



**KENTUCKY INFRASTRUCTURE AUTHORITY**

FRANKFORT, KENTUCKY

**FINANCIAL STATEMENTS AND  
INDEPENDENT AUDITOR'S REPORT**

June 30, 2005 and 2004

**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, 2005, 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.

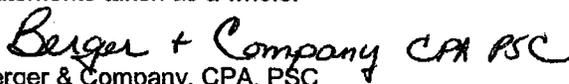
We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan 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, 2005, 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 October 31, 2005, 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  
October 31, 2005

## **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, 2005.

### **Financial Highlights**

- As of the close of the current fiscal year, the Authority reported combined ending retained earnings of \$510,743,767, an increase of \$3,182,221 in comparison with the prior year.
- The Authority's total debt decreased by \$23,508,812 (11.2%) during the current fiscal year. The key factor in this decrease was the restructure of the Governmental Agencies Fund Program (Fund C) with a new bond indenture. Issuance of the Series 2004A Revenue Refunding and Improvement Bonds and the Series 2004B Taxable Revenue Bonds together with cash from the previous indenture allowed the Authority to give borrowers credit for the reserve portion of loans, and pass savings to most borrowers. The Authority is in the process of reviewing program guidelines to enhance benefits and create incentives for local use of this loan fund. There were no new bond issues for State General Fund supported debt.
- The Authority disbursed \$34,516,639 to borrowers for assistance agreements and \$53,096,331 to local governmental entities in state grants. Principal and interest in the amount of \$48,756,339 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.

#### **Overview of the Financial Statements**

**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 11-22 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 26-27 of this report.

Individual fund statements and schedules can be found on pages 28-32 of this report.

Proprietary Fund Financial Analysis

Retained Earnings. The Authority's combined retained earnings increased .63% between fiscal years 2004 and 2005 to \$510,743,767 (See Table A-1.) despite an operating loss of \$50,854,076 (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 increased 26.19 percent due to the increased number of loans (more than double) approved by the Board in FY2004 over FY2003 for the Waste Water Revolving Loan Program. The increase in number of loans approved in the prior year increased the amount of funds drawn by borrowers to build infrastructure. The number of loans approved by the Board for the Drinking Water Revolving Loan Program remained constant. Investment interest income increased 29 percent to \$7,885,809 despite a decrease in cash and investment due to rising interest rates as market conditions improve.

Table A-1  
Kentucky Infrastructure Authority's Retained Earnings

	Total	Total Percentage	
	2004	Change	
	2005	2004-2005	
Current Assets	157,967,921	166,446,764	5.37%
Equipment (Net)	16,858	0	-100.00%
Long Term Investment	179,227,501	136,987,085	-23.57%
Long Term Receivables (Net)	381,492,193	393,574,241	3.17%
Other Assets	1,958,553	1,664,400	-15.02%
Total Assets	<u>720,663,026</u>	<u>698,672,490</u>	-3.05%
Current Liabilities	18,176,863	15,719,708	-13.52%
Long Term Liabilities	194,924,617	172,209,015	-11.65%
Total Liabilities	<u>213,101,480</u>	<u>187,928,723</u>	-11.81%
Retained Earnings	507,561,546	510,743,767	0.63%
Total Liabilities & RE	<u>720,663,026</u>	<u>698,672,490</u>	-3.05%

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

	Total		Total Percentage Change 2004-2005
	2004	2005	
<b>Program revenues</b>			
Assistance agreements	12,908,688	11,250,202	-12.85%
<b>General revenues</b>			
Interest	6,113,550	7,885,809	28.99%
Net inc (dec) in FMV investments	-4,681,463	-1,589,873	-66.04%
Other	25,152	2,394	-90.48%
<b>Total Revenues</b>	<u>14,365,927</u>	<u>17,548,532</u>	
<b>Expenses</b>			
Clean Water SRF (Fund A )	2,602,333	2,769,874	6.44%
Infrastructure Revolving (Fund B)	51,353,177	60,033,184	16.90%
Governmental Agencies (Fund C)	3,238,887	3,063,878	-5.40%
Solid Waste (Fund E)	1,086,302	541,015	-50.20%
Drinking Water SRF (Fund F)	1,981,620	1,994,657	0.66%
<b>Total Expenses</b>	<u>60,262,319</u>	<u>68,402,608</u>	13.51%
<b>Operating Income (Loss)</b>	-45,896,392	-50,854,076	10.80%
<b>Federal grants</b>	21,486,086	27,114,227	26.19%
<b>Excess (deficiency) before special items and transfers</b>	-24,410,306	-23,739,849	-2.75%
<b>Transfer to State General Fund</b>	-1,000,000	0	-100.00%
<b>State Appropriation</b>	109,530,000	6,853,702	-93.74%
<b>Gain on Sale of Investment</b>	0	1,875,214	100.00%
<b>Transfers for debt service</b>	17,298,682	18,193,154	5.17%
<b>Net Income</b>	<u>101,418,376</u>	<u>3,182,221</u>	-96.86%

### Long-term Debt

At year-end, the Authority had \$186,960,000 in bonds outstanding – a decrease of 11.86 percent from last year – as shown in Table A-3. More detailed information about the Authority's long-term liabilities is presented in Note 6 to the financial statements.

New debt resulted from issuing bonds to refund (either current or advance) all outstanding debt of the Governmental Agencies Program (Fund C) in order to restructure the program. The amount of new debt issued was \$43,015,000.

**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		Total Percentage Change
	2004	2005	2004-2005
General fund appropriation supported debt	154,205,000	143,445,000	-6.98%
Program revenue supported debt	57,910,000	43,515,000	-24.86%
Total	<u>212,115,000</u>	<u>186,960,000</u>	-11.86%

### 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 FY2005, approximately \$57.4 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 FY2005, no funds have been disbursed to grantees. Disbursement will occur over the next several years and the projects will require on-going project administration services.

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. Please note during FY2005, the Authority moved its offices from the former location. 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, 2005 AND 2004**

ASSETS

	<u>2005</u>	<u>2004</u>
Current assets:		
Cash and cash equivalents	\$ 61,928,627	\$ 85,034,826
Investments, current portion	75,857,493	46,174,421
Federal Funds Receivable	539,017	538,201
Accrued interest receivable, investments	2,911,223	1,562,451
Accrued interest receivable, loans	1,309,558	1,150,464
Current maturities of long-term receivables	23,900,846	23,900,846
Total current assets	<u>166,446,764</u>	<u>158,361,209</u>
Equipment, Net of Accumulated Depreciation (Note 12)		<u>16,858</u>
Investments	<u>136,987,085</u>	<u>179,227,501</u>
Long-term receivables:		
Assistance agreements receivable:		
Principal	418,609,640	422,623,564
Less:		
Current maturities	(23,900,846)	(23,900,846)
Deposit reserve	(58,031)	(13,031,268)
Unamortized discounts	(1,048,407)	(4,492,400)
Funds held for governmental agencies	(28,115)	(100,145)
Total long-term receivables	<u>393,574,241</u>	<u>381,098,905</u>
Other assets:		
Unamortized costs of issuance	<u>1,664,400</u>	<u>1,958,553</u>
Total assets	<u>\$ 698,672,490</u>	<u>\$ 720,663,026</u>

**KENTUCKY INFRASTRUCTURE AUTHORITY  
BALANCE SHEETS  
JUNE 30, 2005 AND 2004**

**LIABILITIES AND RETAINED EARNINGS**

	<u>2005</u>	<u>2004</u>
<b>Current Liabilities</b>		
Current maturities of revenue bonds payable, less unamortized discounts, premiums and deferred loss on early retirement of debt	\$ 14,281,748	\$ 15,074,958
Accrued interest payable	1,361,309	1,788,631
Due to Division of Water	52,390	193,759
Due to Commonwealth of Kentucky General Fund		1,000,000
Due to Governors Office of Local Development	13,697	
Due to State GSRP	10,564	
Other payables		119,515
<b>Total current liabilities</b>	<u>15,719,708</u>	<u>18,176,863</u>
 <b>Long-term debt:</b>		
Revenue bonds payable, less current maturities and net of unamortized discounts, premiums and deferred loss on early retirement of debt	<u>172,209,015</u>	<u>194,924,617</u>
<b>Total long-term debt</b>	<u>172,209,015</u>	<u>194,924,617</u>
 <b>Total liabilities</b>	<u>187,928,723</u>	<u>213,101,480</u>
 <b>Retained Earnings</b>		
Invested in Capital Assets net of related debt of \$0		16,858
Restricted (Note 13)	<u>510,743,767</u>	<u>507,544,688</u>
<b>Total retained earnings</b>	<u>510,743,767</u>	<u>507,561,546</u>
 <b>Total liabilities and retained earnings</b>	<u>\$ 698,672,490</u>	<u>\$ 720,663,026</u>

**KENTUCKY INFRASTRUCTURE AUTHORITY**  
**STATEMENTS OF REVENUES, EXPENSES**  
**AND CHANGES IN RETAINED EARNINGS**  
Years ended June 30, 2005 and 2004

	<u>2005</u>	<u>2004</u>
<b>Operating revenues:</b>		
Assistance agreements:		
Servicing fee	\$ 751,967	\$ 733,536 ①
Interest	8,039,522	8,372,402 ①
Interest Received Securing Revenue Bonds	2,186,253	3,333,442 ①
Amortization of discount	197,064	403,344 ①
Amortization of bond premiums	75,396	65,964 ①
Income from investments	7,885,809	6,113,550 ②
Miscellaneous Income	2,394	25,152 ②
Net increase (decrease) in fair market value of investments	(1,589,873)	(4,681,463) ②
Total operating revenues	<u>17,548,532</u>	<u>14,365,927</u>
 <b>Operating expenses:</b>		
General and administrative	2,697,192	2,423,627
Intergovernmental administrative expense reimbursement	1,482,131	1,279,632
Grants	53,096,331	45,280,500
Depreciation	16,858	16,857
Revenue bonds payable:		
Amortization of discount	37,008	72,324
Amortization of costs of issuance	161,656	227,314
Interest on reserves	1,145,287	167,796
Interest	9,766,145	10,794,269
Total operating expenses	<u>68,402,608</u>	<u>60,262,319</u> Expenses
Operating income (loss)	(50,854,076)	(45,896,392)
 <b>Nonoperating revenues:</b>		
Federal grants and reimbursements	<u>27,114,227</u>	<u>21,486,086</u> ②
Income (loss) before operating transfers	(23,739,849)	(24,410,306)
Operating transfers to State general fund		(1,000,000)
Gain (Loss) on Sale of Investments	1,875,214	
State Appropriation	6,853,702	109,530,000
Operating transfers in for debt service	<u>18,193,154</u>	<u>17,298,682</u>
Net income	3,182,221	101,418,376
Retained earnings, beginning of year,	<u>507,561,546</u>	<u>406,143,170</u>
Retained earnings at end of year	<u>\$ 510,743,767</u>	<u>\$ 507,561,546</u>

*Change for law*

*op Grant / Gov*

See accompanying notes.

**KENTUCKY INFRASTRUCTURE AUTHORITY**  
**STATEMENTS OF CASH FLOWS**  
Years ended June 30, 2005 and 2004

	<u>2005</u>	<u>2004</u>
<b>Cash flows from operating activities:</b>		
Cash received from customers	\$ 751,967	\$ 733,536
Collections on assistance agreements	22,784,316	28,783,835
Advances on assistance agreements	(34,516,639)	(40,489,450)
Grants	(53,096,331)	(45,280,500)
Miscellaneous income	2,394	25,152
Interest received on loans	10,066,681	11,751,818
Cash payments to suppliers for goods and services	(4,429,644)	(3,930,864)
Net cash used in operating activities	<u>(58,437,256)</u>	<u>(48,406,473)</u>
<b>Cash flows from noncapital financing activities:</b>		
Proceeds from the issuance of revenue and revenue refunding bonds	43,015,000	11,300,000
Receipt of grants, net	27,113,411	21,479,966
State appropriation for debt service	18,193,154	17,298,682
Receipt of State Appropriation	6,853,702	109,530,000
Payment of Deposit Reserve to borrowers		(6,601,650)
Payment of Funds Held to borrowers	(72,030)	(1,087,991)
Receipt of bond premiums and accrued interest on bond proceeds	1,100,992	31,890
Payment of bond discount and costs of issuance	(635,211)	(72,546)
Payment to refund bond escrow agent	(54,433,264)	
Principal payments on long-term debt	(15,010,000)	(15,895,000)
Interest paid on long-term debt	(9,888,278)	(10,751,639)
Net cash provided by noncapital financing activities	<u>16,237,476</u>	<u>125,231,712</u>
<b>Cash flows from investing activities:</b>		
Purchase of investment securities	(190,106,225)	(148,826,922)
Proceeds from sale and maturities of investment securities	202,663,569	68,956,049
Investment income received	6,537,037	6,352,215
Net cash provided by (used in) investing activities	<u>19,094,381</u>	<u>(73,518,658)</u>
Increase (decrease) in cash and cash equivalents	(23,105,399)	3,306,581
Cash and cash equivalents at beginning of year	<u>85,034,026</u>	<u>81,728,245</u>
Cash and cash equivalents at end of year	<u>\$ 61,928,627</u>	<u>\$ 85,034,826</u>
<b>Reconciliation of operating income to net cash used in operating activities:</b>		
Operating income	\$ (50,854,076)	(45,896,392)
Adjustments to reconcile operating income to net cash used in operating activities:		
Amortization and Depreciation	215,522	316,495
Amortization of discount	(197,064)	(403,344)
Amortization of bond premium	(75,396)	(65,964)
Loan credits in restructuring deposit reserve (Note 7)	(15,746,247)	
Investment Income	(7,885,809)	(6,113,550)
Interest expense	10,911,432	10,962,065
Net (increase) decrease in fair market value of investments	1,589,873	4,681,463
Change in assets and liabilities:		
Increase (decrease) in other payables	(119,515)	(30,336)
Decrease (increase) in accrued loan interest receivable	(159,094)	45,974
Increase (decrease) in due to State GSRP	10,564	
Increase (decrease) in due to Division of Water	(141,369)	(197,269)
(Increase) decrease in assistance agreements receivable	4,013,923	(11,705,615)
Net cash used in operating activities	<u>\$ (58,437,256)</u>	<u>\$ (48,406,473)</u>

See accompanying notes.

# **KENTUCKY INFRASTRUCTURE AUTHORITY**

## **NOTES TO THE FINANCIAL STATEMENTS**

June 30, 2005 and 2004

### **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.

#### **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,

# **KENTUCKY INFRASTRUCTURE AUTHORITY**

## **NOTES TO THE FINANCIAL STATEMENTS**

June 30, 2005 and 2004

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 has 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.

# **KENTUCKY INFRASTRUCTURE AUTHORITY**

## **NOTES TO THE FINANCIAL STATEMENTS**

June 30, 2005 and 2004

### **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.

### **Statement of Cash Flows:**

For purposes of the 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 list 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:

# **KENTUCKY INFRASTRUCTURE AUTHORITY**

## **NOTES TO THE FINANCIAL STATEMENTS**

June 30, 2005 and 2004

### **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 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 where 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.

Water and Sewer Resource Development Funds were created and authorized by the 2002 General Assembly to be administered by the Kentucky Infrastructure Authority. Fifty-four million, seven hundred and sixty-five thousand dollars (\$54,765,000) was authorized for each of these two programs with one program directed toward coal producing counties and including 103 individual line-item projects enumerated in the Appropriations Act and the companion fund enumerating some 164 projects to tobacco counties throughout the Commonwealth. Activity for these programs is accounted for in Fund B.

Infrastructure for Economic Development Funds were created and authorized by the 2005 General Assembly to be administered by the Kentucky Infrastructure Authority. Eighty million dollars (\$80,000,000) was authorized for coal producing counties including 192 individual line-item projects enumerated in the Appropriations Act. One hundred, twenty six million dollars (\$126,000,000) was authorized for tobacco counties including 300 individual line-item projects enumerated in the Appropriations Act. Bonds will be sold by the Commonwealth's State Property and Buildings Commission and will be transferred to the Authority for disbursement. Activity for these programs will be accounted for in Fund B.

# KENTUCKY INFRASTRUCTURE AUTHORITY

## NOTES TO THE FINANCIAL STATEMENTS

June 30, 2005 and 2004

### 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 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, 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

# KENTUCKY INFRASTRUCTURE AUTHORITY

## NOTES TO THE FINANCIAL STATEMENTS

June 30, 2005 and 2004

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
<b>Total</b>	<b>\$ 61,928,627</b>	<b>\$212,844,578</b>	<b>\$ 274,773,205</b>

Components of the Revenue Bond Fund accounts by cash, cash equivalents and investments at June 30, 2004 are summarized below:

	Cash and Cash Equivalents	Investments	Total
Operating fund	\$ 513,937	\$ 2,039,609	\$ 2,553,547
Revolving fund	27,410,604	108,207,200	135,617,804
Government agency fund	36,881,898	8,739,566	45,621,464
Debt service reserve fund	3,509,441	4,619,254	8,128,696
Debt service fund	4,702,509	-	4,702,509
Revenue fund	999,773	-	999,773
Surplus fund	4,946,602	20,521,269	25,467,870
Rebate fund	86	-	86
Cost of issuance fund	54,370	-	54,370
Cash in State System	6,015,605	81,275,024	87,290,629
<b>Total</b>	<b>\$ 85,034,826</b>	<b>\$225,401,922</b>	<b>\$ 310,436,748</b>

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**

This account is 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.

# **KENTUCKY INFRASTRUCTURE AUTHORITY**

## **NOTES TO THE FINANCIAL STATEMENTS**

June 30, 2005 and 2004

### **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**

This fund is 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 advances to municipalities in anticipation of new bond issues, and transfers to other funds to cover deficiencies.

### **H. Rebate Fund**

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

### **I. Cost of Issuance Fund**

Upon issuance, a portion of the proceeds are 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.

**KENTUCKY INFRASTRUCTURE AUTHORITY**  
**NOTES TO THE FINANCIAL STATEMENTS**  
June 30, 2005 and 2004

**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 institutions trust department in the Authority's name. The Authority's policy regarding custodial credit risk for deposits is the same as that for the Commonwealth of Kentucky.

The carrying amount of the Authority's deposits were \$61,928,627 and \$85,034,826 at June 30, 2005 and June 30, 2004, 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, 2005 and June 30, 2004 consisted of the following:

	<u>June 30, 2005</u>	<u>June 30, 2004</u>
U.S. Government Backed Securities	\$61,179,577	\$ 79,019,211
Cash Deposited With State	<u>749,050</u>	<u>6,015,615</u>
Total	<u>\$61,928,627</u>	<u>\$85,034,826</u>

**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, 2005 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.

# KENTUCKY INFRASTRUCTURE AUTHORITY

## NOTES TO THE FINANCIAL STATEMENTS

June 30, 2005 and 2004

**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, 2005.

At June 30, 2005 and June 30, 2004, the Authority's investment balances were as follows:

As of June 30, 2005:

Investment:	<u>Fair Value</u>	<u>Maturity</u>	<u>Rate</u>
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
	<u>153,416,845</u>		
Investments in State System	<u>59,427,733</u>		
Total	<u>212,844,578</u>		
Less: Current Portion	<u>(75,857,493)</u>		
Long-Term Investments	<u>\$ 136,987,085</u>		

# KENTUCKY INFRASTRUCTURE AUTHORITY

## NOTES TO THE FINANCIAL STATEMENTS

June 30, 2005 and 2004

As of June 30, 2004:

<u>Investment:</u>	<u>Fair Value</u>	<u>Maturity</u>	<u>Rate</u>
Federal Home Loan Banks Debenture	4,245,952	3/6/2006	5.125
Federal Home Loan Banks	4,227,475	2/15/2006	5.375
Federal Home Loan Banks	3,977,869	5/15/2006	5.375
Federal Home Loan Banks	3,834,356	11/15/2005	3.625
Federal Home Loan Banks	8,188,366	8/15/2005	3
Federal Home Loan Banks	3,878,939	12/15/2005	2.5
Federal Home Loan Banks	8,212,880	8/15/2005	2.375
Federal Home Loan Banks	3,773,438	9/15/2006	2.875
Federal Home Loan Banks	6,327,085	11/15/2006	2.75
Federal Home Loan Mortgage Corp	5,097,126	12/15/2006	2.875
Federal Home Loan Mortgage Corp	4,635,202	1/15/2006	5.25
Federal Home Loan Mortgage Corp	2,441,899	9/15/2005	2.875
Federal Home Loan Mortgage Corp	2,373,053	4/15/2006	2.375
FNMA	5,494,297	7/15/2005	7
FNMA	4,371,987	6/15/2006	5.25
FNMA	4,176,088	10/15/2006	4.375
FNMA	3,505,516	10/15/2005	2.875
Federal Home Loan Banks	4,130,000	8/1/2014	4.45
Federal Home Loan Banks	3,655,560	2/15/2005	7.125
Federal Home Loan Banks	3,613,500	6/15/2005	6.955
Federal Home Loan Banks	3,622,500	10/15/2004	3.625
Federal Home Loan Banks	4,859,815	12/15/2004	3.875
Federal Home Loan Banks	4,743,000	4/15/2005	4.625
Federal Home Loan Banks	5,770,794	5/13/2005	4.125
Federal Home Loan Banks	3,692,756	3/10/2005	7.59
Federal Home Loan Mortgage Corp Debenture	4,695,675	1/15/2005	6.875
Federal Home Loan Mortgage Corp	4,529,520	11/15/2004	3.25
Federal Home Loan Mortgage Corp	4,868,559	6/15/2005	4.25
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	38,743	11/15/2005	N/A
U.S. Treasury Sec Stripped Interest Payment	6,743,029	5/15/2008	N/A
U.S. Treasury Sec Stripped Interest Payment	39,103	11/15/2008	N/A
U.S. Treasury Sec Stripped Interest Payment	16,993	11/15/2009	N/A
U.S. Treasury Sec Stripped Interest Payment	88,021	11/15/2010	N/A
U.S. Treasury Sec Stripped Interest Payment	1,154,424	5/15/2011	N/A
U.S. Treasury Sec Stripped Interest Payment	205,860	11/15/2011	N/A
U.S. Treasury Sec Stripped Interest Payment	133,304	11/15/2012	N/A
U.S. Treasury Sec Stripped Interest Payment	982,124	5/15/2013	N/A
U.S. Treasury Sec Stripped Interest Payment	604,532	11/15/2013	N/A
U.S. Treasury Sec Stripped Interest Payment	938,313	5/15/2014	N/A

**KENTUCKY INFRASTRUCTURE AUTHORITY**  
**NOTES TO THE FINANCIAL STATEMENTS**  
June 30, 2005 and 2004

U.S. Treasury Sec Stripped Interest Payment	99,055	11/15/2015	N/A
U.S. Treasury Sec Stripped Interest Payment	44,082	11/15/2017	N/A
	<u>144,126,898</u>		
Investments in State System	81,275,024		
Total	225,401,922		
Less: Current Portion	<u>(46,174,421)</u>		
Long-Term Investments	<u>\$ 179,227,501</u>		

**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 \$418,609,640 in assistance agreements receivable at June 30, 2005, the Authority has commitments remaining to disburse funds summarized as follows:

Fund A - Waste Water Revolving Loan Program	\$ 68,869,961
Fund B - Infrastructure Revolving Loan Program	6,568,878
Fund C - Governmental Agencies Program	3,339,093
Fund F - Drinking Water Revolving Loan Program	<u>12,679,751</u>
Total commitments outstanding	<u>\$ 91,457,683</u>

**NOTE 6 - LONG-TERM DEBT REVENUE BONDS PAYABLE**

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

	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2006	\$ 14,575,000	\$ 8,815,813	\$ 23,390,813
2007	14,840,000	8,198,232	23,038,232
2008	15,515,000	7,552,222	23,067,222
2009	16,095,000	6,870,953	22,965,953
2010	14,025,000	6,162,167	20,187,167
2011-2015	67,045,000	20,881,355	87,926,355
2016-2020	35,230,000	7,462,469	42,692,469
2021-2025	<u>9,635,000</u>	<u>1,539,213</u>	<u>11,174,213</u>
	<u>\$ 186,960,000</u>	<u>\$ 67,482,424</u>	<u>\$ 254,442,424</u>

**KENTUCKY INFRASTRUCTURE AUTHORITY**  
**NOTES TO THE FINANCIAL STATEMENTS**  
June 30, 2005 and 2004

Long-term debt consists of the following:

Kentucky Infrastructure Authority Revenue Bonds:	June 30, 2005		
	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	\$41,430,000	\$3,040,000	\$38,390,000
Fund B, Infrastructure Revolving Fund Revenue Bonds, interest of 2.75% to 5.95%, due semi-annually, principal due annually to June 1, 2021	83,450,000	7,035,000	76,415,000
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	43,515,000	3,415,000	40,100,000
Fund E, Solid Waste Revolving Fund Revenue Bonds, interest of 2.50% to 5.25%, due semi- annually, principal due annually to June 1, 2013	4,665,000	490,000	4,175,000
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	13,900,000	595,000	13,305,000
	<u>\$ 186,960,000</u>	<u>\$ 14,575,000</u>	<u>\$ 172,385,000</u>
Plus: Unamortized premiums	1,476,541	122,676	1,353,865
Less: Unamortized discounts	(201,994)	(32,909)	(169,085)
Unamortized deferred loss on early retirement of debt	(1,743,784)	(383,019)	(1,360,765)
	<u>\$ 186,490,763</u>	<u>\$ 14,281,748</u>	<u>\$ 172,209,015</u>

# KENTUCKY INFRASTRUCTURE AUTHORITY

## NOTES TO THE FINANCIAL STATEMENTS

June 30, 2005 and 2004

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 7 - DEPOSIT RESERVE

The prior Fund C bond indenture had established a debt service reserve that was funded from the revenue bond proceeds. The municipalities' initial deposit from the revenue bond proceeds to the debt service reserve was a restricted asset of the Authority established for additional security in the event of any loan defaults regarding the assistance agreements receivable. As part of the restructuring of the Fund C program, the governmental agencies were given credit for the amount of debt service reserve that was initially funded plus accrued interest. Any additional debt service reserve required of issues from the new indenture will be funded from sources other than the revenue bond proceeds.

### NOTE 8 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, 2005 is \$32,030,000.

### NOTE 9 GRANT COMMITMENTS

KIA has committed to disburse grants as follows:

<u>Fund</u>	<u>Amount</u>
B	\$ 3,610,124
B - 2020	\$ 9,801,167
B - Coal Development	\$ 26,541,362
B - Tobacco Development	\$ 30,802,319
E	\$ 1,436,389
B - Coal IEDF	\$ 79,395,960
B - Tobacco IEDF	\$ 120,660,220

Coal and Tobacco IEDF grants will not be funded with current Authority resources. Bonds will be sold by the Commonwealth's State Property and Buildings Commission and transferred in to the Authority for disbursement.

# KENTUCKY INFRASTRUCTURE AUTHORITY

## NOTES TO THE FINANCIAL STATEMENTS

June 30, 2005 and 2004

### NOTE 10 DEFEASED DEBT

During the year ended June 30, 2005, the Authority issued Governmental Agencies Program Revenue Refunding and Improvement Bonds, 2004 Series A and Government Agencies Program Taxable Revenue Refunding Bonds, 2004 Series B.

Governmental Agencies Program Revenue and Revenue Refunding Bonds, 2004 Series A, interest of 2.25% to 5.25%, due semi-annually, principal due annually to August 1, 2022. Par value of \$25,640,000.

\$17,468,370 of the proceeds along with other available funds will be placed in a redemption account to redeem bonds as follows:

<u>Series Name</u>	<u>Redemption Date</u>	<u>Refunded Principal Amount</u>	<u>Redemption Price</u>
1993 Series E	8/1/2004	\$ 9,185,000	101%
1993 Series F	8/1/2004	<u>\$13,805,000</u>	101%
Total		<u>\$22,990,000</u>	

\$8,396,072 of the proceeds from the bonds along with other available moneys were used to purchase U.S. Government securities which were deposited in an irrevocable trust with an escrow agent to advance refund outstanding bonds as follows:

<u>Series Name</u>	<u>Redemption Date</u>	<u>Refunded Principal</u>	<u>Redemption Price</u>
1995 Series H	8/1/2005	\$ 108,653	102%
1998 Series I	6/1/2007	\$1,535,993	101%
1999 Series J	6/1/2008	\$1,933,138	101%
2002 Series K	6/1/2013	<u>\$5,408,651</u>	100%
		<u>\$8,986,435</u>	

Governmental Agencies Program Taxable Revenue Refunding Bonds, 2004 Series B, interest of 2.25% to 5.29%, due semi-annually, principal due annually to August 1, 2014. Par value of \$17,375,000, \$13,485,821 together with other available moneys deposited in an irrevocable trust with an escrow agent to advance refund outstanding bonds as follows:

<u>Series Name</u>	<u>Redemption Date</u>	<u>Refunded Principal</u>	<u>Redemption Price</u>
1995 Series G	8/1/2005	\$ 300,000	N/A
1995 Series H	8/1/2005	\$7,501,347	102%
1998 Series I	8/1/2008	\$ 964,007	101%
1999 Series J	8/1/2009	\$5,946,862	101%
2002 Series K	6/1/2012	<u>\$6,471,349</u>	100%
		<u>\$21,183,565</u>	

# **KENTUCKY INFRASTRUCTURE AUTHORITY**

## **NOTES TO THE FINANCIAL STATEMENTS**

June 30, 2005 and 2004

The advanced refunding has met the requirements of in-substance debt defeasance and the refunded debt has been removed from long-term debt in the accompanying balance sheets.

The advanced refunding resulted in a difference between the reacquisition price and the net carrying amount of the old debt of \$1,273,263. This difference, reported in the accompanying financial statements as a deduction from bonds payable, is being charged to operations through the year 2015 using the straight-line method. KIA completed the advance refunding to reduce its total debt service payments over the next 12 years by \$4,690,290 (net of funds on hand contributed) and to obtain an economic gain (difference between the present values of the old and new debt service payments) of \$1,509,470.

### **NOTE 11 – 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, 2005 there were no such purchases and thus, the historical cost of equipment did not change from the previous year. The Authority's accumulated depreciation increased from the prior year's balance of \$67,431 by the current year's depreciation expense of \$16,858 for an ending balance of \$84,288. The only capitalized assets consist of computer equipment which the Authority depreciates over five (5) years using the straight-line method.

### **NOTE 12 – RETAINED EARNINGS**

Since the use of the Authority's resources is mandated by the Kentucky Revised Statutes and the United State's Environmental Protection Agency, 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.

### **NOTE 13 – RECLASSIFICATION FROM PRIOR YEARS**

Certain prior year balances have been reclassified to more closely compare to the current year amounts. Interest received on Fund C loans have been separately listed on the Statement of Revenue, Expenses and Changes in Retained Earnings to disclose interest received to secure revenue bonds.

**KENTUCKY INFRASTRUCTURE AUTHORITY**  
**SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS**  
**FOR THE YEAR ENDED JUNE 30, 2005**

<u>Grant Name</u>	<u>CFDA Number</u>	<u>Grant Period</u>	<u>Expenditures</u>	<u>Passed Through To Other Agencies (Including Revenue Redistributions)</u>
<b><u>U.S. Environmental Protection Agency</u></b>				
Direct Programs:				
Capitalization Grants for Clean Water State Revolving Funds	66.458	9/1999 - 9/2005	152,665	
Capitalization Grants for Clean Water State Revolving Funds	66.458	10/2000 - 3/2005	10,604,347	
Capitalization Grants for Clean Water State Revolving Funds	66.458	10/2001 - 9/2006	6,740,291	
Capitalization Grants for Clean Water State Revolving Funds	66.458	10/2003 - 9/2005	61,846	192,526
Capitalization Grants for Clean Water State Revolving Funds	66.458	9/2004 - 9/2008		98,989
<b>Total Capitalization Grants for Clean Water State Revolving Funds</b>			<b><u>\$ 17,559,149</u></b>	<b><u>\$ 291,515</u></b>
Direct Programs:				
Capitalization Grants for Drinking Water State Revolving Fund	66.468	7/2000 - 9/2005		
Capitalization Grants for Drinking Water State Revolving Fund	66.468	10/2000 - 9/2005		160,819
Capitalization Grants for Drinking Water State Revolving Fund	66.468	1/2002 - 3/2005	2,071,709	46,570
Capitalization Grants for Drinking Water State Revolving Fund	66.468	1/2002 - 9/2005	5,626,231	619,028
Capitalization Grants for Drinking Water State Revolving Fund	66.468	9/2004 - 9/2008	97,462	339,406
Capitalization Grants for Drinking Water State Revolving Fund	66.468	9/2004 - 9/2009	101,102	24,793
<b>Total Capitalization Grants for Drinking Water State Revolving Funds</b>			<b><u>\$ 7,896,504</u></b>	<b><u>\$ 1,190,616</u></b>
<b>Total U. S. Environmental Protection Agency</b>			<b><u>\$ 25,455,653</u></b>	<b><u>\$ 1,482,131</u></b>
<b>Total All Programs</b>			<b><u>\$ 25,455,653</u></b>	<b><u>\$ 1,482,131</u></b>

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, 2005

**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**

<u>CFDA #</u>	<u>Grant Name</u>	<u>Amount</u>	<u>Passed Through To Whom?</u>
66.458	Clean Water State Revolving Funds	\$ 291,515	Environmental and Public Protection Cabinet
66.468	Drinking Water State Revolving Funds	\$ 1,190,616	Environmental and Public Protection Cabinet



**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, 2005, 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 26 through 29 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  
October 31, 2005

**KENTUCKY INFRASTRUCTURE AUTHORITY**  
**COMBINING BALANCE SHEET**  
June 30, 2005

	ASSETS	
	Fund A	Fund B
<b>Current assets:</b>		
Cash and cash equivalents	\$ 34,900,791	\$ 17,643,304
Investments, current portion	54,513,272	13,467,989
Federal Funds Receivable		
Accrued interest receivable, investments	2,235,106	337,541
Accrued interest receivable, loans	679,910	124,982
Current maturities of long-term receivables	15,199,021	3,022,258
Total current assets	107,528,100	34,596,074
 Equipment, Net of Accumulated Depreciation (Note 11)		
 Investments	52,798,251	60,223,874
<b>Long-term receivables:</b>		
Assistance agreements receivable:		
Principal	253,477,683	49,950,278
Less:		
Current maturities	(15,199,021)	(3,022,258)
Deposit reserve		
Unamortized discounts/premiums		
Funds held for governmental agencies		
Total long-term receivables	238,278,662	46,928,020
 <b>Other assets:</b>		
Unamortized costs of issuance	458,206	684,123
Total assets	\$ 399,063,219	\$ 142,432,091

**LIABILITIES AND RETAINED EARNINGS**

<b>Current liabilities:</b>		
Current maturities of revenue bonds payable, less unamortized discounts and deferred loss on early retirement of debt	\$ 2,964,892	\$ 6,752,069
Accrued interest payable	160,783	348,616
Due to Division of Water		
Due to Governor's Office of Local Development		13,697
Due to State GSRP	10,564	
Total current liabilities	3,136,239	7,114,382
 <b>Long-term debt:</b>		
Revenue bonds payable, less current maturities and unamortized discounts and deferred loss on early retirement of debt	37,784,155	76,005,998
Total liabilities	40,920,394	83,120,380
 <b>Retained Earnings:</b>		
Invested in Capital Assets net of related debt of \$0 Restricted (Note 12)	358,142,825	59,311,711
Total retained earnings	358,142,825	59,311,711
Total liabilities and retained earnings	\$ 399,063,219	\$ 142,432,091

<u>Fund C</u>	<u>Fund E</u>	<u>Fund F</u>	<u>Total</u>
\$ 5,934,545	\$ 858,894	\$ 2,591,093	\$ 61,928,627
3,012,749	1,323,255	3,540,228	75,857,493
		539,017	539,017
131,440	51,551	155,585	2,911,223
162,019	7,643	335,004	1,309,558
<u>3,742,295</u>	<u>328,376</u>	<u>1,608,896</u>	<u>23,900,846</u>
<u>12,983,048</u>	<u>2,569,719</u>	<u>8,769,823</u>	<u>166,446,764</u>
			-
<u>18,844,323</u>	<u>1,520,531</u>	<u>3,600,106</u>	<u>136,987,085</u>
48,727,384	1,522,203	64,932,092	418,609,640
(3,742,295)	(328,376)	(1,608,896)	(23,900,846)
(58,031)			(58,031)
(1,048,407)			(1,048,407)
<u>(28,115)</u>			<u>(28,115)</u>
<u>43,850,536</u>	<u>1,193,827</u>	<u>63,323,196</u>	<u>393,574,241</u>
321,888	41,549	158,634	1,664,400
\$ <u>75,999,795</u>	\$ <u>5,325,626</u>	\$ <u>75,851,759</u>	\$ <u>698,672,490</u>
\$ 3,515,667	\$ 455,116	\$ 594,004	\$ 14,281,748
777,090	18,795	56,025	1,361,309
		52,390	52,390
			13,697
			<u>10,564</u>
<u>4,292,757</u>	<u>473,911</u>	<u>702,419</u>	<u>15,719,708</u>
41,171,175	3,954,957	13,292,730	172,209,015
<u>45,463,932</u>	<u>4,428,868</u>	<u>13,995,149</u>	<u>187,928,723</u>
30,535,863	896,758	61,856,610	510,743,767
<u>30,535,863</u>	<u>896,758</u>	<u>61,856,610</u>	<u>510,743,767</u>
\$ <u>75,999,795</u>	\$ <u>5,325,626</u>	\$ <u>75,851,759</u>	\$ <u>698,672,490</u>

**KENTUCKY INFRASTRUCTURE AUTHORITY**  
**COMBINED STATEMENT OF REVENUES, EXPENSES AND**  
**CHANGES IN RETAINED EARNINGS**  
Year ended June 30, 2005

	<u>Fund A</u>	<u>Fund B</u>
Operating revenues:		
Assistance agreements:		
Servicing fee	\$ 456,770	\$ 106,152
Interest	5,339,170	1,545,796
Interest Received Securing Revenue Bonds		
Amortization of loan premiums	43,992	
Amortization of bond premiums		74,724
Income from investments	4,230,285	2,742,563
Miscellaneous Income		
Net increase (decrease) in fair market value of investments	<u>(445,475)</u>	<u>219,584</u>
Total operating revenues	<u>9,624,742</u>	<u>4,688,819</u>
Operating expenses:		
General and administrative	253,754	2,314,068
Intergovernmental administrative expense reimbursement	291,515	
Grants		52,844,851
Depreciation		16,858
Revenue bonds payable:		
Amortization of discount	18,324	8,808
Amortization of costs of issuance	54,444	58,692
Interest on reserves		
Interest	<u>2,151,837</u>	<u>4,789,907</u>
Total operating expenses	<u>2,769,874</u>	<u>60,033,184</u>
Operating income (loss)	6,854,868	(55,344,365)
Nonoperating revenues:		
Federal grants and reimbursements	<u>18,027,106</u>	
Net Income (loss) before operating transfers	24,881,974	(55,344,365)
State Appropriation		6,276,631
Gain (Loss) on Sale of Investments		
Operating transfers in for debt service	<u>4,971,555</u>	<u>11,231,955</u>
Net income (loss)	29,853,529	(37,835,779)
Retained earnings (deficit), beginning of year	<u>328,289,296</u>	<u>97,147,490</u>
Retained earnings (deficit) at end of year	<u>\$ 358,142,825</u>	<u>\$ 59,311,711</u>

<u>Fund C</u>	<u>Fund E</u>	<u>Fund F</u>	<u>Total</u>
\$ 94,858	\$ 3,887	\$ 90,300	\$ 751,967
	53,415	1,101,141	8,039,522
2,186,253			2,186,253
149,784	3,288		197,064
		672	75,396
335,932	98,564	478,465	7,885,809
2,394			2,394
<u>(1,303,548)</u>	<u>(11,780)</u>	<u>(48,654)</u>	<u>(1,589,873)</u>
<u>1,465,673</u>	<u>147,374</u>	<u>1,621,924</u>	<u>17,548,532</u>
29,526	905	98,939	2,697,192
		1,190,616	1,482,131
	251,480		53,096,331
			16,858
4,476	3,732	1,668	37,008
32,848	5,400	10,272	161,656
1,145,287			1,145,287
1,851,741	279,498	693,162	9,766,145
<u>3,063,878</u>	<u>541,015</u>	<u>1,994,657</u>	<u>68,402,608</u>
(1,598,205)	(393,641)	(372,733)	(50,854,076)
		9,087,121	27,114,227
(1,598,205)	(393,641)	8,714,388	(23,739,849)
	577,071		6,853,702
1,875,214			1,875,214
	716,833	1,272,811	18,193,154
277,009	900,263	9,987,199	3,182,221
<u>30,258,854</u>	<u>(3,505)</u>	<u>51,869,411</u>	<u>507,561,546</u>
\$ <u>30,535,863</u>	\$ <u>896,758</u>	<u>61,856,610</u>	\$ <u>510,743,767</u>



**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, 2005, and have issued our report thereon dated October 31, 2005. 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  
October 31, 2005



**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 program for the year ended June 30, 2005. The Kentucky Infrastructure Authority's major federal program is 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 program for the year ended June 30, 2005.

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  
October 31, 2005

**KENTUCKY INFRASTRUCTURE AUTHORITY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
Year ended June 30, 2005**

**Summary of Auditor's Results**

We have issued an unqualified opinion, dated October 31, 2005, on the financial statements of Kentucky Infrastructure Authority as of and for the year ended June 30, 2005.

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 October 31, 2005, 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, 2005, 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, 2005**

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