

**RURAL WATER DISTRICT NO. 3  
BUTLER COUNTY, KANSAS**

Independent Auditors' Report and  
Financial Statement with  
Supplementary Information

For the Year Ended  
December 31, 2014

**RURAL WATER DISTRICT NO. 3**  
Butler County, Kansas

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**JARRED, GILMORE & PHILLIPS, PA**  
CERTIFIED PUBLIC ACCOUNTANTS

**INDEPENDENT AUDITORS' REPORT**

Board of Directors  
Rural Water District No. 3  
Butler County, Kansas

We have audited the accompanying fund summary statement of regulatory basis receipts, expenditures, and unencumbered cash balances of Rural Water District No. 3, Butler County, Kansas, as of and for the year ended December 31, 2014, and the related notes to the financial statement.

***Management's Responsibility for the Financial Statement***

Management is responsible for the preparation and fair presentation of this financial statement in accordance with the Kansas Municipal Audit and Accounting Guide as described in Note 1 to meet the financial reporting requirements of the State of Kansas; this includes determining that the regulatory basis of accounting is an acceptable basis for the preparation of the financial statement in the circumstances. Management is also responsible for the design, implementation and maintenance of internal control relevant to the preparation and fair presentation of the financial statement that is free from material misstatement, whether due to fraud or error.

***Auditors' Responsibility***

Our responsibility is to express an opinion on the financial statement based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America, and the Kansas Municipal Audit and Accounting Guide. Those standards require we plan and perform the audit to obtain reasonable assurance about whether the financial statement is free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statement. The procedures selected depend on auditors' judgment, including the assessment of the risks of material misstatement of the financial statement, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the District's preparation and fair presentation of the financial statement 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 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 statement.

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

***Basis for Adverse Opinion on U.S. Generally Accepted Accounting Principles***

As described in Note 1 of the financial statement, the financial statement is prepared by Rural Water District No. 3, Butler County, Kansas to meet the requirements of the State of Kansas on the basis of the financial reporting provisions of the Kansas Municipal Audit and Accounting Guide, which is a basis of accounting other than accounting principles generally accepted in the United States of America.

The effects on the financial statement of the variances between the regulatory basis of accounting described in Note 1 and accounting principles generally accepted in the United States of America, although not reasonably determinable, are presumed to be material.

***Adverse Opinion on U.S. Generally Accepted Accounting Principles***

In our opinion, because of the significance of the matter discussed in the “Basis for Adverse Opinion on U.S. Generally Accepted Accounting Principles” paragraph, the financial statement referred to above does not present fairly, in conformity with accounting principles generally accepted in the United States of America, the financial position of Rural Water District No. 3, Butler County, Kansas as of December 31, 2014, or changes in financial position and cash flows thereof for the year then ended.

***Opinion on Regulatory Basis of Accounting***

In our opinion, the financial statement referred to above presents fairly, in all material respects, the aggregate cash and unencumbered cash balance of Rural Water District No. 3, Butler County, Kansas as of December 31, 2014, and the aggregate receipts and expenditures for the year then ended in accordance with the financial reporting provisions of the Kansas Municipal Audit and Accounting Guide described in Note 1.

***Report on Supplementary Information***

Our audit was conducted for the purpose of forming an opinion on the fund summary statement of regulatory basis receipts, expenditures, and unencumbered cash balances (basic financial statement) as a whole.

The individual fund schedule of regulatory basis receipts and expenditures-actual (Schedule 1 as listed in the table of contents) is presented for analysis and is not a required part of the basic financial statement, however is required to be presented under the provisions of the Kansas Municipal Audit and Accounting Guide. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statement. The information has been subjected to the auditing procedures applied in the audit of the basic financial statement and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statement or to the basic financial statement itself, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the basic financial statement as a whole, on the basis of accounting described in Note 1.

The Schedule of Insurance (Schedule 2 as listed in the table of contents) has not been subjected to the auditing procedures applied in the audit of the basic financial statement and, accordingly, we do not express an opinion or provide any assurance on it.

The 2013 Actual column presented in the individual fund schedules of regulatory basis receipts and expenditures – actual (Schedule 1 as listed in the table of contents) is also presented for comparative analysis and is not a required part of the 2014 basic financial statement upon which we rendered an unmodified opinion dated March 6, 2014. The 2013 basic financial statement and our accompanying report are not presented herein, but are available in electronic form from the web site of the Kansas Department of Administration at the following link <http://da.ks.gov/ar/muniserv/>. Such 2013 comparative information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the 2013 basic financial statement. The 2013 comparative information was subjected to the auditing procedures applied in the audit of the 2013 basic financial statement and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the 2013 basic financial statement or to the 2013 basic financial statement itself, and other additional procedures in accordance with auditing standards generally accepted in the United

States of America. In our opinion, the 2013 comparative information is fairly stated in all material respects in relation to the 2013 basic financial statement as a whole, on the basis of accounting described in Note 1.

*Jarred, Gilmore & Phillips, PA*

JARRED, GILMORE & PHILLIPS, PA  
Certified Public Accountants

February 27, 2015  
Chanute, Kansas

**Statement 1**

**RURAL WATER DISTRICT NO. 3**

Butler County, Kansas

Summary Statement of Receipts, Expenditures, and Unencumbered Cash

Regulatory Basis

For the Year Ended December 31, 2014

Funds	Beginning		Expenditures	Ending		Ending Cash December 31, 2014
	Unencumbered Cash Balance	Receipts		Unencumbered Cash Balance	Add Encumbrances and Accounts Payable	
Special Purpose Funds:						
Capital Improvements	\$ -	\$ 77,000.00	\$ 18,264.17	\$ 58,735.83	\$ 1,950.00	\$ 60,685.83
Business Funds:						
Water Utility	529,339.30	458,312.91	409,440.37	578,211.84	25,074.33	603,286.17
Total Reporting Entity	<u>\$ 529,339.30</u>	<u>\$ 535,312.91</u>	<u>\$ 427,704.54</u>	<u>\$ 636,947.67</u>	<u>\$ 27,024.33</u>	<u>\$ 663,972.00</u>
Composition of Cash:						
Community National Bank:						
Change Fund .....						\$ 50.00
Checking Account .....						5,417.17
Savings Account.....						446,557.34
Certificates of Deposit.....						211,947.49
Total Cash and Investments .....						<u>\$ 663,972.00</u>

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

**RURAL WATER DISTRICT NO. 3**  
Butler County, Kansas

Notes to Financial Statement  
For the Year Ended December 31, 2014

**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

Financial Reporting Entity

Rural Water District No. 3, Butler County, Kansas (the District) was organized under Kansas law and provides water to rural Butler County in Kansas. Rural Water District No. 3, Butler County, Kansas, is a municipal corporation governed by an elected six-member board.

*Related Municipal Entities:* A related municipal entity is determined by the following criteria. Whether the District exercises oversight responsibility on financial interdependency, selection of governing authority, designation of management, ability to significantly influence operations and accountability for fiscal matters, scope of the public service, and significant operational or financial relationships with the District. Related municipal entities are not required to be included in the District's audit by the Kansas Municipal Audit and Accounting Guide (KMAAG).

The District has determined that no outside agency meets the above criteria and, therefore, no outside agency has been included as a related municipal entity in the financial statement.

Regulatory Basis Fund Types

A fund is defined as an independent fiscal and accounting entity with a self-balancing set of accounts recording cash and other financial resources, together with all related liabilities and residual equities or balances, and changes therein, which are segregated for the purpose of carrying on specific activities or attaining certain objectives in accordance with special regulations, restrictions, or limitations.

The following types of funds comprise the financial activities of the Rural Water District No. 3, Butler County, Kansas for the year of 2014:

Business fund – funds financed in whole or in part by fees charged to users of the goods or services (i.e. enterprise and internal service fund etc.)

Special purpose fund – used to account for the proceeds of specific tax levies and other specific revenue sources (other than Capital Project and tax levies for long-term debt) that are intended for specified purposes.

Basis of Accounting

*Regulatory Basis of Accounting and Departure from Accounting Principles Generally Accepted in the United States of America.* The Kansas Municipal Audit and Accounting Guide (KMAAG) regulatory basis of accounting involves the recognition of cash, cash equivalents, marketable investments, and certain accounts payable and encumbrance obligations to arrive at a net unencumbered cash and investments balance on a regulatory basis for each fund, and the reporting of changes in unencumbered cash and investments of a fund resulting from the difference in regulatory basis receipts and regulatory basis expenditures for the fiscal year. All recognized assets and liabilities are measured and reported at cost, unless they have been permanently impaired and have no future cash value or represent no future obligation against cash. The KMAAG regulatory basis does not recognize capital assets, long-term debt, accrued receivables and payables, or any other assets, liabilities or deferred inflows or outflows, other than those mentioned above.

## **1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

### Basis of Accounting (Continued)

The District has approved a resolution that is in compliance with K.S.A. 75-1120a(c), waiving the requirement for application of generally accepted accounting principles and allowing the municipality to use the regulatory basis of accounting.

### Reimbursed Expenses

K.S.A. 79-2934 provides that reimbursed expenditures, in excess of those budgeted, should be recorded as reductions in expenditures rather than as revenues. In the financial statement comparisons presented in this report, reimbursements and refunds follow these guidelines.

### Income Tax Status

Rural Water District No. 3, Butler County, Kansas is recognized by the Internal Revenue Service as a quasi-municipal corporation under K.S.A. 88a-616, and is exempt from Federal and Kansas income taxes. Accordingly, this financial statement does not present a provision for income taxes.

### Budgetary Information

Rural water districts are not subject to Kansas statutes requiring a legally adopted budget.

## **2. STEWARDSHIP, COMPLIANCE, AND ACCOUNTABILITY**

### Compliance with Kansas Statutes

Statement 1 is designed to show compliance with the cash basis laws of Kansas. As shown in Statement 1, the District was in apparent compliance with the cash basis laws of Kansas.

## **3. DEPOSITS AND INVESTMENTS**

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 branch 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.

*Concentration of credit risk.* State statutes place no limit on the amount the District may invest in any one issuer as long as the investments are adequately secured under K.S.A. 9-1402 and 9-1405.

*Custodial credit risk – deposits.* Custodial credit risk is the risk that in the event of a bank failure, the District's deposits may not be returned to it. State statutes require the District's deposits in financial institutions to be entirely covered by federal depository insurance or by collateral held under a joint custody receipt issued by a bank within the State of Kansas, the Federal Reserve Bank of Kansas City, or the Federal Home Loan Bank of Topeka.



### **3. DEPOSITS AND INVESTMENTS** (Continued)

At December 31, 2014, the District's carrying amount of deposits was \$663,922.00 and the bank balance was \$664,567.88. The bank balance was held by one bank resulting in a concentration of credit risk. Of the bank balance, \$250,000.00 was covered by federal depository insurance and \$414,567.88 was collateralized with securities held by the pledging financial institutions' agents in the District's name.

### **4. RISK MANAGEMENT**

The District is exposed to various risks of loss related to torts; theft of, damage to, or destruction of assets, errors and omissions; injuries to employees; employees' health and life; and natural disasters. The District manages these risks of loss through the purchase of various insurance policies.

### **5. OTHER LONG-TERM OBLIGATIONS FROM OPERATIONS**

All full-time employees are allotted two weeks of vacation after one year of service and three weeks after two years of service. Up to fifteen days may be rolled over to the new year. Any days not rolled over will be paid out at the end of year. At no time may more than 30 days be accumulated.

A liability should be accrued for compensated absences which meet the following criteria:

1. The District's obligation relating to employees' rights to receive compensation for future absences is attributable to employees' services already rendered.
2. The obligation relates to rights that vest or accumulate.
3. Payment of the compensation is probable.
4. The amount can be reasonably estimated.

In accordance with the above criteria, the District has not estimated a liability for personal leave at December 31, 2014 as there was none.

As provided by K.S.A. 12-5040, the District allows retirees to participate in the group health insurance plan. While each retiree pays the full amount of the applicable premium, conceptually, the District is subsidizing the retirees because each participant is charged a level of premium regardless of age. However, the cost of this subsidy has not been quantified in these financial statements.

Under the Consolidated Omnibus Budget Reconciliation Act (COBRA), the District makes health care benefits available to eligible former employees and eligible dependents. Certain requirements are outlined by the Federal government for this coverage. The premium is paid in full by the insured. There is no cost to the District under this program.

### **6. ECONOMIC DEPENDENCY**

Currently, the District purchases its water from Public Wholesale Water Supply District No. 8. To continue serving its patrons, the District is dependent upon Public Wholesale Water Supply District No. 8 to provide adequate, reasonably priced water. All water sales are made to residents in the area of the District. Accordingly, the District's operations are dependent upon the ability to purchase water from Public Wholesale Water Supply District No. 8.

**7. CONCENTRATION OF RISK**

The District sells water to the City of Cassody, along with their residential customers. In 2014 the District sold 12.29% of their sales to the City.

**8. RELATED PARTY TRANSACTIONS**

All board members of the District are benefit unit owners and customers.

**9. NUMBER OF CUSTOMERS SERVED**

Customers served December 31, 2013	608
Customers served December 31, 2014	611

**10. INTERFUND TRANSFERS**

Operating and residual transfers were as follows:

<u>From Fund:</u>	<u>To Fund:</u>	<u>Statutory Authority</u>	<u>Amount</u>
Water Utility	Capital Improvements	K.S.A. 12-825d	\$ 65,000.00

**11. SUBSEQUENT EVENTS**

There were no subsequent events requiring recognition in the financial statement. Additionally, there were no nonrecognized subsequent events requiring disclosure.

## **SUPPLEMENTARY INFORMATION**

**RURAL WATER DISTRICT NO. 3**

Butler County, Kansas

**CAPITAL IMPROVEMENTS FUND**

Schedule of Receipts and Expenditures - Actual

Regulatory Basis

For the Year Ended December 31, 2014

(With Comparative Actual Totals for the Prior Year Ended December 31, 2013)

	Prior Year Actual	Current Year Actual	
Receipts			
Use of Money and Property			
Benefit Units Sold	\$ 15,000.00	\$ 12,000.00	
Other Revenues			
Reimbursed Expense	1,848.54	-	
Operating Transfers from:			
Water Utility Fund	20,479.68	65,000.00	
	37,328.22	77,000.00	
Total Receipts			
Expenditures			
Improvements			
Capital Outlay	99,236.75	18,264.17	
	99,236.75	18,264.17	
Total Expenditures			
Receipts Over(Under) Expenditures	(61,908.53)	58,735.83	
Unencumbered Cash, Beginning	61,908.53	-	
	\$ -	\$ 58,735.83	
Unencumbered Cash, Ending			

**RURAL WATER DISTRICT NO. 3**

Butler County, Kansas

**WATER UTILITY FUND**

Schedule of Receipts and Expenditures - Actual

Regulatory Basis

For the Year Ended December 31, 2014

(With Comparative Actual Totals for the Prior Year Ended December 31, 2013)

	Prior Year Actual	Current Year Actual	
Receipts			
Operating Revenues			
Water Sales	\$ 437,693.35	\$ 453,912.65	
Transfer Fees	900.00	1,252.18	
Use of Money and Property			
Interest Income	1,970.35	1,583.69	
Dividends	1,625.86	1,564.39	
	442,189.56	458,312.91	
Total Receipts			
Expenditures			
Utility Operations			
Operating Expenditures			
Personal Services	101,058.97	99,580.65	
Contractual Services	74,802.38	60,734.47	
Commodities	173,628.08	184,125.25	
Operating Transfers to:			
Capital Improvement Fund	20,479.68	65,000.00	
	369,969.11	409,440.37	
Total Expenditures			
Receipts Over(Under) Expenditures	72,220.45	48,872.54	
Unencumbered Cash, Beginning	457,118.85	529,339.30	
Unencumbered Cash, Ending	\$ 529,339.30	\$ 578,211.84	

## RURAL WATER DISTRICT NO. 3

Butler County, Kansas

## Schedule of Insurance Coverage

December 31, 2014

	<u>Date Expires</u>	<u>Amount</u>
Commercial General Liability Schedule:		
Annual aggregate, Other Than Products	6/9/2015	\$ 2,000,000
Annual aggregate, Products & Complete Operations	6/9/2015	2,000,000
Personal and Advertising Injury	6/9/2015	1,000,000
Damage to Rented Premises	6/9/2015	100,000
Medical Expense Limit (any one person)	6/9/2015	5,000
Buildings and Business Personal Property:		
Building and Pump, including equipment (Location #1)	6/9/2015	56,672
Stand Pipe, including equipment (Location #1)	6/9/2015	123,202
Stand Pipe, including equipment (Location #2)	6/9/2015	123,202
Pump station, including equipment (Location #3)	6/9/2015	56,672
Pump station, including equipment (Location #5)	6/9/2015	43,122
Office contents (Location #6)	6/9/2015	20,000
Coinsurance is 90% with a \$500 deductible per occurrence; policy includes replacement cost coverage		
Equipment Floater		
Scheduled Equipment (\$250 deductible)	6/9/2015	19,500
Computers (\$500 deductible)	6/9/2015	2,700
Coinsurance is 80% with a deductible per occurrence policy includes replacement cost coverage on computers		
Workers' Compensation:		
Bodily Injury by Accident	6/9/2015	500,000
Bodily Injury by Disease (Each employee)	6/9/2015	500,000
Bodily Injury by Disease (Policy limit)	6/9/2015	500,000
Public Official Errors & Omissions		
General aggregate limit	6/9/2015	1,000,000
Each Loss (Limit of Liability)	6/9/2015	500,000
Deductible per loss	6/9/2015	1,500
Data Breach		
General aggregate limit	6/9/2015	50,000
Deductible per loss	6/9/2015	1,000
Non-owned/Hired Auto		
Each Loss (Limit of Liability)	6/9/2015	1,000,000
Commercial Auto		
Liability	6/9/2015	1,000,000
Comprehensive (\$500 deductible)	6/9/2015	N/A
Collision (\$500 deductible)	6/9/2015	N/A
Public Employee Dishonesty		
Each Loss (\$1,000 deductible)	8/28/2015	250,000



Board of Directors  
Rural Water District No. 3  
Butler County, Kansas

In planning and performing our audit of the financial statement of Rural Water District No. 3, Butler County, Kansas as of and for the year ended December 31, 2014, in accordance with auditing standards generally accepted in the United States of America, we considered Rural Water District No. 3, Butler County, Kansas' internal control over financial reporting (internal control) as a basis for designing audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statement, but not for the purpose of expressing an opinion on the effectiveness of the Rural Water District No. 3, Butler County, Kansas' internal control. Accordingly, we do not express an opinion on the effectiveness of the Rural Water District No. 3, Butler County, Kansas' internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore material weaknesses or significant deficiencies may exist that were not identified. However, as discussed below, we identified certain deficiencies in internal control that we consider to be material weaknesses.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A material weakness is a deficiency or a combination of deficiencies in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected, on a timely basis. We consider the following deficiencies in Rural Water District No. 3, Butler County, Kansas' internal control to be material weaknesses:

#### Preparation of Financial Statement

Accounting standards states the client must be able to accept responsibility and be able to identify a material misstatement when reviewing the financial statement, including footnotes and supplemental information. This would also include knowing if a required footnote disclosure was missing or not correctly stated. Presently, the District staff does not have the ability to process and prepare the required financial statement, including footnotes. The potential effects of this material weakness could be unrecognized errors on the financial statement. While we recognize that this condition is not unusual for a district your size, it is important that you be aware of this condition for financial reporting purposes. Management and the Board should continually be aware of the financial reporting of the District and changes in reporting requirements.

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Jarred, Gilmore & Phillips, PA  
CERTIFIED PUBLIC ACCOUNTANTS

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Segregation of Duties

An internal control structure is, quite simply, the procedures and policies in effect which ensure that the District's financial activity is properly recorded, processed, summarized, and reported in the financial statements. A weakness in the control structure occurs when one person is responsible for all of the accounting activities such as performing billings, receipting cash, making deposits, reconciling the bank accounts, and having access to all books and records of the District. Due to small staff size, it is not possible for reviews of daily work to take place, potentially resulting in errors in financial records and reports.

This communication is intended solely for the information and use of management, Board of Directors, and others within the District, and is not intended to be, and should not be, used by anyone other than these specified parties.



JARRED, GILMORE & PHILLIPS, PA  
Certified Public Accountants

February 27, 2015  
Chanute, Kansas