



**BERBERICH TRAHAN & CO., P.A.**  
*Certified Public Accountants*

**EL PASO WATER COMPANY, INC.  
CITY OF DERBY, KANSAS**

---

**FINANCIAL STATEMENTS**  
WITH SUPPLEMENTARY INFORMATION  
**YEARS ENDED DECEMBER 31, 2017 AND 2016**

EL PASO WATER COMPANY, INC.  
CITY OF DERBY, KANSAS

FINANCIAL STATEMENTS  
WITH SUPPLEMENTARY INFORMATION

Years Ended December 31, 2017 and 2016

TABLE OF CONTENTS

	<u>Page</u>
Independent Auditor's Report	1 - 2
Financial Statements:	
Balance Sheets	3 - 4
Statements of Income	5
Statements of Retained Earnings	6
Statements of Cash Flows	7
Notes to Financial Statements	8 - 13
Supplementary Information:	
Schedules of Operation and Maintenance Expenses	14



BERBERICH TRAHAN & CO., P.A.  
Certified Public Accountants

3630 SW Burlingame Road Topeka, Kansas 66611 | t: 785.234.3427 | toll-free: 800.530.5526 | f: 785.233.1768 | w: btandcoepa.com

## INDEPENDENT AUDITOR'S REPORT

To the Board of Directors  
El Paso Water Company, Inc.  
Derby, Kansas

### **Report on the Financial Statements**

We have audited the accompanying financial statements of El Paso Water Company, Inc. (the Company) which comprise the balance sheets as of December 31, 2017 and 2016, and the related statements of income, retained earnings and cash flows for the years then ended and the related notes to the financial statements.

### **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. 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 opinion.

An Independently Owned Member, RSM US Alliance

RSM US Alliance member firms are separate and independent businesses and legal entities that are responsible for their own acts and omissions, and each are separate and independent from RSM US LLP. RSM US LLP is the U.S. member firm of RSM International, a global network of independent audit, tax, and consulting firms. Members of RSM US Alliance have access to RSM International resources through RSM US LLP but are not member firms of RSM International.

## **Opinion**

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Company as of December 31, 2017 and 2016, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

## **Other Matter**

Our audits were conducted for the purpose of forming an opinion on the financial statements as a whole. The accompanying supplementary information is presented for purposes of additional analysis and is not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audits of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.

*Berberich Trahan & Co., P.A.*

Topeka, Kansas  
March 28, 2018

THIS PAGE INTENTIONALLY LEFT BLANK

EL PASO WATER COMPANY, INC.  
CITY OF DERBY, KANSAS

BALANCE SHEETS

December 31, 2017 and 2016

	2017	2016
<u>ASSETS</u>		
Utility plant:		
Land and land improvements	\$ 75,059	\$ 75,059
Wells, pumphouses and equipment	992,572	992,572
Mains and storage tanks	4,457,556	4,457,556
Meters	2,280,114	2,347,893
Warehouse building	58,954	58,954
Office furniture and equipment	27,488	25,213
Automotive and other equipment	337,267	354,614
	8,229,010	8,311,861
Less allowance for depreciation	(6,691,650)	(6,609,416)
Total	1,537,360	1,702,445
Current assets:		
Cash	554,077	385,640
Accounts receivable	424,559	387,224
Unbilled receivables	222,810	209,240
Materials and supplies	95,605	85,222
Prepaid insurance	3,362	3,362
	1,300,413	1,070,688
Total current assets	\$ 2,837,773	\$ 2,773,133

See accompanying notes to financial statements.

	<u>2017</u>	<u>2016</u>
<u>LIABILITIES AND STOCKHOLDER'S EQUITY</u>		
Current liabilities:		
Accounts payable	\$ 169,954	\$ 269,393
Stockholder's equity:		
Common stock, no par value, stated value \$ 25 per share: authorized 40,000 shares; issued and outstanding 34,860 shares	871,500	871,500
Additional paid-in capital	303,053	303,053
Retained earnings	2,093,257	1,929,178
	<u>3,267,810</u>	<u>3,103,731</u>
Treasury stock at cost - 3,545 shares	<u>(599,991)</u>	<u>(599,991)</u>
Total stockholder's equity	2,667,819	2,503,740
	<u>\$ 2,837,773</u>	<u>\$ 2,773,133</u>

EL PASO WATER COMPANY, INC.  
CITY OF DERBY, KANSAS

STATEMENTS OF INCOME

Years Ended December 31, 2017 and 2016

	<u>2017</u>	<u>2016</u>
Operating revenues	<u>\$ 5,309,525</u>	<u>\$ 4,838,987</u>
Operating expenses:		
Operation and maintenance	4,359,814	3,676,235
Depreciation	<u>167,360</u>	<u>187,854</u>
Total operating expenses	<u>4,527,174</u>	<u>3,864,089</u>
Net income	<u><u>\$ 782,351</u></u>	<u><u>\$ 974,898</u></u>

See accompanying notes to financial statements.

EL PASO WATER COMPANY, INC.  
CITY OF DERBY, KANSAS

STATEMENTS OF RETAINED EARNINGS

Years Ended December 31, 2017 and 2016

	<u>2017</u>	<u>2016</u>
Balance, beginning of year	\$ 1,929,178	\$ 2,215,130
Net income	782,351	974,898
Cash dividends to the City of Derby, Kansas	<u>(618,272)</u>	<u>(1,260,850)</u>
Balance, end of year	<u>\$ 2,093,257</u>	<u>\$ 1,929,178</u>

See accompanying notes to financial statements.

EL PASO WATER COMPANY, INC.  
CITY OF DERBY, KANSAS

STATEMENTS OF CASH FLOWS

Years Ended December 31, 2017 and 2016

	2017	2016
Cash flows from operating activities:		
Net income	\$ 782,351	\$ 974,898
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	167,360	187,854
Changes in assets and liabilities:		
Accounts and unbilled receivables	(50,905)	(6,388)
Materials and supplies	(10,383)	32,517
Accounts payable	(99,439)	99,829
	788,984	1,288,710
Cash flows from investing activities:		
Purchases of equipment	(2,275)	(7,945)
Cash flows from financing activities:		
Dividends paid	(618,272)	(1,260,850)
Net increase in cash	168,437	19,915
Cash, beginning of year	385,640	365,725
Cash, end of year	\$ 554,077	\$ 385,640

See accompanying notes to financial statements.

EL PASO WATER COMPANY, INC.  
CITY OF DERBY, KANSAS

NOTES TO FINANCIAL STATEMENTS

December 31, 2017 and 2016

1 - Nature of Organization and Summary of Significant Accounting Policies

Organization and Operations

El Paso Water Company, Inc. (the Company) is a water utility company serving customers located in Derby, Kansas. Water sales comprise the majority of the Company's operating revenues, which could be adversely affected by the amount of local rainfall, conservation measures by customers or an interruption of service from the City of Wichita, Kansas water supply. On January 27, 1999, all stock of the company not redeemed as treasury stock was acquired by the City of Derby, Kansas.

Deposits

The Company maintains deposits in banks. These deposits are insured by the Federal Deposit Insurance Corporation (FDIC) up to \$ 250,000 per bank. The Company's deposits may have exceeded the FDIC insurance limits during the year ended December 31, 2017.

Utility Plant

Utility plant assets are reflected at cost as of the time of acquisition. The Company generally capitalizes all expenditures for utility plant assets in excess of \$ 2,500.

Maintenance and repair costs are charged to income as incurred, and significant renewals and betterments are capitalized. When assets are retired or disposed of, the related costs and accumulated depreciation are removed from the respective accounts and any gain or loss is credited or charged to income.

EL PASO WATER COMPANY, INC.  
CITY OF DERBY, KANSAS

NOTES TO FINANCIAL STATEMENTS  
(Continued)

1 - Nature of Organization and Summary of Significant Accounting Policies (Continued)

Utility Plant (Continued)

Depreciation is provided for in amounts sufficient to charge the cost of depreciable assets to operations over their estimated service lives. For substantially all capital assets acquired prior to 1987, an accelerated method of depreciation (declining-balance) is used for financial reporting purposes, except for assets acquired prior to January 1, 1976, which are depreciated using the straight-line method for financial reporting purposes. All capital assets acquired subsequent to 1987 are depreciated using the straight-line method. Estimated useful lives are as follows:

	<u>Years</u>
Land improvements	20
Wells, pumphouses and equipment	40
Mains and storage tanks	50
Meters	5 - 15
Warehouse building	40
Office furniture and equipment	5 - 7
Other	3 - 10

In previous years, purchased water meters were classified as capital assets and depreciated over their estimated useful lives. Beginning on January 1, 2013, the Company determined that new meter costs going forward will be recognized as expenses in the period incurred as the individual meter costs are below the capitalization threshold of the Company.

Accounts Receivable and Revenue Recognition

Revenue is recognized as service is provided to customers. All customers are billed monthly.

Accounts receivable consist of both residential and commercial water sales. Unbilled receivables are recorded for services provided for which customers have not been billed at December 31, 2017 and 2016. The Company utilizes the direct write-off method of accounting for bad debts. Accounts greater than 90 days past due are considered uncollectible and are written off. Management has determined that an allowance for doubtful accounts is not necessary at December 31, 2017 and 2016.

EL PASO WATER COMPANY, INC.  
CITY OF DERBY, KANSAS

NOTES TO FINANCIAL STATEMENTS  
(Continued)

1 - Nature of Organization and Summary of Significant Accounting Policies (Continued)

Materials and Supplies

Inventories of materials and supplies are stated at the lower of cost or market; cost is determined using the last-in, first-out method.

Income Tax Matters

The Company has received a Private Letter Ruling from the Internal Revenue Service concluding that the Company is a public utility for purposes of Internal Revenue Code 115(1) and, accordingly, its income from the operation of the public utility is excludable from taxation.

The Company's policy is to evaluate uncertain tax positions annually. Management evaluated the Company's tax positions and concluded that the Company had taken no uncertain tax positions that require adjustment to the financial statements.

The Company files income tax returns in the U.S. federal jurisdiction and Kansas state jurisdiction. With few exceptions, the Company is no longer subject to U.S. federal or state and local income tax examinations by tax authorities for years before 2014.

Use of Estimates

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

EL PASO WATER COMPANY, INC.  
CITY OF DERBY, KANSAS

NOTES TO FINANCIAL STATEMENTS  
(Continued)

1 - Nature of Organization and Summary of Significant Accounting Policies (Continued)

Recent Accounting Pronouncements

In February 2016, FASB issued ASU 2016-02, Leases (Topic 842). The guidance in this ASU supersedes the leasing guidance in Topic 840, Leases. Under the new guidance, lessees are required to recognize lease assets and lease liabilities on the balance sheet for all leases with terms longer than 12 months. Leases will be classified as either finance or operating with classification affecting the pattern of expense recognition in the income statement. The new standard is effective for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years. Management is currently evaluating the effect that the standard will have on the financial statements.

2 - Related Party Transactions

The Board of Directors of El Paso Water Company, Inc. is comprised of the Mayor and City Council members of the City of Derby, Kansas. The City of Derby, Kansas bills the water charges for the Company.

All employees of the Company are employees of the City of Derby, Kansas. The Company makes a monthly reimbursement to the City of Derby, Kansas for contract labor. The total contract labor reimbursement from the Company to the City of Derby, Kansas for the years ended December 31, 2017 and 2016 was \$ 651,778 and \$ 615,569, respectively.

The City of Derby, Kansas receives dividends from the Company. Cash dividends paid to the City of Derby, Kansas from the Company were \$ 618,272 and \$ 1,260,850 for the years ended December 31, 2017 and 2016, respectively.

The Company also leases office space from the City of Derby, Kansas. Total rental expense included in operations was \$ 14,300 for each of the years 2017 and 2016.

EL PASO WATER COMPANY, INC.  
CITY OF DERBY, KANSAS

NOTES TO FINANCIAL STATEMENTS  
(Continued)

3 - Water Rights

As of December 31, 1996, the Company hired a consultant to prepare a business valuation of the Company. Included in the valuation were water rights with a value of \$ 851,600. This value was based upon transactions in water rights in the area. The Company does not have a cost basis in the water rights, and therefore, in accordance with accounting principles generally accepted in the United States of America, they are not reflected on the balance sheets.

4 - Commitments

In April 2004, the City of Derby, Kansas issued \$ 9,455,000, 1.10% - 5.00% General Obligation Water System Refunding Bonds, Series 2004-A, with varying maturities up to December 1, 2022. Principal payments for 2016 through 2022 were refunded in September 2013, when the City of Derby, Kansas issued \$ 3,375,000, 2.50% - 3.00% General Obligation Water System Refunding Bonds, Series 2013-B, with varying maturities up to December 1, 2022. All of the Series 2013-B issuance pertained to the Company. The remaining principal payment for 2015 was refunded in June 2014, when the City of Derby, Kansas issued \$ 4,510,000, 2.00% - 4.00% General Obligation Refunding and Improvement Bonds, Series 2014-A, with varying maturities up to December 1, 2034. Of the \$ 4,510,000 Series 2014-A issuance, \$ 605,000 pertained to the Company, and the balance was paid off as of December 31, 2015.

In September 2012, the City of Derby, Kansas issued \$ 3,165,000, 1.00% - 2.125% General Obligation Bonds, Series 2012-B, with varying maturities up to December 1, 2026. Of the \$ 3,165,000 Series 2012-B issuance, \$ 708,120 pertained to the Company.

The Company paid dividends to the City of Derby, Kansas of \$ 618,273 and \$ 1,260,850 for the years 2017 and 2016, respectively, related to principal and interest payments on the Series 2012-B and Series 2013-B bond issues. Future dividend payments to the City of Derby, Kansas are anticipated in order to retire the Series 2012-B and Series 2013-B bonds.

5 - Water Purchased from City of Wichita

All water sold is purchased from the City of Wichita, Kansas under a twenty-year contract. The contract agreement originally contained a 100% "take or pay" provision. In March 2014, the City of Wichita, Kansas modified the "take or pay" provision to reduce the threshold to 50% for one year. The City of Wichita, Kansas has further extended the modification through November 30, 2022. No amounts were paid under the "take or pay" provision for 2017 or 2016.

EL PASO WATER COMPANY, INC.  
CITY OF DERBY, KANSAS

NOTES TO FINANCIAL STATEMENTS  
(Continued)

6 - Subsequent Events

The Company has evaluated subsequent events through the date of the independent auditor's report, which is the date the financial statements are available to be issued.

SUPPLEMENTARY INFORMATION

EL PASO WATER COMPANY, INC.  
CITY OF DERBY, KANSAS

SCHEDULES OF OPERATION AND MAINTENANCE EXPENSES

Years Ended December 31, 2017 and 2016

	<u>2017</u>	<u>2016</u>
Contract labor	\$ 651,778	\$ 615,569
Repairs and maintenance	333,462	291,614
Wichita water purchases	3,090,093	2,484,783
Electric power	21,961	31,525
Other utilities	4,782	2,559
Office supplies and postage	13,286	16,467
Rentals/operating leases	14,300	14,300
Water treating supplies	3,912	7,392
Insurance	21,028	12,852
Professional fees	100,720	101,806
Dues and subscriptions	2,973	1,997
Other taxes	1,847	3,711
Miscellaneous	99,672	91,660
Total	<u>\$ 4,359,814</u>	<u>\$ 3,676,235</u>

See accompanying independent auditor's report.