

**KENTUCKY LEAGUE OF CITIES, INC. AND  
SUBSIDIARIES**

**Consolidated Financial Statements**

*Years Ended June 30, 2016 and 2015  
with Report of Independent Auditors*

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## **Report of Independent Auditors**

Board of Directors  
Kentucky League of Cities, Inc. and Subsidiaries  
Lexington, Kentucky

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

We have audited the accompanying consolidated financial statements of Kentucky League of Cities, Inc. and Subsidiaries (collectively, KLC) which comprise the consolidated statements of net position as of June 30, 2016 and 2015, and the related consolidated statements of revenues, expenses and changes in net position 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 consolidated financial statements in accordance with the 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 consolidated 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 consolidated 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 consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated 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 consolidated 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 consolidated financial statements.

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

Board of Directors  
Kentucky League of Cities, Inc. and Subsidiaries  
Report of Independent Auditors, continued

## **Opinion**

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Kentucky League of Cities, Inc. and Subsidiaries as of June 30, 2016 and 2015, and the changes in its financial position and its cash flows thereof for the years then ended in accordance 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 on pages 4 - 6 and the Schedule of the Proportionate Share of the Net Pension Liability and Schedule of Contributions on pages 38 - 39 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 the 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 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 audits 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 Information*

Our audits were conducted for the purpose of forming opinions on the consolidated financial statements that collectively comprise KLC's basic financial statements. The consolidating schedules on pages 32 - 37 are presented for purposes of additional analysis and are not a required part of the basic 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 basic financial statements. The supplementary information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the supplementary information is fairly stated in all material respects in relation to the financial statements taken as a whole.

Board of Directors  
Kentucky League of Cities, Inc. and Subsidiaries  
Report of Independent Auditors, continued

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

In accordance with *Government Auditing Standards*, we have also issued our report dated September 20, 2016 on our consideration of KLC'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 KLC's internal control over financial reporting and compliance.

*Dean Dotson Allen Ford, PLLC*

September 20, 2016  
Lexington, Kentucky

# KENTUCKY LEAGUE OF CITIES, INC. AND SUBSIDIARIES

## Management's Discussion and Analysis (Unaudited)

Our discussion and analysis of the Kentucky League of Cities, Inc. and Subsidiaries (KLC or the Organization) provides an overview of the Organization's financial activity for the fiscal year ended June 30, 2016. It should be read in conjunction with the consolidated financial statements, which begin on page 7.

### Using this Annual Report

This report consists of a series of financial statements. The consolidated statements of net position on page 7 provide information about the Organization as a whole.

### Statements of Net Position

Table 1 shows all of the assets and liabilities of the Organization and is presented on the accrual basis. The total net position increased by \$293,557 in the current year. Operating revenues increased with favorable results in the bond financing and training programs. The recording of KLC's long-term obligation for pension and health benefits under Governmental Accounting Standards Board (GASB) Statement No. 68 (See Note 2 for further details) produced an overall increase in operating expenses.

**Table 1**  
**Net Position**

	<u>2016</u>	<u>2015</u>
Current assets	\$ 11,694,724	\$ 11,480,004
Capital and other assets	<u>7,639,366</u>	<u>7,999,913</u>
Total assets	19,334,090	19,479,917
Deferred outflows of resources	<u>1,606,815</u>	<u>587,675</u>
Combined assets and deferred outflows of resources	20,940,905	20,067,592
Current liabilities	2,315,668	2,680,618
Long-term liabilities	3,305,356	3,630,654
Net pension liability	8,292,148	6,466,000
Deferred inflows of resources	<u>165,856</u>	<u>722,000</u>
Combined liabilities and deferred inflows of resources	<u>14,079,028</u>	<u>13,499,272</u>
Total net position	\$ <u>6,861,877</u>	\$ <u>6,568,320</u>

# KENTUCKY LEAGUE OF CITIES, INC. AND SUBSIDIARIES

## Management's Discussion and Analysis (*Unaudited*), continued

### Statements of Revenues, Expenses and Changes in Net Position

Table 2 shows all the revenues and expenses of the Organization and is also presented on the accrual basis. The administrative fees received for providing staffing and overhead to the KLC related entities (KLCWC, KBC, KBDC, KLCIS, KLCUCRT, KSBIT) increased approximately \$100,000, mostly from issuance fees received from favorable results in the bond pool programs. Total operating expenses increased approximately \$714,000 from the prior year primarily due to increases in salaries and benefits, including the adoption of KLC's long-term obligation for pension and health benefits under GASB Statement No. 68 (See Note 2 for further details).

**Table 2**  
**Revenues, Expenses and Changes in Net Position**

	<u>2016</u>	<u>2015</u>
Operating revenue:		
Administrative fees	\$ 7,242,221	\$ 7,142,682
Commissions	2,474,035	2,688,813
Member dues	523,203	492,224
Member meeting and training income	426,427	358,100
Premium finance revenue	177,680	176,533
Other	350,440	309,416
Publication income	<u>4,768</u>	<u>23,822</u>
Total operating revenue	11,198,774	11,191,590
Operating expenses:		
Administrative and general	(4,861,007)	(3,828,956)
Legislative services	(1,502,766)	(1,463,728)
Member financial services	(249,257)	(262,321)
Member insurance services	(5,048,408)	(5,369,742)
Member meeting and training services	<u>(223,981)</u>	<u>(246,410)</u>
Total operating expenses	(11,885,419)	(11,171,157)
Nonoperating revenue, net	<u>980,202</u>	<u>990,703</u>
Change in net position	\$ <u>293,557</u>	\$ <u>1,011,136</u>

## KENTUCKY LEAGUE OF CITIES, INC. AND SUBSIDIARIES

### Management's Discussion and Analysis (*Unaudited*), continued

#### Description of Current and Expected Conditions

The management of KLC is not aware of any other significant changes in conditions that would have a significant effect on the financial position or results of operations of the Organization in the near future.

#### Contacting KLC's Financial Management

This financial report is designed to provide a general overview of KLC and its subsidiaries' finances and to show KLC's accountability to its members. If you have questions about this report or need additional information, contact KLC's office at 100 E. Vine St., Lexington, KY 40507.



# KENTUCKY LEAGUE OF CITIES, INC. AND SUBSIDIARIES

## Consolidated Statements of Net Position

June 30, 2016 and 2015

	<u>2016</u>	<u>2015</u>
<b>Assets</b>		
Current assets:		
Cash and cash equivalents	\$ 4,640,538	\$ 3,933,758
Investments	5,725,241	5,705,761
Accounts receivable	484,231	198,576
Premiums receivable	21,342	51,650
Prepaid expenses and other assets	511,725	498,702
Due from related parties	<u>311,647</u>	<u>1,091,557</u>
Total current assets	11,694,724	11,480,004
Capital assets, net	<u>7,639,366</u>	<u>7,999,913</u>
Total assets	19,334,090	19,479,917
<b>Deferred Outflows of Resources</b>		
Deferred amount related to pension plan	<u>1,606,815</u>	<u>587,675</u>
Combined assets and deferred outflows of resources	20,940,905	20,067,592
<b>Liabilities</b>		
Current liabilities:		
Accounts payable	204,558	273,368
Accrued liabilities	1,016,549	961,503
Unearned revenue	629,281	622,784
Due to related parties	115,771	483,451
Current maturities of note payable	53,990	51,872
Current maturities of bond payable	<u>295,519</u>	<u>287,640</u>
Total current liabilities	2,315,668	2,680,618
Note payable, net of current maturities	759,992	813,982
Bond payable, net of current maturities	2,545,364	2,816,672
Net pension liability	<u>8,292,148</u>	<u>6,466,000</u>
Total liabilities	13,913,172	12,777,272
<b>Deferred Inflows of Resources</b>		
Deferred amount related to pension plan	<u>165,856</u>	<u>722,000</u>
Combined liabilities and deferred inflows of resources	<u>14,079,028</u>	<u>13,499,272</u>
<b>Net Position</b>		
Invested in fixed assets, net of related debt	3,984,501	4,029,747
Unrestricted	<u>2,877,376</u>	<u>2,538,573</u>
Total net position	<u>\$ 6,861,877</u>	<u>\$ 6,568,320</u>

See accompanying notes.

# KENTUCKY LEAGUE OF CITIES, INC. AND SUBSIDIARIES

## Consolidated Statements of Revenues, Expenses and Changes in Net Position

Years ended June 30, 2016 and 2015

	<u>2016</u>	<u>2015</u>
Operating revenue:		
Administrative fee - KLCIS	\$ 4,661,498	\$ 4,591,085
Administrative fee - KLCWCT	1,707,944	1,721,364
Administrative fee - Bond Pools	752,435	579,578
Administrative fee - KLCUCRT	120,344	119,434
Administrative fee - KSBIT	-	131,221
Commissions	2,474,035	2,688,813
Member dues	523,203	492,224
Member meeting and training income	426,427	358,100
Premium finance revenue	177,680	176,533
Other	350,440	309,416
Publication income	<u>4,768</u>	<u>23,822</u>
Total operating revenue	11,198,774	11,191,590
Operating expenses	<u>11,885,419</u>	<u>11,171,157</u>
Operating (loss) income	(686,645)	20,433
Nonoperating revenue (expenses):		
Interest and investment income	81,158	54,185
Interest expense	(96,585)	(101,101)
(Loss) gain on disposal of capital assets	(925)	48,505
Net rental income	<u>996,554</u>	<u>989,114</u>
Total nonoperating revenue	<u>980,202</u>	<u>990,703</u>
Change in net position before cumulative effect of a change in accounting principle	293,557	1,011,136
Cumulative effect on prior years (to June 30, 2014) resulting from the retroactive change in accounting for pensions (Note 2)	<u>-</u>	<u>(6,670,000)</u>
Change in net position	293,557	(5,658,864)
Net position, beginning of year	<u>6,568,320</u>	<u>12,227,184</u>
Net position, end of year	\$ <u>6,861,877</u>	\$ <u>6,568,320</u>

See accompanying notes.

# KENTUCKY LEAGUE OF CITIES, INC. AND SUBSIDIARIES

## Consolidated Statements of Cash Flows

Years ended June 30, 2016 and 2015

	<u>2016</u>	<u>2015</u>
<b>Cash flows from operating activities:</b>		
Cash received from members and affiliates	\$ 10,953,242	\$ 11,267,017
Cash paid to suppliers and employees	<u>(10,858,255)</u>	<u>(10,391,419)</u>
Net cash provided by operating activities	94,987	875,598
<b>Cash flows from noncapital financing activities:</b>		
Payments from (to) related parties	<u>412,230</u>	<u>(54,430)</u>
Net cash provided by (used in) noncapital financing activities	412,230	(54,430)
<b>Cash flows from capital and related financing activities:</b>		
Capital expenditures	(446,783)	(411,318)
Proceeds from sale of capital assets	-	48,505
Principal payments on bond payable	(263,429)	(279,442)
Principal payments on note payable	(51,872)	(50,138)
Interest paid	<u>(96,585)</u>	<u>(101,101)</u>
Net cash used in capital and related financing activities	(858,669)	(793,494)
<b>Cash flows from investing activities:</b>		
Proceeds from sale and maturity of investments	2,337,658	2,241,207
Interest and income on investments	33,589	133,517
Purchase of investments	(2,309,569)	(3,771,580)
Proceeds from rental activities	<u>996,554</u>	<u>989,114</u>
Net cash provided by (used in) investing activities	<u>1,058,232</u>	<u>(407,742)</u>
Net increase (decrease) in cash and cash equivalents	706,780	(380,068)
Cash and cash equivalents, beginning of year	<u>3,933,758</u>	<u>4,313,826</u>
Cash and cash equivalents, end of year	\$ <u>4,640,538</u>	\$ <u>3,933,758</u>

# KENTUCKY LEAGUE OF CITIES, INC. AND SUBSIDIARIES

## Consolidated Statements of Cash Flows, continued

Years ended June 30, 2016 and 2015

	<u>2016</u>	<u>2015</u>
<b>Reconciliation of operating (loss) income to net cash provided by operating activities:</b>		
Operating (loss) income	\$ (686,645)	\$ 20,433
Adjustments:		
Depreciation and amortization	812,201	848,978
Pension liability, net of deferred inflows and outflows of resources	250,864	(69,675)
(Recovery of) provision for bad debts	(3,318)	5,163
Increase (decrease) in cash due to changes in:		
Accounts receivable	(282,337)	486,156
Premiums receivable	30,308	9,636
Prepaid expenses and other assets	(18,819)	(109,249)
Accounts payable	(68,810)	(24,361)
Accrued liabilities	55,046	128,882
Unearned revenue	<u>6,497</u>	<u>(420,365)</u>
Net cash provided by operating activities	\$ <u>94,987</u>	\$ <u>875,598</u>

See accompanying notes.

# KENTUCKY LEAGUE OF CITIES, INC. AND SUBSIDIARIES

## Notes to the Consolidated Financial Statements

### 1. Nature of Organization and Operations

The Kentucky League of Cities, Inc. and Subsidiaries (KLC) is an incorporated association of cities whose purpose is to provide legislative, financial, insurance, and legal assistance to its members. This is primarily accomplished through lobbying, publications and training seminars. KLC publishes a monthly newsletter and a weekly bulletin on the status of legislation. KLC's revenues are substantially comprised of fees earned for administration of entities related to KLC and member dues. Member dues are based on the members' respective populations.

Kentucky League of Cities Insurance Agency (KLCIA) was incorporated on December 27, 1995 by its sole stockholder, KLC. KLCIA was organized to transact business as an insurance agency. KLCIA sells health, life, and bonding insurance to municipalities in the Commonwealth of Kentucky and also markets insurance offered by other KLC related entities.

Kentucky League of Cities Premium Finance Company (KLCRFC) was incorporated on March 26, 2003 by its sole stockholder, KLC. KLCRFC was organized to finance insurance premiums for member cities. See also Note 7.

The consolidated financial statements of KLC include the accounts of KLC, KLCIA, and KLCRFC. All significant intercompany balances and transactions have been eliminated upon consolidation.

The following entities are KLC related entities:

- Kentucky Bond Corporation (KBC)
- Kentucky Bond Development Corporation (KBDC)
- Kentucky League of Cities Funding Trust (KLCFT)
- Kentucky League of Cities Investment Pool (KLCIP)
- Kentucky League of Cities Insurance Services (KLCIS)
- Kentucky League of Cities Unemployment Compensation Reimbursement Trust (KLCUCRT)
- Kentucky League of Cities Workers Compensation Trust (KLCWCT)
- Kentucky Local Government Health Trust (KLGHT)

### 2. Summary of Significant Accounting Policies

The consolidated financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America (GAAP) which require management to make estimates and assumptions that affect the reported amounts and disclosures in the financial statements. Actual results could differ from those estimates. The following is a summary of the significant accounting policies consistently followed by KLC in the preparation of its consolidated financial statements.

## KENTUCKY LEAGUE OF CITIES, INC. AND SUBSIDIARIES

### Notes to the Consolidated Financial Statements, continued

#### 2. Summary of Significant Accounting Policies, continued

##### Basis of Presentation

KLC presents its financial statements in conformity with GAAP as applied to government units. Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. As a proprietary activity, KLC has adopted GASB Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*. Therefore, KLC follows GASB pronouncements and all Financial Accounting Standards Board and predecessor boards' pronouncements except those that conflict with or contradict GASB pronouncements.

Operating revenues are those revenues that are generated from the primary operations. All other revenues are reported as non-operating revenues. Operating expenses are those expenses that are essential to the primary operations. All other expenses are reported as non-operating expenses.

##### Change in Accounting Principle

Effective July 1, 2014, KLC was required to adopt GASB Statement No. 68, *Accounting and Financial Reporting for Pensions* (Statement 68). Statement 68 replaced the requirements of GASB Statement No. 27, *Accounting for Pensions by State and Local Governmental Employers* and GASB Statement No. 50, *Pension Disclosures*, as they relate to governments that provide pensions through pension plans administered as trusts or similar arrangements that meet certain criteria. Statement 68 requires governments providing defined benefit pensions to recognize their long-term obligation for pension benefits as a liability to more comprehensively and comparably measure the annual costs of pension benefits. Cost-sharing governmental employers, such as KLC, are required to report a net pension liability, pension expense and pension-related assets and liabilities based on their proportionate share of the collective amounts for all governments in the plan.

KLC has elected to utilize the cumulative effect of a change in accounting principle option permitted by Statement 68 as KLC has determined that restatement of all prior periods presented is not practical. The adjustment resulted in a \$6,670,000 reduction in beginning net position for 2015.

##### Cash and Cash Equivalents

Cash and cash equivalents include certain investments in highly liquid debt instruments with original maturities of three months or less.

KLC has a concentration of credit risk in that it periodically maintains bank accounts which, at times, may exceed the coverage provided by the Federal Deposit Insurance Corporation (FDIC). Cash equivalents include investments in a money market fund that are not FDIC insured.

## KENTUCKY LEAGUE OF CITIES, INC. AND SUBSIDIARIES

### Notes to the Consolidated Financial Statements, continued

#### 2. Summary of Significant Accounting Policies, continued

##### Investments

Investment securities consist of U.S. government agency equity securities and mutual funds consisting of governmental securities and debt and equity securities. Investments are stated at fair value based, generally, on quoted market prices.

Realized gains and losses on investments are calculated as the difference between the proceeds of the sale and the original cost of the investments sold. This calculation is independent of the calculation of the net change in the fair value of investments. Realized gains and losses on investments that were held in prior years and sold in the current year were included as a net change in the fair value of investments as reported in the prior year.

##### Capital Assets

Capital assets consisting of land, buildings, parking lot and improvements, furniture, equipment, and building and land improvements, are stated at cost. Depreciation is calculated on the straight-line method over the estimated useful lives of the assets.

<u>Asset Type</u>	<u>Useful Life</u>
Buildings	39 years
Furniture and fixtures	2-15 years
Improvements	15-20 years

When properties are retired or otherwise disposed of, the cost and related accumulated depreciation are removed from the account with any resulting gain or loss reflected in income.

##### Income Taxes

The Internal Revenue Service (IRS) has ruled that the income of KLC is excludable from gross income and, therefore, exempt from taxation pursuant to Internal Revenue Code (IRC) Section 115, which pertains to instrumentalities of state and local governments.

##### Unearned Revenue

Unearned revenue consists of KLC members' dues and premiums financed through KLCPCF. Members' annual dues are billed in advance throughout the year. These dues are deferred and subsequently recognized on a pro-rata basis. Total unearned revenue related to members' dues was \$263,414 and \$256,500 as of June 30, 2016 and 2015, respectively. KLCPCF finances insurance premiums for members of KLCIS throughout the year. Those premium amounts that are received in advance of the policy period are classified as advanced (unearned) revenue until earned. Total unearned premiums as of June 30, 2016 and 2015 were \$150,300 and \$128,581, respectively. Unearned revenue also includes convention, administrative fees, advertising fees and rent received in advance. Total other unearned revenue for KLC as of June 30, 2016 and 2015 was \$185,682 and \$198,847, respectively.

## KENTUCKY LEAGUE OF CITIES, INC. AND SUBSIDIARIES

### Notes to the Consolidated Financial Statements, continued

#### 2. Summary of Significant Accounting Policies, continued

##### Unearned Revenue, continued

Additionally, KLCIA has received commissions from certain insurance carriers for advance premiums sold to member cities. These commissions are earned over the life of the premium policy period. Total unearned revenue for KLCIA as of June 30, 2016 and 2015 was \$29,885 and \$38,856, respectively.

##### Pensions

KLC participates in the County Employees Retirement System (CERS) administered by the Board of Trustees of the Kentucky Retirement Systems. This is a cost sharing, multiple employer defined benefit pension plan, which covers all eligible full-time employees and provides for retirement, disability and death benefits to plan members.

In accordance with Statement 68, cost-sharing governmental employers, such as KLC, are required to report a net pension liability, pension expense and pension-related assets and liabilities based on their proportionate share of the collective amounts for all governments in the plan. For purposes of measuring the net pension liability, deferred outflows of resources and deferred inflows of resources related to pensions, and pension expense, information about the fiduciary net position of CERS and additions to or deductions from CERS' fiduciary net position have been determined on the same basis as they are reported by CERS. For this purpose, benefit payments (including refunds of employee contributions) are recognized when due and payable in accordance with the benefit terms. Investments are reported at fair value.

All governments participating in the defined benefit pension plan also are required to disclose various information in the footnotes to the consolidated financial statements – see Note 6.

##### Restatement

During fiscal 2016, KLC became aware that its fiscal 2015 pension expense was understated due to incorrectly classifying contributions to the CERS health benefits funds as deferred outflows. These contributions should have been reported as pension expense. As such, for fiscal 2015 reporting, KLC added \$226,774 to pension expense and reduced deferred outflows by \$226,774. The net impact of this restatement was a decrease to 2015 net position and change in net position by \$226,774.



## KENTUCKY LEAGUE OF CITIES, INC. AND SUBSIDIARIES

### Notes to the Consolidated Financial Statements, continued

#### 2. Summary of Significant Accounting Policies, continued

##### Recent Accounting Pronouncements

In June 2015, the GASB issued Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*. The primary objective of this Statement is to improve accounting and financial reporting by state and local governments for postemployment benefits other than pensions (other postemployment benefits or OPEB). It also improves information provided by state and local governmental employers about financial support for OPEB that is provided by other entities. This Statement requires reporting of the entity's OPEB liability on the face of the financial statements and more extensive note disclosures and required supplementary information about OPEB liabilities. The provisions of this Statement are effective for reporting periods beginning after June 15, 2017. KLC is currently evaluating the effects of this statement on its financial statements.

##### Subsequent Events

KLC's management evaluated the period from July 1, 2015 to September 20, 2016 (the date the consolidated financial statements were ready to be issued) for subsequent events. Except as disclosed in Note 11, there were no events occurring during the evaluation period that require recognition or disclosure in the consolidated financial statements.

#### 3. Deposits and Investments

Deposits and investments held by KLC as of June 30 are as follows:

	<u>2016</u>	<u>2015</u>
Deposits and investments classified as cash and cash equivalents:		
Cash and cash equivalents	\$ 1,992,788	\$ 3,743,792
Money market mutual funds	<u>2,647,750</u>	<u>189,966</u>
Total deposits	4,640,538	3,933,758
Investments classified as investment securities:		
U.S. government agencies and municipal obligations	1,749,965	1,483,663
Corporate and foreign bonds	735,387	716,680
Bond mutual funds	351,955	398,302
Equity mutual funds	97,832	219,787
Equity securities	<u>2,790,102</u>	<u>2,887,329</u>
Total investments	<u>5,725,241</u>	<u>5,705,761</u>
Total deposits and investments	\$ <u>10,365,779</u>	\$ <u>9,639,519</u>

# KENTUCKY LEAGUE OF CITIES, INC. AND SUBSIDIARIES

## Notes to the Consolidated Financial Statements, continued

### 3. Deposits and Investments, continued

Interest and investment income is comprised of the following for the years ended June 30:

	<u>2016</u>	<u>2015</u>
Interest and dividend income	\$ 75,755	\$ 66,498
Realized (losses) gains on sales of securities	(42,167)	67,020
Unrealized gains (losses) on securities	<u>47,570</u>	<u>(79,333)</u>
	<u>\$ 81,158</u>	<u>\$ 54,185</u>

#### Fair Value

Investments, including derivative instruments that are not hedging derivatives, are measured at fair value on a recurring basis. Fair value measurements are categorized based on the valuation inputs used to measure an asset's fair value: Level 1 inputs are quotes prices in active markets for identical assets; Level 2 inputs are significant other observable inputs; Level 3 inputs are significant unobservable inputs.

All of KLC's investments are actively traded and categorized as Level 1 investments in the fair value hierarchy.

#### Interest Rate Risk

Interest rate risk is the risk that interest rates will change and cause a decrease in the value of an entity's investments. KLC does not have a formal investment policy that limits investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates.

#### Credit Risk

Credit risk is the risk that issuers of securities owned by an entity will default or that other parties that owe the entity money will not pay. KLC minimizes these risks by adhering to a conservative investment strategy, by utilizing sound financial advice of reputable investment advisors, by maintaining credit and collection policies, and by providing an allowance for any amounts deemed uncollectible.

As of June 30, 2016, KLC was invested in several U.S. government agency bonds, state and local municipal bonds, corporate and foreign bonds which have the following ratings as of June 30, 2016:

AAA	\$ 114,873
AA	453,651
A	405,827
Below A	50,865
Not rated or other	<u>1,460,136</u>
	<u>\$ 2,485,352</u>

# KENTUCKY LEAGUE OF CITIES, INC. AND SUBSIDIARIES

## Notes to the Consolidated Financial Statements, continued

### 3. Deposits and Investments, continued

#### Concentration of Credit Risk

KLC's investment policy limits investments in any single holding to no more than 5% of the market value of the account, except for bonds issued by the Kentucky Bond Corporation, up to an aggregate limit of \$2,000,000, as well as setting guidelines for the type and quality of investments. At June 30, 2016 and 2015, KLC had one investment that exceeded the 5% limit, which was within the policy guidelines as it was a series of bonds issued by the Kentucky Bond Corporation.

As of June 30, 2016, KLC had the following investment maturities:

	Investment Maturities (in years)			
	Less than 1	1-5	6-10	More than 10
Corporate and foreign bonds	\$ -	\$ 360,189	\$ 288,330	\$ 86,868
U.S. government agencies and municipal obligations	<u>45,040</u>	<u>56,459</u>	<u>220,374</u>	<u>1,428,092</u>
Total maturities	<u>\$ 45,040</u>	<u>\$ 416,648</u>	<u>\$ 508,704</u>	<u>\$ 1,514,960</u>

### 4. Capital Assets

Capital asset activity for the year ended June 30, 2016 is as follows:

	Beginning Balance	Additions	Retirements	Ending Balance
Capital assets at cost:				
Land	\$ 674,175	\$ -	\$ -	\$ 674,175
Buildings	6,431,825	22,064	-	6,453,889
Parking lot and improvements	1,239,306	-	-	1,239,306
Furniture and fixtures	2,792,874	130,959	(1,040)	2,922,793
Improvements	5,490,683	47,645	-	5,538,328
Construction in progress	<u>-</u>	<u>246,115</u>	<u>-</u>	<u>246,115</u>
Total capital assets at cost	16,628,863	446,783	(1,040)	17,074,606
Less: accumulated depreciation	<u>(8,628,950)</u>	<u>(806,405)</u>	<u>115</u>	<u>(9,435,240)</u>
Total net capital assets	<u>\$ 7,999,913</u>	<u>\$ (359,622)</u>	<u>\$ (925)</u>	<u>\$ 7,639,366</u>

# KENTUCKY LEAGUE OF CITIES, INC. AND SUBSIDIARIES

## Notes to the Consolidated Financial Statements, continued

### 4. Capital Assets, continued

Capital asset activity for the year ended June 30, 2015 is as follows:

	Beginning Balance	Additions	Retirements	Ending Balance
Capital assets at cost:				
Land	\$ 674,175	\$ -	\$ -	\$ 674,175
Buildings	6,427,420	4,405	-	6,431,825
Parking lot and improvements	1,239,306	-	-	1,239,306
Furniture and fixtures	2,745,269	205,403	(157,798)	2,792,874
Improvements	<u>5,289,173</u>	<u>201,510</u>	<u>-</u>	<u>5,490,683</u>
Total capital assets at cost	16,375,343	411,318	(157,798)	16,628,863
Less: accumulated depreciation	<u>(7,943,566)</u>	<u>(843,182)</u>	<u>157,798</u>	<u>(8,628,950)</u>
Total net capital assets	\$ <u>8,431,777</u>	\$ <u>(431,864)</u>	\$ <u>-</u>	\$ <u>7,999,913</u>

### 5. Long Term Debt

#### Bond Payable

On March 1, 2006, KLC issued an adjustable rate, taxable 2006 series bond in the amount of \$5,000,000. On December 1, 2009, this bond was refinanced by three 15-year variable rate leases. Repayment on these leases began January 1, 2011. The interest rates on the leases as of June 30, 2016 were 2.149%, 2.149% and 1.649%, respectively. The leases are included in the bond pools that are administered by KLC (see Note 8). The leases bear interest at variable rates based on the SIFMA municipal index. In order to secure the loan, KLC pledged the following as security for the loan repayment: all rental income derived from the building, \$2,000,000 of KLC's investments, and a negative lien pledge/covenant on the building. The following is a schedule of the required future principal payments in accordance with the refinancing agreement.

Year ending June 30,

2017	\$ 295,519
2018	304,250
2019	313,285
2020	322,538
2021	332,145
Thereafter	<u>1,273,146</u>
	\$ <u>2,840,883</u>

## KENTUCKY LEAGUE OF CITIES, INC. AND SUBSIDIARIES

### Notes to the Consolidated Financial Statements, continued

#### 5. Long Term Debt, continued

##### Note Payable

On July 10, 2013, KLC signed a promissory note with a financial institution in the amount of \$960,000, for the purpose of purchasing a parking lot. This note has a fixed interest rate of 3.79% for the term of the note, which is 15 years. The note is secured by the deed to the parking lot. The following is a schedule of the required future principal payments in accordance with the promissory note.

Year ending June 30,		
2017	\$	53,990
2018		56,101
2019		58,295
2020		60,511
2021		62,942
Thereafter		<u>522,143</u>
	\$	<u>813,982</u>

#### 6. Retirement Plans

##### 457 Deferred Compensation Plan

KLC previously offered its employees a deferred compensation plan created in accordance with Internal Revenue Code (IRC) Section 457 in which KLC contributed 10% of each participant's annual salary. Contributions by KLC to this plan ceased in April 1994, however, the plan remains as a strictly voluntary plan and all full-time employees are eligible to participate from the time of hire.

##### 401(a) Deferred Compensation Plan

In April 1994, KLC created a plan in accordance with IRC Section 401(a) that was available to all full-time employees who had completed one year of service. Only employees hired prior to September 1, 2000 may elect to participate in this plan. KLC made contributions to the 401(a) plan of 10% of each eligible participant's annual salary. For the years ended June 30, 2016 and 2015 contributions totaled \$124,558 and \$123,066, respectively.

## KENTUCKY LEAGUE OF CITIES, INC. AND SUBSIDIARIES

### Notes to the Consolidated Financial Statements, continued

#### 6. Retirement Plans, continued

##### County Employees Retirement System (CERS) Deferred Compensation Plan

*Plan description* – Beginning September 1, 2000, KLC has elected to participate in CERS, pursuant to KRS 78.530 administered by the Board of Trustees of the Kentucky Retirement Systems. This is a cost sharing, multiple employer defined benefit pension plan, which covers all eligible full-time employees and provides for retirement, disability and death benefits to plan members. Benefit contributions and provisions are established by statute. CERS issues a publicly available financial report that includes financial statements and required supplementary information. That report may be obtained by writing to Kentucky Retirement Systems, Perimeter Park West, 1260 Louisville Road, Frankfort, Kentucky 40601-6124 or by calling (502) 696-8800.

*Benefits provided* – CERS provides retirement, disability, and death benefits. Aspects of benefits for nonhazardous employees include retirement after 27 years of service or age 65. Nonhazardous employees who begin participation on or after September 1, 2008 must meet the rule of 87 (members age plus years of service credit must equal 87, and the member must be a minimum of 57 years of age) or the member is age 65, with a minimum of 60 months service credit. All KLC employees are deemed nonhazardous.

Each employee covered by CERS is entitled to a monthly benefit based upon their months of service multiplied by the average of 5 full fiscal years of salary (highest 5 or last 5 based on date of participation) upon attainment of CERS specified age (or age and service combinations). Participants have a fully vested interest after the completion of 60 months of service, 12 of which are current service.

Retirement benefits are determined as 2.5 percent of the employee's final 3-year average compensation times the employee's years of service. Employees with 10 years of continuous service are eligible to retire at age 60. Employees are eligible for service-related disability benefits regardless of length of service. Five years of service is required for nonservice-related disability eligibility. Disability benefits are determined in the same manner as retirement benefits but are payable immediately without an actuarial reduction. Death benefits equal the employee's final full-year salary.

*Contributions* – Benefit and contribution rates are established by state statute. Nonhazardous covered employees are required to contribute 5.00% of their salary to the plan. Nonhazardous covered employees who begin participation on or after September 1, 2008, are required to contribute 6.00% of their salary to the plan. KLC's contribution rate for nonhazardous employees, for both pension benefits and health benefits funds, was 17.06%, 17.67% and 18.89% for the years ended June 30, 2016, 2015 and 2014, respectively.

KLC's contributions to CERS related to pension benefits for the years ended June 30, 2016, 2015 and 2014 amount to \$627,399, \$587,675, and approximately \$628,000, respectively.

# KENTUCKY LEAGUE OF CITIES, INC. AND SUBSIDIARIES

## Notes to the Consolidated Financial Statements, continued

### 6. Retirement Plans, continued

#### County Employees Retirement System (CERS) Deferred Compensation Plan, continued

*Pension liabilities, pension expense, and deferred outflows of resources and deferred inflows of resources related to pensions* – At June 30, 2016 and 2015, and KLC reported a liability of \$8,292,148 and \$6,466,000, respectively, for its proportionate share of the net pension liability. The net pension liability was measured as of June 30, 2015 and 2014, and the total pension liability used to calculate the net pension liability was determined by an actuarial valuation as of those dates. KLC's proportion of the net pension liability was based on a projection of KLC's long-term share of contributions to the pension plan relative to the projected contributions of all participating organizations, actuarially determined. At June 30, 2015 and 2014, KLC's proportion was 0.193% and 0.199%, respectively.

For the years ended June 30, 2016 and 2015, KLC recognized pension expense of \$878,263 and \$518,000.

At June 30, 2016, KLC reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

	Deferred Outflows of Resources	Deferred Inflows of Resources
Differences between expected and actual experience	\$ 68,911	\$ -
Changes in assumption	836,173	-
Net difference between projected and actual earnings on pension plan investments	74,332	-
Changes in proportion and differences between KLC's contributions and proportionate share of contributions	-	165,856
District's contributions subsequent to the measurement date of June 30, 2015	<u>627,399</u>	<u>-</u>
Total	<u>\$ 1,606,815</u>	<u>\$ 165,856</u>

At June 30, 2015, KLC reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

	Deferred Outflows of Resources	Deferred Inflows of Resources
Net difference between projected and actual earnings on pension plan investments	\$ -	\$ 722,000
District's contributions subsequent to the measurement date of June 30, 2014	<u>587,675</u>	<u>-</u>
Total	<u>\$ 587,675</u>	<u>\$ 722,000</u>

## KENTUCKY LEAGUE OF CITIES, INC. AND SUBSIDIARIES

### Notes to the Consolidated Financial Statements, continued

#### 6. Retirement Plans, continued

##### County Employees Retirement System (CERS) Deferred Compensation Plan, continued

The deferred outflows of resources relate to KLC's contributions to the CERS plan subsequent to the measurement date and will be recognized as a reduction of the net pension liability in the year ending June 30, 2017. Other amounts reported as deferred outflows of resources and deferred inflows of resources related to pensions will be recognized in pension expense as follows:

Year ending June 30:	
2017	\$ 198,145
2018	198,145
2019	198,145
2020	252,295
2021	<u>(33,170)</u>
Total	\$ <u>813,560</u>

*Actuarial assumptions* – The total pension liability in the June 30, 2015 actuarial valuation was determined using the following actuarial assumptions, applied to all periods included in the measurement:

Inflation	3.25 percent
Salary increases	4.0 percent, average, including inflation
Investment rate of return	7.5 percent, net of pension plan investment expense, including inflation

The rates of mortality for the period after service retirement are according to the RP-2000 Combined Mortality Table for all retired members and beneficiaries. The RP-2000 Combined Mortality Table projected with Scale BB to 2013 is used for the period after disability retirement.

The actuarial assumptions used in the June 30, 2015 valuation were based on the results of an actuarial experience study for the period July 1, 2008 to June 30, 2013.

The long-term expected rate of return on pension plan investments was determined using a building-block method in which best-estimate ranges of expected future real rates of return (expected returns, net of pension plan investment expense and inflation) are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and by adding expected inflation. The target allocation and best estimates of arithmetic real rates of return for each major asset class are summarized in the following table:



# KENTUCKY LEAGUE OF CITIES, INC. AND SUBSIDIARIES

## Notes to the Consolidated Financial Statements, continued

### 6. Retirement Plans, continued

#### County Employees Retirement System (CERS) Deferred Compensation Plan, continued

	Target Allocation	Long Term Nominal Rate of Return
Combined Equity	44%	5.40%
Combined Fixed Income	19%	1.50%
Real Return (Diversification Inflation Strategies)	10%	3.50%
Real Estate	5%	4.50%
Absolute Return (Diversified Hedge Funds)	10%	4.25%
Private Equity	10%	8.50%
Cash	2%	-0.25%
Total	100%	

*Discount rate* – The discount rate used to measure the total pension liability was 7.5%. The projection of cash flows used to determine the discount rate assumed that contributions from plan members and employers will be made at statutory contribution rates. Based on those assumptions, the pension plan's fiduciary net position was projected to be available to make all projected future benefit payment of current active and inactive employees. Therefore, the long-term expected rate of return on pension plan investments was applied to all periods of projected benefit payments to determine the total pension liability.

*Sensitivity of the KLC's proportionate share of the net pension liability to changes in the discount rate* – The following presents KLC's proportionate share of the net pension liability calculated using the discount rate of 7.5%, as well as what the KLC's proportionate share of the net pension liability would be if it were calculated using a discount rate that is 1 percentage point lower (6.5%) or 1 percentage point higher (8.5%) than the current rate:

	1% Decrease (6.5%)	Current Discount Rate (7.5%)	1% Increase (8.5%)
KLC's share of the net pension liability	\$ 10,585,957	\$ 8,292,148	\$ 6,237,704

*Pension plan fiduciary net position* – Detailed information about the pension plan's fiduciary net position is available in the separately issued CERS financial report.

## KENTUCKY LEAGUE OF CITIES, INC. AND SUBSIDIARIES

### Notes to the Consolidated Financial Statements, continued

#### 7. Premium Financing Activities

As mentioned in Note 1 to the consolidated financial statements, KLCPFC was organized to finance insurance premiums for member cities that purchase property, liability and workers compensation insurance from KLCIS and KLCWCT (the Insurance Companies), respectively. KLCPFC enters into short-term financing agreements with member cities who wish to finance their premiums over a period of time. The length of the financing contracts range from six to twelve months and the finance charges range from 3.75% to 7.49% depending on the dollar amount of the premium financed. KLCPFC also requires a 20% down payment on all amounts financed.

When a member signs a financing contract, KLCPFC recognizes a receivable from the member city and a payable to the Insurance Companies. Premium amounts financed are transferred on a monthly basis to the Insurance Companies. Should a member be cancelled or withdraw from the insurance plans, KLCPFC would receive the unearned amount of the premium from the Insurance Companies. KLCPFC recognizes premium finance revenue as earned based upon the terms of the contract. Total premium finance income for June 30, 2016 and 2015 was \$177,680 and \$176,533, respectively. Total premiums receivable as of June 30, 2016 and 2015 were \$21,342 and \$51,650, respectively. Total premiums to be paid to the Insurance Companies as of June 30, 2016 and 2015, for the years ending June 30, 2017 and ended June 30, 2016, were \$598,301 and \$521,266, respectively.

#### 8. Administration Fees

Revenues for the years ended June 30, 2016 and 2015 include administrative fees and commissions from the following related parties, together with receivables and payables due to and from these affiliates:

	Fees and Commissions		Receivables and (Payables)	
	2016	2015	2016	2015
KLCIS	\$ 5,624,060	\$ 5,556,135	\$ 107,085	\$ 673,384
KLCWCT	2,029,238	2,018,433	88,791	(65,278)
KLCUCRT	120,344	119,434	-	-
KBC	343,857	321,711	-	-
KBDC	204,690	25,765	-	-
KLCFT	203,888	232,102	-	-
KSBITWCF	-	50,213	-	-
KSBITPLF	-	49,840	-	-

KLC has an administrative agreement with KLCIS, KLCWCT, and KLCUCRT to provide substantially all operational, management and administrative services in exchange for a reimbursement of administrative costs. Additionally, KLCIA entered into a marketing agreement with KLCIS and KLCWCT which provides that KLCIS and KLCWCT pay a commission to KLCIA for insurance which KLCIA markets and an administrative fee, as a percentage of premiums, for general marketing. Each agreement is subject to termination by either party upon 90 days written notice.

## KENTUCKY LEAGUE OF CITIES, INC. AND SUBSIDIARIES

### Notes to the Consolidated Financial Statements, continued

#### 8. Administration Fees, continued

KLC had administrative agreements with KSBITPLF and KSBITWCT (collectively, KSBIT) to provide substantially all operational, management and administrative services in exchange for a reimbursement of administrative costs and a management fee, calculated as a percentage of annual gross premiums. During the year ended June 30, 2013, the agreement was modified at the direction of the Kentucky Department of Insurance to discontinue the management fee due to KLC because of KSBIT's net position. KLC assisted KSBIT during its transition to another administrator and these agreements were terminated on November 1, 2014 and November 30, 2014, for KSBITPLF and KSBITWCT, respectively.

KLC has an administrative agreement with KBC to provide monitoring of bond proceeds, origination of financing agreements, servicing of financing agreements, and other administrative services, in exchange for an administrative fee. This fee is comprised of an initial issuance fee and a financing fee equal to .25% of the aggregate unpaid principal components of all financing payments calculated on a quarterly basis, payable to the extent that monies are available in KBC's reserve funds. For the years ended June 30, 2016 and 2015, KBC issued approximately \$13.3 million and \$21.8 million, respectively, in bonds. The agreement is subject to termination by either party with 30 days written notice. The President and Second Vice President of KLC serve as members, non-voting and voting, respectively, of the Board of Trustees of KBC and the KLC Executive Board appoints the remaining four members of KBC's Board of Trustees.

KLC provides similar services for commensurate fees to KBDC. The program was developed to allow local governments to support economic development projects issued by 501(c)(3) entities. For the years ended June 30, 2016 and 2015, KBDC issued approximately \$278.1 million and \$17.2 million, respectively, in bonds. The agreement is subject to termination by either party with 30 days written notice. The President and Second Vice President of KLC serve as members, non-voting and voting, respectively, of the Board of Trustees of KBDC and the KLC Executive Board appoints the remaining four members of KBDC's Board of Trustees.

KLC functions as the program administrator for KLCFT, which provides tax-exempt financing to members of KLC. In exchange for administrative services performed KLCFT pay's KLC an administrative fee. Additionally, KLC finances three lease agreements through the KLCFT, with outstanding principal balances of \$2,840,883 and \$3,104,312, as of June 30, 2016 and 2015, respectively.

KLC also functions as the program administrator for KLCIP, which provides pooled investment services to members of KLC. The KLC Executive Board appoints the members of KLCIP's Board of Trustees. KLC did not receive an administrative fee for 2016 or 2015.

#### 9. Litigation

On August 26, 2014, the Department filed a suit against KLC, KLCIS, and the Kentucky School Boards Association for an unspecified amount of damages related to the administration of KSBIT. Specifically, the complaint contains allegations of negligence and misrepresentation in connection with the management of KSBITWCF and KSBITPLF. The allegations against KLC and KLCIS are limited to the time period beginning January 2010 through July 2013.

# KENTUCKY LEAGUE OF CITIES, INC. AND SUBSIDIARIES

## Notes to the Consolidated Financial Statements, continued

### 9. Litigation, continued

During 2016, KLC and its insurance carrier reached a settlement agreement with the Department. As a result of insurance coverage and KLCIS's payments of legal costs, KLC did not ultimately incur any direct expense related to this litigation.

### 10. Operating Expenses

Operating expenses for 2016 and 2015 by natural classification are as follows:

	<u>2016</u>	<u>2015</u>
Salaries	\$ 6,257,723	\$ 5,836,097
Retirement	1,237,212	867,840
Employee benefits	932,637	858,146
Depreciation and amortization	812,201	848,978
Payroll taxes	433,364	409,072
Professional services	412,703	548,653
Meetings	397,009	361,698
Building management	278,299	304,498
Utilities	247,653	262,307
Travel	133,717	137,486
Legislative services	131,645	125,699
Insurance	116,969	107,213
Telephones	94,916	92,562
Program and development	75,111	100,986
Dues	57,113	59,993
Postage	54,735	50,493
KLCPFC finance expenses	44,707	28,634
Office supplies	33,869	47,010
Publications	32,066	51,208
Bond administration	4,267	4,763
Other expenses	<u>97,503</u>	<u>67,821</u>
	<u>\$ 11,885,419</u>	<u>\$ 11,171,157</u>

## KENTUCKY LEAGUE OF CITIES, INC. AND SUBSIDIARIES

### Notes to the Consolidated Financial Statements, continued

#### 10. Operating Expenses, continued

Operating expenses for 2016 and 2015 by functional classification are as follows:

	<u>2016</u>	<u>2015</u>
Administrative and general	\$ 4,861,007	\$ 3,828,956
Member insurance services	5,048,408	5,369,742
Legislative services	1,502,766	1,463,728
Member financial services	249,257	262,321
Member meeting and training services	<u>223,981</u>	<u>246,410</u>
	<u>\$ 11,885,419</u>	<u>\$ 11,171,157</u>

#### 11. Subsequent Event

On September 20, 2016, KLCRFC entered into a \$5,900,000 line of credit agreement with a financial institution with a variable interest rate based on the 30-day LIBOR rate plus 1.9%. This line of credit matures on April 30, 2017. KLC is a guarantor on the line of credit. The complete line of credit was drawn on September 21, 2016, in order for KLCRFC to pay KLCIS in full for premiums financed by members.

**Independent Auditors' Report on Internal Control Over Financial Reporting  
and on Compliance and Other Matters Based on an Audit of Financial  
Statements Performed in Accordance with *Government Auditing Standards***

Board of Directors  
Kentucky League of Cities, Inc. and Subsidiaries  
Lexington, Kentucky

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the consolidated financial statements of Kentucky League of Cities, Inc. and Subsidiaries (KLC) as of and for the year ended June 30, 2016, and the related notes to the consolidated financial statements, which collectively comprise KLC's basic consolidated financial statements, and have issued our report thereon dated September 20, 2016.

**Internal Control Over Financial Reporting**

In planning and performing our audit of the consolidated financial statements, we considered KLC'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 consolidated financial statements, but not for the purpose of expressing an opinion on the effectiveness of KLC's internal control. Accordingly, we do not express an opinion on the effectiveness of KLC'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 internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be material weaknesses or significant deficiencies and, therefore, material weaknesses or significant deficiencies may exist that were not identified. 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. We consider the deficiency described in the accompanying Schedule of Findings and Responses to be a significant deficiency.

### **Compliance and Other Matters**

As part of obtaining reasonable assurance about whether KLC's consolidated 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 consolidated 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*.

### **Management's Response to Finding**

Management's response to the finding identified in our audit is described in the accompanying Schedule of Findings and Responses. Management's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

### **Purpose of this Report**

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

*Dean Dotson Allen Ford, PLLC*

September 20, 2016  
Lexington, Kentucky

**KENTUCKY LEAGUE OF CITIES, INC. AND SUBSIDIARIES**

**Schedule of Findings and Responses**

**Year ended June 30, 2016**

**Section I - Summary of Auditors' Results**

- a. The type of report issued on the financial statements: **Unmodified opinion**
- b. Material weaknesses identified in the internal control over financial reporting: **No**
- c. Significant deficiencies identified in the internal control over financial reporting: **No**
- d. Non-compliance which is material to the financial statements: **No**

**Section II - Summary of Findings and Responses**

*None*



## KENTUCKY LEAGUE OF CITIES, INC. AND SUBSIDIARIES

### Schedule of Prior Year Findings

Year ended June 30, 2016

#### Section I - Status of Prior Year Findings

##### **Finding 2015-001:**

###### *Criteria, Condition, and Effect:*

During the 2015 audit of a related entity, it came to our attention that the 2014 KLCIA commission revenue was understated by \$687,418. This understatement occurred because an intercompany commission check from KLCIS, written on June 25, 2014, was not deposited until July 3, 2014 and it was not included on the June 2014 bank reconciliation as a deposit in transit. KLC identified the error when the check was deposited, but did not have a process in place to ensure that intercompany payments and receipts were recorded in the proper time period in both entities' accounting records. As a result, a material adjusting entry was required to restate the 2014 financial statements.

###### *Recommendation:*

We recommend that the additional step of scanning through the subsequent month's deposits and checks for potential intercompany outstanding items be included in the monthly bank reconciliation process. In addition, the review of bank reconciliations should be performed simultaneously in order to identify intercompany in transit deposits and checks at the reviewer level.

###### *Current Year Status:*

This finding was resolved in the current year.

##### **Finding 2015-002:**

###### *Criteria, Condition, and Effect:*

Understanding and monitoring executed agreements is important in providing for the services necessary for the performance of administrative services on behalf of related entities. During our audit, DDAF noted that there is not any executed contract with the Kentucky Bond Development Corporation.

###### *Recommendation:*

We recommend that, upon approval of services, executed agreements are prepared and approved by all parties to the contract.

###### *Current Year Status*

This finding was resolved in the current year.

# KENTUCKY LEAGUE OF CITIES, INC. AND SUBSIDIARIES

## Consolidating Statements of Net Position

June 30, 2016

	KLC	KLCIA	KLCPFC	Consolidating Entries	Consolidated Total
<b>Assets</b>					
Current assets:					
Cash and cash equivalents	\$ 3,736,679	\$ 233,153	\$ 670,706	\$ -	\$ 4,640,538
Investments	4,671,289	1,353,952	-	(300,000)	5,725,241
Accounts receivable	481,138	3,093	-	-	484,231
Premiums receivable	-	-	21,342	-	21,342
Prepaid expenses and other assets	478,728	26,245	6,752	-	511,725
Due from related parties	<u>850,764</u>	<u>102</u>	<u>295,004</u>	<u>(834,223)</u>	<u>311,647</u>
Total current assets	10,218,598	1,616,545	993,804	(1,134,223)	11,694,724
Capital assets, net	<u>7,639,366</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>7,639,366</u>
Total assets	17,857,964	1,616,545	993,804	(1,134,223)	19,334,090
<b>Deferred Outflows of Resources</b>					
Deferred amount related to pension plan	<u>1,606,815</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>1,606,815</u>
Combined assets and deferred outflows of resources	19,464,779	1,616,545	993,804	(1,134,223)	20,940,905

# KENTUCKY LEAGUE OF CITIES, INC. AND SUBSIDIARIES

## Consolidating Statements of Net Position, continued

June 30, 2016

	KLC	KLCIA	KLCPFC	Consolidating Entries	Consolidated Total
<b>Liabilities</b>					
Current liabilities:					
Accounts payable	193,127	11,431	-	-	204,558
Accrued liabilities	1,011,536	5,013	-	-	1,016,549
Unearned revenue	449,096	29,885	150,300	-	629,281
Due to related parties	115,771	834,223	-	(834,223)	115,771
Current maturities of note payable	53,990	-	-	-	53,990
Current maturities of bond payable	<u>295,519</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>295,519</u>
Total current liabilities	2,119,039	880,552	150,300	(834,223)	2,315,668
Note payable, net of current maturities	759,992	-	-	-	759,992
Bond payable, net of current maturities	2,545,364	-	-	-	2,545,364
Net pension liability	<u>8,292,148</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>8,292,148</u>
Total liabilities	13,716,543	880,552	150,300	(834,223)	13,913,172
<b>Deferred Inflows of Resources</b>					
Deferred amount related to pension plan	<u>165,856</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>165,856</u>
Combined liabilities and deferred inflows of resources	<u>13,882,399</u>	<u>880,552</u>	<u>150,300</u>	<u>(834,223)</u>	<u>14,079,028</u>
<b>Net Position</b>					
Invested in fixed assets, net of related debt	3,984,501	-	-	-	3,984,501
Unrestricted	<u>1,597,879</u>	<u>735,993</u>	<u>843,504</u>	<u>(300,000)</u>	<u>2,877,376</u>
Total net position	<u>\$ 5,582,380</u>	<u>\$ 735,993</u>	<u>\$ 843,504</u>	<u>\$ (300,000)</u>	<u>\$ 6,861,877</u>

See accompanying notes and report of independent auditors.

# KENTUCKY LEAGUE OF CITIES, INC. AND SUBSIDIARIES

## Consolidating Statements of Net Position

June 30, 2015

	<u>KLC</u>	<u>KLCIA</u>	<u>KLCPFC</u>	<u>Consolidating Entries</u>	<u>Consolidated Total</u>
<b>Assets</b>					
Current assets:					
Cash and cash equivalents	\$ 3,241,607	\$ 219,086	\$ 473,065	\$ -	\$ 3,933,758
Investments	4,670,995	1,334,766	-	(300,000)	5,705,761
Accounts receivable	188,639	9,937	-	-	198,576
Premiums receivable	-	-	51,650	-	51,650
Prepaid expenses and other assets	475,721	21,561	1,420	-	498,702
Due from related parties	<u>2,856,421</u>	<u>1,881,057</u>	<u>382,793</u>	<u>(4,028,714)</u>	<u>1,091,557</u>
Total current assets	11,433,383	3,466,407	908,928	(4,328,714)	11,480,004
Capital assets, net	<u>7,999,913</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>7,999,913</u>
Total assets	19,433,296	3,466,407	908,928	(4,328,714)	19,479,917
<b>Deferred Outflows of Resources</b>					
Deferred amount related to pension plan	<u>587,675</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>587,675</u>
Combined assets and deferred outflows of resources	20,020,971	3,466,407	908,928	(4,328,714)	20,067,592

# KENTUCKY LEAGUE OF CITIES, INC. AND SUBSIDIARIES

## Consolidating Statements of Net Position, continued

June 30, 2015

	KLC	KLCIA	KLCPFC	Consolidating Entries	Consolidated Total
<b>Liabilities</b>					
Current liabilities:					
Accounts payable	265,470	7,898	-	-	273,368
Accrued liabilities	961,503	-	-	-	961,503
Unearned revenue	455,347	38,856	128,581	-	622,784
Due to related parties	1,655,744	2,856,421	-	(4,028,714)	483,451
Current maturities of note payable	51,872	-	-	-	51,872
Current maturities of bond payable	<u>287,640</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>287,640</u>
Total current liabilities	3,677,576	2,903,175	128,581	(4,028,714)	2,680,618
Note payable, net of current maturities	813,982	-	-	-	813,982
Bond payable, net of current maturities	2,816,672	-	-	-	2,816,672
Net pension liability	<u>6,466,000</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>6,466,000</u>
Total liabilities	13,774,230	2,903,175	128,581	(4,028,714)	12,777,272
<b>Deferred Inflows of Resources</b>					
Deferred amount related to pension plan	<u>722,000</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>722,000</u>
Combined liabilities and deferred inflows of resources	<u>14,496,230</u>	<u>2,903,175</u>	<u>128,581</u>	<u>(4,028,714)</u>	<u>13,499,272</u>
<b>Net Position</b>					
Invested in fixed assets, net of related debt	4,029,747	-	-	-	4,029,747
Unrestricted	<u>1,494,994</u>	<u>563,232</u>	<u>780,347</u>	<u>(300,000)</u>	<u>2,538,573</u>
Total net position	<u>\$ 5,524,741</u>	<u>\$ 563,232</u>	<u>\$ 780,347</u>	<u>\$ (300,000)</u>	<u>\$ 6,568,320</u>

See accompanying notes and report of independent auditors.

# KENTUCKY LEAGUE OF CITIES, INC. AND SUBSIDIARIES

## Consolidating Statements of Revenues, Expenses and Changes in Net Position

Year ended June 30, 2016

	KLC	KLCIA	KLCPFC	Consolidating Entries	Consolidated Total
Operating revenue:					
Administrative fee - KLCIS	\$ 4,661,498	\$ -	\$ -	\$ -	\$ 4,661,498
Administrative fee - KLCWCT	1,707,944	-	-	-	1,707,944
Administrative fee - Bond Pools	752,435	-	-	-	752,435
Administrative fee - KLCUCRT	120,344	-	-	-	120,344
Administrative fee - Financial Services	75,000	-	-	(75,000)	-
Commissions	2,226,545	2,474,035	-	(2,226,545)	2,474,035
Member dues	523,203	-	-	-	523,203
Member meeting and training income	426,427	-	-	-	426,427
Premium finance income	-	-	177,680	-	177,680
Other	309,634	31,258	9,548	-	350,440
Publication income	4,768	-	-	-	4,768
Total operating revenue	10,807,798	2,505,293	187,228	(2,301,545)	11,198,774
Operating expenses	11,704,250	2,358,526	124,188	(2,301,545)	11,885,419
Operating income	(896,452)	146,767	63,040	-	(686,645)
Nonoperating revenue (expenses):					
Interest and investment income (loss)	55,047	25,994	117	-	81,158
Interest expense	(96,585)	-	-	-	(96,585)
Gain on sale of fixed assets	(925)	-	-	-	(925)
Net rental income	996,554	-	-	-	996,554
Total nonoperating revenue (expenses)	954,091	25,994	117	-	980,202
Change in net position	57,639	172,761	63,157	-	293,557
Net position, beginning of year	5,524,741	563,232	780,347	(300,000)	6,568,320
Net position, end of year	\$ 5,582,380	\$ 735,993	\$ 843,504	\$ (300,000)	\$ 6,861,877

See accompanying notes and report of independent auditors.

# KENTUCKY LEAGUE OF CITIES, INC. AND SUBSIDIARIES

## Consolidating Statements of Revenues, Expenses and Changes in Net Position, continued

Year ended June 30, 2015

	KLC	KLCIA	KLCRFC	Consolidating Entries	Consolidated Total
Operating revenue:					
Administrative fee - KLCIS	\$ 4,591,085	\$ -	\$ -	\$ -	\$ 4,591,085
Administrative fee - KLCWCT	1,721,364	-	-	-	1,721,364
Administrative fee - Bond Pools	579,578	-	-	-	579,578
Administrative fee - KLCUCRT	119,434	-	-	-	119,434
Administrative fee - Financial Services	75,000	-	-	(75,000)	-
Administrative fee - KSBIT	131,221	-	-	-	131,221
Commissions	2,419,932	2,688,813	-	(2,419,932)	2,688,813
Member dues	492,224	-	-	-	492,224
Member meeting and training income	358,100	-	-	-	358,100
Premium finance revenue	-	-	176,533	-	176,533
Other	275,387	25,084	8,945	-	309,416
Publication income	23,822	-	-	-	23,822
Total operating revenue	10,787,147	2,713,897	185,478	(2,494,932)	11,191,590
Operating expenses	<u>11,002,232</u>	<u>2,589,346</u>	<u>74,511</u>	<u>(2,494,932)</u>	<u>11,171,157</u>
Operating (loss) income	(215,085)	124,551	110,967	-	20,433
Nonoperating revenue (expenses):					
Interest and investment income	61,553	(7,484)	116	-	54,185
Interest expense	(101,101)	-	-	-	(101,101)
Gain on sale of fixed assets	48,505	-	-	-	48,505
Net rental income	<u>989,114</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>989,114</u>
Total nonoperating revenue	<u>998,071</u>	<u>(7,484)</u>	<u>116</u>	<u>-</u>	<u>990,703</u>
Change in net position before cumulative effect of a change in accounting principle	782,986	117,067	111,083	-	1,011,136
Cumulative effect on prior years (to June 30, 2014) resulting from the retroactive change in accounting for pensions (Note 2)	<u>(6,670,000)</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>(6,670,000)</u>
Change in net position	(5,887,014)	117,067	111,083	-	(5,658,864)
Net position, beginning of year	<u>11,411,755</u>	<u>446,165</u>	<u>669,264</u>	<u>(300,000)</u>	<u>12,227,184</u>
Net position, end of year	<u>\$ 5,524,741</u>	<u>\$ 563,232</u>	<u>\$ 780,347</u>	<u>\$ (300,000)</u>	<u>\$ 6,568,320</u>

See accompanying notes and report of independent auditors.

# KENTUCKY LEAGUE OF CITIES, INC. AND SUBSIDIARIES

## Schedules of Required Supplementary Information

### Schedule of the Proportionate Share of the Net Pension Liability

#### County Employees Retirement System (CERS) Deferred Compensation Plan (Amounts in thousands)

	2015	2014	2013	2012	2011	2010	2009	2008	2007	2006
Portion of the net pension liability (asset)	0.19 %	0.20 %								
Proportionate share of the net pension liability (asset)	\$ 8,292	\$ 6,466								
Covered- Employee Payroll	\$ 4,962	\$ 4,591								
Proportionate share of the net pension liability (asset) as a percentage of its covered-employee payroll	167.11 %	140.84 %								
Plan fiduciary net position as a percentage of the total pension liability	59.97 %	66.80 %								

See accompanying notes and report of independent auditors.



# KENTUCKY LEAGUE OF CITIES, INC. AND SUBSIDIARIES

## Schedules of Required Supplementary Information

### Schedule of Contributions

#### County Employees Retirement System (CERS) Deferred Compensation Plan (Amounts in thousands)

	<u>2015</u>	<u>2014</u>	<u>2013</u>	<u>2012</u>	<u>2011</u>	<u>2010</u>	<u>2009</u>	<u>2008</u>	<u>2007</u>	<u>2006</u>
Contractually required contribution	\$ 633	\$ 631								
Contributions in relation to the contractually required contribution	<u>588</u>	<u>628</u>								
Contribution deficiency (excess)	\$ <u>45</u>	\$ <u>3</u>								
Covered-employee payroll	\$ 4,962	\$ 4,591								
Contributions as a percentage of covered-employee payroll	11.85 %	13.68 %								

See accompanying notes and report of independent auditors.