

Knox County Utility Commission
Artemus, Kentucky

Independent Auditors' Report
And Financial Statements
For the Years Ended
December 31, 2018 and 2017

Knox County Utility Commission
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Independent Auditors' Report

To the Commissioners
Knox County Utility Commission
Artemus, Kentucky

Report on the Financial Statements

We have audited the accompanying financial statements of the business-type activities of the Knox County Utility Commission, (the Commission), as of and for the years ended December 31, 2018 and 2017, and the related notes to the financial statements, which collectively comprise the Commission'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.

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits 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 auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the business-type activities of the Knox County Utility Commission, as of December 31, 2018 and 2017, and the respective changes in financial position, and cash flows thereof for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Change in Accounting Principle

As discussed in Note 8 to the financial statements, during the year ended December 31, 2018 the Commission adopted new accounting guidance, *GASB Statement No. 75, Accounting and Financial Reporting for Postemployment Benefits Other than Pensions*. Accordingly, an adjustment has been made to net position as of December 31, 2017 to record the Commission's share of the net OPEB liability. 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 Schedule of the Commission's Proportionate Share of the Net Pension Liability, the Schedule of the Commission's Proportionate Share of the Net OPEB Liability, the Schedule of the Commission's Pension Contributions, and the Schedule of the Commission's OPEB Contributions on pages 37-40 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

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

Other Information

Our audits were conducted for the purpose of forming an opinion on the financial statements that collectively comprise the Commission's basic financial statements. The accompanying departmental statements for the water and sewer departments are presented separately for the purpose of additional analysis and are not a required part of the basic financial statements.

The accompanying departmental statements for the water and sewer departments 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, the information is fairly stated in all material respects in relation to the basic financial statements as a whole.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated June 28, 2019 on our consideration of the Knox County Utility Commission's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is 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 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 the Knox County Utility Commission's internal control over financial reporting and compliance.

Christian Sturgeon, PLLC

Christian Sturgeon, PLLC
London, Kentucky

June 28, 2019

Knox County Utility Commission
Statements of Net Position
December 31, 2018 and 2017

	<u>2018</u>	<u>2017</u>
Assets		
Current Assets		
Cash and cash equivalents	\$ 940,440	\$ 989,933
Receivables, less allowance	100,623	88,639
Unbilled accounts receivable	83,149	102,639
Inventories	24,600	24,806
Other current assets	5,252	4,525
Total Current Assets	<u>1,154,064</u>	<u>1,210,542</u>
Noncurrent Assets		
Restricted Assets		
Restricted cash and cash equivalents	<u>50,843</u>	<u>39,057</u>
Total Restricted Assets	<u>50,843</u>	<u>39,057</u>
Capital Assets		
Land and improvements	44,619	44,619
Structures and improvements	520,949	518,699
Pumping equipment	226,606	217,126
Meters and meter installation	874,934	816,036
Hydrants	53,816	53,816
Storage tanks	1,148,102	1,148,102
Transmission and distribution plant	10,416,631	10,416,631
Vehicles and other equipment	472,952	473,342
Office equipment	74,359	60,364
Lift stations	344,195	344,195
Construction in progress	15,799	7,543
Less: accumulated depreciation	<u>(6,890,468)</u>	<u>(6,682,565)</u>
Net Capital Assets	<u>7,302,494</u>	<u>7,417,908</u>
Total Noncurrent Assets	<u>7,353,337</u>	<u>7,456,965</u>
Total Assets	<u>8,507,401</u>	<u>8,667,507</u>
Deferred Outflows of Resources		
Bond issue costs, net of amortization	61,783	64,847
Differences between expected and actual experience related to pensions	25,604	850
Net differences between projected and actual earnings on pension plan investments	-	8,478
Changes of assumptions related to pensions	76,715	126,490
Changes of assumptions related to OPEB	45,700	51,228
Changes in proportion and differences between employer pension contributions and proportionate share of contributions	56,472	28,531
Changes in proportion and differences between employer OPEB contributions and proportionate share of contributions	15,690	-
Pension contributions subsequent to measurement date	26,989	21,757
OPEB contributions subsequent to measurement date	<u>8,752</u>	<u>7,062</u>
Total Deferred Outflows of Resources	<u>317,705</u>	<u>309,243</u>

See accompanying notes to financial statements.

Knox County Utility Commission
Statements of Net Position (Continued)
December 31, 2018 and 2017

	<u>2018</u>	<u>2017</u>
Liabilities		
Current Liabilities		
Current portion of long-term debt	85,000	85,000
Accounts payable	39,746	33,081
Accrued interest payable	47	47
Accrued salaries and taxes payable	71,391	60,741
Other current liabilities	1,588	1,112
Total Current Liabilities	197,772	179,981
Noncurrent Liabilities		
Customer deposits	44,554	33,108
Net pension liability	784,979	685,481
Net OPEB liability	228,824	235,431
Long-term debt, less current portion	2,075,000	2,160,000
Total Noncurrent Liabilities	3,133,357	3,114,020
Total Liabilities	3,331,129	3,294,001
Deferred Inflows of Resources		
Differences between expected and actual experience related to pensions	11,490	17,400
Differences between expected and actual experience related to OPEB	26,666	654
Net differences between projected and actual earnings on pension plan investments	9,412	-
Net differences between projected and actual earnings on OPEB plan investments	15,761	11,126
Changes of assumptions related to OPEB	529	-
Changes in proportion and differences between employer pension contributions and proportionate share of contributions	5,038	17,325
Changes in proportion and differences between employer OPEB contributions and proportionate share of contributions	443	546
Total Deferred Inflows of Resources	69,339	47,051
Net Position		
Net investment in capital assets	5,142,494	5,172,908
Restricted	50,843	39,057
Unrestricted (as restated)	231,301	423,733
Total Net Position	\$ 5,424,638	\$ 5,635,698

See accompanying notes to financial statements.

Knox County Utility Commission
Statements of Revenues, Expenses and Changes in Net Position
For the Years Ended December 31, 2018 and 2017

	<u>2018</u>	<u>2017</u>
Operating Revenues		
Water sales	\$ 1,349,944	\$ 1,379,471
Sewer sales	26,622	25,653
Service charges	15,830	17,415
Tap fees	15,600	8,000
Penalties	39,311	39,404
Other revenues	7,310	5,530
Total Operating Revenues	<u>1,454,617</u>	<u>1,475,473</u>
Operating Expenses		
Salaries and wages	362,859	331,002
Employee benefits	349,023	295,342
Purchased power	224,486	182,537
Utilities	66,520	60,725
Chemicals	89,330	62,103
Repairs and maintenance	64,523	33,867
Contracted services	27,315	32,303
Vehicle and equipment expenses	31,918	22,986
Insurance	42,313	35,811
Sewer treatment	25,150	24,876
Amortization	3,064	3,064
Depreciation	233,959	232,802
Bad debt expense, net of recoveries	19,469	22,083
Other operating expenses	69,602	51,790
Total Operating Expenses	<u>1,609,531</u>	<u>1,391,291</u>
Operating Income (Loss)	<u>(154,914)</u>	<u>84,182</u>
Non-operating Revenues (Expenses)		
Interest income	6,251	5,705
Federal and state grants	8,553	14,544
Gain on disposal of assets	1,325	6,745
Interest expense	(72,275)	(75,483)
Total Non-operating Revenues (Expenses)	<u>(56,146)</u>	<u>(48,489)</u>
Change in Net Position	(211,060)	35,693
Net Position, Beginning of Year (as previously reported)	5,635,698	5,789,472
Prior period adjustment	-	(189,467)
Net Position, Beginning of Year (as restated)	<u>5,635,698</u>	<u>5,600,005</u>
Net Position, End of Year	<u>\$ 5,424,638</u>	<u>\$ 5,635,698</u>

See accompanying notes to financial statements.

Knox County Utility Commission
Statements of Cash Flows
For the Years Ended December 31, 2018 and 2017

	<u>2018</u>	<u>2017</u>
Cash Flows From Operating Activities		
Receipts from customers	\$ 1,466,735	\$ 1,456,308
Receipts from other activities	7,310	5,530
Payments to employees	(248,554)	(250,582)
Payments to suppliers	(1,003,507)	(828,769)
Net Cash Provided by Operating Activities	<u>221,984</u>	<u>382,487</u>
Cash Flows From Capital and Related Financing Activities		
Purchases of property, plant and equipment	(118,545)	(70,576)
Proceeds on sale of equipment	1,325	6,745
Principal payments on debt	(85,000)	(95,000)
Interest payments on debt	(72,275)	(75,483)
Federal, state and local grants	8,553	14,544
Net Cash Used by Capital and Related Financing Activities	<u>(265,942)</u>	<u>(219,770)</u>
Cash Flows From Investing Activities		
Interest on cash and investments	6,251	5,705
Net Cash Provided by Investing Activities	<u>6,251</u>	<u>5,705</u>
Net Increase (Decrease) in Cash and Cash Equivalents	(37,707)	168,422
Cash and Cash Equivalents at Beginning of Year	<u>1,028,990</u>	<u>860,568</u>
Cash and Cash Equivalents at End of Year	<u>\$ 991,283</u>	<u>\$ 1,028,990</u>
Reconciliation of Cash and Cash Equivalents at End of Year		
Cash and Cash Equivalents	\$ 940,440	\$ 989,933
Restricted Cash and Cash Equivalents	50,843	39,057
Total Cash and Cash Equivalents at End of Year	<u>\$ 991,283</u>	<u>\$ 1,028,990</u>

Knox County Utility Commission
 Statements of Cash Flows (Continued)
 For the Years Ended December 31, 2018 and 2017

	<u>2018</u>	<u>2017</u>
Reconciliation of Operating Income (Loss) to Net Cash		
Provided by Operating Activities:		
Operating income (loss)	\$ (154,914)	\$ 84,182
Adjustments to reconcile operating income (loss) to net cash provided by operating activities		
Depreciation	233,959	232,802
Amortization	3,064	3,064
(Increase) Decrease in:		
Accounts receivable	(11,984)	10,448
Unbilled accounts receivable	19,490	(26,919)
Inventory	206	1,795
Prepaid expenses and other assets	(727)	(3,911)
Deferred pension & OPEB costs	10,762	(75,216)
Increase (Decrease) in:		
Accounts payable	6,665	(2,230)
Customer deposits	11,446	2,456
Accrued expenses	10,650	4,054
Other current liabilities	476	380
Net pension & OPEB liabilities	92,891	151,582
Net Cash Provided by Operating Activities	\$ 221,984	\$ 382,487

Knox County Utility Commission
Notes to Financial Statements
December 31, 2018 and 2017

Note 1 – Summary of Significant Accounting Policies

Reporting Entity

The Knox County Utility Commission, of Knox County, Kentucky (the Commission) was created in 2001 from a merger of the East Knox Water District and the Dewitt Water District. Water Districts are organized under Chapter 74 of the Kentucky Revised Statutes. The Commission is governed by a five person board of Commissioners which is appointed by the Knox County Fiscal Court. The Commission is regulated by the Kentucky Public Service Commission.

The Commission is a rural water utility system whose purpose is to provide water and sewer services to its customers in a portion of Knox County, Kentucky. The Commission's primary source of revenue is from water and sewer sales to its customers, including public bodies and local businesses in its service area.

Basis of Accounting, Financial Presentation and Measurement Focus

The basic financial statements of the Commission have been prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP") as applied to governmental units. The Governmental Accounting Standards Board ("GASB") is the standard-setting body for governmental accounting and financial reporting. The GASB periodically updates its codification of the existing Governmental Accounting and Financial Reporting Standards which, along with subsequent GASB pronouncements (Statements and Interpretations), constitutes GAAP for governmental units.

The Commission applies all relevant Financial Accounting Standards Board (FASB) pronouncements and Accounting Principles Board (APB) opinions issued on or before November 30, 1989, unless those pronouncements conflict or contradict GASB pronouncements, in which case, GASB prevails. In addition, the Commission applies all applicable FASB Statements and Interpretations issued after November 30, 1989, except those that conflict with or contradict GASB pronouncements.

The Statements of Net Position and Statements of Revenues, Expenses and Changes in Net Position display information about the Commission as a whole. These statements include all funds of the Commission. The statements distinguish between governmental and business-type activities. The Commission does not have any governmental activities.

The financial statements are prepared using the accrual basis of accounting. Revenues are recognized when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows.

Operating income reported by the Commission includes revenues and expenses related to the continuing operation of water and sewer service for its customers. Principal operating revenues are charges to customers for services. Principal operating expenses are the costs of providing the services and include administrative expenses and depreciation of capital assets. Other revenues and expenses are classified as non-operating in the financial statements.

Cash and Cash Equivalents

The Commission considers demand deposits and certificates of deposit with maturities of less than three months to be cash equivalents.

Knox County Utility Commission
Notes to Financial Statements (Continued)
December 31, 2018 and 2017

Note 1 - Summary of Significant Accounting Policies (Continued)

Investments

The Commission is authorized by state statute to invest in: 1) obligations of the United States and of its agencies and instrumentalities; 2) bonds or certificates of indebtedness of this state and of its agencies and instrumentalities; 3) shares of any savings and loan insured by an agency of the government of the United States up to the amount so insured; 4) interest bearing deposits in nationally chartered or state banks chartered in Kentucky and insured by an agency of the government of the United States up to the amount so insured, and in larger amounts provided such bank shall pledge as security obligations of the United States government, its agencies and instrumentalities.

Accounts Receivable

Receivables include amounts due from customers for water and sewer services. These receivables are due at the time the services are billed. Billing is completed monthly and accounts are considered past due on the twenty-first day after the end of each billing period. Accounts receivable are presented net of uncollectible accounts. The allowance amount is estimated using a percentage of accounts past due more than 90 days. At December 31, 2018 and 2017, the allowance for doubtful accounts totaled \$15,500.

Unbilled Accounts Receivable

Estimated unbilled revenues from water and sewer sales are recognized at the end of each fiscal year on a pro rata basis. The estimated amount is based on billing during the month following the close of the fiscal year.

Inventories and Prepaid Expenses

Inventories consist of expendable supplies held for consumption stated on a first-in, first-out basis. They are reported at cost and are recorded as an expense at the time individual items are used. Prepaid expenses include payments to vendors that benefit future reporting periods and are reported on the consumption basis.

Capital Assets

The Commission's property, plant and equipment with useful lives of more than one year are stated at historical cost. The costs of normal maintenance and repairs that do not add to the asset value or materially extend useful lives are not capitalized. Capital assets are depreciated using the straight-line method. When assets are disposed, the cost and applicable accumulated depreciation are removed from the respective accounts, and the resulting gain or loss is recorded in operations.

Estimated useful lives for depreciable assets are as follows:

<u>Asset Classification</u>	<u>Range of Lives</u>
Structures and improvements	35-40 years
Transmission distribution mains	50-75 years
Meters and services	30-50 years
Other equipment and vehicles	5-20 years

Knox County Utility Commission
Notes to Financial Statements (Continued)
December 31, 2018 and 2017

Note 1 – Significant Accounting Policies (Continued)

Customer Deposits

The Commission collects and holds in escrow an \$80 deposit from customers to ensure collection of its water and sewer charges. Interest at an annual rate of 1.41% is paid on these deposits.

Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles 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.

Net Position

Net position is comprised of the various net earnings from operating income, non-operating revenues and expenses, and capital contributions. Net position is classified in the following three components:

Net investment in capital assets – This component of net position consists of capital assets, net of accumulated depreciation, reduced by the outstanding balances of any bonds, mortgages, notes or other borrowings that are attributable to the acquisition, construction or improvement of those assets.

Restricted – This component of net position consists of restricted assets less liabilities and deferred inflows of resources related to those assets. Restricted assets are those with limits on their use that are externally imposed constraints imposed by creditors (such as through debt covenants), grantors, contributors, or laws or regulations of other governments or constraints imposed by law through constitutional provisions or enabling legislation.

Unrestricted – This component of net position consists of net amounts of the assets, deferred outflows of resources, liabilities, and deferred inflows of resources that are not included in the determination of the net investment in capital assets or the restricted component of net position.

When an expense is incurred for purposes for which both restricted and unrestricted net position are available, the Commission would typically use restricted assets first, but reserves the right to selectively spend unrestricted assets first.

Pensions & OPEB

For purposes of measuring net pension liability, net OPEB liability, deferred outflows of resources and deferred inflows of resources related to pensions & OPEB, and pension and OPEB 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. For this purpose, benefit payments (including refunds of employee contributions) are recognized when due and payable in accordance with the benefit terms. The plan's financial statements are prepared using the accrual basis of accounting and are prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) that apply to governmental accounting for fiduciary funds. Investments are reported at fair value.

Knox County Utility Commission
Notes to Financial Statements (Continued)
December 31, 2018 and 2017

Note 2 – Restricted Assets

Restricted assets consist of customer water and sewer deposits. The balance of customer deposits held at December 31, 2018 and 2017 was \$50,843 and \$39,057, respectively.

Note 3 – Kentucky Revised Statute

At December 31, 2018 and 2017, all of the cash of the Commission was covered by federal depository insurance and securities pledged as collateral on behalf of the Commission. In accordance with Kentucky Revised Statute (KRS) 91A.060, the deposits are to be insured by the Federal Depository Insurance Corporation or collateralized to the extent uninsured by any obligations permitted by KRS 41.240(4). According to KRS 41.240(4), financial institutions shall either pledge or provide as collateral securities or other obligations having an aggregate current face value or current quoted market value at least equal to the deposits. According to KRS 91A.060, the Commission is allowed to invest in obligations of the U.S. Treasury and U.S. agencies, repurchase agreements, obligations of the Commonwealth of Kentucky and its agencies, interest bearing deposits of insured savings and loans, or interest bearing deposits of insured national or state banks. For additional cash descriptive information, see Note 1.

Note 4 – Custodial Credit Risk - Deposits

Custodial credit risk is the risk that in the event of a bank failure, the Commission's deposits may not be returned to it. The Commission does not have a deposit policy for custodial credit risk. As of December 31, 2018 and 2017, \$744,067 and \$774,210 of the Commission's total deposits at banks of \$994,067 and \$1,024,210, respectively, were exposed to custodial credit risk as follows:

	<u>2018</u>	<u>2017</u>
Uninsured and uncollateralized	\$ -	\$ -
Uninsured and collateral held by pledging bank	744,067	774,210
Uninsured and collateral held by pledging bank's trust department not in the Commission's name	-	-
Total	<u><u>\$ 744,067</u></u>	<u><u>\$ 774,210</u></u>

Knox County Utility Commission
Notes to Financial Statements (Continued)
December 31, 2018 and 2017

Note 5 – Capital Assets

The following is a summary of capital asset transactions for the year ended December 31, 2018:

	Balance Dec. 31, 2017	Additions	Dispositions	Balance Dec. 31, 2018
Land and land improvements	\$ 44,619	\$ -	\$ -	\$ 44,619
Structures and improvements	518,699	2,250	-	520,949
Pumping equipment	217,126	9,480	-	226,606
Meters and meter installation	816,036	58,898	-	874,934
Hydrants	53,816	-	-	53,816
Storage tanks	1,148,102	-	-	1,148,102
Transmission and distribution plant	10,416,631	-	-	10,416,631
Vehicles and other equipment	473,342	25,665	26,055	472,952
Office equipment	60,364	13,995	-	74,359
Lift stations	344,195	-	-	344,195
Construction in progress	7,543	8,256	-	15,799
Totals at historical cost	<u>14,100,473</u>	<u>118,544</u>	<u>26,055</u>	<u>14,192,962</u>
Less accumulated depreciation for:				
Structures and improvements	436,500	5,374	-	441,874
Pumping equipment	115,682	8,372	-	124,054
Meters and meter installation	530,866	14,236	-	545,102
Hydrants	39,811	903	-	40,714
Storage tanks	566,397	21,569	-	587,966
Transmission and distribution plant	4,403,337	160,134	-	4,563,471
Vehicles and other equipment	392,074	12,208	26,055	378,227
Office equipment	55,657	3,513	-	59,170
Lift stations	142,241	7,649	-	149,890
Total accumulated depreciation	<u>6,682,565</u>	<u>233,958</u>	<u>26,055</u>	<u>6,890,468</u>
Capital assets - net	<u>\$ 7,417,908</u>	<u>\$ (115,414)</u>	<u>\$ -</u>	<u>\$ 7,302,494</u>

Knox County Utility Commission
Notes to Financial Statements (Continued)
December 31, 2018 and 2017

Note 5 – Capital Assets (Continued)

The following is a summary of capital asset transactions for the year ended December 31, 2017:

	Balance Dec. 31, 2016	Additions	Dispositions	Balance Dec. 31, 2017
Land and land improvements	\$ 44,619	\$ -	\$ -	\$ 44,619
Structures and improvements	511,387	7,312	-	518,699
Pumping equipment	207,431	9,695	-	217,126
Meters and meter installation	794,186	21,850	-	816,036
Hydrants	53,816	-	-	53,816
Storage tanks	1,148,102	-	-	1,148,102
Transmission and distribution plant	10,416,631	-	-	10,416,631
Vehicles and other equipment	464,215	24,127	15,000	473,342
Office equipment	60,315	49	-	60,364
Lift stations	344,195	-	-	344,195
Construction in progress	-	7,543	-	7,543
Totals at historical cost	<u>14,044,897</u>	<u>70,576</u>	<u>15,000</u>	<u>14,100,473</u>
Less accumulated depreciation for:				
Structures and improvements	431,239	5,261	-	436,500
Pumping equipment	107,638	8,044	-	115,682
Meters and meter installation	516,743	14,123	-	530,866
Hydrants	38,855	956	-	39,811
Storage tanks	544,828	21,569	-	566,397
Transmission and distribution plant	4,243,204	160,133	-	4,403,337
Vehicles and other equipment	395,268	11,806	15,000	392,074
Office equipment	52,396	3,261	-	55,657
Lift stations	134,592	7,649	-	142,241
Total accumulated depreciation	<u>6,464,763</u>	<u>232,802</u>	<u>15,000</u>	<u>6,682,565</u>
Capital assets - net	<u>\$ 7,580,134</u>	<u>\$ (162,226)</u>	<u>\$ -</u>	<u>\$ 7,417,908</u>

Knox County Utility Commission
Notes to Financial Statements (Continued)
December 31, 2018 and 2017

Note 6 – Long-Term Debt

The following is a summary of long-term debt transactions for the year ended December 31, 2018:

	<u>Balance</u> <u>Dec. 31, 2017</u>	<u>Additions</u>	<u>Payments</u>	<u>Balance</u> <u>Dec. 31, 2018</u>	<u>Due Within</u> <u>One Year</u>
Loan payable to Kentucky Rural Water Finance Corporation, payable annually in varying principal amounts, with final payment due January 1, 2039; interest payable on a semi-annual basis at rates varying from 2.25% to 3.5%	\$ 2,245,000	\$ -	\$ 85,000	\$ 2,160,000	\$ 85,000
	<u>\$ 2,245,000</u>	<u>\$ -</u>	<u>\$ 85,000</u>	<u>\$ 2,160,000</u>	<u>\$ 85,000</u>

The following is a summary of long-term debt transactions for the year ended December 31, 2017:

	<u>Balance</u> <u>Dec. 31, 2016</u>	<u>Additions</u>	<u>Payments</u>	<u>Balance</u> <u>Dec. 31, 2017</u>	<u>Due Within</u> <u>One Year</u>
Loan payable to Kentucky Rural Water Finance Corporation, payable annually in varying principal amounts, with final payment due January 1, 2039; interest payable on a semi-annual basis at rates varying from 2.25% to 3.5%	\$ 2,340,000	\$ -	\$ 95,000	\$ 2,245,000	\$ 85,000
	<u>\$ 2,340,000</u>	<u>\$ -</u>	<u>\$ 95,000</u>	<u>\$ 2,245,000</u>	<u>\$ 85,000</u>

The aggregate annual principal repayments on long-term debt are summarized as follows:

<u>Year ending</u> <u>December 31:</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2019	\$ 85,000	\$ 70,200	\$ 155,200
2020	90,000	68,288	158,288
2021	90,000	66,263	156,263
2022	95,000	63,338	158,338
2023	95,000	60,250	155,250
2024-2028	530,000	252,175	782,175
2029-2033	590,000	160,694	750,694
2034-2035	585,000	62,650	647,650
Total	<u>\$ 2,160,000</u>	<u>\$ 803,858</u>	<u>\$ 2,963,858</u>

Knox County Utility Commission
Notes to Financial Statements (Continued)
December 31, 2018 and 2017

Note 7 – Retirement Plan

Knox County Utility Commission is a participating employer of the County Employees Retirement System (CERS). Under the provisions of Kentucky Revised Statute Section 61.645, the Board of Trustees of the Kentucky Retirement Systems administers CERS, in accordance with the provisions of Kentucky Revised Statute Sections 16.555, 61.570, and 78.630. The assets of the system are segregated by plan (KERS, CERS, and SPRS), where each system's assets are used only for the payment of benefits to the members of that plan and a pro rata share of administrative costs. The plan issues a publicly available financial report that includes financial statements and required supplementary information. That report may be downloaded from the Kentucky Retirement Systems website or may be obtained by writing to Kentucky Retirement Systems, 1260 Louisville Road, Frankfort, Kentucky 40601.

Plan Description

CERS is a cost sharing, multiple-employer, defined benefit pension plan that covers substantially all regular full-time members employed in non-hazardous and hazardous duty positions of each participating state department, board, agency, county, city, school board, and any additional eligible local agencies electing to participate in the System.

Benefits Provided

The plan provides for retirement, disability, and death benefits to plan members. Retirement benefits may be extended to beneficiaries of plan members under certain circumstances. Benefits under the plan will vary based on final compensation, years of service and other factors as fully described in the Plan documents. Cost-of-living adjustments (COLA) are provided at the discretion of state legislature.

Contributions

Funding for the plan is provided through payroll withholdings and contributions by the Commission. All employees meeting the requirements for membership are required to contribute a percentage of their gross wages. For the years ended December 31, 2018 and 2017, plan members in non-hazardous positions were required to contribute 5% of the employee's total compensation subject to contribution. Employees hired after September 1, 2008 are required to contribute an additional 1% to cover the cost of medical insurance that is provided through CERS. Participating employers are required to contribute at an actuarially determined rate. Per Kentucky Revised Statute Section 61.565, normal contribution and past service contribution rates shall be determined by the Kentucky Retirement Systems Board of Trustees on the basis of the annual actuarial valuation last preceding the July 1 of a new biennium. The Board may amend contribution rates as of July 1 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 in accordance with the actuarial basis adopted by the Board. The Commission's required contribution rates for the year ended December 31, 2018 were 19.18% (January through June 2018) and 21.48% (July through December 2018). The Commission's required contribution rates for the year ended December 31, 2017 were 18.68% (January through June 2017) and 19.18% (July through December 2017). Required contribution rates were actuarially determined and adopted by the Kentucky Retirement Systems Board of Trustees. Administrative costs of the Kentucky Retirement System are financed through employer contributions and investment earnings.

Knox County Utility Commission
Notes to Financial Statements (Continued)
December 31, 2018 and 2017

Note 7 – Retirement Plan (Continued)

Contributions (Continued)

Plan members who began participating on or after January 1, 2014 are required to contribute to the Cash Balance Plan. 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. A Cash Balance Plan resembles a defined contribution plan because it determines the value of benefits for each participant based on individual accounts. However, the assets of the plan remain in a single investment pool like a traditional defined benefit plan. A Cash Balance Plan resembles a defined benefit plan since it uses a specific formula to determine benefits. Members and employers contribute specified percentages of the member's wages each month to the member's account. Non-hazardous plan members are required to contribute 5% of wages to their individual account. All members are required to contribute 1% to the health insurance fund. The employer contribution rate is set annually by the Board based on an actuarial valuation. 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 account earns a guaranteed amount of interest, 4% on both the member contributions and the Employer Pay Credit Balance, at the end of each fiscal year. If the member contributed to the plan during the fiscal year, there may be additional interest credit added to the member's account depending on Kentucky Retirement Systems' investment returns. This "upside" interest sharing is based on the 5-year average geometric investment return. If it exceeds 4% the member's account will be credited with 75% of the amount of the returns over 4% on the account balance as of June 30 of the previous year. For the fiscal years ended June 30, 2018 and 2017, the interest earned on CERS non-hazardous plans was 6.54% and 7.85%, respectively.

The Commission's payroll for the years ended December 31, 2018, 2017, and 2016 was \$335,581, \$301,660, and \$254,414, respectively, all of which was covered by CERS. The Commission's contribution requirements for CERS for the years ended December 31, 2018, 2017, and 2016 were \$68,192 (\$51,488 allocated to the CERS pension fund and \$16,704 allocated to the CERS insurance fund), \$57,101 (\$42,878 allocated to the CERS pension fund and \$14,223 allocated to the CERS insurance fund), and \$45,570 (\$33,645 allocated to the CERS pension fund and \$11,925 allocated to the CERS insurance fund), respectively. The Commission contributed 100% of their required contributions for the years ended December 31, 2018, 2017, and 2016.

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

At December 31, 2018 and 2017, the Commission reported a liability of \$784,979 and \$685,481, respectively for their proportionate share of the net pension liability. The net pension liability was measured as of June 30, 2018 and 2017, respectively, and the total pension liability used to calculate net pension liability was determined by an actuarial valuation as of those dates. The Commission's proportion of the net pension liability was based on a projection of the Commission's long-term share of contributions to the pension plan relative to the projected contributions of all participating plan members, as actuarially determined. At the June 30, 2018 and 2017 measurement dates, the Commission's proportion was 0.01289% and 0.01171%, respectively.

Knox County Utility Commission
Notes to Financial Statements (Continued)
December 31, 2018 and 2017

Note 7 – Retirement Plan (Continued)

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

For financial reporting, the actuarial valuation as of June 30, 2018, was performed by Gabriel Roeder Smith (GRS). The total pension liability, net pension liability, and sensitivity information as of June 30, 2018 were based on an actuarial valuation date of June 30, 2017. The total pension liability was rolled forward from the valuation date (June 30, 2017) to the plan's fiscal year ending June 30, 2018, using generally accepted actuarial principles. There have been no changes in actuarial assumptions since June 30, 2017. The actuarial assumptions are:

Inflation	2.30%
Salary Increase	3.05%
Investment Rate of Return	6.25% for CERS non-hazardous and hazardous

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

The Commission recognized pension expense of \$142,528 and \$119,244 for the years ended December 31, 2018 and 2017, respectively. At December 31, 2018, the Commission reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

	Deferred Outflows of Resources	Deferred Inflows of Resources
Difference between expected and actual experience	\$ 25,604	\$ 11,490
Net difference between projected and actual investment earnings on pension plan investments	-	9,412
Changes of assumptions	76,715	-
Changes in proportion and differences between employer contributions and proportionate share of pension contributions	56,472	5,038
Employer pension contributions subsequent to the measurement date	26,989	-
Total	<u>\$ 185,780</u>	<u>\$ 25,940</u>

Deferred outflows and inflows related to differences between projected and actual earnings on plan investments are netted and amortized over a closed five-year period. Deferred outflows and inflows related to experience gains/losses, the impact of changes in actuarial assumptions, changes in the employer's proportionate share of net pension liability, and differences between employer contributions and the proportionate share of contributions are amortized over the average remaining service life of the active and inactive System members at the beginning of the fiscal year.

Knox County Utility Commission
Notes to Financial Statements (Continued)
December 31, 2018 and 2017

Note 7 – Retirement Plan (Continued)

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

\$26,989 reported as deferred outflows of resources related to pensions resulting from Commission contributions subsequent to the measurement date will be recognized as a reduction of the net pension liability in the year ended December 31, 2019. Other amounts reported as deferred outflows of resources related to pensions will be recognized in pension expense as follows:

Year ended December 31:

	2019	\$	85,278
	2020		53,300
	2021		(1,515)
	2022		(4,212)
	2023		-
	Thereafter		-
Total		<u>\$</u>	<u>132,851</u>

At December 31, 2017, the Commission reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

	<u>Deferred Outflows of Resources</u>	<u>Deferred Inflows of Resources</u>
Difference between expected and actual experience	\$ 850	\$ 17,400
Net difference between projected and actual investment earnings on pension plan investments	8,478	-
Changes of assumptions	126,490	-
Changes in proportion and differences between employer contributions and proportionate share of pension contributions	28,531	17,325
Employer pension contributions subsequent to the measurement date	21,757	-
Total	<u>\$ 186,106</u>	<u>\$ 34,725</u>

Knox County Utility Commission
Notes to Financial Statements (Continued)
December 31, 2018 and 2017

Note 7 – Retirement Plan (Continued)

Actuarial Assumptions

The following actuarial methods and assumptions were used to determine the actuarially determined contributions effective for the fiscal year ending June 30, 2018:

Valuation Date	June 30, 2016
Experience Study	July 1, 2008 - June 30, 2013
Actuarial Cost Method	Entry Age Normal
Amortization Method	Level percent of pay
Remaining Amortization Period	27 years, closed
Payroll Growth Rate	4.00%
Asset Valuation Method	20% of the difference between the market value of assets and the expected actuarial value of assets is recognized
Inflation	3.25%
Salary Increase	4.00%, average
Investment Rate of Return	7.50%

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.

Knox County Utility Commission
Notes to Financial Statements (Continued)
December 31, 2018 and 2017

Note 7 – Retirement Plan (Continued)

Actuarial Assumptions (Continued)

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

Asset Class	Target Allocation	Long-Term Expected Real Rate of Return
US Equity*	17.50%	
US Large Cap	5.00%	4.50%
US Mid Cap	6.00%	4.50%
US Small Cap	6.50%	5.50%
Non US Equity*	17.50%	
International Developed	12.50%	6.50%
Emerging Markets	5.00%	7.25%
Global Bonds	4.00%	3.00%
Credit Fixed	24.00%	
Global IG Credit	2.00%	3.75%
High Yield	7.00%	5.50%
Emerging Market Debt	5.00%	6.00%
Illiquid Private	10.00%	8.50%
Private Equity	10.00%	6.50%
Real Estate*	5.00%	9.00%
Absolute Return	10.00%	5.00%
Real Return*	10.00%	7.00%
Cash	2.00%	1.50%
Total	100.00%	6.09%

*Long-Term Expected Real Rates of Return may vary by plans depending on the risk tolerance of the plan

Discount Rate

The discount rate used to measure the total pension liability was 6.25 percent. 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 25 years (closed) amortization period of the unfunded actuarial accrued liability. The discount rate determination does not use a municipal bond rate. The target asset allocation and best estimates of arithmetic nominal rates of return for each major asset class are summarized in the CAFR. Projected future benefit payments for all current plan members were projected through 2117.

Knox County Utility Commission
Notes to Financial Statements (Continued)
December 31, 2018 and 2017

Note 7 – Retirement Plan (Continued)

Sensitivity of the Commission’s Proportionate Share of the Net Pension Liability to Changes in the Discount Rate

The following table presents the net pension liability of the Commission’s CERS pension plan, calculated using the discount rate of 6.25 percent, as well as what the Commission’s 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%)
Commission's net pension liability	\$ 988,208	\$ 784,979	\$ 614,710

Payable to the Pension Plan

At December 31, 2018 and 2017, the Commission reported payables of \$6,930 and \$7,125 for the outstanding amounts of contributions to the pension plan required for the years ended December 31, 2018 and 2017, respectively.

Note 8 –OPEB Plan

During the year ended December 31, 2018, the Commission adopted new accounting guidance, *GASB Statement No. 75, Accounting and Financial Reporting for Postemployment Benefits Other than Pensions*. The objective of this Statement is to address accounting and financial reporting for Other Postemployment Benefits (OPEB) that are provided to the employees of state and local governmental employers. In accordance with GASB 75, a prior period adjustment of \$189,467 was made to reduce beginning net position to record the Commission’s share of the net OPEB liability.

Plan Description

As a participating employer of the County Employees’ Retirement System (CERS), the Commission also participates in the County Employees Retirement System Insurance Fund (Insurance Fund). Under the provisions of Kentucky Revised Statute Sections 61.645 and 61.701, the Board of Trustees of Kentucky Retirement Systems administers the Kentucky Retirement Systems Insurance Fund (KERS), County Employees Retirement System (CERS) and State Police Retirement System (SPRS). The statutes provide for a single insurance fund to provide group hospital and medical benefits to retirees drawing a benefit from the three pension funds administered by Kentucky Retirement Systems (KERS, CERS, and SPRS). The assets of the Insurance Fund are also segregated by plan. The plan issues a publicly available financial report that includes financial statements and required supplementary information. That report may be downloaded from the Kentucky Retirement Systems website or may be obtained by writing to Kentucky Retirement Systems, 1260 Louisville Road, Frankfort, Kentucky 40601.

CERS Insurance Fund is a cost sharing, multiple-employer, defined benefit OPEB plan that covers substantially all regular full-time members employed in non-hazardous and hazardous duty positions of each participating state department, board, agency, county, city, school board, and any additional eligible local agencies electing to participate in the System.

Knox County Utility Commission
Notes to Financial Statements (Continued)
December 31, 2018 and 2017

Note 8 –OPEB Plan (Continued)

Plan Membership

The net OPEB liability was calculated based on the Insurance plan membership as of June 30, 2017:

Membership Status	Non-Hazardous
Inactive plan members currently receiving benefits	33,481
Inactive plan members entitled to but not yet receiving benefits	8,230
Active plan members	81,891
Total Membership	123,602

Benefits Provided

The Insurance Fund was established to provide hospital and medical insurance for eligible members receiving benefits from KERS, CERS, and SPRS. The eligible non-Medicare retirees are covered by the Department of Employee Insurance (DEI) plans. Kentucky Retirement Systems submits the premium payments to DEI. The Board contracts with Humana to provide health care benefits to the eligible Medicare retirees through a Medicare Advantage Plan. The Insurance Fund pays a prescribed contribution for whole or partial payment of required premiums to purchase hospital and medical insurance. The Insurance Fund pays a proportion of hospital and medical insurance premiums for the spouse and dependents of retired hazardous members killed in the line of duty. The amount of contribution paid by the Insurance Fund is based on years of service. Additional details can be found in the publicly available Kentucky Retirement Systems Comprehensive Annual Financial Report which may be downloaded from the Kentucky Retirement Systems website.

Contributions

Funding for the plan is provided through payroll withholdings and contributions by the Commission. See Note 7 for a description of the Commission’s covered payroll and contribution requirements as well as the breakdown of contributions between the pension and insurance funds.

OPEB Liabilities, OPEB Expense, and Deferred Outflows of Resources and Deferred Inflows of Resources Related to OPEB

At December 31, 2018 the Commission reported a liability of \$228,824 for its proportionate share of the net OPEB liability. The net OPEB liability was measured as of June 30, 2018, and the total OPEB liability used to calculate net OPEB liability was determined by an actuarial valuation as of that date. The Commission’s proportion of the net OPEB liability was based on a projection of the Commission’s long-term share of contributions to the OPEB plan relative to the projected contributions of all participating plan members, as actuarially determined. At the June 30, 2018 measurement date, the Commission’s proportion was 0.01289 percent.

Knox County Utility Commission
Notes to Financial Statements (Continued)
December 31, 2018 and 2017

Note 8 –OPEB Plan (Continued)

OPEB Liabilities, OPEB Expense, and Deferred Outflows of Resources and Deferred Inflows of Resources Related to OPEB (Continued)

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

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

Inflation	2.30%
Payroll Growth Rate	2.00% for CERS non-hazardous and hazardous
Salary Increases	3.05%, average
Investment Rate of Return	6.25%
Healthcare Trend Rates	
Pre - 65	Initial trend starting at 7.00% at January 1, 2020, and gradually decreasing to an ultimate trend rate of 4.05% over a period of 12 years.
Post - 65	Initial trend starting at 5.00% at January 1, 2020, and gradually decreasing to an ultimate trend rate of 4.05% over a period of 10 years.

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

The long-term expected return was determined by using the building-block method in which best-estimate ranges of expected future real rates of returns are developed for each asset class. The ranges are combined by weighting the expected future real rate of return by the target allocation percentage. The target allocation and best estimates of arithmetic real rates of return for each major asset class are the same as those adopted for the CERS Pension Plan and are summarized in the table in Note 7.

Knox County Utility Commission
Notes to Financial Statements (Continued)
December 31, 2018 and 2017

Note 8 –OPEB Plan (Continued)

OPEB Liabilities, OPEB Expense, and Deferred Outflows of Resources and Deferred Inflows of Resources Related to OPEB (Continued)

The Commission recognized OPEB expense of \$32,050 for the year ended December 31, 2018. At December 31, 2018, the Commission reported deferred outflows of resources and deferred inflows of resources related to OPEB from the following sources:

	Deferred Outflows of Resources	Deferred Inflows of Resources
Difference between expected and actual experience	\$ -	\$ 26,666
Net difference between projected and actual investment earnings on OPEB plan investments	-	15,761
Changes of assumptions	45,700	529
Changes in proportion and differences between employer contributions and proportionate share of OPEB contributions	15,690	443
Employer OPEB contributions subsequent to the measurement date	8,752	-
Total	\$ 70,142	\$ 43,399

Deferred outflows and inflows related to differences between projected and actual earnings on plan investments are netted and amortized over a closed five-year period. Deferred outflows and inflows related to experience gains/losses, the impact of changes in actuarial assumptions, changes in the employer's proportionate share of net OPEB liability, and differences between employer contributions and the proportionate share of contributions are amortized over the average remaining service life of the active and inactive System members at the beginning of the fiscal year.

The \$8,752 reported as deferred outflows of resources related to OPEB resulting from the Commission's contributions subsequent to the measurement date will be recognized as a reduction of the net pension liability in the year ending December 31, 2019. Other amounts reported as deferred outflows of resources related to pensions will be recognized in OPEB expense as follows:

Year ended December 31:

	2019	\$	3,671
	2020		3,671
	2021		3,671
	2022		6,733
	2023		861
	Thereafter		(616)
Total		\$	17,991

Knox County Utility Commission
Notes to Financial Statements (Continued)
December 31, 2018 and 2017

Note 8 –OPEB Plan (Continued)

Investment Policy

Kentucky Revised Statute 61.650 grants the responsibility for the investment of plan assets to the Kentucky Retirement System Board. The Board has established an Investment Committee which is specifically charged with oversight and investment of plan assets. The Investment Committee recognizes their duty to invest the funds in accordance with the “Prudent Person Rule” (set forth in Kentucky Revised Statute 61.650) and manage those funds consistent with the long-term nature of the systems. The Investment Committee has adopted a Statement of Investment Policy that contains guidelines and restrictions for deposits and investments. By statute, all investments are to be registered and held in the name of Kentucky Retirement Systems. The Statement of Investment Policy contains the specific guidelines for the investment of Pension and Insurance assets. The target allocation and best estimates of arithmetic real rates of return for each major asset class adopted by the Kentucky Retirement System Board for the Insurance Plan are the same as those adopted for the CERS Pension Plan (See Note 7).

Net OPEB Liability

The components of the net OPEB liability of the participating employers in the CERS Non-Hazardous System and the Commission’s proportionate share at June 30, 2018 were as follows:

	Total CERS Non- Hazardous System	Commission's Proportionate Share
Total OPEB liability	\$ 4,189,606,000	\$ 539,956
Plan fiduciary net position	(2,414,126,000)	(311,132)
Employers' Net OPEB Liability	\$ 1,775,480,000	\$ 228,824
 Plan Fiduciary Net Position as a Percentage of the Total OPEB Liability	57.62%	57.62%

Knox County Utility Commission
Notes to Financial Statements (Continued)
December 31, 2018 and 2017

Note 8 –OPEB Plan (Continued)

Actuarial Methods and Assumptions

The following actuarial methods and assumptions were used to determine the actuarially determined contributions effective for the fiscal year ending June 30, 2018:

Valuation Date	June 30, 2016
Experience Study	July 1, 2008 - June 30, 2013
Actuarial Cost Method	Entry Age Normal
Amortization Method	Level percent of pay
Remaining Amortization Period	27 years, closed
Payroll Growth Rate	4.00%
Asset Valuation Method	20% of the difference between the market value of assets and the expected actuarial value of assets is recognized
Inflation	3.25%
Salary Increases	4.00%, average
Investment Rate of Return	7.50%
Healthcare Trend Rates	
Pre - 65	Initial trend starting at 7.50% and gradually decreasing to an ultimate trend rate of 5.00% over a period of 5 years.
Post - 65	Initial trend starting at 5.50% and gradually decreasing to an ultimate trend rate of 5.00% over a period of 2 years.

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

Discount Rate

The discount rate used to measure the total OPEB liability was 5.85 percent. 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 25 years (closed) amortization period of the unfunded actuarial accrued liability. The discount rate determination used an expected rate of return of 6.25% and a municipal bond rate of 3.62%, as reported in Fidelity Index's "20 – Year Municipal GO AA Index" as of June 30, 2018. However, the cost associated with the implicit employer subsidy was not included in the calculation of the System's actuarial determined contributions, and any cost associated with the implicit subsidy will not be paid out of the System's trusts. Therefore, the municipal bond rate was applied to future expected benefit payments associated with the implicit subsidy.

Knox County Utility Commission
Notes to Financial Statements (Continued)
December 31, 2018 and 2017

Note 8 – OPEB Plan (Continued)

Sensitivity of the Commission's Proportionate Share of the Net OPEB Liability to Changes in the Discount Rate

The following presents the Commission's proportionate share of the net OPEB liability calculated using the discount rate of 5.85 percent, as well as what the Commission's proportionate share of the net OPEB liability would be if it were calculated using a discount rate that is 1-percentage-point lower (4.85 percent) or 1-percentage-point higher (6.85 percent) than the current rate:

	1% Decrease (4.85%)	Current Discount Rate (5.85%)	1% Increase (6.85%)
Commission's net OPEB liability	\$ 297,206	\$ 228,824	\$ 170,575

Sensitivity of the Commission's Proportionate Share of the Net OPEB Liability to Changes in the Healthcare Cost Trend Rates

The following presents the Commission's proportionate share of the net OPEB liability calculated using the healthcare cost trend rate of 7.00 percent decreasing to 4.05%, as well as what the Commission's proportionate share of the net OPEB liability would be if it were calculated using a healthcare cost trend rate that is 1-percentage-point lower (6.00 percent decreasing to 3.05%) or 1-percentage-point higher (8.00 percent decreasing to 5.05%) than the current rate:

	1% Decrease	Current Healthcare Cost Trend Rate	1% Increase
Commission's net OPEB liability	\$ 170,362	\$ 228,824	\$ 297,734

Note 9 – Risk Management

The Commission is exposed to various risks of loss related to limited torts; theft of, damage to and destruction of assets; errors and omissions and natural disasters for which the Commission carries commercial insurance. There have been no significant reductions in coverage for the year and settlements have not exceeded coverage in the past three years.

Note 10 - Subsequent Events

Management of the Commission has evaluated subsequent events through June 28, 2019, the date on which the financial statements were available to be issued.

Knox County Utility Commission
 Departmental Statements of Net Position - Water Department
 December 31, 2018 and 2017

	<u>2018</u>	<u>2017</u>
Assets		
Current Assets		
Cash and cash equivalents	\$ 946,856	\$ 993,175
Receivables, less allowance	99,312	88,082
Unbilled accounts receivable	83,149	102,639
Inventories	24,600	24,806
Other current assets	5,252	4,525
Total Current Assets	1,159,169	1,213,227
Noncurrent Assets		
Restricted Assets		
Restricted cash and cash equivalents	50,843	39,057
Total Restricted Assets	50,843	39,057
Capital Assets		
Land and improvements	44,619	44,619
Structures and improvements	520,949	518,699
Pumping equipment	206,012	196,532
Meters and meter installation	874,839	815,941
Hydrants	53,816	53,816
Storage tanks	1,148,102	1,148,102
Transmission and distribution plant	9,886,781	9,886,781
Vehicles and other equipment	472,238	472,628
Office equipment	74,359	60,364
Construction in progress	15,799	7,543
Less: accumulated depreciation	(6,604,258)	(6,413,554)
Net Capital Assets	6,693,256	6,791,471
Total Noncurrent Assets	6,744,099	6,830,528
Total Assets	7,903,268	8,043,755
Deferred Outflows of Resources		
Bond issue costs, net of amortization	61,783	64,847
Differences between expected and actual experience related to pensions	25,604	850
Net differences between projected and actual earnings on pension plan investments	-	8,478
Changes of assumptions related to pensions	76,715	126,490
Changes of assumptions related to OPEB	45,700	51,228
Changes in proportion and differences between employer pension contributions and proportionate share of contributions	56,472	28,531
Changes in proportion and differences between employer OPEB contributions and proportionate share of contributions	15,690	-
Pension contributions subsequent to measurement date	26,989	21,757
OPEB contributions subsequent to measurement date	8,752	7,062
Total Deferred Outflows of Resources	317,705	309,243

See accompanying notes to financial statements.

Knox County Utility Commission
 Departmental Statements of Net Position - Water Department (Continued)
 December 31, 2018 and 2017

	<u>2018</u>	<u>2017</u>
Liabilities		
Current Liabilities		
Current portion of long-term debt	85,000	85,000
Accounts payable	38,073	30,151
Accrued interest payable	47	47
Accrued salaries and taxes payable	71,391	60,741
Other current liabilities	1,588	1,112
Total Current Liabilities	196,099	177,051
Noncurrent Liabilities		
Customer deposits	44,554	33,108
Net pension liability	784,979	685,481
Net OPEB liability	228,824	235,431
Long-term debt, less current portion	2,075,000	2,160,000
Total Noncurrent Liabilities	3,133,357	3,114,020
Total Liabilities	3,329,456	3,291,071
Deferred Inflows of Resources		
Differences between expected and actual experience related to pensions	11,490	17,400
Differences between expected and actual experience related to OPEB	26,666	654
Net differences between projected and actual earnings on pension plan investments	9,412	-
Net differences between projected and actual earnings on OPEB plan investments	15,761	11,126
Changes of assumptions related to OPEB	529	-
Changes in proportion and differences between employer pension contributions and proportionate share of contributions	5,038	17,325
Changes in proportion and differences between employer OPEB contributions and proportionate share of contributions	443	546
Total Deferred Inflows of Resources	69,339	47,051
Net Position		
Net investment in capital assets	4,533,256	4,546,471
Restricted	50,843	39,057
Unrestricted (as restated)	238,079	429,348
Total Net Position	\$ 4,822,178	\$ 5,014,876

Knox County Utility Commission
 Departmental Statements of Revenues, Expenses and Changes in Net Position - Water Department
 For the Years Ended December 31, 2018 and 2017

	<u>2018</u>	<u>2017</u>
Operating Revenues		
Water sales	\$ 1,349,944	\$ 1,379,471
Service charges	15,830	17,415
Tap fees	15,600	8,000
Penalties	39,180	39,275
Other revenues	7,310	5,530
Total Operating Revenues	<u>1,427,864</u>	<u>1,449,691</u>
Operating Expenses		
Salaries and wages	361,681	329,811
Employee benefits	348,933	295,251
Purchased power	224,486	182,537
Utilities	65,110	59,358
Chemicals	89,330	62,103
Repairs and maintenance	64,523	31,405
Contracted services	27,315	32,303
Vehicle and equipment expenses	31,918	22,986
Insurance	42,313	35,811
Amortization	3,064	3,064
Depreciation	216,760	215,603
Bad debt expense, net of recoveries	19,381	22,024
Other operating expenses	69,602	51,790
Total Operating Expenses	<u>1,564,416</u>	<u>1,344,046</u>
Operating Income (Loss)	<u>(136,552)</u>	<u>105,645</u>
Non-operating Revenues (Expenses)		
Interest income	6,251	5,705
Federal and state grants	8,553	14,544
Gain on disposal of assets	1,325	6,745
Interest expense	(72,275)	(75,483)
Total Non-operating Revenues (Expenses)	<u>(56,146)</u>	<u>(48,489)</u>
Change in Net Position	(192,698)	57,156
Net Position, Beginning of Year (as previously reported)	5,014,876	5,147,187
Prior period adjustment	-	(189,467)
Net Position, Beginning of Year (as restated)	<u>5,014,876</u>	<u>4,957,720</u>
Net Position, End of Year	<u>\$ 4,822,178</u>	<u>\$ 5,014,876</u>

Knox County Utility Commission
 Departmental Statements of Cash Flows - Water Department
 For the Years Ended December 31, 2018 and 2017

	<u>2018</u>	<u>2017</u>
Cash Flows From Operating Activities		
Receipts from customers	\$ 1,440,736	\$ 1,430,826
Receipts from other activities	7,310	5,530
Payments to employees	(247,376)	(249,391)
Payments to suppliers	(975,512)	(800,516)
Net Cash Provided by Operating Activities	<u>225,158</u>	<u>386,449</u>
 Cash Flows From Capital and Related Financing Activities		
Purchases of property, plant and equipment	(118,545)	(70,575)
Proceeds from sale of equipment	1,325	6,745
Principal payments on debt	(85,000)	(95,000)
Interest payments on debt	(72,275)	(75,483)
Federal, state and local grants	8,553	14,544
Net Cash Used by Capital and Related Financing Activities	<u>(265,942)</u>	<u>(219,769)</u>
 Cash Flows From Investing Activities		
Interest on cash and investments	6,251	5,705
Net Cash Provided by Investing Activities	<u>6,251</u>	<u>5,705</u>
 Net Increase (Decrease) in Cash and Cash Equivalents	(34,533)	172,385
 Cash and Cash Equivalents at Beginning of Year	<u>1,032,232</u>	<u>859,847</u>
 Cash and Cash Equivalents at End of Year	<u>\$ 997,699</u>	<u>\$ 1,032,232</u>
 Reconciliation of Cash and Cash Equivalents at End of Year		
Cash and Cash Equivalents	\$ 946,856	\$ 993,175
Restricted Cash and Cash Equivalents	50,843	39,057
Total Cash and Cash Equivalents at End of Year	<u>\$ 997,699</u>	<u>\$ 1,032,232</u>

Knox County Utility Commission
 Departmental Statements of Cash Flows - Water Department (Continued)
 For the Years Ended December 31, 2018 and 2017

	<u>2018</u>	<u>2017</u>
Reconciliation of Operating Income (Loss) to Net Cash		
Provided by Operating Activities:		
Operating income (loss)	\$ (136,552)	\$ 105,645
Adjustments to reconcile operating income (loss)		
to net cash provided by operating activities		
Depreciation	216,760	215,603
Amortization	3,064	3,064
(Increase) Decrease in:		
Accounts receivable	(11,230)	10,748
Unbilled accounts receivable	19,490	(26,919)
Inventory	206	1,795
Other current assets	(727)	(3,911)
Deferred pension & OPEB costs	10,762	(75,216)
Increase (Decrease) in:		
Accounts payable	7,922	(2,832)
Customer deposits	11,446	2,456
Accrued expenses	10,650	4,054
Other current liabilities	476	380
Net Pension & OPEB liabilities	92,891	151,582
	<u>92,891</u>	<u>151,582</u>
Net Cash Provided by Operating Activities	<u>\$ 225,158</u>	<u>\$ 386,449</u>

Knox County Utility Commission
 Departmental Statements of Net Position - Sewer Department
 December 31, 2018 and 2017

	<u>2018</u>	<u>2017</u>
Assets		
Current Assets		
Cash and cash equivalents	\$ (6,416)	\$ (3,242)
Receivables, less allowance	1,311	557
Total Current Assets	<u>(5,105)</u>	<u>(2,685)</u>
Noncurrent Assets		
Capital Assets		
Pumping equipment	20,594	20,594
Meters and meter installation	95	95
Transmission and distribution plant	529,850	529,850
Vehicles and other equipment	714	714
Lift stations	344,195	344,195
Less: accumulated depreciation	<u>(286,210)</u>	<u>(269,011)</u>
Net Capital Assets	<u>609,238</u>	<u>626,437</u>
Total Noncurrent Assets	<u>609,238</u>	<u>626,437</u>
Total Assets	<u>604,133</u>	<u>623,752</u>
Liabilities and Net Position		
Liabilities		
Accounts payable	<u>1,673</u>	<u>2,930</u>
Total Liabilities	<u>1,673</u>	<u>2,930</u>
Net Position		
Net investment in capital assets	609,238	626,437
Unrestricted	<u>(6,778)</u>	<u>(5,615)</u>
Total Net Position	<u>\$ 602,460</u>	<u>\$ 620,822</u>

Knox County Utility Commission
 Departmental Statements of Revenues, Expenses and Changes in Net Position - Sewer Department
 For the Years Ended December 31, 2018 and 2017

	<u>2018</u>	<u>2017</u>
Operating Revenues		
Sewer sales	\$ 26,622	\$ 25,653
Penalties	131	129
Total Operating Revenues	<u>26,753</u>	<u>25,782</u>
Operating Expenses		
Salaries and wages	1,178	1,191
Employee benefits	90	91
Utilities	1,410	1,367
Repairs and maintenance	-	2,462
Sewer treatment	25,150	24,876
Depreciation	17,199	17,199
Bad debt expense, net of recoveries	<u>88</u>	<u>59</u>
Total Operating Expenses	<u>45,115</u>	<u>47,245</u>
Operating Income (Loss)	<u>(18,362)</u>	<u>(21,463)</u>
Change in Net Position	(18,362)	(21,463)
Net Position, Beginning of Year	<u>620,822</u>	<u>642,285</u>
Net Position, End of Year	<u>\$ 602,460</u>	<u>\$ 620,822</u>

Knox County Utility Commission
 Departmental Statements of Cash Flows - Sewer Department
 For the Years Ended December 31, 2018 and 2017

	<u>2018</u>	<u>2017</u>
Cash Flows From Operating Activities		
Receipts from customers	\$ 25,999	\$ 25,482
Payments to employees	(1,178)	(1,191)
Payments to suppliers	(27,995)	(28,253)
Net Cash Provided (Used) by Operating Activities	<u>(3,174)</u>	<u>(3,962)</u>
 Cash Flows From Capital and Related Financing Activities		
Purchases of property, plant and equipment	-	(1)
Net Cash Used by Capital and Related Financing Activities	<u>-</u>	<u>(1)</u>
 Net Decrease in Cash and Cash Equivalents	(3,174)	(3,963)
 Cash and Cash Equivalents at Beginning of Year	<u>(3,242)</u>	<u>721</u>
 Cash and Cash Equivalents at End of Year	<u>\$ (6,416)</u>	<u>\$ (3,242)</u>
 Reconciliation of Operating Loss to Net Cash Provided (Used) by Operating Activities:		
Operating loss	\$ (18,362)	\$ (21,463)
Adjustments to reconcile operating loss to net cash provided (used) by operating activities		
Depreciation	17,199	17,199
(Increase) Decrease in:		
Accounts receivable	(754)	(300)
Increase (Decrease) in:		
Accounts payable	(1,257)	602
Net Cash Provided (Used) by Operating Activities	<u>\$ (3,174)</u>	<u>\$ (3,962)</u>

Knox County Utility Commission
Schedule of the Commission's Proportionate Share of the Net Pension Liability
County Employees Retirement System (CERS) Pension Plan
Last Ten Fiscal Years*

	<u>2018</u>	<u>2017</u>	<u>2016</u>	<u>2015</u>	<u>2014</u>
Commission's proportion of the net pension liability (asset)	0.01289%	0.01171%	0.01084%	0.01195%	0.01154%
Commission's proportionate share of the net pension liability (asset)	\$ 784,979	\$ 685,481	\$ 533,899	\$ 513,737	\$ 374,454
Commission's covered-employee payroll	\$ 335,581	\$ 301,660	\$ 254,414	\$ 280,292	\$ 270,908
Commission's proportionate share of the net pension liability (asset) as a percentage of its covered-employee payroll	233.92%	227.24%	209.85%	183.29%	138.22%
Plan fiduciary net position as a percentage of the total pension liability	53.54%	53.32%	55.50%	59.97%	66.80%

Source: Kentucky Retirement Systems

Notes: There were no changes in benefit terms, size or composition of the population covered by the benefit terms since the prior year. See the notes to the financial statements for a description of changes in actuarial assumptions from the prior year.

This schedule is presented to illustrate the requirement to show information for ten years. However, until a full ten year trend is compiled, the Commission will present information for those years for which information is available.

* The amounts presented for each year were determined (measured) as of the fiscal year-end that occurred within the calendar year.

Knox County Utility Commission
Schedule of the Commission's Proportionate Share of the Net OPEB Liability
County Employees Retirement System (CERS) OPEB Plan
Last Ten Fiscal Years*

	<u>2018</u>	<u>2017</u>
Commission's proportion of the net OPEB liability (asset)	0.01289%	0.01171%
Commission's proportionate share of the total OPEB liability (asset)	\$ 539,956	\$ 494,541
Commission's proportionate share of the plan fiduciary net position	<u>(311,132)</u>	<u>(259,110)</u>
Commission's proportionate share of the net OPEB liability (asset)	\$ 228,824	\$ 235,431
Commission's covered-employee payroll	\$ 335,581	\$ 301,660
Commission's proportionate share of the net OPEB liability (asset) as a percentage of its covered-employee payroll	68.19%	78.05%
Plan fiduciary net position as a percentage of the total OPEB liability	57.62%	52.39%

Source: Kentucky Retirement Systems

Notes: There were no changes in benefit terms, size or composition of the population covered by the benefit terms since the prior year. See the notes to the financial statements for a description of changes in actuarial assumptions from the prior year.

This schedule is presented to illustrate the requirement to show information for ten years. However, until a full ten year trend is compiled, the Commission will present information for those years for which information is available.

* The amounts presented for each year were determined (measured) as of the fiscal year-end that occurred within the calendar year.

Knox County Utility Commission
Schedule of the Commission's Pension Contributions
County Employees Retirement System (CERS) Pension Plan
Last Ten Fiscal Years*

	<u>2018</u>	<u>2017</u>	<u>2016</u>	<u>2015</u>	<u>2014</u>
Contractually required contribution	\$ 51,487	\$ 42,878	\$ 33,645	\$ 35,282	\$ 35,871
Contributions in relation to the contractually required contribution	<u>(51,487)</u>	<u>(42,878)</u>	<u>(33,645)</u>	<u>(35,282)</u>	<u>(35,871)</u>
Contribution deficiency (excess)	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>
Commission's covered-employee payroll	\$ 335,581	\$ 301,660	\$ 254,414	\$ 280,292	\$ 270,908
Contributions as a percentage of covered-employee payroll	15.34%	14.21%	13.22%	12.59%	13.24%

Source: Kentucky Retirement Systems

Notes: There were no changes in benefit terms, size or composition of the population covered by the benefit terms since the prior year. See the notes to the financial statements for a description of changes in actuarial assumptions from the prior year.

Contractually required employer contributions exclude the portion of contributions paid to CERS but allocated to the insurance fund of the CERS. The above contributions include those contributions allocated directly to the CERS pension fund.

This schedule is presented to illustrate the requirement to show information for ten years. However, until a full ten year trend is compiled, the Commission will present information for those years for which information is available.

* The amounts presented for each year were determined (measured) as of the fiscal year-end that occurred within the calendar year.

Knox County Utility Commission
Schedule of the Commission's OPEB Contributions
County Employees Retirement System (CERS) OPEB Plan
Last Ten Fiscal Years*

	<u>2018</u>	<u>2017</u>
Contractually required contribution	\$ 16,704	\$ 14,223
Contributions in relation to the contractually required contribution	<u>(16,704)</u>	<u>(14,223)</u>
Contribution deficiency (excess)	<u>\$ -</u>	<u>\$ -</u>
Commission's covered-employee payroll	\$ 335,581	\$ 301,660
Contributions as a percentage of covered-employee payroll	4.98%	4.71%

Source: Kentucky Retirement Systems

Notes: There were no changes in benefit terms, size or composition of the population covered by the benefit terms since the prior year. See the notes to the financial statements for a description of changes in actuarial assumptions from the prior year.

Contractually required employer contributions exclude the portion of contributions paid to CERS but allocated to the pension fund of the CERS. The above contributions include those contributions allocated directly to the CERS insurance fund.

This schedule is presented to illustrate the requirement to show information for ten years. However, until a full ten year trend is compiled, the Commission will present information for those years for which information is available.

* The amounts presented for each year were determined (measured) as of the fiscal year-end that occurred within the calendar year.



Independent Auditors' Report on Internal Control Over
Financial Reporting and on Compliance and Other Matters
Based on an Audit of Financial Statements Performed in
Accordance With *Government Auditing Standards*

To the Commissioners
Knox County Utility Commission
Artemus, Kentucky

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

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered Knox County Utility Commission'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 the Commission's internal control. Accordingly, we do not express an opinion on the effectiveness of the Commission's internal control.

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

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and, therefore, material weaknesses or significant deficiencies may exist that were not identified. However, as described in the accompanying schedule of findings and responses, we identified certain deficiencies in internal control that we consider to be material weaknesses (See 2018-1 and 2018-2).

Compliance and Other Matters

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

Knox County Utility Commission's Response to Findings

Knox County Utility Commission's response to the findings identified in our audit is described in the accompanying schedule of findings and responses. Knox County Utility Commission's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

Purpose of this Report

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

Christian Sturgeon, PLLC

Christian Sturgeon, PLLC
London, Kentucky

June 28, 2019

Knox County Utility Commission
Schedule of Findings and Responses
December 31, 2018

2018-1

Criteria:

As discussed in *Standards for Internal Control in the Federal Government* published by the General Accounting Office of the United States, internal control is an integral component of an organization's management that provides reasonable assurance that an objective of reliable financial reporting is being achieved. Organizations should implement procedures to ensure this objective is achieved.

Condition:

During the audit procedures performed, instances of this objective not being completely achieved were noted.

Cause:

The Commission's limited internal resources prevents the preparation of financial statements and related note disclosures in accordance with generally accepted accounting principles.

Effect:

The Commission was unable to prepare their financial statements and related note disclosures in accordance with generally accepted accounting principles.

Views of responsible officials and planned corrective actions:

The Commission feels that it would not be cost beneficial to hire the personnel required to complete these tasks.

2018-2

Criteria:

As discussed in *Standards for Internal Control in the Federal Government* published by the General Accounting Office of the United States, internal control is an integral component of an organization's management that provides reasonable assurance that an objective of reliable financial reporting is being achieved. Organizations should implement procedures to ensure this objective is achieved.

Condition:

During the audit procedures performed, instances of this objective not being completely achieved were noted.

Cause:

The size of the Commission's office staff does not allow proper segregation of duties with regard to cash collections, billing, accounts receivable bookkeeping, and payroll processing.

Effect:

This condition creates a weakness in internal controls which could result in unauthorized transactions being processed.

Views of responsible officials and planned corrective actions:

The Commission feels that it would not be cost beneficial to hire the personnel required to complete these tasks.