

WATER DEPARTMENT
CITY OF KINGSTON, NEW YORK

FINANCIAL STATEMENTS

DECEMBER 31, 2014 AND 2013

TABLE OF CONTENTS

	<u>Page</u>
INDEPENDENT AUDITORS' REPORT	2-3
MANAGEMENT DISCUSSION AND ANALYSIS	4-9
FINANCIAL STATEMENTS:	
Statements of Net Position	10
Statements of Revenues, Expenses and Changes in Net Position	11
Statements of Cash Flows	12-13
Notes to the Financial Statements	14-24
SUPPLEMENTARY REPORTING :	
Independent Auditors' Reports on Internal Control and Compliance in Accordance with <i>Government Auditing Standards</i>	25-26

INDEPENDENT AUDITORS' REPORT

To the Board of Water Commissioners
Kingston Water Department
Kingston, New York

Report on the Financial Statements

We have audited the accompanying financial statements of the Water Department, City of Kingston, New York, an enterprise fund of the City of Kingston, as of and for the years ended December 31, 2014 and 2013, 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.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the 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 of 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.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Water Department, City of Kingston, New York, as of December 31, 2014 and 2013, and the changes in financial position and cash flows thereof for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As discussed in Note 1, the financial statements present only the Kingston Water Department and do not purport to, and do not, present fairly the financial position of the City of Kingston, New York, as of December 31, 2014 and 2013, and the changes in its financial position and cash flows for the years 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

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 4 – 9 be presented to supplement the basic financial statement. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated July 6, 2015 on our consideration of the Water Department, City of Kingston, New York's 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 the 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 Water Department, City of Kingston's internal control over financial reporting and compliance.

KIMBALL & O'BRIEN PC

By 

July 6, 2015



**KINGSTON WATER DEPARTMENT
PO BOX 1537
KINGSTON, NY 12402**

Management's Discussion and Analysis

This discussion and analysis of the Kingston Water Department's financial performance provides an overview of the Department's financial activities for the fiscal years ended December 31, 2014 and 2013. Administered by the Board of Water Commissioners, the Kingston Water Department is a financially and administratively independent department of the City of Kingston. Therefore, this report is restricted to a discussion and analysis of the business activities of the Water Department.

Financial Highlights

The Department's net position at year end 2014 was \$4,068,340. This is a decrease of \$92,099 from 2013. In 2014, operating revenues increased by \$196,927 while operating expenses increased by \$99,708.

Using This Annual Report

The Water Department is charged with the operation and maintenance of the City's water supply and is administered by the Board of Water Commissioners. All revenues for the operation of this utility come from the sale of water and related activities in the form of water rates and other fees that are charged to our customers. Since the Department's activities are restricted to the operation of the water supply, its annual report is limited to the Statements of Net Position, Statements of Revenues, Expenses and Changes in Net Position, and the Statements of Cash Flows.

Like most private-sector companies, the Water Department uses an accrual accounting system and, under this system, all of the current year's revenues and expenses are taken into account, regardless of when the cash is received or paid. In addition, our financial statements disclose the Department's assets and liabilities and report the difference between our assets and liabilities as net position. By reviewing and analyzing our financial statements, you can determine if the Department benefited from the previous year's operations and, by tracking changes in our net position, evaluate our overall financial health. However, to gain a complete understanding of the overall condition of the Department, you will need to also consider the condition of such non-financial factors as our reservoirs, treatment system, and distribution grid.

Condensed Comparative Financial Statements and Analysis

The Department's net position for 2014 is \$4,068,340. In contrast, the previous year's net position was \$4,160,439, a net decrease of \$92,099. Table 1 depicts the Department's net position for the last two years while Figure 1 and Table 2 shows how net position has changed over five years and two years, respectively. There was a decrease in net position of \$92,099 in the current year and there has been a net decrease in net position of \$874,609 in the past five years.

Table 1: Net Position

	2014	2013
Current and other Assets	\$ 6,578,747	\$ 3,137,005
Capital Assets	\$ 10,373,893	9,668,424
Total Assets	<u>\$ 16,952,640</u>	<u>\$ 12,805,429</u>
Long-term Debt Outstanding	\$ 7,850,960	\$ 7,933,070
Other Liabilities	\$ 5,033,340	711,920
Total Liabilities	<u>\$ 12,884,300</u>	<u>\$ 8,644,990</u>
Net Position:		
Invested in Capital Assets, Net of Debt	\$ 3,779,724	\$ 3,713,471
Restricted for Capital Projects	\$ 226,370	251,370
Unrestricted Assets	\$ 62,246	195,598
Total Net Position	<u>\$ 4,068,340</u>	<u>\$ 4,160,439</u>

Figure 1: Change in Net Position

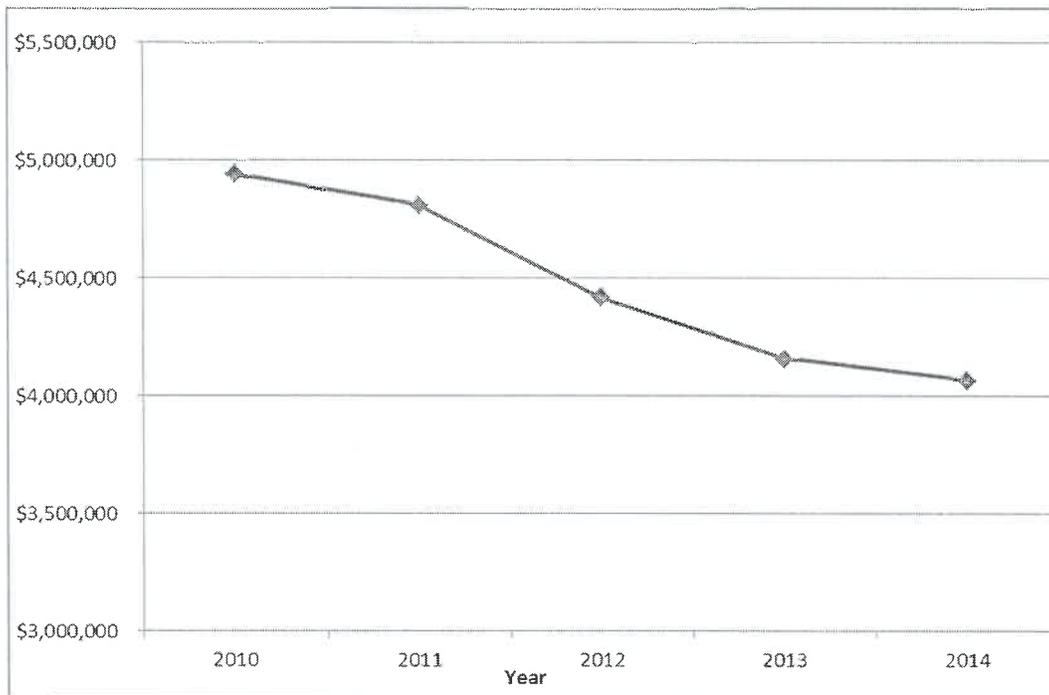
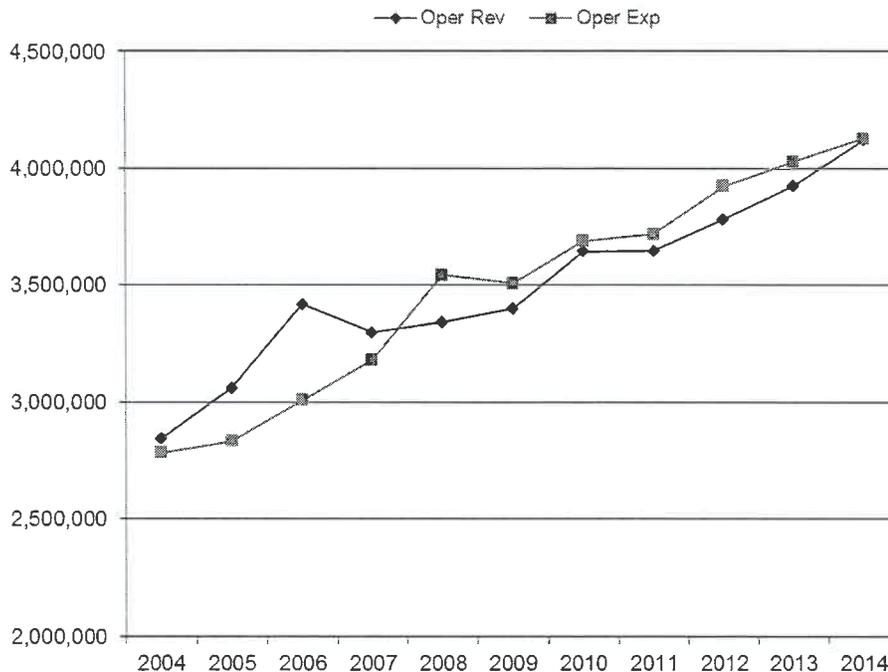


Table 2: Changes in Net Position

	2014	2013
Revenues		
Operating Revenues:		
Water Sales	\$ 3,812,502	\$ 3,654,510
Other	\$ 311,834	272,899
Total Operating Revenue	<u>\$ 4,124,336</u>	<u>3,927,409</u>
Non-operating Revenues:		
Sale of Property	\$ 9,416	2,206
Other	\$ 52,553	51,953
Total Revenues	<u>\$ 4,186,305</u>	<u>3,981,568</u>
Expenses		
Operating Expenses	\$ 4,130,658	4,030,950
Non-operating Expenses	\$ 147,746	210,797
Total Expenses	<u>\$ 4,278,404</u>	<u>4,241,747</u>
Decrease in Net Position	<u>\$ (92,099)</u>	<u>\$ (260,179)</u>

In 2014, the Department's revenues were \$4,186,305 and expenses were \$4,278,404 a net decrease in net position of \$92,099. Operations accounted for 99 percent of total revenues in both years. Operating expenses contributed 97 percent of total expenditures in 2014 and 95 percent of total expenditures in 2013. Figure 2 shows the relative change in operating revenues and expenses since 2004.

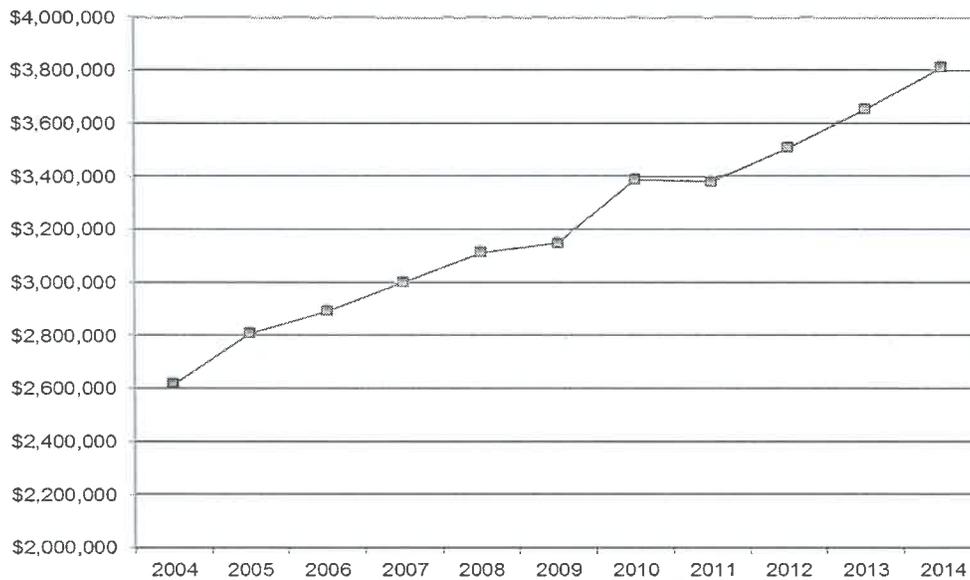
Figure 2: Operating Revenues and Expenses



In 2008, the implementation of the requirements of GASB 45 caused operating expenses to exceed operating revenue. That trend continues, but the gap appears to be narrowing. In 2014, expenses from operations exceeded operating revenues by \$6,322. In 2013, the gap was \$103,541. Although the actuarial algorithms used to calculate the Department's post-employment healthcare liability are complex, the philosophy behind the change in the accounting standard is relatively straightforward. Since all post-employment retirement benefits are part of the employee's compensation, they should be recognized while the employee is still working, rather than after they have retired. For that reason, GASB 45 has had a significant impact on the Department's financial reporting since 2008 in terms of the Statement of Net Position, Statement of Revenues and Expenses, and Changes in Net Position. However, it has no implication for the Statement of Cash Flows since there is no requirement, at this time, to fund the post employment healthcare liability while the employee is still in service. The Department continues to fund retiree health insurance costs from operations on a month to month basis as they are incurred. Therefore, there should be no adverse impact on the Department's annual budget estimates or on rates as a result of this change.

Water sales are the most significant component of Operating Revenue and accounted for 99 percent of Operating Revenue in both 2014 and 2013. As shown in Figure 3, the net increase in water sales from 2013 to 2014 was \$157,992. This is in line with the net increase of \$144,141 in the previous year.

Figure 3: Water Sales



Capital Asset and Debt Administration

Capital Assets

Table 3 lists the amounts that have been invested in a broad range of capital assets. These include investment in our watershed, treatment facilities, distribution system, and our business office. Without factoring in accumulated depreciation, these amounts represent additions of approximately \$1,142,795 in 2014 and \$4,129,010 since 2010. Through sound investment in capital improvements, the Board of Water Commissioners has increased the Department's capital assets by almost 300 percent over the past 15 years.

During the past 5 years, the Department has reconstructed the raw water intake, built a new ultraviolet water treatment facility, and began a mandated dam safety inspection and evaluation program at our reservoirs that will require that significant repair and rehabilitation work be undertaken in the near future. In addition, the Department has painted the exterior of the Florence Street Tank, re-installed key water

mains under the CSX railroad tracks, and made significant investments to improve its technology across all sectors of its operations. This was done to improve efficiencies, meet regulatory mandates, and enhance security.

Table 3: Capital assets at Year-end (Net of Depreciation)

	2014	2013
Land	\$ 118,729	\$ 118,729
Construction in Progress	\$ 686,333	466,599
Buildings and Equipment	\$ 16,266,948	15,343,887
Subtotals	\$ 17,072,010	15,929,215
Accumulated Depreciation	\$ (6,698,117)	(6,260,791)
Totals	\$ 10,373,893	\$ 9,668,424

Debt

All of the Department’s debt is issued through the City of Kingston. The City’s bond rating is A+. Other obligations include accrued compensated absences and post-employment healthcare benefits. More detailed information about the Department’s long-term liabilities is presented in Note 2 (B)3 to the Financial Statements. Table 4 presents a summary of our outstanding debt at year-end.

Table 4: Outstanding Debt at Year-end

	2014	2013
General Obligation Bonds (Backed by the City)	\$ 36,000	\$ 41,000
Revenue Bonds (NYS EFC RLF)	5,425,000	5,792,158
Post-emp Health Care Benefits	2,448,452	2,141,745
Compensated Absences	235,407	269,218
Installment Purchase Debt	46,210	60,017
Totals	\$8,191,069	\$ 8,304,138

Economic Factors and Next Year’s Budget and Rates

Since the Water Department is only engaged in business-type activities, it does not have a legally adopted budget. However, the Board of Water Commissioners prepares and adopts an annual budget that is used by the Department as a planning tool. The Board and staff have worked hard to balance any increase in spending with the need to maintain our infrastructure and the level of service to our customers in a difficult economy. Through careful management, the 2015 budget is \$4,673,000 and represents an increase of \$542,000 over the 2014 budget of \$4,131,000. The majority of the increase, which was funded by a 5 percent increase in rates as well as a transfer from the Department’s capital account, was due to increases in debt service for capital projects related to infrastructure improvements and regulatory mandates.

The Department has a Capital Improvement Plan that is updated regularly. The current plan spans the period 2015 through 2019 and calls for \$17,815,029 to be spent on projects during that period. These include mandated improvements to the Cooper Lake Dam, the replacement of the backwash tower at the Plant, the installation of a system-wide control system, as well as distribution system repair and

replacement projects. Residents of Kingston enjoy water of the highest quality and the Department's infrastructure network is the lifeblood of our water supply. As we enter our 120th year of operation, we must continue to make an investment in that infrastructure so that we can pass this resource on to future generations. In addition, new regulations and security concerns dictate that we continue to upgrade our technology and improve our capabilities. On the revenue side, water sales in 2015 are projected to account for 87 percent (\$4,062,000) of the Department's income. Five percent of budget revenues are expected to come from transfers from the Department's capital account. The balance of the Department's revenue (\$376,000) will be derived from related fees.

The Board of Water Commissioners struggles to fulfill the Department's mandate to provide the residents and businesses of the City of Kingston with high quality drinking water while keeping rates affordable. Kingston's tap water delivers public health protection, fire protection, support for the economy, and the overall quality of life we enjoy at a cost of about \$1.30 for 250 gallons of water for most of our customers.

Contacting the Department's Financial Management

The financial report is designed to provide citizens, customers, and creditors with a general overview of the Water Department's finances and to show the Department's accountability for the money it receives. If you have questions about this report or need additional financial information, please contact Superintendent Judith Hansen at 845- 331-0175 or by email at water@kingston-ny.gov.

Judith A. Hansen
Superintendent
July 6, 2015

WATER DEPARTMENT, CITY OF KINGSTON, NY
STATEMENTS OF NET POSITION
DECEMBER 31, 2014 AND 2013

	<u>2014</u>	<u>2013</u>
ASSETS:		
Current assets:		
Cash and cash equivalents	\$ 1,069,956	\$ 721,897
Accounts receivable	1,019,027	983,531
Inventory	127,875	110,464
Prepaid expenses	232,683	200,408
Due from City of Kingston	8,090	3,863
Total current assets	<u>2,457,631</u>	<u>2,020,163</u>
Noncurrent assets:		
Cash and cash equivalents, long-term	3,894,746	865,472
Investments	226,370	251,370
Capital Assets:		
Land	118,729	118,729
Construction in progress	686,333	466,599
Buildings and equipment	16,266,948	15,343,887
Less: accumulated depreciation	<u>(6,698,117)</u>	<u>(6,260,791)</u>
Total capital assets, net	<u>10,373,893</u>	<u>9,668,424</u>
Total noncurrent assets	<u>14,495,009</u>	<u>10,785,266</u>
Total assets	<u>\$ 16,952,640</u>	<u>\$ 12,805,429</u>
LIABILITIES:		
Current liabilities:		
Accounts payable	\$ 144,584	\$ 166,456
Accrued expenses	87,056	54,309
Due to City of Kingston	4,007	67,199
Due to other governments	5,917	5,703
Bonds and notes payable	380,576	385,965
Bond anticipation notes payable	4,410,400	-
Compensated absences payable	-	31,488
Deposits	800	800
Total current liabilities	<u>5,033,340</u>	<u>711,920</u>
Noncurrent liabilities:		
Bonds and notes payable	5,126,634	5,507,210
Postemployment healthcare benefits	2,448,452	2,141,745
Due to other governments	40,467	46,385
Compensated absences payable	235,407	237,730
Total noncurrent liabilities	<u>7,850,960</u>	<u>7,933,070</u>
Total liabilities	<u>12,884,300</u>	<u>8,644,990</u>
NET POSITION:		
Invested in capital assets, net of related debt	3,779,724	3,713,471
Restricted for Capital Projects	226,370	251,370
Unrestricted	62,246	195,598
Total net position	<u>4,068,340</u>	<u>4,160,439</u>
Total liabilities and net position	<u>\$ 16,952,640</u>	<u>\$ 12,805,429</u>

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

WATER DEPARTMENT, CITY OF KINGSTON, NY
STATEMENTS OF REVENUES, EXPENSES & CHANGES IN NET POSITION
YEARS ENDED DECEMBER 31, 2014 AND 2013

	<u>2014</u>	<u>2013</u>
OPERATING REVENUES		
Water sales	\$ 3,812,502	\$ 3,654,510
Water service charges	62,495	63,425
Interest and penalties on water sales	72,228	64,725
Water analysis fees	75,865	81,408
City of Kingston revenue	51,849	47,457
Miscellaneous revenues	49,397	15,884
Total operating revenues	<u>4,124,336</u>	<u>3,927,409</u>
OPERATING EXPENDITURES		
Water administration	467,313	437,259
Source of supply, power and pumping	2,639	2,382
Purification	881,344	795,983
Laboratory	18,097	16,719
Transmission and distribution	739,917	722,393
Engineering	28,360	30,597
Real estate taxes	268,099	269,815
Depreciation	530,634	508,788
Employee benefits	<u>1,194,255</u>	<u>1,247,014</u>
Total operating expenses	<u>4,130,658</u>	<u>4,030,950</u>
Operating loss	<u>(6,322)</u>	<u>(103,541)</u>
NONOPERATING REVENUES (EXPENSES)		
Investment earnings	1,430	1,617
Loss on disposal of assets	(6,649)	(44,832)
Sale of property	9,416	2,206
Rental income	51,123	50,336
Interest expense	<u>(141,097)</u>	<u>(165,965)</u>
Total nonoperating expenses	<u>(85,777)</u>	<u>(156,638)</u>
Change in net position	(92,099)	(260,179)
Net position, beginning of year	<u>4,160,439</u>	<u>4,420,618</u>
Net position, end of year	<u>\$ 4,068,340</u>	<u>\$ 4,160,439</u>

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

WATER DEPARTMENT, CITY OF KINGSTON, NY
STATEMENTS OF CASH FLOWS
YEARS ENDED DECEMBER 31, 2014 AND 2013

	<u>2014</u>	<u>2013</u>
CASH FLOWS FROM OPERATING ACTIVITIES:		
Receipts from customers	\$ 4,084,613	\$ 3,873,186
Payments to suppliers	(2,038,056)	(1,701,826)
Payments to employees	<u>(1,382,625)</u>	<u>(1,400,472)</u>
Net cash provided by operating activities	<u>663,932</u>	<u>770,888</u>
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES:		
Proceeds from capital debt	4,410,400	-
Proceeds from sale of capital assets	9,416	2,206
Acquisition of capital assets	(1,252,486)	(236,975)
Principal paid on capital debt	(385,965)	(421,078)
Interest paid on debt	<u>(145,517)</u>	<u>(163,491)</u>
Net cash provided by (used for) financing activities	<u>2,635,848</u>	<u>(819,338)</u>
CASH FLOWS FROM INVESTING ACTIVITIES:		
Proceeds from investments	25,000	119,712
Interest on investments	1,430	1,617
Rental income	<u>51,123</u>	<u>50,336</u>
Net cash provided by investing activities	<u>77,553</u>	<u>171,665</u>
NET INCREASE IN CASH AND CASH EQUIVALENTS	3,377,333	123,215
CASH AND CASH EQUIVALENTS - BEGINNING	<u>1,587,369</u>	<u>1,464,154</u>
CASH AND CASH EQUIVALENTS - ENDING	<u>\$ 4,964,702</u>	<u>\$ 1,587,369</u>
Cash and cash equivalents	\$ 1,069,956	\$ 721,897
Cash and cash equivalents, long-term	<u>3,894,746</u>	<u>865,472</u>
Total cash and cash equivalents at end of year	<u>\$ 4,964,702</u>	<u>\$ 1,587,369</u>
 NON-CASH INVESTING ACTIVITY-		
Fixed assets in accounts payable	<u>\$ 44,293</u>	<u>\$ 61,778</u>

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

WATER DEPARTMENT, CITY OF KINGSTON, NY
STATEMENTS OF CASH FLOWS
YEARS ENDED DECEMBER 31, 2014 AND 2013

	<u>2014</u>	<u>2013</u>
RECONCILIATION OF OPERATING INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES:		
Operating loss	\$ (6,322)	\$ (103,541)
Adjustments to reconcile operating loss to net cash provided by operating activities:		
Depreciation	530,634	508,788
Changes in assets and liabilities:		
Accounts receivable	(35,496)	(64,036)
Inventory	(25,162)	5,764
Due from City of Kingston	(4,227)	9,813
Prepaid expenses	(32,275)	12,034
Accounts payable (operating)	(4,387)	31,532
Due to other governments	(5,704)	(3,138)
Due to City of Kingston	(63,192)	64,548
Accrued expenses	37,167	(21,413)
Postemployment healthcare benefits	306,707	346,021
Compensated absences payable	(33,811)	(15,484)
	<u>\$ 663,932</u>	<u>\$ 770,888</u>

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

WATER DEPARTMENT, CITY OF KINGSTON, NEW YORK
NOTES TO THE FINANCIAL STATEMENTS
DECEMBER 31, 2014 AND 2013

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Water Department of the City of Kingston, New York (Water Department) is an enterprise fund of the City of Kingston established in 1895. It operates a municipal water system for city residents and businesses and includes delivery and processing of the water as well as maintenance of the plant and equipment necessary for this goal. The basic operations of the Water Department are financed by billings collected from residents and businesses based on metered readings determining usage of municipal water.

The financial statements of the Water Department have been prepared in accordance with generally accepted accounting principles (GAAP) as applied to government units. The Governmental Accounting Standards Board (GASB) is the accepted standard setting body for establishing governmental accounting and financial reporting principles. The more significant accounting policies used by the Water Department are discussed below.

The Water Department has implemented the financial reporting requirements of GASB Statement No. 34, *Basic Financial Statements-and Management's Discussion and Analysis-for State and Local Governments*. These requirements include a Management Discussion and Analysis (MD&A) section providing an analysis of the Water Department's overall financial position and results of operations. As an enterprise fund, the Water Department presents only one set of financial statements.

A. Reporting Entity

These financial statements are intended to present the financial position and results of operations and cash flows of only that portion of the funds of the City of Kingston, New York, that is attributable to the transactions of the Water Department. The Water Department's policies are governed by a Board of Commissioners (the Board).

The City of Kingston's charter states that any funds in excess of what is required for operations must first be applied to the payment of principal and interest on debt obligations. Any funds in excess of the needs of operations or debt service is available for the City of Kingston's purposes.

B. Basis of Accounting / Measurement Focus

Governmental units that conduct business and quasi-business activities are accounted for in a manner similar to commercial enterprises. The Water Department uses an "economic resources" measurement focus. The accounting objectives of this measurement focus are the determination of operating income, changes in net assets, financial position, and cash flows. The Water Department utilizes the accrual basis of accounting. Under the accrual basis of accounting, revenues are recognized when earned and expenses are recorded when the liability is incurred or economic asset used. Operating revenues and expenses result from the supplying of water as noted above.

WATER DEPARTMENT, CITY OF KINGSTON, NEW YORK
NOTES TO THE FINANCIAL STATEMENTS
DECEMBER 31, 2014 AND 2013

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

C. Deferred Outflows/Inflows of Resources

GASB Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*, and GASB Statement No. 65, *Items Previously Reported as Assets and Liabilities*, defined and classified deferred outflows of resources and deferred inflows of resources. A deferred outflow of resources is a consumption of net assets that applies to future period(s), and as such, will not be recognized as an outflow of resources (expense/expenditure) until that time. A deferred inflow of resources is an acquisition of net assets that applies to future period(s), and as such, will not be recognized as an inflow of resources (revenue) until that time.

D. Financial Statement Amounts

1) Cash and Cash Equivalents – For purposes of reporting cash flows, the cash equivalents are defined as short-term, highly liquid investments that are both readily convertible and near their maturity. Cash and cash equivalents, long-term, represents internally restricted cash. It is the Water Department's intent to use this cash to fund certain capital projects and as a result has classified this cash and cash equivalents as long-term.

2) Accounts Receivable - No allowance for doubtful accounts is maintained as uncollected accounts are turned over to the City at the end of the year to be added on to the tax bills. The City reimburses the Water Department for the full amount even though the City may not have actually received payment.

3) Inventory – Inventory is recorded at cost using the first-in, first-out (FIFO) method.

4) Capital Assets – Capital assets (including infrastructure) are recorded at cost. Interest is capitalized for debt related to construction in progress. Depreciation is computed by straight-line methods at rates adequate to recover the cost of all assets over their expected useful lives.

Major outlays for capital assets and improvements are capitalized as projects are constructed. The cost of normal maintenance and repairs that do not add to the value of the asset or materially extend assets lives are not capitalized.

5) Insurance – The Water Department assumes the liability for most risk including, but not limited to, property damage and personal injury liability. Risk of loss is controlled by the purchase of commercial insurance. Judgments and claims are recorded when it is probable that an asset has been impaired or a liability has been incurred and the amount of loss can be reasonably estimated.

WATER DEPARTMENT, CITY OF KINGSTON, NEW YORK
NOTES TO THE FINANCIAL STATEMENTS
DECEMBER 31, 2014 AND 2013

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

D. Financial Statement Amounts (continued)

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

7) Net Position – Net position is an element of proprietary fund financial statements, and is measured by the difference between (a) assets and deferred outflows of resources and (b) liabilities and deferred inflows of resources.

NOTE 2 - DETAILED NOTES

A. Assets

1) Cash – The Water Department's investment policies are governed by state statutes. In addition, the Department has its own investment policy. Water Department monies must be deposited in FDIC-insured commercial banks or trust companies located within the state. The Superintendent is authorized to use demand accounts and certificates of deposit. Collateral is required for all deposits not covered by federal deposit insurance. Obligations that may be pledged as collateral are obligations of the United States and its agencies and obligations of the State and its municipalities and school districts. Deposits at year-end were entirely covered by federal depository insurance or by collateral held by the bank in the City of Kingston's name.

2) Investments – The Water Department received the proceeds from the issuance of the State Revolving Funds Revenue Bonds described in Note B(3) in the form of Guaranteed Investment Contracts. The funds are held by M&T and released upon approval by NYS Environmental Facilities Corporation of requisition for disbursement for construction costs.

WATER DEPARTMENT, CITY OF KINGSTON, NEW YORK
NOTES TO THE FINANCIAL STATEMENTS
DECEMBER 31, 2014 AND 2013

NOTE 2 - DETAILED NOTES (CONTINUED)

3) Capital Assets - A summary of changes in capital assets follows:

	Balance 12/31/13	Additions	Disposal / Transfers	Balance 12/31/14
Reservoir improvements	\$ 3,659,349	\$ 5,406	\$ (1,244)	\$ 3,663,511
Machinery and tools	218,474	9,866	(36,633)	191,707
Filter house equipment	157,592	-	(18,865)	138,727
Vehicles and heavy equipment	433,631	-	-	433,631
Office equipment	155,936	12,630	(20,491)	148,075
Distribution system	2,764,270	14,529	926,705	3,705,504
Filter plant and lagoon	5,812,138	14,328	(2,023)	5,824,443
Meters	950,651	47,787	(28,934)	969,504
Chemical treatment facility	373,310	-	-	373,310
Office renovation	937,265	-	-	937,265
	<u>15,462,616</u>	<u>104,546</u>	<u>818,515</u>	<u>16,385,677</u>
Construction in progress	<u>466,599</u>	<u>1,130,456</u>	<u>(910,722)</u>	<u>686,333</u>
	<u>\$ 15,929,215</u>	<u>\$ 1,235,002</u>	<u>\$ (92,207)</u>	<u>\$ 17,072,010</u>

4) Due from City of Kingston Balances – Generally, outstanding balances include outstanding charges between the City of Kingston and the Water Department for services and borrowing arrangements. The Water Department acts as the billing and collection agent for the Sewer Fund of the City of Kingston. Below is a schedule of amounts due from (to) other funds of the City of Kingston.

Due from:

General Fund	\$ <u>8,090</u>
--------------	-----------------

Due to:

General Fund	\$ 2,865
Sewer Fund	<u>1,142</u>
	<u>\$ 4,007</u>

WATER DEPARTMENT, CITY OF KINGSTON, NEW YORK
NOTES TO THE FINANCIAL STATEMENTS
DECEMBER 31, 2014 AND 2013

NOTE 2 - DETAILED NOTES (CONTINUED)

B. Liabilities

1) Pension Plan

a) Plan Description – The Water Department of the City of Kingston participates in the New York State and Local Employees' Retirement System (ERS) and the Public Employees' Group Life Insurance Plan, collectively known as NYSLRS. These are cost-sharing multiple-employer retirement systems. The NYSLRS provides retirement benefits as well as death and disability benefits. Obligations of employers and employees to contribute and benefits to employees are governed by the New York State Retirement and Social Security Law (NYSRSSL). As set forth in the NYSRSSL, the Comptroller of the State of New York (Comptroller) serves as sole trustee and administrative head of the NYSLRS. The Comptroller shall adopt and may amend rules and regulations for the administration and transaction of the business of the NYSLRS and for the custody and control of its funds. The NYSLRS issue a publicly available financial report that includes financial statements and required supplementary information. That report may be found at www.osc.state.ny.us/retire/publications/index.php or obtained by writing to the New York State and Local Retirement Systems, 110 State Street, Albany, NY 12244.

b) Funding Policy – The Systems are noncontributory except for employees who joined the Retirement System after July 27, 1976, who contribute 3% of their salary for the first ten years of membership and employees who joined on or after January 1, 2010 (ERS) who generally contribute 3% of their salary for the entire length of service. Under the authority of the NYSRSSL, the Comptroller annually certifies the actuarially determined rates expressly used in computing the employers' contributions based on salaries paid during the NYSLRS' fiscal year ending March 31. Contributions for 2012-2014 were equal to 100 percent of the contributions required, and were as follows:

2014	\$247,323
2013	272,811
2012	260,268

Chapter 57 of the Laws of 2010 of the State of New York was enacted that allows local employers to amortize a portion of their retirement bill for 10 years in accordance with the following stipulations:

- For State fiscal year 2010-11, the amount in excess of the graded rate of 9.5 percent of employees' covered pensionable salaries, with the first payment of those pension costs not due until the fiscal year succeeding that fiscal year in which the amortization was instituted.
- For subsequent State fiscal years, the graded rate will increase or decrease by up to one percent depending on the gap between the increase or decrease in the NYSLRS's average rate and the previous graded rate.

WATER DEPARTMENT, CITY OF KINGSTON, NEW YORK
NOTES TO THE FINANCIAL STATEMENTS
DECEMBER 31, 2014 AND 2013

NOTE 2 - DETAILED NOTES (CONTINUED)

B. Liabilities (continued)

1) Pension Plan (continued)

b) Funding Policy (continued)

- For subsequent State fiscal years in which the NYSLRS's average rates are lower than the graded rates, the employer will be required to pay the graded rate. Any additional contributions made will first be used to pay off existing amortizations, and then any excess will be deposited into a reserve account and will be used to offset future increases in contribution rates.

This law requires participating employers to make payments on a current basis, while amortizing existing unpaid amounts relating to the NYSLRS's fiscal years when the local employer opts to participate in the program. The Department paid \$144,814 in 2011 and is amortizing \$62,883 of the required contribution over 10 years. The Department made principal and interest payments of \$7,657 in 2014 and 2013, leaving a liability of \$46,384 and \$52,088 at December 31, 2014 and 2013, respectively.

2) Short-Term Debt

The Department will issue bond anticipation notes (BANS) for short-term financing. The notes or renewals thereof may not extend more than two years beyond the original date of issue unless a portion is redeemed within two years and within each 12-month period thereafter. State law requires that BANS issued for capital purposes be converted to long-term obligations within five years after the original issue date.

The following is a summary of BANS outstanding at December 31, 2014:

<u>Description</u>	<u>Date of Issue</u>	<u>Maturity Date</u>	<u>Interest Rate</u>	<u>Balance 12/31/14</u>
1) To replace water mains.	3/25/2014	3/25/2015	0.49%	\$ 675,000
2) To paint the Florence Street water tower.	3/25/2014	3/25/2015	0.49%	575,000
3) For reconstruction and construction of improvements to the water treatment facility, including filter rehabilitation and backwash tank replacement.	10/29/2014	3/25/2015	1.00%	3,160,400
				<u><u>\$ 4,410,400</u></u>

WATER DEPARTMENT, CITY OF KINGSTON, NEW YORK
NOTES TO THE FINANCIAL STATEMENTS
DECEMBER 31, 2014 AND 2013

NOTE 2 - DETAILED NOTES (CONTINUED)

B. Liabilities (continued)

3) Long-Term Debt

a) Serial Bonds – The Common Council has authorized the issuance of various serial bonds, backed by the full faith and credit of the City, for improvements to the water distribution system of the City of Kingston.

b) Loans Payable – NYS Environmental Facilities –

The Department received \$1,183,625 from the 1998 State Clean Water and Drinking Water Revolving Fund Revenue Bond for improvements to the filtration plant. In addition, the Department received \$2,545,816 from the 2004 Bond and \$571,283 from the 2005 Bond for improvements to the water treatment plant. Interest payments are reduced by subsidies from the state.

The Department issued \$3,135,128 of long-term financing in June 2012 to refinance short term financing: \$2,805,906 for the Binnewater Reservoir Compliance Project and \$746,252 for the Mink Hollow Renovation Project. After subtracting bond issuance costs of \$54,416, the remaining proceeds of \$365,614 were placed in a fund administered by M&T Bank to be used per Note 2(A)(2).

c) Installment Purchase Debt – The Department entered into a lease purchase agreement with Navistar Financial Corporation during 2010 in the amount of \$96,888 for the purchase of a vehicle.

The outstanding loan balances are as follows:

Date of Issue	Interest Rate	Balance			Balance 12/31/14
		12/31/13	Issued	Paid	
July 22, 2004	1.99-5.025%	\$ 1,705,000	\$ -	\$ 120,000	\$ 1,585,000
March 3, 2005	2.10-4.405%	375,000	-	25,000	350,000
July 15, 2006	4.25-4.375%	41,000	-	5,000	36,000
June 11, 2010**	5.9%	60,017	-	13,807	46,210
February 11, 2011	.789-3.283%	325,000	-	65,000	260,000
June 21, 2012	.285-3.400%	2,675,906	-	125,906	2,550,000
June 21, 2012	.285-3.400%	711,252	-	31,252	680,000
		<u>\$ 5,893,175</u>	<u>\$ -</u>	<u>\$ 385,965</u>	<u>\$ 5,507,210</u>

**Installment purchase debt described in Note 3 c).

WATER DEPARTMENT, CITY OF KINGSTON, NEW YORK
NOTES TO THE FINANCIAL STATEMENTS
DECEMBER 31, 2014 AND 2013

NOTE 2 - DETAILED NOTES (CONTINUED)

B. Liabilities (continued)

3) Long-Term Debt (continued)

The outstanding bonds mature as follows:

<u>Period</u>	<u>Principal</u>	<u>Interest</u>	<u>Period</u>	<u>Principal</u>	<u>Interest</u>
2015	\$ 380,576	\$ 145,924	2020-24	1,785,000	429,940
2016	395,388	138,682	2025-29	1,160,000	190,733
2017	406,246	130,526	2030-32	650,000	33,128
2018	395,000	121,462	Total	<u>\$ 5,507,210</u>	<u>\$ 1,303,676</u>
2019	335,000	113,281			

The total interest incurred for 2014 and 2013 was \$149,288 and \$161,446 respectively, of which \$10,144 was capitalized in 2014. The total interest due to maturity is estimated to be \$1,303,676. The exact amount is unknown due to the interest subsidy on the New York State DWRLF bonds. The amount of the subsidy is based on investment earnings. The total subsidy for 2014 and 2013 was \$34,441 and \$33,854 respectively.

d) Compensated Absences – The sick leave policy for the Water Department allows an employee to accumulate up to 150 sick days. After 20 years of service and upon retirement the employee is compensated at a rate of 75% of the accumulated amount. Since most employees are long-term, the 75% rate is applied to all employee balances even though they have not obtained 20 years of service. Vested sick leave is recorded in proprietary funds as a liability and expense.

e) Post employment healthcare benefits - In addition to the liability for compensated absences, the Department started recording a liability for postemployment healthcare benefits (OPEB) at December 31, 2008, as required by GASB 45 and as described in note 3.

A summary of other non-current liabilities follows:

	<u>Balance</u>			<u>Balance</u>	<u>Due Within</u>
	<u>12/31/13</u>	<u>Additions</u>	<u>Payments</u>	<u>12/31/14</u>	<u>One Year</u>
Compensated absences	\$ 269,218	\$ -	\$ 33,811	\$ 235,407	\$ -
OPEB liability	2,141,745	440,315	133,608	2,448,452	-
Total	<u>\$ 2,410,963</u>	<u>\$ 440,315</u>	<u>\$ 167,419</u>	<u>\$2,683,859</u>	<u>\$ -</u>

WATER DEPARTMENT, CITY OF KINGSTON, NEW YORK
NOTES TO THE FINANCIAL STATEMENTS
DECEMBER 31, 2014 AND 2013

NOTE 3 - POSTEMPLOYMENT HEALTHCARE BENEFITS

From an accrual accounting perspective, the cost of postemployment healthcare benefits, like the cost of pension benefits, generally should be associated with the periods in which the cost occurs, rather than in the future year when it will be paid. In adopting the requirements of GASB statement No. 45 during the year ended December 31, 2008, the Water Department recognizes the cost of postemployment healthcare in the year when the employee services are received, reports the accumulated liability from prior years, and provides information useful in assessing potential demands on the Water Department's future cash flows. Recognitions of the liability accumulated from prior years will be phased in over 30 years, commencing with the 2008 liability.

a) Plan Description - The Water Department provides continuation of medical insurance coverage to employees that retire directly from Water Department employment after retirement age with a minimum of ten years of service. Based on collective bargaining agreements, the retiree and his or her beneficiaries receive this coverage for the life of the retiree and survivor. Healthcare benefits for non-union employees are based on those of union employees. Currently the retiree's share of premium cost ranges from 0 to 65%, depending on the plan coverage and lengths of service. These contracts will be renegotiated at various times in the future.

The number of participants as of January 1, 2014, the effective date of the latest OPEB valuations, follows:

Active employees	26
Retired employees, including spouses of retired employees and deceased retirees	<u>23</u>
	<u>49</u>

b) Funding Policy – The Water Department currently pays for postemployment healthcare benefits on a pay-as-you-go basis through premiums paid to insurance companies and reimbursements to retirees for their Medicare premiums.

c) Annual Other Postemployment Benefit Cost – For the year ended December 31, 2014, the Department's annual OPEB cost (expense) of \$440,314 was equal to the Annual Required Contribution and adjusted for interest and an adjustment to the ARC. The payment of current health insurance premiums and Medicare reimbursement, which totaled \$133,608 for retirees and their survivors, resulted in a net OPEB obligation of \$306,706 for the year ended December 31, 2014.

WATER DEPARTMENT, CITY OF KINGSTON, NEW YORK
NOTES TO THE FINANCIAL STATEMENTS
DECEMBER 31, 2014 AND 2013

NOTE 3 - POSTEMPLOYMENT HEALTHCARE BENEFITS (CONTINUED)

These calculations are based on the January 1, 2014 actuarial valuation.

Amortization of UAAL over 30 Years	\$ 255,814
Normal cost with interest to end of year	<u>184,186</u>
Annual required contribution (ARC)	440,000
Interest on net OPEB obligation	80,315
Adjustment to annual required contribution	<u>(80,000)</u>
Annual OPEB cost	440,315
Contributions made	<u>(133,608)</u>
Increase in net OPEB obligation	306,707
Net OPEB obligation - beginning of year	<u>2,141,745</u>
Net OPEB obligation - end of year	<u><u>\$ 2,448,452</u></u>

Year	Annual OPEB Cost	% of Annual OPEB Cost Contributed	Net OPEB Obligation	Unfunded Actuarial Liability	Funded Ratio	Covered Payroll	UAAL as % of Payroll
2014	\$440,000	30.37%	\$ 2,448,452	6,290,000	0%	\$ 1,390,000	452.52%
2013	455,695	24.07%	2,141,746	6,139,900	0%	1,431,593	428.89%
2012	435,480	22.03%	1,795,724	5,825,600	0%	1,431,821	406.87%
2011	445,734	24.60%	1,456,160	5,870,000	0%	1,371,657	427.95%
2010	423,812	23.57%	1,116,111	5,540,200	0%	1,350,903	410.11%

d) Actuarial Methods and Assumptions – Projections of benefits for financial reporting purposes are based on the substantive plan (the plan as understood by the employer and the plan members) and include the types of benefits provided at the time of each valuation and the historical pattern of sharing benefit costs between the employer and plan members to that point. Since coverage is community rated, retiree claim costs are based on the actual rates without adjustment for age. The unfunded actuarial accrued liability is being amortized over 30 years on a level percentage of projected payroll basis.

In the January 1, 2014 actuarial valuation, the most recent actuarial valuation date, the liabilities were computed using the projected unit credit method. The actuarial assumptions utilized a 3.75% discount rate. Because the plan is unfunded, this rate was selected based on the expected earnings of the City of Kingston's short-term investments such as certificates of deposit. The valuation assumes a current 8.5% healthcare cost trend increase, reduced by decrements to a rate of 4.5% after 9 years.

WATER DEPARTMENT, CITY OF KINGSTON, NEW YORK
NOTES TO THE FINANCIAL STATEMENTS
DECEMBER 31, 2014 AND 2013

NOTE 4 - DEFERRED COMPENSATION PLAN

On October 1, 1997, the New York State Deferred Compensation Board (Board) created a Trust and Custody agreement making Chase Manhattan Bank the Trustee and Custodian of the Plan. Since the Board is no longer the trustee of the New York State Deferred Compensation Plan (Plan), the plan no longer meets the criteria for inclusion in New York State's financial statements. Therefore, municipalities which participate in the Plan are no longer required to record the value of the plan assets.

NOTE 5 - MAJOR PROJECTS AND COMMITMENTS

The Water Department has prepared a four-year capital plan that has been prioritized based on specific criteria, the highest of which is that the project is legally mandated. The total cost of projects anticipated for the next five years is approximately \$17,800,000. These projects will be funded by a combination of budget appropriations, grants and borrowing.

NOTE 6 – RISK MANAGEMENT

The Water Department is exposed to various risks of loss related to torts; theft of, damage to, or destruction of assets; errors and omissions; injuries to employees; employee health and life; and natural disasters. The Department manages these various risks of loss per the following table. Management believes such coverage is sufficient to preclude any significant uninsured losses to the City. Settled claims have not exceeded this insurance coverage.

<u>Type of Loss</u>	<u>Method Managed</u>	<u>Risk Retained</u>
a. Torts; theft of, damage to or destruction of assets; errors and omissions; natural disasters; health and life	Purchased commercial insurance	None
b. Injuries to employees	Purchased Workers' Compensation through NYS Insurance Fund	None

NOTE 7 – SUBSEQUENT EVENTS

The Department has evaluated subsequent events through July 6, 2015, which is the date the financial statements were available to be issued, and determined that any events or transactions occurring during this period that would require recognition or disclosure are properly addressed in these financial statements.

**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***

To the Board of Commissioners
Kingston Water Department
City of Kingston, New York

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 Water Department, City of Kingston, New York, an enterprise fund of the City of Kingston, as of and for the years ended December 31, 2014 and 2013, and have issued our report thereon dated July 6, 2015.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Water Department, City of Kingston's internal control over financial reporting 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 Water Department, City of Kingston, New York's internal control. Accordingly, we do not express an opinion on the effectiveness of the Water Department, City of Kingston, New York'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 a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. 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 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. 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 Water Department, City of Kingston, New York's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Purpose of this Report

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

KIMBALL & O'BRIEN PC

By 

July 6, 2015