

CITY OF GRAYSON, KENTUCKY

**FINANCIAL STATEMENTS
AND SUPPLEMENTAL INFORMATION**

FOR THE YEAR ENDED JUNE 30, 2014

TOGETHER WITH INDEPENDENT AUDITOR'S REPORTS

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INDEPENDENT AUDITOR'S REPORT

The Honorable Mayor and
City Council
City of Grayson
Grayson, Kentucky .

Report on the Financial Statements

We have audited the accompanying financial statements of the governmental activities, the business-type activities, and each major fund of the City of Grayson, Kentucky (the "City") as of and for the year ended June 30, 2014, and the related notes to the financial statements, which collectively comprise the City's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express opinions on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, and each major fund of the City of Grayson, Kentucky as of June 30, 2014, and the respective changes in financial position and, where applicable, cash flows thereof, and the respective budgetary comparison for each major fund for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis information on pages 4 through 7 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in the appropriate operational, economic, and historical context. We have applied certain limited procedures, which consisted principally of inquiries of management about the methods of preparing the information and comparing the information for consistency in management's responses to our inquiries, the basic financial statements, and knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or any assurance.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated January 22, 2015, on our consideration of the City's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the City's internal control over financial reporting and compliance.

Kelley Dalloway Smith Doolby, PSC

January 22, 2015
Ashland, Kentucky

**City of Grayson, Kentucky
Management's Discussion and Analysis
Year Ended June 30, 2014**

The discussion and analysis of the City of Grayson, Kentucky's financial performance provides an overview of the City's financial activities for the fiscal year ended June 30, 2014. This information is presented in conjunction with the audited financial statements that follow this section.

FINANCIAL HIGHLIGHTS

- The assets of the Government exceeded its liabilities at the end of the fiscal year by \$18,630,166 (net position). Governmental activities' unrestricted net position was \$647,268 and is used to meet the Government's ongoing obligations. Business-type activities' unrestricted net position was \$2,090,986.
- The Government's total net position decreased by \$389,564. Net position of governmental activities increased by \$19,686 and net position of business-type activities decreased by \$409,250.
- At June 30, 2014, the governmental activities had \$5,024,872 in assets and \$2,226,817 in liabilities. Business-type activities had \$22,556,050 in assets and \$6,723,939 in liabilities.

OVERVIEW OF FINANCIAL STATEMENTS

This discussion and analysis is intended to serve as an introduction to the City's basic financial statements. The City's basic financial statements comprise three components: 1) government- wide financial statements, 2) fund financial statements, 3) budgetary comparisons, and 4) notes to the financial statements.

Government-wide financial statements. The government-wide financial statements are designed to provide readers with a broad overview of the City's finances, in a manner similar to a private - sector business.

The statement of net position presents information on all of the City's assets and liabilities, with the difference between the two reported as net position. Over time, increases or decreases in net position may serve as a useful indicator of whether the financial position of the City is improving or deteriorating.

The statement of activities presents information showing how the City's net position changed during the most recent fiscal year. All changes in net position are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods.

The government-wide financial statements outline functions of the City that are principally supported by property taxes and intergovernmental revenues (governmental activities). The governmental activities of the City include public safety, public works, recreation, and community development. Fixed assets and related debt are also supported by taxes and intergovernmental revenues.

The government-wide financial statements can be found on pages 8 - 9 of this report.

Fund financial statements. A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives.

The fund financial statements can be found on pages 10 - 19 of this report.

Notes to the financial statements. The notes provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements. The notes to the financial statements can be found on pages 20 - 30 of this report.

GOVERNMENT-WIDE FINANCIAL ANALYSIS

Net position may serve over time as a useful indicator of a government's financial position. In the case of the City, assets exceeded liabilities by \$18,630,166 at the close of the most recent fiscal year. The City's net position decreased 2.0% percent which is reported as the change in net position in the statement of activities.

City of Grayson, Kentucky's Net Position

	<u>Government- type Activities</u> 2014	<u>Business-type Activities</u> 2014	<u>Government- type Activities</u> 2013	<u>Business-type Activities</u> 2013
Current assets	\$ 835,866	\$ 3,486,585	\$ 838,243	\$ 3,559,337
Capital assets	4,189,006	19,069,465	4,113,586	19,727,675
Total assets	<u>5,024,872</u>	<u>22,556,050</u>	<u>4,951,829</u>	<u>23,287,012</u>
Current liabilities	345,870	808,564	205,763	600,966
Long-term liabilities	1,880,947	5,915,375	1,967,697	6,386,560
Total liabilities	<u>2,226,817</u>	<u>6,723,939</u>	<u>2,173,460</u>	<u>6,987,526</u>
Net position:				
Net investment in capital assets	2,143,882	12,775,249	1,995,566	12,945,942
Restricted	6,905	965,876	63,449	951,933
Unrestricted	647,268	2,090,986	719,354	2,401,611
Total net position	<u>\$ 2,798,055</u>	<u>\$ 15,832,111</u>	<u>\$ 2,778,369</u>	<u>\$ 16,299,486</u>

By far the largest portion of the City's net position reflects its investment in capital assets (e.g., land, buildings, machinery and equipment), less any related debt used to acquire those assets still outstanding. The City uses these capital assets to provide services to citizens and consumers; consequently, these assets are *not* available for future spending. Although the City's investment in its capital assets is reported net of related debt, it should be noted that the resources needed to repay this debt must be provided from other sources, since the capital assets themselves cannot be used to liquidate those liabilities.

City of Grayson, Kentucky's Changes in Net Position

	<u>Government- type Activities</u> 2014	<u>Business-type Activities</u> 2014	<u>Government- type Activities</u> 2013	<u>Business-type Activities</u> 2013
Revenues:				
Charges for services	\$ 2,565	\$ 5,291,469	\$ 3,605	\$ 5,070,311
Tax levies	1,782,806	-	1,701,493	-
Licenses, fees and permits	163,285	-	88,470	-
Franchise fees	18,191	-	20,490	-
Grants/contributions	270,352	59,136	264,112	253,872
Investment earnings	603	3,076	703	3,603
Miscellaneous	205,958	1,200	42,596	520
Total revenues	<u>2,443,760</u>	<u>5,354,881</u>	<u>2,121,469</u>	<u>5,328,306</u>

Expenses:

General government	355,273	-	339,499	-
Fire	379,787	-	273,276	-
Police	1,003,233	-	979,357	-
Highways and streets	500,850	-	364,906	-
Parks and recreation	69,745	-	46,325	-
Emergency management	28,977	-	22,331	-
Cemetery	-	-	225	-
Debt service	86,209	-	68,255	-
Utilities	-	5,764,131	-	5,185,873
Total expenses	<u>2,424,074</u>	<u>5,764,131</u>	<u>2,094,174</u>	<u>5,185,873</u>
Change in net position	<u>19,686</u>	<u>(409,250)</u>	<u>27,295</u>	<u>142,433</u>
Net position, beginning of year, as restated	<u>2,778,369</u>	<u>16,241,361</u>	<u>2,751,074</u>	<u>16,098,928</u>
Net position, ending of year	<u>\$ 2,798,055</u>	<u>\$ 15,832,111</u>	<u>\$ 2,778,369</u>	<u>\$ 16,241,361</u>

Government-type activity. Government-type activity net position increased by \$19,686 or .7%.

Business-type activity. Business-type activity net position decreased by \$409,250 or 2.5%.

FINANCIAL ANALYSIS OF THE CITY'S FUNDS

The City uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. Fund financial statements report the Government's operations in more detail than the government-wide statements by providing information about the Government's most significant funds. Two types of funds are presented in the fund financial statements: governmental funds and proprietary funds.

Governmental funds. Most of the Government's basic services are reported in the governmental funds. These statements provide a short-term view of general government operations and how these services are financed as well as the balances left at year end that are available for future spending. These funds are reported using the modified accrual basis of accounting, which measures cash and all other financial assets that can be readily converted to cash.

Proprietary funds. The City's proprietary fund provides the same type of information found in government-wide financial statements, but in more detail.

Enterprise fund. The Utility Enterprise Fund accounts for operations in a manner similar to a private business enterprise. Operations are accounted for in such a manner as to show net income or loss and the funds are intended to be predominately self supported from user charges.

Capital Assets

The City's investment in capital assets for governmental and business-type activities as of June 30, 2014, amounts to \$23,258,471 (net of accumulated depreciation). The investment in capital assets includes land, buildings, improvements, machinery and equipment. The increase in the City's investment in capital assets for the current year was 1.7% percent, before current depreciation.

Major capital asset events during the current fiscal year included water line extensions and the purchase of street equipment.

Additional information on the City's capital assets can be found in Note (5) of the financial statements.

Debt Administration

At the end of the current fiscal year, the City had total debt outstanding of \$8,339,340 as compared to \$8,841,628 in the prior year. The City issued new debt in the amount of \$83,208 for the purchase of street equipment in the current year. Additional information on the City's long-term debt can be found in Note (6) of the financial statements.

Budget Comparisons

- General fund revenues were \$24,875 less than budgeted. General fund expenditures were \$10,825 more than budgeted.
- Special revenue fund - Municipal Road Aid revenues were \$8,786 more than budgeted. Expenditures were \$66,531 more than budgeted.

ECONOMIC FACTORS AND NEXT YEAR'S RATES

In considering the City budget for the fiscal year 2015, the City expects no significant changes.

REQUESTS FOR INFORMATION

This financial report is designed to provide citizens, customers, investors, and creditors, with a general overview of the City's finances and to demonstrate the City's accountability for the money it receives. If you have any questions about this report or need any additional information, contact George Steele, Mayor or Cindy Stratton, City Clerk at 302 East Main St., Grayson, Kentucky 41143 or phone (606) 474-6651.

CITY OF GRAYSON, KENTUCKY
STATEMENT OF NET POSITION
JUNE 30, 2014

	Governmental Activities	Business-Type Activities	Total
ASSETS			
Cash and cash equivalents	\$ 369,632	\$ 1,773,867	\$ 2,143,499
Accounts receivable:			
Unbilled receivables	-	228,632	228,632
Customers	-	373,905	373,905
Property taxes	240,734	-	240,734
Interest	-	126	126
Other	162,463	-	162,463
Allowance for doubtful accounts	(15,620)	(18,116)	(33,736)
Prepaid expenses	489	-	489
Inventory for supplies	-	162,295	162,295
Restricted assets -			
Cash and cash equivalents	78,168	965,876	1,044,044
Nondepreciable capital assets	925,116	629,540	1,554,656
Depreciable capital assets	5,675,848	35,498,205	41,174,053
Accumulated depreciation	(2,411,958)	(17,058,280)	(19,470,238)
	<u>5,024,872</u>	<u>22,556,050</u>	<u>27,580,922</u>
Total assets			
LIABILITIES			
Accounts payable	138,487	166,142	304,629
Accrued wages	17,866	63,849	81,715
Other accrued liabilities	25,340	10,838	36,178
Current portion of long-term debt	164,177	519,893	684,070
Accrued interest payable	-	47,842	47,842
Customer deposits	-	141,052	141,052
Long-term debt, net of current portion	1,880,947	5,774,323	7,655,270
	<u>2,226,817</u>	<u>6,723,939</u>	<u>8,950,756</u>
Total liabilities			
NET POSITION			
Net investment in capital assets	2,143,882	12,775,249	14,919,131
Restricted	6,905	965,876	972,781
Unrestricted	647,268	2,090,986	2,738,254
	<u>\$ 2,798,055</u>	<u>\$ 15,832,111</u>	<u>\$ 18,630,166</u>
Total net position			

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

**CITY OF GRAYSON, KENTUCKY
STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED JUNE 30, 2014**

Functions/Programs	Expenses	Program Revenues			Net (Expense) Revenue and Changes in Net Position		
		Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	Governmental Activities	Business-Type Activities	Total
Governmental Activities							
General government	\$ 355,273	\$ -	\$ -	\$ -	\$ (355,273)	\$ -	\$ (355,273)
Fire	379,787	-	42,235	-	(337,552)	-	(337,552)
Police	1,003,233	2,565	92,665	-	(908,003)	-	(908,003)
Highways and streets	500,850	-	135,452	-	(365,398)	-	(365,398)
Parks and recreation	69,745	-	-	-	(69,745)	-	(69,745)
Emergency management	28,977	-	-	-	(28,977)	-	(28,977)
Interest expense	86,209	-	-	-	(86,209)	-	(86,209)
Total governmental activities	<u>2,424,074</u>	<u>2,565</u>	<u>270,352</u>	<u>-</u>	<u>(2,151,157)</u>	<u>-</u>	<u>(2,151,157)</u>
Business-Type Activities							
Utility fund	5,764,131	5,291,469	-	59,136	-	(413,526)	(413,526)
Total business-type activities	<u>5,764,131</u>	<u>5,291,469</u>	<u>-</u>	<u>59,136</u>	<u>-</u>	<u>(413,526)</u>	<u>(413,526)</u>
Total primary government	<u>\$ 8,188,205</u>	<u>\$ 5,294,034</u>	<u>\$ 270,352</u>	<u>\$ 59,136</u>	<u>\$ (2,151,157)</u>	<u>\$ (413,526)</u>	<u>\$ (2,564,683)</u>
General Revenues:							
Payroll tax					\$ 876,536	\$ -	\$ 876,536
Property and other local taxes					906,270	-	906,270
Fines & forfeitures					29,430	-	29,430
Franchise fees					18,191	-	18,191
Licenses, fees and permits					163,285	-	163,285
Rent income					525	-	525
Interest income					603	3,076	3,679
Other revenues					176,003	-	176,003
Gain (loss) on sale of fixed assets					-	1,200	1,200
Total general revenues					<u>2,170,843</u>	<u>4,276</u>	<u>2,175,119</u>
Change in net position					19,686	(409,250)	(389,564)
Net position, June 30, 2013, as restated					<u>2,778,369</u>	<u>16,241,361</u>	<u>19,019,730</u>
Net position, June 30, 2014					<u>\$ 2,798,055</u>	<u>\$ 15,832,111</u>	<u>\$ 18,630,166</u>

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

CITY OF GRAYSON, KENTUCKY
BALANCE SHEET
GOVERNMENTAL FUNDS
JUNE 30, 2014

		Special Revenue Funds		Total
	General	Grant	Municipal Road Aid	Governmental Funds
Assets				
Cash	\$ 369,632	\$ 6,428	\$ 71,740	\$ 447,800
Taxes receivable	240,734	-	-	240,734
Grant receivable	2,043	-	8,737	10,780
Other receivables	151,683	-	-	151,683
Allowance for uncollectible taxes	(15,620)	-	-	(15,620)
Prepaid expense	489	-	-	489
Total assets	<u>\$ 748,961</u>	<u>\$ 6,428</u>	<u>\$ 80,477</u>	<u>\$ 835,866</u>
Liabilities and Fund Balances				
Liabilities:				
Accounts payable	\$ 58,487	\$ -	\$ 80,000	\$ 138,487
Accrued wages	17,866	-	-	17,866
Other accrued liabilities	25,340	-	-	25,340
Total liabilities	<u>101,693</u>	<u>-</u>	<u>80,000</u>	<u>181,693</u>
Fund Balances:				
Restricted	-	6,428	477	6,905
Non-spendable	489	-	-	489
Unassigned	646,779	-	-	646,779
Total fund balances	<u>647,268</u>	<u>6,428</u>	<u>477</u>	<u>654,173</u>
Total liabilities and fund balances	<u>\$ 748,961</u>	<u>\$ 6,428</u>	<u>\$ 80,477</u>	<u>\$ 835,866</u>

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

CITY OF GRAYSON, KENTUCKY
RECONCILIATION OF THE BALANCE SHEET - GOVERNMENTAL FUNDS TO THE
STATEMENT OF NET POSITION
JUNE 30, 2014

Total fund balance - Governmental Funds	\$ 654,173
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Amounts reported for governmental activities in the statement of net position are different because:

Capital assets of \$6,600,964 net of accumulated depreciation of \$2,411,958 used in governmental activities are not financial resources and therefore are not reported in the governmental funds.	4,189,006
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Long-term liabilities, including bonds payable, are not due and payable in the current period and therefore are not reported in the governmental funds.	<u>(2,045,124)</u>
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Net position, end of year - Governmental Activities	<u><u>\$ 2,798,055</u></u>
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The accompanying notes to financial statements are an integral part of this statement.

CITY OF GRAYSON, KENTUCKY
STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES
GOVERNMENTAL FUNDS
FOR THE YEAR ENDED JUNE 30, 2014

	General	Special Revenue Funds		Total Governmental Funds
		Grant	Municipal Road Aid	
Revenues				
Taxes:				
Insurance	\$ 433,376	\$ -	\$ -	\$ 433,376
Mineral and coal	-	-	25,990	25,990
Motor vehicle	28,845	-	-	28,845
Payroll	876,536	-	-	876,536
Property	444,049	-	-	444,049
Fines & forfeitures	29,430	-	-	29,430
Franchise fees	18,191	-	-	18,191
Intergovernmental revenue:				
Base court	12,272	-	-	12,272
Grants	88,772	-	-	88,772
Alcohol license fees	80,311	-	-	80,311
Other license, fees, & permits	82,974	-	-	82,974
Municipal road aid	-	-	109,462	109,462
Police incentive	33,856	-	-	33,856
Interest income	552	2	49	603
Rental income	525	-	-	525
Other revenues	173,487	5,081	-	178,568
Total revenues	<u>2,303,176</u>	<u>5,083</u>	<u>135,501</u>	<u>2,443,760</u>
Expenditures				
General government	343,344	-	-	343,344
Fire	526,095	-	-	526,095
Police	1,085,588	7,052	-	1,092,640
Highways and streets	402,139	-	193,246	595,385
Parks and recreation	82,383	-	-	82,383
Emergency management	15,751	-	-	15,751
Cemetery	-	-	-	-
Total expenditures	<u>2,455,300</u>	<u>7,052</u>	<u>193,246</u>	<u>2,655,598</u>
Excess (deficiency) of revenues over (under) expenditures	<u>(152,124)</u>	<u>(1,969)</u>	<u>(57,745)</u>	<u>(211,838)</u>
Other Financing Sources (Uses)				
Loan proceeds	83,208	-	-	83,208
Transfers	-	-	-	-
Total other financing sources (uses)	<u>83,208</u>	<u>-</u>	<u>-</u>	<u>83,208</u>
Net change in fund balances	(68,916)	(1,969)	(57,745)	(128,630)
Fund balance, beginning of year	<u>716,184</u>	<u>8,397</u>	<u>58,222</u>	<u>782,803</u>
Fund balance, end of year	<u>\$ 647,268</u>	<u>\$ 6,428</u>	<u>\$ 477</u>	<u>\$ 654,173</u>

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

**CITY OF GRAYSON, KENTUCKY
RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES,
AND CHANGES IN FUND BALANCES OF GOVERNMENTAL FUNDS
TO THE STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED JUNE 30, 2014**

Net change in fund balances - Governmental Funds	\$	(128,630)
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Governmental funds report capital outlays as expenditures. However, in the Statement of Activities the cost of these assets are allocated over their estimated useful lives and reported as depreciation expense. This is the amount by which capital outlays exceeded depreciation expense in the current period.		75,420
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The issuance of long-term debt provides current financial resources to governmental funds, while repayment of the principal and interest consumes current financial resources of governmental funds. This amount is the net effect of these differences in the treatment of long-term debt and related items.		<div style="border-top: 1px solid black; display: inline-block; width: 100%;">72,896</div>
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Change in net position of Governmental Activities	\$	<div style="border-top: 1px solid black; border-bottom: 3px double black; display: inline-block; width: 100%;">19,686</div>
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The accompanying notes to financial statements are an integral part of this statement.

CITY OF GRAYSON, KENTUCKY
STATEMENT OF NET POSITION
PROPRIETARY FUND
JUNE 30, 2014

ASSETS

Cash and cash equivalents	\$ 1,773,867
Accounts receivable:	
Unbilled receivables	228,632
Customers	373,905
Interest	126
Allowance for doubtful accounts	(18,116)
Inventory for supplies	162,295
Restricted assets -	
Cash and cash equivalents	965,876
Nondepreciable capital assets	629,540
Depreciable capital assets	35,498,205
Accumulated depreciation	<u>(17,058,280)</u>
 Total assets	 <u>22,556,050</u>

LIABILITIES

Accounts payable	166,142
Accrued wages	63,849
Other accrued liabilities	10,838
Current portion of long-term debt	519,893
Accrued interest payable	47,842
Customer deposits	141,052
Long-term debt, net of current portion	<u>5,774,323</u>
 Total liabilities	 <u>6,723,939</u>

NET POSITION

Net investment in capital assets	12,775,249
Restricted	965,876
Unrestricted	<u>2,090,986</u>
 Total net position	 <u><u>\$ 15,832,111</u></u>

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

CITY OF GRAYSON, KENTUCKY
STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET POSITION
PROPRIETARY FUND
FOR THE YEAR ENDED JUNE 30, 2014

OPERATING REVENUES

Gas	\$ 1,685,057
Sewer	914,696
Water	2,089,178
Garbage	602,538
Total operating revenues	<u>5,291,469</u>

OPERATING EXPENSES

Gas:

Gas purchases	1,215,411
Salaries and benefits	188,712
Contractual services	22,299
Depreciation	108,619
Materials and supplies	112,946
Other operating expenses	91,347
	<u>1,739,334</u>

Sewer:

Salaries and benefits	269,159
Contractual services	18,050
Depreciation	308,673
Materials and supplies	148,507
Other operating expenses	289,776
	<u>1,034,165</u>

Water:

Salaries and benefits	682,033
Contractual services	76,672
Depreciation	451,832
Materials and supplies	500,898
Other operating expenses	496,181
	<u>2,207,616</u>

Garbage:

Contract	589,712
Total operating expenses	<u>5,570,827</u>

OPERATING INCOME (LOSS)

(279,358)

**NON-OPERATING REVENUES
(EXPENSES)**

Interest income	3,076
Gain on disposal of assets	1,200
Interest expense	(193,304)
Grant income	13,933
Total non-operating revenues (expenses)	<u>(175,095)</u>

LOSS BEFORE CAPITAL CONTRIBUTIONS

(454,453)

CAPITAL CONTRIBUTIONS

45,203

DECREASE IN NET POSITION

(409,250)

NET POSITION, JUNE 30, 2013, as restated

16,241,361

NET POSITION, JUNE 30, 2014

\$ 15,832,111

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

CITY OF GRAYSON, KENTUCKY
STATEMENT OF CASH FLOWS
PROPRIETARY FUNDS
FOR THE YEAR ENDED JUNE 30, 2014

CASH FLOWS FROM OPERATING ACTIVITIES

Cash received from customers	\$ 5,276,522
Cash payments to suppliers for goods and services	(3,386,801)
Cash payments to employees	<u>(1,121,337)</u>
Net cash provided by operating activities	<u>768,384</u>

**CASH FLOWS FROM CAPITAL
AND RELATED FINANCING ACTIVITIES**

Acquisition and construction of capital assets	(269,039)
Proceeds from sale of assets	1,200
Proceeds from issuance of long-term debt	30,680
Principal paid on long-term debt	(460,072)
Interest paid on long-term debt	(194,583)
Capital contributions	45,203
Capital grants received	<u>13,933</u>
Net cash used for capital and related financing activities	<u>(832,678)</u>

CASH FLOWS FROM INVESTING ACTIVITIES

Interest income	<u>3,075</u>
Net cash provided by investing activities	<u>3,075</u>

Net decrease in cash and cash equivalents (61,219)

Cash and cash equivalents, June 30, 2013 2,800,962

Cash and cash equivalents, June 30, 2014 \$ 2,739,743

**RECONCILIATION OF OPERATING LOSS
TO NET CASH PROVIDED BY OPERATING ACTIVITIES**

Operating loss	\$ (279,358)
Adjustments:	
Depreciation	869,124
Changes in assets and liabilities:	
Increase in accounts receivable	(14,947)
Decrease in inventory	26,481
Increase in accounts payable	148,517
Increase in accrued wages	22,266
Decrease in other accrued liabilities	(652)
Decrease in customer deposits	<u>(3,047)</u>
Net cash provided by operating activities	<u><u>\$ 768,384</u></u>

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

CITY OF GRAYSON, KENTUCKY
STATEMENT OF REVENUES, EXPENDITURES AND CHANGES
IN FUND BALANCE - BUDGET AND ACTUAL (NON-GAAP BUDGETARY BASIS)
GENERAL FUND
FOR THE YEAR ENDED JUNE 30, 2014

	Original Budget	Revisions	Revised Budget	Actual	Variance Positive (Negative)
Revenues					
Taxes:					
Property	\$ 406,750	\$ 42,420	\$ 449,170	\$ 472,894	\$ 23,724
License, fees, & permits	1,462,150	18,547	1,480,697	1,491,388	10,691
Intergovernmental revenues	147,767	(53,424)	94,343	92,665	(1,678)
Fines & forfeitures	22,000	4,865	26,865	29,430	2,565
Charges for services	3,800	(318)	3,482	2,565	(917)
Other revenues	5,733	225,526	231,259	171,999	(59,260)
Total revenues	2,048,200	237,616	2,285,816	2,260,941	(24,875)
Expenditures					
General government	332,112	1,228	333,340	343,344	(10,004)
Fire	279,223	195,925	475,148	484,947	(9,799)
Police	1,098,693	(12,230)	1,086,463	1,085,588	875
Highways and streets	298,608	88,653	387,261	402,139	(14,878)
Parks and recreation	110,500	16,514	127,014	82,383	44,631
Emergency management	15,486	265	15,751	15,751	-
Total expenditures	2,134,622	290,355	2,424,977	2,414,152	10,825
Excess (deficiency) of revenues over (under) expenditures	(86,422)	(52,739)	(139,161)	(153,211)	(14,050)
Other Financing Sources (Uses)					
Loan proceeds	-	83,208	83,208	83,208	-
Transfers	-	-	-	-	-
Total other financing sources (uses)	-	83,208	83,208	83,208	-
Net change in fund balance	(86,422)	30,469	(55,953)	(70,003)	(14,050)
Fund balance, beginning of year	86,422	(30,469)	55,953	716,184	660,231
Fund balance, end of year	\$ -	\$ -	\$ -	\$ 646,181	\$ 646,181
Adjustments to Generally Accepted Accounting Principles -					
Firemen's fund grant revenues				42,235	
Firemen's fund expenditures				(41,148)	
Fund balance, end of year (GAAP basis)				\$ 647,268	

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

CITY OF GRAYSON, KENTUCKY
STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCE - BUDGET AND ACTUAL
SPECIAL REVENUE FUND - GRANT
FOR THE YEAR ENDED JUNE 30, 2014

	Original Budget	Revisions	Revised Budget	Actual	Variance Positive (Negative)
Revenues					
Interest income	\$ -	\$ -	\$ -	\$ 2	\$ 2
Other revenues	-	-	-	5,081	5,081
Total revenues	-	-	-	5,083	5,083
Expenditures					
Police	-	-	-	7,052	(7,052)
Total expenditures	-	-	-	7,052	(7,052)
Net change in fund balance	-	-	-	(1,969)	(1,969)
Fund balance, beginning of year	-	-	-	8,397	8,397
Fund balance, end of year	\$ -	\$ -	\$ -	\$ 6,428	\$ 6,428

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

CITY OF GRAYSON, KENTUCKY
STATEMENT OF REVENUES, EXPENDITURES AND CHANGES
IN FUND BALANCE - BUDGET AND ACTUAL
SPECIAL REVENUE FUND - MUNICIPAL ROAD AID
JUNE 30, 2014

	Original Budget	Revisions	Revised Budget	Actual	Variance Positive (Negative)
Revenues					
Taxes					
Mineral and coal	\$ 20,133	\$ 5,857	\$ 25,990	\$ 25,990	\$ -
Intergovernmental revenues					
Grants	-	-	-	-	-
Municipal road aid	88,000	12,725	100,725	109,462	8,737
Interest income	-	-	-	49	49
Other revenues	-	-	-	-	-
Total revenues	<u>108,133</u>	<u>18,582</u>	<u>126,715</u>	<u>135,501</u>	<u>8,786</u>
Expenditures					
Highways and streets	<u>108,133</u>	<u>18,582</u>	<u>126,715</u>	<u>193,246</u>	<u>(66,531)</u>
Total expenditures	<u>108,133</u>	<u>18,582</u>	<u>126,715</u>	<u>193,246</u>	<u>(66,531)</u>
Excess (deficiency) of revenues over (under) expenditures	<u>-</u>	<u>-</u>	<u>-</u>	<u>(57,745)</u>	<u>(57,745)</u>
Other financing sources (uses)					
Loan proceeds	-	-	-	-	-
Transfers	-	-	-	-	-
Total other financing sources (uses)	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
Net change in fund balance	<u>-</u>	<u>-</u>	<u>-</u>	<u>(57,745)</u>	<u>(57,745)</u>
Fund balance, beginning of year	<u>-</u>	<u>-</u>	<u>-</u>	<u>58,222</u>	<u>58,222</u>
Fund balance, end of year	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 477</u>	<u>\$ 477</u>

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

CITY OF GRAYSON, KENTUCKY
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2014

(1) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. Reporting Entity

The City of Grayson (the "City") is a political subdivision of the Commonwealth of Kentucky. It is governed and operated under the Mayor/Council form of government and provides such services as public safety, public works, recreation, and community development. The financial statements of the City include those of separately administered organizations that are controlled by or dependent upon the City. Control or dependence is determined on the basis of funding and appointment of the voting majority of the governing board.

Based upon the foregoing criteria, the financial statements of the City of Grayson, Kentucky Utility Commission are blended into the City's financial statements, although retaining separate legal identity. A brief description of the activities and relationship to the City follows.

The City of Grayson, Kentucky established a Utility Commission in November 2000, for the purpose of managing and directing the various utility operations of the City. The Commission is composed of five members: the Mayor of the City of Grayson, Kentucky and four public members. The Commission has the full power and authority to appoint and remove all employees of the Grayson Utilities and to fix and allow compensation of employees. The Commission also has the power and authority to purchase all supplies, initiate repairs and maintenance and choose depositories for funds. The power and authority to change utility rates and initiate permanent/capital improvements remains with the City Council of the City of Grayson, Kentucky. The Commission is to make recommendations for rate changes and capital projects.

Complete financial statements of the component unit may be obtained at the Commission's administrative office:

City of Grayson, Kentucky Utility Commission
671 S. State Hwy 7
Grayson, Kentucky 41143

B. Government-Wide and Fund Financial Statements

The government-wide financial statements (i.e., the statement of net position and the statement of activities) report information on all of the activities of the City and its component unit. For the most part, the effect of interfund activity has been removed from these statements. *Governmental activities*, which normally are supported by taxes and intergovernmental revenues, are reported separately from *business-type activities*, which rely to a significant extent on fees and charges for support.

The statement of activities demonstrates the degree to which the direct expenses of a given function or segment is offset by program revenues. *Direct expenses* are those that are clearly identifiable with a specific function or segment. *Program revenues* include 1) charges to customers or applicants who purchase, use, or directly benefit from goods, services, or privileges provided by a given function or segment and 2) grants and contributions that are restricted to meeting the operational or capital requirements of a particular function or segment. Taxes and other items not properly included among program revenues are reported instead as *general revenues*.

Separate financial statements are provided for governmental funds and proprietary funds. The City considers all governmental and proprietary funds to be major funds, due to their belief that all of these funds present financial information which is important to the financial statement users. Thus, individual governmental funds and individual proprietary funds are reported as separate columns in the fund financial statements.

C. Measurement Focus, Basis of Accounting, and Financial Statement Presentation

The government-wide financial statements are reported using the *economic resources measurement focus* and the *accrual basis of accounting*, as are the proprietary fund financial statements. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Property taxes are recognized as revenues in the year for which they are levied. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

Governmental fund financial statements are reported using the *current financial resources measurement focus* and the *modified accrual basis of accounting*. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be *available* when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the City considers revenues to be available if they are collected within 60 days of the end of the current fiscal period. Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However, debt service expenditures, as well as expenditures related to compensated absences and claims and judgments, are recorded only when payment is due.

Property taxes, franchise taxes, grants, and interest associated with the current fiscal period are all considered to be susceptible to accrual and so have been recognized as revenues of the current fiscal period. All other revenue items are considered to be measurable and available only when cash is received by the government.

The City reports the following major Governmental Funds:

General Fund - The General Fund is the general operating fund of the City. It is used to account for all financial resources except those required to be accounted for in another fund.

Special Revenue Funds - Special Revenue Funds are used to account for the proceeds of specific revenue sources (other than expendable trusts or major capital projects) that are legally restricted to expenditures for specified purposes. The Grant Fund and Municipal Road Aid Funds are Special Revenue Funds that are major funds.

The City reports the following major Proprietary Fund:

Utility Fund - The Utility Fund is used to account for gas, water, wastewater (sewer) and garbage services for the City and surrounding communities.

As a general rule, the effect of interfund activity has been eliminated from the government-wide financial statements. Exceptions to this general rule are charges between the City Utility Fund and various other functions of the government. Elimination of these charges would distort the direct costs and program revenues reported for the various functions concerned.

Proprietary funds distinguish *operating* revenues and expenses from *nonoperating* items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. The principal operating revenue of the City's Enterprise Funds, are charges to customers for sales and services. Operating expenses for Enterprise Funds include the cost of sales and services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

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

D. Budget and Budgetary Accounting

The City follows these procedures in establishing the budgetary data reflected in the financial statements:

1. Prior to May 1, the City Clerk obtains estimates from the department heads in order to prepare the proposed budget.
2. Prior to June 30, the City Clerk submits to the City Council a proposed budget for the fiscal year commencing the following July 1. The proposed budget includes proposed operating and capital expenditures and the means of financing them.
3. Public hearings are conducted at council meetings in order to review the proposed budget and to obtain comments from taxpayers and other interested parties.
4. Prior to the first day beginning the fiscal year, the budget is legally adopted through the passage of an ordinance for the General Fund, all Special Revenue Funds, and all Enterprise Funds, and a separate budgetary report is prepared for utilization by the City, and for informational purposes for the general public.
5. The City Clerk is authorized to transfer budgeted amounts within departments of any fund; however, any revisions that alter the total expenditures of any department or fund must be approved by the City Council. Therefore, the level of control on budgetary items is maintained at the department level.
6. Budgets for the Special Revenue Funds are adopted on the modified accrual basis. Budgets for all Enterprise Funds are adopted on the accrual basis. Both methods are consistent with Generally Accepted Accounting Principles (GAAP). Budgeted amounts are as originally adopted, or as amended periodically by the City Council. Departmental revisions were not material in relation to the original appropriations which were amended. All appropriations lapse at the end of the fiscal year, even if encumbered.
7. Budgetary Basis of Accounting: The City's General Fund budgetary process accounts for certain transactions on a basis other than Generally Accepted Accounting Principles (GAAP). The major difference between the budgetary basis and the GAAP basis is that the firemen's fund is not budgeted in the General Fund, since those accounting records are maintained by the Fire Department and the activity added to the General Fund at year-end to include in the audit.

E. Deposits and Investments

Investments are stated at amortized cost which approximates fair value. Kentucky Revised Statute 66.480 permits the City to invest in U.S. Treasury obligations, U.S. Agency obligations, certain Federal instruments, repurchase agreements, commercial banks' certificates of deposit, savings and loan deposits, Commonwealth of Kentucky investment pool and the Kentucky League of Cities investment pool.

F. Inventories

Inventories are valued at the lower of cost (first-in, first-out method) or market.

G. Capital Assets and Depreciation

General capital assets are those assets not specifically related to activities reported in the proprietary funds. These assets generally result from expenditures in the governmental funds. These assets are reported in the governmental activities column of the government-wide statement of net position but are not reported in the fund financial statements. Capital assets utilized by the proprietary funds are reported both in the business-type activities column of the government-wide statement of net position and in the respective funds.

All capital assets are capitalized at cost (or estimated historical cost) and updated for additions and retirements during the year. Donated fixed assets are recorded at their fair market values as of the date received. Improvements are capitalized; the cost of normal

maintenance and repairs that do not add to the value of the asset or materially extend an assets life are not.

All reported capital assets are depreciated with the exception of land and construction in progress. Improvements are depreciated over the remaining useful lives of the related capital assets. Depreciation is computed using the straight-line method over the following useful lives for both general capital assets and proprietary fund assets:

<u>Description</u>	<u>Estimated Lives</u>
Gas System	22 years
Water and Sewer Systems	40-50 years
Equipment & Vehicles	3-10 years
Buildings	40 years

The City is required by GASB 34 to prospectively report general infrastructure assets in the statement of net position. During the 2014 fiscal year, there were no additions considered to be infrastructure assets.

H. Encumbrances

The City does not use a system of encumbrances in their accounting and reporting methods.

I. Interfund Transactions

During the course of normal operations, the City has numerous transactions between funds including expenditures and transfers of resources to provide services, construct assets, and service debt. The accompanying financial statements generally reflect such transactions as transfers.

J. Interfund Receivables and Payables

Activity between funds that are representative of lending/borrowing arrangements outstanding at the end of the fiscal year are referred to as either "due to/from other funds."

K. Compensated Absences

The City's accrued liabilities for future compensated absences are recorded to the extent the future leaves (1) relate to rights attributable to employee services already rendered, (2) relate to rights that vest or accumulate, (3) where payment is probable, and (4) where amounts can be reasonably estimated. Amounts that normally would be paid with expendable available financial resources are recorded in the Governmental Fund Financial Statements. Amounts paid or payable within 60 days are deemed to be payable from expendable available financial resources. Liabilities for compensated absences are recorded in full in the Government-wide and Proprietary Fund financial statements.

L. Fund Balances

The following classifications describe the relative strength of the spending constraints placed on the purposes for which resources can be used:

- Nonspendable fund balance-amounts that are not in a spendable form (such as inventory) or are required to be maintained intact;
- Restricted fund balance-amounts constrained to specific purposes by their providers (such as grantors, bondholders and higher levels of government), through constitutional provisions, or by enabling legislation;
- Committed fund balance-amounts constrained to specific purposes by the City itself, using its decision-making authority; to be reported as committed, amounts cannot be used for any other purpose unless the City takes the action to remove or change the constraint;

- Assigned fund balance-amounts the City intends to use for a specific purpose (such as encumbrances); intent can be expressed by the City Council or by an official or body to which the City delegates the authority;
- Unassigned fund balance-amounts that are available for any purpose; unassigned amounts are reported only in the General Fund.

When committed, assigned and unassigned resources are available for use, it is the City's policy to use committed and assigned resources first, then unassigned resources as they are needed.

M. Cash and Cash Equivalents

For purposes of the statements of cash flows, the Proprietary Funds consider all highly liquid investments (including restricted assets) with a maturity of three months or less when purchased to be cash equivalents.

N. Allowance for Doubtful Accounts

The allowance for doubtful accounts is estimated using accounts receivable past due more than 60 days.

O. Bond Issuance Costs

Debt issuance costs are expensed in the period they are incurred.

P. Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the recorded amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported revenues and expenditures during the reporting period. Material estimates that are particularly susceptible to significant changes relate to the determination of the allowance for uncollectible accounts and the useful lives used to depreciate capital assets. Actual results could differ from estimated amounts.

Q. Recent Accounting Pronouncements

The Governmental Accounting Standards Board (GASB) has issued GASB No. 65, *Items Previously Reported as Assets and Liabilities* which clarifies the use of deferred outflows of resources and deferred inflows of resources to ensure consistency in financial reporting. This statement requires certain items which were previously reported as assets and liabilities to be reported as deferred outflows of resources, deferred inflows of resources and as revenues or expenses. The City adopted GASB No. 65 for the year ended June 30, 2014. See Note 11.

The Governmental Accounting Standards Board (GASB) issued GASB No. 68, *Accounting and Financial Reporting for Pensions*, which changes the way pensions are reported on the financial statements of employers. Employers participating in a multiple-employer cost-sharing plan will be required to report net pension liability on the government-wide statements for their proportionate share of the liability. Cities will be required to record net pension liability for their share of the liability associated with employees participating in County Employees Retirement System (CERS) as well as any city-sponsored pension plans. There will be little to no impact on the balance sheets of the governmental funds. Additional note disclosures and required supplementary information (RSI) also are addressed in the standard. The standard is effective for fiscal year ending June 30, 2015. Management has not yet determined the effect this statement will have on the financial statements.

(2) CASH AND CASH EQUIVALENTS AND INVESTMENTS

Cash and cash equivalents at June 30, 2014 consisted of the following:

	Total	Unrestricted	Restricted
Petty cash	\$ 332	\$ 332	\$ -
Cash in banks	2,559,211	2,143,167	416,044
Certificates of deposit	628,000	-	628,000
	<u>\$ 3,187,543</u>	<u>\$ 2,143,499</u>	<u>\$ 1,044,044</u>

At June 30, 2014, the carrying amounts of the City's deposits were \$3,187,543 (cash in banks and certificates of deposits above) and the bank balances were \$3,329,030. Of the bank balances, \$981,571 was covered by the Deposit Insurance Fund and \$2,347,459 was collateralized with pledged securities held by the depositories in the City's name.

(3) PROPERTY TAX REVENUES

Property taxes include amounts levied against all real, public utility and tangible (used in business) property located in the City. Real property, tangible and public utility property taxes are levied prior to December 31 of each year based upon the assessed value as of January 1. Per KRS 91.487, the lien date for assessed taxes is January 1 of each fiscal year. The City imposes penalties of 2% for January and 6% thereafter.

Real property and tangible property taxes are due and payable by December 31 of each year. Public utility taxes are due and payable within thirty days from the date the bills are mailed. Assessed values are established by State Law at 100% of fair value. Real property and tangible property taxes are recognized as revenue on the modified accrual basis. Public utility taxes are not accrued at June 30, since assessed amounts are not available until the subsequent fiscal year.

Motor vehicle property taxes are assessed as of January 1 of each year and are collected by the County Clerk and remitted to the City. These taxes are not accrued, as amounts are payable upon the birth dates of the owners of the vehicles.

The 2014 assessed value for real and tangible property was \$184,773,543. The tax rate adopted was \$.198 per \$100 valuation.

(4) RESTRICTED ASSETS

Sinking and Debt Service Reserve Funds for Bond and Note Retirement

"Bond and Note Sinking Funds" and "Debt Service Reserve Funds" are being maintained as required by various bond and note documents. Deposits into Bond and Note Sinking Funds are made monthly in order to accumulate funds for payment of bond and note principal and interest. A Debt Service Reserve Fund is required for the purpose of having monies available in order to prevent a default in the payment of the principal or interest. A Debt Service Replacement Reserve Fund in the amount of \$491,000 is being invested in various federally insured banks (See Note 2). In addition, sinking funds are maintained on Rural Development bonds in the amount of \$337,876 as required.

Reserve for Depreciation

The "Depreciation Fund" is being maintained as required by various bond and loan documents. These funds are required to be deposited into separate accounts for the purpose of maintaining the water, sewer and gas systems. The amount deposited in these accounts was \$137,000 at June 30, 2014.

(5) CAPITAL ASSETS

A summary of changes in the City's capital assets is as follows:

	June 30, 2013	Increases	Decreases	June 30, 2014
<u>Governmental Activities</u>				
Capital Assets, Not Depreciated:				
Land	\$ 925,116	\$ -	\$ -	\$ 925,116
Capital Assets, Depreciated:				
City Hall	159,414	-	-	159,414
Leasehold improvements	26,979	-	-	26,979
Administrative office & equipment	67,673	-	-	67,673
Street equipment	766,285	166,067	-	932,352
Fire equipment & vehicles	1,362,269	179,053	-	1,541,322
Fire department buildings	1,586,614	-	-	1,586,614
Parks and recreation	89,861	18,927	-	108,788
Emergency management equipment	87,852	-	-	87,852
Police building	637,385	-	-	637,385
Police equipment & vehicles	439,297	88,172	-	527,469
Totals	6,148,745	452,219	-	6,600,964
Less: Accumulated Depreciation	2,035,159	376,799	-	2,411,958
Governmental Activities Capital Assets, Net	\$ 4,113,586	\$ 75,420	\$ -	\$ 4,189,006
<u>Business-type Activities</u>				
Capital Assets, Not Depreciated:				
Land	\$ 572,950	\$ -	\$ -	\$ 572,950
Construction in progress	13,450	43,140	-	56,590
Capital Assets, Depreciated:				
Cooks Wastewater Plant	2,023,385	-	-	2,023,385
General Equipment and vehicles	4,570,113	23,075	-	4,593,188
Water System	15,337,846	148,800	15,500	15,471,146
Gas System	3,591,549	-	-	3,591,549
Sewer System	9,764,913	54,024	-	9,818,937
Totals	35,874,206	269,039	15,500	36,127,745
Less: Accumulated Depreciation	16,204,656	869,124	15,500	17,058,280
Business-type Activities Capital Assets, Net	\$ 19,669,550	\$ (600,085)	\$ -	\$ 19,069,465

Depreciation expense was allocated to functions/programs of the primary government as follows:

Governmental activities:	
General government	\$ 11,929
Police	77,885
Fire	183,415
Street	84,055
Park	6,289
Emergency management	13,226
	<u>\$ 376,799</u>
Business-type activities:	
Utilities	<u>\$ 869,124</u>

(6) DEBT

The following is a summary of changes in long-term debt (including current portions) of the City for the year ended June 30, 2014:

	Balance June 30, 2013	Additions	Reductions	Balance June 30, 2014
<u>Governmental Activities</u>				
3.13% Kentucky League Of Cities note payable - Fire Station	\$ 1,193,819	\$ -	\$ 58,750	\$ 1,135,069

4.10% Capital Lease - Police station and Sallyport	568,535	-	57,358	511,177
2.88% Capital Lease - Tractor and bush hog	44,832	-	10,052	34,780
3.15% Capital Lease - Street Backhoe	-	51,485	537	50,948
3.25% Capital Lease - Street Truck	-	31,723	480	31,243
2.85% Capital Lease - New pumper truck	<u>310,834</u>	<u>-</u>	<u>28,927</u>	<u>281,907</u>
Total Governmental Activities	<u>\$ 2,118,020</u>	<u>\$ 83,208</u>	<u>\$ 156,104</u>	<u>\$ 2,045,124</u>
	Balance			Balance
<u>Business-type Activities</u>	<u>June 30, 2013</u>	<u>Additions</u>	<u>Reductions</u>	<u>June 30, 2014</u>
Notes payable	\$ 4,578,608	\$ 30,680	\$ 421,072	\$ 4,188,216
Bonds payable	<u>2,145,000</u>	<u>-</u>	<u>39,000</u>	<u>2,106,000</u>
Total Business-type Activities	<u>\$ 6,723,608</u>	<u>\$ 30,680</u>	<u>\$ 460,072</u>	<u>\$ 6,294,216</u>

Governmental Activities

The annual requirements to amortize the City's Governmental Activities indebtedness as of June 30, 2014 (including interest payments) are as follows:

<u>Year Ending June 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2015	\$ 164,177	\$ 66,869	\$ 231,046
2016	175,263	65,381	240,644
2017	182,178	59,410	241,588
2018	180,570	53,456	234,026
2019	184,145	47,429	231,574
2020-2024	710,095	152,139	862,234
2025-2029	448,696	50,750	499,446
	<u>\$ 2,045,124</u>	<u>\$ 495,434</u>	<u>\$ 2,540,558</u>

Conduit Debt Obligations

From time to time, the City has issued Industrial Revenue Bonds to provide financial assistance to private-sector entities for the acquisition and construction of industrial and commercial facilities deemed to be in the public interest. The bonds are secured by the property financed and are payable solely from payments received on the underlying loan agreements. Upon repayment of the bonds, ownership of the acquired facilities transfers to the private-sector entity served by the bond issuance. Neither the City, the state, nor any political subdivision thereof is obligated in any manner for repayment of the bonds. Accordingly, the bonds are not reported as liabilities in the accompanying financial statements.

As of June 30, 2014, there was one series of Industrial Revenue Bonds outstanding, with an aggregate principal amount payable of approximately \$4.4 million.

Business-Type Activities

The Utility Commission's notes payable at June 30, 2014 consisted of the following:

Kentucky Infrastructure Authority, payable in semi-annual installments of \$30,156, including interest of 1.7%, final payment due December 2025, collateralized by all the assets of the Commission's water system.	\$ 627,592
Kentucky Area Development District, payable in varying semi-annual installments, with interest at 2.5% to 5.4%, final payment due October 22, 2022, collateralized by the new utility building and water tower.	225,000
Kentucky Rural Water Finance Corporation Flexible Term Finance Program Series 2001H, payable in varying semi-annual installments, with interest at 2.25% to 4.375%, final payment due August 1, 2020, collateralized by all the assets of the Commission's water system.	225,000
Kentucky Infrastructure Authority, payable in semi-annual installments estimated at \$101,855, including interest of 1.8%, final payment due December 2022, collateralized by all the assets of the Commission's water system.	1,900,581
Kentucky Infrastructure Authority, payable in semi-annual installments, amount to be determined upon project completion, including interest of 1.0%, final payment due July 2032, collateralized by a pledge of utility revenues.	50,930
Kentucky Infrastructure Authority, payable in semi-annual installments of \$101,942, including interest of 1.8%, final payment due June 1, 2020, collateralized by all the assets of the Commission's wastewater system.	<u>1,159,113</u>
Total Utility Fund Notes Payable	<u>\$ 4,188,216</u>

The annual requirements to amortize all Proprietary Fund debt, excluding revenue bonds payable outstanding as of June 30, 2014, including interest are as follows:

<u>Year</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2015	\$ 478,393	\$ 86,352	\$ 564,745
2016	439,148	77,394	516,542
2017	445,952	67,835	513,787
2018	457,878	58,156	516,034
2019	464,930	48,095	513,025
2020-2024	1,409,970	119,376	1,529,346
2025-2026	491,945	12,878	504,823
Totals	<u>\$ 4,188,216</u>	<u>\$ 470,086</u>	<u>\$ 4,658,302</u>

Bonds Payable included in long-term debt in the accompanying financial statements includes the following:

Revenue Bonds:

\$450,000 Utilities Revenue Bonds, 1998A series, maturing through February 1, 2019, with interest at 4.5%	\$ 361,000
\$2,000,000 Utilities Revenue Bonds, 2001 series, maturing through February 1, 2042 with interest at 4.5%	<u>1,745,000</u>
Total Utility Fund Bonds Payable	<u>\$ 2,106,000</u>

Pledge of Utility Fund Revenues

Under the terms of the Ordinance authorizing the Series 1998 and the Ordinance authorizing the Series 1998A Bonds (the "1998A Ordinance"), the Series 1998 Bonds are payable from and secured by a first lien pledge of revenues and income derived from the ownership, operation, and use of services of the Utility's system.

Compliance with Bond Ordinances

The bond ordinances contain significant limitations and restrictions on annual debt reserve requirements, maintenance of and flow of monies through various restricted accounts, minimum amounts to be maintained in various sinking funds and minimum revenue bond coverage's. Funds held in the various reserves at June 30, 2014 required by the revenue bond ordinances are reported in the accompanying financial statements as restricted cash and cash equivalents.

Sinking Fund Requirements

Sinking Fund requirements are equal to the debt service requirement. The annual requirements to amortize all bonds as of June 30, 2014, including interest payments are as follows:

<u>Year</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2015	\$ 41,500	\$ 94,737	\$ 136,237
2016	42,500	92,870	135,370
2017	45,500	90,912	136,412
2018	47,000	88,865	135,865
2019	48,500	86,750	135,250
2020-2024	279,500	397,394	676,894
2025-2029	347,500	328,094	675,594
2030-2034	434,500	241,516	676,016
2035-2039	515,500	134,506	650,006
2040-2042	304,000	27,607	331,607
Totals	<u>\$ 2,106,000</u>	<u>\$ 1,583,251</u>	<u>\$ 3,689,251</u>

(7) RETIREMENT PLAN

The City of Grayson adopted a 457(b) retirement plan for its employees which includes the Utility Commission employees as of July 1, 1999. Participation in the plan is on a voluntary basis with eligibility starting after one year of full time employment. The City has no contract with the administrator of the plan specifying the time period for the vesting of matching funds, therefore, by default, upon participation all plan benefits are fully vested. The City contributes three percent of the employees' eligible salary, and the employees are required to match the three percent. Additional employee contributions are permissible up to ten percent of eligible salaries. A third party administrator maintains the plan assets and calculates benefits due. The City's contributions to the plan for the year ending June 30, 2014 were \$17,946.

The City participates in the County Employees Retirement System ("CERS"). CERS is a cost-sharing, multiple-employer, defined benefit plan administered by the Kentucky General Assembly. The plan covers substantially all regular full-time members employed in non-hazardous duty positions of each county and school board, and any additional eligible local agencies electing to participate in the plan. The plan provides for retirement, disability and death benefits to plan members.

CERS issues a publicly available financial report included in the Kentucky Retirement Systems Annual Report that includes financial statements and the required supplementary information for CERS. That report may be obtained by writing to Kentucky Retirement Systems, Perimeter Park West, 1260 Louisville Road, Frankfort, Kentucky 40601, or from the KRS website at <https://kyret.ky.gov>.

Funding for CERS is provided by members who contribute 5.00% of their salary through payroll deductions and by employers of members who contribute 18.89% of the member's salary. Plan members hired after July 1, 2008 contribute an additional 1% towards health insurance. The contribution requirements of CERS are established and may be amended by the CERS Board of Trustees. The City's contributions to CERS for the years ending June 30, 2014, 2013, and 2012 were \$119,914, \$120,308, and \$109,767, respectively, equal to the required contributions for the year.

(8) LEGAL CONTINGENCIES

The City is a defendant in various legal actions arising from normal business operations. The City's legal counsel believes these actions are without merit, adequately covered by insurance, or that the ultimate liability, if any, will not materially effect the City's financial position.

(9) RISK MANAGEMENT

Significant losses are covered by commercial insurance. There have been no significant reductions in insurance coverage. Settlement amounts have not exceeded insurance coverage for the current year or the three prior years.

(10) ECONOMIC DEPENDENCE

Two of the City's taxpayers provided \$300,574 (34%) of the City's occupational license withholding tax. The total amount paid by these companies represents 13% of the General Fund revenues.

(11) CHANGES IN BEGINNING NET POSITION

The City adopted a change in accounting principle for the year ending June 30, 2014. GASB 65, *Items Previously Reported as Assets and Liabilities* amends or supersedes accounting principles which required debt issuance costs to be amortized over the life of the debt issuance. Under GASB 65, the City is required to recognize debt issuance costs as an expense of the current period. While there were costs being amortized from prior periods, as a result, beginning net position of business-type activities was decreased \$58,125 to expense bond issue costs related to previous revenue bond issues.



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

The Honorable Mayor and
City Council
City of Grayson
Grayson, Kentucky

We have audited in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States the financial statements of the governmental activities, the business-type activities, and each major fund of the City of Grayson (the "City") as of and for the year ended June 30, 2014, and the related notes to the financial statements, which collectively comprise the City of Grayson's basic financial statements, and have issued our report thereon dated January 22, 2015.

Internal Control Over Financial Reporting

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

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

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

Compliance and Other Matters

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

Purpose of this Report

This 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 City's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Kelley Halloway Smith Toolsey, PSC

January 22, 2015
Ashland, Kentucky