for customers	432,193	498,495
Unrestricted	17,127,801	17,079,178
TOTAL NET POSITION	$ 74,720,949	$ 73,099,508

HARDIN COUNTY WATER DISTRICT NO. 2

SCHEDULE V - SCHEDULE OF REVENUES, EXPENSES AND CHANGES IN FUND NET POSITION - WATER DIVISION

YEARS ENDED DECEMBER 31, 2017 AND 2016

	2017	2016
OPERATING REVENUES:		
Water sales	$ 13,040,102	$ 12,512,174
Other operating income	838,780	820,005
TOTAL OPERATING REVENUES	13,878,882	13,332,179
OPERATING EXPENSES:		
Power purchased	808,028	822,983
Purchased water	302,321	-
Pumping and treatment labor	1,291,392	1,007,379
Purification supplies and expense	336,357	556,493
Transmission and distribution labor	1,690,446	1,525,723
Transmission and distribution supplies and expense	224,722	242,028
Transmission and distribution maintenance and repairs	72,390	54,476
Equipment rental	5,014	5,131
Transportation expense	151,224	154,429
Water treatment maintenance and expense	176,574	152,360
General and administrative expenses	2,674,895	2,711,567
Depreciation	2,935,452	2,768,074
TOTAL OPERATING EXPENSES	10,668,815	10,000,643
OPERATING INCOME	3,210,067	3,331,536
NON-OPERATING REVENUES (EXPENSES):		
Investment income	557,408	384,592
Other income	146,768	179,376
Gain on disposal of capital assets	33,075	8,607
Bond issuance costs	-	(120,614)
Interest expense on long-term debt	(573,693)	(706,250)
Interest expense on customer deposits	-	(295)
Amortization of bond discount and utility acquisition	(27,938)	(31,855)
TOTAL NON-OPERATING REVENUES (EXPENSES)	135,620	(286,439)
TRANSFERS	(2,218,669)	-
CAPITAL CONTRIBUTIONS	494,423	6,326,795
CHANGE IN NET POSITION	1,621,441	9,371,892
NET POSITION, beginning of year	73,099,508	63,727,616
NET POSITION, end of year	$ 74,720,949	$ 73,099,508

HARDIN COUNTY WATER DISTRICT NO. 2

SCHEDULE VI - SCHEDULE OF NET POSITION - SEWER DIVISION

DECEMBER 31, 2017 AND 2016

	2017	2016
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	$ 133	$ -
Investments	-	-
Accounts receivable, net	-	-
Prepaid insurance	-	-
State grants receivable	136,805	-
Due from water division	191	-
TOTAL CURRENT ASSETS	137,129	-
NONCURRENT ASSETS:		
Restricted cash and cash equivalents	500,910	-
Non-depreciable capital assets	2,218,669	-
TOTAL NONCURRENT ASSETS	2,719,579	-
TOTAL ASSETS	2,856,708	-
LIABILITIES		
NONCURRENT LIABILITIES:		
Due to water division	500,000	-
TOTAL NONCURRENT LIABILITIES	500,000	-
TOTAL LIABILITIES	500,000	-
NET POSITION		
Net investment in capital assets	2,218,669	-
Restricted for capital projects	136,805	-
Unrestricted	1,234	-
TOTAL NET POSITION	$ 2,356,708	$ -

HARDIN COUNTY WATER DISTRICT NO. 2

SCHEDULE VII - SCHEDULE OF REVENUES, EXPENSES AND CHANGES IN FUND NET POSITION - SEWER DIVISION

YEARS ENDED DECEMBER 31, 2017 AND 2016

	2017	2016
OPERATING REVENUES:		
Sewer sales	$ -	$ -
Other operating income	-	-
TOTAL OPERATING REVENUES	-	-
OPERATING EXPENSES:		
General and administrative expenses	93	-
TOTAL OPERATING EXPENSES	93	-
OPERATING INCOME (LOSS)	(93)	-
NON-OPERATING REVENUES (EXPENSES):		
Investment income	1,327	-
TOTAL NON-OPERATING REVENUES (EXPENSES)	1,327	-
CAPITAL CONTRIBUTIONS	136,805	
TRANSFERS	2,218,669	-
CHANGE IN NET POSITION	2,356,708	-
NET POSITION, beginning of year	-	-
NET POSITION, end of year	$ 2,356,708	$ -

INTERNAL CONTROL AND FISCAL COMPLIANCE

HARDIN COUNTY WATER DISTRICT NO. 2

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

YEAR ENDED DECEMBER 31, 2017

FEDERAL GRANTOR/PASS-THROUGH GRANTOR / PROGRAM TITLE	FEDERAL CFDA NUMBER	PASS THROUGH GRANTOR'S NUMBER	FEDERAL EXPENDITURES
U.S. DEPARTMENT OF AGRICULTURE			
Water and Waste Disposal Systems for Rural Communities	10.760	N/A	$ 1,496,718
TOTAL U.S. DEPT. OF AGRICULTURE			$ 1,496,718
TOTAL EXPENDITURES OF FEDERAL AWARDS			$ 1,496,718

The accompanying notes are an integral part of this schedule.

HARDIN COUNTY WATER DISTRICT NO. 2

NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

Year Ended December 31, 2017

NOTE A – BASIS OF PRESENTATION

The accompanying schedule of expenditures of federal awards includes the federal grant activity of Hardin County Water District No. 2 under programs of the federal government for the year ended December 31, 2017. The information in this schedule is presented in accordance with the requirements of Title 2 U.S. *Code of Federal Regulations Part 200, Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance). Because the schedule presents only a selected portion of the operations of Hardin County Water District No. 2, it is not intended to and does not present the financial position, changes in net position or cash flows of Hardin County Water District No. 2.

NOTE B – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Expenditures reported on the schedule are reported on the accrual basis of accounting. Such expenditures are recognized following the cost principles contained in the Uniform Guidance, wherein certain types of expenditures are not allowable or are limited as to reimbursement. Negative amounts shown on the Schedule represent adjustments or credits made in the normal course of business to amounts reported as expenditures in prior years. Pass-through entity identifying numbers are presented where available.

NOTE C – INDIRECT COST RATE

The District has elected to not use the 10 percent de minimum indirect cost rate allowed under the Uniform Guidance.

NOTE D – SUBRECIPIENTS

There were no subrecipients during the fiscal year.

HARDIN COUNTY WATER DISTRICT NO. 2
Schedule of Findings and Questioned Costs
For the Year Ended December 31, 2017

Section I-Summary of Auditor's Results

Financial Statements

Type of auditor's report issued (unmodified):

Internal control over financial reporting:

- Material weakness(es) identified? ______yes ___X__none reported
- Significant deficiency(ies) identified that are not considered to be material weaknesses? ______yes ___X__none reported

Noncompliance material to financial statements noted? ______yes ___X__no

Federal Awards

Internal control over major programs:

- Material weakness(es) identified? ______yes ___X__no
- Significant deficiency(ies) identified that are not considered to be material weakness(es)? ______yes ___X__none reported

Type of auditor's report issued on compliance for major programs (unmodified):

Any audit findings disclosed that are required to be reported in accordance with 2 CFR 200.516(a)? ______yes ___X__no

Identification of major programs:

CFDA Number	Federal Program or Cluster
10.760	Water and Waste Disposal Systems for Rural Communities

Dollar threshold used to distinguish Between type A and type B programs: $ 750,000

Auditee qualified as low-risk auditee? ______yes ___X__no

Section II – Financial Statement Findings

No matters were reported.

Section III – Federal Award Findings and Questioned Costs

No matters were reported.

HARDIN COUNTY WATER DISTRICT NO. 2

SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS

December 31, 2017

FINDING 2016-001 – MATERIAL WEAKNESS – ADJUSTMENTS

Condition This finding was a material weakness stating that material adjustments were required to the financial statements.

Recommendation: The auditor recommended that the District review its procedures to ensure all adjustments are made to the financial statements.

Current Status: The finding was not repeated in the December 31, 2017 audit.

Chris R. Carter, CPA
Ann M. Fisher, CPA
Scott Kisselbaugh, CPA
Philip A. Logsdon, CPA
Brian S. Woosley, CPA

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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*

Board of Commissioners
Hardin County Water District No. 2
Elizabethtown, Kentucky

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the Hardin County Water District No. 2, as of and for the year ended December 31, 2017, and the related notes to the financial statements, which collectively comprise Hardin County Water District No. 2's basic financial statements and have issued our report thereon dated June 12, 2018.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered Hardin County Water District No. 2's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of Hardin County Water District No. 2's internal control. Accordingly, we do not express an opinion on the effectiveness of Hardin County Water District No. 2'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 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.

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Compliance and Other Matters

As part of obtaining reasonable assurance about whether Hardin County Water District No. 2's 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 results of that testing, and not to provide an opinion on the effectiveness of the District's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Stiles, Carter & Associates

Certified Public Accountants
Elizabethtown, Kentucky
June 12, 2018

CHRIS R. CARTER, CPA
ANN M. FISHER, CPA
SCOTT KISSELBAUGH, CPA
PHILIP A. LOGSDON, CPA
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INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE FOR EACH MAJOR PROGRAM AND INTERNAL CONTROL OVER COMPLIANCE REQUIRED BY THE UNIFORM GUIDANCE

Board of Commissioners
Hardin County Water District No. 2
Elizabethtown, Kentucky

Report on Compliance for Each Major Federal Program

We have audited Hardin County Water District No. 2's compliance with the types of compliance requirements described in the *OMB Compliance Supplement* that could have a direct and material effect on each of Hardin County Water District No. 2's major federal programs for the year ended December 31, 2017. Hardin County Water District No. 2's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs.

Management's Responsibility

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

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for each of Hardin County Water District No. 2's major federal programs based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and the audit requirements of Title 2 U.S. *Code of Federal Regulations* Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance). Those standards and the Uniform Guidance require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about Hardin County Water District No. 2's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

We believe that our audit provides a reasonable basis for our opinion on compliance for each major federal program. However, our audit does not provide a legal determination of Hardin County Water District No. 2's compliance.

Opinion on Each Major Federal Program

In our opinion, Hardin County Water District No. 2 complied, in all material respects, with the compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended December 31, 2017.

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Report on Internal Control Over Compliance

Management of Hardin County Water District No. 2 is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered Hardin County Water District No. 2's internal control over compliance with the types of requirements that could have a direct and material effect on each major federal program in order to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major program and to test and report on internal control over compliance in accordance with the Uniform Guidance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of Hardin County Water District No. 2's internal control over compliance.

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

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

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

Stiles, Carter & Associates

Certified Public Accountants
Elizabethtown, Kentucky
June 12, 2018