



Certified Public Accountants

EL PASO WATER COMPANY, INC.
A COMPONENT UNIT OF THE CITY OF DERBY, KANSAS

FINANCIAL STATEMENTS
YEARS ENDED DECEMBER 31, 2022 AND 2021

EL PASO WATER COMPANY, INC.
A COMPONENT UNIT OF THE CITY OF DERBY, KANSAS
FINANCIAL STATEMENTS
Years Ended December 31, 2022 and 2021

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EL PASO WATER COMPANY, INC.
A COMPONENT UNIT OF THE CITY OF DERBY, KANSAS
Board of Directors
December 31, 2022

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EL PASO WATER COMPANY, INC.
A COMPONENT UNIT OF THE CITY OF DERBY, KANSAS
Officers
December 31, 2022

Kiel Mangus, President
836 E. Freedom
Derby, KS 67037

Robert Mendoza, Vice-President
1637 E Blue Spruce Circle
Derby, KS 67037

Lynn Ciarleglio, Secretary
501 S Georgie
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Megan Sneller, Treasurer
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Mulvane, KS 67110



INDEPENDENT AUDITORS' REPORT

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

Report on the Audit of the Financial Statements

Opinion

We have audited the financial statements of El Paso Water Company, Inc. (the Company), a component unit of the City of Derby, Kansas, which comprise the balance sheets as of December 31, 2022 and 2021, the related statements of income, retained earnings, and cash flows for the years then ended, and the related notes to the financial statements.

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the Company as of December 31, 2022 and 2021, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Basis for Opinion

We conducted our audits in accordance with auditing standards generally accepted in the United States of America (GAAS). Our responsibilities under those standards are further described in the Auditors' Responsibilities for the Audit of the Financial Statements section of our report. We are required to be independent of the Company and to meet our other ethical responsibilities, in accordance with the relevant ethical requirements relating to our audits. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Responsibilities of Management for the Financial Statements

Management is responsible for the preparation and fair presentation of the financial statements in accordance with accounting principles generally accepted in the United States of America, and for 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.

In preparing the financial statements, management is required to evaluate whether there are conditions or events, considered in the aggregate, that raise substantial doubt about the Company's ability to continue as a going concern within one year after the date that the financial statements are issued or available to be issued.

An Independently Owned Member, RSM US Alliance

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

Auditors' Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditors' report that includes our opinion. Reasonable assurance is a high level of assurance but is not absolute assurance and therefore is not a guarantee that an audit conducted in accordance with GAAS will always detect a material misstatement when it exists. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control. Misstatements are considered material if there is a substantial likelihood that, individually or in the aggregate, they would influence the judgment made by a reasonable user based on the financial statements.

In performing an audit in accordance with GAAS, we:

- Exercise professional judgment and maintain professional skepticism throughout the audit.
- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, and design and perform audit procedures responsive to those risks. Such procedures include examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements.
- Obtain an understanding of internal control relevant to the audit 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 Company's internal control. Accordingly, no such opinion is expressed.
- Evaluate the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluate the overall presentation of the financial statements.
- Conclude whether, in our judgment, there are conditions or events, considered in the aggregate, that raise substantial doubt about the Company's ability to continue as a going concern for a reasonable period of time.

We are required to communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit, significant audit findings, and certain internal control-related matters that we identified during the audit.

Supplementary Information

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

BT & Co., P.A.

March 24, 2023
Topeka, Kansas

EL PASO WATER COMPANY, INC.
A COMPONENT UNIT OF THE CITY OF DERBY, KANSAS
BALANCE SHEETS
December 31, 2022 and 2021

	2022	2021
<u>ASSETS</u>		
Utility plant:		
Land and land improvements	\$ 75,059	\$ 75,059
Wells, pumphouses and equipment	995,839	995,839
Mains and storage tanks	4,457,556	4,457,556
Meters	656,203	673,283
Warehouse building	58,954	58,954
Office furniture and equipment	25,213	25,213
Automotive and other equipment	357,665	357,665
	6,626,489	6,643,569
Less accumulated depreciation	(5,631,438)	(5,569,110)
Net utility plant	995,051	1,074,459
Current assets:		
Cash	687,965	833,785
Accounts receivable	566,741	513,562
Unbilled receivables	331,177	305,191
Materials and supplies	23,641	10,938
Prepaid insurance	3,362	3,362
	1,612,886	1,666,838
Total current assets	1,612,886	1,666,838
Total assets	\$ 2,607,937	\$ 2,741,297

(Continued)

EL PASO WATER COMPANY, INC.
A COMPONENT UNIT OF THE CITY OF DERBY, KANSAS
BALANCE SHEETS
(Continued)
December 31, 2022 and 2021

	2022	2021
<u>LIABILITIES AND STOCKHOLDER'S EQUITY</u>		
Current liabilities:		
Accounts payable	\$ 241,439	\$ 312,337
Stockholder's equity:		
Common stock, no par value, stated value \$ 25 per share: authorized 40,000 shares; issued and outstanding 34,860 shares	871,500	871,500
Additional paid-in capital	303,054	303,054
Retained earnings	1,791,935	1,854,397
	2,966,489	3,028,951
Treasury stock at cost - 3,545 shares	(599,991)	(599,991)
Total stockholder's equity	2,366,498	2,428,960
Total liabilities and stockholder's equity	\$ 2,607,937	\$ 2,741,297

See accompanying notes to financial statements.

EL PASO WATER COMPANY, INC.
A COMPONENT UNIT OF THE CITY OF DERBY, KANSAS
STATEMENTS OF INCOME
Years Ended December 31, 2022 and 2021

	2022	2021
Operating revenues	\$ 8,332,753	\$ 7,054,121
Operating expenses:		
Operation and maintenance	5,472,215	4,481,711
Depreciation	79,408	105,687
Total operating expenses	5,551,623	4,587,398
Net income	\$ 2,781,130	\$ 2,466,723

See accompanying notes to financial statements.

EL PASO WATER COMPANY, INC.
A COMPONENT UNIT OF THE CITY OF DERBY, KANSAS
STATEMENTS OF RETAINED EARNINGS
Years Ended December 31, 2022 and 2021

	2022	2021
Balance, beginning of year	\$ 1,854,397	\$ 1,924,053
Net income	2,781,130	2,466,723
Cash dividends to the City of Derby, Kansas	(2,843,592)	(2,536,379)
Balance, end of year	\$ 1,791,935	\$ 1,854,397

See accompanying notes to financial statements.

EL PASO WATER COMPANY, INC.
A COMPONENT UNIT OF THE CITY OF DERBY, KANSAS
STATEMENTS OF CASH FLOWS
Years Ended December 31, 2022 and 2021

	2022	2021
Cash flows from operating activities:		
Net income	\$ 2,781,130	\$ 2,466,723
Adjustments to reconcile net income to net cash flows from operating activities:		
Depreciation	79,408	105,687
Changes in assets and liabilities:		
Accounts and unbilled receivables	(79,165)	(53,776)
Materials and supplies	(12,703)	28,448
Accounts payable	(70,898)	35,712
	2,697,772	2,582,794
Cash flows from financing activities:		
Dividends paid	(2,843,592)	(2,536,379)
Net increase (decrease) in cash	(145,820)	46,415
Cash, beginning of year	833,785	787,370
Cash, end of year	\$ 687,965	\$ 833,785

See accompanying notes to financial statements.

EL PASO WATER COMPANY, INC.
A COMPONENT UNIT OF THE CITY OF DERBY, KANSAS
NOTES TO FINANCIAL STATEMENTS
December 31, 2022 and 2021

1 - Nature of Organization and Summary of Significant Accounting Policies

Organization and Operations

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

Utility Plant

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

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

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

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

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

EL PASO WATER COMPANY, INC.
A COMPONENT UNIT OF THE CITY OF DERBY, KANSAS
NOTES TO FINANCIAL STATEMENTS
(Continued)

Cash

The Company maintains deposits in banks. The Federal Deposit Insurance Corporation insures amounts held by each institution in the Company's name up to \$ 250,000. The Company manages deposit concentration risk by placing cash with financial institutions believed by management to be creditworthy. At times, the amounts on deposit may exceed insured limits. To date, the Company has not experienced losses in any of these accounts.

Accounts Receivable and Unbilled Receivables

Accounts receivable consist of both residential and commercial water sales. Unbilled receivables are recorded for services provided for which customers have not been billed at December 31, 2022 and 2021. The Company utilizes the direct write-off method of accounting for bad debts. Accounts greater than 90 days past due are considered uncollectible and are written off. Management has determined that an allowance for doubtful accounts is not necessary at December 31, 2022 and 2021.

Materials and Supplies

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

Revenue Recognition

Revenue is primarily derived from the sale of water to customers. Revenues are recognized as services are provided. Sales and other taxes the Company collects concurrently are excluded from revenue. The Company does not have a significant financing component. The Company recognizes revenue in accordance with ASC Topic 606, *Revenue from Contracts with Customers*, which provides a five-step model for recognizing revenue from contracts with customers as follows: 1) identify the contract, 2) identify performance obligations, 3) determine the transaction price, 4) allocate the transaction price, and 5) recognize revenue.

The Company's customers consist of private customers, primarily located within the City of Derby, Kansas.

For performance obligations related to water sales, control transfers to the customer over time. Revenue under water sales contracts is recognized on the basis of gallons used using rates approved by the City of Derby, Kansas city council.

The Company has elected as a practical expedient the accounting policy under which it excludes from the transaction price taxes it collects from its customers that were assessed by a government authority on (or contemporaneous with) the Company's revenue-generating transactions with its customers. The Company therefore reports sales revenue net of sales tax.

EL PASO WATER COMPANY, INC.
A COMPONENT UNIT OF THE CITY OF DERBY, KANSAS
NOTES TO FINANCIAL STATEMENTS
(Continued)

Leases

On January 1, 2022, the Company adopted Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) Topic 842, *Leases*, using the modified retrospective approach by electing a package of practical expedients including (1) to not reassess its prior conclusions under ASC Topic 840, *Leases*, regarding (a) whether a preexisting contract is or contains a lease, (b) whether a preexisting lease should be classified as an operating or finance lease and (c) whether the initial direct costs capitalized for a preexisting lease under Topic 840 qualify for capitalization.

The Company leases antenna placement space on its water tower to telecommunications companies. Each lessee has a land easement to maintain its own antenna; however, the Company has overall control of the easement. These leases may contain extension and termination options.

Topic 842 provides lessors a practical expedient, applicable by class of underlying asset, to not separate nonlease components from the associated lease component if certain criteria are met. An underlying asset is an asset that is the subject of a lease for which a right to use that asset has been conveyed to a lessee. The Company considers storage tanks as the class of underlying assets.

Lease components are elements of an arrangement that provide the customer with the right to use an identified asset. Nonlease components are distinct elements of a contract that are not related to securing the use of the leased asset and revenue is recognized in accordance with ASC Topic 606, *Revenue from Contracts with Customers*. In the case of the Company's business, the identified asset would be antenna placement space on its water tower.

The Company assessed and concluded that the timing and pattern of transfer for nonlease components and the associated lease components are the same. The Company determined that the predominant components were the lease components and, as such, its leases will continue to be accounted for as operating leases, and the Company has made a policy election to account for and present the lease components and the nonlease components as a single component in the revenue section of the statements of income within operating income.

Income Tax Matters

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

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

The Company files income tax returns in the U.S. federal jurisdiction and Kansas state jurisdiction. With few exceptions, the Company is no longer subject to U.S. federal or state and local income tax examinations by tax authorities for years before 2018.

EL PASO WATER COMPANY, INC.
A COMPONENT UNIT OF THE CITY OF DERBY, KANSAS
NOTES TO FINANCIAL STATEMENTS
(Continued)

Use of Estimates

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

2 - Related Party Transactions

The Board of Directors of El Paso Water Company, Inc. is comprised of the mayor and city council members of the City of Derby, Kansas. The City of Derby, Kansas bills the water charges for the Company. All employees of the Company are employees of the City of Derby, Kansas. The Company makes a monthly reimbursement to the City of Derby, Kansas for contract labor. The total contract labor reimbursement from the Company to the City of Derby, Kansas for the years ended December 31, 2022 and 2021 was \$ 722,495 and \$ 649,783, respectively.

The City of Derby, Kansas receives dividends from the Company. Cash dividends paid to the City of Derby, Kansas from the Company were \$ 2,843,592 and \$ 2,536,379 for the years ended December 31, 2022 and 2021, respectively.

The Company also leases office space from the City of Derby, Kansas. Total rental expense included in operations was \$ 14,300 for the years 2022 and 2021.

3 - Water Rights

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

EL PASO WATER COMPANY, INC.
A COMPONENT UNIT OF THE CITY OF DERBY, KANSAS
NOTES TO FINANCIAL STATEMENTS
(Continued)

4 - Leases

The Company's antenna placement space on its water tower is leased to telecommunications companies under operating leases with initial term expiration dates through 2031 and renewal expiration dates through 2041. The Company's investment in storage tanks upon which antenna placement space is held under operating leases in which the Company is lessor are as follows:

	2022	2021
Class of underlying assets:		
Storage tanks	\$ 1,304,431	\$ 1,304,431
Less accumulated depreciation	(1,003,626)	(982,960)
Total	\$ 300,805	\$ 321,471

The Company's rental income is primarily composed of payments defined under each lease agreement and is primarily subject to scheduled fixed increases. The Company recognized rental income of \$ 147,572 and \$ 142,378 during the years ended December 31, 2022 and 2021, respectively, which is included within the Company's statements of income.

Future undiscounted cash flows to be received for each of the next five years and thereafter are as follows as of December 31, 2022:

Years Ending December 31	Operating Leases
2023	\$ 113,045
2024	116,436
2025	90,671
2026	83,638
2027	86,147
2028 - 2032	413,794
2033 - 2037	256,866
2038 - 2041	224,182
Total lease payments	\$ 1,384,779

EL PASO WATER COMPANY, INC.
A COMPONENT UNIT OF THE CITY OF DERBY, KANSAS
NOTES TO FINANCIAL STATEMENTS
(Continued)

Future minimum lease payments to be received, as determined under Topic 840, or all non-cancelable leases for each of the five succeeding fiscal years are as follows as of December 31, 2021:

Years Ending December 31	Operating Leases
2022	\$ 109,753
2023	113,045
2024	116,436
2025	90,671
2026	83,638
2027 - 2031	452,968
2032 - 2036	249,385
2037 - 2041	278,636
Total lease payments	\$ 1,494,532

5 - Commitments

In April 2004, the City of Derby, Kansas issued \$ 9,455,000, 1.10% - 5.00% General Obligation Water System Refunding Bonds, Series 2004-A, with varying maturities up to December 1, 2022. Principal payments for 2016 through 2022 were refunded in September 2013, when the City of Derby, Kansas issued \$ 3,375,000, 2.50% - 3.00% General Obligation Water System Refunding Bonds, Series 2013-B, with varying maturities up to December 1, 2022. All of the Series 2013-B issuance pertained to the Company. The remaining principal payment for 2015 was refunded in June 2014, when the City of Derby, Kansas issued \$ 4,685,000, 2.10% - 4.00% General Obligation Refunding and Improvement Bonds, Series 2014-A, with varying maturities up to December 1, 2034. Of the \$ 4,685,000 Series 2014-A issuance, \$ 610,000 pertained to the Company.

In September 2012, the City of Derby, Kansas issued \$ 3,165,000, 1.00% - 2.125% General Obligation Bonds, Series 2012-B, with varying maturities up to December 1, 2027. Of the \$ 3,165,000 Series 2012-B issuance, \$ 708,120 pertained to the Company.

In December 2018, the City of Derby, Kansas issued both \$ 6,900,000, 3.00% - 3.35% General Obligation Bonds, Series 2018-A, with varying maturities up to December 1, 2038 and \$ 5,680,000, 3.50% - 5.00% General Obligation Bonds, Series 2018-B, with varying maturities up to December 1, 2039. Of the \$ 6,900,000 Series 2018-A bond issuance, \$ 775,000 pertained to the Company. Of the \$ 5,680,000 Series 2018-B bond issuance, \$ 2,710,000 pertained to the Company.

The Company paid dividends to the City of Derby, Kansas of \$ 2,843,592 and \$ 2,536,379 for the years 2022 and 2021, respectively, related to principal and interest payments on the Series 2012-B, Series 2013-B, Series 2018-A and Series 2018-B bond issues. Future dividend payments to the City of Derby, Kansas are anticipated in order to retire the Series 2012-B, Series 2014-A, Series 2018-A and Series 2018-B bonds.

EL PASO WATER COMPANY, INC.
A COMPONENT UNIT OF THE CITY OF DERBY, KANSAS
NOTES TO FINANCIAL STATEMENTS
(Continued)

6 - Water Purchased from City of Wichita

All water sold is purchased from the City of Wichita, Kansas. In November 2020, the Company entered into a contract with the City of Wichita, Kansas for wholesale water services. The contract contained a 50% “take or pay” provision based on the volume of water specified in a schedule of projected water usage. The term of the contract is 23 years, and it has the option to extend for an additional 10 years. No amounts were paid under the “take or pay” provision for 2022 or 2021.

7 - Subsequent Events

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

SUPPLEMENTARY INFORMATION

EL PASO WATER COMPANY, INC.
A COMPONENT UNIT OF THE CITY OF DERBY, KANSAS
SCHEDULES OF OPERATION AND MAINTENANCE EXPENSES
Years Ended December 31, 2022 and 2021

	2022	2021
Contract labor	\$ 722,495	\$ 649,783
Repairs and maintenance	287,924	197,939
Wichita water purchases	4,070,945	3,355,916
Electric power	24,883	21,969
Other utilities	5,137	3,717
Office supplies and postage	21,345	14,601
Rentals/operating leases	14,300	14,300
Water treating supplies	9,014	-
Insurance	27,765	20,431
Professional fees	155,456	89,785
Dues and subscriptions	4,382	3,241
Other taxes	21	20
Miscellaneous	128,548	110,009
	\$ 5,472,215	\$ 4,481,711
Total		