

**COVINGTON ELECTRIC SYSTEM**  
**FINANCIAL STATEMENTS**  
**AND SUPPLEMENTARY INFORMATION**  
**FOR YEARS ENDED**  
**JUNE 30, 2018 AND 2017**

# COVINGTON ELECTRIC SYSTEM

## TABLE OF CONTENTS

### Introductory Section

Directory .....	1
-----------------	---

### Financial Section

Independent Auditor's Report .....	2
------------------------------------	---

Management Discussion and Analysis .....	5
--	---

#### Financial Statements:

Statements of Net Position .....	11
----------------------------------	----

Statements of Revenues, Expenses, and Changes in Net Position .....	13
---	----

Statements of Cash Flows .....	14
--------------------------------	----

Statements of Fiduciary Net Position – Defined Benefit Plan .....	16
---	----

Statements of Changes in Fiduciary Net Position – Defined Benefit Plan .....	17
--	----

Statements of Fiduciary Net Position – 457 Plan .....	18
---	----

Statements of Changes in Fiduciary Net Position – 457 Plan .....	19
--	----

Notes to Financial Statements .....	20
-------------------------------------	----

#### Required Supplementary Information:

##### Schedules of Changes in Net Position Liability (Asset) and Related

Ratios Based on Participation in the Public Employee Pension Plan .....	37
---	----

##### Schedules of Contributions Based on Participation in the Public

Employee Pension Plan .....	38
-----------------------------	----

Schedules of Investment Returns .....	39
---------------------------------------	----

Notes to Required Supplementary Information .....	40
---	----

### Supplementary and Other Information Section

Schedules of Operating Revenues and Expenses - Electric System .....	41
--	----

Schedule of Long-Term Debt .....	43
----------------------------------	----

Electric Rates in Force .....	44
-------------------------------	----

Supplemental Information - Electric System - Unaudited .....	45
--	----

### Internal Control and Compliance Section

#### Independent Auditor's Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial

Statements Performed in Accordance with <i>Governmental Auditing Standards</i> .....	46
--	----

Schedule of Findings .....	48
----------------------------	----

Schedule of Prior Year Findings .....	49
---------------------------------------	----

**INTRODUCTORY SECTION  
COVINGTON ELECTRIC SYSTEM  
DIRECTORY**  
June 30, 2018

**GOVERNING BOARD**

Keith McCalla  
Mary Jones  
James Baddour  
Christy Hayden  
Justin D. Glass

**MANAGEMENT TEAM**

Tim Sallee, General Manager  
Kathy McClinton, Comptroller

**COUNSEL**

David E. Owen  
Covington, Tennessee

**INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS**

Alexander Thompson Arnold PLLC  
Jackson, Tennessee

## **FINANCIAL SECTION**



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## Independent Auditor's Report

Board of Directors  
Covington Electric System  
Covington, Tennessee

### Report on the Financial Statements

We have audited the accompanying financial statements of the major fund and the Covington Electric System Employees' 457 Plan of the Covington Electric System (the System), which are enterprise and fiduciary funds of the City of Covington, Tennessee, as of and for the years ended June 30, 2018 and 2017, and the financial statements of the Covington Electric System Employees' Retirement Plan (fiduciary fund) as of and for the years ended March 31, 2018 and 2017, and the related notes to the financial statements, which collectively comprise the System's basic financial statements as listed in the table of contents.

### ***Management's Responsibility for the Financial Statements***

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

### ***Auditor's Responsibility***

Our responsibility is to express opinions on these financial statements based on our 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 *Governmental Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

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

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

## ***Opinions***

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the major fund and the Covington Electric System Employees' 457 Plan of the System as of June 30, 2018 and 2017, and the Covington Electric System Employees' Retirement Plan as of years ended March 31, 2018 and 2017 and the respective changes in financial position and cash flows thereof for the years then ended in accordance with accounting principles generally accepted in the United States of America.

## ***Emphasis of Matters***

As discussed in Note 1, the financial statements present only the Covington Electric System funds and do not purport to, and do not, present fairly the financial position of the City of Covington, Tennessee, as of June 30, 2018 and 2017, the changes in its financial position or, where applicable, its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

## ***Other Matters***

### ***Required Supplementary Information***

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis, Schedules of Changes in Net Position Liability (Asset) and Related Ratios Based on Participation in the Public Employee Pension Plan, Schedules of Contributions Based on Participation in the Public Employee Pension Plan, Schedules of Investment Returns, and the Notes to the Required Supplementary Information as listed in the table of contents be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our 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 financial statements that collectively comprise the System's basic financial statements. The introductory section and supplementary and other information section as listed in the Table of Contents are presented for purposes of additional analysis and are not a required part of the financial statements.

The supplementary and other information section as listed in the Table of Contents, except that which has been marked unaudited, 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. Such information has been subjected to the auditing procedures applied in the audits 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 and other information section as listed in the Table of Contents except that which is

marked unaudited is fairly stated, in all material respects, in relation to the basic financial statements as a whole.

The introductory section and the supplementary and other information marked unaudited have not been subjected to the auditing procedures applied in the audits of the basic financial statements, and accordingly, we do not express an opinion or provide any assurance on them.

**Other Reporting Required by *Governmental Auditing Standards***

In accordance with *Governmental Auditing Standards*, we have also issued our report dated October 22, 2018 on our consideration of the System'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 solely describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the System's internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Governmental Auditing Standards* in considering the System's internal control over financial reporting and compliance.

Alexander Thompson Arnold PLLC

Jackson, Tennessee  
October 22, 2018

## **MANAGEMENT DISCUSSION AND ANALYSIS**

As management of the Covington Electric System, we offer readers of the System's financial statements this narrative overview and analysis of the financial activities of the System for the fiscal years ended June 30, 2018 and 2017. All amounts, unless otherwise indicated, are expressed in actual dollars.

### **FINANCIAL HIGHLIGHTS**

Management believes the System's financial condition is strong. The System is well within the stringent financial policies and guidelines set by the Board and management. The following are combined key financial highlights for the Electric System.

- Total assets and deferred outflows of resources at year-end were \$23.96 million and exceeded liabilities and deferred inflows of resources in the amount of \$17.69 million (i.e. net position).
- Net position increased \$243 thousand during the current year. Unrestricted net position increased by \$381 thousand, net investment in capital assets decreased by \$145 thousand, and restricted for debt service increased by \$7 thousand.
- During fiscal year 2018, the System delivered 241.08 million kWh compared to 245.57 million kWh during the fiscal year 2017.
- Operating revenues were \$20.95 million, a decrease from fiscal year 2017 in the amount of \$329 thousand.
- Operating expenses were \$20.33 million, a decrease from fiscal year 2017 in the amount of \$513 thousand.
- The operating income for the year was \$621 thousand as compared to \$437 thousand during the 2017 fiscal year.

### **OVERVIEW OF THE FINANCIAL STATEMENTS AND SUPPLEMENTARY INFORMATION**

Management's Discussion and Analysis (MD&A) serves as an introduction to, and should be read in conjunction with, the financial statements and supplementary information. The MD&A represents management's examination and analysis of the System's financial condition and performance. Summary financial statement data, key financial and operational indicators used in the System's strategic plan, budget, bond resolutions and other management tools were used for this analysis. The Financial Statements and Supplementary Information is made up of four sections: 1) the introductory section, 2) the financial section, 3) the supplementary and other information section, and 4) the internal control and compliance section. The introductory section includes the System's directory. The financial section includes the required MD&A, the independent auditor's report, the financial statements with accompanying notes, and the required supplementary information. The supplementary and other information section includes selected financial and operational information. The internal control and compliance section includes the report on internal control and compliance. These sections make up the financial report presented here.

### **REQUIRED FINANCIAL STATEMENTS**

An Enterprise Fund is used to account for the operations of the System, which is financed and operated in a manner similar to private business enterprises where the intent is that the costs of providing services to the general public on a continuing basis be financed or recovered primarily through user charges. The financial statements report information about the System, using accounting methods similar to those used by private sector companies. These statements offer short-term and long-term financial information about its activities.

A Fiduciary Fund is used to account for resources held for the benefit of parties outside of the government. Fiduciary funds are not reported in the government-wide financial statements because the resources of those funds are not available to support Covington Electric System's own programs. The accounting used for fiduciary funds is much like that used for proprietary funds.

## MANAGEMENT DISCUSSION AND ANALYSIS

Covington Electric System maintains two types of fiduciary fund. The pension trust fund is used to report resources held for retirees and beneficiaries covered by the defined benefit plan. They also report a deferred compensation trust plan that allows employees to contribute a portion of their salary toward the plan.

The fiduciary fund financial statements can be found as listed in the table of contents.

The *Statement of Net Position* presents the financial position of the System on a full accrual historical cost basis. The statement includes all of the System's assets, liabilities, and deferred inflows/outflows of resources with the differences reported as net position. Over time, increases and decreases in net position may serve as a useful indicator of whether the financial position of the System is improving or deteriorating.

The *Statement of Revenues, Expenses, and Changes in Net Position* presents the results of the business activities over the course of the fiscal year and information as to how the net position changed during the year. All changes in net position are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of the related cash flows. This statement measures the success of the System's operations and can be used to determine whether the System has successfully recovered all of its costs. This statement also measures the System's profitability and credit worthiness.

The *Statement of Cash Flows* presents changes in cash and cash equivalents, resulting from operational, financing, and investing activities. This statement presents cash receipt and cash disbursement information, without consideration of the earnings event, when an obligation arises.

The *Notes to the Financial Statements* provide required disclosures and other information that are essential to a full understanding of material data provided in the statements. The notes present information about the System's accounting policies, significant account balances and activities, material risks, obligations, commitments, contingencies and subsequent events, if any.

### FINANCIAL ANALYSIS

One of the most important questions asked about the System's finances is "Is the System, as a whole, better off or worse off as a result of the year's activities?" The Statement of Net Position and the Statement of Revenues, Expenses, and Changes in Net Position report information about the System's activities in a way that will help answer this question. These two statements report the net position of the System, and the changes in the net position. Net position is one way to measure the financial health or financial position of the System. Over time, increases or decreases in the System's net position is an indicator of whether its financial health is improving or deteriorating. However, you will need to also consider other non-financial factors such as changes in economic conditions, customer growth, and legislative mandates.

The System's total net position increased by \$243 thousand for the fiscal year ended June 30, 2018 and increased \$3 thousand for the fiscal year ended June 30, 2017. The analysis below focuses on the System's net position (Tables 1A and 1B) and changes in net position during the year (Tables 2A and 2B).

## MANAGEMENT DISCUSSION AND ANALYSIS

Table 1A  
CONDENSED STATEMENT OF NET POSITION

	<u>June 30, 2018</u>	<u>June 30, 2017</u>	Increase (Decrease)	
			<u>\$</u>	<u>%</u>
<b>Assets</b>				
Current and other assets	\$ 12,491,055	\$ 11,653,666	\$ 837,389	7.19%
Capital assets	11,217,385	11,480,670	(263,285)	-2.29%
Total assets	<u>23,708,440</u>	<u>23,134,336</u>	<u>574,104</u>	2.48%
<b>Deferred outflows of resources</b>	<u>250,303</u>	<u>341,166</u>	<u>(90,863)</u>	-26.63%
<b>Liabilities</b>				
Long-term liabilities	1,153,360	1,408,785	(255,425)	-18.13%
Other liabilities	4,912,083	4,506,157	405,926	9.01%
Total liabilities	<u>6,065,443</u>	<u>5,914,942</u>	<u>150,501</u>	2.54%
<b>Deferred inflows of resources</b>	<u>205,566</u>	<u>115,808</u>	<u>89,758</u>	77.51%
<b>Net Position</b>				
Net investment in capital assets	10,394,273	10,538,983	(144,710)	-1.37%
Restricted for debt service	314,998	308,329	6,669	2.16%
Unrestricted	6,978,463	6,597,440	381,023	5.78%
<b>Total net position</b>	<b><u>\$ 17,687,734</u></b>	<b><u>\$ 17,444,752</u></b>	<b><u>\$ 242,982</u></b>	<b>1.39%</b>

Table 1B  
CONDENSED STATEMENT OF NET POSITION

	<u>June 30, 2017</u>	<u>June 30, 2016</u>	Increase (Decrease)	
			<u>\$</u>	<u>%</u>
<b>Assets</b>				
Current and other assets	\$ 11,653,666	\$ 11,194,966	\$ 458,700	4.10%
Capital assets	11,480,670	12,014,505	(533,835)	-4.44%
Total assets	<u>23,134,336</u>	<u>23,209,471</u>	<u>(75,135)</u>	-0.32%
<b>Deferred outflows of resources</b>				
Unamortized debt discounts	<u>341,166</u>	<u>362,288</u>	<u>(21,122)</u>	-5.83%
<b>Liabilities</b>				
Long-term liabilities	1,408,785	1,494,538	(85,753)	-5.74%
Other liabilities	4,506,157	4,510,759	(4,602)	-0.10%
Total liabilities	<u>5,914,942</u>	<u>6,005,297</u>	<u>(90,355)</u>	-1.50%
<b>Deferred inflows of resources</b>	<u>115,808</u>	<u>124,383</u>	<u>(8,575)</u>	-6.89%
<b>Net Position</b>				
Net investment in capital assets	10,538,983	10,959,243	(420,260)	-3.83%
Restricted for debt service	308,329	303,350	4,979	1.64%
Unrestricted	6,597,440	6,179,486	417,954	6.76%
<b>Total net position</b>	<b><u>\$ 17,444,752</u></b>	<b><u>\$ 17,442,079</u></b>	<b><u>\$ 2,673</u></b>	<b>0.02%</b>

## MANAGEMENT DISCUSSION AND ANALYSIS

Over the three year period, the decrease in capital assets was primarily due to the depreciation of assets. The increase in current and other assets was due to an increase in cash and cash equivalents on deposit.

Changes in the System's net position can be determined by reviewing the following condensed Statement of Revenues, Expenses, and Changes in Net Position for the years.

Table 2A

<b>CONDENSED STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET POSITION</b>				
	<b>June 30, 2018</b>	<b>June 30, 2017</b>	<b>Increase (Decrease)</b>	
			<b>\$</b>	<b>%</b>
<b>Revenues</b>				
Operating revenues	\$ 20,952,990	\$ 21,282,337	\$ (329,347)	-1.55%
Non-operating revenues	34,486	10,810	23,676	219.02%
Total revenues	20,987,476	21,293,147	(305,671)	-1.44%
<b>Expenses</b>				
Cost of sales and services	17,112,807	17,427,379	(314,572)	-1.81%
Operations expense	1,860,611	1,782,833	77,778	4.36%
Maintenance expense	532,120	810,718	(278,598)	-34.36%
Depreciation and amortization	729,682	731,793	(2,111)	-0.29%
Taxes	97,061	92,540	4,521	4.89%
Interest and other expenses	46,152	52,752	(6,600)	-12.51%
Total expenses	20,378,433	20,898,015	(519,582)	-2.49%
Transfers in (out)	(366,061)	(392,459)	26,398	-6.73%
<b>Change in net position</b>	<b>242,982</b>	<b>2,673</b>	<b>240,309</b>	<b>8990.24%</b>
Beginning net position	17,444,752	17,442,079	2,673	0.02%
Ending net position	<b>\$ 17,687,734</b>	<b>\$ 17,444,752</b>	<b>\$ 242,982</b>	1.39%

## MANAGEMENT DISCUSSION AND ANALYSIS

Table 2B

### CONDENSED STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET POSITION

	<u>June 30, 2017</u>	<u>June 30, 2016</u>	Increase (Decrease)	
			<u>\$</u>	<u>%</u>
<b>Revenues</b>				
Operating revenues	\$ 21,282,337	\$ 20,678,387	\$ 603,950	2.92%
Non-operating revenues	10,810	37,674	(26,864)	-71.31%
Total revenues	<u>21,293,147</u>	<u>20,716,061</u>	<u>577,086</u>	2.79%
<b>Expenses</b>				
Cost of sales and services	17,427,379	16,947,201	480,178	2.83%
Operations expense	1,782,833	1,770,220	12,613	0.71%
Maintenance expense	810,718	471,368	339,350	71.99%
Depreciation and amortization	731,793	718,373	13,420	1.87%
Taxes	92,540	86,564	5,976	6.90%
Interest and other expenses	52,752	59,188	(6,436)	-10.87%
Total expenses	<u>20,898,015</u>	<u>20,052,914</u>	<u>845,101</u>	4.21%
Transfers in (out)	<u>(392,459)</u>	<u>(396,084)</u>	<u>3,625</u>	-0.92%
<b>Change in net position</b>	<u><b>2,673</b></u>	<u><b>267,063</b></u>	<u><b>(264,390)</b></u>	<b>-99.00%</b>
Beginning net position	17,442,079	17,392,371	49,708	0.29%
Restatement of net position, beginning	-	(217,355)	217,355	100.00%
Beginning net position, as restated	<u>17,442,079</u>	<u>17,175,016</u>	<u>267,063</u>	1.55%
Ending net position	<u>\$ 17,444,752</u>	<u>\$ 17,442,079</u>	<u>\$ 2,673</u>	0.02%

Operating revenues showed a 1.55% decrease and a 2.92% increase from 2017 to 2018 and 2016 to 2017. The fluctuations are due primarily to changes in rates and usage. Non-operating revenues increased 219.02% in 2018 and decreased 71.31% in 2017, as the result of fluctuations in amounts invested and their respective interest rates on certificates of deposits and savings accounts. Total expenses decreased 2.49% in 2018 due to a decrease in maintenance expense from utility line maintenance. Total expenses increased 4.21% in 2017 due to an increase in operating expenses in relation to increased line maintenance expense. Although the System increased its rates, it did so in response to TVA's rate increase. TVA's rate increase caused operating expenses, specifically cost of sales and service to increase. Ending net position showed an increase of 1.39% in 2018 and an increase of 0.02% in 2017, due to the above mentioned.

### CAPITAL ASSETS AND DEBT ADMINISTRATION

#### Capital Assets

At the end of fiscal years 2018 and 2017, the system had \$11.22 million (net of accumulated depreciation) and \$11.48 million (net of accumulated depreciation), respectively, invested in a broad range of System capital assets. This investment includes land, land rights, distribution and transmission systems and their related equipment, and various types of equipment. Based on the uses of the aforementioned assets, they are classified for financial purposes as general plant, transmission plant, distribution plant, and construction in progress. This investment represents an overall decrease of 6.63% over the three year period, due to depreciation.

## MANAGEMENT DISCUSSION AND ANALYSIS

The following table summarizes the System's capital assets, net of accumulated depreciation, and changes therein, for the years ended June 30, 2018 and 2017. These changes are presented in detail in Note 3D to the financial statements.

Table 3A

### CAPITAL ASSETS, NET OF ACCUMULATED DEPRECIATION

	June 30, 2018	June 30, 2017	Increase (Decrease)	
			\$	%
General plant	\$ 4,154,201	\$ 4,193,659	\$ (39,458)	-0.94%
Transmission plant	881,085	965,770	(84,685)	-8.77%
Distribution plant	6,018,268	6,189,335	(171,067)	-2.76%
Unamortized acquisition adjustment	100,684	124,848	(24,164)	-19.35%
Construction in progress	63,147	7,058	56,089	794.69%
<b>Total capital assets</b>	<b>\$ 11,217,385</b>	<b>\$ 11,480,670</b>	<b>\$ (263,285)</b>	<b>-2.29%</b>

Table 3B

### CAPITAL ASSETS, NET OF ACCUMULATED DEPRECIATION

	June 30, 2017	June 30, 2016	Increase (Decrease)	
			\$	%
General plant	\$ 4,193,659	\$ 4,399,739	\$ (206,080)	-4.68%
Transmission plant	965,770	1,050,320	(84,550)	-8.05%
Distribution plant	6,189,335	6,336,928	(147,593)	-2.33%
Unamortized acquisition adjustment	124,848	149,012	(24,164)	-16.22%
Construction in progress	7,058	78,506	(71,448)	-91.01%
<b>Total capital assets</b>	<b>\$ 11,480,670</b>	<b>\$ 12,014,505</b>	<b>\$ (533,835)</b>	<b>-4.44%</b>

### Debt Administration

The System has outstanding Revenue Bonds of \$830 thousand as of June 30, 2018 and \$950 thousand as of June 30, 2017. Principal payments are due in the upcoming fiscal year in the amount of \$125,000 with interest payments totaling \$32,648 also due. Details relating to the outstanding debt can be found in Note 3G. The System also has no current plans to issue new debt or refund outstanding debt.

### ECONOMIC FACTORS AND NEXT YEAR'S BUDGET AND RATES

The System's electric supplier is also expected to increase rates in the next fiscal year, and this will cause the System to have to pass on the additional costs to customers. The City is actively recruiting new industries to the area to make up for past plant closures. Any new industry that comes to the area will increase the System's power sales and should help the overall financial condition of the System.

### CONTACTING THE SYSTEM'S FINANCIAL MANAGEMENT

This financial report is designed to provide a general overview of the System's finances for all those with an interest in the System's finances and to demonstrate the System's accountability for the money it receives. Questions concerning any information provided in this report or requests for any additional information should be directed to the General Manager of the Covington Electric System, P.O. Box 488, Covington, TN, 38019.

**COVINGTON ELECTRIC SYSTEM  
STATEMENTS OF NET POSITION**

June 30, 2018 and 2017

	<b>2018</b>	<b>2017</b>
<b>Assets</b>		
<b>Current assets:</b>		
Cash on hand	\$ 2,150	\$ 2,150
Cash and cash equivalents on deposit	9,629,643	8,806,063
Accounts receivable	2,081,082	2,066,874
Due from other funds - municipality	384	665
Inventories	224,678	246,232
Prepayments and other current assets	188,668	168,666
Total current assets	12,126,605	11,290,650
<b>Noncurrent assets:</b>		
Restricted cash, cash equivalents, and investments:		
Cash and cash equivalents on deposit	323,785	318,286
Customer's CD's held for deposit	20,655	20,647
Total restricted assets	344,440	338,933
Other assets:		
Investments in associated companies	6,165	4,815
Unamortized debt expense	11,694	14,114
Advances to customers - Home insulation	2,151	5,154
Total other assets	20,010	24,083
Capital assets:		
Not being depreciated		
General plant	195,885	195,885
Transmission plant	8,267	8,267
Distribution plant	16,560	16,560
Construction in progress	63,147	7,058
Being depreciated		
General plant	6,636,755	6,504,609
Transmission plant	2,161,810	2,161,810
Distribution plant	12,792,200	12,616,681
Less: Accumulated depreciation	(10,757,923)	(10,155,048)
Unamortized acquisition adjustment	100,684	124,848
Total capital assets (net of accumulated depreciation)	11,217,385	11,480,670
Total noncurrent assets	11,581,835	11,843,686
<b>Total assets</b>	<b>23,708,440</b>	<b>23,134,336</b>
<b>Deferred outflows of resources:</b>		
Pension contributions subsequent to the measurement date	132,956	146,866
Net difference between expected and actual experience	96,370	102,795
Net difference between projected and actual earnings in pension investments	20,977	91,505
<b>Total deferred outflows of resources</b>	<b>\$ 250,303</b>	<b>\$ 341,166</b>

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

**COVINGTON ELECTRIC SYSTEM  
STATEMENTS OF NET POSITION**

June 30, 2018 and 2017

	<u>2018</u>	<u>2017</u>
<b>Liabilities</b>		
<b>Current liabilities:</b>		
Accounts payable	\$ 3,419,588	\$ 3,066,537
Customer deposits	1,250,103	1,192,437
Compensated absences - current portion	10,027	9,978
Accrued expenses and other liabilities	<u>77,923</u>	<u>86,601</u>
Total current liabilities	<u>4,757,641</u>	<u>4,355,553</u>
<b>Current liabilities payable from restricted assets:</b>		
Accrued interest payable	8,787	9,957
Consumer's deposits	20,655	20,647
Current maturities of long-term debt	<u>125,000</u>	<u>120,000</u>
Total current liabilities payable from restricted assets	<u>154,442</u>	<u>150,604</u>
<b>Noncurrent liabilities:</b>		
Advances - Home insulation program	2,419	5,422
Compensated absences	90,242	89,802
Net pension liability	362,587	491,874
Bonds payable (less current maturities)	<u>698,112</u>	<u>821,687</u>
Total noncurrent liabilities	<u>1,153,360</u>	<u>1,408,785</u>
<b>Total liabilities</b>	<u><b>6,065,443</b></u>	<u><b>5,914,942</b></u>
<b>Deferred inflows of resources</b>		
Net difference between expected and actual experience-pension	<u><b>205,566</b></u>	<u><b>115,808</b></u>
<b>Net Position</b>		
Net investment in capital assets	10,394,273	10,538,983
Restricted for debt service	314,998	308,329
Unrestricted	<u>6,978,463</u>	<u>6,597,440</u>
<b>Total net position</b>	<u><b>\$ 17,687,734</b></u>	<u><b>\$ 17,444,752</b></u>

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

**COVINGTON ELECTRIC SYSTEM**  
**STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN NET POSITION**  
For the Years Ended June 30, 2018 and 2017

	<b>2018</b>	<b>2017</b>
<b>Operating revenues:</b>		
Charges for sales and services	\$ 20,655,623	\$ 20,979,406
Other revenue	297,367	302,931
Total operating revenues	20,952,990	21,282,337
<b>Operating expenses:</b>		
Cost of sales and services	17,112,807	17,427,379
Operations expense	1,860,611	1,782,833
Maintenance expense	532,120	810,718
Depreciation	729,682	731,793
Payroll taxes	97,061	92,540
Total operating expenses	20,332,281	20,845,263
Operating income (loss)	620,709	437,074
<b>Nonoperating revenues (expenses):</b>		
Interest and other revenue	34,486	10,810
Other expenses	(9,833)	(11,809)
Interest	(36,319)	(40,943)
Total nonoperating revenues (expenses)	(11,666)	(41,942)
Change in net position before transfers	609,043	395,132
Transfers in (out) - City - in lieu of taxes	(366,061)	(392,459)
<b>Change in net position</b>	<b>242,982</b>	<b>2,673</b>
Total net position - beginning	17,444,752	17,442,079
Total net position - ending	<b>\$ 17,687,734</b>	<b>\$ 17,444,752</b>

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

**COVINGTON ELECTRIC SYSTEM**  
**STATEMENTS OF CASH FLOWS**  
For the Years Ended June 30, 2018 and 2017

	<u>2018</u>	<u>2017</u>
<b>Cash flows from operating activities:</b>		
Cash received from consumers	\$ 20,938,782	\$ 21,451,072
Cash paid to suppliers and employees	(19,106,083)	(19,920,672)
Taxes paid including payments in lieu of taxes	(97,061)	(92,540)
Transfers to the City - payment in lieu of taxes	(366,061)	(392,459)
Customer deposits received	365,890	271,588
Customer deposits refunded	(308,225)	(343,523)
Net cash provided (used) by operating activities	<u>1,427,242</u>	<u>973,466</u>
<b>Cash flows from non-capital and related financing activities:</b>		
Increase (decrease) in advances from TVA	<u>(3,003)</u>	<u>(2,821)</u>
Net cash provided (used) by non-capital and related financing activities	<u>(3,003)</u>	<u>(2,821)</u>
<b>Cash flows from capital and related financing activities:</b>		
Principal paid on debt	(120,000)	(115,000)
Interest paid on bonds, notes and leases	(37,489)	(42,057)
Construction and acquisition of plant	(507,880)	(449,307)
Disposal of plant	58,422	281,864
Plant removal cost	(34,721)	(48,297)
Materials salvaged from retirements	<u>20,202</u>	<u>20,202</u>
Net cash provided (used) by capital and related financing activities	<u>(621,466)</u>	<u>(352,595)</u>
<b>Cash flows from investing activities:</b>		
Interest earned	34,486	10,810
Cash paid for other nonoperating expenses	(9,833)	(11,809)
(Increase) decrease in investments in associated companies	(1,350)	(1,440)
(Increase) decrease in conservation loans	<u>3,003</u>	<u>2,821</u>
Net cash provided (used) by investing activities	<u>26,306</u>	<u>382</u>
<b>Net increase (decrease) in cash and cash equivalents</b>	<b>829,079</b>	<b>618,432</b>
Cash and cash equivalents - beginning of year	<u>9,126,499</u>	<u>8,508,067</u>
Cash and cash equivalents - end of year	<u>\$ 9,955,578</u>	<u>\$ 9,126,499</u>
Cash and cash equivalents		
Unrestricted cash on hand	\$ 2,150	\$ 2,150
Unrestricted cash and cash equivalents on deposit	9,629,643	8,806,063
Restricted cash and cash equivalents on deposit	<u>323,785</u>	<u>318,286</u>
Total cash and cash equivalents	<u>\$ 9,955,578</u>	<u>\$ 9,126,499</u>

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

**COVINGTON ELECTRIC SYSTEM**  
**STATEMENTS OF CASH FLOWS**  
For the Years Ended June 30, 2018 and 2017

	<b>2018</b>	<b>2017</b>
Reconciliation of operating income (loss) to net cash provided (used) by operating activities:		
Operating income (loss)	\$ 620,709	\$ 437,074
Adjustments to reconcile operating income (loss) to net cash provided (used) by operating activities:		
Depreciation	729,682	731,793
Amortization of bond discount	1,425	1,425
Pension contributions in excess of actuarially determined pension expense	51,334	39,841
Operating transfer in (out)	(366,061)	(392,459)
Changes in operation assets and liabilities:		
Accounts and other receivable	(14,208)	168,735
Inventories	21,554	(15,581)
Prepayments and other current assets	(19,521)	12,512
Due from other funds	281	(458)
Accounts payable and accrued expenses	344,373	(81,351)
Customer deposits	57,674	71,935
Net cash provided (used) by operating activities	\$ 1,427,242	\$ 973,466

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

**COVINGTON ELECTRIC SYSTEM**  
**STATEMENTS OF FIDUCIARY NET POSITION - DEFINED BENEFIT PLAN**  
 March 31, 2018 and 2017

Assets	2018	2017
Cash and cash equivalents	\$ 95,714	\$ 4,879
Investments		
Equity	857,061	1,219,919
Balanced	667,167	76,799
Fixed	1,039,068	1,497,013
International	762,197	376,391
Total investments	3,325,493	3,170,122
Net position available for benefits	3,421,207	3,175,001
Liabilities	-	-
<b>Net position restricted for pensions</b>	<b>\$ 3,421,207</b>	<b>\$ 3,175,001</b>

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

**COVINGTON ELECTRIC SYSTEM**  
**STATEMENTS OF CHANGES IN FIDUCIARY NET POSITION - DEFINED BENEFIT PLAN**  
 March 31, 2018 and 2017

Additions	2018	2017
Contributions		
Employer	\$ 146,866	\$ 135,141
Investment income		
Interest income	-	396
Dividend income	60,074	67,178
Realized losses	4,300	87,715
Investment rebates	-	489
Net appreciation in fair value of investments	182,317	129,771
Total investment income	246,691	285,549
Total additions	393,557	420,690
Deductions		
Benefit payments	119,767	117,249
Administrative expenses	27,584	28,884
Total deductions	147,351	146,133
<b>Net change in fiduciary net position</b>	<b>246,206</b>	<b>274,557</b>
<b>Net position restricted for pensions</b>		
Beginning of year	3,175,001	2,900,444
End of year	\$ 3,421,207	\$ 3,175,001

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

**COVINGTON ELECTRIC SYSTEM**  
**STATEMENTS OF FIDUCIARY NET POSITION - 457 PLAN**  
June 30, 2018 and 2017

Assets	2018	2017
Investments		
Equity	\$ 511	\$ 432
Balanced	235,288	196,068
Fixed	225,595	219,087
International	11,796	9,611
Total investments	473,190	425,198
Net position available for benefits	473,190	425,198
Liabilities	-	-
<b>Net position restricted for pensions</b>	<b>\$ 473,190</b>	<b>\$ 425,198</b>

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

**COVINGTON ELECTRIC SYSTEM**  
**STATEMENTS OF CHANGES IN FIDUCIARY NET POSITION - 457 PLAN**  
For the Years Ended June 30, 2018 and 2017

Additions	2018	2017
Contributions		
Employer	\$ 40,928	\$ 29,720
Investment income		
Dividend income	-	279
Net appreciation in fair value of investments	18,364	27,872
Total investment income	18,364	57,871
Total additions	59,292	57,871
Deductions		
Benefit payments	11,300	1,573
Total deductions	11,300	1,573
<b>Net change in fiduciary net position</b>	<b>47,992</b>	<b>56,298</b>
<b>Net position restricted for pensions</b>		
Beginning of year	425,198	368,900
End of year	\$ 473,190	\$ 425,198

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

**COVINGTON ELECTRIC SYSTEM**  
**NOTES TO FINANCIAL STATEMENTS**  
June 30, 2018 and 2017

**NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**A. Reporting Entity**

The financial statements provide information about the government's funds; including its fiduciary funds and include only the financial activities of the Covington Electric System, Covington, Tennessee (the System). Separate statements for each fund category (enterprise and fiduciary) are presented. The oversight unit consists of the funds maintained by the Office of the City Recorder of the City of Covington, Tennessee (the City). The System is under the regulatory authority of the Tennessee Valley Authority.

**B. Measurement Focus, Basis of Accounting, and Financial Statement Presentation**

The accounting and financial reporting treatment is determined by the applicable measurement focus and basis of accounting. Measurement focus indicates the type of resources being measured such as current financial resources or economic resources. The basis of accounting indicates the timing of transactions or events for recognition in the financial statements.

The System's enterprise and pension funds are reported using the economic resources measurement focus and the full accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. The accounting policies of the System conform to applicable accounting principles generally accepted in the United States of America as defined in by the *Governmental Accounting Standards Board (GASB)*.

The enterprise fund distinguishes operating revenues and expense from non-operating items. Operating revenues and expenses generally result from providing services and delivering goods in connection with the enterprise fund's principal ongoing operations. The principal operating revenues of the System are charges for sales to customers for sales and service. Operating expenses for the enterprise funds include the cost of sales and services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

Additionally, the government reports the following fiduciary funds:

The deferred compensation trust fund is used to account for assets held for employees in accordance with the provisions of Internal Revenue Service Code Section 457.

The defined benefit pension plan which accumulates the resources for pension benefit payments to qualified public safety employees. The pension trust fund reports on a March 31 year end.

**C. Assets, Liabilities, and Net Position**

**Deposits and Investments**

The System's cash and cash equivalents are considered to be cash on hand, demand deposits, and short-term investments with original maturities of three months or less from the date of acquisition.

**COVINGTON ELECTRIC SYSTEM**  
**NOTES TO FINANCIAL STATEMENTS**  
June 30, 2018 and 2017

State statutes authorize the System to invest in certificates of deposit, obligations of the U. S. Treasury, agencies, instrumentalities, and obligations guaranteed as to principal and interest by the United States or any of its agencies, repurchase agreements, and the Tennessee local government investment pool.

**Investments in Pension Plan**

*Investment policy:* The pension plan's policy in regard to the allocation of invested assets is established and may be amended by the Board of Directors by a majority vote of its members. It is the policy of the Board of Directors to pursue an investment strategy that reduces risk through the prudent diversification of the portfolio across a broad selection of distinct asset classes.

Investments are stated at fair market value. The Plan's investments consist of stocks in U.S. and foreign publically traded companies and mutual funds. Dividend income is accrued on the ex-dividend date. Purchases and sales of securities are recorded on the trade-date basis. Realized gains and losses from security transactions are reported on the average cost method.

**Receivables and Payables**

During the course of operations, numerous transactions occur between individual funds for goods provided or services rendered. These receivables and payables are classified as "due from other funds" or "due to other funds" on the Statement of Net Position.

Trade receivables result from unpaid billings for service to customers and from unpaid billings related to work performed for or materials sold to certain entities. All trade receivables are shown at their estimated realizable amount, which does not include an allowance for uncollectible accounts. The System did not record an allowance for uncollectible customer accounts based on the past history of uncollectible accounts and management's analysis of the current accounts.

**Inventories and Prepaid Items**

All inventories are valued at the lower of average cost or market, using the first-in/first-out (FIFO) method. Certain payments to vendors reflect costs applicable to future accounting periods and are recorded as prepaid items in the financial statements.

**Restricted Assets**

Certain proceeds of the bond issues, as well as certain resources set aside for their repayment, are classified as restricted assets on the statement of net position because they are maintained in separate bank accounts and their use is limited by applicable bond covenants. The System elects to use restricted assets before unrestricted assets when the situation arises where either can be used.

**Capital Assets**

Capital assets, which include property, plant, equipment, and construction in progress, are recorded at historical cost or estimated historical cost if purchased or constructed. Capital assets are defined by the system as assets with an initial undivided cost of more than \$500 and an estimated useful life of at least 5 years. Assets acquired through contributions from developers or other customers are capitalized at their estimated fair market value at the date of donation.

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

**COVINGTON ELECTRIC SYSTEM**  
**NOTES TO FINANCIAL STATEMENTS**  
June 30, 2018 and 2017

capitalized as projects are constructed. Interest incurred during the construction phase of capital assets is included as part of the capitalized value of the assets constructed.

Property, plant, and equipment of the System are depreciated using the straight line method over the following useful lives:

General plant	5 - 50 years
Transmission plant	25 - 33.33 years
Distribution plant	16.66 - 36.36 years

**Compensated Absences**

It is the System's policy to permit employees to accumulate earned but unused vacation benefits. All vacation pay has been accrued and is reflected by current and noncurrent liabilities on the financial statements.

**Long-term Obligations**

Bond premiums and discounts, as well as issuance costs, are deferred and amortized over the life of the bonds using the effective interest method. Bonds payable are reported net of the applicable bond premium or discount. The Utility will continue to report bond cost as an asset and amortize those over the life of the bonds instead of expensing those costs in the current year in accordance with certain provisions included in GASB Statement No. 62 – *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*. This regulatory option as part of GASB Statement No. 65 is available due to the above mentioned cost being used for rate setting by the utility.

**Deferred Outflows/Inflows of Resources**

In addition to assets, the statement of net position will sometimes report a separate section for deferred outflows of resources. This separate financial statement element, deferred outflows of resources, represents a consumption of net position that applies to a future period and so will not be recognized as an outflow of resources (expense/expenditure) until then. The System currently has three items that qualify for reporting in this category: Pension contributions subsequent to the measurement date, net difference between expected and actual experience, and pension net difference between projected and actual earnings in pension investments.

In addition to liabilities, the statement of financial position will sometimes report a separate section for deferred inflows of resources. This separate financial statement element, deferred inflows of resources, represents acquisition of net position that applies to a future period and so will not be recognized as an inflow of resources (revenue) until that time. The System has one item that qualifies for reporting in this category as of June 30, 2018, the pension difference between expected and actual experience.

**Net Position Flow Assumption**

Sometimes the System will fund outlays for a particular purpose from both restricted (e.g., restricted bond or grant proceeds) and unrestricted resources. In order to calculate the amounts to report as restricted – net position and unrestricted – net position in the financial statements, a flow assumption must be made about the order in which the resources are considered to be applied. It is the System policy to consider restricted – net position to have been depleted before unrestricted – net position is applied.

**COVINGTON ELECTRIC SYSTEM**  
**NOTES TO FINANCIAL STATEMENTS**  
June 30, 2018 and 2017

**Net Position**

Equity is classified as net position and displayed in the following three components:

- Net Investment in Capital Assets - Consists of capital assets, net of accumulated depreciation and reduced by the outstanding balances of any bonds that are attributable to the acquisition, construction, or improvement of those assets; debt related to unspent proceeds or other restricted cash and investments is excluded from the determination.
- Restricted for Debt Service – Consists of net position for which constraints are placed thereon by external parties, such as lenders, grantors, contributors, laws, regulations, and enabling legislation, including self-imposed legal mandates, less any related liabilities.
- Unrestricted – All other net position that does not meet the description of the above categories.

**Pensions**

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 Covington Electric System's participation in Covington Electric System's Employees' Retirement Plan, and additions to/deductions from Covington Electric System's fiduciary net position have been determined on the same basis as they are reported by Covington Electric System's Employees' Retirement Plan. For this purpose, benefits (including refunds of employee contributions) are recognized when due and payable in accordance with the benefit terms of Covington Electric System's Employees' Retirement Plan. Investments are reported at fair value.

*Payment of Benefits:* Benefits are recorded when the participant has met all of the Plan requirements to receive a benefit. At March 31, 2018 no benefits were payable and not paid.

*Administrative and Other Expenses:* Qualified Plan administrative expenses are paid by the Plan. During the years ended March 31, 2018 and 2017 administrative and other expenses paid were \$27,583 and \$28,884.

**NOTE 2 - STEWARDSHIP, COMPLIANCE, AND ACCOUNTABILITY**

**A. Budgetary Information**

The System adopts flexible annual operating and capital budgets. Budgets are adopted on a basis consistent with generally accepted accounting principles. The current operating budget details the System's plans to earn and expend funds for charges incurred for operation, maintenance, certain interest, and general functions and other charges for the fiscal year. The capital budget details the plan to receive and expend cash basis capital contribution fees, special assessments, grants, borrowings, and certain revenues for capital projects.

All unexpended appropriations in the operating budget remaining at the end of the fiscal year lapse.

Management submits a proposed budget to the System's Board. A budget is then adopted for the next fiscal year. During the year, management is authorized to transfer budgeted amounts between line items.

**COVINGTON ELECTRIC SYSTEM**  
**NOTES TO FINANCIAL STATEMENTS**  
June 30, 2018 and 2017

**NOTE 3 - DETAILED NOTES ON ALL FUNDS**

**A. Deposits and Investments**

**Electric**

Deposits and investments: At June 30, 2018, the System had cash on hand of \$2,150 and deposits with a carrying amount of \$9,953,428 and a bank balance of \$9,953,968, as compared to June 30, 2017, at which the System had cash on hand of \$2,150 and deposits with a carrying amount of \$9,124,349 and a bank balance of \$9,123,495. Of the bank balances, \$250,000 was covered by federal depository insurance, with the remaining covered by the State Collateral Pool. Investments were made up of consumer's certificates of deposits held for customer deposits totaling \$20,655 for 2018 and \$20,647 for 2017 and investment in associated companies of \$6,165 for 2018 and \$4,815 for 2017.

Custodial Credit Risk: The System's policies limit deposits and investments to those instruments allowed by applicable state laws and described in Note 1. State statute requires that all deposits with financial institutions must be collateralized by securities whose market value is equal to 105% of the value of uninsured deposits. The deposits must be collateralized by federal depository insurance or the Tennessee Bank Collateral Pool, by collateral held by the System's agent in the System's name, or by the Federal Reserve Banks acting as third party agents. State statutes also authorize the System to invest in bonds, notes, or treasury bills of the United States or any of its agencies, certificates of deposit at Tennessee state chartered banks and savings and loan associations, and federally chartered banks and savings and loan associations, or repurchase agreements utilizing obligations of the United States or its agencies, as the underlying repurchase agreements must have a market value of at least equal to the amount of funds invested in the repurchase transaction. As of June 30, 2018 and 2017, all bank deposits were fully collateralized or insured.

**Pension Plan**

The following are the asset allocations as of March 31, 2018 and 2017:

	2018		2017	
	Market Value	Percentage of Total	Market Value	Percentage of Total
Equities	\$ 857,061	25.77%	\$ 1,219,919	38.48%
Balanced	667,167	20.06%	76,799	2.42%
Fixed income	1,039,068	31.25%	1,497,013	47.22%
International	762,197	22.92%	376,391	11.87%
Total	\$ 3,325,493	100.00%	\$ 3,170,122	100.00%

The following investments represent more than 5% of the fiduciary net position and are not issued or explicitly guaranteed by the U.S. government at March 31, 2018 and 2017:

**COVINGTON ELECTRIC SYSTEM**  
**NOTES TO FINANCIAL STATEMENTS**  
June 30, 2018 and 2017

	2018	2017
iShares Core S&P 500 ETF	\$ 317,383	\$ -
Advisers Inv't TR Johcm Intl SI I	174,915	-
Baron Emerging Markets Funds	185,424	-

For the years ended March 31, 2018 and 2017, the annual money-weighted rate of return on pension plan investments, net of pension plan investment expense, was 6.70 and 8.70 percent. The money-weighted rate of return expresses investment performance, net of investment expense, adjusted for the changing amounts actually invested.

*Fair Value Measurements:* The Plan categorizes its fair value measurements within the fair value hierarchy established by generally accepted accounting principles. The Plan has the following recurring fair value measurements as of March 31, 2018:

	Fair Value Measurements Using			
	Quoted Prices in			
		Active Markets for	Significant Other	Significant
	Total	Identical Assets	Observable Inputs	Unobservable Inputs
	(Level 1)	(Level 2)	(Level 3)	
Investments by fair value level				
Equity securities				
Mutual funds	\$ 1,504,196	\$ 1,504,196	\$ -	\$ -
Common stocks	1,821,297	1,821,297	-	-
total equity securities	\$ 3,325,493	\$ 3,325,493	\$ -	\$ -

The Plan has the following recurring fair value measurements as of March 31, 2017:

	Fair Value Measurements Using			
	Quoted Prices in			
		Active Markets for	Significant Other	Significant
	Total	Identical Assets	Observable Inputs	Unobservable Inputs
	(Level 1)	(Level 2)	(Level 3)	
Investments by fair value level				
Equity securities				
Mutual funds	\$ 2,406,901	\$ 2,406,901	\$ -	\$ -
Common stocks	763,221	763,221	-	-
total equity securities	\$ 3,170,122	\$ 3,170,122	\$ -	\$ -

Debt and equity securities classified in Level 1 of the fair value hierarchy are valued using prices quoted in active markets for those securities.

**Deferred Compensation Plan (457 Plan)**

The following are the asset allocations as of June 30, 2018 and 2017:

**COVINGTON ELECTRIC SYSTEM**  
**NOTES TO FINANCIAL STATEMENTS**  
June 30, 2018 and 2017

	2018		2017	
	Market Value	Percentage of Total	Market Value	Percentage of Total
Equities	\$ 511	0.11%	\$ 432	0.10%
Balanced	235,288	49.72%	196,068	46.11%
Fixed income	225,595	47.68%	219,087	51.53%
International	11,796	2.49%	9,611	2.26%
Total	<u>\$ 473,190</u>	100.00%	<u>\$ 425,198</u>	100.00%

The following investments represent more than 5% of the fiduciary net position and are not issued or explicitly guaranteed by the U.S. government at June 30, 2018 and 2017:

	2018	2017
VOYA Growth and Income Portfolio	\$ 39,661	\$ 36,247
Amer Cent One Choice 2045 Portfolio	71,240	55,086
VOYA Intermediate Bond Portfolio 1	43,436	36,788
VOYA Fixed Account	225,187	217,008

For the years ended June 30, 2018 and 2017, the annual money-weighted rate of return on plan investments, net of plan investment expense, was 11.29 and 7.12 percent. The money-weighted rate of return expresses investment performance, net of investment expense, adjusted for the changing amounts actually invested.

*Fair Value Measurements:* The Plan categorizes its fair value measurements within the fair value hierarchy established by generally accepted accounting principles. The Plan has the following recurring fair value measurements as of June 30, 2018:

	Fair Value Measurements Using			
	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Investments by fair value level				
Equity securities				
Mutual funds	\$ 226,106	\$ 226,106	\$ -	\$ -
Common stocks	247,084	247,084	-	-
total equity securities	<u>\$ 473,190</u>	<u>\$ 473,190</u>	<u>\$ -</u>	<u>\$ -</u>

The Plan has the following recurring fair value measurements as of June 30, 2017:

**COVINGTON ELECTRIC SYSTEM**  
**NOTES TO FINANCIAL STATEMENTS**  
June 30, 2018 and 2017

	Fair Value Measurements Using			
	Total	Quoted Prices in		
		Active Markets for	Significant Other	Significant
		Identical Assets	Observable Inputs	Unobservable Inputs
	(Level 1)	(Level 2)	(Level 3)	
Investments by fair value level				
Equity securities				
Mutual funds	\$ 219,519	\$ 219,519	\$ -	\$ -
Common stocks	205,679	205,679	-	-
total equity securities	\$ 425,198	\$ 425,198	\$ -	\$ -

Debt and equity securities classified in Level 1 of the fair value hierarchy are valued using prices quoted in active markets for those securities.

**B. Receivables**

Receivables as of the fiscal years ended were made up of the following:

	June 30,	
	2018	2017
Billed services for utility customers	\$ 2,081,082	\$ 2,066,874
Less: Allowance for uncollectibles	-	-
Total	\$ 2,081,082	\$ 2,066,874

**C. Restricted Assets**

The following amounts represent only the accounts with restrictions associated with use of the funds. The funding applicable to the bonds issued is in compliance with the funding requirements.

	June 30,	
	2018	2017
Sinking funds	\$ 106,294	\$ 103,592
Reserve funds	217,491	214,694
Certificates of deposit	20,655	20,647
Total	\$ 344,440	\$ 338,933

**D. Capital Assets**

Capital asset activity during the fiscal years ended was as follows:

**COVINGTON ELECTRIC SYSTEM**  
**NOTES TO FINANCIAL STATEMENTS**  
June 30, 2018 and 2017

Description	Balance at June 30, 2017	Additions	Disposals	Reclassifications	Balance at June 30, 2018
Capital assets, not being depreciated					
General plant	\$ 195,885	\$ -	\$ -	\$ -	\$ 195,885
Transmission plant	8,267	-	-	-	8,267
Distribution plant	16,560	-	-	-	16,560
Construction in progress	7,058	56,089	-	-	63,147
Total capital assets not being depreciated	<u>227,770</u>	<u>56,089</u>	<u>-</u>	<u>-</u>	<u>283,859</u>
Capital assets, being depreciated					
General plant	6,504,609	172,671	40,525	-	6,636,755
Transmission plant	2,161,810	-	-	-	2,161,810
Distribution plant	12,616,681	233,939	58,420	-	12,792,200
Total capital assets being depreciated	<u>21,283,100</u>	<u>406,610</u>	<u>98,945</u>	<u>-</u>	<u>21,590,765</u>
Less accumulated depreciation for:					
General plant	2,506,835	211,629	40,025	-	2,678,439
Transmission plant	1,204,307	84,685	-	-	1,288,992
Distribution plant	6,443,906	433,368	86,782	-	6,790,492
Total accumulated depreciation	<u>10,155,048</u>	<u>729,682</u>	<u>126,807</u>	<u>-</u>	<u>10,757,923</u>
Total capital assets, being depreciated, net	<u>11,128,052</u>	<u>(323,072)</u>	<u>(27,862)</u>	<u>-</u>	<u>10,832,842</u>
Unamortized acquisition adjustment	<u>124,848</u>	<u>-</u>	<u>24,164</u>	<u>-</u>	<u>100,684</u>
Total capital assets, net	<u>\$ 11,480,670</u>	<u>\$ (266,983)</u>	<u>\$ (3,698)</u>	<u>\$ -</u>	<u>\$ 11,217,385</u>

Depreciation expense amounted to \$729,682 (additional \$30,119 charged to transportation clearing) for the fiscal year ended June 30, 2018.

**COVINGTON ELECTRIC SYSTEM**  
**NOTES TO FINANCIAL STATEMENTS**  
June 30, 2018 and 2017

Description	Balance at June 30, 2016	Additions	Disposals	Reclassifications	Balance at June 30, 2017
<b>Capital assets, not being depreciated</b>					
General plant	\$ 195,885	\$ -	\$ -	\$ -	\$ 195,885
Transmission plant	8,267	-	-	-	8,267
Distribution plant	16,560	-	-	-	16,560
Construction in progress	78,506	-	71,448	-	7,058
Total capital assets not being depreciated	<u>299,218</u>	<u>-</u>	<u>71,448</u>	<u>-</u>	<u>227,770</u>
<b>Capital assets, being depreciated</b>					
General plant	6,495,010	9,599	-	-	6,504,609
Transmission plant	2,161,810	-	-	-	2,161,810
Distribution plant	12,642,667	255,878	281,864	-	12,616,681
Total capital assets being depreciated	<u>21,299,487</u>	<u>265,477</u>	<u>281,864</u>	<u>-</u>	<u>21,283,100</u>
<b>Less accumulated depreciation for:</b>					
General plant	2,291,156	215,679	-	-	2,506,835
Transmission plant	1,119,757	84,550	-	-	1,204,307
Distribution plant	6,322,299	431,564	309,957	-	6,443,906
Total accumulated depreciation	<u>9,733,212</u>	<u>731,793</u>	<u>309,957</u>	<u>-</u>	<u>10,155,048</u>
Total capital assets, being depreciated, net	<u>11,566,275</u>	<u>(466,316)</u>	<u>(28,093)</u>	<u>-</u>	<u>11,128,052</u>
Unamortized acquisition adjustment	<u>149,012</u>	<u>-</u>	<u>24,164</u>	<u>-</u>	<u>124,848</u>
Total capital assets, net	<u>\$ 12,014,505</u>	<u>\$ (466,316)</u>	<u>\$ 67,519</u>	<u>\$ -</u>	<u>\$ 11,480,670</u>

Depreciation expense amounted to \$731,793 (additional \$29,606 charged to transportation clearing) for the fiscal year ended June 30, 2017.

**E. Interfund Receivables, Payables, and Transfers**

The composition of interfund balances as of June 30, 2018 is as follows:

	Due from City		City - Transfer In
Due to Electric	\$ 384	Transfer out	\$ 366,061

The composition of interfund balances as of June 30, 2017 is as follows:

	Due from City		City
Due to Electric	\$ 665	Transfer out	\$ 392,459

For both fiscal years end, the interfund receivables to Electric from the City are for unpaid invoices.

The transfer from the Electric System to the City is for property taxes for fiscal years 2018 and 2017.

**COVINGTON ELECTRIC SYSTEM**  
**NOTES TO FINANCIAL STATEMENTS**  
June 30, 2018 and 2017

**F. Leases**

**Operating Leases**

The System leases its copy machine usage. This lease has been classified as an operating lease for reporting purposes. The System makes a monthly payment that is dependent upon the number of copies used.

Lease expense for the years ended June 30, 2018 and 2017 was \$618 and \$342, respectively.

**G. Long-term Debt**

**Revenue and Tax Bonds**

On April 1, 2003, the System issued \$2,280,000 in Electric System Revenue Bonds, Series 2003 with interest of 2.50% to 4.375% to provide funds to finance the construction of improvements and expansion of the City's electrical power distribution system. The bonds are to be repaid solely from and be secured by a pledge of the net revenues to be derived from the operation of the system.

	June 30,	
	2018	2017
Bonds payable are as follows:		
Electric System Revenue Bonds, Series 2003, 2.50% to 4.375%, due serially through 2024 (net of discount)	\$ 830,000	\$ 950,000
Less bond discounts	6,888	8,313
Less current portion bonds payable	125,000	120,000
Total long-term portion bonds payable	\$ 698,112	\$ 821,687

The annual requirements to amortize all debt outstanding at June 30, 2018, including interest of \$127,886 are as follows:

Year ending June 30	Revenue and Tax Bonds	
	Principal	Interest
2019	125,000	32,648
2020	130,000	27,483
2021	135,000	22,034
2022	140,000	16,188
2023	145,000	16,188
2024	155,000	13,345
	830,000	127,886

**COVINGTON ELECTRIC SYSTEM**  
**NOTES TO FINANCIAL STATEMENTS**  
June 30, 2018 and 2017

The following is a summary of long-term debt transactions for the year ended June 30, 2018.

	Balance at June 30, 2017	Additions	Retirements	Balance at June 30, 2018	Due within one year
Electric System					
Revenue and tax bonds payable	\$ 950,000	\$ -	\$ 120,000	\$ 830,000	\$ (125,000)
Compensated absences	99,780	489	-	100,269	10,027
Bond discounts	(8,313)	-	(1,425)	(6,888)	(1,425)
Total debt outstanding	<u>\$ 1,041,467</u>	<u>\$ 489</u>	<u>\$ 118,575</u>	<u>\$ 923,381</u>	<u>\$ (116,398)</u>

The following is a summary of long-term debt transactions for the year ended June 30, 2017.

	Balance at June 30, 2016	Additions	Retirements	Balance at June 30, 2017	Due within one year
Electric System					
Revenue and tax bonds payable	\$ 1,065,000	\$ -	\$ 115,000	\$ 950,000	\$ (120,000)
Compensated absences	90,503	9,277	-	99,780	9,978
Bond discounts	(9,738)	-	(1,425)	(8,313)	(1,425)
Total debt outstanding	<u>\$ 1,145,765</u>	<u>\$ 9,277</u>	<u>\$ 113,575</u>	<u>\$ 1,041,467</u>	<u>\$ (111,447)</u>

#### H. Net Position

Net position represents the difference between assets and liabilities and deferred outflows/inflows of resources. The restricted net position amounts were as follows:

	June 30,	
	2018	2017
Net investment in capital assets		
Net property, plant, and equipment in services	\$ 11,217,385	\$ 11,480,670
Unamortized debt discount	6,888	8,313
Less: Debt as disclosed in Note 3G	(830,000)	(950,000)
Total invested in capital assets	<u>10,394,273</u>	<u>10,538,983</u>
Restricted for debt service:		
Restricted cash and cash equivalents	323,785	318,286
Restricted investments	20,655	20,647
Less: Current liabilities payable from restricted assets	(29,442)	(30,604)
Total restricted for debt service	<u>314,998</u>	<u>308,329</u>
Unrestricted	<u>6,978,463</u>	<u>6,597,440</u>
Total net position	<u>\$ 17,687,734</u>	<u>\$ 17,444,752</u>

**COVINGTON ELECTRIC SYSTEM**  
**NOTES TO FINANCIAL STATEMENTS**  
June 30, 2018 and 2017

**NOTE 4 - OTHER INFORMATION**

**A. Pension Plan**

*Plan Description:* The Retirement Plan Committee accounts for the activity of the Retirement Plan for employees of Covington Electric System. The Plan is a single employer public employee retirement System (PERS) administered by Ellis & Ward Consulting Group Inc.. All employees of the Covington Electric System participate as of April 1<sup>st</sup> following one year of service.

The Retirement Plan for employees of Covington Electric System issues a publically available report that can be obtained by contacting Ellis & Ward Consulting Group Inc. P.O. Box 2470, Cordova, TN 38088-2470.

*Benefits Provided:* The Plan provides retirement benefits as well as death and disability benefits. Retirement benefits vest at a rate of 20% per year beginning with three years of service. Employees may retire after age 60 and the completion of 10 years of service with a reduction for early commencement.

*Normal retirement benefit:* The amount of retirement benefit to be provided for each Participant who retires on the Participant's Normal Retirement Date shall be a monthly income equal to the number of years of continuous service multiplied by 1.6% of the final average monthly compensation.

*Early retirement, death benefits and benefits upon termination of employment:* The accrued retirement income will be determined using the final average monthly compensation and continuous services at the date of termination. A participant is eligible for early retirement when he / she has both completed at least 10 years of service and attained age sixty (60). The normal retirement for early retirement is the accrued retirement income calculated as described above, and reduced by an actuarial reduction factor due to younger age at retirement and earlier commencement of retirement income payments. Upon the death of a participant after his / her initial vesting date and prior to his / her normal retirement date, his / her beneficiary will receive the actuarial equivalent of the participant's vested accrued benefit. A participant whose employment is terminated due to total and permanent disability shall be entitled to the retirement income at normal retirement age which the participant would have received had he continued in employment to his normal retirement date assuming constant earnings.

*Normal form of retirement income:* The normal form of retirement income is life only income

At March 31, 2018, the Retirement Plan membership consisted of:

	2018	2017
Inactive plan members or beneficiaries currently receiving benefits	21	19
Inactive plan members entitled to but not yet receiving benefits	-	-
Active plan members	19	19
	40	38

*Contributions:* Required contributions are determined by The Retirement Plan for employees of Covington Electric System based on calculations performed by an independent actuary. The actuarially determined rate is the estimated amount necessary to finance the costs of benefits

**COVINGTON ELECTRIC SYSTEM**  
**NOTES TO FINANCIAL STATEMENTS**  
June 30, 2018 and 2017

earned by employees during the year, with an additional amount to finance any unfunded accrued liability. The current contribution rate is 11.70% of payroll.

The Utility's required contribution for the years ended as follows.

<u>Year</u>	<u>Minimum Contribution</u>	<u>Actual Contribution</u>
2018	132,956	146,866
2017	135,141	135,141
2016	120,292	120,292

*Funded status and funding progress:* As of March 31, 2018 the actuarial accrued liability for benefits was \$3,783,796 and the net pension liability was \$362,587. Total covered payroll was \$1,255,270 and the ratio of net pension liability to covered payroll was 28.89%. As of March 31, 2017 the actuarial accrued liability for benefits was \$3,666,876 and the net pension liability was \$491,874. Total covered payroll was \$1,105,403 and the ratio of net pension liability to covered payroll was 44.50%.

*Net Pension Liability (Asset):* Covington Electric System's net pension liability (asset) was measured as of March 31, 2018, and the total pension liability used to calculate net pension liability (asset) was determined by an actuarial valuation as of that date.

*Actuarial assumptions:* The total pension liability as of March 31, 2018 actuarial valuation was determined using the following actuarial assumptions, applied to all periods included in the measurement:

Actuarial cost method	Aggregate
Asset valuation method	Market value
Inflation	2.5%
Salary increases	3.0% including inflation
Investment rate of return	6.5%, net of plan investment expense, including inflation
Retirement age	65
Mortality	RP-2000
Withdrawal rates	None

The actuarial assumptions used in the April 1, 2018 actuarial valuation were based on the results of an actuarial experience study performed for the period April 1, 2017 through March 31, 2018. The demographic assumptions were adjusted to more closely reflect actual and expected future experience.

*Discount Rate:* The discount rate used to measure the total pension liability was 6.5%. The projection of cash flows used to determine the discount rate assumes that employee contributions will be made at the current contribution rate and the employer will continue to contribute the actuarially determined contribution in accordance with the plan's current funding policy on an annual basis. Based on that assumption, the pension plan's fiduciary net position is projected to be available to make all projected future benefit payments 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.

**COVINGTON ELECTRIC SYSTEM**  
**NOTES TO FINANCIAL STATEMENTS**  
June 30, 2018 and 2017

*Changes in the Net Pension Liability (Asset):*

**2018 Changes in net pension liability (asset)**

	Increase/Decrease		
	Total Pension Liability	Plan Fiduciary Net Position	Net Pension Liability
Balance at March 31, 2017	\$ 3,666,876	\$ 3,175,002	\$ 491,874
Changes for the year:			
Service cost	103,352	-	103,352
Interest cost	237,814	-	237,814
Difference between expected and actual experience	(104,479)	-	(104,479)
Employer contributions	-	146,866	(146,866)
Employee contributions	-	-	-
Net investment income	-	206,360	(206,360)
Actual vs Expected Income	-	40,331	(40,331)
Benefit payments	(119,767)	(119,767)	-
Administrative expense	-	(27,583)	27,583
Other charges	-	-	-
Net changes:	<u>116,920</u>	<u>246,207</u>	<u>(129,287)</u>
Balance at March 31, 2018	<u>\$ 3,783,796</u>	<u>\$ 3,421,209</u>	<u>\$ 362,587</u>

**2017 Changes in net pension liability (asset)**

	Increase/Decrease		
	Total Pension Liability	Plan Fiduciary Net Position	Net Pension Liability
Balance at March 31, 2016	\$ 3,365,024	\$ 2,900,444	\$ 464,580
Changes for the year:			
Service cost	91,976	-	91,976
Interest cost	217,905	-	217,905
Difference between expected and actual experience	109,220	-	109,220
Employer contributions	-	135,141	(135,141)
Employee contributions	-	-	-
Net investment income	-	285,550	(285,550)
Benefit payments	(117,249)	(117,249)	-
Administrative expense	-	(28,884)	28,884
Other charges	-	-	-
Net changes:	<u>301,852</u>	<u>274,558</u>	<u>27,294</u>
Balance at March 31, 2017	<u>\$ 3,666,876</u>	<u>\$ 3,175,002</u>	<u>\$ 491,874</u>

*Sensitivity of the net pension liability (asset) to changes in the discount rate:* The following presents the net pension liability (asset) of Covington Electric System calculated using the discount rate of 6.5 percent, as well as what the net pension liability (asset) would be if it were calculated using a discount rate that is 1-percentage-point lower (5.5 percent) or 1-percentage-point higher (7.5 percent) than the current rate:

	2018	2017
Net Pension Liability with a 1% Decrease in Discount Rate: 5.5%	\$ 872,520	\$ 998,977
Net Pension Liability at Current Discount Rate: 6.5%	362,587	491,874
Net Pension Liability with a 1% Increase in Discount Rate: 7.5%	(69,263)	63,759

**COVINGTON ELECTRIC SYSTEM**  
**NOTES TO FINANCIAL STATEMENTS**  
June 30, 2018 and 2017

*Plan Fiduciary Net Position:* Detailed information about the Plan's fiduciary net position is available on pages 16 and 17 of this report.

*Pension Expense (Income) and Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions:* For the year ended June 30, 2018 and 2017, the Utility recognized pension expense of \$184,290 and \$186,707 respectively.

At June 30, 2018 and 2017, deferred outflows of resources and inflows of resources in relation to pensions were as follows:

<b>2018 Deferred outflows/inflows of resources</b>	<b>Deferred Outflows</b>	<b>Deferred Inflows</b>
Difference between expected and actual experience	\$ 96,370	\$ 205,566
Net difference between projected and actual earnings in pension investments	111,669	90,692
Pension contributions subsequent to measurement date	132,956	-
	<u>\$ 340,995</u>	<u>\$ 296,258</u>

<b>2017 Deferred outflows/inflows of resources</b>	<b>Deferred Outflows</b>	<b>Deferred Inflows</b>
Difference between expected and actual experience	\$ 102,795	\$ 115,808
Net difference between projected and actual earnings in pension investments	169,408	77,903
Pension contributions subsequent to measurement date	146,866	-
	<u>\$ 419,069</u>	<u>\$ 193,711</u>

The System makes an annual contribution to the pension plan instead of monthly contributions. This contribution is typically made in May/June of each year, so there will be a full year of contributions included in deferred outflows as "pension contributions subsequent to measurement date" in most years.

Amounts reported as deferred outflows of resources and deferred inflows of resources will be recognized in pension expense as follows:

Year ending March 31,		
2019	\$	21,902
2020		18,091
2021		(35,838)
2022		(16,362)
2023		(8,296)
Thereafter	\$	(67,716)

*Payable to The Retirement Plan for employees of Covington Electric System:* At June 30, 2018 and 2017, the utility showed no amounts outstanding for contributions due to The Retirement Plan for Employees of Covington Electric System.

**COVINGTON ELECTRIC SYSTEM**  
**NOTES TO FINANCIAL STATEMENTS**  
June 30, 2018 and 2017

**B. Risks and Uncertainties – Pension Plan**

The Plan invests in various investment securities. Investment securities are exposed to various risks such as interest rate, market, and credit risks. Due to the level of risk associated with certain investment securities, it is at least reasonably possible that changes in the values of investment securities will occur in the near term and, that such changes could materially affect the amounts reported in the statement of net position available for benefits.

Plan contributions are made and the actuarial present value of accumulated plan benefits are reported based on certain assumptions pertaining to interest rates, inflation rates and employee demographics, all of which are subject to change. Due to uncertainties inherent in the estimations and assumptions process, it is at least reasonably possible that changes in these estimates and assumptions in the near term would be material to the financial statements.

**C. Deferred Compensation Plan (457 Plan)**

The System offers a deferred compensation plan (Covington Electric System Employees' 457 Plan) that is administered by VOYA. The contribution rates for this plan are determined by the employee while the System does not match any contributions. The employee can change contributions rates at any time while on the plan. The amount of pension expense recognized by the System in the current period was \$0. The amount of forfeitures reflected in pension expense were \$0 during the current period, and there will never be forfeitures due to the fact that the employee is 100% vested at the time of contribution. The System did not have a liability at June 30, 2018.

**D. Power Contract**

The System has a power contract with the Tennessee Valley Authority (TVA) whereby the System purchases all its electric power from TVA and is subject to certain restrictions and conditions as provided for in the power contract. Such restrictions include, but are not limited to, prohibitions against furnishing, advancing, lending, pledging, or otherwise diverting System funds, revenues, or property to other operations of the municipality and the purchase or payment of or providing security for indebtedness on other obligations applicable to such other operations.

**E. Risk Management**

The System is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. During the years ended June 30, 2018 and 2017, the System purchased commercial insurance for all of the above risks. Settled claims have not exceeded this commercial coverage in any of the past three years and there has been no significant reduction in the amount of coverage.

**F. Unamortized Acquisition Adjustment - Vandergrift Annexation**

As of May 2012, the System has made an agreement to pay Southwest Tennessee Electric Membership Corporation a one time payment in the amount of \$241,642 for lost revenue in a recent Vandergrift annexation. This payment took place in the fiscal year 2013 when the project was closed. The annexation cost is reflected as an unamortized acquisition adjustment on the Statements of Net Positions and is amortized monthly over 10 years. The amortization expense related to this annexation as of June 30, 2018 and 2017 was \$24,164. The balance as of June 30, 2018 is \$100,684. The balance at June 30, 2017 was \$124,848.

## **REQUIRED SUPPLEMENTARY INFORMATION**

**COVINGTON ELECTRIC SYSTEM**  
**SCHEDULES OF CHANGES IN NET POSITION LIABILITY (ASSET) AND RELATED**  
**RATIOS BASED ON PARTICIPATION IN THE PUBLIC EMPLOYEE PENSION PLAN**  
March 31, 2018 and 2017

	<u>2018</u>	<u>2017</u>	<u>2016</u>	<u>2015</u>
<b>Total pension liability</b>				
Service cost	\$ 103,352	\$ 91,976	\$ 95,438	\$ 92,286
Interest	237,814	217,905	207,893	201,831
Changes in benefit terms	-	-	-	-
Differences between actual & expected experience	(104,479)	109,220	(36,904)	(102,458)
Change of assumptions	-	-	-	-
Benefit payments, including refunds of employee contributions	<u>(119,767)</u>	<u>(117,249)</u>	<u>(104,077)</u>	<u>(95,873)</u>
<b>Net change in total pension liability</b>	<b>\$ 116,920</b>	<b>301,852</b>	<b>162,350</b>	<b>95,786</b>
Total pension liability - beginning	<u>3,666,876</u>	<u>3,365,024</u>	<u>3,202,674</u>	<u>3,106,888</u>
Total pension liability - ending (a)	<u>3,783,796</u>	<u>3,666,876</u>	<u>3,365,024</u>	<u>3,202,674</u>
<b>Plan fiduciary net position</b>				
Contributions - employer	146,866	135,141	120,292	127,307
Contributions - employee	-	-	-	-
Net investment income (loss)	246,691	285,550	(75,956)	164,946
Benefit payments, including refunds of employee contributions	(119,767)	(117,249)	(104,077)	(95,873)
Administrative expense	<u>(27,583)</u>	<u>(28,884)</u>	<u>(23,130)</u>	<u>(28,073)</u>
<b>Net change in plan fiduciary net position - beginning</b>	<b>246,207</b>	<b>274,558</b>	<b>(82,871)</b>	<b>168,307</b>
Plan fiduciary net position - beginning	<u>3,175,002</u>	<u>2,900,444</u>	<u>2,983,315</u>	<u>2,815,008</u>
Plan fiduciary net position - ending (b)	<u>3,421,209</u>	<u>3,175,002</u>	<u>2,900,444</u>	<u>2,983,315</u>
<b>Net pension liability (asset) - ending (a) - (b)</b>	<b>362,587</b>	<b>\$ 491,874</b>	<b>\$ 464,580</b>	<b>\$ 219,359</b>
<b>Plan fiduciary net position as a percentage of total pension liability</b>	<b>90.42%</b>	<b>86.59%</b>	<b>86.19%</b>	<b>93.15%</b>
<b>Covered - employee payroll</b>	<b>\$ 1,255,270</b>	<b>\$ 1,105,403</b>	<b>\$ 1,150,884</b>	<b>\$ 1,198,494</b>
<b>Net pension liability (asset) as a percentage of covered employee payroll</b>	<b>28.89%</b>	<b>44.50%</b>	<b>40.37%</b>	<b>18.30%</b>

*This is a 10-year schedule; however, the information in this schedule is not required to be presented retroactively. Years will be added to this schedule in future fiscal years until 10 years of information is available.*

*See independent auditor's report.*

**COVINGTON ELECTRIC SYSTEM**  
**SCHEDULES OF CONTRIBUTIONS BASED ON PARTICIPATION IN THE PUBLIC**  
**EMPLOYEE PENSION PLAN**  
Last Ten Fiscal Years

	<u>2018</u>	<u>2017</u>	<u>2016</u>	<u>2015</u>
Actuarially determined contribution	\$ 146,866	\$ 135,141	\$ 120,292	\$ 127,307
Contributions in relation to the actuarially determined contribution	<u>146,866</u>	<u>135,141</u>	<u>120,292</u>	<u>127,307</u>
Contribution deficiency (excess)	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>
Covered-employee payroll	\$ 1,255,270	\$ 1,105,403	\$1,150,884	\$1,198,494
Contributions as a percentage of covered - employee payroll	11.70%	12.23%	10.45%	10.62%

This is a 10-year schedule; however, the information in this schedule is not required to be presented retroactively.

Years will be added to this schedule in the future fiscal years until 10 years of information is available.

*See independent auditor's report.*

**COVINGTON ELECTRIC SYSTEM**  
**SCHEDULES OF INVESTMENT RETURNS**  
**EMPLOYEE PENSION PLAN**  
Last Ten Fiscal Years

	<u>2018</u>	<u>2017</u>	<u>2016</u>	<u>2015</u>
Annual money-weighted rate of return, net of investment expense	6.70%	8.70%	-3.30%	4.80%

\* Only four years are available from actuarial valuation.

*See independent auditor's report.*

**COVINGTON ELECTRIC SYSTEM**  
**NOTES TO REQUIRED SUPPLEMENTARY INFORMATION**  
For the Years Ended June 30, 2018 and 2017

Valuation Date	Actuarially determined contributions are calculated as of April 1st, three months prior to the fiscal year in which contributions are reported
Actuarial cost method	Aggregate Cost Method
Amortization Method	NA
Remaining Amortization	NA
Asset valuation	Market Value
Inflation	2.5%
Withdrawal Rates	None
Salary Increases	3% , including inflation
Investment Rate of Return	6.5 percent, net of plan investment expense, including inflation
Retirement age	Age 65
Mortality	RP-2000 Mortality Table

*See independent auditor's report.*

## **SUPPLEMENTARY AND OTHER INFORMATION SECTION**

**COVINGTON ELECTRIC SYSTEM**  
**SCHEDULES OF OPERATING REVENUES AND EXPENSES - ELECTRIC SYSTEM**  
For the Years Ended June 30, 2018 and 2017

	<u>2018</u>		<u>2017</u>	
	<u>Amount</u>	<u>Percent</u>	<u>Amount</u>	<u>Percent</u>
<b>Operating revenues:</b>				
Charges for sales and services:				
Residential sales	\$ 4,971,099	23.73	\$ 4,896,278	23.01
Small lighting and power sales	1,838,302	8.77	1,884,632	8.86
Large lighting and power sales	14,275,506	68.13	14,722,676	69.18
Power credit	(818,993)	(3.91)	(903,633)	(4.25)
Street and athletic lighting sales	150,462	0.72	148,592	0.70
Outdoor lighting	247,508	1.18	249,418	1.17
Uncollectible accounts	(8,261)	(0.04)	(18,557)	(0.09)
Total charges for sales and services	<u>20,655,623</u>	<u>98.58</u>	<u>20,979,406</u>	<u>98.58</u>
Other revenues				
Forfeited discounts	108,178	0.52	113,247	0.53
Miscellaneous service revenue	52,756	0.25	52,572	0.25
Rent from electric property	123,993	0.59	119,945	0.56
Other electric revenue	12,440	0.06	17,167	0.08
Total other revenues	<u>297,367</u>	<u>1.42</u>	<u>302,931</u>	<u>1.42</u>
Total operating revenues	<u>20,952,990</u>	<u>100.00</u>	<u>21,282,337</u>	<u>100.00</u>
<b>Operating expenses:</b>				
Cost of sales and services:				
Purchased power	<u>17,112,807</u>	<u>81.67</u>	<u>17,427,379</u>	<u>81.89</u>
Operations expenses:				
Distribution expenses:				
Supervision and engineering	63,900	0.30	66,128	0.31
Station expense	52,124	0.25	29,985	0.14
Overhead line expense	183,083	0.87	194,490	0.91
Underground line expense	12,310	0.06	32,916	0.15
Street lighting and signal system	9,263	0.04	5,112	0.02
Meter expense	102,621	0.49	119,922	0.56
Customer installation expense	16,176	0.08	5,026	0.02
Miscellaneous	39,037	0.19	39,669	0.19
Rents	14,707	0.07	13,787	0.06
Total distribution expenses	<u>\$ 493,221</u>	<u>2.35</u>	<u>\$ 507,035</u>	<u>2.38</u>

*See independent auditor's report.*

**COVINGTON ELECTRIC SYSTEM**  
**SCHEDULES OF OPERATING REVENUES AND EXPENSES - ELECTRIC SYSTEM**  
For the Years Ended June 30, 2018 and 2017

	<u>2018</u>		<u>2017</u>	
	<u>Amount</u>	<u>Percent</u>	<u>Amount</u>	<u>Percent</u>
Customer accounts expenses:				
Supervision Customer Accounts	\$ 55,445	0.26	\$ 55,813	0.26
Meter reading expense	64,417	0.31	63,108	0.30
Customer records and collection	257,671	1.23	269,946	1.27
Total customer accounts expenses	<u>377,533</u>	<u>1.80</u>	<u>388,867</u>	<u>1.83</u>
Customer service and information expenses:				
Customer assistance expense	14,265	0.07	6,251	0.03
Miscellaneous customer service	7,500	0.04	7,500	0.04
Total customer service and information expenses	<u>21,765</u>	<u>0.10</u>	<u>13,751</u>	<u>0.06</u>
Administrative expenses				
Salaries	305,356	1.46	275,860	1.30
Office supplies and expense	72,880	0.35	86,610	0.41
Administrative expenses transferred	(50,942)	(0.24)	(50,330)	(0.24)
Outside services employed	40,159	0.19	28,592	0.13
Insurance	21,471	0.10	21,098	0.10
Injuries and damages	97,002	0.46	66,985	0.31
Employee pension and benefits	407,775	1.95	374,073	1.76
Advertising	210	0.00	412	0.00
Miscellaneous	74,181	0.35	69,880	0.33
Total administrative expenses	<u>968,092</u>	<u>4.62</u>	<u>873,180</u>	<u>4.10</u>
Total operations expenses	<u>1,860,611</u>	<u>8.88</u>	<u>1,782,833</u>	<u>8.38</u>
Maintenance expenses				
Distribution expenses:				
Supervision and engineering	63,932	0.31	66,128	0.31
Station equipment	29,153	0.14	15,818	0.07
Overhead lines	247,267	1.18	494,539	2.32
Underground lines	7,775	0.04	11,357	0.05
Line transformers	-	-	2,246	0.01
Street lights and signal system	11,630	0.06	45,321	0.21
Outdoor lighting	29,916	0.14	17,648	0.08
Total distribution expenses	<u>389,673</u>	<u>1.86</u>	<u>653,057</u>	<u>3.07</u>
Administrative expenses:				
General plant and equipment	142,447	0.68	157,661	0.74
Total maintenance expenses	<u>532,120</u>	<u>2.54</u>	<u>810,718</u>	<u>3.81</u>
Depreciation and amortization	<u>729,682</u>	<u>3.48</u>	<u>731,793</u>	<u>3.44</u>
Taxes	<u>97,061</u>	<u>0.46</u>	<u>92,540</u>	<u>0.43</u>
Total operating expenses	<u>\$ 20,332,281</u>	<u>97.04</u>	<u>\$ 20,845,263</u>	<u>97.95</u>

*See independent auditor's report.*

**COVINGTON ELECTRIC SYSTEM**  
**SCHEDULE OF LONG-TERM DEBT**  
June 30, 2018

Year Ended June 30,	Series 2003	
	Electric Revenue and Tax Bonds	
	Principal	Interest
2019	125,000	32,648
2020	130,000	27,483
2021	135,000	22,034
2022	140,000	16,188
2023	145,000	9,954
2024	155,000	3,391
	\$ 830,000	\$ 111,698

*See independent auditor's report.*

**COVINGTON ELECTRIC SYSTEM**  
**ELECTRIC RATES IN FORCE**  
June 30, 2018

<b>Residential rate schedule</b>	
Customer charge - per delivery point per month	\$ 14.40
Energy charge - cents per kWh	0.08963
<b>General power schedule</b>	
GSA1 (Under 50 kW demand & less than 15,000 kWh)	
Customer charge - per delivery point per month	32.00
Energy charge - cents per kWh	0.10298
GSA2 (51-1000 kW demand or more than 15,000 kWh)	
Customer charge - per delivery point per month	125.00
Demand charges - per kW per month	
First 50 Kw	1.00
Excess over 50 kW	13.90
Energy charge - cents per kWh	
First 15,000 kWh per month	0.10147
Additional kWh per month	0.06076
GSA3 (1000 - 5000 kW demand)	
Customer charge - per delivery point per month	400.00
Demand charges - per kW per month	
First 1,000 kW	13.13
Excess over 1,000 kW	13.13
Excess over 2,500 kW	13.13
Energy charge - cents per kWh	0.06551
SMSB (Seasonal Demand and Energy - Manufacturing Service)	
Customer charge - per delivery point per month	1,500.00
Administrative charge	350.00
OnPeak kW	9.97
Max kW	2.07
OffPeak Excess of Contract kW	9.97
Outdoor Lighting LS	\$ 0.06560

*See independent auditor's report.*

**COVINGTON ELECTRIC SYSTEM**  
**SUPPLEMENTAL INFORMATION - ELECTRIC SYSTEM - UNAUDITED**  
For the Years Ended June 30,

	<u>2018</u>	<u>2017</u>	<u>2016</u>	<u>2015</u>	<u>2014</u>
<b>Revenue</b>					
Residential	\$ 4,971,099	\$ 4,896,278	\$ 4,871,108	\$ 4,987,937	\$ 4,869,572
Small lighting	1,838,302	1,884,632	1,726,998	1,729,783	1,704,784
Large lighting	13,456,513	13,819,043	13,514,028	12,278,732	12,085,778
Street and athletic lighting	150,462	148,592	164,034	171,194	164,898
Outdoor lighting	247,508	249,418	225,989	223,851	217,026
Uncollectible accounts	(8,261)	(18,557)	(4,835)	(11,955)	(5,524)
Other operating	297,367	302,931	293,221	300,259	261,731
Interest and other revenue	34,486	10,810	25,388	26,064	27,856
	<u>20,987,476</u>	<u>21,293,147</u>	<u>20,815,931</u>	<u>19,705,865</u>	<u>19,326,121</u>
<b>Expense</b>					
Electric power costs	17,112,807	17,427,379	17,141,050	15,935,924	15,717,411
Other operating expenses	2,392,731	2,593,551	2,425,660	2,050,261	2,086,057
Provision for depreciation	729,682	731,793	703,259	704,869	698,990
Taxes	97,061	92,540	92,312	85,573	86,471
Extraordinary item	-	-	-	152,622	-
Transfer - tax equivalent	366,061	392,459	382,786	385,106	370,348
Interest and other expense	46,152	52,752	68,278	66,972	68,784
	<u>20,744,494</u>	<u>21,290,474</u>	<u>20,813,345</u>	<u>19,381,327</u>	<u>19,028,061</u>
Net income (loss)	<u>\$ 242,982</u>	<u>\$ 2,673</u>	<u>\$ 2,586</u>	<u>\$ 324,538</u>	<u>\$ 298,060</u>
<b>Financial</b>					
Plant in service (at original cost)	<u>\$ 21,874,624</u>	<u>\$ 21,635,718</u>	<u>\$ 21,480,215</u>	<u>\$ 21,171,149</u>	<u>\$ 20,988,625</u>
Bonds and notes outstanding	<u>\$ 830,000</u>	<u>\$ 950,000</u>	<u>\$ 1,175,000</u>	<u>\$ 1,280,000</u>	<u>\$ 1,380,000</u>
<b>Power in use - kWh</b>					
Residential	49,602,628	48,426,182	48,296,913	50,126,898	51,793,728
Small commercial	14,999,913	15,445,297	14,665,330	14,419,190	14,646,330
Large commercial	172,972,197	178,229,254	178,045,760	166,848,132	146,593,119
Street and athletic lighting	1,519,464	1,496,166	1,504,698	1,510,016	1,613,465
Outdoor lighting	1,986,799	1,973,004	1,867,136	1,777,038	1,753,610
Total	<u>241,081,001</u>	<u>245,569,903</u>	<u>244,379,837</u>	<u>234,681,274</u>	<u>216,400,252</u>
Peak kW demand	<u>49,786</u>	<u>52,777</u>	<u>52,598</u>	<u>46,959</u>	<u>46,959</u>
<b>Number of customers</b>					
Residential	3,729	3,710	3,724	3,795	3,761
Small lighting	808	799	805	811	796
Large lighting	127	130	135	138	132
Street and athletic lighting	29	27	30	30	30
Outdoor lighting	34	32	33	31	28
	<u>4,727</u>	<u>4,698</u>	<u>4,727</u>	<u>4,805</u>	<u>4,747</u>
Line loss	<u>2.45%</u>	<u>2.25%</u>	<u>2.25%</u>	<u>2.20%</u>	<u>2.37%</u>

See independent auditor's report.

## **INTERNAL CONTROL AND COMPLIANCE SECTION**



**Independent Auditor's Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance With Governmental Auditing Standards**

Board of Directors  
Covington Electric System  
Covington, Tennessee

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 *Governmental Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the major fund and the Covington Electric System Employees' 457 Plan of the Covington Electric System (the System), which are enterprise and fiduciary funds of the City of Covington, Tennessee, as of and for the year ended June 30, 2018, and the Covington Electric System Employees' Retirement Plan as of and for the year ended March 31, 2018, and the related notes to the financial statements, which collectively comprise the System's basic financial statements, and have issued our report thereon dated October 22, 2018.

**Internal Control Over Financial Reporting**

In planning and performing our audit of the financial statements, we considered the System's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the System's internal control. Accordingly, we do not express an opinion on the effectiveness of the System'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 that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

**Compliance and Other Matters**

As part of obtaining reasonable assurance about whether the System's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion.

The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Governmental Auditing Standards*.

**Purpose of this Report**

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

Alexander Thompson Arnold PLLC

Jackson, Tennessee  
October 22, 2018

**COVINGTON ELECTRIC SYSTEM**  
**SCHEDULE OF FINDINGS**  
June 30, 2018 and 2017

**Current Year Findings:**

No current year findings reported.

**COVINGTON ELECTRIC SYSTEM**  
**SCHEDULE OF PRIOR YEAR FINDINGS**  
June 30, 2018 and 2017

**Prior Year Findings:**

No prior year findings reported.