

RURAL WATER DISTRICT NO. 3
DOUGLAS COUNTY, KANSAS

FINANCIAL STATEMENTS
WITH
SUPPLEMENTAL INFORMATION
DECEMBER 31, 2017 and 2016
TOGETHER WITH INDEPENDENT AUDITOR'S REPORT

RURAL WATER DISTRICT NO. 3, DOUGLAS COUNTY, KANSAS

**FINANCIAL STATEMENTS
DECEMBER 31, 2017 and 2016**

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Independent Auditor's Report

To the Board of Directors
Rural Water District No. 3
Douglas County, Kansas

We have audited the accompanying financial statements of Rural Water District No. 3, Douglas County, Kansas as of and for the years ended December 31, 2017 and 2016, and the related notes to the financial statements, which collectively comprise the District's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the *Kansas Municipal Audit and Accounting Guide*. 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 water district'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 water district's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

Opinion

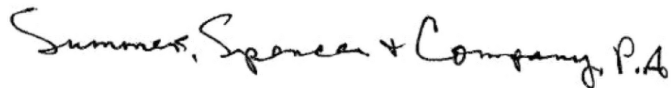
In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Rural Water District No. 3, Douglas County, Kansas, as of December 31, 2017 and 2016, and the changes in its net position and cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters*Required Supplementary Information*

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

Other Information

Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise Rural Water District No. 3, Douglas County Kansas' basic financial statements. The supplemental information on pages 12 – 14 is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information has not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we do not express an opinion or provide any assurance on it.

A handwritten signature in cursive script that reads "Summers, Spencer & Company, P.A.".

Summers, Spencer & Company, P.A.
Topeka, Kansas

February 20, 2018

RURAL WATER DISTRICT NO. 3, DOUGLAS COUNTY, KANSAS

STATEMENTS OF NET POSITION

December 31,	2017	2016
ASSETS		
Current assets		
Cash and cash equivalents	\$ 372,896	\$ 338,935
Certificates of deposit	236,812	235,483
Accounts receivable	200,906	197,926
Prepaid expenses	48,864	48,864
Material inventory	59,208	59,208
<i>Total current assets</i>	<u>918,686</u>	<u>880,416</u>
Long-term assets		
Water rights, net	46,155	54,545
Capital assets, net	10,239,581	11,037,679
<i>Total long-term assets</i>	<u>10,285,736</u>	<u>11,092,224</u>
Restricted assets		
Principal and interest account	237,861	237,468
Bond reserve account	588,393	580,809
<i>Total restricted assets</i>	<u>826,254</u>	<u>818,277</u>
Total assets	<u><u>\$ 12,030,676</u></u>	<u><u>\$ 12,790,917</u></u>
LIABILITIES AND NET POSITION		
Current Liabilities		
Accounts payable	\$ 80,438	\$ 74,042
Accrued payroll and related liabilities	33,753	34,154
Current portion of deferred revenue	5,423	5,423
Current portion of long-term debt	410,000	400,000
Accrued interest	65,475	69,975
<i>Total current liabilities</i>	<u>595,089</u>	<u>583,594</u>
Long-term liabilities		
Long-term debt, less current maturities	<u>5,410,000</u>	<u>5,820,000</u>
Deferred inflows of resources	<u>5,416</u>	<u>10,839</u>
<i>Total liabilities</i>	<u>6,010,505</u>	<u>6,414,433</u>
Net position		
Invested in capital assets, net of related debt		
Tri-District	3,142,224	3,353,889
Other	1,277,357	1,463,790
Restricted		
Tri-District	187,540	140,710
Debt service	760,779	748,302
Unrestricted	652,271	669,793
<i>Total net position</i>	<u>6,020,171</u>	<u>6,376,484</u>
<i>Total liabilities and net position</i>	<u><u>\$ 12,030,676</u></u>	<u><u>\$ 12,790,917</u></u>

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

RURAL WATER DISTRICT NO. 3, DOUGLAS COUNTY, KANSAS
STATEMENTS OF REVENUES, EXPENSES, AND CHANGE IN NET POSITION

For the year ended December 31,	2017	2016
Revenues		
Water sales	\$ 2,138,415	\$ 2,039,893
Fixed cost recovery	123,500	82,250
Other revenue	36,972	9,961
<i>Total operating revenue</i>	<u>2,298,887</u>	<u>2,132,104</u>
Expenses		
Water purchases	37,222	51,044
Salaries, benefits and payroll taxes	474,303	386,876
Chemicals and supplies	234,580	237,962
Meter reading	10,585	9,972
Repairs and maintenance	505,378	262,125
Professional and other services	57,849	109,709
Utilities	189,525	200,376
Insurance	40,304	31,904
Truck and mileage	22,647	16,817
Office supplies and rent	38,508	34,958
Director's fees	13,066	13,250
Dues and fees	15,107	21,667
Depreciation and amortization	931,916	949,862
Other	5,531	9,839
<i>Total expenses</i>	<u>2,576,521</u>	<u>2,336,361</u>
Operating income (loss)	<u>(277,634)</u>	<u>(204,257)</u>
Other revenues (expenses)		
New meters	75,681	90,000
Interest income	9,333	9,263
Interest expense	(160,740)	(171,610)
Gain on capital assets	(2,953)	-
<i>Total other income (expense)</i>	<u>(78,679)</u>	<u>(72,347)</u>
Contributed capital	<u>-</u>	<u>25,000</u>
Change in net position	(356,313)	(251,604)
Net position, beginning of year, as restated	<u>6,376,484</u>	<u>6,628,088</u>
Net position, end of year	<u>\$ 6,020,171</u>	<u>\$ 6,376,484</u>

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

RURAL WATER DISTRICT NO. 3, DOUGLAS COUNTY, KANSAS

STATEMENTS OF CASH FLOWS

For the year ended December 31,	2017	2016
Cash flows from operating activities		
Receipts from customers	\$ 2,253,512	\$ 2,111,384
Payments to suppliers for goods and services	(1,166,859)	(1,036,762)
Payments to employees from payroll	(474,704)	(376,324)
Other operating receipts	36,972	9,961
<i>Net cash provided by operating activities</i>	<u>648,921</u>	<u>708,259</u>
Cash flows from investing activities		
Interest	9,333	9,263
Purchase of investments	(9,306)	(20,421)
<i>Net cash provided by (used in) investing activities</i>	<u>27</u>	<u>(11,158)</u>
Cash flows from capital and related financing activities		
Principal paid on long term capital debt	(400,000)	(385,000)
Interest paid on long term capital debt	(165,240)	(175,770)
Benefit units sold	75,681	90,000
Capital contributions	-	25,000
Proceeds from sale of capital assets	7,682	-
Purchase of capital assets	(133,110)	(267,071)
<i>Net cash used for capital and related financing activities</i>	<u>(614,987)</u>	<u>(712,841)</u>
Net increase (decrease) in cash and cash equivalents	33,961	(15,740)
Cash and cash equivalents, beginning of year	338,935	354,675
Cash and cash equivalents, end of year	<u>\$ 372,896</u>	<u>\$ 338,935</u>
Reconciliation of operating income to net cash provided by operating activities		
Operating loss	\$ (277,634)	\$ (204,257)
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation and amortization	931,916	949,862
Loss on disposal of capital assets	(2,953)	-
(Increase) decrease in operating assets:		
Accounts receivable	(2,980)	(5,336)
Inventory	-	719
Prepaid expenses	-	(32,931)
Increase (decrease) in operating liabilities:		
Accounts payable	6,396	(4,927)
Accrued payroll and related liabilities	(401)	10,552
Deferred revenue	(5,423)	(5,423)
<i>Net cash provided by operating activities</i>	<u>\$ 648,921</u>	<u>\$ 708,259</u>

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

RURAL WATER DISTRICT NO. 3, DOUGLAS COUNTY, KANSAS

NOTES TO THE FINANCIAL STATEMENTS

Note 1 – Financial reporting entity

Rural Water District No. 3, Douglas County, Kansas (the District) was organized on January 11, 1965 by order of the Board of County Commissioners, Douglas County, Kansas. The District, a Kansas municipality, was organized to provide water for residents within the District and is exempt from federal and state income taxes.

In August 1979, the District executed an agreement with Rural Water District No. 5, Osage County, Kansas and Rural Water District No. 8, Shawnee County, Kansas to establish the Tri-District Committee (Tri-District) for purposes of constructing and managing an intake structure, pumping facilities, and a water treatment plant at Clinton Lake in Douglas County, Kansas for the treatment and distribution of water to each of the three districts. The title to all assets and the liability for all financing is in the name of Rural Water District No. 3, Douglas County, Kansas. As such, these financial statement reflect the combined operations of the District and the Tri-District.

The amended Tri-District agreement stipulates that Rural Water District No. 5, Osage County, Kansas is entitled to purchase 30 percent of the treated water for which it agreed to pay 30 percent of the costs of constructing and maintaining the facility, and that Rural Water District No. 8, Shawnee County, Kansas is entitled to purchase 35 percent on the same basis. Rural Water District No. 3, Douglas County, Kansas is entitled to the remaining 35 percent on the same basis.

Management and district legal counsel have determined that the Tri-District Committee does not constitute a legal entity, and therefore, has no power to contract, sue or to be sued. The water right being utilized to take water from Clinton Lake, the plant site, and plant facilities are all presently in the name of the District. Similarly, all obligations for indebtedness are on the District. However, the District would have a right of indemnification against the other two districts pursuant to the Tri-District Committee Agreements.

Management has evaluated subsequent events through February 20, 2018, the date which the financial statements were available to be issued.

Note 2 – Summary of significant accounting policies

Basis of accounting

The financial statements of the District have been prepared using the accrual basis of accounting. Revenues are recognized when they are earned and expenses are recognized when they are incurred.

Cash and cash equivalents

The District considers all unrestricted cash and money market accounts to be cash or cash equivalents. Investments in certificates of deposit are recorded as certificates of deposit and are not included in cash or cash equivalents.

Accounts receivable

Accounts receivable arise from the sale of water and are stated at the unpaid balance. Uncollected water service receivables are recorded at year end. The District considers accounts receivable to be fully collectible; accordingly, no allowance for doubtful accounts is required. In the event accounts become uncollectible, they are charged to operations at the time that determination is made.

Inventory

Inventory consists of miscellaneous parts and is recorded at historical cost.

RURAL WATER DISTRICT NO. 3, DOUGLAS COUNTY, KANSAS

NOTES TO THE FINANCIAL STATEMENTS

Capital assets

Capital assets are recorded at cost. Depreciation is recorded on the straight-line method over the estimated useful lives of the assets as follows:

Office equipment	5-10 years
Plant and equipment	5-40 years

The cost of maintenance and repairs is charged to income as incurred; significant renewals and betterments are capitalized.

Net assets

Net assets comprise the various net earnings from operating income, nonoperating revenues and expenses, and capital contributions. Net assets are classified in the following three components:

Invested in Capital Assets, Net of Related Debt - This component of net assets consists of 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. If there are significant unspent related debt proceeds at year-end, the portion of the debt attributable to the unspent proceeds is not included in the calculation of invested capital assets, net of related debt. Rather, that portion of the debt is included in the same net assets component as the unspent proceeds.

Restricted - This component of net assets consists of constraints imposed by creditors (such as through debt covenants), grantors, contributors or laws or regulations of other governments or constraints imposed by law through constitutional provisions or enabling legislation.

Unrestricted - This component of net assets consists of net assets that do not meet the definition of "restricted" or "invested in capital assets, net of related debt."

Revenue recognition

Operating revenues consist of those revenues that result from the ongoing principal operations of the District and are recognized when earned. Revenues from line extensions and the sale of meters are deferred until the District has completed the line extensions and set the meters.

Compensated absences

The District pays for vacation and sick time. These amounts are expensed in the period when incurred. No accrued vacation is included in these financial statements as the amounts cannot be reasonably estimated.

Use of estimates

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

RURAL WATER DISTRICT NO. 3, DOUGLAS COUNTY, KANSAS

NOTES TO THE FINANCIAL STATEMENTS

Note 3 – Deposits

K.S.A. 9-1401 establishes the depositories which may be used by the District. The statute requires banks eligible to hold the District's funds have a main or branch bank in the county in which the District is located, or in an adjoining county if such institution has been designated as an official depository, and the banks provide an acceptable rate of return on funds. In addition, K.S.A. 9-1402 requires the banks to pledge securities for deposits in excess of FDIC coverage. The District has no other policies that would further limit interest rate risk.

K.S.A. 12-1675 limits the District's investment of idle funds to time deposits, open accounts, and certificates of deposit with allowable financial institutions; U.S. Government securities; temporary notes; no-fund warrants; repurchase agreements; and the Kansas Municipal Investment Pool. The District has no investment policy that would further limit its investment choices.

At December 31, 2017 and 2016, the bank balance of the District's deposits were covered by federal deposit insurance and the balance by pledged securities with a market value of approximately \$1,742,463 and \$1,399,564, respectively, held by third parties.

Note 4 – Capital assets

Capital assets, together with activity for the year ended December 31, 2017 and 2016 consisted of the following:

	2016	Additions	Reductions	Reclassifications	2017
Capital Assets:					
Land	\$ 204,758	\$ 15,528	\$ -	\$ -	\$ 220,286
Water sytem	14,429,553	6,000	(1,202,681)	-	13,232,872
Furniture and equipment	279,595	-	(36,600)	(68,485)	174,510
Tri-District water system	9,731,395	48,393	(254,578)	-	9,525,210
Vehicles	25,200	63,189	-	68,485	156,874
	24,670,501	133,110	(1,493,859)	-	23,309,752
Less: Depreciation	(13,632,822)	(923,526)	1,486,177	-	(13,070,171)
Net capital assests	<u>\$ 11,037,679</u>	<u>\$ (790,416)</u>	<u>\$ (7,682)</u>	<u>\$ -</u>	<u>\$ 10,239,581</u>

	2015	Additions	Reductions	2016
Capital Assets:				
Land	\$ 204,758	\$ -	\$ -	\$ 204,758
Capital improvements	14,359,482	70,071	-	14,429,553
Furniture and equipment	273,395	6,200	-	279,595
Tri-District water system	9,563,229	168,166	-	9,731,395
Vehicles	3,200	22,000	-	25,200
	24,404,064	266,437	-	24,670,501
Less: Depreciation	(12,691,973)	(940,849)	-	(13,632,822)
Net capital assests	<u>\$ 11,712,091</u>	<u>\$ (674,412)</u>	<u>\$ -</u>	<u>\$ 11,037,679</u>

Depreciation and amortization expense for the years ended December 31, 2017 and 2016 is \$931,916 and \$949,862, respectively.

RURAL WATER DISTRICT NO. 3, DOUGLAS COUNTY, KANSAS

NOTES TO THE FINANCIAL STATEMENTS

Note 5 – Long-term debt

Long-term debt consists of Water System Revenue Bonds, payable in semi-annual payments from utility revenues and secured by these revenues, set to mature August 1, 2029.

The following is a detailed listing of the District's long-term debt:

<u>Debt Issue</u>	<u>Date Issued</u>	<u>Original Amount</u>	<u>Interest Rate</u>
Revenue Bonds	5/16/2013	\$7,525,000	2.9%

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

	<u>Beginning Principal Balance</u>	<u>Additions to Principal</u>	<u>Reductions of Principal</u>	<u>Ending Principal Outstanding</u>
Revenue Bonds	\$ 6,220,000	\$ -	\$ 400,000	\$ 5,820,000

The following is a summary of changes in long-term debt for the year ended December 31, 2016:

	<u>Beginning Principal Balance</u>	<u>Additions to Principal</u>	<u>Reductions of Principal</u>	<u>Ending Principal Outstanding</u>
Revenue Bonds	\$ 6,605,000	\$ -	\$ 385,000	\$ 6,220,000

The annual debt service requirements to maturity for bonded debt as of December 31, 2017 is as follows:

<u>Year Ending December 31,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2018	\$ 410,000	154,373	564,373
2019	420,000	143,235	563,235
2020	430,000	131,828	561,828
2021	445,000	120,150	565,150
2022-2026	2,400,000	413,303	2,813,303
2026-2029	<u>1,715,000</u>	<u>84,848</u>	<u>1,799,848</u>
	<u>\$ 5,820,000</u>	<u>\$ 1,047,737</u>	<u>\$ 6,867,737</u>

The District has certain loan covenants within the bond resolution requiring total revenue available for debt service, as defined in the bond agreement, of at least 110% of debt requirements. This requirement was met for the years ended December 31, 2017 and 2016, respectively. The District last approved a rate increase effective March 1, 2010.

Interest expense on long-term debt totaled \$160,740 and \$171,610 for the year ended December 31, 2017 and 2016 respectively.

RURAL WATER DISTRICT NO. 3, DOUGLAS COUNTY, KANSAS

NOTES TO THE FINANCIAL STATEMENTS

Note 6 – Retirement plan

The District maintains a defined contribution plan covering all eligible employees. The District contributes seven percent of the employee's gross wages to the plan on a monthly basis. Employees are eligible for plan participation once they have reached 21 years of age and have been employed for more than one year. For the year ended December 31, 2017 and 2016, retirement plan expense was \$23,374 and \$11,948 respectively.

Note 7 – Water purchase contracts

On December 13, 1979, the District entered into a water purchase contract with the Kansas Water Resource Board to withdraw water from Clinton Lake. The contract is for 40 years and allows the District to withdraw a maximum of 720.0 million gallons of raw water each year.

Effective December 13, 1989, the price of water increased to \$0.1753 per each one-thousand gallons withdrawn. However, the District's contract was negotiated under statutes that limited the charge to no less than \$0.05 and no more than \$0.10 per one-thousand gallons. Therefore, the adjusted rate for water under the contract will be \$0.10 per one thousand gallons for the period December 13, 1989 through December 13, 2019.

Note 8 – Concentration of credit risk

The District is engaged in the sale of water to customers located in an area around Douglas County, Kansas. The District grants credit to those customers and requires no collateral.

Note 9 – Statutory compliance

The district is required to remit bond principal and interest payments to the state fiscal agent at least 20 days before the day of maturity or any bonds, or the interest thereon per K.S.A. 10-130. The district has been notified they are in violation of this statute in 2017.

SUPPLEMENTAL INFORMATION

RURAL WATER DISTRICT NO. 3
INSURANCE COVERAGE

Property Covered	Premium	Coverage	Expiration date
RURAL WATER DISTRICT NO.3			
Commercial property: (9A5-76-22-17) All locations	\$ 14,145	90% Coinsurance 2,443,587	6/2/2018
General liability: (9D5-76-22-17) Aggregate Limit - products/completed operations other than products/completed ops Personal and advertising injury Medical expense (per person)	\$ 2,114	 1,000,000 1,000,000 500,000 5,000	6/2/2018
Commercial Auto: (9E5-76-22-17) Liability insurance (per loss)	\$ 1,272	 500,000	6/2/2018
Worker's compensation: (9H5-76-22-17) Bodily injury by accident Bodily injury by disease (per employee) Bodily injury by disease (policy limit)	\$ 5,034	 500,000 500,000 500,000	6/2/2018
Public Employee Dishonesty: (9FS-76-22-17) Per loss	\$ 503	 450,000	6/2/2018
Directors' and Officers' Liability: (9K5-76-22-17)	\$ 2,667	1,000,000	6/2/2018
Commercial Inland Marine: (9M5-76-22-17) Contractor Equipment	\$ 225	 108,000	6/2/2018

RURAL WATER DISTRICT NO. 3
INSURANCE COVERAGE

<u>Property Covered</u>	<u>Premium</u>	<u>Coverage</u>	<u>Expiration date</u>
TRI-DISTRICT			
Commercial property: (9A5-39-69-17)	\$ 11,523	90% Coinsurance	4/10/2018
Building and personal property		6,701,118	
Loss of income		50% Coinsurance	
		100,000	
General liability: (9D5-39-69-17)	\$ 2,495		4/10/2018
Aggregate Limit -			
products/completed operations		1,000,000	
other than products/completed ops		1,000,000	
Personal and advertising injury		500,000	
Medical expense (per person)		5,000	
Inland Marine: (9C5-39-69-17)	\$ 536		4/10/2018
Hardware		10,000	
Programs, applications and media		7,500	
Property in-transit or off premise		20,300	
Commercial Auto: (9E5-39-69-17)	\$ 956		4/10/2018
Liability insurance (per loss)		500,000	

RURAL WATER DISTRICT NO. 3
CUSTOMERS SERVED
DECEMBER 31, 2017

	<u>Beginning of the year</u>	<u>End of the year</u>
Number of meters	1,860	1,869
Estimated number of customers served	4,650	4,673