BERGER & COMPANY
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KENTUCKY INFRASTRUCTURE AUTHORITY

FRANKFORT, KENTUCKY

FINANCIAL STATEMENTS AND
INDEPENDENT AUDITOR'S REPORT

June 30, 2006 and 2005

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KENTUCKY INFRASTRUCTURE AUTHORITY
FRANKFORT, KENTUCKY

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INDEPENDENT AUDITOR'S REPORT

To the Board of Directors
Kentucky Infrastructure Authority
Frankfort, Kentucky

We have audited the accompanying financial statements of the Kentucky Infrastructure Authority, a component unit of the Commonwealth of Kentucky, as of and for the year ended June 30, 2006, as listed in the table of contents. These financial statements are the responsibility of the Kentucky Infrastructure Authority's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As discussed in Note 1, the financial statements present only the Kentucky Infrastructure Authority and are not intended to present fairly the financial position of the Commonwealth of Kentucky and the results of its operations and cash flows of its proprietary fund types and nonexpendable trust funds in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Kentucky Infrastructure Authority, as of June 30, 2006, and the results of its operations and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with Government Auditing Standards, we have also issued our report dated November 14, 2006 on our consideration of the Kentucky Infrastructure Authority's internal control over financial reporting, and our tests of its compliance with certain laws, regulations, contracts and grants.

Our audit was performed for the purpose of forming an opinion on the financial statements of the Kentucky Infrastructure Authority, taken as a whole. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is not a required part of the financial statements. Such information has been subjected to the auditing procedures applied in the audit of the financial statements and, in our opinion, is fairly stated in all material respects in relation to the financial statements taken as a whole.

Berger & Company CPA PSC
Berger & Company, CPA, PSC
November 14, 2006

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Management's Discussion and Analysis

As management of the Kentucky Infrastructure Authority (the Authority), we offer readers of the Authority's financial statements this brief narrative overview and analysis of the financial activities of the Authority for the fiscal year ended June 30, 2006.

Financial Highlights

- As of the close of the current fiscal year, the Authority reported combined ending retained earnings of $549,718,278, an increase of $38,974,511 in comparison with the prior year.
- The Authority's total debt decreased by $14,575,000 (7.8%) during the current fiscal year. The only factor in this decrease was the payment of principal that was due. There were no new bond issues by the Authority for state general fund supported debt or program revenue supported debt.
- The Authority disbursed $38,404,458 to borrowers for assistance agreements and $58,823,315 to local governmental entities in state grants. Principal and interest in the amount of $39,608,066 was collected from borrowers for assistance agreements.

Overview of the Financial Statements

This discussion and analysis are intended to serve as an introduction to the Authority's basic financial statements. The Authority's basic financial statements comprise two components: 1) proprietary fund financial statements, and 2) notes to the financial statement. This report also contains other supplementary information in addition to the basic financial statements themselves.

Proprietary Fund Financial Statements. The proprietary fund financial statements are designed to provide readers with a broad overview of the Authority's finances, in a manner similar to a private-sector business. The Authority is a proprietary fund component unit of the Commonwealth of Kentucky.

The proprietary fund financial statements can be found on pages 7-10 of this report.

Notes To The Financial Statements. The notes provide additional information that is essential to a full understanding of the data provided in the proprietary fund financial statements. The notes to the financial statements can be found on pages 11-23 of this report.

Other information. In addition to the basic financial statements and accompanying notes, this report also presents the schedule of expenditure of federal awards, together with related notes, as required by the Single Audit Act Amendments of 1996. The schedule of expenditure of federal awards and related notes can be found on pages 24-25 of this report.

Individual fund statements and schedules can be found on pages 27-30 of this report.

Proprietary Fund Financial Analysis

Retained Earnings. The Authority's combined retained earnings increased 7.63% between fiscal years 2005 and 2006 to $549,718,278 (See Table A-1.) despite an operating loss of $53,772,724 (See Table A-2) which resulted from increased expenditures related to initiatives set forth in SB409 from the 2000 General Assembly for which no additional revenue was provided, and the

increased number of grant expenditures as opposed to loans. Until the 2005 General Assembly, no source of administrative fee was provided to administer grants. In addition, the Authority administered numerous water and sewer grants funded by single county coal severance tax receipts that were assigned to the Governor's Office for Local Development. The Authority received no increase in state appropriation to cover the cost of project administration. The Governor's Office for Local Development, in the Comprehensive Annual Financial Report, reports expenditures for these grants for the Commonwealth of Kentucky.

Federal grant revenue decreased 1.66 percent due to the number of large projects in the Drinking Water State Revolving Fund that have other funding sources included with Authority funds. Entities with grant money included in the funding packet would normally draw grant funds first to reduce interest costs of the project. Investment interest income increased 22 percent to $9,634,763.

Table A-1
Kentucky Infrastructure Authority's Retained Earnings

	Total		Total Percentage Change
	2005	2006	2005-2006
Current Assets	166,446,764	167,315,387	0.52%
Equipment (Net)	0	0	0.00%
Long Term Investment	136,987,085	154,314,683	12.65%
Long Term Receivables (Net)	393,574,241	400,698,926	1.81%
Other Assets	1,664,400	1,522,730	-8.51%
Total Assets	698,672,490	723,851,726	3.60%
Current Liabilities	15,719,708	16,478,208	4.83%
Long Term Liabilities	172,209,015	157,655,240	-8.45%
Total Liabilities	187,928,723	174,133,448	-7.34%
Restricted Retained Earnings	510,743,767	549,718,278	7.63%
Total Liabilities & RE	698,672,490	723,851,726	3.60%

Table A-2
Changes in Kentucky Infrastructure Authority's Retained Earnings

	Total		Total Percentage Change
	2005	2006	2005-2006
Program revenues			
Assistance agreements	11,250,202	10,475,730	-6.88%
Grant Admin Fees	0	303,143	100.00%
General revenues			
Interest	7,885,809	9,634,763	22.18%

Net inc (dec) in FMV investments	-1,589,873	-1,573,812	-1.01%
Other	2,394	0	-100.00%
Total Revenues	17,548,532	18,839,824	
Expenses			
Clean Water SRF (Fund A)	2,769,874	2,429,810	-12.28%
Infrastructure Revolving (Fund B)	60,033,184	65,493,745	9.10%
Governmental Agencies (Fund C)	3,063,878	1,714,432	-44.04%
Solid Waste (Fund E)	541,015	284,675	-47.38%
Drinking Water SRF (Fund F)	1,994,657	2,689,886	34.85%
Total Expenses	68,402,608	72,612,548	6.15%
Operating Income (Loss)	-50,854,076	-53,772,724	5.74%
Federal grants	27,114,227	26,664,604	-1.66%
Excess (deficiency) before special items and transfers	-23,739,849	-27,108,120	14.19%
Transfer to State General Fund	0	-3,600,000	100.00%
State Appropriation	6,853,702	51,512,019	651.59%
Gain on Sale of Investment	1,875,214	0	-100.00%
Transfers for debt service	18,193,154	18,170,612	-0.12%
Net Income	3,182,221	38,974,511	1124.76%

Long-term Debt

At year-end, the Authority had $172,385,000 in bonds outstanding – a decrease of 7.8 percent from last year – as shown in Table A-3. More detailed information about the Authority's long-term liabilities is presented in Note 8 to the financial statements.

There was no new debt issued during the year.

Bond Ratings. The Authority's appropriation supported debt rating is A+ from Standard & Poor's, AA- from Fitch and Aa3 from Moody's. This is one step below the Commonwealth's general obligation credit rating of AA- and Aa2. Standard & Poor's upgraded the revenue bonds of the Authority to AA based on the restructuring of the program.

Limitations on Debt. The Authority is required by KRS 56.870(1) to obtain General Assembly approval for issuance of general fund appropriation supported debt. For debt related to issues that require no appropriation of state funds, General Assembly approval must be obtained for bonds or notes having a final maturity extending beyond three (3) years, if the aggregate principal amount of the bonds or notes outstanding under any trust indenture or bond resolution exceeds the sum of one hundred twenty-five million dollars ($125,000,000). Our outstanding debt in the Fund C program, which meets this criterion, is significantly below this limit.

Table A-3
Kentucky Infrastructure Authority's Outstanding Debt

	Total 2005	Total 2006	Total Percentage Change 2005-2006
General fund appropriation supported debt	143,445,000	132,285,000	-7.78%
Program revenue supported debt	43,515,000	40,100,000	-7.85%
Total	186,960,000	172,385,000	-7.80%

Items Expected to have a Significant Impact on Future Financial Position

In the coming year, the Authority will continue to administer the remainder of water and sewer related projects funded through coal severance tax receipts, in addition to a significant number appropriated by the General Assembly in the 2005 session, in order to provide a single state agency contact for the industry. While the Governor's Office for Local Development will actually disburse funds, the Authority will provide project administration activities. There has been no increase in state appropriation to cover administrative costs including staff.

The 2002 General Assembly abolished the legal authority for the Authority's solid waste program. Authority staff is in the process of requesting re-establishment of the program.

The 2003 General Assembly identified 267 projects totaling $59,071,343 for tobacco impacted counties and $54,861,998 for coal producing counties to be disbursed and administered by KIA as grants from proceeds of bonds in the amount of $54,765,000 (first year debt service to be paid from tobacco settlement funds) and $54,765,000 (first year debt service to be paid from multi-county coal severance tax receipts). There was no increase in state appropriation to cover the cost of administering these projects. At the end of FY2006, approximately $37 million remained to be disbursed to grantees. Disbursement will occur over the next several years and the projects will require on-going project administration services.

The 2005 General Assembly identified 500 projects totaling $120,660,220 for tobacco impacted counties and $79,395,960 for coal producing counties to be disbursed and administered by KIA as grants from proceeds of bonds to be issued by the Commonwealth's State Property and Buildings Commission. There was allowance for an administrative fee of ½ of one percent of each grant to cover the cost of administering these projects. At the end of FY2006, approximately $168 million remained to be disbursed to grantees. Disbursement will occur over the next several years and the projects will require on-going project administration services.

The 2006 General Assembly identified 559 projects totaling $151,250,000 (corresponding appropriation of $150 million) for non-coal producing counties and $100,955,072 (corresponding appropriation of $100 million) for coal producing counties to be disbursed and administered by KIA as grants from proceeds of bonds to be issued by the Commonwealth's State Property and Buildings Commission. There was allowance for an

administrative fee of ½ of one percent of each grant to cover the cost of administering these projects. At the end of FY2006, no funds had been disbursed to grantees. Disbursement will occur over the next several years and the projects will require on-going project administration services.

Although progress has been made, Authority staff will continue to facilitate streamlining activities in the federally assisted wastewater and drinking water programs. Streamlining efforts consists of elimination of unnecessary steps and paperwork, and modification of planning processes, which will speed processing times and move projects more quickly through the system.

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Contacting the Kentucky Infrastructure Authority's Financial Management

This financial report is designed to provide our legislators, citizens, taxpayers, customers, and federal government officials, as well as, investors and creditors with a general overview of the Authority's finances and to demonstrate the Authority's accountability for the money it receives. If you have questions about this report or need additional financial information, contact Kentucky Infrastructure Authority, Fiscal Officer, 1024 Capital Center Drive, Suite 340, Frankfort, Kentucky, 40601.

KENTUCKY INFRASTRUCTURE AUTHORITY
BALANCE SHEETS
JUNE 30, 2006 AND 2005

ASSETS

	2006	2005
Current assets:		
Cash and cash equivalents	$ 46,759,989	$ 61,928,627
Investments, current portion	90,226,579	75,857,493
Federal Funds Receivable	630,441	539,017
Accrued interest receivable, investments	3,849,386	2,911,223
Accrued interest receivable, loans	1,186,961	1,309,558
Current maturities of long-term receivables	24,662,031	23,900,846
Total current assets	167,315,387	166,446,764
Equipment, Net of Accumulated Depreciation (Note 10)	-	-
Investments	154,314,683	136,987,085
Long-term receivables:		
Assistance agreements receivable:		
Principal	427,072,440	418,609,640
Less:		
Current maturities	(24,662,031)	(23,900,846)
Deposit reserve	(702,490)	(58,031)
Unamortized discounts	(980,878)	(1,048,407)
Funds held for governmental agencies	(28,115)	(28,115)
Total long-term receivables	400,698,926	393,574,241
Other assets:		
Unamortized costs of issuance	1,522,730	1,664,400
Total assets	$ 723,851,726	$ 698,672,490

See accompanying notes.

KENTUCKY INFRASTRUCTURE AUTHORITY
BALANCE SHEETS
JUNE 30, 2006 AND 2005

LIABILITIES AND RETAINED EARNINGS

	2006	2005
Current Liabilities		
Current maturities of revenue bonds payable, less unamortized discounts, premiums and deferred loss on early retirement of debt	$ 14,554,741	$ 14,281,748
Accrued interest payable	1,268,765	1,361,309
Due to Division of Water	630,441	52,390
Due to Governors Office of Local Development	13,697	13,697
Other payables	10,564	10,564
Total current liabilities	16,478,208	15,719,708
Long-term debt:		
Revenue bonds payable, less current maturities and net of unamortized discounts, premiums and deferred loss on early retirement of debt	157,655,240	172,209,015
Total long-term debt	157,655,240	172,209,015
Total liabilities	174,133,448	187,928,723
Retained Earnings		
Invested in Capital Assets net of related debt of $0	-	-
Restricted (Note 11)	549,718,278	510,743,767
Total retained earnings	549,718,278	510,743,767
Total liabilities and retained earnings	$ 723,851,726	$ 698,672,490

See accompanying notes.

KENTUCKY INFRASTRUCTURE AUTHORITY
STATEMENTS OF REVENUES, EXPENSES
AND CHANGES IN RETAINED EARNINGS
Years ended June 30, 2006 and 2005

	2006	2005
Operating revenues:		
Assistance agreements:		
Servicing fee	$ 758,406	$ 751,967
Interest	7,756,245	8,039,522
Interest Received Securing Revenue Bonds	1,787,567	2,186,253
Amortization of discount	108,142	197,064
Grant Admin Fees	303,143	
Amortization of bond premiums	65,370	75,396
Income from investments	9,634,763	7,885,809
Miscellaneous Income		2,394
Net increase (decrease) in fair market value of investments	(1,573,812)	(1,589,873)
Total operating revenues	18,839,824	17,548,532
Operating expenses:		
General and administrative	2,565,006	2,988,708
Intergovernmental administrative expense reimbursement	1,959,016	1,190,616
Grants	58,823,315	53,096,331
Depreciation		16,857
Revenue bonds payable:		
Amortization of discount	33,197	37,008
Amortization of costs of issuance	141,671	161,656
Interest on reserves	-	1,145,287
Interest	9,090,343	9,766,145
Total operating expenses	72,612,548	68,402,608
Operating income (loss)	(53,772,724)	(50,854,076)
Nonoperating revenues:		
Federal grants and reimbursements	26,664,604	27,114,227
Income (loss) before operating transfers	(27,108,120)	(23,739,849)
Operating transfers to State general fund	(3,600,000)	
Gain (Loss) on Sale of Investments	-	1,875,214
State Appropriation	51,512,019	6,853,702
Operating transfers in for debt service	18,170,612	18,193,154
Net income	38,974,511	3,182,221
Retained earnings, beginning of year	510,743,767	507,561,546
Retained earnings at end of year	$ 549,718,278	$ 510,743,767

See accompanying notes.

KENTUCKY INFRASTRUCTURE AUTHORIT
STATEMENTS OF CASH FLOWS
Years ended June 30, 2006 and 2005

	2006	2005
Cash flows from operating activities:		
Cash received from customers	$ 758,406	$ 751,967
Collections on assistance agreements	29,941,657	22,784,316
Advances on assistance agreements	(38,404,458)	(34,516,639)
Grants	(58,823,315)	(53,096,331)
Grant Admin Fees Received	303,143	
Miscellaneous income		2,394
Interest received on loans	9,666,409	10,066,681
Cash payments to suppliers for goods and services	(3,945,971)	(4,429,644)
Net cash used in operating activities	(60,504,129)	(58,437,256)
Cash flows from noncapital financing activities:		
Proceeds from the issuance of revenue and revenue refunding bonds		43,015,000
Operating Transfer to State General Fund	(3,600,000)	
Receipt of grants, net	26,573,180	27,113,411
State appropriation for debt service	18,170,612	18,193,154
Receipt of State Appropriation	51,512,019	6,853,702
Receipt of Deposit Reserve Funds from borrowers	644,459	
Payment of Funds Held to borrowers		(72,030)
Receipt of bond premiums and accrued interest on bond proceeds		1,100,992
Payment of bond discount and costs of issuance		(635,211)
Payment to refund bond escrow agent		(54,433,264)
Principal payments on long-term debt	(14,575,000)	(15,010,000)
Interest paid on long-term debt	(9,182,887)	(9,888,278)
Net cash provided by noncapital financing activities	69,542,383	16,237,476
Cash flows from investing activities:		
Purchase of investment securities	(203,040,973)	(190,106,225)
Proceeds from sale and maturities of investment securities	170,137,481	202,663,569
Investment income received	8,696,600	6,537,037
Net cash provided by (used in) investing activities	(24,206,892)	19,094,381
Increase (decrease) in cash and cash equivalents	(15,168,638)	(23,105,399)
Cash and cash equivalents at beginning of year	61,928,627	85,034,026
Cash and cash equivalents at end of year	$ 46,759,989	$ 61,928,627
Reconciliation of operating income to net cash used in operating activities:		
Operating income	$ (53,772,724)	(50,854,076)
Adjustments to reconcile operating income to net cash used in operating activities:		
Amortization and Depreciation	174,868	215,521
Amortization of discount	(108,142)	(197,064)
Amortization of bond premium	(65,370)	(75,396)
Loan credits in restructuring deposit reserve (Note 6)		(15,746,246)
Investment Income	(9,634,763)	(7,885,809)
Interest expense	9,090,343	10,911,432
Net (increase) decrease in fair market value of investments	1,573,812	1,589,873
Change in assets and liabilities:		
Increase (decrease) in other payables	-	(108,951)
Decrease (increase) in accrued loan interest receivable	122,597	(159,094)
Increase (decrease) in due to Division of Water	578,051	(141,369)
Increase in assistance agreements receivable	(8,462,801)	4,013,923
Net cash used in operating activities	$ (60,504,129)	$ (58,437,256)

See accompanying notes.

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES

This summary of significant accounting policies of the Kentucky Infrastructure Authority is presented to assist in understanding the combined financial statements. The combined financial statements and notes are representations of the Kentucky Infrastructure Authority's management who is responsible for their integrity and objectivity. These accounting policies conform to accounting principles generally accepted in the United States of America and have been consistently applied in the preparation of the combined financial statements.

Basis of Presentation:

The financial statements of the Authority are accounted for on the accrual basis of accounting. Accordingly, revenues are recognized when they are earned and expenditures are recognized when they are incurred. The Authority applies all Governmental Accounting Standards Board (GASB) pronouncements as well as the Financial Accounting Standards Board (FASB) pronouncements issued on or before November 30, 1989, unless those FASB pronouncements conflict with or contradict GASB pronouncements. Furthermore, the Authority has adopted the provisions of GASB Statement No. 20, "Accounting and Financial Reporting for Proprietary Funds and Other Governmental Funds that use Proprietary Fund Accounting." As permitted by GASB Statement No. 20, the Authority 's enterprise funds have elected not to adopt FASB Statements or Interpretations issued after November 30, 1989, unless GASB specifically adopts such FASB Statements or Interpretations.

Use of Estimates:

Management uses estimates and assumptions in preparing the financial statements. Those estimates and assumptions affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities, and reported revenues and expenses.

Scope of Entity:

In 1972, the General Assembly of Kentucky established the Kentucky Pollution Abatement Authority after determining that pollution was seriously harming the Commonwealth's water resources and would, if unchecked, endanger the health, safety, welfare and well being of the public, and would also destroy the natural chemical, physical and biological integrity of the waters of the Commonwealth. The Act was also adopted to maximize federal grant participation in the Commonwealth in respect of works and facilities undertaken by local governmental units in the Commonwealth for the abatement of water pollution and to provide an alternate source of financing for local governmental units. The Act was amended in 1974 and 1978 (a) to remove the prior requirement that federal grant participation be obtained by local units of government as a condition precedent to Authority aid and (b) to grant to the Authority the power to issue tax-exempt industrial development bonds for pollution control facilities.

The General Assembly again amended the Act in 1984 (a) to grant to the Authority the ability to assist local government units with the implementation of water resource projects intended to conserve and develop the water resources of the Commonwealth, including, among other things, all aspects of water supply, flood damage abatements, navigation, water-related recreation and land conservation facilities and (b) to change the name of the Authority to the "Kentucky Pollution Abatement and Water Resources Finance Authority." In 1988, the Act was further amended to, among other things (a) broaden the scope of the Authority's powers to finance "infrastructure projects," (b) establish two revolving funds to assist in the financing of infrastructure projects and (c) change the name of the Authority to the "Kentucky Infrastructure Authority." A further amendment to the Act in 1990 provided for the establishment of (a) an additional revolving fund to assist in the financing of solid waste projects and (b) a solid waste grant fund, jointly administered with the Natural Resources Cabinet, intended to defray the capital costs associated with promotion of recycling and other similar solid waste management activities. Amendments to the Act in 2000 expanded the role of the Authority to include regional infrastructure planning coordination, promotion of higher levels of technical, managerial, and financial capacity of water-based utilities, as well as expanding the Authority's more traditional role of infrastructure financing for both governmental agencies and investor-owned, private utilities by adding a new account, the 2020 account, to its array of grant and subsidized loan programs.

Reorganization – Governor Ernie Fletcher issued an Executive Order which attached the Authority to the Governor's Office of Local Development for administrative purposes and transferred the administration of the Gas Systems Restoration and Development Project Account to the Authority. The Gas Systems Restoration and Development Project does not meet the criteria of a component unit and thus, no activity of the project is reflected in these financial statements. The project's activity is included in the Commonwealth's comprehensive annual financial report.

The Kentucky Infrastructure Authority is a component unit of the Commonwealth of Kentucky and is included in the Commonwealth of Kentucky's comprehensive annual financial report.

Investments:

The Authority adopted Statement No. 31 of the Governmental Accounting Standards Board, "Accounting for Certain Investments and for External Investment Pools" in 1998. Under Statement No. 31, all investments are valued at their fair values in the balance sheets. Unrealized gains and losses are included in the statements of revenues, expenses and changes in retained earnings.

Legally authorized investments generally include: obligations of or guaranteed by the United States; obligations of any corporation of the United States Government; asset-backed securities; U.S. dollar-denominated corporate securities; collateralized certificates of deposits; bankers' acceptances; commercial paper; and repurchase agreements.

Amortization of Discounts on Assistance Agreements:

Discounts on assistance agreement receivables are amortized using the straight-line method over the life of the related receivable.

Amortization of Bond Discount and Debt Issuance Costs:

Bond discounts and debt issuance costs are amortized on the straight-line method over the life of the bond issue.

Amortization of Deferred Loss on Early Retirement of Debt:

Deferred loss on early retirement of debt is amortized on the straight-line method over the original remaining life of the old debt or the life of the new debt, whichever is less.

Cash and Cash Equivalents and Statement of Cash Flows:

The Authority considers all highly liquid investments with a maturity of three months or less when purchased to be cash equivalents.

Operating Revenues and Expenses:

The Authority considers interest income received on loans to be operating revenue. In order not to overstate the income from operations, the Authority also includes the interest paid on bonds issued to fund such loans and investment interest received on the unspent proceeds of these bonds as operating income and expense as well. For the statement of cash flows, the Authority includes interest income received on loans as an operating receipt but lists investment interest income and bond interest paid as nonoperating items in order to match them in the same cash flow category with the corresponding bond principal or investment on the statement of cash flows.

Industrial Development Bonds:

The Authority has issued Pollution Control Revenue Bonds in accordance with the statutes governing the issuance of Industrial Revenue Bonds for various projects since 1980. These bonds do not constitute a general debt, liability or moral obligation of the Authority or the Commonwealth of Kentucky. Accordingly, these financial statements do not include any assets or liabilities related to the issuance of these bonds.

NOTE 2 - FUND DESCRIPTIONS

The Authority is authorized by KRS Chapter 224A to issue notes and bonds to provide loans to governmental agencies and private, investor-owned utilities in Kentucky. The provisions of KRS 224A.165 dictate certain limits on the amount of notes and bonds the authority can have outstanding. The purpose of the loans is to assist such entities in financing the construction of infrastructure projects. The following provides a description of the Authority's various programs:

Fund A - Waste Water Revolving Loan Program:

Local waste water treatment facilities that qualify under the U.S. Environmental Protection Agency requirements can be financed through this program. Jointly administered by the KIA and the Natural Resources Cabinet, loans will be provided at below-market interest rates with repayments not exceeding twenty years. The state's share of construction is funded with state appropriation-supported bonds. The Commonwealth appropriates an amount equal to this fund's debt service to make its bond payments.

Fund B - Infrastructure Revolving Loan Program:

This fund was established to provide financing for any type of infrastructure that will enhance economic development and job creation. Loans are made to governmental entities of the Commonwealth that are unable to finance a complete project through other public grant or loan programs, through commercial credit at reasonable rates, or from its own resources.

The loans will be at or below market interest rates and will not exceed thirty years. Grants are available, but are reserved for borrowers in which the Authority determines both a hardship and extreme health hazard exist. The Commonwealth appropriates an amount equal to this fund's debt service to make its bond payments.

As part of this program, a 2020 water service account has been established to assist in making potable water available to all Kentuckians by the year 2020. Loans or grants are made to utilities with emphasis on regionalization, uniform system of accounts and cost-based rates.

The General Assembly, from time to time, appropriates funds to be administered and disbursed by the Authority in the form of water and wastewater grants. During FY06, projects were being administered from the 2002 General Assembly and the 2005 General Assembly. Activities for these grants are accounted for in Fund B.

Fund C – Governmental Agencies Program:

This program provides local governmental agencies access to funding through the municipal bond market at better terms than could be obtained on an individual basis. Financial assistance is available on a loan basis for up to thirty years for any infrastructure

owned by governmental entities in the Commonwealth. The loans may be used to totally fund a construction project or they can be used to supplement grants or cash contributions.

Fund E - Solid Waste Revolving Loan Program:

This fund was established to assist local government units in the financing of solid waste projects. Financial assistance is available for the useful life of the project or thirty years, whichever is shorter. Grants are also available from this fund. Jointly administered by the Environmental and Public Protection Cabinet, the fund provides grants up to $75,000 per project per funding cycle to defray capital costs associated with solid waste management activities. The Commonwealth appropriates an amount equal to this fund's debt service to make its bond payments. There is no current authorization for new activity in this fund.

Fund F – Drinking Water Revolving Loan Fund

This fund was established to assist in financing local drinking water treatment and distribution facilities that qualify under U. S. Environmental Protection Agency (EPA) requirements. Projects must be recommended by the Kentucky Division of Water from the Project Priority List and must be financially feasible as determined by KIA staff. Loan funds are available on short terms for planning and preliminary design work. The state's share of construction is funded with state appropriation-supported bonds. The Commonwealth appropriates an amount equal to this fund's debt service to make its bond payments.

NOTE 3 - REVENUE BOND FUND ACCOUNTS

Components of the Revenue Bond Fund accounts by cash, cash equivalents and investments at June 30, 2006 are summarized below:

	Cash and Cash Equivalents	Investments	Total
Operating fund	$ 1,181,828	$ 2,819,994	$ 4,001,822
Revolving fund	28,410,531	151,528,525	179,939,056
Government agency fund	9,912,802	10,908,997	20,821,799
Debt service reserve fund	229	6,096,108	6,096,337
Debt service fund	3,900,855	-	3,900,855
Revenue fund	52,506	-	52,506
Surplus fund	1,175,450	16,226,362	17,401,812
Rebate fund	86	-	86
Cash in State System	2,125,702	56,961,276	59,086,978
Total	$ 46,759,989	$ 244,541,262	$ 291,301,251

Components of the Revenue Bond Fund accounts by cash, cash equivalents and investments at June 30, 2005 are summarized below:

	Cash and Cash Equivalents	Investments	Total
Operating fund	$ 773,961	$ 2,361,479	$ 3,135,440
Revolving fund	38,268,448	116,873,887	155,142,335
Government agency fund	16,388,257	12,898,660	29,286,917
Debt service reserve fund	147,424	6,096,108	6,243,532
Debt service fund	3,832,520	-	3,832,520
Revenue fund	58,226	-	58,226
Surplus fund	1,710,655	15,186,711	16,897,366
Rebate fund	86	-	86
Cash in State System	749,050	59,427,733	60,176,783
Total	$ 61,928,627	$212,844,578	$ 274,773,205

Trust indentures contain provisions which establish that specific accounts be maintained by the Authority to properly account for the financial activities as described below:

A. Operating Fund

Designated for paying operating costs incurred by the Authority.

B. Revolving Fund

Designated to receive debt service payments from the revolving loan program in order to recycle money for new loans.

C. Government Agency Fund

Designated for funds invested during the construction phase of new loans. The money is disbursed under the direction of the Authority in accordance with the loan assistance agreement.

D. Debt Service Reserve Fund

Designated as an allowance or reserve for the payment of principal and interest on revenue bonds as to which there would otherwise be a default in payment.

E. Debt Service Fund

Funds designated for the sole purpose of paying principal and interest on revenue bonds payable as they come due.

F. Revenue Fund

Designated for receipt of principal and interest payments from governmental agencies and which are subsequently transferred to the Debt Service Fund or other funds as needed.

G. Surplus Fund

This fund is a reserve for the 1989 Series A refunding issue, used for advances to municipalities in anticipation of new bond issues, and also used for transfers to other funds to cover deficiencies.

H. Rebate Fund

Funds designated for the purpose of paying anticipated liabilities due to municipalities based on excess earnings of specific bond issues.

I. Cost of Issuance Fund

Upon issuance, a portion of the proceeds is set aside to pay the cost associated with the issue (attorneys' fees, etc.). After all fees are paid, any remaining funds are transferred to the Bond or Note Payment Fund.

J. Capitalized Interest Fund

Funds designated for the purpose of paying capitalized interest associated with the revenue bond and bond anticipation notes.

K. Project Fund

Funds designated for the purpose of construction projects associated with the issuance of revenue bond anticipation notes.

NOTE 4 - CASH AND CASH EQUIVALENTS AND INVESTMENTS

Cash and Cash Equivalents

All of the Authority's cash that is outside the State system is either insured or collateralized. All deposits exceeding the federal deposit insurance coverage level are collateralized with securities held by the financial institution's trust department in the Authority's name. The Authority's policy regarding custodial credit risk for deposits is the same as that for the State of Kentucky.

The carrying amount of the Authority's deposits were $46,759,989 and $61,928,627 at June 30, 2006 and June 30, 2005, respectively, which equaled the bank balance. There were no differences between the bank balance and the carrying amount since checks of the Authority are paid through the State system and are debited from the Authority's cash balance as they are written.

Cash and cash equivalents of the Authority at June 30, 2006 and June 30, 2005 consisted of the following:

	June 30, 2006	June 30, 2005
U.S. Government-Backed Securities	$44,634,246	$ 61,179,577
Cash Deposited With State	2,125,743	749,050
Total	$46,759,989	$61,928,627

Investments

The investment policy of the Authority is the same as that of the Commonwealth of Kentucky. Legally authorized investments generally include obligations of or guaranteed by the United States of America; obligations of any corporation of the United States Government asset-backed securities; U.S. dollar-denominated corporate securities; collateralized certificates of deposit; bankers' acceptances; commercial paper and repurchase agreements. The Commonwealth is also eligible to invest in reverse repurchase agreements. For credit risk associated with the Authority's investments deposited with the State, see the Commonwealth's Comprehensive Annual Financial Report for the year ended June 30, 2006 for disclosure of the credit risk classifications of the cash and investment pool.

Interest Rate Risk: The Authority does not have a formal investment policy that limits investment maturities as a means of managing its exposure to fair value losses from increasing interest rates.

Credit Risk: The Authority's credit risk policy is the same as that found in the Commonwealth's Comprehensive Annual Financial Report for the year ended June 30, 2006.

At June 30, 2006 and June 30, 2005, the Authority's investment balances were as follows:

As of June 30, 2006:

Investment:	Fair Value	Maturity	Rate
Federal Home Loan Banks Debenture	4,061,555	10/15/2006	4.375
Fedeal Home Loan Banks	6,333,031	11/15/2006	2.75
FHLMC Debenture	5,087,501	12/15/2006	2.875
FNMAMTN	6,547,508	1/15/2007	5
Federal Home Loan Banks	30,824,813	1/18/2007	3.2
FHLMCMTN	10,694,924	3/15/2007	3.75
FNMAMTN	10,699,640	4/12/2007	2.9
Federal Home Loan Banks	10,643,832	5/15/2007	3.5
Federal Home Loan Banks	5,333,775	6/8/2007	3.875
FNMAMTN	5,371,822	7/6/2007	3.8
FHLMCMTN	8,872,055	8/15/2007	4.35
Federal Home Loan Banks	15,356,056	9/14/2007	4.25
FNMA Debenture	15,248,218	10/15/2007	6.625
Federal Home Loan Banks	15,599,475	11/15/2007	3.5
Federal Home Loan Banks	15,558,094	12/14/2007	4.5
FNMAMTN	5,407,827	1/15/2008	4.625
U.S. Treasury Sec Stripped Interest Payment	7,041,134	5/15/2008	N/A
U.S. Treasury Sec Stripped Interest Payment	40,775	11/15/2008	N/A
U.S. Treasury Sec Stripped Interest Payment	17,708	11/15/2009	N/A
U.S. Treasury Sec Stripped Interest Payment	92,613	11/15/2010	N/A
U.S. Treasury Sec Stripped Interest Payment	1,230,597	5/15/2011	N/A
U.S. Treasury Sec Stripped Interest Payment	220,912	11/15/2011	N/A
U.S. Treasury Sec Stripped Interest Payment	142,784	11/15/2012	N/A
U.S. Treasury Sec Stripped Interest Payment	1,057,223	5/15/2013	N/A
U.S. Treasury Notes State & Local Governments	2,300,215	8/1/2014	4.45
U.S. Treasury Notes State & Local Governments	1,314,791	8/1/2014	4.45
U.S. Treasury Notes State & Local Governments	2,481,108	8/1/2022	5.12
	187,579,986		
Investments in State System	56,961,276		
Total	244,541,262		
Less: Current Portion	(90,226,579)		
Long-Term Investments	$ 154,314,683		

As of June 30, 2005:

Investment:	Fair Value	Maturity	Rate
FNMA Debenture	$ 3,480,479	10/15/2005	2.875
Federal Home Loan Banks	3,781,172	11/15/2005	3.625
Federal Home Loan Banks	35,019,025	12/15/2005	2.5
FHLMC Debenture	4,502,517	1/15/2006	5.25
Federal Home Loan Banks	4,098,083	2/15/2006	5.375
Federal Home Loan Banks	4,128,364	3/6/2006	5.125
FHLMC Debenture	2,368,576	4/15/2006	2.375

FNMA Debenture	4,168,238	4/15/2006	2.125
Federal Home Loan Banks	3,862,388	5/15/2006	5.375
FNMA Debenture	4,252,681	6/15/2006	5.25
FHLMC Debenture	2,714,880	7/15/2006	5.5
Federal Home Loan Banks	8,202,468	8/15/2006	2.375
Federal Home Loan Banks	3,748,537	9/15/2006	2.875
FNMA Debenture	4,106,113	10/15/2006	4.375
Federal Home Loan Banks	6,301,057	11/15/2006	2.75
FHLMC Debenture	5,081,067	12/15/2006	2.875
FNMA Debenture	6,687,078	1/15/2007	5
Federal Home Loan Banks	30,922,516	1/18/2007	3.2
U.S. Treasury Notes State and Local Govt Series	1,314,791	8/1/2014	4.45
U.S. Treasury Notes State and Local Govt Series	2,481,108	8/1/2022	5.12
U.S. Treasury Notes State and Local Govt Series	2,300,209	8/1/2014	4.45
U.S. Treasury Sec Stripped Interest Payment	39,516	11/15/2005	N/A
U.S. Treasury Sec Stripped Interest Payment	6,980,723	5/15/2008	N/A
U.S. Treasury Sec Stripped Interest Payment	40,677	11/15/2008	N/A
U.S. Treasury Sec Stripped Interest Payment	17,906	11/15/2009	N/A
U.S. Treasury Sec Stripped Interest Payment	94,941	11/15/2010	N/A
U.S. Treasury Sec Stripped Interest Payment	1,251,253	5/15/2011	N/A
U.S. Treasury Sec Stripped Interest Payment	224,582	11/15/2011	N/A
U.S. Treasury Sec Stripped Interest Payment	148,076	11/15/2012	N/A
U.S. Treasury Sec Stripped Interest Payment	1,097,824	5/15/2013	N/A
	153,416,845		
Investments in State System	59,427,733		
Total	212,844,578		
Less: Current Portion	(75,857,493)		
Long-Term Investments	$ 136,987,085		

NOTE 5 - ASSISTANCE AGREEMENTS RECEIVABLE

Assistance agreements receivable are loans made to governmental entities for construction of infrastructure projects. The principal and interest are due in periodic installments used to either meet the principal and interest requirements of the Authority's revenue bonds or used to fund additional projects.

A total loan amount is approved for each governmental entity. In addition to the $427,072,440 in assistance agreements receivable at June 30, 2006, the Authority has commitments remaining to disburse funds summarized as follows:

Fund A - Waste Water Revolving Loan Program	$ 56,748,678
Fund B – Infrastructure Revolving Loan Program	8,253,465
Fund C - Governmental Agencies Program	1,564,971
Fund F – Drinking Water Revolving Loan Program	17,885,491
Total commitments outstanding	$ 84,452,605

NOTE 6 - DEPOSIT RESERVE

Because of the way in which maturities were structured in the bond issue that refunded all outstanding debt in the Fund C program in FY05, loans in the original 1993F series issue did not have level debt service. In an effort to create a fixed payment over the life of the loan, the borrowers are paying more than the required amount due in the early years of the loan repayments. The excess between the required amount due and the actual fixed payment amount is deposited into a deposit reserve account which will be used to pay the difference between the required payment and the actual payment in the later years of the loan repayment schedule. By providing the borrowers a fixed payment over the life of a loan, the Authority hopes to aid in the budgeting and cash flow management of the payees.

NOTE 7 - PRIOR YEARS' DEBT DEFEASANCE

In prior years, the Authority has defeased various bond issues by creating separate irrevocable trust funds. New debt has been issued and the proceeds have been used to purchase U.S. government securities that were placed in the trust funds. The investments and fixed earnings from the investments are sufficient to fully service the defeased debt until the debt is called or matures. For financial reporting purposes, the trust account assets and the liabilities for the defeased bonds has been considered defeased and therefore removed as a liability from the Authority's financial statements. The total amount of defeased debt from advance refunding that remains outstanding at June 30, 2006 is $20,495,000.

NOTE 8 - LONG-TERM DEBT REVENUE BONDS PAYABLE

The required annual payments for all debt for each of the next five fiscal years are as follows:

	INTEREST	PRINCIPAL	TOTAL
2007	$ 8,198,232	$ 14,840,000	$ 23,038,232
2008	7,552,222	15,515,000	23,067,222
2009	6,870,953	16,095,000	22,965,953
2010	6,162,167	14,025,000	20,187,167
2011	5,500,981	14,915,000	20,415,981
2012-2016	17,598,399	59,615,000	77,213,399
2017-2021	5,713,556	34,130,000	39,843,556
2022-2024	283,363	3,250,000	3,533,363
	$ 57,879,873	$ 172,385,000	$ 230,264,873

Long-term debt consists of the following:

Kentucky Infrastructure Authority Revenue Bonds:	June 30, 2006 Balance	Current	Long-term
Fund A, Waste Water Revolving Fund Revenue and Revenue Refunding Bonds, interest of 2.50% to 6.00%, due semi-annually, principal due annually to June 1, 2024	$38,390,000	$3,180,000	$35,210,000
Fund B, Infrastructure Revolving Fund Revenue Bonds, interest of 2.75% to 5.95%, due semi-annually, principal due annually to June 1, 2021	76,415,000	7,375,000	69,040,000
Fund C, Governmental Agencies Program Revenue and Revenue Refunding Bonds, interest of 2.25% to 5.5%, due semi-annually, principal due annually to August 1, 2022	40,100,000	3,150,000	36,950,000
Fund E, Solid Waste Revolving Fund Revenue Bonds, interest of 2.50% to 5.50%, due semi-annually, principal due annually to June 1, 2015	4,175,000	515,000	3,660,000
Fund F, Drinking Water Revolving Fund Revenue Bonds, interest of 3.00% to 6.00%, due semi-annually, principal due annually to June 1, 2024	13,305,000	620,000	12,685,000
	$ 172,385,000	$ 14,840,000	$ 157,545,000
Plus: Unamortized premiums	1,370,558	105,983	1,264,575
Less: Unamortized discounts	(168,797)	(24,238)	(144,559)
Unamortized deferred loss on early retirement of debt	(1,376,780)	(367,004)	(1,009,776)
	$ 172,209,981	$ 14,554,741	$ 157,655,240

Except for cash deposited with the State, all assets of the Authority are held by trustee banks. Most of these assets are pledged as collateral for bond indebtedness and have certain investment restrictions as outlined in the bond indentures.

NOTE 9 GRANT COMMITMENTS

KIA has committed to disburse grants as follows:

Fund	Amount
B	$ 1,955,975
B - 2020	$ 5,761,150
B - Coal Development	$ 16,465,464
B - Tobacco Development	$ 20,580,702
B - Coal IEDF	$ 65,444,280
B – Tobacco IEDF	$ 102,633,355

NOTE 10 – FIXED ASSETS

The Authority's policy is to capitalize purchases of assets over $5,000 with a useful life of more than one year. During the fiscal year ended June 30, 2006 there were no such purchases and thus, the historical cost of equipment did not change from the previous year. The Authority's fixed assets and accumulated depreciation did not increase from the prior year's balance of $84,288 since all assets are fully depreciated. The current year's depreciation expense is $0. The only capitalized assets consist of computer equipment which the Authority depreciated over five (5) years using the straight-line method.

NOTE 11 – RETAINED EARNINGS

Since the use of the Authority's resources is mandated by Kentucky Revised Statute 224A, the Authority considers all of its retained earnings to be restricted. However, the Authority does have significant latitude in how it uses much of its resources.

KENTUCKY INFRASTRUCTURE AUTHORITY

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

FOR THE YEAR ENDED JUNE 30, 2006

Grant Name	CFDA Number	Grant Period	Expenditures	Passed Through To Other Agencies (Including Revenue Redistributions)
U.S. Environmental Protection Agency				
Direct Programs:				
Capitalization Grants for Clean Water State Revolving Funds	66.458	10/2001 - 9/2006	5,740,037	
Capitalization Grants for Clean Water State Revolving Funds	66.458	10/2003 - 9/2006	9,880,745	
Capitalization Grants for Clean Water State Revolving Fund	66.458	9/2004 - 9/2008	3,120,000	245,384
Total Capitalization Grants for Clean Water State Revolving Fund			$ 18,740,782	$ 245,384
Direct Programs:				
Capitalization Grants for Drinking Water State Revolving Fund	66.468	9/1998 - 10/06		147,106
Capitalization Grants for Drinking Water State Revolving Fund	66.468	4/1999 - 9/06		19,213
Capitalization Grants for Drinking Water State Revolving Fund	66.468	10/00 - 9/05	4,158	
Capitalization Grants for Drinking Water State Revolving Fund	66.468	1/02 - 3/05		142,419
Capitalization Grants for Drinking Water State Revolving Fund	66.468	1/02 - 9/05	2,413,951	30,014
Capitalization Grants for Drinking Water State Revolving Fund	66.468	9/04 - 9/08	3,479,968	846,474
Capitalization Grants for Drinking Water State Revolving Fund	66.468	9/04 - 9/09	-	553,486
Total Capitalization Grants for Drinking Water State Revolving Funds			$ 5,898,077	$ 1,738,712
Total U. S. Environmental Protection Agency			$ 24,638,859	$ 1,984,096
Total All Programs			$ 24,638,859	$ 1,984,096

See notes to the schedule of expenditures of federal awards.

KENTUCKY INFRASTRUCTURE AUTHORITY
NOTES TO THE SUPPLEMENTARY SCHEDULE OF
EXPENDITURES OF FEDERAL AWARDS
Year ended June 30, 2006

NOTE 1 - BASIS OF ACCOUNTING

The supplementary schedule of expenditures of federal awards is presented on the modified cash basis of accounting.

NOTE 2 – PASSED THROUGH TO OTHER AGENCIES

CFDA #	Grant Name		Amount	Passed Through To Whom?
66.458	Clean Water State Revolving Funds	$	245,384	Environmental and Public Protection Cabinet
66.468	Drinking Water State Revolving Funds	$	1,738,712	Environmental and Public Protection Cabinet

BERGER & COMPANY
CPA, PSC

INDEPENDENT AUDITOR'S REPORT ON THE SUPPLEMENTAL INFORMATION

To the Board of Directors
Kentucky Infrastructure Authority
Frankfort, Kentucky

Our report on our audit of the basic financial statements of the Kentucky Infrastructure Authority for the year ended June 30, 2006 appears on page 1. Our audit was made for the purpose of forming an opinion on the basic financial statements taken as a whole. The supplemental information included in the schedules on pages 27 through 30 is presented for purposes of additional analysis and is not a required part of the financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the financial statements taken as a whole.

Berger + Company CPA PSC

Berger & Company, CPA, PSC
November 14, 2006

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KENTUCKY INFRASTRUCTURE AUTHORITY
COMBINING BALANCE SHEET
June 30, 2006

ASSETS

	Fund A	Fund B
Current assets:		
Cash and cash equivalents	$ 26,420,287	$ 13,069,420
Investments, current portion	72,287,710	8,585,947
Federal Funds Receivable	73,134	
Accrued interest receivable, investments	3,045,826	394,250
Accrued interest receivable, loans	509,282	251,744
Current maturities of long-term receivables	15,801,540	3,088,357
Total current assets	118,137,779	25,389,718
Equipment, Net of Accumulated Depreciation (Note 12)		
Investments	65,279,046	64,243,361
Long-term receivables:		
Assistance agreements receivable:		
Principal	260,261,152	49,369,265
Less:		
Current maturities	(15,801,540)	(3,088,357)
Deposit reserve		
Unamortized discounts/premiums		
Funds held for governmental agencies		
Total long-term receivables	244,459,612	46,280,908
Other assets:		
Unamortized costs of issuance	413,314	628,839
Total assets	$ 428,289,751	$ 136,542,826

LIABILITIES AND RETAINED EARNINGS

Current liabilities:		
Current maturities of revenue bonds payable, less unamortized discounts and deferred loss on early retirement of debt	$ 3,098,721	$ 7,106,344
Accrued interest payable	150,320	320,120
Due to Division of Water	73,134	
Due to Governor's Office of Local Development		13,697
Due to State GSRP	10,564	
Total current liabilities	3,332,739	7,440,161
Long-term debt:		
Revenue bonds payable, less current maturities and unamortized discounts and deferred loss on early retirement of debt	34,691,605	68,893,961
Total liabilities	38,024,344	76,334,122
Retained Earnings:		
Invested in Capital Assets net of related debt of $0		
Restricted (Note 13)	390,265,407	60,208,704
Total retained earnings	390,265,407	60,208,704
Total liabilities and retained earnings	$ 428,289,751	$ 136,542,826

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KENTUCKY INFRASTRUCTURE AUTHORITY
COMBINING STATEMENT OF REVENUES, EXPENSES AND
CHANGES IN RETAINED EARNINGS
Year ended June 30, 2006

	Fund A	Fund B
Operating revenues:		
Assistance agreements:		
Servicing fee	$ 447,127	$ 88,274
Interest	5,091,596	1,207,899
Interest Received Securing Revenue Bonds		
Amortization of loan premiums	37,809	
Grant Admin Fees		303,143
Amortization of bond premiums		64,666
Income from investments	5,466,701	3,030,310
Net increase (decrease) in fair market value of investments	(488,449)	(1,021,948)
Total operating revenues	10,554,784	3,672,344
Operating expenses:		
General and administrative	346,895	1,902,904
Intergovernmental administrative expense reimbursement		220,705
Grants		58,818,050
Revenue bonds payable:		
Amortization of discount	18,312	9,072
Amortization of costs of issuance	44,892	55,284
Interest	2,019,711	4,487,730
Total operating expenses	2,429,810	65,493,745
Operating income (loss)	8,124,974	(61,821,401)
Nonoperating revenues:		
Federal grants and reimbursements	19,028,216	
Net Income (loss) before operating transfers	27,153,190	(61,821,401)
Operating transfer to State General Fund		
State Appropriation		51,500,000
Operating transfers in for debt service	4,969,392	11,218,394
Net income (loss)	32,122,582	896,993
Retained earnings (deficit), beginning of year	358,142,825	59,311,711
Retained earnings (deficit) at end of year	$ 390,265,407	$ 60,208,704

	Fund C		Fund E		Fund F		Total
$	5,246,471	$	75,778	$	1,948,033	$	46,759,989
	3,691,532		100,986		5,560,404		90,226,579
					557,307		630,441
	169,306		4,465		235,539		3,849,386
	289,715		2,788		133,432		1,186,961
	3,272,638		218,597		2,280,899		24,662,031
	12,669,662		402,614		10,715,614		167,315,387
	19,270,808		504,185		5,017,283		154,314,683
	46,165,660		1,184,864		70,091,499		427,072,440
	(3,272,638)		(218,597)		(2,280,899)		(24,662,031)
	(702,490)						(702,490)
	(980,878)						(980,878)
	(28,115)						(28,115)
	41,181,539		966,267		67,810,600		400,698,926
	295,562		36,149		148,866		1,522,730
$	73,417,571	$	1,909,215	$	83,692,363	$	723,851,726
$	3,251,044	$	479,608	$	619,024	$	14,554,741
	727,292		16,911		54,122		1,268,765
					557,307		630,441
							13,697
							10,564
	3,978,336		496,519		1,230,453		16,478,208
	37,920,131		3,475,857		12,673,686		157,655,240
	41,898,467		3,972,376		13,904,139		174,133,448
	31,519,104		(2,063,161)		69,788,224		549,718,278
	31,519,104		(2,063,161)		69,788,224		549,718,278
$	73,417,571	$	1,909,215	$	83,692,363	$	723,851,726

Fund C	Fund E	Fund F	Total
$ 87,060	$ 3,055	$ 132,890	$ 758,406
	44,068	1,412,682	7,756,245
1,787,567			1,787,567
67,529	2,804		108,142
			303,143
		704	65,370
792,761	128,618	216,373	9,634,763
(37,244)	18,657	(44,828)	(1,573,812)
2,697,673	197,202	1,717,821	18,839,824
33,312	12,163	269,732	2,565,006
		1,738,311	1,959,016
	5,265		58,823,315
377	3,756	1,680	33,197
26,327	5,400	9,768	141,671
1,654,416	258,091	670,395	9,090,343
1,714,432	284,675	2,689,886	72,612,548
983,241	(87,473)	(972,065)	(53,772,724)
		7,636,388	26,664,604
983,241	(87,473)	6,664,323	(27,108,120)
	(3,600,000)		(3,600,000)
	12,019		51,512,019
	715,535	1,267,291	18,170,612
983,241	(2,959,919)	7,931,614	38,974,511
30,535,863	896,758	61,856,610	510,743,767
$ 31,519,104	$ (2,063,161)	69,788,224	$ 549,718,278

BERGER & COMPANY
CPA, PSC

REPORT ON COMPLIANCE AND ON INTERNAL CONTROL OVER FINANCIAL REPORTING BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS

To the Board of Directors
Kentucky Infrastructure Authority
Frankfort, Kentucky

We have audited the financial statements of the Kentucky Infrastructure Authority as of and for the year ended June 30, 2006, and have issued our report thereon dated November 14, 2006. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Compliance

As part of obtaining reasonable assurance about whether the Kentucky Infrastructure Authority's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, 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 that are required to be reported under *Government Auditing Standards*.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Kentucky Infrastructure Authority's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses.

This report is intended for the information of the Board of Directors, management, the Auditor of Public Accounts of the Commonwealth of Kentucky, and federal awarding agencies and passthrough entities and is not intended to be and should not be used by anyone other than these specified parties.

Berger + Company CPA PSC

Berger & Company, CPA, PSC
November 14, 2006

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BERGER & COMPANY
CPA, PSC

REPORT ON COMPLIANCE WITH REQUIREMENTS APPLICABLE TO EACH MAJOR PROGRAM AND INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133

To the Board of Directors
Kentucky Infrastructure Authority
Frankfort, Kentucky

Compliance

We have audited the compliance of the Kentucky Infrastructure Authority with the types of compliance requirements described in the U. S. Office of Management and Budget (OMB) Circular 33 Compliance Supplement that are applicable to its major federal programs for the year ended June 30, 2006. The Kentucky Infrastructure Authority's major federal programs are identified in the Summary of Auditor's Results section of the accompanying Schedule of Findings and Questioned Costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to its major federal program is the responsibility of the Kentucky Infrastructure Authority's management. Our responsibility is to express an opinion on the Kentucky Infrastructure Authority's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by Comptroller General of the United States; and OMB Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the Kentucky Infrastructure Authority's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on the Kentucky Infrastructure Authority's compliance with those requirements.

In our opinion, the Kentucky Infrastructure Authority complied, in all material respects, with the requirements referred to above that are applicable to its major federal programs for the year ended June 30, 2006.

Internal Control Over Compliance

The management of the Kentucky infrastructure Authority is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts and grants applicable to federal programs. In planning and performing our audit, we considered the Authority's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133.

Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that noncompliance with applicable requirements of laws, regulations, contracts and grants that would be material in relation to a major federal program being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over compliance and its operation that we consider to be material weaknesses.

This report is intended for the information of the Board of Directors, management, the Auditor of Public Accounts of the Commonwealth of Kentucky, and federal awarding agencies and passthrough entities. However, this report is a matter of public record and its distribution is not limited.

Berger + Company CPA PSC

Berger & Company, CPA, PSC
November 14, 2006

KENTUCKY INFRASTRUCTURE AUTHORITY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
Year ended June 30, 2006

Summary of Auditor's Results

We have issued an unqualified opinion, dated November 14, 2006, on the financial statements of Kentucky Infrastructure Authority as of and for the year ended June 30, 2006.

Our audit disclosed no instances of noncompliance which are material to the Kentucky Infrastructure Authority's financial statements.

We have issued an unqualified opinion, dated November 14, 2006, on the Kentucky Infrastructure Authority's compliance for major programs.

Our audit disclosed no findings required to be reported under the provisions of OMB Circular A-133.

The Kentucky Infrastructure Authority's major federal programs for the year ended June 30, 2006, were the U.S. Environmental Protection Agency, CFDA Numbers 66.458 and 66.468.

The Kentucky Infrastructure Authority qualified as a low-risk auditee under the provisions of OMB Circular A-133.

Findings Relating to the Financial Statements

Our audit disclosed no findings which are required to be reported in accordance with *Governmental Auditing Standards.*

Findings and Questioned Costs for Federal Awards

Our audit disclosed no findings or questioned costs for federal awards as defined by OMB Circular A-133.

KENTUCKY INFRASTRUCTURE AUTHORITY
SCHEDULE OF PRIOR AUDIT FINDINGS AND THEIR RESOLUTIONS
Year ended June 30, 2006

The prior-year's audit disclosed no findings which are required to be reported in accordance with *Government Auditing Standards*.