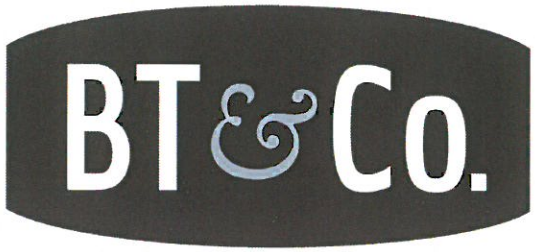

BERBERICH TRAHAN & CO., P.A.

Certified Public Accountants

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

FINANCIAL STATEMENTS
WITH SUPPLEMENTARY INFORMATION
YEARS ENDED DECEMBER 31, 2013 AND 2012

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

FINANCIAL STATEMENTS
WITH SUPPLEMENTARY INFORMATION

Years Ended December 31, 2013 and 2012

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

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, 2013 and 2012, 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 reasonable basis for our audit opinion.

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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, 2013 and 2012, 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
May 7, 2014

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	2013	2012
LIABILITIES AND STOCKHOLDER'S EQUITY		
Current liabilities:		
Accounts payable	$ 188,765	$ 180,419
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	2,368,256	2,644,353
	3,542,809	3,818,906
Treasury stock at cost - 3,545 shares	(599,991)	(599,991)
Total stockholder's equity	2,942,818	3,218,915
	$ 3,131,583	$ 3,399,334

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

STATEMENTS OF INCOME

Years Ended December 31, 2013 and 2012

	2013	2012
Operating revenues	$ 3,875,860	$ 4,150,952
Operating expenses:		
Operation and maintenance	2,900,950	2,732,704
Depreciation	196,677	194,069
Total operating expenses	3,097,627	2,926,773
Net income	$ 778,233	$ 1,224,179

See accompanying notes to financial statements.

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

STATEMENTS OF RETAINED EARNINGS

Years Ended December 31, 2013 and 2012

	2013	2012
Balance, beginning of year	$ 2,644,353	$ 2,703,236
Net income	778,233	1,224,179
Cash dividends to the City of Derby	(1,054,330)	(1,283,062)
Balance, end of year	$ 2,368,256	$ 2,644,353

See accompanying notes to financial statements.

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

STATEMENTS OF CASH FLOWS

Years Ended December 31, 2013 and 2012

	2013	2012
Cash flows from operating activities:		
Net income	$ 778,233	$ 1,224,179
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	196,677	194,069
Changes in assets and liabilities:		
Accounts and unbilled receivables	10,686	(94,281)
Materials and supplies	81,997	(83,836)
Accounts payable	8,346	61,422
Net cash provided by operating activities	1,075,939	1,301,553
Cash flows from investing activities:		
Purchases of equipment	(33,430)	(49,264)
Cash flows from financing activities:		
Dividends paid	(1,054,330)	(1,283,062)
Net decrease in cash	(11,821)	(30,773)
Cash, beginning of year	394,910	425,683
Cash, end of year	$ 383,089	$ 394,910

See accompanying notes to financial statements.

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

NOTES TO FINANCIAL STATEMENTS

December 31, 2013 and 2012

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 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, 2013.

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.

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:

	Years
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, 2013. 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, 2013 and 2012.

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 2010.

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.

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. The City of Derby bills the water charges for the Company.

All employees of the Company are employees of the City of Derby. The Company makes a monthly reimbursement to the City of Derby for contract labor. The total contract labor reimbursement from the Company to the City of Derby for the years ended December 31, 2013 and 2012 was $ 441,102 and $ 490,412, respectively.

The City of Derby receives dividends from the Company. Cash dividends paid to the City of Derby from the Company were $ 1,054,330 and $ 1,283,062 for the years ended December 31, 2013 and 2012, respectively.

The Company also leases office space from the City of Derby. Total rental expense included in operations was $ 9,600 for each of the years 2013 and 2012.

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 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 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. The Company paid dividends to the City of $ 1,054,330 and $ 1,283,062 for the years 2013 and 2012, respectively, related to principal and interest payments on the 2013B and 2004-A bond issues. Future dividend payments to the City are anticipated in order to retire the Series 2004-A 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 contains a 100% "take or pay" provision. No amounts were paid under the "take or pay" provision for 2013 and 2012.

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, 2013 and 2012

	2013	2012
Contract labor	$ 441,102	$ 490,412
Repairs and maintenance	322,117	95,855
Wichita water purchases	1,867,326	1,942,992
Electric power	31,020	18,741
Other utilities	6,272	3,573
Office supplies and postage	21,734	14,395
Rentals/operating leases	14,300	14,300
Water treating supplies	5,905	4,300
Insurance	12,596	15,403
Professional fees	100,425	101,111
Dues and subscriptions	1,720	251
Other taxes	3,727	3,723
Miscellaneous	72,706	27,648
Total	$ 2,900,950	$ 2,732,704

See accompanying independent auditor's report.