

**PADUCAH MCCRACKEN JOINT SEWER AGENCY  
PADUCAH, KENTUCKY**

**FINANCIAL STATEMENTS  
With Independent Auditor's Report**

**YEARS ENDED JUNE 30, 2014 and 2013**

**TABLE OF CONTENTS**

	Page
<b>INDEPENDENT AUDITOR’S REPORT</b> .....	1
<b>REQUIRED SUPPLEMENTARY INFORMATION</b>	
Management Discussion and Analysis .....	3
<b>BASIC FINANCIAL STATEMENTS</b>	
Statements of Net Position .....	9
Statements of Revenues, Expenses and Changes in Net Position .....	10
Statements of Cash Flows .....	11
<b>NOTES TO FINANCIAL STATEMENTS</b> .....	13
<b>SUPPLEMENTAL INFORMATION</b>	
Statement of Revenues and Expenses, Actual to Budget – Current Year.....	23
Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with <i>Government Auditing Standards</i> .....	24
Independent Auditor’s Report on Compliance with Requirements Applicable to Each Major Program and Internal Control Over Compliance in Accordance with OMB Circular A-133 .....	26
Schedule of Expenditures of Federal Awards.....	28
Schedule of Findings and Questioned Costs .....	29
Summary Schedule of Prior Audit Findings.....	30



## INDEPENDENT AUDITOR'S REPORT

Board of Directors  
Paducah McCracken Joint Sewer Agency  
Paducah, Kentucky

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

We have audited the accompanying financial statements of the business-type activities of Paducah McCracken Joint Sewer Agency, as of and for the years ended June 30, 2014 and 2013, and the related notes to the financial statements, which collectively comprise the Agency's basic financial statements as listed in the table of contents.

### ***Management's Responsibility for the Financial Statements***

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

### ***Auditor's Responsibility***

Our responsibility is to express 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 and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the 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 financial position of the business-type activities of the Paducah McCracken Joint Sewer Agency as of June 30, 2014 and 2013, and the respective changes in financial position, and cash flows thereof for the years then ended in accordance with accounting principles generally accepted in the United States of America.

## ***Other Matters***

### *Required Supplementary Information*

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis pages 3 through 8 and budgetary comparison information on page 23 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

### *Other Information*

Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise the Paducah McCracken Joint Sewer Agency's basic financial statements. The schedule of expenditures of federal awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is also not a required part of the financial statements.

The schedule of expenditures of federal awards is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. Such information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the schedule of expenditures of federal awards is fairly stated in all material respects in relation to the 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 September 18, 2014, on our consideration of the Paducah McCracken County Joint Sewer Agency's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering Paducah McCracken County Joint Sewer Agency's internal control over financial reporting and compliance.

*Kempner CPA Group LLP*

Certified Public Accountants and Consultants  
Paducah, Kentucky  
September 18, 2014

**REQUIRED SUPPLEMENTARY INFORMATION**



As management of the Paducah McCracken Joint Sewer Agency (JSA), we offer readers of the JSA's financial statements this narrative overview and analysis of the financial activities for the fiscal year ended June 30, 2014.

### **Financial Highlights**

- Total assets increased \$2.5 million (3.2%) as a result of FY 2014 operations
- Unrestricted net assets increased \$2.7 million (23.0%) over the prior fiscal year
- Operating expenses finished \$166 thousand less than budget including \$49 thousand less than budgeted depreciation
- Debt service coverage ratios remain well above the level of compliance

### **Required Financial Statements**

Statement of Net Position – The purpose of the Statement of Net Position is to report all of the assets held and liabilities owed by the JSA. The statement shows the JSA's level of investment in resources (assets) and the obligations to creditors (liabilities). The difference between the assets and liabilities is labeled net position and is similar to owners' equity presented by a commercial enterprise. The purpose of the JSA is not to accumulate net assets, but rather to reinvest in the infrastructure and to build sufficient reserves in the event of an emergency. In general, increases in net position indicate that the financial position of the JSA is improving over time.

Statement of Revenues, Expenses and Changes in Net Position – The purpose of this statement is to identify the revenues and expenses generated and incurred by the JSA. The focus of this statement is to help the user identify the operating results of the JSA during the fiscal year. The difference between revenues and expenses is called the change in net position and is similar to net income reported by a commercial entity.

Statement of Cash Flows – The purpose of the Statement of Cash Flows is to analyze the cash receipts and disbursements made by the JSA during the fiscal year. The statement reports cash inflows and outflows resulting from three main business activities: operating, financing and investing. The statement addresses the sources and uses of cash, and the change in cash balances from the previous reporting period.

## Financial Information

### EXHIBIT 1: Condensed Statements of Net Position (in thousands)

	<u>FYE</u> <u>6/30/14</u>	<u>FYE</u> <u>6/30/13</u>	<u>Dollar</u> <u>Change</u>	<u>Percent</u> <u>Change</u>
<b>Assets</b>				
Current assets	\$ 14,773	\$ 13,071	\$ 1,702	13.0%
Capital assets	62,741	62,655	86	0.1%
Restricted funds	1,881	1,731	150	8.7%
Deferred charges & other	<u>635</u>	<u>65</u>	<u>570</u>	876.9%
Total assets	<u>80,030</u>	<u>77,522</u>	<u>2,508</u>	3.2%
<b>Liabilities &amp; net position</b>				
Current liabilities	1,759	1,948	(189)	-9.7%
Noncurrent liabilities	<u>20,559</u>	<u>17,818</u>	<u>2,741</u>	15.4%
Total liabilities	<u>22,318</u>	<u>19,766</u>	<u>2,552</u>	12.9%
Invested in capital assets, net	41,199	44,125	(2,926)	-6.6%
Restricted	1,881	1,731	150	8.7%
Unrestricted	<u>14,632</u>	<u>11,900</u>	<u>2,732</u>	23.0%
Total net position	<u>\$ 57,712</u>	<u>\$ 57,756</u>	<u>\$ (44)</u>	-0.1%

### Net Position

The JSA's total net position decreased by \$44 thousand during FY 2014. The JSA continues to rebuild the aging sewer infrastructure as well as extend sewers to previously unsewered and undeveloped areas of the city and county. The JSA is committed to capital investments in infrastructure assets to protect the integrity of and enhance the existing sewer system.

### Capital Assets and Long-Term Debt Activity

At the close of FY 2014, the JSA had \$62.7 million in undepreciated cost of total capital assets. Capital assets increased due to the purchase of capital assets, the completion of capital projects and the contribution of assets to the JSA by private developers.

During FY 2011, the JSA began constructing a two-phase, multi-year project, named the Massac Creek Interceptor, Force Main and Pump Station Project. Phase I of this project was placed in service during December, 2012 at a total cost of \$9.1 million. Phase II was placed in service in September, 2013 for \$4.8 million completing the project.

The current fiscal year brought construction of the Wallace Park Sewer Separation Project. This project consists of two phases – Phase I being a stormwater detention structure and Phase II being a sanitary sewer separation project. The total project is expected to cost approximately \$5.5 million.

Total liabilities increased during FY 2014 by \$2.6 million or 12.9% over FY 2013. JSA secured a \$10 million loan from the Kentucky Infrastructure Authority (KIA) during FY 2011 to aid in financing the Massac Creek Project. Principal payments commenced on the loan during FY 2014.

During FY 2012, the JSA also secured an \$8 million loan from KIA to fund various projects, including the Wallace Park Sewer Separation Project. This is currently a construction-type loan where the liability is recorded as money is received from KIA and interest-only is currently due on that money semi-annually.

**EXHIBIT 2: Condensed Statements of Revenues, Expenses and Changes in Net Position**  
(in thousands)

	<b>FYE 6/30/14</b>	<b>FYE 6/30/13</b>	<b>Dollar Change</b>	<b>Percent Change</b>
<b>Revenues</b>				
Operating revenues	\$ 6,912	\$ 6,971	\$ (59)	-0.8%
Non-operating revenues	<u>364</u>	<u>373</u>	<u>(9)</u>	-2.4%
Total revenues	<u>7,276</u>	<u>7,344</u>	<u>(68)</u>	-0.9%
<b>Expenses</b>				
Depreciation	2,536	2,299	237	10.3%
Operating expenses	4,342	4,189	153	3.7%
Non-operating expenses	<u>485</u>	<u>185</u>	<u>300</u>	162.2%
Total expenses	<u>7,363</u>	<u>6,673</u>	<u>690</u>	10.3%
<b>Contributions</b>	<u>43</u>	<u>1,793</u>	<u>(1,750)</u>	-97.6%
<b>Change in net position</b>	<b>(44)</b>	<b>2,464</b>	<b>(2,508)</b>	<b>-101.8%</b>
Beginning net position	<u>57,756</u>	<u>55,292</u>	<u>2,464</u>	4.5%
<b>Ending net position</b>	<b>\$ 57,712</b>	<b>\$ 57,756</b>	<b>\$ (44)</b>	<b>-0.1%</b>

**Budget**

The JSA conducts its activities in accordance with a budget for operating revenues, operating expenses, and capital purchases. The JSA is required to adopt a budget annually. Through monitoring and review by the JSA Board, the Agency continuously meets its responsibility for sound financial management.

Operating revenues for FY 2014 finished \$59 thousand below the amount for the prior year. Sewer charges comprise the bulk of operating revenues and are billed based on customer water consumption. These charges came in \$126 thousand less than budget for FY 2014. Operating expenses came in under budget for the fiscal year finishing \$166 thousand below estimate. Net non-operating revenue for FY 2014 was more than the budgeted amount due to construction period interest being capitalized rather than expensed during the fiscal year and due to tap on fee revenue being favorable for the current year ended. JSA finished the fiscal year with an (\$87) thousand decrease in net position before capital contributions.

### Results of Operations

Overall revenues totaled \$7.3 million for FY 2014, a decrease of \$68 thousand or -0.9% from FY 2013. Total expenses increased \$690 thousand over FY 2013 to nearly \$7.4 million. The largest contributing factors to the increase in total expenses was the high cost of power during the fiscal year, depreciation expense and the interest cost to fund capital projects.

EXHIBIT 3: Detail of Operating Expenses

Operating Expenses, excluding depreciation (in thousands)	FYE 6/30/14	FYE 6/30/13	Dollar Change	Percent Change
Salaries and benefits	\$ 2,248	\$ 2,179	\$ 69	3.2%
Chemicals, testing & solids disposal	333	309	24	7.8%
Utilities	797	653	144	22.1%
Material, supplies and repairs	365	435	(70)	-16.1%
Fleet expense	106	127	(21)	-16.5%
Professional fees	113	153	(40)	-26.1%
Billing, collection and bad debts	162	143	19	13.3%
All other	218	190	28	14.7%
Total	\$ 4,342	\$ 4,189	\$ 153	3.7%

### Salaries and Benefits

Salaries and benefits comprise the bulk of operating expenses. Benefits total 52% of actual wages, with health insurance comprising 40% of the benefits cost. While pension funding has risen over the past several years, it has remained steady during FY 2014 and 2013 costing the Agency \$286 and \$271 thousand respectively, or 37% of total benefits each year. Employees received annual wage increases during FY 2014 and 2013.

### Other Operating Expenses

Chemicals, testing and solids disposal showed a \$24 thousand increase from the prior year. Chemical usage amounts and costs vary from year to year based on a variety of factors, including economic conditions and pricing, as well as certain operational parameters which vary due to odor control requirements, treatment plant flows, and the maintenance of the bacterial inventory at the wastewater treatment plants. Solids disposal costs vary primarily based on the treated flow amounts, the efficiency of the wastewater treatment plant digesters and the ability for the City of Paducah's composting facility to efficiently handle the Paducah wastewater treatment plant's fully digested sludge inventory. In times of low composting supply material (i.e. branches, leaves, sticks, etc.) or composting facility equipment breakdown, the JSA is forced to landfill sludge at higher costs.

The largest component of utilities expense is electricity costs. The budget for electricity was \$549 thousand with actual costs totaling \$667 thousand. Electricity costs vary from year to year based on flows received and pumped. Electricity costs this year are particularly high due to the JSA's primary electrical provider, Paducah Power, experiencing a high power cost adjustment factor due to issues associated with their power supplier, Prairie State Energy Campus.

Materials, supplies and repairs are ordinary and necessary costs incurred to keep the sewer utility process in good working order. The FY 2014 budget for materials, supplies and repairs was \$512 thousand resulting in a positive variance of \$147 thousand. This is due to successful preventive maintenance programs as well as a reduction of higher-cost dig and repairs. In addition, JSA did not perform subcontract smoke testing as planned, due to less than satisfactory ground conditions necessary for the work.

The largest component of the material, supplies and repairs category is repairs, which include collection system point repairs, pump rebuilds, and plant equipment repairs. Contract labor is sometimes used for these repairs and is charged to this category, while internal labor for repair work is expensed to salaries and wages. Expenses are categorized using the three main components of a sewer system: pipes, pumps and motors. Repairs were made as follows:

EXHIBIT 4: Repairs by Department (in thousands)

<u>Department</u>	<u>FYE 2014</u>	<u>FYE 2013</u>	<u>Dollar Change</u>	<u>Percent Change</u>
Collection System (pipes)	\$ 66	\$ 159	\$ (93)	-58.5%
Lift Stations (pipes & pumps)	71	54	17	31.5%
Treatment Plants (pipes, pumps & motors)	44	43	1	2.3%
<b>Total</b>	<u>\$ 181</u>	<u>\$ 256</u>	<u>\$ (75)</u>	<u>-29.3%</u>

Fleet expense declined \$21 thousand, or 16.5%, over the prior fiscal year. The JSA maintains a vehicle replacement program to cull the aging fleet and attempt to minimize extensive repair costs. Fleet expense finished \$29 thousand less than budget for the current fiscal year.

FY 2014 professional fees were \$40 thousand less than in FY 2013. This is due to litigation with a developer that arose during fiscal year 2013 and was finalized during FY 2014. The budget for professional fees was \$148 thousand for FY 2014.

Paducah Water provides billing and collection services for the JSA. Bad debt write offs finished higher than expected at 0.86% of sewer charges.

All other expenses totaled \$218 thousand for FY 2014 and included costs for insurance, office, safety, training and miscellaneous expenses. The budget for all other expenses was \$212 thousand. While some expenses included in this category finished near budget, safety came in \$6 thousand less and training came in \$4 thousand less than budget, while miscellaneous expense finished \$19 thousand over budget. A portion of the safety expense is paid to a third party provider and fluctuates based on the working environment and safety conditions encountered. Training is a cyclical expense, and can depend on courses offered, timing, employee interest and other factors. Miscellaneous expense can vary widely due to insurance claims, grant fees, legal advertising and certain travel expenses.

### **Debt Service Coverage**

Debt service coverage ratio is an indicator of the JSA's ability to meet its debt obligations. The JSA Board strives to maintain a minimum debt service coverage ratio of 1.3 times the required debt service payments. For purposes of this calculation, gross revenues include investment income, grant revenues and connection fees, but exclude the deduction for depreciation expense. The JSA is exceeding the minimum level of net revenue equal to 1.3 times of the required debt service payments. The JSA's debt service coverage ratio was 1.95 in 2014 and 3.82 in 2013.

### **Relevant Current Economic Factors and Other Significant Matters**

Regional economic trends that affect the financial condition of the JSA have remained sluggish throughout this fiscal year. New home construction was slow which is representative of the current U.S. market.

Investment returns have continued to remain flat. These returns will fluctuate with adjustments in interest rates, due to the nature of JSA's investments.

The Paducah McCracken Joint Sewer Agency entered into a Consent Judgment with the Kentucky Environmental and Public Protection Cabinet in September 2007 to bring combined and sanitary sewer overflows into compliance with Federal and State guidelines. The Agency will be bound by this Judgment for many years to come and will incur costs to bring the system into compliance that can only be determined as solutions to the issues are proposed and approved by the Cabinet as outlined in the Consent Judgment. The total cost of complying with this Consent Judgment has not been determined, but will be significant. As a result, future rate increases will be necessary to achieve compliance. JSA will undergo an analysis of rates and fees during fiscal year 2015, with planned changes proposed to be placed in effect July 1, 2015. The JSA strives to utilize sound business principals while meeting the needs of the community and maintaining environmental compliance with Federal, State and local regulations.

The JSA continues to pursue alternative means of funding in the form of grants and low-interest loans to aid in the funding of the Agency's capital expenditures. The JSA has been successful in securing \$10.2 million in grants from the Kentucky Infrastructure Authority (KIA) and the United States Department of Agriculture (USDA) Rural Development since FY 2005. JSA was also awarded a \$100 thousand grant from Delta Regional Authority and expended \$100 thousand of those funds during FY 2013. These funds have been expended on projects relating to expansion of the collection system, maximization of flow at Paducah's wastewater treatment plant, the separation of flow from JSA's combined sewer system, various compliance related planning documents, and the Massac Creek Interceptor Project, thus reducing the burden of these projects on JSA ratepayers.

### **Requests for Additional Information**

This report is intended to provide readers with a general overview of the JSA's finances and to show the JSA's accountability for the money it receives. If you have questions about this report or need additional financial information, contact the JSA at 621 Northview Street, Paducah, KY 42001 or (270) 575-0056.

## **BASIC FINANCIAL STATEMENTS**

**PADUCAH McCracken Joint Sewer Agency**  
**Statements of Net Position**  
**June 30, 2014 and 2013**

	<b>2014</b>	<i>As Restated</i> <b>2013</b>
<b>ASSETS</b>		
<b>CURRENT ASSETS</b>		
Cash and cash equivalents	\$ 5,234,911	\$ 4,311,660
Investments and accrued interest	8,066,700	6,845,778
Customer accounts receivable	429,834	385,096
Grants and other receivables	169,315	659,439
Accrued unbilled revenue	554,000	544,000
Inventories and prepaid expenses	318,321	324,669
	<b>Total Current Assets</b>	<b>13,070,642</b>
	14,773,081	13,070,642
<b>NON-CURRENT ASSETS</b>		
Utility Plant and Capital assets, net	62,741,032	62,654,717
Restricted assets and investments	1,880,538	1,731,224
Bond discount - net	55,137	60,613
Notes receivable	1,622	4,755
Other non-current assets	578,534	-
	<b>Total Noncurrent Assets</b>	<b>64,451,309</b>
	65,256,863	64,451,309
<b>TOTAL ASSETS</b>	<b>80,029,944</b>	<b>77,521,951</b>
	80,029,944	77,521,951
<b>LIABILITIES</b>		
<b>CURRENT LIABILITIES</b>		
Notes and bonds payable	983,057	711,288
Accounts payable	488,508	1,050,266
Salaries and benefits payable	86,295	102,320
Other current liabilities	200,775	84,127
	<b>Total Current Liabilities</b>	<b>1,948,001</b>
	1,758,635	1,948,001
<b>NON-CURRENT LIABILITIES</b>		
Notes and bonds payable	20,559,124	17,818,151
	<b>Total Noncurrent Liabilities</b>	<b>17,818,151</b>
	20,559,124	17,818,151
<b>TOTAL LIABILITIES</b>	<b>22,317,759</b>	<b>19,766,152</b>
	22,317,759	19,766,152
<b>NET POSITION</b>		
Invested in capital assets, net of related debt	41,198,849	44,125,277
Restricted for:		
Debt service	1,880,538	1,731,224
Unrestricted - net assets	14,632,798	11,899,298
	<b>Total Net Position</b>	<b>\$ 57,755,799</b>
	\$ 57,712,185	\$ 57,755,799

The notes to financial statements are an integral part of this statement.

**PADUCAH McCracken Joint Sewer Agency**  
**Statements of Revenues, Expenses and Changes in Net Position**  
For the Years ended June 30, 2014 and 2013

	<u>2014</u>	<i>As Restated</i> <u>2013</u>
<b>Operating Revenues</b>		
Charges for service	\$ 6,912,425	\$ 6,971,035
<b>Operating Expenses</b>		
Salaries, wages and benefits	2,247,859	2,179,431
Chemicals, testing and solid disposal	333,090	309,472
Utilities	796,724	653,216
Materials, supplies and repairs	365,428	434,821
Fleet expense	106,181	126,952
Liability insurance	113,656	104,406
Training, safety and dues	30,338	42,173
Professional fees	112,968	152,963
Office expense	14,424	15,753
Public education	750	750
Billing and collections	102,047	101,345
Bad debts	59,571	41,310
Board of directors expense	16,800	16,800
Miscellaneous	41,856	10,098
Depreciation	2,536,013	2,299,209
	<u>6,877,705</u>	<u>6,488,699</u>
<b>Operating Income</b>	<u>34,720</u>	<u>482,336</u>
<b>Non-operating Revenues (Expenses)</b>		
Investment income	35,785	34,398
Interest expense	(445,966)	(163,235)
Amortization	(5,476)	(5,572)
Gain (loss) on sale of assets	(34,080)	(16,186)
Tap-on and assessment fees	310,008	335,696
Other, net	17,976	3,552
Total non-operating revenue (expenses), net	<u>(121,753)</u>	<u>188,653</u>
Change in net position before capital contributions	(87,033)	670,989
<b>Capital Contributions</b>		
Grant revenue	3,544	1,144,980
Contributions from developers	39,875	648,020
	<u>43,419</u>	<u>1,793,000</u>
<b>Change in Net Position</b>	(43,614)	2,463,989
<b>Net Position, Beginning</b>	<u>57,755,799</u>	<u>55,291,810</u>
<b>NET POSITION, ENDING</b>	<u><u>\$ 57,712,185</u></u>	<u><u>\$ 57,755,799</u></u>

The notes to financial statements are an integral part of this statement.

**PADUCAH McCRACKEN JOINT SEWER AGENCY**  
**STATEMENTS OF CASH FLOWS**  
**For the Years ended June 30, 2014 and 2013**

	<u>2014</u>	<u>2013</u>
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Collections from customers	\$ 6,857,687	\$ 6,904,471
Cash paid to suppliers	(2,648,576)	(2,373,103)
Cash paid to employees	(2,263,884)	(2,152,020)
<b>NET CASH PROVIDED BY (USED IN)</b>		
<b>OPERATING ACTIVITIES</b>	<u>1,945,227</u>	<u>2,379,348</u>
 <b>CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES</b>		
Grants and contributed capital	493,668	1,144,980
Tap-on fees and assessments	310,008	335,696
Acquisition of capital assets	(2,616,533)	(6,719,558)
Proceeds from the sale of fixed assets	-	2,862
Proceeds from debt issues	3,966,125	7,183,894
Principal payments on long term debt	(950,250)	(5,019,318)
Interest payments on long term debt	(329,985)	(475,936)
Increase in other non-current asset	(578,534)	
Other, net	17,976	(30,254)
<b>NET CASH PROVIDED BY (USED IN) CAPITAL AND RELATED FINANCING ACTIVITIES</b>	<u>312,475</u>	<u>(3,577,634)</u>
 <b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Proceeds from sales and maturities of investments	7,037,593	10,751,398
Purchases of investments	(8,407,829)	(9,168,582)
Investment earnings	35,785	42,406
<b>NET CASH PROVIDED BY (USED IN) INVESTING ACTIVITIES</b>	<u>(1,334,451)</u>	<u>1,625,222</u>
 <b>NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS</b>	923,251	426,936
 <b>CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR</b>	<u>4,311,660</u>	<u>3,884,724</u>
 <b>CASH AND CASH EQUIVALENTS, END OF YEAR</b>	<u><u>\$ 5,234,911</u></u>	<u><u>\$ 4,311,660</u></u>

The notes to financial statements are an integral part of this statement.

**PADUCAH McCRACKEN JOINT SEWER AGENCY  
STATEMENTS OF CASH FLOWS (CONTINUED)**

**For the Years ended June 30, 2014 and 2013**

	<u>2014</u>	<u>2013</u>
<b>RECONCILIATION OF OPERATING INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES</b>		
Operating income	\$ 34,720	\$ 482,336
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation	2,536,013	2,299,209
Change in assets and liabilities:		
Accounts receivable	(44,738)	(14,993)
Accrued unbilled revenue	(10,000)	22,000
Inventory and prepaid expenses	6,348	(9,186)
Accounts payable	(561,758)	(105,871)
Salaries and benefits payable	(16,025)	27,411
Other current liabilities	667	(321,558)
<b>NET CASH PROVIDED BY OPERATING ACTIVITIES</b>	<u>\$ 1,945,227</u>	<u>\$ 2,379,348</u>

The notes to financial statements are an integral part of this statement.

**PADUCAH McCracken JOINT SEWER AGENCY  
NOTES TO FINANCIAL STATEMENTS**

**NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**Reporting Entity**

The Paducah McCracken Joint Sewer Agency, the “Agency”, was established pursuant to Chapter 76 of the Kentucky Revised Statutes. The Agency provides wastewater services to the residents of the City of Paducah and McCracken County, Kentucky. The Agency was established by merging the City of Paducah Wastewater Enterprise Fund with the three sewer districts of McCracken County. Substantially all of the assets and liabilities of the separate component entities were contributed to create the Paducah McCracken Joint Sewer Agency effective July 1, 1999.

**Accounting Method**

The Paducah McCracken Joint Sewer Agency maintains its books and these financial statements are presented on the accrual basis of accounting. Proprietary funds are accounted for using the “economic resources” measurement focus and the accrual basis of accounting. Accordingly, all assets and liabilities (whether current or noncurrent) are included on the Statement of Net Position. The Statement of Revenues, Expenses and Changes in Fund Net Position present increases (revenues) and decreases (expenses) in total net position. Under the accrual basis of accounting, revenues are recognized in the period in which they are earned while expenses are recognized in the period in which the liability is incurred.

Proprietary funds distinguish operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and delivering goods in connection with a proprietary fund’s ongoing operations. The principal operating revenues of the Agency are charges for sewer service. Operating expenses for proprietary 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 nonoperating revenues and expenses.

The significant accounting policies, as summarized below, are in conformity with generally accepted accounting principles as applicable to governmental units as prescribed by the Governmental Accounting Standards Board. The Agency applies Financial Accounting Standards Board (FASB) Accounting Standards Codification (Codification) issued on or before November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements, in which case, GASB prevails.

**Cash and Investments**

The Agency adopted formal deposit and investment policies in 1999. These policies apply to all Agency funds not contained in public trusts.

For the purpose of the Statements of Cash Flows, “cash and cash equivalents” includes unrestricted demand and savings accounts of the Agency.

**Accounts Receivable and Bad Debts**

Accounts receivable are uncollateralized customer obligations due under normal trade terms requiring payment within 30 days from the invoice mailing date. Customer account balances with invoices dated over 30 days old are considered delinquent. Payments of accounts receivable are allocated to the specific invoices identified on the customer’s remittance advice or, if unspecified, are applied to the earliest unpaid invoices.

No allowance for doubtful accounts has been provided since it is believed the balance in accounts receivable is fully collectible. Overdue accounts are monitored and written off as necessary. The effect of using this method is not significantly different from results which would be obtained by using the allowance method.

**Accrued Unbilled Revenue**

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

**Inventories**

Materials and supplies are carried in an inventory account at cost and are subsequently capitalized or charged to expense when consumed utilizing the first-in, first out (FIFO) method.

**PADUCAH McCRACKEN JOINT SEWER AGENCY  
NOTES TO FINANCIAL STATEMENTS**

**NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

**Notes Receivable**

Notes receivable represent balances due from customers in developed areas/subdivisions that have elected to pay their sewer service tap-on fee in installments. The Agency charges new customers an initial fee to connect to the system. That fee is paid upon connection, or the customer in developed areas/subdivisions may elect to spread the payment over ten years. The monthly installments include six percent interest. The Agency obtains a lien against the property until the tap-on fee is satisfied.

**Capital Assets**

Capital assets are recorded at cost. Donated assets are stated at fair value on the date donated. The Agency generally does not capitalize assets with costs less than \$1,000. The costs of normal maintenance and repairs that do not add to the asset value or materially extend useful lives are not capitalized.

When capital assets are disposed, the cost and applicable accumulated depreciation are removed from the respective accounts, and the resulting gain or loss is recorded. Depreciation is provided by the straight-line method over the estimated useful lives of the various classes of assets as follows:

	<u>Years</u>
Utility plant	20-60
Vehicles	5-7
General plant and office equipment	3-10

**Capital Contributions**

Capital contributions are derived from developers, when they construct and pay for sewer lines and then donate these additions to the Agency, and other governments, in the form of grants or contributions of capital assets. Developer contributions are recorded at fair value when the property is transferred to the Agency and are depreciated over their estimated useful lives using the straight-line method.

**Use 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.

**Reclassifications**

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

**NOTE B - RESTRICTED FUNDS**

Restricted funds consist of certificates of deposit and other securities, which have been set aside for the repayment of bonds and notes or for maintenance reserves as required and for ongoing capital projects. These balances are classified as restricted assets on the statement of net assets because their use is limited by applicable bond ordinances and loan agreements.

**PADUCAH McCracken JOINT SEWER AGENCY  
NOTES TO FINANCIAL STATEMENTS**

**NOTE B - RESTRICTED FUNDS (Continued)**

At June 30, 2014, these restricted funds were comprised of the following investments:

	<b>2014</b>	<b>2013</b>
Certificates of deposit – various financial institutions	\$ 1,235,000	\$ 1,199,999
U.S. Government money market funds	1,859	1,172
U.S. Government treasury obligations	643,679	530,053
<b>TOTAL</b>	<b>\$ 1,880,538</b>	<b>\$ 1,731,224</b>

When both restricted and unrestricted resources are available for use, it is the Agency’s policy to use restricted resources first, then unrestricted resources as they are needed.

**NOTE C – DEPOSITS AND INVESTMENTS WITH FINANCIAL INSTITUTIONS**

**Deposits**

**Custodial credit risk** for deposits is the risk that in the event of a bank failure, the Agency’s deposits may not be returned or the Agency will not be able to recover collateral securities in the possession of an outside party. The Agency’s investment policy requires all investments be made in accordance with applicable legal requirements with consideration of investment safety. Accordingly, the Agency maintains collateral agreements with its financial institutions, whereby deposits are secured with collateral valued at market or par, whichever is lower. The Board of Directors has authorized the Executive Director to utilize depository institutions located within McCracken County, which have been evaluated by the Board and/or Executive Director and Finance Director.

During the year ended June 30, 2014 and 2013, the Agency’s investments include U.S. government money market funds, short-term treasury obligations, demand deposits and certificates of deposit. The bank balance of cash and investments totaled \$15,301,241 and \$12,878,479, respectively at June 30, 2014 and 2013, with \$69,000 and \$ 0, respectively, uninsured and uncollateralized.

**Credit Risk** is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. Generally, the Agency’s investing activities are managed under the direction of the Executive Director and Finance Director. Investing is performed in accordance with investment policies adopted by the Board of Directors complying with State Statutes. The state statutes authorize the Agency to invest in direct obligations of the United States government, obligations backed by the full faith and credit of the United States government, certificates of deposit or other interest bearing accounts issued by any bank or savings and loan institution provided that such investments are insured by the FDIC or guaranteed by the pledge of direct United States government obligations, bonds issued by the Commonwealth of Kentucky or one of its agencies and instrumentalities, securities issued by any state or local government of the United States rated in one of the three highest categories by a nationally recognized rating agency, certain mutual funds, commercial paper rated in the highest category by a nationally recognized rating agency, or bankers’ acceptances for banks rated in one of the three highest categories by a nationally recognized rating agency.

**PADUCAH McCRACKEN JOINT SEWER AGENCY  
NOTES TO FINANCIAL STATEMENTS**

**NOTE D - CONSTRUCTION IN PROGRESS**

The Agency had the following projects in process at June 30,:

	<u>2014</u>	<u>2013</u>
Blandville West Estates Rehabilitation	\$ -	\$ 792
Cairo Road & Exit 3 Sewer Extension	12,298	-
Chickadee Lift Station Elimination Project	10,493	144
Cook Street Overflow Tank	43,188	144
Gatewood Lift Station Elimination Project	2,622	144
Handrails at PWWTP	-	51,395
Homewood/Milliken Pump Station Refurbishment	-	405,253
James Marine Sewer Extension	40,919	774
Long Term Control Plan	816,503	805,578
Massac Creek Interceptor		
Pump Station and Force Main Phase II	-	4,136,109
Pump Station and Force Main Phase III Study	18,526	-
Milton Pump Station Control Panel Upgrade	-	12,118
Old Highway 60 Extension	4,250	4,250
Pecan Drive Property	2,632	-
Rate Study	3,763	-
Rehab and Manhole Contract CY '12	-	1,266,779
Rehab and Manhole Contract CY '13	-	20,229
Rehab and Manhole Contract CY '14	18,985	-
Terre Verte Package Plant	7,375	-
Video & Cleaning Contract #9	-	48,528
Video & Cleaning Contract #10	14,821	-
Wallace Park Sewer Separation	720,925	560,513
WIN 911 System and Pump Stations/WWTP	-	1,760
Capitalized Interest	-	<u>144,322</u>
<b>TOTALS</b>	<u>\$ 1,717,300</u>	<u>\$ 7,458,832</u>

Construction in progress related invoices of \$279,236 and \$614,631 were included in accounts payable at June 30, 2014 and 2013, respectively.

**PADUCAH McCracken Joint Sewer Agency  
Notes to Financial Statements**

**NOTE E - UTILITY PLANT**

Utility plant consists of the following at June 30:

	<b>2014</b>			
	<u>Balance as of June 30, 2013</u>	<u>Increases</u>	<u>Decreases</u>	<u>Balance as of June 30, 2014</u>
<b><u>Capital assets, not being depreciated:</u></b>				
Land	\$ 745,309	\$ 122,793	\$ -	\$ 868,102
Construction in progress	<u>7,458,832</u>	<u>2,987,793</u>	<u>8,729,325</u>	<u>1,717,300</u>
Total capital assets, not being depreciated:	<u>8,204,141</u>	<u>3,110,586</u>	<u>8,729,325</u>	<u>2,585,402</u>
<b><u>Capital assets, being depreciated:</u></b>				
Utility assets (pipes, pumps, plants, structures)	78,587,320	8,161,615	76,446	86,672,489
Vehicles	1,323,864	24,370	-	1,348,234
General plant and office furniture	<u>2,356,665</u>	<u>89,160</u>	<u>24,316</u>	<u>2,421,509</u>
Totals at historical cost	<u>82,267,849</u>	<u>8,275,145</u>	<u>100,762</u>	<u>90,442,232</u>
Less: accumulated depreciation				
Utility assets	25,225,278	2,214,024	46,533	27,392,769
General plant and office furniture	1,545,535	156,458	-	1,701,993
Vehicles	<u>1,046,460</u>	<u>165,531</u>	<u>20,151</u>	<u>1,191,840</u>
Total accumulated depreciation	<u>27,817,273</u>	<u>2,536,013</u>	<u>66,684</u>	<u>30,286,602</u>
Total capital assets, being depreciated, net:	<u>54,450,576</u>	<u>5,739,132</u>	<u>34,078</u>	<u>60,155,630</u>
<b>Total System capital assets – net:</b>	<u>\$ 62,654,717</u>	<u>\$ 8,849,718</u>	<u>\$ 8,763,403</u>	<u>\$ 62,741,032</u>

  

	<b>2013</b>			
	<u>Balance as of June 30, 2012</u>	<u>Increases</u>	<u>Decreases</u>	<u>Balance as of June 30, 2013</u>
<b><u>Capital assets, not being depreciated:</u></b>				
Land	\$ 542,149	\$ 203,160	\$ -	\$ 745,309
Construction in progress	<u>12,890,772</u>	<u>7,178,991</u>	<u>12,610,931</u>	<u>7,458,832</u>
Total capital assets, not being depreciated:	<u>13,432,921</u>	<u>7,382,151</u>	<u>12,610,931</u>	<u>8,204,141</u>
<b><u>Capital assets, being depreciated:</u></b>				
Utility assets (pipes, pumps, plants, structures)	65,719,127	12,907,027	38,834	78,587,320
Vehicles	1,361,584	8,752	46,472	1,323,864
General plant and office furniture	<u>2,359,669</u>	<u>9,466</u>	<u>12,470</u>	<u>2,356,665</u>
Totals at historical cost	<u>69,440,380</u>	<u>12,925,245</u>	<u>97,776</u>	<u>82,267,849</u>
Less: accumulated depreciation				
Utility assets	23,294,970	1,956,256	25,948	25,225,278
General plant and office furniture	1,377,787	176,139	8,391	1,545,535
Vehicles	<u>924,035</u>	<u>166,814</u>	<u>44,389</u>	<u>1,046,460</u>
Total accumulated depreciation	<u>25,596,792</u>	<u>2,299,209</u>	<u>78,728</u>	<u>27,817,273</u>
Total capital assets, being depreciated, net:	<u>43,843,588</u>	<u>10,626,036</u>	<u>19,048</u>	<u>54,450,576</u>
<b>Total System capital assets – net:</b>	<u>\$ 57,276,509</u>	<u>\$ 18,008,187</u>	<u>\$ 12,629,979</u>	<u>\$ 62,654,717</u>

**PADUCAH McCracken Joint Sewer Agency  
Notes to Financial Statements**

**NOTE F – LONG-TERM DEBT**

Notes and bond payable consists of the following:

	<b>2014</b>	<b>2013</b>
Notes Payable		
Kentucky Infrastructure Agency	\$ 12,877,681	\$ 9,605,439
Bonds Payable		
Sewer Revenue Bonds, Series 2011	4,264,500	4,324,000
2010 Revenue Bonds	4,400,000	4,600,000
	21,542,181	18,529,439
Less current maturities	983,057	711,288
	<b>\$ 20,559,124</b>	<b>\$ 17,818,151</b>

Debt service requirements on notes payable and bonds payable at June 30, 2014, are as follows:

<b>Years Ending June 30,</b>	<b>Principal</b>	<b>Interest</b>	<b>Service Fee</b>	<b>R&amp;M Reserves</b>	<b>Total</b>
2015	\$ 983,057	\$ 517,087	\$ 19,770	\$ 14,380	\$ 1,534,294
2016	1,004,477	495,044	18,329	-	1,517,850
2017	1,021,244	472,035	16,858	-	1,510,137
2018	1,048,866	447,460	15,358	-	1,511,684
2019	951,664	421,646	13,828	-	1,387,138
2020 – 2024	4,387,420	1,780,976	51,975	-	6,220,371
2025 – 2029	4,142,484	1,171,907	26,118	-	5,340,509
2030 – 2034	2,611,676	523,341	6,481	-	3,141,498
2035 – 2039	619,000	321,379	-	-	940,379
2040 – 2044	726,500	230,574	-	-	957,074
Thereafter	4,045,793	139,563	-	-	4,185,356
	<b>\$ 21,542,181</b>	<b>\$ 6,521,012</b>	<b>\$ 168,717</b>	<b>\$ 14,380</b>	<b>\$ 28,246,290</b>

Notes payable are secured by capital assets and restricted funds. At June 30, 2014, the above notes are payable to the Kentucky Infrastructure Authority and are payable in semi-annual installments, including interest ranging from 1% to 3.2%. These agreements provide capital project funding utilizing a combination of both long-term borrowing and federal stimulus grants funds from the American Recovery and Reinvestment Act.

During the year ended June 30, 2011, the Agency issued Series 2010 (Build America Bonds) Taxable Sewer Revenue Bonds, in the amount of \$4,995,000, to finance the acquisition, construction, development and equipping of improvements and renovations to address combined sewer overflows and eliminate sanitary sewer overflows. These taxable bonds were created as part of the Recovery Act of 2009 to finance municipal agency’s capital expenditures for which the US Treasury Department pays a direct subsidy of 35 percent of the interest cost to the issuer. During the fiscal year ended June 30, 2014 and 2013, the Agency received a 7.2 and 8.7 percent, respectively, reduction in the interest subsidy received due to the Federal Government Sequestration. There is a possibility of additional reductions in future interest subsidies relative to Build America Bonds.

During the year ended June 30, 2013, the Agency formally issued Sewer Revenue Bonds, Series 2011, in the amount of \$4,324,000 with the first principal payment due January 1, 2014. The interest rate on the bond is 2.75% and the bonds require annual principal payments and semi-annual interest payments through 2051. Proceeds from the bonds, which mature January 1, 2051, were used to repay the Rural Water note.

**PADUCAH McCracken JOINT SEWER AGENCY  
NOTES TO FINANCIAL STATEMENTS**

**NOTE G – CHANGES IN LONG-TERM LIABILITIES**

Long-term liability activity for the year ended June 30, 2014, was as follows:

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending Balance</u>	<u>Due Within One Year</u>
Long-term liabilities:					
Bonds Payable	\$ 8,924,000	\$ -	\$ (259,500)	\$ 8,664,500	\$ 266,000
Notes payable	<u>9,605,439</u>	<u>3,966,125</u>	<u>(693,883)</u>	<u>12,877,681</u>	<u>717,057</u>
Total long-term liabilities	<u>\$ 18,529,439</u>	<u>\$ 3,966,125</u>	<u>\$ (953,383)</u>	<u>\$ 21,542,181</u>	<u>\$ 983,057</u>

**NOTE H - CONTRIBUTED CAPITAL**

For the years ended June 30, 2014 and 2013, the Agency accepted sewer line extensions valued \$39,875 and \$648,020 for extensions put into service during the year by developers in McCracken County, Kentucky.

**NOTE I – DISCLOSURES REGARDING STATEMENTS OF CASH FLOWS**

**Non-cash Investing and Financing**

	<u>2014</u>	<u>2013</u>
Non-cash investing and financing transactions received during the years ended June 30 as follows:		
Developer contributions	\$ 39,875	\$ 648,020
Loss on abandonment of construction in progress	\$ -	\$ 56,121
Undepreciated costs of assets disposed	\$ 34,078	\$ -
Receivable due from City of Paducah for capital project	\$ 60,929	\$ -

**NOTE J - RISK MANAGEMENT**

The Agency 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. To handle the risk of loss, the Agency participates in a public entity risk pool offered to the members of the Kentucky Municipal Risk Management Association. Participating members pool their funds in order to provide self-insurance, and, when necessary, third-party insurance, against various public liability exposure.

The Agency is responsible for paying annual and supplementary contributions which are determined by the Board that governs the operation of the pool. The contributions are calculated based on actuarial evaluations, ratings plans, and other analyses of the amounts necessary for the payment of claims and losses.

In exchange, the Agency is provided with payment of all claims and losses incurred, subject to certain terms and conditions such as deductibles and coverage limits. Due to the nature of the public entity risk pool established within this policy, the Agency can receive a distribution of surplus funds in the event of excess pool assets or be assessed in the event of pool shortfalls.

**NOTE K - EMPLOYEE RETIREMENT SYSTEM**

The Paducah McCracken Joint Sewer Agency employees participate in the County Employees Retirement System (CERS), a cost-sharing, multi-employer public employee retirement system that provides retirement, disability, and death benefits to members of the plan. Benefits and contribution rates are established by state statute. Under the provisions of Kentucky Revised Statute 61.645, the Board of Trustees of Kentucky Retirement Systems administers the CERS. Kentucky Retirement Systems issues a publicly available financial report that includes financial statements and required supplementary information for CERS. Requests for a copy of the report should be made in writing and submitted to Kentucky Retirement Systems, Perimeter Park West, 1260 Louisville Road, Frankfort, Kentucky 40601.

CERS participants have a fully vested interest after completion of sixty (60) months of service, twelve (12) months of which are current service. At a minimum, terminated employees are refunded their contributions with credited interest at 3 percent compounded annually through June 30, 1981, 6 percent thereafter through June 30, 1986, and 4 percent thereafter. Benefits and contribution rates are established by State statute.

**PADUCAH McCRACKEN JOINT SEWER AGENCY  
NOTES TO FINANCIAL STATEMENTS**

**NOTE K - EMPLOYEE RETIREMENT SYSTEM (Continued)**

CERS covered non-hazardous employees are required to contribute an amount equal to 5.00% of their annual covered salary and 6.00% for all new members hired after August 31, 2009. For the years ended June 30, 2013, 2012 and 2011, the System contributed 18.89%, 19.55%, and 18.96%, respectively, of each non-hazardous employee's creditable compensation. These actuarially determined rates are set by the Board of Trustees of Kentucky Retirement Systems. Total contributions made for the years ended June 30, 2014, 2013 and 2012 were \$362,073, \$342,943 and \$344,320, of which \$285,603, \$271,263 and \$270,111 were made by the employer and \$76,470, \$71,680 and \$74,209 were made by employees, respectively, equal to the required contributions for each year.

**NOTE L – DEFERRED COMPENSATION**

The Agency participates in the Kentucky Public Employees' Deferred Compensation Plan, a self-directed multi-employer 401(k) and 457(b) plan. Under the plan, employees may defer up to 25% of eligible compensation, not to exceed the statutory limits, currently \$16,500.

The Agency made discretionary contributions to the 401(k) plan on behalf of the employees in an amount equal to 5.36% of eligible compensation. Participants are immediately vested in the employer contribution. Employer contributions for the years ended June 30, 2014 and 2013, were \$79,220 and \$74,549, respectively.

**NOTE M - COMMITMENTS AND CONTINGENCIES**

The Agency has entered into a Consent Decree with the Kentucky Environmental and Public Protection Cabinet. The Agency is required to bring combined and sanitary sewer overflows into compliance with Federal and State guidelines. The Agency is bound by the Decree for many years to come and will incur significant costs to bring the system into compliance that can only be determined as solutions to the issues are proposed and approved by the Cabinet as outlined in the Consent Decree. The total cost of complying with this Consent Decree has not been determined, but will be significant.

The following significant contracts in progress represent future construction contractual obligations on executed construction contracts as of June 30, 2014.

	<u>Contract Total</u>	<u>Contract Cost-to-date</u>	<u>Future Commitment</u>
Charter Oak Dr./Cairo Rd Sewer Extension Project	\$ 136,913	\$ -	\$ 136,913
Chickadee Lift Station Elimination	10,980	9,882	1,098
Cook Street Overflow Tank	42,000	-	42,000
Gatewood Lift Station Elimination	14,152	-	14,152
Long Term Control Plan	781,024	757,195	23,829
Massac Creek Ph III Study	19,500	18,526	974
Old Highway 60 Sewer Extension	7,500	3,750	3,750
*Olivet Church Road Sewer Relocation Project	239,761	44,584	195,177
PWWTP Digester Gas Utilization Evaluation	4,000	-	4,000
Sewer Cleaning and Video Inspection Contract #10	124,928	-	124,928
Sewer System Rehabilitation Contract 2014	19,200	17,280	1,920
Wallace Park Combined Sewer Separation Project	3,794,217	252,863	3,541,354
	<u>\$ 5,194,175</u>	<u>\$ 1,104,080</u>	<u>\$ 4,090,095</u>

**PADUCAH McCRACKEN JOINT SEWER AGENCY  
NOTES TO FINANCIAL STATEMENTS**

**NOTE M - COMMITMENTS AND CONTINGENCIES (Continued)**

\* On May 22, 2014, the Agency entered into a reimbursement agreement with the City of Paducah; whereby the City has agreed to reimburse the Agency for all costs associated with this project.

The Agency has entered into an agreement with the City of Paducah to donate a portion of the Wallace Park Sewer Separation project to the City upon completion of the project. This portion of the project was \$578,534 at June 30, 2014 and is classified as an other asset. The project was not near completion at June 30, 2014.

**NOTE N – BOARD DESIGNATED FUNDS**

It is the policy of the current Board of Directors to designate \$135,000 annually for high dollar capital equipment purchases, emergencies or rate stabilization in the event of a loss of substantial revenue stream. The Board's intent is to establish a maximum funding level of \$3 million and a minimum level of \$750 thousand in this fund. Designations of amounts represent tentative management plans and are subject to change. Unrestricted net assets at June 30, 2014 and 2013, consist of the following:

	<b>2014</b>	<b>2013</b>
Designations – high dollar capital equipment emergencies and rate stabilization	\$ 3,000,000	\$ 3,000,000
Undesignated	11,632,798	8,988,289
	<u>\$ 14,632,798</u>	<u>\$ 11,988,289</u>

**NOTE O – INTEREST EXPENSE**

For the years ended June 30, 2014 and 2013, interest expense before adjustment for capitalized construction period interest was \$562,846 and \$475,935, respectively. For the years ended June 30, 2014 and 2013, interest expense of \$116,880 and \$312,701, respectively, was capitalized as part of construction in progress.

**NOTE P – RECENTLY ISSUED ACCOUNTING STANDARDS**

During the year ended June 30, 2012, the Governmental Accounting Standards Board (GASB) issued a new pronouncement that will have a future impact on the Agency. This relates to the recognition of Other Post-Employments Benefits earned by employees whose governmental agency participates in multi-employer, cost-sharing pension plan. The new statement is Statement No. 68, Accounting and Financial Reporting for Pensions, effective for years beginning after June 30, 2014. This GASB statement requires cost-sharing governments to report a net pension liability, pension expense and pension-related deferred inflows and outflows of resources based on their proportionate share of the collective amounts for all the governments in the plan. These amounts are not being calculated for the year ended June 30, 2014, but will likely have a significant impact in the year of implementation.

**NOTE Q – SUBSEQUENT EVENTS**

Management has evaluated subsequent events through September 18, 2014, the date which the financial statements were available to be issued.

**PADUCAH McCracken Joint Sewer Agency  
Notes to Financial Statements**

**NOTE R – Restatement of Net Position for New Pronouncement**

During the year ended June 30, 2014, the Agency implemented Governmental Accounting Standards Board (GASB) Statement No. 65, *Items Previously Reported as Assets and Liabilities*, effective for years beginning after June 15, 2013. Implementation of the new statement resulted in reclassification of certain bond issue costs previously reported as an asset in the Agency’s statement of net position. During fiscal year ended June 30, 2013, the Agency incurred additional bond issue costs and had recorded amortization of prior bond issue costs. The effect of this implementation of this new pronouncement on the 2013 financial statements as follows:

	<b>As Originally Presented</b>	<b>Effect of Restatement</b>	<b>As Restated</b>
<b>STATEMENT OF NET POSITION</b>			
Unamortized bond discount and related costs	\$ 149,605	(\$ 88,992)	\$ 60,613
Total non-current assets	\$ 64,590,301	(\$ 88,992)	\$ 64,501,309
Total assets	\$ 77,610,943	(\$ 88,992)	\$ 77,521,951
Net Position at June 30, 2013	\$ 57,844,791	(\$ 88,992)	\$ 57,755,799
<b>STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET POSITION</b>			
Non-operating expense- amortization	\$ 12,120	(\$ 6,548)	\$ 5,572
Non-operating other income (expense)	\$ 34,479	(\$ 30,927)	\$ 3,552
Change in net position before capital contributions	\$ 695,368	(\$ 24,379)	\$ 670,989
Net Position, beginning	\$ 55,356,423	(\$ 61,613)	\$ 55,294,810
Net Position, ending	\$ 57,844,791	(\$ 88,992)	\$ 57,755,799

**SUPPLEMENTAL INFORMATION**

**PADUCAH McCracken Joint Sewer Agency**  
**STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS**  
**ACTUAL TO BUDGET**  
**For the Year Ended June 30, 2014**

	<b>Original and Final Budget Amounts</b>	<b>Actual Amounts</b>	<b>Variance Favorable (Unfavorable)</b>
<b>Operating Revenues</b>			
Charges for service	\$ 7,038,620	\$ 6,912,425	\$ (126,195)
<b>Operating Expenses</b>			
Salaries and wages	2,295,190	2,247,859	47,331
Chemicals, testing and solid disposal	325,500	333,090	(7,590)
Utilities	681,875	796,724	(114,849)
Materials, supplies and repairs	512,100	365,428	146,672
Fleet expense	135,000	106,181	28,819
Liability insurance	113,000	113,656	(656)
Training, safety and dues	40,825	30,338	10,487
Professional fees	147,500	112,968	34,532
Office expense	15,250	14,424	826
Public education	4,000	750	3,250
Billing and collections	103,000	102,047	953
Bad debts	46,300	59,571	(13,271)
Board of directors expense	16,800	16,800	-
Miscellaneous	22,350	41,856	(19,506)
Depreciation	2,585,500	2,536,013	49,487
	<u>7,044,190</u>	<u>6,877,705</u>	<u>166,485</u>
<b>Operating Income (Loss)</b>	<u>(5,570)</u>	<u>34,720</u>	<u>40,290</u>
<b>Non-operating Revenues (Expenses)</b>			
Investment income	25,000	35,785	10,785
Interest expense	(573,000)	(445,966)	127,034
Amortization	(12,000)	(5,476)	6,524
Gain (loss) on sale of assets	(25,000)	(34,080)	(9,080)
Tap-on and assessment fees	200,000	310,008	110,008
Other, net	19,323	17,976	(1,347)
Total non-operating revenue (expenses), net	<u>(365,677)</u>	<u>(121,753)</u>	<u>243,924</u>
Change in net position before capital contribution:	(371,247)	(87,033)	284,214
<b>Capital Contributions</b>			
Grant revenue	-	3,544	3,544
Contributed capital	-	39,875	39,875
	<u>-</u>	<u>43,419</u>	<u>43,419</u>
<b>Increase (decrease) in net assets</b>	<u>\$ (371,247)</u>	<u>\$ (43,614)</u>	<u>\$ 327,633</u>

See Independent Auditor's Report



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

Board of Directors  
Paducah McCracken Joint Sewer Agency  
Paducah, Kentucky

We have audited in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, the financial statements of the business-type activities of Paducah McCracken Joint Sewer Agency as of and for the year ended June 30, 2014, and the related notes to the financial statements, which collectively comprise Paducah McCracken County Joint Sewer Agency's basic financial statements, and have issued our report thereon dated September 18, 2014.

**Internal Control Over Financial Reporting**

In planning and performing our audit of the financial statements, we considered Paducah McCracken Joint Sewer Agency's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of Paducah McCracken Joint Sewer Agency's internal control. Accordingly, we do not express an opinion on the effectiveness of Paducah McCracken Joint Sewer Agency's internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of Paducah McCracken Joint Sewer Agency'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 over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

**Compliance and Other Matters**

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

**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.

*Kempel CPA Group LLP*

Certified Public Accountants and Consultants  
Paducah, Kentucky  
September 18, 2014

**INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE FOR EACH MAJOR PROGRAM  
AND ON INTERNAL CONTROL OVER COMPLIANCE REQUIRED BY OMB CIRCULAR A-133**

Board of Directors  
Paducah McCracken Joint Sewer Agency  
Paducah, Kentucky

**Report on Compliance for Each Major Federal Program**

We have audited Paducah McCracken Joint Sewer Agency's compliance with the types of compliance requirements described in the OMB Circular A-133 *Compliance Supplement* that could have a direct and material effect on each of Paducah McCracken Joint Sewer Agency's major federal programs for the year then ended June 30, 2014. Paducah McCracken Joint Sewer Agency's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs.

***Management's Responsibility***

Management is responsible for compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs.

***Auditor's Responsibility***

Our responsibility is to express an opinion on compliance for each of Paducah McCracken Joint Sewer Agency's major federal programs based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about Paducah McCracken Joint Sewer Agency's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

We believe that our audit provides a reasonable basis for our opinion on compliance for each major federal program. However, our audit does not provide a legal determination of Paducah McCracken Joint Sewer Agency's compliance.

***Opinion on Each Major Federal Program***

In our opinion, Paducah McCracken Joint Sewer Agency, complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended June 30, 2014.

**Report on Internal Control Over Compliance**

Management of the Paducah McCracken Joint Sewer Agency, is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered Paducah McCracken Joint Sewer Agency's internal control over compliance with the types of requirements that could have a direct and material effect on each major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing our opinion on compliance for each major federal program and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of Paducah McCracken Joint Sewer Agency's internal control over compliance.

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

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

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of OMB Circular A-133. Accordingly, this report is not suitable for any other purpose.

*Kempner CPA Group LLP*

Certified Public Accountants and Consultants  
Paducah, Kentucky  
September 18, 2014

**PADUCAH McCRACKEN COUNTY JOINT SEWER AGENCY  
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS  
FOR THE YEAR ENDED JUNE 30, 2014**

	<u>Federal CFDA Number</u>	<u>Pass Through Grantor's Number</u>	<u>Federal Expenditures</u>
<b>US Environmental Protection Agency</b>			
Passed through Kentucky Infrastructure Authority:			
Capitalization Grants for Clean Water State Revolving Funds	66.458	A12-08	\$ <u>700,634</u>
Total US Environmental Protection Agency			<u>700,634</u>
<b>Total Federal Awards</b>			<u>\$ 700,634</u>

**NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS  
FOR THE YEAR ENDED JUNE 30, 2014**

**NOTE A – BASIS OF PRESENTATION**

The accompanying schedule of expenditures of federal awards includes the federal grant activity of the Paducah McCracken Joint Sewer Agency and is presented on the accrual method of accounting. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of, the basic financial statements.

**NOTE B – RECONCILIATION TO FINANCIAL STATEMENTS**

Total federal award expenditures above	\$ 700,634
Less: Federal award expenditures above applicable to loan program	<u>(700,634)</u>
	-
Other grants	<u>3,544</u>
Total grant revenue per Statement of Revenues, Expenses and Changes in Net Position	<u>\$ 3,544</u>

See Independent Auditor's Report

**PADUCAH McCracken County Joint Sewer Agency  
 SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
 FOR THE YEAR ENDED JUNE 30, 2014**

**Section I – Summary of Auditor’s Results**

1. The auditor’s report expresses an unmodified opinion on the financial statements of the Paducah McCracken County Joint Sewer Agency.
2. No significant deficiencies were disclosed relating to the audit of the financial statements. No material weaknesses are reported.
3. No instances of noncompliance material to the financial statements of the Paducah McCracken County Joint Sewer Agency were disclosed during the audit.
4. No instances of significant deficiencies were disclosed during the audit of internal control over major federal award programs. No material weaknesses are reported.
5. The auditor’s report on compliance for the major federal award programs for the Paducah McCracken County Joint Sewer Agency expresses an unmodified opinion.
6. There were no audit findings that required reporting in accordance with Section 510(a) of OMB Circular A-133 is reported in this schedule.
7. The programs tested as major program include:

<u>Name</u>	<u>CFDA</u>
Capitalization Grants for Clean Water State Revolving Funds	66.458

8. The threshold used for distinguishing Types A and B programs was \$300,000.
9. The Paducah McCracken County Joint Sewer Agency was not determined to be a high-risk auditee.

**Section II – Findings – Financial Statements Audit**

There were no findings in the current year required to be reported.

**Section III – Findings and Questioned Costs – Major Federal Awards Programs**

There were no findings in the current year required to be reported.

**PADUCAH McCracken County Joint Sewer Agency  
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS  
FOR THE YEAR ENDED JUNE 30, 2013**

**Section II – Findings – Financial Statements Audit**

There were no findings reported.

**Section III – Findings and Questioned Costs – Major Federal Awards Programs**

There were no findings or questioned costs.