

**WINCHESTER MUNICIPAL UTILITIES
WINCHESTER, KENTUCKY**

**AUDITED FINANCIAL STATEMENTS
And Required Supplementary Information**

YEARS ENDED JUNE 30, 2018 and 2017

**WINCHESTER MUNICIPAL UTILITIES
WINCHESTER, KENTUCKY
JUNE 30, 2018 and 2017**

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SUMMERS, MCCRARY & SPARKS, P.S.C.

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INDEPENDENT AUDITOR'S REPORT

To the Board of Commissioners
Winchester Municipal Utilities
Winchester, KY

We have audited the accompanying financial statements of the business-type activities of Winchester Municipal Utilities, component unit of the City of Winchester, Kentucky, as of and for the years ended June 30, 2018 and 2017, and the related notes to the financial statements, which collectively comprise the Utilities' 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 opinions on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend 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 opinions.

Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the business-type activities of Winchester Municipal Utilities, component unit of the City of Winchester, Kentucky, as of June 30, 2018 and 2017, and the respective changes in financial position and, where applicable, cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis, the Schedule of Proportionate Share of the Net Pension Liability and the Schedule of Contributions on pages 4–25 and 58-63 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 opinions on the financial statements that collectively comprise Winchester Municipal Utilities', component unit of the City of Winchester, Kentucky, basic financial statements. Schedule I – Department Expenses and Schedule II – Revenue Bond Debt Services are presented for purposes of additional analysis and are not a required part of the basic financial statements.

Schedule I – Department Expenses and Schedule II – Revenue Bond Debt 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, Schedule I – Department Expenses and Schedule II – Revenue Bond Debt are 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 November 9, 2018, on our consideration of Winchester Municipal Utilities', component unit of the City of Winchester, Kentucky, 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 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 Winchester Municipal Utilities', component unit of the City of Winchester, Kentucky, internal control over financial reporting and compliance.

Summers, McCrary & Sparks, PSC

Winchester, Kentucky
November 9, 2018

**MANAGEMENT'S DISCUSSION AND ANALYSIS
WINCHESTER MUNICIPAL UTILITIES
JUNE 30, 2018**

UTILITY PROFILE

Winchester Municipal Utilities (WMU), an enterprise fund of the City of Winchester, Kentucky (City), was established in 1958 by ordinance of the City to provide water, sanitary sewer (wastewater) and solid waste services for the City and portions of Clark County. WMU is governed by a Board of Commissioners appointed by the Mayor with approval of the Board of Commissioners of the City. The Winchester Municipal Utilities Commission (WMUC) provides direction and oversight of the Utility and its operations, adopts the budget, sets the operating policies, hires the General Manager and Counsel of the Utility, and recommends to the City utility rates necessary to support the operations of the Utility, repair and replacement of the Utility's assets and payment of the Utility's debt service.

WMU has 11,843 water customers, 11,586 wastewater customers and 8,627 solid waste customers.

Fiscal Year 2018/2019 budget reflects annual revenue of \$16,373,400 and annual debt service of \$5,743,691.

• **Water System**

WMU currently has two sources of raw water – Pool No. 10 of the Kentucky River and the Carroll Ecton Reservoir (Reservoir). WMU's primary source of water is Pool No. 10, a 25-mile pool of the river. WMU is the only water utility withdrawing water from this source. WMU is permitted to withdraw up to 15 million gallons per day (MGD) from Pool No. 10 under normal river flow conditions, with restrictions being imposed during times of below normal river flow. The Reservoir impounds approximately 500,000,000 gallons of water on an unnamed tributary of Lower Howards Creek. WMU is permitted to withdraw up to 5.3 MGD from the Reservoir.

The water treatment plant under special provision is rated to produce 6.0 million gallons per day (MGD). Clearwell storage is 1,000,000 gallons; elevated storage totals 3,500,000 gallons. WMU maintains approximately 181.52 miles of water line in the distribution system.

Average day water production for FY 2017/2018 was 4.42 MGD. Peak day water production for FY 2017/2018 was 5.49 MGD in January of 2018. In addition to the provision of service to its retail customers, WMU provides water for resale to the East Clark County Water District (ECCWD) and the Kentucky American Water Company (KAWC).

Wastewater System

WMU maintains approximately 157.50 miles of gravity and force main sanitary sewers, ten (10) sewage-pumping stations (excluding the landfill pump stations) and two (2) wastewater treatment plants (WWTP). The Strodes Creek WWTP is rated at 7.2 MGD and the Lower Howards Creek WWTP is rated at 2.0 MGD. The Strodes Creek WWTP is designed to handle a biological load approximately four times greater than typical domestic sewage. The Lower Howards Creek WWTP is designed to handle typical domestic sewage. In addition, WMU operates solids processing facilities at both locations with the Strodes Creek WWTP currently having the capability to produce and distribute for beneficial reuse Class A biosolids in compliance with 40 Code of Federal Regulations (CFR) §503.

Average day wastewater treatment for FY 2017/2018 at Strodes Creek was 4.54 MGD with a peak day wastewater treatment for FY 2017/2018 at 13.65 MGD. Average day wastewater treatment for FY 2017/2018 at Lower Howards Creek was 1.10 MGD with a peak day wastewater treatment for FY 2017/2018 at 4.98 MGD. For FY 2017/2018 0.0 tons of Class A biosolids were produced at the Strodes Creek WWTP. Due to equipment maintenance and other factors Class B biosolids were produced at Strodes Creek for FY 2017/2018, totaling 2,003.0 tons. Total Class B biosolids produced at Lower Howards Creek was 78.1 dry tons.

- **Solid Waste System**

WMU is responsible for the daily collection of solid waste and recycling material (residential) generated within the City and transportation for ultimate disposal in a privately owned and permitted solid waste landfill and/or material recovery facility. In addition, WMU collects and grinds yard waste for beneficial reuse, operates and maintains a voluntary recycling operation for newspaper, white and mixed paper, cardboard, glass, plastics, tin, and aluminum, and maintains a 20-acre, non-operating landfill that is classified as *in post-closure care*.

Average day solid waste collection and disposal for FY 2017/2018 was 58.00 tons and average monthly yard waste collection for FY 2017/2018 was 115.08 tons. Average monthly recycling collection for FY 2017/2018 was 85.96 tons.

SIGNIFICANT ISSUES

- **Water Supply, Treatment and Distribution**

Addressing the water supply, treatment and distribution needs of the community continues to be at the forefront of priorities for the Utility. Historical growth pattern projections and water usage data indicate the need for additional potable water capacity. As would be expected the timeframe of those needs are directly

impacted based upon the needs of the industrial community. While the Utility lost a significant industrial customer (Alltech) during the 2017/2018 timeframe a new industry has announced plans to re-occupy the same facility with similar water requirements. In addition, plans to increase water demands at several local industries remain very much a reality, however overall industrial water usages seem to be trending downward. As general industry continues to look at cost saving measures for their operations normally water saving processes are at the forefront of evaluation. Determination of the water requirements for the remaining lots in the Industrial Park, Phase VI will factor into defining the ultimate water needs of the Utility.

As previously stated WMU's current permitted capacity is 6.0 million gallons per day (MGD) with current average day demand of 4.42 MGD and peak day demand of 5.49 MGD. WMU's average day production is down approximately 200,000 GPD from the previous fiscal year due to the loss of the industry noted above. Projections of WMU's 20-year demand as outlined in previous studies are 12.0 MGD based upon normal growth patterns which can be skewed with the addition or loss of any significant industry or other large user. Normal and peak day average water production is expected to trend upward as industry comes online and development activities continue to increase. Careful consideration has been given to all these factors when sizing the new water treatment plant (WTP) facilities and associated infrastructure.

Discussions in 2008 between the WMU and City Commissions led to a decision to construct a new WTP. Construction was proposed to be phased with the initial capacity being 6.0 MGD to operate in concert with the existing WTP yielding an effective capacity of 8.0 – 9.0 MGD. It was determined during preliminary design that operation of a single WTP at 9.0 MGD would be the most cost effective and logical choice. The final effective capacity of the new WTP will be determined by the Division of Water (DOW). Several significant questions were answered during preliminary design which included decommissioning of the existing WTP upon completion of the new WTP facilities and continued use of the Carroll Ecton Reservoir for a back-up raw water supply. With completion of the final design of a new WTP and advertisement for bids in the Fourth Quarter of 2017, construction was initiated during the First Quarter of 2018. Judy Construction Company was awarded the construction contract in the amount of \$19,982,300.00. As of June 30, 2018 construction of the new water treatment plant facilities were 10% complete with construction being initiated on March 5, 2018.

The total estimated cost (preliminary engineering costs) of the initial phase of water system improvements ranged from \$24 - \$28 million dollars based on the best available information at the time. The revised estimate based upon as-bid and finished construction information is \$31,586,377.80. Construction of the new water treatment plant is expected during March/April 2020. Preliminary grade work and siting of the new WTP facilities was constructed as part of the Lower

Howards Creek Wastewater Treatment Plant project at a cost of \$2,189,500. In addition, raw water pump upgrades and raw and finished water transmission improvements were completed during calendar year 2016 which will insure the delivery of the additional capacity.

The finished water main improvements began at WMU's Kentucky River Pump Station (1001 Ford Road) extended to the future site of the proposed WTP located at 7055 Boonesboro Road, interconnected with the existing WTP facilities at 365 Water Works Road and ended with connection to the existing 12-inch water main near 550 Bypass Road. The total cost of improvements was \$8,244,329.12.

The Kentucky River Pump Station improvements included the addition of one (1) raw water vertical turbine pump, pump control valves, HVAC upgrades, electrical upgrades and other associated piping and valve improvements. Construction of the improvements was completed and accepted by the Commission in January 2017 at a cost of \$1,170,248.66.

Construction of the aforementioned water improvements and proposed improvements necessitated rate adjustments to facilitate construction. In March of 2010 it was necessary for WMU and the City of Winchester to enact phased rate increases to provide the revenue and funds to construct the capital improvements to meet the water needs of the community currently and in the future. These adjustments have equated to a total adjustment of \$15.97/month (77.1%) for city customers and \$12.89/month (47.5%) for county customers for the average 6,000 gallon/month user on the monthly utility bill for water.

- **Consent Decree**

Compliance with requirements of the Consent Decree remains a top priority for the Utility. Much progress has been made since April of 2007 to comply with the requirements of this enforcement action. The Consent Decree is the settlement agreement between the United States Environmental Agency (EPA), the Kentucky Energy and Environment Cabinet (EEC, formerly known as the Environmental and Public Protection Cabinet), the City and WMU detailing actions to be taken by the City and WMU for violations of the Clean Water Act , 33 U.S.C. § 1319. The basic tenants of the Consent Decree call for the City and WMU to:

- Eliminate existing and recurring sanitary sewer overflows (SSOs)
- Reduce the potential for future SSOs

Such has been achieved through a defined capital program and structured operation and maintenance (O&M) programs.

Deadlines outlined in the Consent Decree for completion of capital projects to eliminate SSO's are shown in the chart below:

Project	Project Area	Proposed Completion Date	Project Cost
Lower Howards Creek Sanitary Sewer Improvements	Snowfall Stoneybrook	January 31, 2013 (Complete)	\$32,765,179.90
Bel-Air Sanitary Sewer Improvements	Bel-Air Westside	July 31, 2013 (Complete)	\$559,867.96
Hampton Manor Sanitary Sewer Improvements	(Bonnie Brook and Mockingbird Valley)	July 31, 2019 (Complete)	\$1,288,128.00
Flanagan and Madison Street Sanitary Sewer Improvements	Madison, Flanagan, & East Washington Street	January 20, 2021 (Design)	\$5,289,000.00. (Estimate)
Other locations identified in Exhibit A of the Consent Decree	WMU Collection System	January 20, 2024 (Design)	Undetermined

The Lower Howards Creek Project involved a facilities plan update, construction of sanitary sewer interceptors, force main and construction of a new wastewater treatment plant. The Lower Howards Creek Project is complete and received final acceptance January 2, 2014. The Bel-Air Sanitary Sewer Improvements project involved construction of an interstate road bore and new interceptor sewer that eliminated two (2) sewage pumping stations. Construction of Bel-Air is complete and was formally accepted on June 20, 2013. The Hampton Manor Sanitary Sewer Improvements project was proposed to eliminate two (2) recurring SSOs in the Bonnie Brook and Mockingbird Valley area (MH's 14-76A and 14-51). Construction of the Hampton Manor project is complete and was formally accepted on April 19, 2018. Construction of the Madison, Flanagan, and East Washington Street project includes the rehabilitation of the East Interceptor Sewer coupled with construction of larger diameter sewers in the downtown area of Winchester to replace aging infrastructure. This project along with all other locations identified in Exhibit A of the Consent Decree are being designed based upon flow monitoring data and updates to the Sewer Hydraulic Model as required. Completion of an SSO Elimination Study in January 2018 provided an outline of WMU's overall plan moving forward for elimination of SSOs No. 15, 16, 17, 19, 25, and 26 as delineated in WMU's Consent Decree. The purpose of the Study was to provide a global perspective for future design of projects

intended to eliminate SSOs at these specific locations. WMU's approved Sanitary Sewer Overflow Plan (SSOP) calls for elimination of the above-mentioned SSO locations in the 2021 – 2025 timeframe. With completion of the Study, WMU has initiated design of the Flanagan and Madison Street Sanitary Sewer Improvements project. Design of this project is expected to be completed during the First Quarter of 2019. Staff has inquired of EPA officials regarding extension of the remaining deadlines in the Consent Decree. Feedback has been positive, while staff awaits further direction from EPA/KDOW officials on proper protocol for requesting such extension.

Structured O&M programs have been developed, submitted, and reviewed/approved by the EPA. These programs are known as the Capacity, Management, Operation and Maintenance (CMOM) programs. WMU developed fourteen (14) required CMOM programs, seven (7) of which were submitted, reviewed and approved by EPA. A list of the CMOM Programs developed and submitted to EPA are as follows:

- Sewer Overflow Response Plan (SORP)
- Inter Jurisdictional Agreement Program
- Public Education Program
- Spill Impact Water Quality Monitoring Program
- Corrosion Control Program
- Routine Hydraulic Cleaning Program
- Root Control Program
- Capacity Assurance Program (CAP)
- Acquisition Consideration Program
- Infrastructure Rehabilitation Program (IRP)
- Sewer System Assessment Program (CSSAP)
- Sewer System Inventory Program
- Fats, Oils, and Grease Control Program (FOG)
- Financial and Cost Analysis Program

Additional requirements of the Consent Decree included a Supplemental Environmental Project (SEP). As a result, it was determined to be environmentally beneficial to the public to implement a SEP which would commission a study of the streams in the Lower Howards Creek Watershed (LHCW) and develop a Lower Howards Creek Watershed Management Plan (LHCWMP). The SEP Completion Report was submitted to the EPA and KDOW on November 20, 2012. On January 8, 2013 WMU received written confirmation that the SEP Completion Report in accordance with General Provision 4 of Exhibit D of the Consent Decree was approved by the EPA.

As would be expected the requirements of the Consent Decree have had a substantial fiscal effect on WMU ratepayers. In March of 2010 it was necessary for WMU and the City of Winchester to enact phased rate increases to provide the revenue and funds necessary to comply with the requirements of the Consent

Decree that included capital construction projects and CMOM activities. The phased rate increases adjusted utility bills approximately 20% per year from 2010–2013. In 2014 and 2015 rates were adjusted approximately 5% annually and adjusted thereafter based upon the CPI index. With the rate increases as enacted the monthly sewer bill for the average user (6,000 gallons) has increased from \$28.88/month in 2010 to \$67.12/month in 2015. This equated to a total adjustment of \$38.24/month for the average customer or an overall increase of 132% for the average customer on the monthly utility bill for sewer service.

Since entry of the Consent Decree in April 2007 WMU has spent \$72,461,230.67 on Consent Decree capital projects. These expenditures amount to approximately \$6,254.21 for each of WMU's 11,586 customers. Similarly during this same timeframe, WMU has spent \$3,111,174.49 on CMOM, flow monitoring and I/I reduction programs. These expenditures amount to approximately \$268.52 for each of WMU's 11,586 customers. The economy continues to move in a positive direction, however growth still remains at minimal levels. This being the case, opportunities are limited to bring down the individual costs to each customer.

- **Kentucky River Lock and Dam No. 10**

Construction of the Kentucky River Lock and Dam No. 10 were completed in 1905. The lock and dam were owned and operated by the United States Army Corps of Engineers (COE) until 1996 at which time ownership and the responsibility for maintenance and replacement of the lock and dam were transferred to the Commonwealth of Kentucky. The General Assembly created by statute the Kentucky River Authority (KRA) to oversee the operation, maintenance and replacement of the 14 locks and dams on the Kentucky River. Implicit in that charge of authority is the maintenance of the 14 pools of water for water supply. The Kentucky River supplies water to approximately 22% of Kentucky's population. WMU, like all other water utilities that withdraw water from the Kentucky River, pays a withdrawal fee for each gallon of water withdrawn from the Kentucky River and the Carroll Ecton Reservoir and passes that cost to its customers. The withdrawal fees are used by KRA for repair and replacement of the 14 locks and dams. The withdrawal fees were recently increased (July 2018) to help facilitate the repair and replacement of the aging infrastructure along the River. More specifically, the fees were increased to support the rehabilitation activities associated with Dam No. 10.

Dam No. 10 was built as a timber crib dam with a plain concrete face, i.e., the dam is a series of timber boxes, stacked and filled with large rock and covered with a concrete skin that has no reinforcement. The dam is well over 100 years old and has received no substantial rehabilitation during its service life. The dam impounds Pool No. 10 which creates the water supply for Winchester and most of Clark County.

Pool No. 10 is the longest pool on the Kentucky River stretching nearly 25 miles along the 260 miles of the Kentucky River. The East Kentucky Power (EKP) Dale Generating Plant did withdraw cooling water for the power generating plant from this pool. EKP has since decommissioned the facility located at this location and has finalized removal of coal ash from the sedimentation ponds. With this decommissioning the WMU withdrawal is the only permitted withdrawal from Pool No. 10. Upstream from WMU's water intake in Pool No. 10 is one of the City of Richmond Utilities Wastewater Treatment Plants (WWTP) permitted discharges, Otter Creek in Madison County. The permitted WWTP discharge meets the Kentucky, five-mile separation rule between a WWTP discharge and a WTP intake.

The Kentucky River is subject to wide variations in flow from 0 flow to 1 billion gallons per day. The wide variations in flow and resulting stress on the dam and scour below the dam make Dam No. 10 vulnerable to overturning. As such, KRA has designed improvements and is currently in the construction phase to make the necessary improvements. Construction is expected to last approximately 3-4 years depending upon weather conditions and flows in the river. The engineer of record for the project is Stantec (Lexington) with C.J. Mahan Construction Company (Ohio) providing construction services.

As previously mentioned withdrawal fees were increased in July 2018 in order to finance the proposed improvements. The Kentucky Department of Finance approved the KRA Board's recommendation to adjust the rate structure for Tier II user fees from \$0.13 to \$0.22 per thousand gallons withdrawn. Construction of the improvements is an approximate \$24.5M investment for the citizens of Winchester/Clark County. Inaction on the part of KRA would potentially result in a failed dam leaving Winchester without its primary water supply. KRA has indicated their emergency action plan to repair a failed dam would place the burden on the water withdrawer for a minimum of 7-14 days until equipment could be mobilized. WMU's Carroll Ecton Reservoir would yield, without mandatory conservation measures, approximately a 30-45 day supply of water under normal weather patterns.

The Kentucky River is a non-protected watershed. It is subject to contamination from straight pipes (unauthorized sewer discharges), agricultural runoff (chemical contamination), chemical spills, and drought. Yet approximately one quarter of the state's population relies upon the river for water supply.

- **Carroll Ecton Reservoir**

The Carroll Ecton Reservoir (CER) currently serves as a secondary source of water supply for the City of Winchester and Clark County. As previously mentioned the CER impounds approximately 500,000,000 gallons of water on an unnamed tributary in Lower Howards Creek. Excess raw water flow from the

Kentucky River can be pumped to the CER during normal operation. Over the years significant leakage has developed out of the hillside (rock face) just below the dam and an unknown amount of silt has accumulated within the body of water both of which effect storage volumes. The WMU Commission has determined that the CER should remain a secondary raw water source and has authorized design and construction of improvements in conjunction with the new WTP facilities provided that funds are available to do so. This will ensure a reliable secondary raw water source for the community in the event problems are experienced along the Kentucky River.

- **Solid Waste Enhancements**

The WMU Commission authorized a comprehensive solid waste study of the solid waste operations for WMU on May 31, 2012. The scope of services was comprised of four (4) phases of work that included 1) Compilation and review of existing information, 2) Cost and rate analysis, 3) Review of alternatives (optional), and 4) Reporting. The final report delivered in March of 2013 provided a comprehensive review of the operational and financial performance of WMU's solid waste services, including collection, recycling, and operation of the transfer station. The final report also included state and national benchmarking of municipal and solid waste management systems to gauge the "state of the industry" and to identify best practices for consideration by WMU. Key findings from the study included elimination of the mandatory commercial customer charge, establishment of a multi-family customer class, validation and implementation of several operational alternatives including integration of elderly/disabled collection into regular refuse routes; conversion of the second weekly refuse collection service to curbside recycling collection; consideration of a Pay As You Throw (PAYT) structure; and establishment of commercial collection for corrugated cardboard recycling. The final report developed rate structures for "full cost" and "revenue sufficiency".

Since completion of the final report WMU has implemented several of the recommendations and findings or variations thereof that include Residential Single Stream Curbside Recycling, Phases I (March 7, 2014) and II (October 2, 2014) and established a multi-family customer class with container rates.

The WMU Commission authorized an additional solid waste study of the solid waste operations in December of 2015 to evaluate 1) Conversion to weight-based tipping fees, 2) Commercial sector recycling, and 3) Commercial haulers use of the WMU Transfer Station. A final report was delivered in May of 2016 which provided recommendations to convert to a weight-based tip fee versus volumetric tipping fees for refuse disposal. The report also acknowledged that WMU should seek feedback from the commercial sector customers prior to making any decisions related to commercial curbside customer recycling and WMU should investigate the opportunities to expand the throughput of the WMU Transfer Station to help offset the cost per ton for refuse disposal.

Installation of Transfer Station truck scales in September 2015 via Kentucky Pride Grant Funds provided the opportunity for conversion to weight-based tipping fees. Consequently, revisions to Sections 14-81-7 and 14-81-8 of the Winchester Code of Ordinances No. 8-2016 received final approval by the Winchester City Commission in August of 2016. The revisions included conversions to weight-based tipping fees and clarification on WMU Transfer Station disposal fees. WMU continues to review recommendations from the 2013 and 2016 reports that can be implemented and enhance the overall operation of the Solid Waste Department.

A recent decline in recycling commodity pricing and increased processing costs at the Materials Recovery Facility (MRF) have required staff to review options related to the single stream curbside recycling services currently provided. Current information indicates that the cost to dispose of recycling is \$47.72/ton while disposal of solid waste is \$31.03/ton. This poses the question of cost effectiveness and the Utility's ability to maintain these types of enhanced services. One of the options being considered is streamlining of the existing collection routes as a cost saving measure. Any changes will require approval of both the WMU and City Commissions.

As mentioned in previous sections in March of 2010 it was necessary for WMU and the City of Winchester to enact phased rate increases to provide the revenue and funds to meet the solid waste needs of the community currently and in the future. These adjustments have equated to a total adjustment of \$16.72/month for customers on their monthly utility bill for solid waste.

- **Affordability**

Affordability of services is a major concern for the City Commission, the Utility Commission and to Management. The WMU service area population is approximately 27,000 – 30,000 of which 51% fall in the low to moderate income (LMI) level. While the economy continues to show signs of improvement and recovery, limited local development further impacts the affordability of WMU's services.

The primary costs in WMU's budget are capital costs including renewals and replacements. The cost of compliance with the Consent Decree and elimination of I/I (approximately \$75.6 (million to-date), cost for upgrading and expanding WMU's water system capacity and additional capital needs are expected to exceed \$100 million. Renewals and replacements exceed \$2,000,000 each year. The driving factors in WMU's operations and maintenance budget are power, fuel, chemical and personnel costs.

The City and WMU Commissions, in concert with Management, have continuously worked to reduce the financial burden of rate increases. Cost-effective decisions must be considered and made with respect to capital needs.

Management is focused on cost-effective operations while taking into consideration the high level of service demanded by WMU's customers. One of the cost effective measures included in the budgeting process for the five-year capital plan includes setting aside monies in the Depreciation budget to fund new water system improvements. Total accumulated funds are expected to be nearly \$3.2 million.

The City and WMU Commissions passed rate increases that became effective in February 2010. Rates have been adjusted annually with the last increase implemented in January 2015. These rate increases were necessary despite a depressed economy, high unemployment, and a declining stock market. Implementation of the rate increases allow WMU to upgrade and improve WMU's water system, comply with the Consent Decree, and contribute to replacement of WMU's aging water and wastewater infrastructure. This ensures a high level of service to existing customers and positions the community to be able to attract and retain residential, commercial and industrial development while balancing the affordability of providing a prescribed level of service.

Previously, the City and WMU Commissions passed an annual adjustment to the rate structure tied to the Consumer Price Index (CPI). This adjustment allows WMU to maintain its operating and maintenance budget current with the cost of living through annual adjustments to the rate versus the historical flat line approach with infrequent but significant adjustments. This approach was favored in a community survey by 73.5 % of the respondents. The WMU Commission recently approved a CPI increase of 2.1% that became effective in March 2018.

The City and WMU Commissions, in concert with the Fiscal Court, have adopted legislation (Privilege Fee) that will ensure that the costs of growth for WMU's sanitary sewer system are apportioned to all benefitted properties versus being solely supported by the existing customer base. The privilege fee approach is favored for its equity and for the benefit to the community by insuring that sanitary sewers are sized on a watershed basis versus the historical "first in, one size fits all approach". The Privilege Fee Ordinance and Policies have been approved by the respective legislative bodies and WMU's first Privilege Fee Agreement (PFA), located in the Strodes Creek, Basin B received final approval on September 21, 2014. Recent efforts by entities in the Hancock Creek watershed to move a second PFA project forward have stalled due to the potential costs of those involved. A project in this watershed would involve multiple PFA's.

The City and WMU Commissions have secured grants and sought the best possible financing for WMU's capital needs. The City and WMU received a \$36,600,000 low interest (2.2%; 20 years) loan for the Lower Howards Creek Wastewater System Improvements. The City and WMU received a \$750,000 Community Development Block Grant and \$750,000 Economic Development Grant to construct the Forest Park Sanitary Sewer Improvements project.

Management applied for but did not receive grant funds to construct the Bel-Air Sanitary Sewer Improvements project. Funding for the Bel-Air project was secured via a low interest loan from the Kentucky Infrastructure Authority (2.2%; 20 years). Financing of the Hampton Manor Sewer Improvements was via low interest funds from the Kentucky Infrastructure Authority. Financing of the Water System Improvements is a combination of accumulated funds that include Depreciation funds as previously mentioned, System Development Charge funds and the sale of revenue bonds in the range of 4-5% for 20 years. Expectations for funding of the Flanagan and Madison Street Sanitary Sewer Improvements will be a combination of accumulated funds as well as low interest KIA funds.

BUSINESS FACTORS

• Facilities Planning

WMU is required by federal and state regulation to maintain a Facilities Plan that outlines the long-term plan for growth of the sanitary sewer system and treatment works. A Facilities Plan Update was completed and approved by the Energy and Environmental Cabinet (EEC) for the upgrade of the Strodes Creek Wastewater Treatment Plant. The last Facilities Plan with respect to the collection system was completed in 1973. The plan should be updated on a minimum 20-year cycle. The WMU Commission authorized a Facilities Plan Update for the sanitary sewer collection system in August 2008. The Facilities Plan Update was necessary to determine the recommended end-of-pipe sewage management plan for the Lower Howards Creek Sanitary Sewer Improvements which was a requirement of the Consent Decree. The Facilities Plan Update was completed at a cost of \$189,000, approved by the Kentucky Division of Water on August 11, 2010 and identifies and addresses sanitary sewer collection recommendations for WMU's 14 sub-watersheds listed below:

- Strodes Creek Basins A, B, C, and D
- Lower Howards Creek Basins A, B, and C
- Hancock Creek Basins A, B, and C
- Hoods Creek
- Four Mile Creek Basins A, B, and C

Conversely, there is no such mandate for the drinking water system with respect to planning. However, in November 2009 Hazen & Sawyer prepared a Water System Planning Study outlining recommendations for significant improvements needed to meet current and future needs for the Utility. Recommendations included conceptual cost estimates for a new WTP, raw water pump station upgrades, raw water transmission main upgrades, finished water transmission upgrades and reservoir improvements. The conceptual cost summary totaled \$58,700,000 of improvements excluding any reservoir improvements.

Since that time, WMU retained Bell Engineering (September 2013) to provide a third party review of existing studies and alternatives relative to the water supply, treatment and transmission main infrastructure. Technical Memorandum No. 1 (TM 1) was completed and presented to the WMU Commission on March 6, 2014. TM 1 included evaluation and recommendations for raw water supply, raw water intake and pump station improvements, raw and finished water transmission main improvements, and an updated opinion of probable construction cost and schedule for the proposed new WTP. The conceptual cost summary from TM 1 which included improvements to maintain the Carroll Ecton Reservoir as a back-up water supply totaled \$42,370,000. The conceptual cost estimate was further developed and as previously mentioned the initial phase of improvements ranged from \$24 - \$28 million dollars based on the best available information. Current information provides for nearly \$32,000,000 to be expended on the water system improvements.

As mentioned in a previous section, construction contracts for raw water pump station upgrades and raw and finished water transmission improvements have been completed. Design of the new WTP has been completed and construction bids were received during the Fourth Quarter of 2017.

In response to initiatives identified in the Clark County Community (CCC) Action Plan, the Winchester Recycling Task Force (RTF) was established in 2009. In the same year, the RTF developed and coordinated a county-wide Recycling Survey mailed to approximately 12,000 customers of WMU, Rumpke, and S&G Sanitation within the December 2009 and January 2010 billing cycle. A total of 2,167 survey responses were received representing a response rate of 22 percent. Of the 2,167 respondents, 1,447 (67%) were WMU customers. Based on the survey results and research efforts of the RTF, the Winchester City Commission and WMU Commission implemented a Pilot Program for the Holiday Hills subdivision the week of August 1, 2011. Based upon positive results of the Pilot Program and recommendations from the Solid Waste Study it was proposed to implement Residential Single Stream Curbside Recycling for WMU customers in two phases. Phase I was implemented March 7, 2014 and Phase II October 2, 2014. Preliminary analysis of the recycling rates indicates that participation and volume are less than 15% of the total volume of material collected. This is below industry thresholds which indicate that 20-25% is an acceptable range for volume and participation. As previously mentioned WMU is considering streamlining of the existing collection routes as a cost saving measure in order to maintain existing recycling services. WMU continues to review recommendations as outlined in the various studies conducted for the solid waste activities.

- **Rate Studies**

The WMU Commission previously authorized rate studies of WMU's three utility functions. The rate studies proposed revenue sufficient rates to support WMU's operations, including the expanded operations as required by CMOM, the

operations of the Strodes Creek WWTP and the planned WTP, the capital needs as required by the Consent Decree and the planned water system improvements. Results of the rate study are reflective of the rates recommended, approved, and implemented February 2010. Staff maintains an in-house Financial Model and updates as necessary to ensure the financial stability of the Utility.

The WMU Commission authorized a wholesale cost of service study to support WMU's wholesale cost of service rate to its only wholesale customer, East Clark County Water District. The rate study has been completed and received Public Service Commission (PSC) approval on October 5, 2010 to increase the cost from \$1.62 to \$1.72 per hundred cubic feet of water sold. With completion of the large Water System Improvements projects the wholesale rate will be reviewed to determine the need for adjustment of this rate.

As part of the Solid Waste Study initiated in May 2012 a cost and rate analysis was conducted of WMU's current rates as well as expanded service rates. As previously mentioned a multi-family customer class was established with corresponding container rates as a result of the study. Implementation of any other recommendations will most likely result in impacts to future budgets.

Due to the significant amount of debt incurred for capital construction projects since the last rate study it would be beneficial for the Utility to review the rate structures for all three utility functions in the near future. Based upon the current capital construction schedule the optimal time would be upon completion of the new WTP and Hampton Manor Sanitary Sewer Improvements project. This would allow the rate study to precede construction costs associated with large sanitary sewer improvements required by the Consent Decree which are proposed for the 2021 and 2024 timeframe. In addition, the study would provide for an independent review of the rates in a 10 – 12 year timeframe.

- **Work Force**

Key issues that continue to face WMU with respect to workforce include retirements, loss of institutional and industry knowledge, finding and attracting qualified replacement employees, paying competitive wages based on industry standards, and training of employees to meet the increasingly sophisticated needs of water, wastewater, and solid waste utility operations including customer service, finance, information systems, administrative services and engineering.

WMU has 84 budgeted staff positions of which 72 are filled, 6 part-time employees and 2 co-op students from the youth program at George Rogers Clark High School. The average age for WMU employees is 40 years. The number of eligible retirements at WMU over the next five years, due to age, years of service, or both, is nine (9) or 12% of the workforce. Since 2002, there have been 50 retirements which equates to a loss of nearly 70% of the WMU workforce. Large scale retirement numbers often enable entities to renew and

refresh operations, systems, and business philosophies. Transition planning has been successful for most key positions, however, such changeover carries the burden of losing institutional and industry knowledge, and challenges Management to find, attract, train, and retain replacements particularly for supervisory positions. As WMU moves forward with construction of additional facilities for both water and wastewater, staffing of those facilities will be of utmost importance. In an effort to screen and find quality employees WMU has acquired the help of a local temporary staffing service agency.

WMU's attractiveness as an employer continues to be its benefits package. With the recent changes in the retirement system the benefit package will become less attractive and other avenues will need to be explored to attract quality employees. That being the case, the Commission has recognized the need to make positive adjustments in WMU's pay scale which has helped with retention of quality employees. These efforts have helped WMU provide salaries that are at least average or comparable to other municipalities. Training for utility operations is typically on-the-job. Certification in operations and driver's licensing (commercial) is a job requirement for all three utility functions. Support functions, customer service and vehicle maintenance, as well as engineering and finance, will require on-the-job training specific to WMU's business operations. Workforce development is critical in maintaining the quality of service delivered by WMU and for compliance with enforcement and regulatory activities. Management continues to look for opportunities to improve salaries for competent and skilled employees and recruitment from the local high school and technical college facilities.

- **Infrastructure Renewal**

A structured approach for infrastructure renewal spreads costs over the long-term and can increase the service life of assets. WMU continues to emphasize the importance and need for ample asset management and infrastructure renewal allocations. WMU's infrastructure renewal program includes a prioritization methodology to maximize capital investment, and annual allocations for defined asset categories. WMU annually allocates an average of \$2,000,000 of its capital investment for this effort. Program elements include:

- Main Replacement Program – Water
- Fire hydrant Replacement
- Gate Valve Box Adjustment – Pavement Overlay
- Elevated Storage Tank Rehabilitation
- Meter Change Out
- Main Replacement Program – Sewer
- Private Sewer Replacement
- Inflow and Inflow (I/I) Rehabilitation
- Curbit Replacement
- Container Replacement

- Vehicles
- Plant & Equipment Improvements

While WMU's program of infrastructure renewal is a model for other utilities and public works agencies in the central Kentucky area, the program is limited in its scope by funding, especially with large water system improvements and Consent Decree requirements planned for the immediate future. Infrastructure renewal funding should be based upon a mathematical model that addresses asset category inventory and asset category service life. WMU's program is based upon funds available. As an example and simply stated, for the waterline asset category, funding for waterline replacement should be based upon the cost for replacing the number of miles of waterline divided by the service life of the pipe. In this example, if WMU owns and maintains 181 miles of waterline with the waterlines having a service life of 60 years, the allocation for waterline replacement should be the average cost of replacing 3 miles of waterline per year. At \$60 per foot for replacement of a waterline this calculates to an annual allocation of \$950,400. WMU typically allocates \$200,000 or more but only allocated \$150,000 for FY 2018/2019. Likewise, if WMU owns and maintains 157 miles of sanitary sewer lines having a service life of 60 years, the allocation for sewer line replacement should be the average cost of replacing 2.61 miles of sewer line per year. At \$70 per foot for replacement of a sewer line, the annual allocation calculates to be \$964,656. WMU typically allocates \$200,000 or more but only allocated \$150,000 for FY 2018/2019. Without adequate funding for infrastructure renewal WMU is susceptible to interruption of service to its customers and a reduced level of service provided to its customers.

- **Regulations**

WMU and its utility functions are highly regulated. Regulation is a necessary part of the utility business to ensure a service delivery level and to protect the public's safety, health, and welfare. Regulations serve to protect the environment for future generations. Regulations ensure conservation and protection of our natural resources.

Regulations are regularly considered and promulgated by state and federal governments. WMU staff is active in monitoring proposed regulations and the impacts such regulations have on a local basis. Comment and impact on the promulgation of regulations on a federal level is limited, however, WMU staff communicate with state and national industry organizations and through direct contact with federal officials elected from Kentucky. On a state level, WMU staff participates on numerous committees and task forces to provide a voice for city-owned water, wastewater, and solid waste utilities.

State regulations typically result as mandates on state regulatory agencies from federal legislation. Kentucky is a primacy state meaning that the State is responsible for implementing and enforcing federal regulation. Staff works to ensure that state regulations, when promulgated, are reasonable and practicable.

The most recent two (2) regulations that were enacted at the State level having a financial impact on WMU were the Kentucky wastewater laboratory certification program for wastewater treatment plants (401KAR 5:320) which required fees in the amount of \$1,900 and implementation of additional quality control standards and the other being HB 1 which requires a special purpose governmental entity (SPGE) to register, pay fees in the amount of \$500, and submit financial disclosure statements each fiscal year to the Kentucky State Auditor. WMU has complied with each of the above-mentioned regulations and continues to monitor other regulations as they are promulgated. WMU's current and future large scale construction projects have been designed considering proposed and future regulations.

- **Vulnerability**

The impacts of 9/11 and the resulting passage of the Bioterrorism Act in 2002 required utilities to consider their vulnerabilities as a primary consideration versus a secondary consideration. For mid-size and smaller utilities such as WMU the probability of an act of international violence or terrorism is extremely low.

However, WMU's vulnerabilities are real and must be considered. Planning must be in place to address catastrophic events, violence, or contamination. Potential threats to WMU include severe weather (tornado, lightning, ice or snow), earthquake, prolonged power outage, contamination of the raw or potable water supply, workplace or customer violence, hazardous chemical spills, contamination or contact, and regular job safety hazards including confined space, vehicular accidents, and personal injury accidents. Management continues to explore opportunities to reduce vulnerabilities of the Utility through upgrades to its systems, allocating budget dollars to make its facilities as safe and secure as possible, securing grant funds to install redundancy in critical equipment and provision of employee safety training on an annual basis. Security upgrades at the WMU Administration building and WTP were completed in FY 2013/2014. Upgrades included customer service area security enhancements for the Administration building as well as keyless entry access for both locations. WMU participates in the Local Disaster Emergency Services (DES) group on a monthly basis. This provides an opportunity for communication of all important stakeholders in the community to voice concerns and offer input for improvements as it relates to responding to various emergencies.

- **Growth**

It has been the policy of the WMU Commission to be neither pro nor con with respect to growth. Rather the Commission has placed as a part of its mission to accommodate growth as approved by the Planning Commission, the City Commission and the Fiscal Court with specified required levels of service. WMU and the City continue to examine and develop policies such as the Privilege Fee Ordinance that provide for growth and that protect the existing customer base from the costs of serving growth. Growth continues to show signs of improvement excepting the loss of the recent large industry as mentioned above.

The Consent Decree requirements impact future extensions to the sanitary sewer system, as a detailed, engineering-capacity analysis per the Capacity Assurance Program (CAP) is required for each extension. The capacity analysis thus has become a defacto growth management tool.

WMU avails itself of every opportunity during the development process to add to and to strengthen the water transmission system and backbone sanitary sewer system taking into consideration long range growth needs.

UTILITY HIGHLIGHTS

- **Renewals and Replacements**

WMU began its program of infrastructure renewals in 1996 with emphasis on improving service delivery and ensuring that all customers are afforded a comparable level of service delivery. Historically, WMU never attempted these types of improvements without incurring new debt. The infrastructure renewal program has been implemented and managed without additional funding allocations or rate increases. Funding for the program was achieved through management of WMU's depreciation funds. To date, this program has resulted in the following replacement totals:

• Waterline Replacements	113,331 (21.46 miles)
• Sanitary Sewer Replacements	107,148 feet (20.29 miles)
• Fire Hydrant Replacements	135
• Gate Valve Replacements	357
• Manhole Replacements	427
• Elevated Storage Tank Rehabilitations	5

The following infrastructure improvements were completed during the 2017/2018 fiscal year.

- Bonnie Brook Lane Water System Improvements – 453' water line, 0 hydrants and 3 isolation valves
- Woodland Drive Water System Improvements – 373' water line, 1 hydrant, and 3 isolation valves

- Hampton Manor Sanitary Sewer Improvements – 3,964' sewer line, 19 manholes
- Short Street Sanitary Sewer Improvements – 163' sewer line, 1 manhole,
- Rowland Avenue Sanitary Sewer Improvements – 336' sewer line, 1 manhole
- Rainmaker Hospitality (Holiday Inn Express Water and Sanitary Sewer Improvements) – 730' water line, 3 fire hydrants, 7 isolation valves, 190' sewer line and 3 manholes
- W&R Rentals Water and Sanitary Sewer Improvements – 1,380' water line, 3 fire hydrants, 6 isolation valves, 1,293' sewer line and 7 manholes
- Fire Hydrant Replacement Program – 3 hydrants at Lexington Avenue/Stamper Drive, Lexington Avenue/Meadowbrook Drive, 16 Manor Drive
- Valve Replacement Program – 8 isolation valves at Lexington Avenue/Stamper Drive (2), Lexington Avenue/Meadowbrook Drive (2), 16 Manor Drive, Old Boonesboro Road (GRC Property) and Old Boonesboro Road/Shanahan Lane (2)

Summary FY 2017/2018

*Water Line = 2,936 feet

*Sewer Line = 5,946 feet

*Fire Hydrants = 10

*Manholes = 31

*Isolation Valves = 27

Moving forward WMU will be designing and constructing infrastructure renewal projects at the Strodes Creek Wastewater Treatment Plant that will include improvements to the Solids Processing Facilities as well as potential expansion of the existing treatment processes (Anaerobic Selector Basins and Oxidation Ditches). The solids facilities are currently beyond their useful life expectancy and experience frequent breakdowns. Costs associated with these improvements are expected to be approximately \$3M. Potential industrial growth is driving improvements to the treatment facilities which are expected to range in cost from \$3M – \$4M. Both projects are likely to be funded from a combination of in-house and KIA funds.

UTILITY HIGHLIGHTS: FINANCIAL

Total Assets increased from \$142,663,229 June 30, 2017, to \$153,825,742 June 30, 2018, a net increase of \$11,162,513 or 7.82%. In the past few years, Winchester Municipal Utilities has completed the Strodes Creek and Lower Howards Creek wastewater treatment plants which were a part of many Consent Decree projects that have been placed into PP&E. The two plants have depreciated over \$1,975,978 in this fiscal year. The 2018 bonds were sold increasing cash reserves by 12.0 million to be used for the construction of the new water treatment plant. In addition, donated capital of ownership and

perpetual maintenance of system water and sewer lines and related appurtenances by developers was placed into PP&E.

Operating Revenues decreased from \$17,428,491 June 30, 2017, to \$16,344,264 June 30, 2018, a net decrease of \$1,084,227 or 6.22%. A decrease in industrial revenue from the loss of AllTech, in our customer base resulted in a decrease in operating revenues.

Operating Expenses increased from \$14,623,352, June 30, 2017, to \$15,767,957, June 30, 2018, a net increase of \$1,144,605 or 7.83%. The increase is due to salaries and related benefit costs. Pension costs have increased due to GASB 68 and GASB 75 that requires reporting of pension liability. Winchester Municipal Utilities is a member of the CERS retirement system which is a part of the retirement system of the State of KY.

Net Income before Contributions changed from \$1,484,014 June 30, 2017, to (\$811,769), June 30, 2018, a net change of \$2,295,783 or -154.70%. The decrease in industrial revenue and the increase of Pension costs related to the reporting changes resulted in a decrease in net income.

- **Statement of Net Assets**

Condensed Statement of Net Assets - Assets

	2018	2017	Difference	Percent
Current Assets	\$13,240,795	\$13,769,654	\$-528,859	-3.84
Non-Current Assets	\$26,617,302	\$13,823,996	\$12,793,306	92.54
Property, Plant & Equip	\$113,967,645	\$115,069,579	\$-1,101,934	-0.96
Total Assets	\$153,825,742	\$142,663,229	\$11,162,513	7.82
Deferred Outflows	\$3,051,922	\$1,736,578	\$1,315,344	75.00

Condensed Statement of Net Position – Liabilities and Net Position

	2018	2017	Difference	Percent
Current Liabilities	\$4,866,376	\$4,649,368	\$217,008	4.67
Noncurrent Liabilities including LTD	\$82,675,455	\$70,713,330	\$11,962,125	20.17
Net Position:				
Deferred Inflows	\$794,657	\$0	\$794,657	100.00
Net Investment of Capital Assets	\$37,600,853	\$49,154,657	\$-11,553,804	-23.51
Restricted Net Assets	\$26,813,784	\$14,002,690	\$12,811,094	91.49
Unrestricted Net Assets	\$4,126,542	\$5,879,762	\$-3,525,604	-46.07
Total Net Position	\$68,541,179	\$69,037,109	\$-2,268,314	-3.20

- **Statement of Revenues, Expenses and Changes in Net Assets**

Condensed Statement of Revenues, Expenses and Changes in Net Assets

	2018	2017	Difference	Percent
Operating Revenues				
Water	\$5,093,741	\$5,266,431	\$-172,690	-3.28
Wastewater	\$7,593,820	\$8,578,082	\$984,262	-11.47
Solid waste	\$3,656,703	\$3,583,978	\$72,725	2.03
Total Operating Revenues	\$16,344,264	\$17,428,491	\$1,084,227	-6.22
Operating Expenses including Depreciation	\$15,767,957	\$14,623,352	\$1,144,605	7.83
Operating Income	\$576,307	\$2,805,139	\$-2,228,832	-79.46
Non-Operating Income	\$422,069	\$348,692	\$73,377	21.04
Interest Expense	\$-1,810,145	\$-1,669,817	\$-140,328	8.40
Net Income before Contributions	\$-811,769	\$1,484,014	\$2,295,783	-154.70
Capital Grants and Contributions	\$315,839	\$643,309	\$-327,470	-50.90
Changes in Net Position	\$-495,930	\$2,127,323	\$-2,623,253	-123.31
Net Assets, Beginning of Year	\$69,037,109	\$68,682,170	\$2,127,323	3.10
Effect of adoption of GASB 75	\$ 0	\$-1,772,384	\$-1,772,384	
Net Position, Beginning of Year, Restated	\$69,037,109	\$66,909,786	\$354,939	0.52
Net Assets, End of Year	\$68,541,179	\$69,037,109	\$2,268,314	-3.20

- **Five-Year Capital Plan**

The WMU Commission maintains and annually updates a five-year capital plan that identifies and prioritizes the capital requirements of WMU necessary for customer service, regulatory compliance, and to accommodate growth. The five-year investment totals in excess of \$8,265,700 that will be invested in infrastructure renewal and administrative support. Additionally \$275,000 is reserved for emergency and / or unexpected expenditures.

- **Debt Administration**

As of July 1, 2018, WMU maintained the following debt:

• Series 2011 Bonds	\$ 6,562,500
• Series 2012 Bonds	\$ 5,595,000
• Series 2014 Bonds	\$ 9,295,000
• Series 2018 Bonds	\$ 13,045,000
• KIA Strodes Creek	\$ 11,548,615
• KIA Vaught	\$ 185,942
• KIA Tank	\$ 228,266
• KIA LHC	\$ 28,767,280
• KIA BelAir	\$ 422,261
• KIA Hampton	\$ 1,249,088

The Debt Service coverage factor for Bonds of 3.43 in FY 2017/2018 is favorable to the required 1.2 coverage limit. The Debt Service coverage factor for KIA debt of 1.16 in FY 2017/2018 is favorable to the required 1.0 coverage limit. Debt Service coverage is based upon the revenue of the combined utility functions – Water, Sewer, and Solid Waste.

- **FY 2018/2019 Budget Assumptions**

Total combined revenues for FY 2018/2019 are projected to decrease from FY 2017/2018 revenues by 8.03%. The main contributing change in budget revenues is from the loss of revenues from Alltech, a large industrial customer which ceased operations in Winchester resulting in a decrease in water and wastewater revenues. Operating expenses excluding depreciation for FY 2018/2019 are projected to decrease from budgeted FY 2017/2018 operating expenses by approximately 1.55%. Operating expenses will be impacted by decreased electricity and chemical treatment supply expenses that are directly attributable to the decreased flow at the water and wastewater treatment plants from the loss of Alltech from the customer base. The decreases were offset slightly by the increase in employee salaries and related benefits including insurance and pension costs.

The debt service coverage ratio is required to be 1.20 for bonds and 1.00 for KIA. Both formulas calculate by adding depreciation, a non-cash expense back to income available for debt service. The budgeted debt service coverage ratio is 2.79 for Bond debt and 1.07 for KIA debt.

CONTACTING THE COMPANY'S FINANCIAL MANAGEMENT

This report is designed to provide the WMU Commission, the City Commission, the customers of WMU and WMU's creditors a general overview of WMU's finances and to demonstrate WMU's financial accountability. Questions should be addressed to:

Michael H. Flynn
General Manager

or

Jennifer Sparks
Director of Finance and Accounting

150 North Main Street
P.O. Box 4177
Winchester, KY 40392-4177
859-744-5434

WINCHESTER MUNICIPAL UTILITIES
STATEMENTS OF NET POSITION
JUNE 30, 2018 AND 2017

ASSETS	2018	2017
CURRENT ASSETS:		
Cash and Cash Equivalents	\$ 9,429,690	\$ 9,965,474
Cash and Cash Equivalents, Restricted	342,778	327,498
Accrued Interest, Restricted	450	371
Accounts Receivable, Customers (Net of Allowance for Doubtful Accounts, 2018 and 2017, \$41,523 and \$51,597)	1,974,870	1,963,957
SDC Assessments Receivable	483,000	489,767
Other Accounts Receivable	17,382	38,775
Inventory -Materials and Supplies	436,859	418,432
Prepaid Expenses	555,769	565,380
Total Current Assets	13,240,798	13,769,654
NONCURRENT ASSETS:		
Cash and Cash Equivalents, Restricted	26,617,302	13,823,996
Property, Plant & Equipment:		
Utility Systems, Net of Depreciation	108,664,315	111,396,193
Land	1,519,050	1,519,050
Construction in Progress	3,784,280	2,154,336
Total Noncurrent Assets	140,584,947	128,893,575
TOTAL ASSETS	\$ 153,825,745	\$ 142,663,229
DEFERRED OUTFLOWS OF RESOURCES		
Pension Plan	\$ 2,376,120	\$ 1,596,934
OPEB	675,802	139,644
Total Deferred Outflows of Resources	\$ 3,051,922	\$ 1,736,578

The accompanying notes are integral part of this statement

WINCHESTER MUNICIPAL UTILITIES
STATEMENTS OF NET POSITION (CONTINUED)
JUNE 30, 2018 AND 2017

	<u>2018</u>	<u>2017</u>
LIABILITIES AND NET POSITION		
CURRENT LIABILITIES:		
Accounts Payable	\$ 728,800	\$ 557,787
Other Accrued Liabilities	155,208	228,390
Customer Deposits	135,538	133,521
Accrued Interest Payable	87,642	92,377
Current Portion of Long-Term Debt	<u>3,759,188</u>	<u>3,637,293</u>
Total Current Liabilities	<u>4,866,376</u>	<u>4,649,368</u>
NONCURRENT LIABILITIES:		
Compensated Absences	532,705	524,097
Noncurrent Portion of Long-Term Debt	72,607,604	62,277,629
Net Pension Liability	7,097,486	5,999,576
Net OPEB Liability	<u>2,437,660</u>	<u>1,912,028</u>
Total Noncurrent Liabilities	<u>82,675,455</u>	<u>70,713,330</u>
TOTAL LIABILITIES	<u>\$ 87,541,831</u>	<u>\$ 75,362,698</u>
DEFERRED INFLOWS OF RESOURCES		
Pension Plan	\$ 667,028	-
OPEB	<u>127,629</u>	<u>-</u>
Total Deferred Inflows of Resources	<u>\$ 794,657</u>	<u>\$ -</u>
NET POSITION:		
Net Investment of Capital Assets	\$ 37,600,853	\$ 49,154,657
Restricted for:		
Restricted for Capital Projects	24,422,826	12,178,161
Restricted for Debt Service	2,390,958	1,824,529
Unrestricted	<u>4,126,542</u>	<u>5,879,762</u>
TOTAL NET POSITION	<u>\$ 68,541,179</u>	<u>\$ 69,037,109</u>

The accompanying notes are integral part of this statement

WINCHESTER MUNICIPAL UTILITIES
STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN FUND NET POSITION
FOR THE YEARS ENDED JUNE 30, 2018 AND 2017

	<u>2018</u>	<u>2017</u>
OPERATING REVENUES:		
Water	\$ 5,093,741	\$ 5,266,431
Wastewater	7,593,820	8,578,082
Solid Waste	3,598,118	3,539,067
Transfer Station	<u>58,585</u>	<u>44,911</u>
Total Operating Revenues	<u>16,344,264</u>	<u>17,428,491</u>
OPERATING EXPENSES:		
Administrative	2,556,217	2,342,836
Solid Waste	2,223,091	2,002,127
Water	3,874,231	3,295,468
Wastewater	6,981,618	6,864,731
Vehicle Maintenance	<u>132,800</u>	<u>118,190</u>
Total Operating Expenses	<u>15,767,957</u>	<u>14,623,352</u>
OPERATING INCOME (LOSS)	576,307	2,805,139
NONOPERATING REVENUES (EXPENSES):		
Interest Income	183,486	132,405
Interest Expense	(1,582,003)	(1,653,017)
Other Income	182,290	187,800
Gain on Sale of Capital Assets	56,293	28,487
Amortization Expense	<u>(228,142)</u>	<u>(16,800)</u>
Total Nonoperating Revenues (Expenses)	<u>(1,388,076)</u>	<u>(1,321,125)</u>
NET INCOME (LOSS) BEFORE CONTRIBUTIONS	(811,769)	1,484,014
CAPITAL CONTRIBUTIONS	<u>315,839</u>	<u>643,309</u>
CHANGE IN NET POSITION	(495,930)	2,127,323
NET POSITION, BEGINNING OF YEAR	69,037,109	68,682,170
Effect of adoption of GASB 75 - See Note xx	<u>-</u>	<u>(1,772,384)</u>
NET POSITION, BEGINNING OF YEAR -Restated	<u>69,037,109</u>	<u>66,909,786</u>
NET POSITION, END OF YEAR	<u>\$ 68,541,179</u>	<u>\$ 69,037,109</u>

The accompanying notes are integral part of this statement

**WINCHESTER MUNICIPAL UTILITIES
STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED JUNE 30, 2018 AND 2017**

	<u>2018</u>	<u>2017</u>
CASH FLOWS FROM OPERATING ACTIVITIES:		
Receipts from Customers	\$ 16,393,871	\$ 17,429,538
Payments to Suppliers	(4,419,384)	(4,594,943)
Payments to Employees	(5,731,486)	(4,738,725)
Other Operating Receipts (Payments)	<u>21,393</u>	<u>58,758</u>
Net Cash Provided (Used) by Operating Activities	<u>6,264,394</u>	<u>8,154,628</u>
CASH PROVIDED (USED) BY CAPITAL AND RELATED FINANCING ACTIVITIES:		
Proceeds from Sale of Equipment	56,293	31,406
Proceeds from Long-Term Debt	14,294,088	-
Principal Payments	(3,637,292)	(3,544,944)
Interest Payments	(1,586,738)	(1,655,545)
Purchase of Property, Plant and Equipment	(3,799,479)	(6,077,109)
Bond Issuance Costs & Escrow	-	-
Contributed Capital Received	315,839	2,445,080
Cash from Other Income	<u>182,290</u>	<u>184,165</u>
Net Cash Provided (Used) by Capital and Related Financing Activities	<u>5,825,001</u>	<u>(8,616,947)</u>
CASH PROVIDED (USED) BY INVESTING ACTIVITIES:		
Proceeds from Sales and Maturities of Investments	-	3,635
Cash from Interest in Investments	<u>183,407</u>	<u>132,378</u>
Net Cash Provided (Used) by Investing Activities	<u>183,407</u>	<u>136,013</u>
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	<u>12,272,802</u>	<u>(326,306)</u>
CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR	<u>24,116,968</u>	<u>24,443,274</u>
CASH AND CASH EQUIVALENTS, END OF YEAR	<u>\$ 36,389,770</u>	<u>\$ 24,116,968</u>
Reconciliation of Cash and Cash Equivalents to the Statement of Net Assets:		
Cash and Cash Equivalents - unrestricted	\$ 9,429,690	\$ 9,965,474
Cash and Cash Equivalents - restricted current	342,778	327,498
Cash and Cash Equivalents - restricted noncurrent	<u>26,617,302</u>	<u>13,823,996</u>
Cash and Cash Equivalents, End of Year	<u>\$ 36,389,770</u>	<u>\$ 24,116,968</u>

The accompanying notes are integral part of this statement

WINCHESTER MUNICIPAL UTILITIES
STATEMENTS OF CASH FLOWS (CONTINUED)
FOR THE YEARS ENDED JUNE 30, 2018 AND 2017

	<u>2018</u>	<u>2017</u>
RECONCILIATION OF OPERATING INCOME (LOSS)		
TO NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES:		
Operating Income (Loss)	\$ 576,307	\$ 2,805,139
Adjustments to Reconcile Operating Income (Loss) to Net Cash Provided (Used) by Operating Activities:		
Depreciation/Amortization	5,299,760	4,820,779
(Increase) Decrease in Assets:		
Accounts Receivable, Customers	(10,913)	23,952
SDC Receivables	6,767	(7,767)
Other Accounts Receivable	21,393	58,758
Material and Supplies	(18,427)	319
Prepaid Expenses	9,614	3,689
Deferred Outflows	(1,454,988)	(337,236)
Increase (Decrease) in Liabilities:		
Accounts Payable	171,013	(67,312)
Accrued Liabilities	(73,182)	15,760
Net Pension Liability	1,763,187	807,097
Compensated Absences	8,608	46,588
Customer Deposits	<u>2,017</u>	<u>(15,138)</u>
Net Cash Provided (Used) by Operating Activities	<u>\$ 6,301,156</u>	<u>\$ 8,154,628</u>
 Supplemental Information, Noncash Transactions		
Donated Capital Assets	\$ <u>208,040</u>	\$ <u>183,091</u>
Depreciation and Amortization Expense	\$ <u>5,299,760</u>	\$ <u>4,820,779</u>

The accompanying notes are integral part of this statement

**WINCHESTER MUNICIPAL UTILITIES
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEARS ENDED JUNE 30, 2018 AND 2017**

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Reporting Entity

Winchester Municipal Utilities (WMU) is a component unit of the City of Winchester, Kentucky and is accounted for as a governmental enterprise fund. The purpose of WMU is to operate the City's water, sewer and solid waste utility services. It is financed and operated in a manner similar to a private business enterprise where the intent of the governing body is that costs (expenses, including depreciation) of providing goods or services to the general public on a continuing basis are financed primarily through user charges. The financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. The accounts are maintained on the accrual basis of accounting. Revenues are recognized when earned and expenses are recognized when incurred.

Cash and Cash Equivalents

For the purposes of the Statement of Cash Flows, WMU considers all short-term highly liquid investments with a maturity of three months or less when purchased to be cash equivalents. WMU invests resources that are restricted by the terms of the bond indentures in premium checking accounts which are interest bearing.

Current Restricted Cash Equivalents are set aside to provide resources for bond and interest payments within the next six months. Noncurrent Restricted Cash Equivalents are set aside to comply with the other provisions of the revenue bond indentures for debt service, depreciation, and capital maintenance as described in Note 3.

Accounts Receivable

Accounts receivable - Customers, are stated at the amount management expects to collect from outstanding balances. Management provides for probable uncollectible amounts through a provision for bad debt expense. An adjustment to an allowance for doubtful accounts is based on its assessment of the current status of individual accounts. Balances that are still outstanding after management has used reasonable collection efforts are written off through a charge to the valuation allowance and a credit to accounts receivable. As of June 30, 2018 and 2017, \$103,886 and \$98,775 were written off as uncollectible, respectively.

SDC assessments and other receivables are stated at the amount management expects to collect from outstanding balances and management expects to fully collect all of these receivables.

Materials and Supplies Inventory

Materials and supplies are stated at cost. Cost is determined using the "first-in, first-out" method.

Prepaid Expenses

Certain payments to vendors reflect costs applicable to future accounting periods and are recorded as prepaid expenses.

**WINCHESTER MUNICIPAL UTILITIES
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEARS ENDED JUNE 30, 2018 AND 2017**

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Restricted Assets

The use of certain assets of enterprise funds is restricted by specific provisions of bond resolutions and agreements with various parties. Assets so designated are identified as restricted assets on the statement of net position. When both restricted and unrestricted resources are available for use, it is WMU's policy to use restricted resources first, and then unrestricted resources as they are needed. Restricted assets are classified as noncurrent if they are for acquisition or construction of capital assets, for liquidation of long-term debt, or are for other current operations.

Property, Plant and Equipment

Property, plant, and equipment are stated at cost and depreciated over their estimated useful lives using the straight-line method. Donated capital assets are recorded at acquisition value, the price that would be paid to acquire an asset with equivalent service potential, at the date of donation. Contractor's cost is a level 1 input used to determine acquisition value at the date developers donated infrastructure improvements to WMU. WMU's capitalization policy is \$500.

Major outlays are capitalized when constructed assets are completed. Interest incurred during the construction phase of capital assets is included as part of the capitalized value of the assets constructed.

The costs of normal maintenance and repairs that do not add to the value of the asset or materially extend assets' lives are not capitalized.

Assets under capitalized lease obligations are recorded at the discounted present value of the future minimum lease payments at the inception of the respective leases. The amounts capitalized are being amortized by the straight-line method over the lesser of the term of the lease or the estimated life of the asset. Amortization of these assets is included in depreciation expense.

Accrued Compensated Absences

Accumulated vacation, sick leave and compensatory time are recorded as an expense and liability as these benefits accrue to employees in accordance with the provisions of Statement No. 16 of the Governmental Accounting Standards Board.

Bond Premium and Discount Amortization

Bond premiums and discounts, are amortized over the life of the bonds. Bonds payable are reported net of the applicable bond premium or discount. Amortization expense for bond discount as of June 30, 2018 and 2017 was \$228,142 and \$16,800, respectively.

Interest

Interest is charged to expense as incurred except, WMU follows the policy of capitalizing interest as a component of construction in progress. For the years ended June 30, 2018 and 2017, total interest incurred and expensed was \$1,582,003 and \$1,653,017, respectively.

**WINCHESTER MUNICIPAL UTILITIES
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEARS ENDED JUNE 30, 2018 AND 2017**

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Pensions

For purposes of measuring the net pension liability, deferred outflows of resources and deferred inflows of resources related to pensions, and pension expense, information about the fiduciary net position of the County Employees Retirement System Non-Hazardous (“CERS”) and additions to/deductions from fiduciary net position have been determined on the same basis as they are reported by the CERS pension system. For this purpose, benefit payments (including refunds of employee contributions) are recognized when due and payable in accordance with the benefit terms. Investments are reported at fair value.

Net Position

Net position represents the difference between assets plus deferred outflows of resources less liabilities plus deferred inflows of resources. Net investment in capital assets consists of capital assets, including restricted capital assets, net of accumulated depreciation and 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 and the related balances in deferred outflows or inflows of resources. If there are unspent related debt proceeds at year-end, the portion of the debt attributable to the unspent proceeds are not included in the calculation of net investment in capital assets. Rather, that portion of the debt is included in the same net position component as the unspent proceeds. Net position is reported as restricted when constraints are placed on net positions use through external constraints imposed by creditors (example: debt covenants), grantors, contributors, or laws or regulations of other governments or constraints imposed by law through constitutional provisions or enabling legislation. Net positions that do not meet the definition of “restricted” or “net investment in capital assets, net of related debt”, are considered unrestricted.

Operating and Nonoperating Revenues and Expenses

Revenues and expenses are distinguished between operating and non-operating items. Operating revenues generally result from providing services and producing, and delivering goods in connection with WMU’s principal ongoing operations. The principal operating revenues of WMU are charges to customers for sales and services. Operating expenses for enterprise funds include the cost of sales and services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

Nonmonetary Transaction

WMU accepts utility installations built by contractors upon inspection. The utility installations are added to fixed assets and contributed capital at contractor’s cost, which approximates the price that would be paid to acquire an asset with equivalent service potential (acquisition value), as required by GASB Statement No. 72.

Capital and Operating Grants and Subsidies

Operating grants and subsidies that may be used to pay operating expenses are recorded as other income. Grants that are restricted to the purchase of property, plant and equipment are recorded as contributed capital.

Tap Fees

Tap Fees are restricted by ordinance for the use of capital improvements.

**WINCHESTER MUNICIPAL UTILITIES
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEARS ENDED JUNE 30, 2018 AND 2017**

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

System Development Charges

WMU assesses system development charges to developers as a means to help finance new construction of systems required to facilitate growth. The charges are restricted by policy for capital construction.

Basis of Estimates

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

Joint Venture

A joint venture is a legal entity or other organization that results from a contractual agreement and that is owned, operated or governed by two or more participants as a separate and specific activity subject to joint control in which the participants retain (a) an ongoing financial interest or (b) an ongoing financial responsibility. WMU participates in the following joint venture:

Clark County Geographic Information System Consortium (CCGIS), is a governmental agency created by an inter-local agreement between the Clark County PVA, City of Winchester and WMU. CCGIS was created to provide a geographic system to serve the needs of Winchester and Clark County. The operations are funded by the City, WMU and the Clark County Fiscal Court. WMU provides management services for CCGIS. WMU contributed \$84,966 and \$84,847 for the years ended 2018 and 2017, respectively. CCGIS had accounts payables to WMU of \$0 and \$5,205 for the years ended 2018 and 2017, for reimbursements of payroll and other expenses. CCGIS had accounts receivable from WMU of \$0 and \$0 for the years ended 2018 and 2017, respectively, for excess reimbursements of payroll and other expenses. Complete financial statements for CCGIS can be obtained from WMU's Director of Finance.

New Accounting Pronouncements

GASB Statement No. 87, *Leases* (GASB 87), increases the usefulness of governments' financial statements by requiring recognition of certain lease assets and liabilities for leases that previously were classified as operating leases and recognized as inflows of resources or outflows of resources based on the payment provisions of the contract. It establishes a single model for lease accounting based on the foundational principle that lease are financings of the right to use an underlying asset. GASB 87 will be effective for reporting periods beginning after December 15, 2019. The District has not determined the financial impact of the implementation of GASBS No. 87.

GASB Statement No. 84, *Fiduciary Activities* (GASB 84), improves guidance regarding the identification of fiduciary activities for accounting and financial reporting purposes and how these activities should be reported. This statement establishes criteria for identifying fiduciary activities for all state and local governments. Separate criteria are included to identify fiduciary component units and postemployment benefit arrangements that are fiduciary activities. GASB 84 will be effective for reporting periods beginning after December 15, 2018. The District has not determined the financial impact of the implementation of GASBS No. 84.

**WINCHESTER MUNICIPAL UTILITIES
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEARS ENDED JUNE 30, 2018 AND 2017**

NOTE 2 – DEPOSITS AND INVESTMENTS

WMU's investment policy conforms to the restrictions outlined in KRS 66.480. WMU deposits its funds in banks insured by FDIC. Investments include short term cash securities and United States backed securities. Collateral is required for all deposits in excess of FDIC at 100% of the carrying amount at the bank. Collateral consists of obligations of the United States and Kentucky municipal bonds.

Interest rate Risk

This is the risk that changes in market interest rates will adversely affect the fair value of an investment. Generally, the longer the maturity of an investment, the greater the sensitivity of its fair value to changes in market interest rates. WMU does not have a formal investment policy that limits investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates. Information about the exposure of WMU's deposits and investments to this risk, using the segmented time distribution model is as follows:

06/30/18		Maturities (in Years)				
Type	Fair Value	< Than 1	1 - 5	6 - 10	> Than 10	
Cash and Cash Equivalents	\$ 36,389,770	\$ 36,389,770	\$ 0	\$ 0	\$ 0	
Total	\$ 36,389,770	\$ 36,389,770	\$ 0	\$ 0	\$ 0	

06/30/17		Maturities (in Years)				
Type	Fair Value	< Than 1	1 - 5	6 - 10	> Than 10	
Cash and Cash Equivalents	\$ 24,116,968	\$ 24,116,968	\$ 0	\$ 0	\$ 0	
Total	\$ 24,116,968	\$ 24,116,968	\$ 0	\$ 0	\$ 0	

Credit Risk

This risk is the risk that an issuer of a debt type investment will not fulfill its obligation to the holder of the investment. This is measured by assignment of a rating by a nationally recognized rating organization. U.S. Government securities or obligations explicitly guaranteed by the U.S. Government are not considered to have credit risk exposure. WMU has no formal policy on managing credit risk; however, Kentucky Revised Statutes authorize municipalities to invest in obligations of the United States and its agencies, obligations of the Commonwealth of Kentucky and its agencies and shares in savings and loan associations insured by federal agencies. Larger amounts can be deposited in savings and loan associations and banks provided such institutions pledge obligations of the United States government or its agencies as security. Presented below is the minimum rating required for each type of deposit and investment:

06/30/18		Ratings			
Type	Fair Value	AAA	AA	A	Unrated
Cash and Cash Equivalents	\$ 36,389,770	\$ 0	\$ 0	\$ 0	\$ 36,389,770
Total	\$ 36,389,770	\$ 0	\$ 0	\$ 0	\$ 36,389,770

06/30/17		Ratings			
Type	Fair Value	AAA	AA	A	Unrated
Cash and Cash Equivalents	\$ 24,116,968	\$ 0	\$ 0	\$ 0	\$ 24,116,968
Total	\$ 24,116,968	\$ 0	\$ 0	\$ 0	\$ 24,116,968

**WINCHESTER MUNICIPAL UTILITIES
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEARS ENDED JUNE 30, 2018 AND 2017**

NOTE 2 – DEPOSITS AND INVESTMENTS (CONTINUED)

Custodial Credit Risk

Custodial credit risk is the risk that, in the event of the failure of the counterparty, WMU will not be able to recover the value of its deposits and investments that are in possession of an outside party. WMU has no formal policy for custodial credit risk; however, as of June 30, 2018 and 2017 all deposits and investments were either fully collateralized by federal depository insurance or by the pledging institution in WMU's name or were held in a bank's trust department in the City of Winchester's name, the primary government of the component unit, WMU.

NOTE 3 – CREATION OF ACCOUNTS AND RESTRICTED ASSETS

The Bond Ordinances require the creation of various separate deposit accounts designated for a specific purpose in accordance with the ordinance. A brief description of each required account is as follows:

Revenue Account

All income to WMU is deposited to the Revenue Account and then transferred to the other ordinance accounts as listed below.

Bond Redemption Account

The Bond Redemption Account was established to provide a source of funds for the payment of the bond principal and interest due within the current year. By the 20th day of each month funds equal to the total of one-sixth of the semiannual interest payment plus one-twelfth of the next annual bond principal payment are to be transferred to the account. The account is reflected as currently restricted asset.

Reserve Account

The Reserve Account was established to provide funds for the payment of debt based on the least of three provisions: 1) maximum annual principal and interest, 2) 125% of the average annual principal and interest or 3) 10% of bond proceeds.

Depreciation Account

The Depreciation Account was established to provide funds for extraordinary repairs, improvements and expansion. WMU is required to fund 12% of the annual gross revenues or \$42,000 whichever is greater annually into the account.

Operation and Maintenance Account

The Operation and Maintenance Account was established to pay the reasonable, necessary costs of operating, maintaining and repairing the systems.

**WINCHESTER MUNICIPAL UTILITIES
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEARS ENDED JUNE 30, 2018 AND 2017**

NOTE 3 – CREATION OF ACCOUNTS AND RESTRICTED ASSETS (CONTINUED)

The restricted assets in the accompanying financial statements are restricted as to use by bond ordinance or by external parties at June 30, 2018 and 2017 follows:

	<u>6/30/18</u>	<u>6/30/17</u>
Restricted by Ordinance:		
Bond Redemption Account	\$ 342,778	\$ 327,498
Reserve Accounts	1,096,967	1,090,407
Depreciation Account	2,741,065	1,742,676
Subtotal	<u>4,180,810</u>	<u>3,160,581</u>
Other Restricted Accounts:		
SDC Water Fund	2,783,018	2,741,440
SDC Wastewater Fund	210,892	185,944
Cash with Escrow Agent	444,144	0
Bond Funds Central	12,051,654	0
Customer Deposits	146,297	148,804
KIA Reserve	507,069	406,624
Water Improvements	3,012,169	2,944,169
2014 Bond Funds	2,471,301	3,582,090
Capital Accum-Water	702,669	608,236
Capital Accum-Wastewater	450,058	373,606
Total	<u>\$ 26,960,080</u>	<u>\$ 14,151,494</u>
Current Restricted	<u>\$ 342,778</u>	<u>\$ 327,498</u>
Noncurrent Restricted	<u>\$ 26,617,302</u>	<u>\$ 13,823,996</u>

NOTE 4 – PROPERTY, PLANT AND EQUIPMENT

WMU's property, plant and equipment as of June 30, 2018 and 2017 are as follows:

<u>6/30/2018</u>	<u>Beginning</u>	<u>Additions</u>	<u>Disposals</u>	<u>Ending</u>
Non-depreciable Assets:				
Land	\$ 1,519,050	\$ 0	\$ 0	\$ 1,519,050
Construction in Progress	2,154,336	2,567,461	(937,517)	3,784,280
Total Non-depreciable Assets	<u>\$ 3,673,386</u>	<u>\$ 2,567,461</u>	<u>\$ (937,517)</u>	<u>\$ 5,303,330</u>
Depreciable Assets:				
Administrative	\$ 3,457,447	\$ 217,652	\$ (161,415)	\$ 3,513,684
Water System	57,407,555	11,117,841	(10,246,951)	58,278,445
Wastewater System	112,258,371	1,881,706	(668,080)	113,471,997
Solid Waste	7,890,376	682,023	(611,072)	7,961,327
Vehicle Maintenance	449,920	27,777	0	477,697
Equipment Capital Lease	33,169	0	0	33,169
Subtotal	<u>181,496,838</u>	<u>13,926,999</u>	<u>(11,687,518)</u>	<u>183,736,319</u>
Accumulated Depreciation:				
Administrative	(2,004,462)	(138,715)	(163)	(2,143,340)
Water System	(15,514,832)	(1,307,259)	6,785	(16,815,306)
Wastewater System	(30,587,330)	(3,160,305)	0	(33,747,635)
Solid Waste	(2,420,861)	(457,481)	93,477	(2,784,865)
Vehicle Maintenance	(342,404)	(7,695)	0	(350,099)
Prior Years Accumulated	(19,230,756)	0	0	(19,230,756)
Subtotal	<u>(70,100,645)</u>	<u>(5,071,455)</u>	<u>100,099</u>	<u>(75,072,001)</u>
Total Net Property, Plant and Equipment	<u>\$ 111,396,193</u>	<u>\$ 8,855,544</u>	<u>\$ (11,587,419)</u>	<u>\$ 108,664,318</u>

**WINCHESTER MUNICIPAL UTILITIES
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEARS ENDED JUNE 30, 2018 AND 2017**

NOTE 4 – PROPERTY, PLANT AND EQUIPMENT (CONTINUED)

<u>06/30/17</u>	<u>Beginning</u>	<u>Additions</u>	<u>Disposals</u>	<u>Ending</u>
Non-depreciable Assets:				
Land	\$ 1,519,050	\$ 0	\$ 0	\$ 1,519,050
Construction in Progress	10,953,543	1,360,108	(10,159,315)	2,154,336
Total Non-depreciable Assets	<u>\$ 12,472,593</u>	<u>\$ 1,360,108</u>	<u>\$ (10,159,315)</u>	<u>\$ 3,673,386</u>
Depreciable Assets:				
Administrative	\$ 3,341,894	\$ 252,906	\$ (137,353)	\$ 3,457,447
Water System	47,228,257	12,084,930	(1,905,632)	57,407,555
Wastewater System	111,720,432	1,659,546	(1,121,607)	112,258,371
Solid Waste	7,538,055	1,078,013	(725,692)	7,890,376
Vehicle Maintenance	449,920	0	0	449,920
Equipment Capital Lease	81,279	0	(48,110)	33,169
Subtotal	<u>170,359,837</u>	<u>15,075,395</u>	<u>(3,938,394)</u>	<u>181,496,838</u>
Accumulated Depreciation:				
Administrative	(1,969,058)	(129,377)	93,973	(2,004,462)
Water System	(14,461,926)	(1,097,380)	44,474	(15,514,832)
Wastewater System	(27,554,568)	(3,141,464)	108,702	(30,587,330)
Solid Waste	(2,157,867)	(428,267)	165,273	(2,420,861)
Vehicle Maintenance	(334,913)	(7,491)	0	(342,404)
Prior Years Accumulated	(19,230,756)	0	0	(19,230,756)
Subtotal	<u>(65,709,088)</u>	<u>(4,803,979)</u>	<u>412,422</u>	<u>(70,100,645)</u>
Total Net Property, Plant and Equipment	<u>\$ 104,650,749</u>	<u>\$ 10,271,416</u>	<u>\$ (3,525,972)</u>	<u>\$ 111,396,193</u>

Depreciation is recorded on a straight-line basis over the useful lives of the assets as follows:

Buildings and Concrete	40-50 years
Main Replacement Program	40 years
Equipment	2-7 years
Vehicles	5-10 years

Depreciation expense in total and by function follows:

<u>Function</u>	<u>2018</u>	<u>2017</u>
Administrative	\$ 138,715	\$ 129,377
Water System	1,307,259	1,097,380
Wastewater System	3,160,305	3,141,464
Solid Waste	457,481	428,267
Vehicle Maintenance	7,695	7,491
Total Depreciation Expense	<u>\$ 5,071,455</u>	<u>\$ 4,803,979</u>

The net investment in capital assets at June 30, 2018 and 2017 is composed of the following elements:

	<u>2018</u>	<u>2017</u>
Capital Assets	\$ 113,967,648	\$ 115,069,579
Total Debt, Net of Unamortized Bond Discount	(76,366,792)	(65,914,922)
Net Investment in Capital Assets	<u>\$ 37,600,856</u>	<u>\$ 49,154,657</u>

**WINCHESTER MUNICIPAL UTILITIES
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEARS ENDED JUNE 30, 2018 AND 2017**

NOTE 5 – LONG-TERM DEBT

WMU issues revenue bonds to finance improvements and extensions to the water and sewer systems. The Winchester Municipal Utilities bonded indebtedness and other long-term notes at June 30, 2018 and 2017, are summarized as follows:

Description	Rate	Maturity	Original Issue	2018 Total	2017 Total
2011 Issue	5.27%	01/01/31	\$ 9,010,000	\$ 6,562,500	\$ 6,943,750
2012 Issue	2.00-3.75%	07/01/32	7,495,000	5,595,000	5,915,000
2014 Issue	2.00-4.00%	07/01/45	9,915,000	9,295,000	9,510,000
2018 Issue	3.00-4.00%	07/01/42	13,045,000	13,045,000	13,045,000
Less: Unamortized Discount				(532,160)	(327,213)
Total Bonds				33,965,340	22,041,519
KIA-Strodes Creek	1.00%	12/01/28	21,000,000	11,548,615	12,586,703
		Estimate			
KIA-Lower Howards Creek	2.00%	01/01/31	36,600,000	28,767,280	30,396,804
		Estimate			
KIA-Bel-Air	2.00%	01/01/31	1,000,000	422,261	446,180
KIA-Industrial Storage Tanks	2.00%	12/01/30	340,326	228,266	244,191
KIA-Vaught Court	2.00%	06/01/31	287,400	185,942	199,525
KIA-Hampton Manor	1.75%	06/01/37	\$ 1,249,088	1,249,088	0
Total KIA Loans				42,401,452	43,873,403
Less: Current Maturities				(3,759,188)	(3,637,293)
Total Long Term				\$ 72,607,604	\$ 62,277,629

The annual bond and long-term debt service requirements, as of June 30, 2018, are as follows:

Fiscal Year	Principal	Interest	Total
2018	\$ 3,759,188	\$ 1,984,233	\$ 5,743,421
2019	3,895,130	1,906,085	5,801,215
2020	3,983,974	1,823,630	5,807,604
2021	4,076,563	1,738,682	5,815,245
2022	4,169,998	1,650,483	5,820,481
2022-2026	22,421,861	6,793,992	29,215,853
2027-2031	20,570,815	3,992,254	24,563,069
2032-2036	6,471,422	2,031,852	8,503,274
2037-2041	6,515,000	848,975	7,363,975
2042-2046	1,035,000	62,600	1,097,600
	\$ 76,898,951	\$ 22,832,786	\$ 99,731,737

**WINCHESTER MUNICIPAL UTILITIES
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEARS ENDED JUNE 30, 2018 AND 2017**

NOTE 5 – LONG-TERM DEBT (CONTINUED)

Series 2011 Bonds

On April 14, 2011, the City issued \$9,010,000 of utilities revenue bonds for WMU secured by a first and prior security interest in any and all right, title and interest of WMU in the portions of the Project (extensions and improvements of the System) that constitute personal property and in all additions, attachments, accessions, and substitutions thereto, and any proceeds therefrom. The 2011 bond issues financed the extensions and improvements to the combined and consolidated municipal waterworks, sanitary sewer and solid waste disposal system. The bonds carry an interest rate of 5.2656174% and mature on January 1, 2031. The interest and principal payments are to be made monthly.

Refunding, Series 2012 Bonds

On April 19, 2012, the City issued \$7,495,000 of utilities refunding revenue bonds for WMU to pay off the Series 2002 Bonds. The bonds were secured by a first pledge of a fixed portion of the gross revenues to be derived from the operation of the system, which fixed portion shall be sufficient to pay the principal and interest of the bonds. The 2002 bond issue financed the acquisition, construction and installation of major new municipal sanitary sewer (wastewater) facilities and paying and discharging the outstanding Utilities Revenue Bond Anticipation Note, Series 1997. The bonds carry interest rates of 2.0% to 3.75% and mature on July 1, 2021. The interest payments are to be made on July 1 and January 1 and the principal payments are to be made on July 1.

Series 2014 Bonds

On December 23, 2014, the City issued \$9,915,000 of utilities revenue bonds for WMU secured by a first and prior security interest in any and all right, title and interest of WMU in the portions of the Project (extensions and improvements of the System) that constitute personal property and in all additions, attachments, accessions, and substitutions thereto, and any proceeds therefrom. The 2014 bond issues financed the extensions and improvements to the combined and consolidated municipal waterworks, sanitary sewer and solid waste disposal system. The bonds carry an interest rate of 2% to 4% and mature on July 1, 2045. The interest payments are to be made on July 1 and January 1 and the principal payments are to be made on July 1.

Series 2018 Bonds

On January 2, 2018, the City issued \$13,045,000 of utilities revenue bonds for WMU secured by and payable solely from Pledged Receipts derived from the collection of rates, rental and charges for the services rendered by the City's (WMU) System. The Bonds are further secured by a statutory mortgage lien upon all properties of the System and extensions thereof and all extensions and appurtenances thereto. The 2018 bond issues financed the new water treatment plant. The bonds carry an interest rate of 3% to 4% and mature on July 1, 2042. The interest payments are to be made on July 1 and January 1 and the principal payments are to be made on July 1.

KIA – Strodes Creek Loan

On July 1, 2005, Winchester Municipal Utilities entered into an "Assistance Agreement" with the Kentucky Infrastructure Authority (KIA), to provide funds for the construction of a new wastewater treatment plant, \$21,000,000. This agreement calls for interest to be paid every six months starting December 1, 2005 at the rate of 1% of the outstanding balance. Principal payments are due to be paid every December 1 and June 1 starting after the wastewater treatment plant goes online. The online date for the plant was July, 2008. Principal payments were due to begin on June 1, 2009, and be due every December 1 and June 1 thereafter until maturity on December 1, 2028.

**WINCHESTER MUNICIPAL UTILITIES
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEARS ENDED JUNE 30, 2018 AND 2017**

NOTE 5 – LONG-TERM DEBT (CONTINUED)

KIA – Vaught Court Loan

On December 1, 2009, Winchester Municipal Utilities entered into an “Assistance Agreement” with the Kentucky Infrastructure Authority (KIA), to provide funds for construction of the Vaught Court Outfall Sewer Project, \$600,000 with a principal forgiveness of \$312,600 and a loan amount of \$287,400. This agreement calls for interest payments to commence within six months from the first draw of funds estimated to be June 1, 2010 with full principal and interest payments to commence within one year of initiation of operation estimated to be June 1, 2011. During the year ended June 30, 2010, \$312,600 of principal was forgiven and \$69,320 of the loan amount was drawn down. During the year ended June 30, 2011, \$218,080 was drawn down, and the project was completed. The loan carries a 2.00% interest rate, with principal and interest payments due on December 1 and June 1 every year until maturity on June 1, 2030. The loan is required to establish a replacement reserve account where \$1,500 is to be added to the account each December 1 until the balance reaches \$15,000 and is to be maintained for the life of the loan.

KIA – Industrial Elevated Storage Tank

On December 1, 2009, Winchester Municipal Utilities entered into an “Assistance Agreement” with the Kentucky Infrastructure Authority (KIA), to provide funds for construction of an Elevated Storage Tank Rehabilitation, \$741,450 with a principal forgiveness of \$401,124 and a loan amount of \$340,326. This agreement calls for interest payments to commence within six months from the first draw of funds estimated to be June 1, 2010 with full principal and interest payments to commence within one year of initiation of operation estimated to be June 1, 2011. During the year ended June 30, 2010, \$401,124 of principal was forgiven. During the year ended June 30, 2011, \$340,326 was drawn down, and the project was completed. The loan carries a 2.00% interest rate, with principal and interest payments due on December 1 and June 1 every year until maturity on December 1, 2030. The loan is required to establish a replacement reserve account where \$2,000 is to be added to the account each December 1 until the balance reaches \$20,000 and is to be maintained for the life of the loan.

KIA – Lower Howards Creek

On February 5, 2010, Winchester Municipal Utilities entered into an “Assistance Agreement” with the Kentucky Infrastructure Authority (KIA), to provide funds for the Lower Howards Creek Wastewater project, \$36,600,000. This agreement calls for interest payments to commence within six months from the first draw of funds with full principal and interest payments to commence within one year of initiation of operation, which was on February 12, 2013. During the year ended June 30, 2014, the final draw of \$999,996 of the loan was drawn down. The loan carries a 2.00% interest rate and matures in twenty years. The loan is required to establish a replacement reserve account where \$91,500 is to be added to the account each December 1 until the balance reaches \$915,000 and is to be maintained for the life of the loan.

The Kentucky Infrastructure Authority has made these loans inferior and subordinate to the security interest and source of payment for the Debt Obligations of Winchester Municipal Utilities payable from the revenues of the System outstanding at the time of the execution of the “Assistance Agreement”. The Agreement also further states that the Kentucky Infrastructure Authority must be notified no less than thirty days (30), in writing, prior to the issuance of any further debt obligations on parity with the current debt obligations.

**WINCHESTER MUNICIPAL UTILITIES
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEARS ENDED JUNE 30, 2018 AND 2017**

NOTE 5 – LONG-TERM DEBT (CONTINUED)

KIA – Bel-Air Sanitary

On October 1, 2012, Winchester Municipal Utilities entered into an “Assistance Agreement” with the Kentucky Infrastructure Authority (KIA), to provide funds for the Bel-Air and Westside pump station projects, \$1,000,000. This agreement calls for interest payments to commence within six months from the first draw of funds with full principal and interest payments to commence within one year of initiation of operation estimated to be December 1, 2013. During the year ended June 30, 2014, the final draw of \$59,095 was drawn on the loan. The loan carries a 2.00% interest rate and matures in twenty years. The loan is required to establish a replacement reserve account where \$2,500 is to be added to the account each December 1 until the balance reaches \$25,000 and is to be maintained for the life of the loan.

KIA – Hampton Manor

On March 1, 2017, City of Winchester and Winchester Municipal Utilities entered into an “Assistance Agreement” with the Kentucky Infrastructure Authority (KIA), to provide funds for the Hampton Manor project which replaces and improves 3200 linear feet of aged sanitary sewer collection pipe along with associated manholes, connections and appurtenances, totaling \$1,249,088. This agreement calls for interest payments to commence within six months from the first draw of funds with full principal and interest payments to commence within one year of initiation of operation estimated to be June 1, 2017. The loan carries a 1.75% interest rate and matures June 1, 2037. The loan is required to establish a replacement reserve account where \$3,500 is to be added to the account each December 1 until the balance reaches \$70,000 and is to be maintained for the life of the loan.

Long-Term Debt consists of bonds and other indebtedness for which the changes in the years ended June 30, 2018 and 2017 are as follows:

06/30/18 Description	Beginning	Borrowings Additions	Repayments Reductions	2018 Ending	Current
Compensated Absences	\$ 524,097	\$ 8,608	\$ 0	\$ 532,705	\$ 0
Bonds	22,041,519	13,045,000	891,015	34,195,504	941,251
KIA-Strodes Creek	12,586,703	0	1,038,087	11,548,616	1,048,495
KIA-Lower Howards	30,396,804	0	1,629,529	28,767,275	1,662,956
KIA-Bel-Air	446,180	0	23,919	422,261	24,401
KIA-Storage Tank	244,191	0	15,925	228,266	16,246
KIA-Vaught Court	199,525	0	13,583	185,942	13,856
KIA-Hampton Manor	0	1,249,088	0	1,249,088	52,661
Total Long-Term Debt	<u>\$ 66,439,019</u>	<u>\$ 14,302,696</u>	<u>\$ 3,612,058</u>	<u>\$ 77,129,657</u>	<u>\$ 3,759,866</u>

06/30/17 Description	Beginning	Borrowings Additions	Repayments Reductions	2017 Ending	Current
Compensated Absences	\$ 477,509	\$ 46,588	\$ 0	\$ 524,097	\$ 0
Bonds	22,908,886	0	867,367	22,041,519	916,251
KIA-Strodes Creek	13,614,487	0	1,027,784	12,586,703	1,038,088
KIA-Lower Howards	31,994,224	0	1,597,420	30,396,804	1,630,202
KIA-Bel-Air	469,627	0	23,447	446,180	23,920
KIA-Storage Tank	259,802	0	15,611	244,191	15,249
KIA-Vaught Court	212,840	0	13,315	199,525	13,583
Total Long-Term Debt	<u>\$ 69,937,375</u>	<u>\$ 46,588</u>	<u>\$ 3,544,944</u>	<u>\$ 66,439,019</u>	<u>\$ 3,637,293</u>

**WINCHESTER MUNICIPAL UTILITIES
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEARS ENDED JUNE 30, 2018 AND 2017**

NOTE 6 – COMPLIANCE WITH COVENANTS

The bonds and KIA loan requires WMU to establish and maintain certain reserves and restricted assets as follows:

Bond Debt Service - Bonds

In the previous year, monthly deposits equal to one-sixth of the next interest payment and one-twelfth of the next principal payment shall be set aside monthly so as to accumulate in the Bond Fund in order to pay interest and principal on the bonds. In addition, the Bond Ordinance requires that a specific amount be maintained in the Debt Service Reserve Account defined as the "Reserve Amount." The account is to be reviewed each year and funded based on the least of three factors: 1) maximum annual principal and interest requirement, 2) 125% of the average annual principal and interest requirement or 3) 10% of the outstanding loan proceeds. The first factor was applicable for June 30, 2017, and required a balance of \$1,048,175.

In the new 2018 Bond Series covenant, WMU entered into an Insurance Agreement with Build America Mutual Assurance Company which guarantees the scheduled payments. The effect of the Insurance Agreement eliminates the bond debt service requirement.

Depreciation Reserve – Bonds and KIA Loan

The Winchester Municipal Utilities is required to transfer 12% of annual gross revenues or \$42,000, whichever is greater, in equal monthly installments to the Depreciation Fund. These funds are to be used for renewals, replacements and/or additions to property, plant and equipment.

Interest Coverage Ratio – Bonds and KIA Loan

On April 3, 2012, a new general bond ordinance was adopted that requires Winchester Municipal Utilities to maintain an interest coverage ratio of 1.2 times - annual debt service requirements for bonds and 1.0 times - annual debt service requirements for bonds and KIA loans. Other changes in coverage ratio are noted below in calculation of ratios as shown. The City of Winchester is required by bond ordinance to adjust rates as necessary to maintain such minimum coverage. Computed as follows:

Bonds:

	2018	2017
Income Available for Debt Service	\$ 998,374	\$ 3,125,344
Add: Depreciation	5,071,619	4,803,979
Cash Available for Bond Debt Service	<u>\$ 6,069,993</u>	<u>\$ 7,292,323</u>
Annual Debt Service on Bonds	<u>1,770,456</u>	<u>1,760,673</u>
Coverage Ratio	<u>3.43</u>	<u>4.14</u>

KIA:

	2018	2017
Income Available for Debt Service	\$ 998,374	\$ 3,125,344
Add: Depreciation	5,071,619	4,803,979
Cash Available for Debt Service	<u>\$ 6,069,993</u>	<u>\$ 7,292,323</u>
Annual Debt Service on all Debt	<u>5,244,743</u>	<u>5,222,354</u>
Coverage Ratio	<u>1.16</u>	<u>1.40</u>

Winchester Municipal Utilities is in compliance with all of the covenants of the bond ordinance and KIA loan agreement as of June 30, 2018 and 2017.

**WINCHESTER MUNICIPAL UTILITIES
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEARS ENDED JUNE 30, 2018 AND 2017**

NOTE 7 – COUNTY EMPLOYEE RETIREMENT SYSTEM (CERS)

General information about the County Employees Retirement System Non-Hazardous (“CERS”)

Plan Description

Employees whose positions do not require a degree beyond a high school diploma are covered by the CERS, a cost-sharing multiple-employer defined benefit pension plan administered by the Kentucky Retirement System, an agency of the Commonwealth of Kentucky. Under the provisions of the Kentucky Revised Statute (“KRS”) Section 61.645, the Board of Trustees of the Kentucky Retirement System administers CERS and the General Assembly has the authority to establish and amend benefit provisions. The Kentucky Retirement System issues a publicly available financial report that includes financial statements and required supplementary information for CERS. That report may be obtained from <http://kyret.ky.gov/>.

Benefits provided

CERS provides retirement, health insurance, death and disability benefits to Plan employees and beneficiaries. Employees are vested in the plan after five years’ service. For retirement purposes, employees are grouped into three tiers, based on hire date:

Tier 1	Participation date	Before September 1, 2008
	Unreduced retirement	27 years service or 65 years old
	Reduced retirement	At least 5 years service and 55 years old At least 25 years service and any age
Tier 2	Participation date	September 1, 2008 - December 31, 2013
	Unreduced retirement	At least 5 years service and 65 years old Or age 57+ and sum of service years plus age equal 87
	Reduced retirement	At least 10 years service and 60 years old
Tier 3	Participation date	After December 31, 2013
	Unreduced retirement	At least 5 years service and 65 years old Or age 57+ and sum of service years plus age equal 87
	Reduced retirement	Not available

Cost of living adjustments are provided at the discretion of the General Assembly. Beginning in 2015, COLAs were suspended until the retirement funds reach 100% funded status.

Retirement benefits are calculated using factors for the number of years’ service multiplied by the “final compensation.” Reduced benefits are based on factors of both of these components. Again, the definitions of “final compensation” and the benefit factor for years’ of service depend on the Tier in which the member participates. Benefits in Tier 3, the cash balance plan, are limited to the accumulated contributions and earnings credited to the member’s account, similar to a defined contribution plan.

**WINCHESTER MUNICIPAL UTILITIES
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEARS ENDED JUNE 30, 2018 AND 2017**

NOTE 7 – COUNTY EMPLOYEE RETIREMENT SYSTEM (CERS) – (CONTINUED)

Benefits provided (Cont'd)

There are, however, minimum rates of return that are guaranteed and funded with employer contributions when actual earnings are less than these minimum rates.

Tier 1	Final Compensation	Average of the highest 5 fiscal years
	Benefit Factor	2.2% prior to 8/1/2004 or 2% after 8/1/2004
	Interest on member accounts	2%
Tier 2	Final Compensation	5 complete fiscal years preceding retirement
	Benefit Factor	Scale of 1.1% to 2% based on number of years of service
	Interest on member accounts	2.50%
Tier 3	Final Compensation	N/A
	Benefit Factor	N/A
	Interest on member accounts	4% plus 75% of the 5 year geometric average earnings in excess of 4%
	Employer Pay Credit	4% of creditable compensation

The 2018 General Assembly enacted several changes to the CERS non-hazardous plan, including the deletion of a guaranteed return for the hybrid cash plan. Interest on member accounts will be determined using 85% of the ten-year geometric average earnings of the CERS non-hazardous plan. However, as of June 30, 2018 these legislative changes have been challenged by the Kentucky Attorney General and other stakeholders. Final determination of the plan revisions is subject to rulings by the Court and additional legislative actions by the General Assembly.

Death benefits are provided for both death after retirement and death prior to retirement. Death benefits after retirement are provided in a \$5,000 lump sum payment. The \$5,000 death benefit was also deleted in the 2018 changes to benefits.

- Death benefits before retirement are based on the member's eligibility for normal or early retirement at the time of death, or five years of service if the member is under the age of 55, or 144 months of service if the member is no longer working for a participating agency.

**WINCHESTER MUNICIPAL UTILITIES
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEARS ENDED JUNE 30, 2018 AND 2017**

NOTE 7 – COUNTY EMPLOYEE RETIREMENT SYSTEM (CERS) – (CONTINUED)

Benefits provided (Cont'd)

- If beneficiaries are eligible for benefits, they may choose a lifetime monthly benefit or a lump sum payment for an actuarial refund, or annuities for 5 or 10 years of monthly payments.
- If the beneficiary is not eligible for monthly benefits, a lump sum payment of the member's contributions and accumulated interest will be paid. Beneficiaries of Tier 3 members will also include the employer pay credit if the member has at least 5 years of service at the time of death.
- If the member dies as a result of a duty-related death, the decedent's beneficiary will receive the higher of the normal death benefit or \$10,000 plus 25% of the decedent's monthly final rate of pay and any dependent child will receive 10% of the decedent's monthly final rate of pay up to 40% for all dependent children.
- Dependent children also receive benefits for duty-related deaths as a monthly benefit equal to 10% of the member's monthly final rate of pay. But, dependent children benefits cannot total more than 40% of the monthly final rate of pay.

Contributions

Required contributions by the employee are based on the tier:

	<u>Required contribution</u>
Tier 1	5%
Tier 2	5% + 1% for insurance
Tier 3	5% + 1% for insurance

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

At June 30, 2018, WMU reported a liability for its proportionate share of the net pension liability for CERS. The amount recognized by WMU as its proportionate share of the net pension liability, the related Commonwealth support, and the total portion of the net pension liability that was associated with WMU was as follows:

WMU 's proportionate share of the net pension liability	\$	7,097,486
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The net pension liability for each plan 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, 2017. The total pension liability was rolled-forward from the valuation date to the plan's fiscal year end, June 30, 2017, using generally accepted actuarial principles. WMU's proportion of the net pension liability for CERS was based on the actual liability of the employees and former employees relative to the total liability of the System as determined by the actuary. At June 30, 2017 the District's proportion was .121256%. For the year ended June 30, 2018, the District recognized pension expense of \$985,752.

**WINCHESTER MUNICIPAL UTILITIES
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEARS ENDED JUNE 30, 2018 AND 2017**

NOTE 7 – COUNTY EMPLOYEE RETIREMENT SYSTEM (CERS) – (CONTINUED)

At June 30, 2018, WMU 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
Differences between expected and actual experience	\$ 8,803	\$ 180,165
Changes of assumptions	1,309,679	-
Net difference between projected and actual earnings on pension plan investments	562,112	474,325
Changes in proportion and differences between WMU's contributions and proportionate share of contributions	47,626	12,538
Contributions subsequent to the measurement date	447,900	-
Total	<u>\$ 2,376,120</u>	<u>\$ 667,028</u>

\$447,900 reported as deferred outflows of resources related to pensions resulting from WMU contributions subsequent to the measurement date will be recognized as a reduction of the net pension liability in the year ended June 30, 2019. Other amounts reported as deferred outflows of resources related to pensions will be recognized in pension expense as follows:

<u>Year ended June 30:</u>	
2019	\$ 580,160
2020	\$ 536,581
2021	\$ 235,586
2022	\$ (91,136)

Actuarial assumptions

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

	<u>CERS</u>
Inflation	2.3%
Projected salary increases	3.3% -11.55% (varies by service)
Investment rate of return, net of investment expense & inflation	6.25%

**WINCHESTER MUNICIPAL UTILITIES
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEARS ENDED JUNE 30, 2018 AND 2017**

NOTE 7 – COUNTY EMPLOYEE RETIREMENT SYSTEM (CERS) – (CONTINUED)

Actuarial assumptions (Cont'd)

For CERS, 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 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. At the time of the last experience study, performed as of June 30, 2013, this mortality assumption provided 37% and 19% margin for future improvement for males and females, respectively. This will be reviewed again when the next experience investigation is conducted.

Several factors are considered in evaluating the long-term rate of return assumption including 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.

In May 2017, the Kentucky Retirement Systems Board of Trustees adopted a new asset allocation policy based on recommendations from the investment professionals serving as trustees on the Board, the actuarial valuation used a long-term expected rate of return 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 rates 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, as provided by CERS' investment trustees, are summarized in the following table:

Asset Class	Target Allocation	Long-Term Expected Real Rate of Return
U.S. Equity	17.5%	5.97%
International Equity	17.5%	7.85%
Global Bonds	4.0%	2.63%
Global Credit	2.0%	3.63%
High Yield	7.0%	5.75%
Emerging Market Debt	5.0%	5.50%
Private Credit	10.0%	8.75%
Real Estate	5.0%	7.63%
Absolute Return	10.0%	5.63%
Real Return	10.0%	6.13%
Private Equity	10.0%	8.25%
Cash	2.0%	1.88%
Total	100.0%	

Discount rate

For CERS, the discount rate used to measure the total pension liability was 6.25%. The projection of cash flows used to determine the discount rate assumed that contributions from plan employees and employers will be made at statutory contribution rates. Projected inflows from investment earnings were calculated using the long-term assumed investment return of 6.25%. The long-term investment rate of return was applied to all periods of projected benefit payments to determine the total pension liability.

**WINCHESTER MUNICIPAL UTILITIES
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEARS ENDED JUNE 30, 2018 AND 2017**

NOTE 7 – COUNTY EMPLOYEE RETIREMENT SYSTEM (CERS) – (CONTINUED)

Sensitivity of CERS proportionate share of net pension liability to changes in the discount rate—
The following table presents the net pension liability of WMU, calculated using the discount rates selected by each pension system, as well as what WMU net pension liability would be if it were calculated using a discount rate that is 1-percentage-point lower or 1-percentage-point higher than the current rate:

	1% Decrease	Current Discount Rate	1% Increase
CERS	5.25%	6.25%	7.25%
WMU's proportionate share of net pension liability:			
Non-Hazardous	\$ 8,951,465	\$ 7,097,486	\$ 5,546,648

Pension plan fiduciary net position

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

Other Pension Plans

WMU offers employees the option to participate in a defined contribution plan under Section 403(B) and 401(K) of the Internal Revenue Code. All regular full time and part time employees are eligible to participate and may contribute up to the maximum amount allowable by law.

Also, WMU offers its employees a deferred compensation plan created in accordance with Internal Revenue Code Section 457. The plan, available to all employees, permits them to defer a portion of their salary until future years. This deferred compensation is not available to employees until their termination, retirement, death or unforeseeable emergency.

GASB Statement No. 32, Accounting and Financial Reporting for Internal Revenue Code Section 457 Deferred Compensation Plans, allows entities with little or no administrative involvement and who do not perform the investing function for these plans to omit plan assets and related liabilities from their financial statements. WMU, therefore, does not report these assets and liabilities on its financial statements.

Employee contributions made to the 401k and 457 plans as of June 30, 2018 and 2017 were \$48,763 and \$38,569, respectively. WMU does not contribute to these plans.

NOTE 8 – OTHER POSTEMPLOYMENT BENEFIT PLANS (OPEB)

WMU's employees are provided with a OPEB plan. Retired District employees receive some health care benefits depending on their length of service. In accordance with Kentucky Revised Statutes, these benefits are provided and advance funded on an actuarially determined basis through the CERS plan. The Kentucky Retirement System's publicly available financial report may be obtained from <http://kyret.ky.gov/>.

**WINCHESTER MUNICIPAL UTILITIES
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEARS ENDED JUNE 30, 2018 AND 2017**

NOTE 8 – OTHER POSTEMPLOYMENT BENEFIT PLANS (OPEB) (Cont'd)

CERS Other Postemployment Benefits

Plan Description—CERS health insurance benefits are also subject to various participation dates to determine eligibility and health insurance contribution rates. For employees who initiated participation in the CERS system prior to July 1, 2003, KRS pays a percentage of the monthly contribution rate for insurance covered based on the retired member's years of service and type of service. Non-hazardous members receive a contribution subsidy for only the member's health insurance premium. Hazardous members receive a contribution subsidy for both the member and dependent coverage.

Benefits Provided—Percentage of premium subsidies ranges from 0% for less than 4 years of service to 100% for 20 years or more of service. For members who initiated participation in the CERS system after July 1, 2003 until August 31, 2008, members must have 120 months of service in a state-administered retirement system to qualify for participation in the KRS health plans.

Members who began participating with KRS on or after September 1, 2008, must have 180 months of service upon retirement to participate in the KRS health plans. Non-hazardous retirees receive \$10 toward the monthly premium for each full year of service.

Hazardous retirees receive \$15 toward the monthly premium and the hazardous retiree's spouse may also receive this contribution upon the retiree's death. The monthly insurance benefit has been increased annually by a Cost of Living Adjustment (COLA) since July 2004.

Contributions—CERS allocates a portion of the employer contributions to the health insurance benefit plans. For the 2017 measurement period, CERS allocated 4.70% of the 19.18% actuarially required contribution rate paid by employers for funding the healthcare benefit. In addition, 1% of the Tier 2 and employee contributions of 6% are allocated to the health insurance plan.

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

At June 30, 2018, WMU reported a liability of \$2,437,660 for its proportionate share of the collective net OPEB liability. The collective net OPEB liability was measured as of June 30, 2017, and the total OPEB liability used to calculate the collective net OPEB liability was based on a projection of WMU's long-term share of contributions to the OPEB plan relative to the projected contributions of all participating employers, actuarially determined. At June 30, 2017, the District's proportion was 0.121256%.

The amount recognized by WMU as its proportionate share of the OPEB liability was \$2,437,660 as of June 30, 2018, and \$1,772,384 as of June 30, 2017. The recognition of WMU's liability as of June 30, 2017 is reflected as a change in accounting principle in the Statement of Activities and Note 19—Change in Accounting Principle and Related Changes to Certain Beginning Balances.

**WINCHESTER MUNICIPAL UTILITIES
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEARS ENDED JUNE 30, 2018 AND 2017**

NOTE 8 – OTHER POSTEMPLOYMENT BENEFIT PLANS (OPEB) (Cont'd)

CERS Other Postemployment Benefits (Cont'd)

For the year ended June 30, 2018, WMU recognized OPEB expense of \$117,103. At June 30, 2018, WMU reported deferred outflows of resources and deferred inflows of resources related to OPEBs from the following sources:

	<u>Deferred Outflows of Resources</u>	<u>Deferred Inflows of Resources</u>
Differences between expected and actual experience	\$ 0	\$ 6,770
Changes of assumptions	530,420	0
Net difference between projected and actual earnings on OPEB plan investments	0	115,203
Changes in proportion and differences between District contributions and proportionate share of contributions	0	5,656
District contributions subsequent to the measurement date	<u>145,382</u>	<u>0</u>
	<u>\$ 675,802</u>	<u>\$ 127,629</u>

Of the total amount reported as deferred outflows of resources related to OPEB, \$145,382 resulting from WMU contributions subsequent to the measurement date and before the end of the fiscal year will be included as a reduction of the collective net OPEB liability in the year ended June 30, 2019. Other amounts reported as deferred outflows of resources and deferred inflows of resources related to OPEB will be recognized in WMU's OPEB expense as follows:

Year ended June 30:

2019	\$69,304
2020	\$69,304
2021	\$69,304
2022	\$69,304
2023	\$98,105
Thereafter	\$27,471

Actuarial assumptions – The total OPEB liability in the June 30, 2017 actuarial valuation was determined using the following actuarial assumptions, applied to all periods included in the measurement:

Investment rate of return	6.25%, net of OPEB plan investment expense, including inflation.
Projected salary increases	4% average
Inflation rate	3.25%

**WINCHESTER MUNICIPAL UTILITIES
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEARS ENDED JUNE 30, 2018 AND 2017**

NOTE 8 – OTHER POSTEMPLOYMENT BENEFIT PLANS (OPEB) (Cont'd)

CERS Other Postemployment Benefits (Cont'd)

Healthcare cost trend rates	
Under 65	Initial trend starting at 7.50% and gradually decreasing to an ultimate trend rate of 5.00% over a period of 5 years
Ages 65 and Older	Initial trend starting at 5.50% and gradually decreasing to an ultimate trend rate of 5.00% over a period of 2 years
Municipal Bond Index Rate	3.56%
Discount Rate	5.84%

Mortality rates were based on the RP-2000 Combined Mortality Table updated with Scale BB from the year 2000 to the year 2013. Pre-retirement mortality male mortality rates are multiplied by 50% and female mortality rates are multiplied by 30%. Post-retirement mortality rates for females are set back one year. The RP-2000 Disabled Mortality Table is used for post-retirement mortality using the Scale BB projected to 2025. Male mortality rates are set back four years.

The remaining actuarial assumptions (e.g. initial per capita costs, health care cost trends, rate of plan participation, rates of plan election, etc.) used in the June 30, 2017 valuation were based on a review of recent plan experience done concurrently with the June 30, 2013 valuation. The investment return, price inflation, and payroll growth assumption were adopted by the Board in May and July 2017 for use with the June 30, 2017 valuation in order to reflect future economic expectations.

The long-term expected rate of return on OPEB plan investments was determined 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 rate of return for each major class are summarized in the table below.

**WINCHESTER MUNICIPAL UTILITIES
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEARS ENDED JUNE 30, 2018 AND 2017**

NOTE 8 – OTHER POSTEMPLOYMENT BENEFIT PLANS (OPEB) (Cont'd)

CERS Other Postemployment Benefits (Cont'd)

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 Yield Credit	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%	6.56%

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

Discount rate – The single discount rate of 5.84% for CERS-Nonhazardous was used to measure the total OPEB liability as of June 30, 2017. The Single discount rate is based on the expected rate of return on OPEB plan investments of 6.25% and a municipal bond rate of 3.56%, as reported in Fidelity Index's "20-Year Municipal GO AA Index" as of June 30, 2017. Future contributions are projected in accordance with the current funding policy mandated in Ky Revised Statutes 61.565, as amended, which includes the requirement that each participating employer in the System contribute the actuarially determined contribution rate, which is determined using a closed funding period (26 years as of June 30, 2017) and the actuarial assumptions and methods adopted by the Board of Trustees. Current assets, future contributions, and investment earnings are projected to be sufficient to pay the projected benefit payments from the retirement system. However, the cost associated with the implicit employer subsidy is not currently included in the calculation of the System's actuarial determined contributions, but any cost associated with the implicit subsidy is not paid out of the System's trust. Therefore, the municipal bond rate was applied to future expected benefit payments associated with the implicit subsidy.

The following table presents WMU's proportionate share of the collective net OPEB liability of the System, calculated using the discount rate of 5.84%, as well as what the District's proportionate share of the collective net OPEB liability would be if it were calculated using a discount rate that is 1-percentage-point lower (4.84%) or 1-percentage-point higher (6.84%) than the current rate:

**WINCHESTER MUNICIPAL UTILITIES
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEARS ENDED JUNE 30, 2018 AND 2017**

NOTE 8 – OTHER POSTEMPLOYMENT BENEFIT PLANS (OPEB) (Cont'd)

CERS Other Postemployment Benefits (Cont'd)

	<u>1% Decrease</u>		<u>Current Discount Rate</u>		<u>1% Increase</u>
	4.84%		5.84%		6.84%
WMU's proportionate share of net OPEB liability	\$ 3,101,788	\$	2,437,660	\$	1,885,002

Sensitivity of the District's proportionate share of the collective net OPEB liability to changes in the healthcare cost trend rates – The following presents the District's proportionate share of the collective net OPEB liability, as well as what the District's proportionate share of the collective net OPEB liability would be if it were calculated using healthcare cost trend rates that were 1-percentage-point lower or 1-percentage-point higher than the current healthcare cost trend rates:

	<u>1% Decrease</u>		<u>Current Health Care Trend Rate</u>		<u>1% Increase</u>
	6.5%		7.5%		8.5%
	decreasing to 4%		decreasing to 5%		decreasing to 6%
WMU's proportionate share of net OPEB liability	\$ 1,869,811	\$	2,437,660	\$	3,175,831

OPEB plan fiduciary net position – Detailed information about the OPEB plan's fiduciary net position is available in the separately issued KRS financial report.

NOTE 9 – ECONOMIC DEPENDENCY

WMU is economically dependent on the following four or five entities which account for 13% and 19%, respectively, of water and wastewater revenues for the following years:

<u>Name</u>	<u>2018</u>	<u>2017</u>
Alltech	\$ 0	\$ 1,073,876
The Kroger Company	710,587	729,864
Sekisui	381,444	475,618
East Clark County WD	295,439	293,031
Catalent	248,171	254,133
	<u>\$ 1,635,641</u>	<u>\$ 2,826,522</u>

NOTE 10 – RISK OF LOSS

WMU is exposed to various risks of loss related to torts; theft of, damage to and destruction of assets; errors and omissions; injuries to employees and natural disasters. WMU carries commercial insurance for the risks of loss, including worker's compensation, and property and casualty loss insurance.

**WINCHESTER MUNICIPAL UTILITIES
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEARS ENDED JUNE 30, 2018 AND 2017**

NOTE 11 – LANDFILL POST-CLOSURE COSTS

In 1992, WMU discontinued its landfill operations and ceased accepting solid waste. Under 401 KAR 47:080, WMU presented a closure plan. The final cap, leachate collection systems, surface water drainage systems, gas vent systems and groundwater monitoring systems have been constructed. On June 4, 1998, the Clark County Fiscal Court entered into a lease agreement with WMU for the rental of county property upon which the County and WMU formerly operated landfills, the term of the lease was for 20 years at \$1 per year. The lease provides provision for the post-closure monitoring requirements of state and federal law to be provided by WMU. The post-closure costs are allocated 30% WMU and 70% Clark County Fiscal Court. The state and federal monitoring and maintenance regulations must be performed at the site for 30 years after closure. A liability was not recorded on WMU's general ledger in the year of closure; instead the actual post-closure expenses have been recorded in operations each year.

On October 16, 2008, WMU received notice from the Kentucky Division of Waste Management that the site had been released from groundwater monitoring. In applying GASB 18, WMU believes these costs were the most significant of the post-closure expenses. The effect of any remaining projected costs will be offset by the lease agreement with Clark County.

The Division of Waste Management has finished construction of a new wetlands treatment system for treating the landfill leachate at the WMU and Clark County Landfills. With construction of this treatment facility a new Kentucky Pollution Discharge Elimination System (KPDES) Permit was required. Laboratory testing/Monitoring required as part of the conditions of this permit were unexpectedly more stringent than the previous permit resulting in a higher monthly cost for operation.

NOTE 12 – UTILITY REVENUES PLEDGED

WMU has pledged future revenues from water, wastewater and solid waste to repay the 2011, 2012, 2014 and 218 bonds and KIA outstanding debt referenced in Note 5. Proceeds from these debt obligations provided financing of the water and wastewater infrastructure, including a new wastewater treatment plant. The debt obligations will be repaid from the previously mentioned utility revenues through the year 2045.

NOTE 13 – FIVE YEAR CAPITAL CONSTRUCTION PLAN

Winchester Municipal Utilities' five-year capital plan includes major capital construction of new wastewater treatment plant, pump station and force mains which are projected to be funded as follows:

Water Utility Improvements	\$ 20,935,480
Wastewater Utility Improvements	17,952,000
Total projected financing requirement	\$ <u>38,887,480</u>

**WINCHESTER MUNICIPAL UTILITIES
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEARS ENDED JUNE 30, 2018 AND 2017**

NOTE 13 – FIVE YEAR CAPITAL CONSTRUCTION PLAN (Cont'd)

Winchester Municipal Utilities' five-year capital plan of depreciation funded projects consists of the following annual allocations in addition to other specifically identified projects:

Finance and Administration:	
Copiers	\$ 5,000
Upgrade Local Area Network	7,000
Replace Microcomputers	6,000
Resurface Front Office Parking Lot	20,000
Engineering	
Purchase Printer/Scanner	12,000
Field Operation Vehicles	330,000
Solid Waste Collection:	
Cubit Replacement	25,000
Container Replacement	50,000
Replace Compactor Ejector Box	10,000
Purchase Compactor Power Unit	50,000
Precrusher Compactor Power Unit	50,000
Solid Waste Recycling	1,000
Water Treatment Plant Equipment Improvements	50,000
Water System Improvements	50,000
Water Distribution:	
Main Replacement	100,000
Fire Hydrant Replacement	12,000
Gate Value Replacement	10,000
Elevated Storage Tank Rehabilitation	100,000
Meter Change-Out/AMR Equipment	230,000
New Meter Services	30,000
Purchase Backhoe	16,000
Meter Reading Handheld Unit	12,500
Wastewater Collection:	
Main Replacement Program	100,000
I&I Rehabilitation	20,000
Rehabilitation of Private Sewers	20,000
Flow Meters	10,000
System Capacity Assurance Program	18,000
Routine Hydraulic Cleaning	60,000
Sewer Inspection Camera & Equipment	40,000
Wastewater Treatment Plant (SC):	
Replacement of Laboratory Equipment	2,000
WWTP Equipment Improvements	407,000
Solids Processing Improvements	297,000
Concrete Road Repairs	28,000
Wastewater Treatment Plant (LHC)	40,000
Wastewater Solids Processing (LHC)	15,000
Total Annual Allocations for Infrastructure Investment	<u>\$ 2,233,500</u>

All annual allocation programs are funded in each year of the five-year capital plan.

**WINCHESTER MUNICIPAL UTILITIES
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEARS ENDED JUNE 30, 2018 AND 2017**

NOTE 14 – COMMITMENTS

On December 7, 2017, WMU approved a contract with Judy Construction Company in the amount of \$19,982,300 for the construction of the new water treatment plant. The project is being primarily financing with the sale of Bonds sold in the current year.

NOTE 15 – SUBSEQUENT EVENTS

WMU has evaluated all subsequent events through November 9 2018, the date the financial statements were available to be issued.

NOTE 16 – CHANGE IN ACCOUNTING PRINCIPLE AND RELATED CHANGES TO CERTAIN BEGINNING BALANCES

Effective July 1, 2017, WMU was required to adopt Governmental Accounting Standards Board (GASB) Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions* (GASB 75). GASB 75 revised employer accounting and reporting for other postemployment benefits (OPEB) and implement requirements similar to the provisions of GASBS No. 68 and No. 73 for pension benefits. GASB 75 requires governments providing defined benefit OPEB to recognize their long-term obligation for OPEB benefits as a liability to more comprehensively and comparably measure the annual costs of OPEB benefits. Cost-sharing governmental employers, such as WMU, are required to report a net OPEB liability, OPEB expense and OPEB-related assets and liabilities based on their proportionate share of the collective amounts for all governments in the plan.

GASB 75 required retrospective application. The adjustment resulted in a \$1,772,384 reduction in net position as shown on the Statement of Activities and in the following table:

CERS Net OPEB Liability at 6/30/17	(\$1,912,028)
CER OPEB Deferred Outflows at 6/30/17	<u>139,644</u>
Total Restatement of Net Position	<u><u>(\$1,772,384)</u></u>

WINCHESTER MUNICIPAL UTILITY
REQUIRED SUPPLEMENTARY INFORMATION

WINCHESTER MUNICIPAL UTILITIES
REQUIRED SUPPLEMENTARY INFORMATION
SCHEDULE OF PROPORTIONATE SHARE OF NET PENSION LIABILITY
FOR THE YEAR ENDED JUNE 30, 2018

	Reporting Fiscal Year (Measurement Date) 2018 (2017)	Reporting Fiscal Year (Measurement Date) 2017 (2016)	Reporting Fiscal Year (Measurement Date) 2016 (2015)	Reporting Fiscal Year (Measurement Date) 2015 (2014)
COUNTY EMPLOYEES RETIREMENT SYSTEM:				
WMU's proportion of the net pension liability	0.121256%	0.121853%	0.120770%	0.114924%
WMU's proportionate share of the net pension liability	\$ 7,097,486	\$ 5,999,576	\$ 5,192,479	\$ 3,728,580
WMU's covered-employee payroll	\$ 2,881,394	\$ 2,960,432	\$ 2,905,451	\$ 2,837,568
WMU's proportionate share of the net pension liability as a percentage of its covered-employee payroll	246.32%	202.66%	178.72%	131.40%
Plan fiduciary net position as a percentage of the total pension liability	53.30%	55.50%	59.97%	66.80%

Note: Schedule is intended to show information for the last 10 fiscal years. Additional years will be displayed as they become available.

**WINCHESTER MUNICIPAL UTILITIES
REQUIRED SUPPLEMENTARY INFORMATION
SCHEDULE OF CONTRIBUTIONS - PENSION
FOR THE YEAR ENDED JUNE 30, 2018**

	2017	2016	2015	2014
COUNTY EMPLOYEES RETIREMENT SYSTEM:				
Contractually required contribution	\$ 411,845	\$ 346,191	\$ 360,574	\$ 498,044
Contributions in relation to the contractually required contribution	<u>411,845</u>	<u>346,191</u>	<u>360,574</u>	<u>498,044</u>
Contribution deficiency (excess)	-	-	-	-
WMU's covered-employee payroll	\$ 2,881,394	\$ 2,960,432	\$ 2,905,451	\$ 2,837,568
WMU's contributions as a percentage of its covered-employee payroll	14.29%	11.69%	12.41%	17.55%

Note: Schedule is intended to show information for the last 10 fiscal years. Additional years will be displayed as they become available.

Note: These amounts are based on the prior year's measurement period, not WMU's fiscal year.

**WINCHESTER MUNICIPAL UTILITIES
NOTES TO REQUIRED SUPPLEMENTARY INFORMATION - PENSION
FOR THE YEAR ENDED JUNE 30, 2018**

COUNTY EMPLOYEES RETIREMENT SYSTEM:

Changes of Benefit Terms -

2014: A cash balance plan was introduced for member whose participation date is on or after January 1, 2014

Changes of Assumptions -

Investment rate of return was lowered from 7.5% to 6.25%

Salary increases were revised from an average of 4% to a range of 3.3% - 11.55%

Inflation was lowered from 3.25% to 2.3%

**WINCHESTER MUNICIPAL UTILITIES
REQUIRED SUPPLEMENTARY INFORMATION
SCHEDULE OF PROPORTIONATE SHARE OF NET OPEB LIABILITY
FOR THE YEAR ENDED JUNE 30, 2018**

	Reporting Fiscal Year (Measurement Date)
	2018 (2017)
COUNTY EMPLOYEES RETIREMENT SYSTEM:	
WMU's proportion of the net OPEB liability	0.121256%
WMU's proportionate share of the net OPEB liability	\$ 2,437,660
WMU's covered-employee payroll	\$ 2,881,394
WMU's proportionate share of the net OPEB liability as a percentage of its covered-employee payroll	84.60%
Plan fiduciary net position as a percentage of the total OPEB liability	52.40%

Note: Schedule is intended to show information for the last 10 fiscal years. Additional years be displayed as they become available.

**WINCHESTER MUNICIPAL UTILITIES
REQUIRED SUPPLEMENTARY INFORMATION
SCHEDULE OF CONTRIBUTIONS - OPEB
FOR THE YEAR ENDED JUNE 30, 2018**

	<u>2017</u>
COUNTY EMPLOYEES RETIREMENT SYSTEM:	
Contractually required contribution	\$ 139,644
Contributions in relation to the contractually required contribution	<u>139,644</u>
Contribution deficiency (excess)	-
District's covered-employee payroll	\$ 2,881,394
District's contributions as a percentage of its covered-employee payroll	4.85%

Note: Schedule is intended to show information for the last 10 fiscal years.
be displayed as they become available.

Note: These amounts are based on the prior year's measurement period, not the
District's fiscal year.

**WINCHESTER MUNICIPAL UTILITIES
NOTES TO REQUIRED SUPPLEMENTARY INFORMATION - OPEB
FOR THE YEAR ENDED JUNE 30, 2018**

COUNTY EMPLOYEES RETIREMENT SYSTEM:

Valuation Date: June 30, 2017

WINCHESTER MUNICIPAL UTILITY
SUPPLEMENTAL SCHEDULES

WINCHESTER MUNICIPAL UTILITIES
SCHEDULE I - DEPARTMENT EXPENSES
FOR THE YEARS ENDED JUNE 30, 2018 AND 2017

	<u>2018</u>	<u>2017</u>
ADMINISTRATIVE		
Salaries	\$ 981,389	\$ 989,558
Employee Benefits	817,211	625,201
Repairs and Maintenance	138,680	111,199
Supplies	21,464	20,974
Small Tools	3,113	4,985
Utilities and Telephone	34,506	38,983
Property Insurance	44,818	45,727
Other	93,964	87,393
Postage and Freight	59,308	69,320
Bad Debts	96,613	92,185
Professional Fees	126,273	127,934
Depreciation/Amortization	<u>138,878</u>	<u>129,377</u>
	<u>2,556,217</u>	<u>2,342,836</u>
 SOLID WASTE		
Salaries	596,228	561,173
Employee Benefits	510,394	416,236
Repairs and Maintenance	304,580	260,697
Supplies	17,173	17,037
Small Tools	5,667	3,127
Utilities and Telephone	21,560	18,930
Property Insurance	43,190	40,841
Other	11,281	14,247
Depreciation	457,481	428,267
Landfill Charges	<u>255,537</u>	<u>241,572</u>
	<u>2,223,091</u>	<u>2,002,127</u>
 WATER		
Salaries	726,706	665,856
Employee Benefits	590,794	429,612
Repairs and Maintenance	246,776	182,533
Supplies	361,001	312,991
Small Tools	28,739	8,473
Utilities and Telephone	486,047	464,900
Property Insurance	78,530	71,074
Other	45,423	52,017
Postage	15	11
Depreciation/Amortization	1,307,259	1,097,380
New Services	<u>2,941</u>	<u>10,621</u>
	<u>\$ 3,874,231</u>	<u>\$ 3,295,468</u>

WINCHESTER MUNICIPAL UTILITIES
SCHEDULE I - DEPARTMENT EXPENSES (CONTINUED)
FOR THE YEARS ENDED JUNE 30, 2018 AND 2017

	<u>2018</u>	<u>2017</u>
WASTEWATER		
Salaries	\$ 1,024,313	\$ 922,581
Employee Benefits	789,547	591,793
Repairs and Maintenance	545,465	487,076
Supplies	202,407	415,335
Small Tools	14,078	19,696
Utilities and Telephone	812,862	896,463
Property Insurance	125,863	128,455
Other	46,710	39,978
Postage	71	-
Professional Fees	259,997	221,707
Depreciation/Amortization	3,160,305	3,141,464
New Services	-	183
	<u>6,981,618</u>	<u>6,864,731</u>
VEHICLE MAINTENANCE		
Salaries	20,337	18,476
Employee Benefits	57,836	50,448
Repairs and Maintenance	8,530	5,293
Supplies	3,221	3,271
Small Tools	1,819	2,714
Utilities and Telephone	22,038	19,949
Property Insurance	10,056	9,931
Other	1,268	617
Depreciation/Amortization	<u>7,695</u>	<u>7,491</u>
	<u>132,800</u>	<u>118,190</u>
TOTAL OPERATING EXPENSES	<u><u>\$ 15,767,957</u></u>	<u><u>\$ 14,623,352</u></u>

**WINCHESTER MUNICIPAL UTILITIES
SCHEDULE II - REVENUE BOND DEBT SERVICES
FOR THE YEAR ENDED JUNE 30, 2018**

Maturity Date	2018 Issue		2014 Issue		2012 Issue		2011 Issue		Total	
	Principal	Interest	Principal	Interest	Principal	Interest	Principal	Interest	Principal	Interest
2018-2019	\$ -	\$ 444,144	\$ 220,000	\$ 322,006	\$ 325,000	\$ 184,744	\$ 396,250	\$ 315,369	\$ 941,250	\$ 822,119
2019-2020	65,000	444,144	225,000	315,406	330,000	174,994	411,250	299,519	966,250	789,919
2020-2021	65,000	441,544	235,000	308,656	345,000	165,094	428,333	283,069	1,008,333	756,819
2021-2022	75,000	438,944	240,000	301,606	355,000	154,744	448,333	265,706	1,043,333	722,056
2022-2023	80,000	435,944	250,000	294,406	365,000	144,094	468,333	246,733	1,083,333	685,233
2023-2024	95,000	432,744	255,000	286,906	375,000	133,144	490,417	226,994	1,120,417	647,044
2024-2025	95,000	428,944	265,000	279,256	390,000	121,894	515,417	203,399	1,170,417	604,549
2025-2026	110,000	425,144	270,000	271,306	400,000	109,705	540,417	178,365	1,210,417	559,376
2026-2027	120,000	420,744	280,000	263,206	415,000	96,705	567,500	151,344	1,262,500	511,255
2027-2028	130,000	415,944	290,000	254,806	430,000	82,700	597,500	122,664	1,317,500	460,170
2028-2029	725,000	410,744	295,000	246,106	445,000	67,650	629,583	91,722	1,369,583	405,478
2029-2030	140,000	381,744	305,000	236,961	460,000	52,074	666,667	58,330	1,431,667	347,365
2030-2031	475,000	376,144	315,000	227,506	480,000	35,400	402,500	22,138	1,197,500	285,044
2031-2032	945,000	361,894	325,000	216,875	480,000	18,000	-	-	805,000	234,875
2032-2033	1,475,000	333,544	340,000	205,906	-	-	-	-	340,000	205,906
2033-2034	790,000	287,450	350,000	194,006	-	-	-	-	350,000	194,006
2034-2035	810,000	261,775	365,000	181,756	-	-	-	-	365,000	181,756
2035-2036	840,000	235,450	375,000	168,981	-	-	-	-	375,000	168,981
2036-2037	865,000	208,150	390,000	155,856	-	-	-	-	390,000	155,856
2037-2038	895,000	178,956	405,000	141,719	-	-	-	-	405,000	141,719
2038-2039	1,010,000	148,750	420,000	127,038	-	-	-	-	420,000	127,038
2039-2040	1,045,000	113,400	435,000	111,817	-	-	-	-	435,000	111,817
2040-2041	1,080,000	76,825	450,000	95,500	-	-	-	-	450,000	95,500
2041-2042	1,115,000	39,025	470,000	78,625	-	-	-	-	470,000	78,625
2042-2043	-	-	490,000	61,000	-	-	-	-	490,000	61,000
2043-2044	-	-	505,000	41,400	-	-	-	-	505,000	41,400
2044-2045	-	-	530,000	21,200	-	-	-	-	530,000	21,200
	<u>\$ 13,045,000</u>	<u>\$ 7,742,091</u>	<u>\$ 9,295,000</u>	<u>\$ 5,409,812</u>	<u>\$ 5,595,000</u>	<u>\$ 1,540,942</u>	<u>\$ 6,562,500</u>	<u>\$ 2,465,352</u>	<u>\$ 21,452,500</u>	<u>\$ 9,416,106</u>

SUMMERS, MCCRARY & SPARKS, P.S.C.

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

To the Board of Commissioners
Winchester Municipal Utilities
Winchester, KY

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 business-type activities of Winchester Municipal Utilities, component unit of the City of Winchester, Kentucky, as of and for the year ended June 30, 2018, and the related notes to the financial statements, which collectively comprise the Utilities' basic financial statements, and have issued our report thereon dated November 9, 2018.

Internal Control over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Winchester Municipal Utilities, component unit of the City of Winchester, Kentucky, internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Winchester Municipal Utilities, component unit of the City of Winchester, Kentucky, internal control. Accordingly, we do not express an opinion on the effectiveness of the Winchester Municipal Utilities, component unit of the City of Winchester, Kentucky, internal control.

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

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

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Winchester Municipal Utilities, component unit of the City of Winchester, Kentucky, 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*.

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.

Summers, McCrary & Sparks, PSC

Winchester, Kentucky
November 9, 2018