

**AUDITED FINANCIAL STATEMENTS  
AND OTHER FINANCIAL INFORMATION**

of

**LINCOLN COUNTY BOARD OF PUBLIC UTILITIES  
FAYETTEVILLE, TENNESSEE**

June 30, 2014

# LINCOLN COUNTY BOARD OF PUBLIC UTILITIES

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**INDEPENDENT AUDITORS' REPORT**

Lincoln County Board of Public Utilities  
Fayetteville, Tennessee

**Report on the Financial Statements**

We have audited the accompanying financial statements of the Lincoln County Board of Public Utilities (the "Board"), an enterprise fund of Lincoln County, Tennessee, as of and for the year ended June 30, 2014, and the related notes to the financial statements, as listed in the table of contents.

*Management's Responsibility for the Financial Statements*

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

*Auditors' Responsibility*

Our responsibility is to express an opinion on these financial statements based on our 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 opinion.

*Opinion*

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Lincoln County Board of Public Utilities as of June 30, 2014, and the changes in financial position and cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

*Emphasis of Matter*

As discussed in Note A, the financial statements present only the Lincoln County Board of Public Utilities and do not purport to, and do not, present fairly the financial position of Lincoln County, Tennessee as of June 30, 2014, the changes in its financial position, or, where applicable, its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

## *Other Matters*

### *Required Supplementary Information*

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

Accounting principles generally accepted in the United States of America require that the schedule of funding progress on page 17 be presented to supplement the financial statements. Such information, although not a part of the financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the 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 financial statements, and other knowledge we obtained during our audit of the 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*

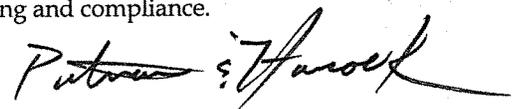
Our audit was conducted for the purpose of forming an opinion on the financial statements taken as a whole. The accompanying supplementary information as listed in the table of contents is presented for purposes of additional analysis and is not a required part of the financial statements of the Lincoln County Board of Public Utilities. The accompanying schedule of expenditures of federal awards on pages 24-25, as required by the Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, is also presented for purposes of additional analysis and is not a required part of the financial statements.

The supplementary information and the schedule of expenditures of federal awards are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the financial statements. The 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 information is fairly stated in all material respects in relation to the financial statements taken as a whole.

The other information, as listed in the table of contents, has not been subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we do not express an opinion or provide any assurance on them.

### *Other Reporting Required by Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated October 15, 2014 on our consideration of the Lincoln County Board of Public Utilities' internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Lincoln County Board of Public Utilities' internal control over financial reporting and compliance.



**LINCOLN COUNTY BOARD OF PUBLIC UTILITIES**

**STATEMENT OF NET POSITION**

June 30, 2014

ASSETS

CURRENT ASSETS

Cash and cash equivalents for general use	\$	3,673,961
Accounts receivable:		
Customers, net of allowance for uncollectible accounts \$2,200		239,665
Other receivables		75,395
Materials and supplies inventory		108,067
Prepaid expenses		29,863
Total Current Assets		4,126,951

SPECIAL FUNDS

289,474

WATER PLANT AND EQUIPMENT:

Water plant, buildings and equipment		37,460,337
Construction in progress		2,456,073
Less accumulated depreciation		(15,713,208)
		24,203,202

OTHER ASSETS

Deposits		750
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TOTAL ASSETS

28,620,377

LIABILITIES AND NET POSITION

CURRENT LIABILITIES

Current maturities of long-term debt payable from current assets		225,802
Accounts payable		167,776
Advance payments from developers		25,800
Customer deposits		11,950
Accrued interest		16,331
Accrued leave		9,704
Accrued liabilities		55,809
Total Current Liabilities		513,172

LONG-TERM LIABILITIES

Bonds payable		11,764,265
Less current maturities		(225,802)
		11,538,463

TOTAL LIABILITIES

12,051,635

NET POSITION

Net investment in capital assets		12,438,937
Restricted for debt service		277,524
Unrestricted		3,852,281
Total Net Position	\$	16,568,742

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

**LINCOLN COUNTY BOARD OF PUBLIC UTILITIES**  
**STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET POSITION**

Year Ended June 30, 2014

<b>OPERATING REVENUES</b>	
Water sales (net of provision for bad debts of \$35,630)	\$ 4,180,497
Penalties, service charges, and other	253,913
Connection fees	104,850
<b>TOTAL OPERATING REVENUES</b>	<u>4,539,260</u>
<b>OPERATING EXPENSES</b>	
Salaries and wages	1,031,263
Employee taxes and benefits	370,712
Water purchases	507,463
Water plant repair and maintenance	142,332
Utilities	301,647
Vehicle and equipment	125,773
Connection materials	18,775
Insurance	129,397
Professional fees	26,455
Water chemicals and testing	68,992
Office supplies	48,307
Postage	33,166
Telephone	27,498
Advertising	5,876
Miscellaneous	44,745
Provision for depreciation	928,141
<b>TOTAL OPERATING EXPENSES</b>	<u>3,810,542</u>
<b>INCOME FROM OPERATIONS</b>	728,718
<b>NONOPERATING REVENUES AND (EXPENSE)</b>	
Interest income	1,357
Interest expense	(403,262)
Debt issuance costs	(2,600)
<b>NONOPERATING REVENUES (EXPENSE) - NET</b>	<u>(404,505)</u>
<b>INCOME BEFORE CAPITAL GRANTS</b>	324,213
Capital grants	684,401
<b>CHANGE IN NET POSITION</b>	1,008,614
Total Net Position, at beginning of year	<u>15,560,128</u>
<b>TOTAL NET POSITION, AT END OF YEAR</b>	<u>\$ 16,568,742</u>

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

**LINCOLN COUNTY BOARD OF PUBLIC UTILITIES**  
**STATEMENT OF CASH FLOWS**  
Year Ended June 30, 2014

CASH FLOWS FROM OPERATING ACTIVITIES:

Receipts from customers and users	\$ 4,475,416
Payments to suppliers and others	(1,868,583)
Payments to employees	<u>(1,029,125)</u>
NET CASH PROVIDED BY OPERATING ACTIVITIES	<u>1,577,708</u>

CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES:

Additions to capital assets, net	(2,255,854)
Capital grants received	684,401
Principal advances on bond anticipation notes	1,632,555
Borrowings repaid	(163,145)
Issue costs paid	(2,600)
Interest paid, net	<u>(480,550)</u>
NET CASH USED BY CAPITAL AND RELATED FINANCING ACTIVITIES	<u>(585,193)</u>

CASH FLOWS FROM INVESTING ACTIVITIES:

Interest received	<u>1,357</u>
NET CASH PROVIDED BY INVESTING ACTIVITIES	<u>1,357</u>

INCREASE IN CASH, NET

CASH AND CASH EQUIVALENTS, AT BEGINNING OF YEAR

CASH AND CASH EQUIVALENTS, AT END OF YEAR

RECONCILIATION OF OPERATING INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES:

Income from operations	\$ 728,718
Adjustments to reconcile income from operations to net cash provided by operating activities -	
Provision for depreciation	928,141
Changes in operating assets and liabilities:	
Accounts and other receivables, net	(63,264)
Inventories	7,598
Prepaid expenses	(25,572)
Accounts payable	(4,497)
Accrued leave	271
Customer deposits	(580)
Accrued liabilities	<u>6,893</u>
NET CASH PROVIDED BY OPERATING ACTIVITIES	<u>\$ 1,577,708</u>

SCHEDULE OF NONCASH FINANCING AND INVESTING ACTIVITIES:

Water interim certificates of indebtedness refinanced	\$ 4,827,000
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The accompanying notes are an integral part of these financial statements.

**LINCOLN COUNTY BOARD OF PUBLIC UTILITIES**  
**NOTES TO FINANCIAL STATEMENTS**  
**June 30, 2014**

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accounting policies of the Lincoln County Board of Public Utilities (the "Board") conform to generally accepted accounting principles applicable to utilities. The Governmental Accounting Standards Board (GASB) is the standard setting body for establishing governmental accounting and financial reporting standards. The GASB's *Codification of Governmental Accounting and Financial Reporting Standards* document these principles. The following is a summary of significant policies:

(1) Reporting Entity

The Lincoln County Board of Public Utilities (the "Board") is an enterprise fund established under Tennessee Code Annotated 5-16-101 by Lincoln County, Tennessee. The Board sells drinking water to residents of Lincoln County not served by municipal systems. The Board is operated by a five member Board of Commissioners appointed by the Lincoln County Commission. The Board of Commissioners employs a Superintendent who is responsible for day-to-day operations of the water system including hiring its other employees. The Board is responsible for generating its own revenue and servicing its debt. The County has the authority to approve or reject budgets presented by the Board and to approve bonds issued by the Board. Some bonds issued by the Board are secured by a pledge of the taxing authority of Lincoln County, Tennessee.

The financial information of the Board is included as an enterprise fund in the Lincoln County, Tennessee Annual Financial Report. Complete financial statements of Lincoln County, Tennessee can be obtained directly from the County's administrative offices.

(2) Basis of Accounting

The Board's financial statements are reported using the economic resources measurement focus and the accrual basis of accounting in conformity with accounting principles generally accepted in the United States of America and general practices of the utility industry. Revenues are recognized when earned and expenses are recognized when incurred regardless of the timing of the related cash flow.

The Board is intended to be operated in a manner whereby the costs of providing water distribution services and system expansion are recovered through user charges. The Board distinguishes operating revenues and expenses from nonoperating items. Operating revenues generally result from charges to customers for the provision of water and related services. Operating expenses include the purchased cost of these services as well as costs to operate and maintain the various treatment, storage, transmission, and distribution systems plus general and administrative costs and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

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

(3) Cash and Cash Equivalents for General Use

For purposes of the Statement of Cash Flows, the Board considers all highly liquid investments with an original maturity of three months or less to be cash equivalents.

LINCOLN COUNTY BOARD OF PUBLIC UTILITIES  
NOTES TO FINANCIAL STATEMENTS  
June 30, 2014

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(4) Allowance for Uncollectible Accounts

The Board provides an allowance for uncollectible receivables equal to the estimated loss that may be incurred in collection of water sales receivables when it is probable that a customer account will be uncollectible. Bad debts offset against water sales revenues in 2014 were \$35,630.

(5) Materials and Supplies Inventories

Inventories are comprised of repair and maintenance supplies and extension materials. They are stated at the lower of average cost or replacement value.

(6) Water Plant and Equipment

The Board's water plant capital assets are capitalized at cost at the time they become part of operations. Donated capital assets are recorded at estimated current cost of construction. Extensions and betterments are capitalized at cost.

Depreciation of capitalized cost is provided on a group straight-line basis over the estimated useful lives of the assets. Under the group depreciation method, gains and losses on asset dispositions are applied against accumulated depreciation and are not reflected as gains or losses in the statement of revenues, expenses and changes in net position. Plant assets and buildings are depreciated over 25-50 years, while vehicles and equipment are depreciated over 6-10 years. The Board capitalizes equipment additions with a cost in excess of \$500 and plant additions in excess of \$2,000.

The costs of maintenance, repairs and replacements of minor items of property are charged to expense accounts as incurred.

(7) Capitalized Interest

Interest cost incurred, net of interest earned, on borrowed funds during the period of construction of capital assets is capitalized as a component of the cost of acquiring those assets. Net interest cost incurred in the current year totaled \$430,476. Of this, \$27,214 was capitalized with the remainder charged to expense.

(8) Debt Issue Costs

Costs of issuance other than insurance are charged to expense in the period incurred. Premiums and discounts realized on debt issuances are deferred and amortized over the terms of the respective debt using a method which approximates the effective interest method.

(9) Compensated Absences

The costs of vacation benefits are recorded as expense when earned. Employees accrue vacation leave of from one to three weeks annually based on years of service. Vacation leave not used is lost if not taken by each employee's employment anniversary date. The amount of accrued leave was \$9,704 at June 30, 2014, all of which was considered a current liability. Sick leave benefits are recorded as expense when used. Employees accrue twelve days sick leave each year with no accumulation limit. Sick leave does not vest, and no liability for unused sick leave is recorded in the financial statements.

LINCOLN COUNTY BOARD OF PUBLIC UTILITIES  
NOTES TO FINANCIAL STATEMENTS  
June 30, 2014

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(10) Deferred Outflows/ Inflows of Resources

In addition to assets, the statement of financial position will sometimes report a separate section for deferred outflows of resources. This separate financial statement element, *deferred outflows of resources*, represents a consumption of net position that applies to a future period(s) and so will not be recognized as an outflow of resources (expense) until then. The Board does not have any items that qualify for reporting in this category.

In addition to liabilities, the statement of financial position will sometimes report a separate section for deferred inflows of resources. This separate financial statement element, *deferred inflows of resources*, represents an acquisition of net position that applies to a future period(s) and so will not be recognized as an inflow of resources (revenue) until that time. The Board does not have any items that qualify for reporting in this category.

(11) Net Position

Net position is the difference between assets plus deferred outflows of resources and liabilities plus deferred inflows of resources. Net investment in capital assets represent capital assets reduced by accumulated depreciation and by any outstanding debt related to the acquisition, construction or improvement of those assets as well as any deferred outflows or inflows of resources attributable to the acquisition, construction, or improvement of those assets. The restricted component of net position consists of restricted assets reduced by liabilities and deferred inflows of resources related to those assets. Restricted assets occur when constraints are placed on the asset by creditors (such as debt covenants), grantors, contributions, laws, regulations, etc. Unrestricted net position is the amount of the assets, deferred outflows of resources, liabilities, and deferred inflows of resources that are not included in the determination of net investment in capital assets or the restricted component of net position. The debt service reserve is presented as a restricted component of net position. The reserve amount is in compliance with the required amount.

(12) Revenues

Revenues from water sales are recognized based on meter reading dates. No asset is recorded for water delivered between the last meter reading in the period and the end of the period. Revenues from connection fees and developer charges are recognized when service is activated.

(13) Contributions in aid of construction

Connection fees charged to customers (including developers) in excess of the actual cost of installation of new services are reflected as non-operating revenues in the period of new service installation. Amounts received as contributions or grants related to new line construction are reflected as capital contributions or grants.

(14) Income Taxes and Tax Equivalents

The Board is an instrumentality of Lincoln County, Tennessee; therefore, it is exempt from payment of federal and state income taxes.

**LINCOLN COUNTY BOARD OF PUBLIC UTILITIES  
NOTES TO FINANCIAL STATEMENTS  
June 30, 2014**

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(15) Management Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. The most significant estimates relate to depreciation and the value of distribution lines contributed to the Board.

(16) Budgets

State law requires the Board to adopt a budget for submission to the Lincoln County Board of Commissioners prior to the start of each fiscal year. The Board adopts its budget considering all cash receipts and disbursements.

NOTE B - CAPITAL ASSETS

The following is a summary of capital asset activity for the year ended June 30, 2014:

	Balance <u>6/30/2013</u>	<u>Additions</u>	<u>Retirements</u>	Balance <u>6/30/2014</u>
Non-depreciable:				
Land	\$ 527,695	\$ -	\$ -	\$ 527,695
Construction in progress	<u>260,150</u>	<u>2,195,922</u>	<u>-</u>	<u>2,456,072</u>
	<u>787,845</u>	<u>2,195,922</u>	<u>-</u>	<u>2,983,767</u>
Depreciable:				
Distribution lines and tanks	29,796,651	30,732	-	29,827,383
Wells and treatment plant	4,590,887	-	-	4,590,887
Buildings and equipment	<u>2,530,678</u>	<u>29,200</u>	<u>(45,505)</u>	<u>2,514,373</u>
	<u>36,918,216</u>	<u>59,932</u>	<u>(45,505)</u>	<u>36,932,643</u>
Total	<u>\$ 37,706,061</u>	<u>\$ 2,255,854</u>	<u>\$ (45,505)</u>	<u>\$ 39,916,410</u>

Accumulated depreciation of major classes of utility plant is as follows:

	Balance <u>6/30/2013</u>	<u>Additions</u>	<u>Retirements</u>	Balance <u>6/30/2014</u>
Distribution lines and tanks	\$ 11,419,480	\$ 688,252	\$ -	\$ 12,107,732
Wells and treatment plant	1,430,440	107,202	-	1,537,642
Buildings and equipment	<u>1,980,652</u>	<u>132,687</u>	<u>(45,505)</u>	<u>2,067,834</u>
	<u>\$ 14,830,572</u>	<u>\$ 928,141</u>	<u>\$ (45,505)</u>	<u>\$ 15,713,208</u>

At June 30, 2014, significant outstanding construction contract commitments totaled \$659,375.

LINCOLN COUNTY BOARD OF PUBLIC UTILITIES  
 NOTES TO FINANCIAL STATEMENTS  
 June 30, 2014

NOTE C - CASH AND CASH EQUIVALENTS

The following is a summary of cash and cash equivalents for general use and special funds as of June 30, 2014:

Cash and cash equivalents for general use	\$ 3,673,961
Special funds - restricted	
Externally restricted	277,524
Internally restricted	11,950
	\$ 3,963,435

Board cash consists of deposits in financial institutions with bank balances of \$3,984,109 and carrying amounts of \$3,963,435. Of the amounts on deposit, \$3,723,009 is fully insured by the Federal Deposit Insurance Corporation (FDIC) or Tennessee Bank Collateral Pool and \$239,926 is collateralized by securities pledged by the financial institution in the name of the Board. The remaining \$500 is cash on hand.

State law limits investments by counties to federal obligations, certain other federally guaranteed obligations or certain other highly rated instruments as well as certificates of deposit at state and federally chartered banks. The Board has not adopted policies to further limit its deposits or investments.

Restricted Assets: Cash is held in sinking fund reserve funds which are to be accumulated up to the maximum annual debt service and used for bond payments in the event funds are not otherwise available. These funds are mandated by bond covenants for bonds not secured by property taxes of Lincoln County. The Board pays scheduled bond payments from unrestricted funds leaving bond reserve funds intact. Restricted assets also include amounts held for payment of customer deposits. Balances in the restricted funds at June 30, 2014 were:

Sinking fund reserve fund - 1996 Bond	\$ 173,880
Sinking fund reserve fund - 1998 Bond	42,756
Sinking fund reserve fund - 2000 Bond	60,888
Customer deposits	11,950
	\$ 289,474

NOTE D - LONG-TERM DEBT

Bonds and notes are payable from revenues of the Board and are also secured by Lincoln County property taxes for the Series 2002, 2004, 2007, and 2010 debt issues described on the next page. All debt may be prepaid. Parity bonds may be issued if net revenues of the Board are at least 120% of scheduled bond payments. The Board's net revenues exceeded this requirement in the year ended June 30, 2014.

**LINCOLN COUNTY BOARD OF PUBLIC UTILITIES**  
**NOTES TO FINANCIAL STATEMENTS**  
**June 30, 2014**

**NOTE D - LONG-TERM DEBT (CONTINUED)**

The Board had bonds and notes outstanding at June 30 as follows:

	<u>2014</u>
Water Revenue and Tax Bonds, Series 2010, issued March 6, 2014 due monthly to USDA in annual principal and interest amounts of \$205,056 through the 2052 fiscal year at 2.75%	\$ 4,809,153
Water Revenue and Tax Bonds, Series 2007, issued April 23, 2008, due monthly to USDA in annual principal and interest amounts of \$90,360 through the 2046 fiscal year at 4.125%	1,598,210
Water Revenue and Tax Bonds, Series 2004, issued September 22, 2005, due monthly to USDA in annual principal and interest amounts of \$73,308 through the 2044 fiscal year at 4.25%	1,223,373
Waterworks Revenue and Tax Bonds, Series 2002, issued March 27, 2003, due monthly to USDA in annual principal and interest amounts of \$21,384 through the 2041 fiscal year at 4.75%	322,096
Waterworks Revenue Bond, Series 2000, issued October 18, 2001, due monthly to USDA in annual principal and interest amounts of \$60,888 through the 2040 fiscal year at 4.375%	927,917
Waterworks Revenue Bond, Series 1998, issued January 13, 2000, due monthly to USDA in annual principal and interest amounts of \$42,756 through the 2038 fiscal year at 4.75%	602,598
Waterworks Revenue Bond, Series 1996, issued August 22, 1997, due monthly to USDA in annual principal and interest amounts of \$173,880 through the 2035 fiscal year at 4.875%	<u>2,280,918</u>
<b>Total</b>	<b>11,764,265</b>
Less current portion of long-term debt	<u>(225,802)</u>
Long-term portion, net	<u><u>\$ 11,538,463</u></u>

Changes in principal balances during the year ended June 30, 2014 are summarized as follows:

Beginning balance	\$ 10,294,855
Advances on Interim Certificate of Indebtedness	1,632,555
Refinance Interim Certificate of Indebtedness	(4,827,000)
Issuance of Water Revenue and Tax Bonds, Series 2010	4,827,000
Principal paid on bonds	<u>(163,145)</u>
	<u><u>\$ 11,764,265</u></u>

**LINCOLN COUNTY BOARD OF PUBLIC UTILITIES**  
**NOTES TO FINANCIAL STATEMENTS**  
**June 30, 2014**

NOTE D - LONG-TERM DEBT (CONTINUED)

The annual requirements to amortize all long-term debt outstanding as of June 30, 2014 are as follows:

<u>Year</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2015	\$ 225,802	\$ 441,830	\$ 667,632
2016	234,638	432,994	667,632
2017	244,507	423,125	667,632
2018	254,469	413,163	667,632
2019	264,858	402,774	667,632
2020 - 2024	1,495,811	1,842,331	3,338,142
2025 - 2029	1,831,806	1,506,356	3,338,162
2030 - 2034	2,247,005	1,091,155	3,338,160
2035 - 2039	1,915,614	651,347	2,566,961
2040 - 2044	1,473,183	350,781	1,823,964
2045 - 2049	1,044,392	142,766	1,187,158
2050 - 2052	<u>532,180</u>	<u>20,561</u>	<u>552,741</u>
	<u>\$ 11,764,265</u>	<u>\$ 7,719,183</u>	<u>\$ 19,483,448</u>

Certain of the Board's bonds require establishment of sinking funds (as described in Note C) and compliance with various covenants. The Board is in compliance with these requirements at June 30, 2014.

NOTE E - PENSION AND BENEFIT PLANS

PLAN DESCRIPTION

Employees of Lincoln County Board of Public Utilities are members of the Political Subdivision Pension Plan (PSPP), an agent multiple-employer defined benefit pension plan administered by the Tennessee Consolidated Retirement System (TCRS). TCRS provides retirement benefits as well as death and disability benefits. Benefits are determined by a formula using the member's high five-year average salary and years of service. Members become eligible to retire at the age of 60 with five years of service or at any age with 30 years of service. A reduced retirement benefit is available to vested members at the age of 55. Disability benefits are available to active members with five years of service who become disabled and cannot engage in gainful employment. There is no service requirement for disability that is the result of an accident or injury occurring while the member was in the performance of duty. Members joining the system after July 1, 1979, become vested after five years of service and members joining prior to July 1, 1979 were vested after four years of service. Benefit provisions are established in state statute found in Title 8, Chapter 34-37 of the Tennessee Code Annotated (TCA). State statutes are amended by the Tennessee General Assembly. Political subdivisions such as Lincoln County Board of Public Utilities participate in the TCRS as individual entities and are liable for all costs associated with the operation and administration of their plan. Benefit improvements are not applicable to a political subdivision unless approved by the chief governing body.

The TCRS issues a publicly available financial report that includes financial statements and required supplementary information for the PSPP. That report may be obtained by writing to Tennessee Treasury Department, Consolidated Retirement System, 15th Floor Andrew Jackson Building, Nashville, TN 37243-0230 or can be accessed at <http://www.tn.gov/treasury/tcrs/PS/>.

**LINCOLN COUNTY BOARD OF PUBLIC UTILITIES**  
**NOTES TO FINANCIAL STATEMENTS**  
**June 30, 2014**

NOTE E - PENSION AND BENEFIT PLANS (CONTINUED)

FUNDING POLICY

Lincoln County Board of Public Utilities requires employees to contribute 5.0 percent of earnable compensation.

Lincoln County Board of Public Utilities is required to contribute at an actuarially determined rate; the rate for the fiscal year ending June 30, 2014 was 8.55% of annual covered payroll. The contribution requirement of plan members is set by state statute. The contribution requirement for the Board is established and may be amended by the TCRS Board of Trustees.

ANNUAL PENSION COST

For the year ending June 30, 2014, the Board's annual pension cost of \$89,791 to TCRS was equal to the Board's required and actual contributions. The required contribution was determined as part of the July 1, 2011 actuarial valuation using the frozen entry age actuarial cost method. Significant actuarial assumptions used in the valuation include, (a) rate of return on investment of present and future assets of 7.5 percent a year compounded annually, (b) projected 3.0 percent annual rate of inflation, (c) projected salary increases of 4.75 percent (graded) annual rate (no explicit assumption is made regarding the portion attributable to the effects of inflation on salaries), (d) projected 3.5 percent annual increase in the Social Security wage base, and (e) projected post retirement increases of 2.5 percent annually. The actuarial value of assets was determined using techniques that smooth the effect of short-term volatility in the market value of total investments over a ten-year period. The Board's unfunded actuarial accrued liability is being amortized as a level dollar amount on a closed basis. The remaining amortization period at July 1, 2011 was 5 years. An actuarial valuation was performed as of July 1, 2011, which established contribution rates effective July 1, 2012.

TREND INFORMATION

Fiscal Year <u>Ending</u>	Annual Pension <u>Cost (APC)</u>	Percentage of APC <u>Contributed</u>	Net Pension <u>Obligation</u>
6/30/14	\$89,791	100.00%	\$0.00
6/30/13	\$92,034	100.00%	\$0.00
6/30/12	\$98,955	100.00%	\$0.00

FUNDED STATUS AND FUNDING PROGRESS

As of July 1, 2013, the most recent actuarial valuation date, the plan was 97.40 percent funded. The actuarial accrued liability for benefits was \$2.28 million, and the actuarial value of assets was \$2.22 million, resulting in an unfunded actuarial accrued liability (UAAL) of \$0.06 million. The covered payroll (annual payroll of active employees covered by the plan) was \$1.04 million, and the ratio of the UAAL to the covered payroll was 5.69 percent.

The schedules of funding progress, presented as required supplementary information (RSI) following the notes to the financial statements, present multiyear trend information about whether the actuarial values of plan assets are increasing or decreasing over time relative to the AALs for benefits.

**LINCOLN COUNTY BOARD OF PUBLIC UTILITIES**  
**NOTES TO FINANCIAL STATEMENTS**  
**June 30, 2014**

NOTE E - PENSION AND BENEFIT PLANS (CONTINUED)

FUNDED STATUS AND FUNDING PROGRESS (CONTINUED)

(Dollar amounts in thousands)

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) - Entry Age (b)	Unfunded AAL (UAAL) (b) - (a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ((b-a)/c)
7/1/13	\$2,224	\$2,283	\$59	97.40%	\$1,044	5.69%
7/1/11	\$1,841	\$2,119	\$278	86.90%	\$1,234	22.50%
7/1/09	\$1,205	\$1,205	\$0	100.00%	\$1,133	0.00%

NOTE F - RISK MANAGEMENT

The Board is exposed to various risks of losses related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. During 2014, the Board participated in a public entity risk pool for coverage of general liability, property, and workers' compensation losses. The Board participated in the Local Government Fund, a public entity risk pool established by an association of Tennessee local governments. The Board pays an annual premium to the pool for the insurance coverage. The pool is created to be self-sustaining through member premiums.

The Board is self-insured for employee health claims between \$250 and \$5,000 per year per covered individual. Employees are responsible for the first \$250 of covered claims, with commercial insurance responsible for amounts over \$5,000. The plan liability at year-end is determined based on subsequent payments. The change in the liability for medical benefits for the years ended June 30, 2014 and 2013 is as follows:

	<u>2014</u>
Balance, beginning of year	\$ 799
Payments made	(27,345)
Incurred claims	<u>27,780</u>
Balance, end of year	<u>\$ 1,234</u>

The Board continues to carry commercial insurance for other risks of loss, including employee bonds and employee health and accident losses above the \$5,000 level. Settled claims from these losses have not exceeded commercial insurance coverage in any of the past three fiscal years.

NOTE G - PLEDGED REVENUES

The Board has pledged its revenues to secure its revenue bonds described in Note D. The current year revenues, debt service, and future pledge commitment are presented on the following page:

**LINCOLN COUNTY BOARD OF PUBLIC UTILITIES**  
**NOTES TO FINANCIAL STATEMENTS**  
**June 30, 2014**

**NOTE G - PLEDGED REVENUES (CONTINUED)**

	Current Year Principal and Interest Paid on	Percent of Current Revenue	Remaining Pledge based on future Principal and Interest Requirements	Commitment Period through Fiscal Year
<u>Operating Revenues</u>	<u>Revenue Bonds</u>	<u>Revenue</u>	<u>Requirements</u>	<u>Fiscal Year</u>
\$4,539,260	\$670,909	14.8%	\$ 19,483,448	2052

**NOTE H - WATER SOURCES**

The Board's primary sources of water are the Taft and Flintville well fields with additional sources being the Elora well field and the City of Fayetteville, Tennessee. The City of Fayetteville is the sole supplier of water to 9% of the Board's customers and is a supplemental and primary backup source of water for the remaining customers.

**NOTE I - RELATED PARTY TRANSACTIONS**

The Board provides water to Lincoln County, Tennessee related entities at the same billing rate as other customers. In the year ended June 30, 2014, these sales totaled \$29,861 and accounts receivable at June 30, 2014 related to these sales were \$869.

**NOTE J - CURRENT AND PLANNED PROJECTS**

The Board is requesting permits from the State of Tennessee that would allow for the construction of a water treatment plant on the Elk River. The plant would enhance the water available from the Board's current wells that are the primary source of water to 91% of the Board's customers. At June 30, 2014, the Board had purchased land for \$202,000, and had recorded construction in progress cost of \$174,768 related to roadway, other site development costs, and engineering and permitting costs. The estimated cost of the treatment plant and related distribution lines is \$18,000,000. No significant costs are anticipated to be incurred in the near-term and actual plant construction is not expected to begin within the next three years.

At June 30, 2014, the Board had incurred costs of \$2,281,304 on the Phase VI project, all of which is included in construction in progress. The Phase V project in the amount of \$3,090,416 was completed and placed in service in 2013. These projects consist of the replacement of approximately 22 miles of waterline in Park City, Tennessee and the surrounding area. Construction began in July 2011 and is expected to be completed in the June 30, 2015 year. The project cost of \$6,638,000 will be funded by a Rural Utility Service bond of \$4,827,000 and grant of \$1,811,000. Both the bond and grant require compliance with requirements of the American Recovery and Reinvestment Act of 2009. The bond portion was closed on March 6, 2014 and principal and interest payments began in April 2014. Monthly debt service on the bond is \$17,088. The Board also began making draws on the grant during 2014, drawing down \$684,401 during 2014. The Board approved a monthly \$1.50 per customer rate increase in September 2010 to assist with debt service. The Board is required to make monthly additions of \$29,000 to an asset management reserve to fund short-lived equipment and system costs when both projects are completed.

**NOTE K - CONTINGENCY**

During the year ended June 30, 2014, the Tennessee Comptroller issued a report that concluded that unauthorized pension contributions were made for both active and currently retired employees. The outcome of this matter cannot presently be determined.

REQUIRED SUPPLEMENTARY INFORMATION

**LINCOLN COUNTY BOARD OF PUBLIC UTILITIES**  
**REQUIRED SUPPLEMENTARY INFORMATION**  
**SCHEDULE OF FUNDING PROGRESS**  
 June 30, 2014

SCHEDULE OF FUNDING PROGRESS

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) - Projected Unit Credit (b)	Unfunded AAL (UAAL) (b - a)	Funded Ratio (a / b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ((b - a) / c)
July 1, 2013	\$ 2,224	\$ 2,283	\$ 59	97.4%	\$ 1,044	5.69%
July 1, 2011	1,841	2,119	278	86.9%	1,234	22.5%
July 1, 2009	1,205	1,205	-	100.0%	1,133	0.0%

SUPPLEMENTARY INFORMATION

**LINCOLN COUNTY BOARD OF PUBLIC UTILITIES  
SCHEDULE OF WATER RATES IN EFFECT AND NUMBER OF CUSTOMERS**

June 30, 2014

<u>METER TYPE</u>	<u>CUSTOMERS</u>	<u>GALLONS</u>	<u>RATES IN EFFECT</u> <u>RATE/1,000</u>
Residential and Commercial	8,684	First 1,000	\$ 24.99
		Next 4,000	4.14
		Over 5,000	4.17
Multi-user (Total of 406 units. Rates are based on usage for each unit.)	122	First 1,000	\$ 21.44
		Next 4,000	4.14
		Over 5,000	4.17
<hr/>			
Total	8,806		

OTHER CHARGES

Tap Fee - individual lot - 3/4 inch tap	\$ 1,300
individual lot - 1 inch tap	1,550
per subdivision lot	1,200
Service initiation - individual lot	100
subdivision lot	200

LINCOLN COUNTY BOARD OF PUBLIC UTILITIES  
ADMINISTRATION

June 30, 2014

LINCOLN COUNTY:

Peggy Bevels	County Executive	8/31/2014
Phyllis Counts	County Clerk	8/31/2014
Mary Jane Porter	County Trustee	8/31/2014

BOARD:

Ron Stanly	Board Chairman	6/30/2014
Paul Butcher	Board Vice-Chairman	6/30/2015
Mike Gooding	Board Secretary/Treasurer	6/30/2016
Danny Walker	Board Member	6/30/2016
Wade Williams	Board Member	6/30/2015

SUPERINTENDENT:

Ronnie Braden

OTHER INFORMATION

**LINCOLN COUNTY BOARD OF PUBLIC UTILITIES  
SCHEDULE OF INSURANCE IN EFFECT - UNAUDITED**

June 30, 2014

		<u>COVERAGE</u>	<u>EXPIRATION</u>
Coverage obtained through Lincoln County:			
Local Government Property and Casualty Fund *	Buildings and tanks	\$ 22,657,300	7/1/2014
	Contents	1,309,881	7/1/2014
	Equipment and vehicles	1,268,497	7/1/2014
	General and vehicle liability	1,000,000	7/1/2014
	Errors and omissions	1,000,000	7/1/2014
	Employee blanket bond	150,000	7/1/2014
Local Government Workers' Compensation Fund *	Workers' compensation	Statutory	7/1/2014
Other coverage:			
RLI Insurance Company	Employee dishonesty bond- Superintendent	\$ 675,000	Effective until cancelled by either party

\* Renewed 7/1/2014

# AWWA Free Water Audit Software: Reporting Worksheet

WAS v5.0  
American Water Works Association  
Copyright © 2014. All Rights Reserved.

Water Audit Report for: **Lincoln County Board of Public Utilities (TN0000884 & TN0000764)**  
Reporting Year: **2014**      **7/2013 - 6/2014**

Please enter data in the white cells below. Where available, metered values should be used; if metered values are unavailable please estimate a value. Indicate your confidence in the accuracy of the input data by grading each component (n/a or 1-10) using the drop-down list to the left of the input cell. Hover the mouse over the cell to obtain a description of the grades

All volumes to be entered as: MILLION GALLONS (US) PER YEAR

To select the correct data grading for each input, determine the highest grade where the utility meets or exceeds all criteria for that grade and all grades below it.

**WATER SUPPLIED**

← Enter grading in column 'E' and 'J' →

Volume from own sources:	<input type="button" value="1"/> <input type="button" value="2"/> <input type="button" value="3"/> <input type="button" value="4"/> <input type="button" value="5"/> <input type="button" value="6"/> <input type="button" value="7"/> <input type="button" value="8"/> <input type="button" value="9"/> <input type="button" value="10"/> <input type="button" value="n/a"/>	5	764.084	MG/Yr
Water imported:	<input type="button" value="1"/> <input type="button" value="2"/> <input type="button" value="3"/> <input type="button" value="4"/> <input type="button" value="5"/> <input type="button" value="6"/> <input type="button" value="7"/> <input type="button" value="8"/> <input type="button" value="9"/> <input type="button" value="10"/> <input type="button" value="n/a"/>	9	118.440	MG/Yr
Water exported:	<input type="button" value="1"/> <input type="button" value="2"/> <input type="button" value="3"/> <input type="button" value="4"/> <input type="button" value="5"/> <input type="button" value="6"/> <input type="button" value="7"/> <input type="button" value="8"/> <input type="button" value="9"/> <input type="button" value="10"/> <input type="button" value="n/a"/>	n/a	0.000	MG/Yr

Master Meter and Supply Error Adjustments

Pcnt:	Value:
<input type="button" value="1"/> <input type="button" value="2"/> <input type="button" value="3"/> <input type="button" value="4"/> <input type="button" value="5"/> <input type="button" value="6"/> <input type="button" value="7"/> <input type="button" value="8"/> <input type="button" value="9"/> <input type="button" value="10"/> <input type="button" value="n/a"/>	8    0.00% <input type="radio"/> <input checked="" type="radio"/>
<input type="button" value="1"/> <input type="button" value="2"/> <input type="button" value="3"/> <input type="button" value="4"/> <input type="button" value="5"/> <input type="button" value="6"/> <input type="button" value="7"/> <input type="button" value="8"/> <input type="button" value="9"/> <input type="button" value="10"/> <input type="button" value="n/a"/>	5    0.00% <input type="radio"/> <input checked="" type="radio"/>
<input type="button" value="1"/> <input type="button" value="2"/> <input type="button" value="3"/> <input type="button" value="4"/> <input type="button" value="5"/> <input type="button" value="6"/> <input type="button" value="7"/> <input type="button" value="8"/> <input type="button" value="9"/> <input type="button" value="10"/> <input type="button" value="n/a"/>	<input type="radio"/> <input type="radio"/>

**WATER SUPPLIED:**      **882.524** MG/Yr

Enter negative % or value for under-registration  
Enter positive % or value for over-registration

**AUTHORIZED CONSUMPTION**

Billed metered:	<input type="button" value="1"/> <input type="button" value="2"/> <input type="button" value="3"/> <input type="button" value="4"/> <input type="button" value="5"/> <input type="button" value="6"/> <input type="button" value="7"/> <input type="button" value="8"/> <input type="button" value="9"/> <input type="button" value="10"/> <input type="button" value="n/a"/>	7	478.989	MG/Yr
Billed unmetered:	<input type="button" value="1"/> <input type="button" value="2"/> <input type="button" value="3"/> <input type="button" value="4"/> <input type="button" value="5"/> <input type="button" value="6"/> <input type="button" value="7"/> <input type="button" value="8"/> <input type="button" value="9"/> <input type="button" value="10"/> <input type="button" value="n/a"/>	n/a	0.000	MG/Yr
Unbilled metered:	<input type="button" value="1"/> <input type="button" value="2"/> <input type="button" value="3"/> <input type="button" value="4"/> <input type="button" value="5"/> <input type="button" value="6"/> <input type="button" value="7"/> <input type="button" value="8"/> <input type="button" value="9"/> <input type="button" value="10"/> <input type="button" value="n/a"/>	10	2.945	MG/Yr
Unbilled unmetered:	<input type="button" value="1"/> <input type="button" value="2"/> <input type="button" value="3"/> <input type="button" value="4"/> <input type="button" value="5"/> <input type="button" value="6"/> <input type="button" value="7"/> <input type="button" value="8"/> <input type="button" value="9"/> <input type="button" value="10"/> <input type="button" value="n/a"/>		11.032	MG/Yr

Click here:  for help using option buttons below

Pcnt:      Value:

Enter a positive value, otherwise a default percentage of 1.25% (of billed metered) is applied and a grading of 5 is applied but not displayed

**AUTHORIZED CONSUMPTION:**      **492.966** MG/Yr

Use buttons to select percentage of water supplied OR value

**WATER LOSSES (Water Supplied - Authorized Consumption)**

**389.558** MG/Yr

**Apparent Losses**

Unauthorized consumption:                 **2.206** MG/Yr

Default option selected for unauthorized consumption - a grading of 5 is applied but not displayed

Customer metering inaccuracies:	<input type="button" value="1"/> <input type="button" value="2"/> <input type="button" value="3"/> <input type="button" value="4"/> <input type="button" value="5"/> <input type="button" value="6"/> <input type="button" value="7"/> <input type="button" value="8"/> <input type="button" value="9"/> <input type="button" value="10"/> <input type="button" value="n/a"/>	7	47.664	MG/Yr
Systematic data handling errors:	<input type="button" value="1"/> <input type="button" value="2"/> <input type="button" value="3"/> <input type="button" value="4"/> <input type="button" value="5"/> <input type="button" value="6"/> <input type="button" value="7"/> <input type="button" value="8"/> <input type="button" value="9"/> <input type="button" value="10"/> <input type="button" value="n/a"/>		1.197	MG/Yr

Default option selected for Systematic data handling errors - a grading of 5 is applied but not displayed

**Apparent Losses:**      **51.068** MG/Yr

Pcnt:      Value:

0.25%   

9.00%   

0.25%   

**Real Losses (Current Annual Real Losses or CARL)**

Real Losses = Water Losses - Apparent Losses:      **338.491** MG/Yr

**WATER LOSSES:**      **389.558** MG/Yr

**NON-REVENUE WATER**

**NON-REVENUE WATER:**      **403.535** MG/Yr

= Water Losses + Unbilled Metered + Unbilled Unmetered

**SYSTEM DATA**

Length of mains:	<input type="button" value="1"/> <input type="button" value="2"/> <input type="button" value="3"/> <input type="button" value="4"/> <input type="button" value="5"/> <input type="button" value="6"/> <input type="button" value="7"/> <input type="button" value="8"/> <input type="button" value="9"/> <input type="button" value="10"/> <input type="button" value="n/a"/>	7	735.0	miles
Number of active AND inactive service connections:	<input type="button" value="1"/> <input type="button" value="2"/> <input type="button" value="3"/> <input type="button" value="4"/> <input type="button" value="5"/> <input type="button" value="6"/> <input type="button" value="7"/> <input type="button" value="8"/> <input type="button" value="9"/> <input type="button" value="10"/> <input type="button" value="n/a"/>	8	8,814	
Service connection density:	<input type="button" value="1"/> <input type="button" value="2"/> <input type="button" value="3"/> <input type="button" value="4"/> <input type="button" value="5"/> <input type="button" value="6"/> <input type="button" value="7"/> <input type="button" value="8"/> <input type="button" value="9"/> <input type="button" value="10"/> <input type="button" value="n/a"/>		12	conn./mile main

Are customer meters typically located at the curbside or property line?       (length of service line, beyond the property boundary, that is the responsibility of the utility)

Average length of customer service line:

Average length of customer service line has been set to zero and a data grading score of 10 has been applied

Average operating pressure:                 **75.0** psi

**COST DATA**

Total annual cost of operating water system:	<input type="button" value="1"/> <input type="button" value="2"/> <input type="button" value="3"/> <input type="button" value="4"/> <input type="button" value="5"/> <input type="button" value="6"/> <input type="button" value="7"/> <input type="button" value="8"/> <input type="button" value="9"/> <input type="button" value="10"/> <input type="button" value="n/a"/>	9	\$4,252,035	\$/Year
Customer retail unit cost (applied to Apparent Losses):	<input type="button" value="1"/> <input type="button" value="2"/> <input type="button" value="3"/> <input type="button" value="4"/> <input type="button" value="5"/> <input type="button" value="6"/> <input type="button" value="7"/> <input type="button" value="8"/> <input type="button" value="9"/> <input type="button" value="10"/> <input type="button" value="n/a"/>	9	\$8.31	\$/1000 gallons (US)
Variable production cost (applied to Real Losses):	<input type="button" value="1"/> <input type="button" value="2"/> <input type="button" value="3"/> <input type="button" value="4"/> <input type="button" value="5"/> <input type="button" value="6"/> <input type="button" value="7"/> <input type="button" value="8"/> <input type="button" value="9"/> <input type="button" value="10"/> <input type="button" value="n/a"/>	9	\$2,812.86	\$/Million gallons <input checked="" type="checkbox"/> Use Customer Retail Unit Cost to value real losses

**WATER AUDIT DATA VALIDITY SCORE:**

\*\*\* YOUR SCORE IS: 70 out of 100 \*\*\*

A weighted scale for the components of consumption and water loss is included in the calculation of the Water Audit Data Validity Score

**PRIORITY AREAS FOR ATTENTION:**

Based on the information provided, audit accuracy can be improved by addressing the following components:

- 1: Volume from own sources
- 2: Billed metered
- 3: Unauthorized consumption

# PUTMAN & HANCOCK

*Certified Public Accountants*

219 East College Street  
P.O. Box 722  
Fayetteville, Tennessee 37334

Phone: (931) 433-1040  
Fax: (931) 433-9290

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

Lincoln County Board of Public Utilities  
Fayetteville, Tennessee

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the Lincoln County Board of Public Utilities (the "Board") as of and for the year ended June 30, 2014, and the related notes to the financial statements, and have issued our report thereon, dated October 15, 2014.

### Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Board's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Board's internal control. Accordingly, we do not express an opinion on the effectiveness of the Board's 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 described in the accompanying schedule of findings and questioned costs, 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 Board's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiency described in the accompanying schedule of findings and questioned costs as item 2014-001 to be a material weakness.

### Compliance and Other Matters

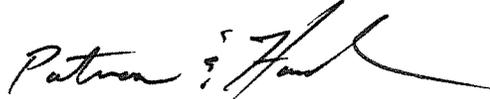
As part of obtaining reasonable assurance about whether the Board's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect 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 instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* and which are described in the accompanying schedule of findings and questioned costs as item 2013-001.

## Lincoln County Board of Public Utilities' Response to Findings

Lincoln County Board of Public Utilities' response to the findings identified in our audit is described in the accompanying schedule of findings and questioned costs. Lincoln County Board of Public Utilities' response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

### Purpose of this Report

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

A handwritten signature in black ink, appearing to read "Patricia S. Hand". The signature is written in a cursive style with a long, sweeping tail.

Fayetteville, Tennessee  
October 15, 2014

SINGLE AUDIT

LINCOLN COUNTY BOARD OF PUBLIC UTILITIES  
 SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS  
 Year Ended June 30, 2014

<u>Federal/State Grantor</u>	<u>CFDA Number</u>	<u>Contract Number</u>	<u>Beginning (Accrued) Deferred</u>	<u>Cash Receipts</u>	<u>Expenditures</u>	<u>Ending (Accrued) Deferred</u>
U. S. Department of Agriculture Water and Waste Disposal Systems for Rural Communities - ARRA	10.781	Phase VI Contract-112 Loan/\$4,827,000	\$ -	\$ 2,274,456	\$ 2,274,446	\$ 10
Total Federal Awards			\$ -	\$ 2,274,456	\$ 2,274,446	\$ 10

**LINCOLN COUNTY BOARD OF PUBLIC UTILITIES**  
**SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS (CONTINUED)**  
Year Ended June 30, 2014

**NOTE A - SIGNIFICANT ACCOUNTING POLICIES**

The accompanying Schedule of Expenditures of Federal Awards summarizes the expenditures of Lincoln County Board of Public Utilities under programs of the federal government for the year ended June 30, 2014. The schedule is presented using the accrual basis of accounting.

**NOTE B - LOANS OUTSTANDING**

In the current year, the System issued a revenue and tax bond in the amount of \$4,827,000 through the U.S. Department of Agriculture (USDA) Rural Utilities Service (RUS) to finance improvements in the water system and to refinance interim certificates of indebtedness. The principal balance at June 30, 2014 was \$4,809,153.

At June 30, 2014, there was an outstanding balance of \$6,955,112 on loans obtained in previous years through the U.S. Department of Agriculture (USDA) Rural Utilities Service (RUS). Payments during the current year totaled \$145,298.

**NOTE C - COMMITMENTS**

At June 30, 2014, the System had outstanding commitments totaling \$659,375 for water line replacement.

**PUTMAN & HANCOCK**  
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**INDEPENDENT AUDITORS' REPORT ON COMPLIANCE FOR EACH MAJOR PROGRAM AND  
ON INTERNAL CONTROL OVER COMPLIANCE REQUIRED BY OMB CIRCULAR A-133**

Lincoln County Board of Public Utilities  
Fayetteville, Tennessee

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

We have audited the Lincoln County Board of Public Utilities' (the "Board'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 the Board's major federal programs for the year ended June 30, 2014. The Board's major federal programs are identified in the summary of auditors' 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 its federal programs.

***Auditors' Responsibility***

Our responsibility is to express an opinion on compliance for each of the Board'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 the Board'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 the Board's compliance.

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

In our opinion, the Board 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.

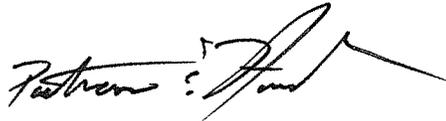
**Report on Internal Control Over Compliance**

Management of the Board 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 the Board'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 an 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 the Board'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.

A handwritten signature in black ink, appearing to read "Festrom : [unclear]", with a stylized flourish extending to the right.

Fayetteville, Tennessee  
October 15, 2014

LINCOLN COUNTY BOARD OF PUBLIC UTILITIES  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
Year Ended June 30, 2014

A. SUMMARY OF AUDITORS' RESULTS

1. The auditors' report expresses an unmodified opinion on the financial statements of the Lincoln County Board of Public Utilities.
2. One material weakness and one significant deficiency relating to the audit of the financial statements are reported in the Independent Auditors' Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards*.
3. No instances of noncompliance material to the financial statements of the Lincoln County Board of Public Utilities were disclosed during the audit.
4. No significant deficiencies relating to the audit of the major federal award programs are reported in the Report on Compliance for Each Major Program and on Internal Control over Compliance Required by OMB Circular A-133.
5. The auditors' report on compliance for the major federal award programs for the Lincoln County Board of Public Utilities expresses an unmodified opinion on all major federal programs.
6. Audit findings that are required to be reported in accordance with Section 510(a) of OMB Circular A-133 are reported in this Schedule.
7. The programs tested as major programs included:  
Water and Waste Disposal Systems for Rural Communities - ARRA, CFDA #10.781
8. The threshold used for distinguishing between Type A and B programs was \$300,000.
9. The Lincoln County Board of Public Utilities did not qualify as a low-risk auditee.

B. FINDINGS - FINANCIAL STATEMENTS AUDIT

FINDING NUMBER 2013-001:

*Condition and Criteria:*

The law governing the Board requires that the Board's purchases be made through the Lincoln County Finance Department. However, purchases continue to be made by the Board's employees who are independent of the Lincoln County Finance Department.

*Effect:*

The Board is not in compliance with this law.

*Auditors' Recommendations:*

Procedures should be changed to comply with the law related to purchasing.

FINDING NUMBER 2013-001 (CONTINUED):

*Management Response:*

The Board is seeking a resolution by the State of Tennessee to grant the Board power do its own purchasing.

FINDING NUMBER 2014-001:

*Condition and Criteria:*

Fidelity bond coverage is required for debt covenant compliance with the Board's USDA debt issuances. The Board allowed this coverage to lapse during the 2014 fiscal year and was without any fidelity bond coverage from October 7, 2013 through December 31, 2013.

*Effect:*

The Board was not in compliance with its debt covenant requirements for approximately 3 months during the year.

*Auditors' Recommendations:*

Procedures should ensure that continuous fidelity bond coverage is maintained by the Board.

*Management Response:*

This lapse occurred because of issues in finding an insurer willing to cover the Board. Coverage was reinstated effective January 1, 2014 and continuous coverage has been maintained by the Board since that date.

C. FINDINGS AND QUESTIONED COSTS - MAJOR FEDERAL AWARD PROGRAMS AUDIT

None

**LINCOLN COUNTY BOARD OF PUBLIC UTILITIES  
SCHEDULE OF PRIOR YEAR FINDINGS  
For the Fiscal Year Ended June 30, 2014**

Financial Statement Findings

<b>Finding Number</b>	<b>Finding Title</b>	<b>Status</b>
2011-001	Financial Statement Preparation	Corrected
2012-002	Check Signing Authority	Corrected
2013-001	Purchasing Procedures	Repeated