

KENTUCKY INFRASTRUCTURE AUTHORITY
FRANKFORT, KENTUCKY

FINANCIAL STATEMENTS AND
INDEPENDENT AUDITOR'S REPORT

June 30, 2008 and 2007

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 (the Authority), a component unit of the Commonwealth of Kentucky, as of and for the year ended June 30, 2008, 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 audit. The financial statements as of June 30, 2007 were audited by other auditors, whose report dated October 31, 2007, expressed an unqualified opinion on those statements.

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. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit 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 audit provides a reasonable basis for our opinion.

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, 2008, and the changes in its financial position and its cash flows for the year then ended in conformity with generally accepted accounting principles.

In accordance with *Government Auditing Standards*, we have also issued our report dated December 9, 2008 on our consideration of the Kentucky Infrastructure Authority's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audits.

The Management's Discussion and Analysis on pages 3 through 9 is not a required part of the financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

To the Board of Directors
Kentucky Infrastructure Authority
Frankfort, Kentucky

Our audit was conducted for the purpose of forming an opinion on such financial statements of the Authority taken as a whole. The supplementary information included in the accompanying schedules on pages 34 through 35 is presented for purposes of additional analysis and is not a required part of the basic financial statements. The accompanying schedule of expenditures of federal awards on page 32 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 basic 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.

Potter + Company, LLP

POTTER & COMPANY, LLP
December 9, 2008



KENTUCKY INFRASTRUCTURE AUTHORITY
MANAGEMENT'S DISCUSSION AND ANALYSIS

As management of the Kentucky Infrastructure Authority (the Authority), a component unit of the Commonwealth of Kentucky, we offer the readers of the Authority's financial statements this narrative overview and analysis of the financial performance of the Authority for the fiscal years ended June 30, 2008 and 2007. We encourage readers to read it in conjunction with the Authority's financial statements and the accompanying notes.

FINANCIAL HIGHLIGHTS

- As of the close of fiscal year 2008, the Authority reported combined ending net assets of approximately \$648,537,000 an increase of approximately \$61,185,000 in comparison with the prior year.
- The Authority's total debt decreased approximately \$15,454,000 (9.8%) during fiscal year 2008. The primary factor in this decrease was the payments of principal that were due. There were no new bond issues by the Authority for state general fund supported debt or program revenue supported debt.
- The Authority disbursed approximately \$55,201,000 to borrowers for assistance agreements and approximately \$131,641,000 to local governmental entities in state grants. Principal and interest in the amount of approximately \$42,259,000 was collected from borrowers for assistance agreements.

OVERVIEW OF THE FINANCIAL STATEMENTS

This financial report consists of three parts: Management's Discussion and Analysis (this section), the basic financial statements, and the accompanying notes to the financial statements. The Kentucky Infrastructure Authority is a self-supporting entity and follows enterprise fund reporting; accordingly, the financial statements are presented using the economic resources measurement focus and the accrual basis of accounting. Enterprise fund statements offer short and long-term financial information about the activities and operations of the Authority. These statements are presented in a manner similar to those of a private business.

The statement of net assets presents information on all of the Authority's assets and liabilities, with the difference between the two reported as net assets. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of the Authority is improving or deteriorating.

The statement of revenues, expenses and changes in net assets presents information showing how the Authority's net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of the related cash flows. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods.

KENTUCKY INFRASTRUCTURE AUTHORITY

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

OVERVIEW OF THE FINANCIAL STATEMENTS (CONTINUED)

The statement of cash flows provides relevant information about the cash receipts and cash payments of the Authority during the fiscal year. The statement should help users assess the Authority's ability to generate future net cash flows, meet future obligations as they become due, the Authority's need for future external financing, the reasons for differences in operating and related cash receipts and cash payments, and the effects on financial position of cash and non-cash investing, capital, non-capital and financing activities.

The notes to the financial statements provide additional information that is essential to a full understanding of the data provided in the basic financial statements. The notes to the financial statements can be found on pages 13 - 31.

FINANCIAL ANALYSIS OF THE AUTHORITY

Condensed Financial Information Statement of Net Assets As of June 30

	<u>2008</u>	% Increase (Decrease)	<u>2007</u>	% Increase (Decrease)	<u>2006</u>
Assets:					
Current assets	\$ 309,475,400	27.2%	\$ 243,388,065	45.5%	\$ 167,315,387
Long-term investments	33,062,432	-53.0%	70,305,254	-54.4%	154,314,683
Long-term receivables	449,032,201	3.9%	431,977,791	7.8%	400,698,926
Net capital assets	19,354	-	0	-	0
Other assets	<u>1,243,882</u>	-10.0%	<u>1,382,637</u>	-9.2%	<u>1,522,730</u>
Total assets	792,833,269	6.1%	747,053,747	3.2%	723,851,726
Liabilities:					
Current liabilities	18,123,550	5.0%	17,260,282	4.7%	16,478,208
Long-term debt	<u>126,173,192</u>	-11.4%	<u>142,441,860</u>	-9.6%	<u>157,655,240</u>
Total liabilities	144,296,742	-9.6%	159,702,142	-8.3%	174,133,448
Net assets:					
Invested in capital net of related debt	19,354	-	0	-	0
Restricted net assets	<u>648,517,173</u>	10.4%	<u>587,351,605</u>	6.8%	<u>549,718,278</u>
Total net assets	\$ <u>648,536,527</u>	10.4%	\$ <u>587,351,605</u>	6.8%	\$ <u>549,718,278</u>

Total assets consist primarily of cash and cash equivalents, investments, and assistance agreements receivable.

During 2008, the Authority's total cash and cash equivalents and investments increased approximately \$52,252,000. During 2007, the Authority's total cash and cash equivalents and investments decreased approximately \$41,130,000.

KENTUCKY INFRASTRUCTURE AUTHORITY

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

FINANCIAL ANALYSIS OF THE AUTHORITY (CONTINUED)

At June 30, 2008, total investments consist of a current portion of approximately \$261,788,000 and a non-current portion of approximately \$33,062,000. As of June 30, 2008, the current portion is representative of U.S. Government Agency debt securities with maturities longer than three months when purchased, but also having maturities prior to June 30, 2009. The non-current portion is representative of the Authority's investments maintained within the State cash and investment pool and other investments with maturities greater than one year. The Authority's investments tend to consist of a large concentration of investments with a maturity of three months or less when purchased (cash equivalents) in order to maintain sufficient liquidity.

During fiscal year 2008, new assistance agreements issued of approximately \$55,201,000 exceeded repayments of assistance agreements receivable of approximately \$32,219,000 contributing to the approximately \$22,982,000 increase in net assistance agreements receivable. During fiscal year 2007, new assistance agreements issued of approximately \$67,337,000 exceeded repayments of assistance agreements receivable of approximately \$31,381,000 contributing to the approximately \$35,957,000 increase in net assistance agreements receivable.

Total liabilities typically consist of current and non-current portions of revenue bonds payable and related accrued interest thereon.

Condensed Financial Information Statement of Revenues, Expenses, and Changes in Net Assets For the Fiscal Years Ended June 30

	2008	% Increase (Decrease)	2007	% Increase (Decrease)	2006
Operating revenue	\$ 12,064,607	5.1%	\$ 11,473,876	6.4%	\$ 10,778,873
Operating expenses	<u>144,757,276</u>	19.8%	<u>120,833,784</u>	66.4%	<u>72,612,548</u>
Operating loss	(132,692,669)	21.3%	(109,359,908)	76.9%	(61,833,675)
Nonoperating revenues:					
Income from investments	13,701,326	18.4%	11,570,691	20.1%	9,634,763
Net increase (decrease) in fair market value of investments	(3,287,986)	-227.6%	2,577,660	-263.8%	(1,573,812)
Federal grants and reimbursements	32,107,111	-25.5%	43,070,404	61.5%	26,664,604
Transfers to state general fund	0	-	0	-	(3,600,000)
Net payments from the Commonwealth	130,599,320	87.1%	69,787,596	35.5%	51,512,019
State appropriations	<u>20,757,820</u>	3.9%	<u>19,986,884</u>	10.0%	<u>18,170,612</u>
Change in net assets	<u>\$ 61,184,922</u>	62.6%	<u>\$ 37,633,327</u>	-3.4%	<u>\$ 38,974,511</u>

KENTUCKY INFRASTRUCTURE AUTHORITY

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

FINANCIAL ANALYSIS OF THE AUTHORITY (CONTINUED)

Operating revenues primarily consist of interest and service fee revenue from assistance agreements receivable and grant administration fees. Interest on assistance agreements receivable and related service fees increased approximately \$297,000 from fiscal year 2007. Grant administration fees increased approximately \$215,000.

Operating Expenses primarily consist of grants, general and administrative costs, and amortization and interest related to revenue bonds payable. Grants are primarily representative of the disbursements made relative to local taxing districts of the Commonwealth as appropriated during the General Assembly. Current year **grants** increased approximately \$24,381,000 from 2007. The increase is primarily attributable to the increase in grants awarded for the Economic Development Fund for Coal and Non-Coal Producing Counties as called for in House Bill 380. General and administrative costs increased approximately \$981,000 due to the increase in grant administration.

Condensed Financial Information (in thousands)

Statement of Cash Flows

For the Fiscal Years Ended June 30

	2008	% Increase (Decrease)	2007	% Increase (Decrease)	2006
Cash flows from operating activities	\$ (148,255,920)	8.7%	\$ (136,371,644)	125.4%	\$ (60,504,129)
Cash flows from noncapital financing activities	209,858,976	101.1%	104,376,003	11.9%	93,300,270
Cash flows from financing activities	(23,067,219)	0.1%	(23,038,080)	-3.0%	(23,757,887)
Cash flows from investing activities	<u>(86,705,439)</u>	-235.4%	<u>64,015,657</u>	-364.5%	<u>(24,206,892)</u>
Net change in cash	(48,169,602)	-636.3%	8,981,936	-159.2%	(15,168,638)
Cash, beginning of year	<u>55,741,925</u>	19.2%	<u>46,759,989</u>	-24.5%	<u>61,928,627</u>
Cash, end of year	<u>\$ 7,572,323</u>	-86.4%	<u>\$ 55,741,925</u>	19.2%	<u>\$ 46,759,989</u>

The **net change in cash and cash equivalents** totaled approximately \$48,170,000 for the year ended June 30, 2008 due principally to the following: \$131,641,000 in payments for grants (net cash used in operating activities), advances on assistance agreement exceeded collections of assistance agreements by approximately \$22,982,000 and interest collected on assistance agreements of approximately \$10,040,000 (net cash used in operating activities); cash received on federal grants of approximately \$58,410,000, state appropriations received of approximately \$20,437,000, and payments received from the Commonwealth related to grants of approximately \$130,599,000 (net cash provided by noncapital financing activities); principal and interest payments on long-term debt of approximately \$23,067,000 (net cash used in financing activities); and investing activities (primarily purchases of investments and proceeds from the maturities of investments) generated a net cash outflow of approximately \$103,710,000 offset by interest and income received from investments of approximately \$17,004,000 (net cash used in investing activities).

KENTUCKY INFRASTRUCTURE AUTHORITY
MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

LONG-TERM DEBT

At June 30, 2008, the Authority had approximately \$142,030,000 in bonds outstanding (principal) - a decrease of 9.8 percent from last year. 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 current fiscal 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 (\$500,000,000). Our outstanding debt in the Fund C program, which meets this criterion, is significantly below this limit.

Kentucky Infrastructure Authority's Outstanding Debt:

	<u>2008</u>	% Increase (Decrease)	<u>2007</u>	% Increase (Decrease)	<u>2006</u>
General fund appropriation supported debt	\$ 108,355,000	-10.1%	\$ 120,595,000	-8.8%	\$ 132,285,000
Program revenue supported debt	<u>33,675,000</u>	-8.9%	<u>36,950,000</u>	-7.9%	<u>40,100,000</u>
Total	<u>\$ 142,030,000</u>	-9.8%	<u>\$ 157,545,000</u>	-8.6%	<u>\$ 172,385,000</u>

KENTUCKY INFRASTRUCTURE AUTHORITY

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

CURRENTLY KNOWN FACTS, DECISIONS, OR CONDITIONS

The 2003 General Assembly, in House Bill 269, identified 271 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 FY2008, approximately \$10.9 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, in House Bill 267, identified 507 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 0.5% of each grant to cover the cost of administering these projects. At the end of FY2008, approximately \$52.4 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 2006 General Assembly, in House Bill 380, identified 563 projects totaling approximately \$146,531,000 (corresponding appropriation of \$145 million) for non-coal producing counties and approximately \$70,127,000 (corresponding appropriation of \$69 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 0.5% of each grant to cover the cost of administering these projects. At the end of FY2008, approximately \$128.5 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, in House Bill 380, also appropriated \$1,740,000 for funding of water and sewer projects for Community Development Projects. At the end of FY2008, approximately \$777,000 remained to be disbursed to grantees for Community Development .

The 2008 General Assembly, in House Bill 406, identified 598 projects totaling \$160,585,000 (corresponding appropriation of \$150 million) for non-coal producing counties and \$79,240,000 (corresponding appropriation of \$75 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 0.5% of each grant to cover the cost of administering these projects. At the end of FY2008, approximately \$239.8 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.

KENTUCKY INFRASTRUCTURE AUTHORITY
MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

CONTACTING THE 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
STATEMENTS OF NET ASSETS
June 30, 2008 and 2007

	<u>2008</u>	<u>2007</u>
<u>A S S E T S</u>		
Current assets:		
Cash and cash equivalents	\$ 7,268,530	\$ 50,951,811
Cash and cash equivalents, restricted for debt service	303,793	4,790,114
Investments, current portion	261,788,230	124,123,851
Federal funds receivable	3,444,158	29,747,061
General fund appropriations receivable	320,766	0
Accrued interest receivable, investments	791,458	4,094,236
Accrued interest receivable, loans	1,231,538	928,794
Current maturities of long-term receivables	34,326,927	28,752,198
Total current assets	<u>309,475,400</u>	<u>243,388,065</u>
Investments	26,966,324	64,209,146
Investments, restricted for debt service	6,096,108	6,096,108
Total noncurrent investments	<u>33,062,432</u>	<u>70,305,254</u>
Long-term receivables:		
Assistance agreements receivable:		
Principal	486,010,840	463,029,157
Less:		
Current maturities	(34,326,927)	(28,752,198)
Deposit reserve	(1,762,826)	(1,350,229)
Unamortized premiums	(860,770)	(920,824)
Funds held for governmental agencies	(28,116)	(28,115)
Total long-term receivables	<u>449,032,201</u>	<u>431,977,791</u>
Capital assets, net	<u>19,354</u>	<u>0</u>
Other assets:		
Unamortized costs of issuance	<u>1,243,882</u>	<u>1,382,637</u>
Total assets	<u>\$ 792,833,269</u>	<u>\$ 747,053,747</u>
<u>L I A B I L I T I E S</u>		
Current liabilities:		
Current maturities of revenue bonds payable, less unamortized discounts and deferred loss on early retirement of debt	\$ 16,035,785	\$ 15,221,560
Accrued interest payable	1,094,420	1,185,628
Due to Division of Water	397,547	828,833
Due to the Department of Local Governments	14,880	13,697
Other payables	580,918	10,564
Total current liabilities	<u>18,123,550</u>	<u>17,260,282</u>
Long-term debt:		
Revenue bonds payable, less current maturities and unamortized discounts and deferred loss on early retirement of debt	<u>126,173,192</u>	<u>142,441,860</u>
Total liabilities	<u>144,296,742</u>	<u>159,702,142</u>
<u>N E T A S S E T S</u>		
Net assets:		
Invested in capital net of related debt	19,354	0
Restricted net assets	<u>648,517,173</u>	<u>587,351,605</u>
Total net assets	<u>\$ 648,536,527</u>	<u>\$ 587,351,605</u>

KENTUCKY INFRASTRUCTURE AUTHORITY
STATEMENTS OF REVENUES, EXPENSES
AND CHANGES IN NET ASSETS
Years ended June 30, 2008 and 2007

	<u>2008</u>	<u>2007</u>
Operating revenues:		
Assistance agreements:		
Servicing fee	\$ 812,708	\$ 803,516
Interest	8,638,017	8,350,051
Interest received securing revenue bonds	1,704,468	1,627,168
Amortization of premium	60,054	97,863
Grant administration fee	742,580	527,104
Amortization of bond premiums	106,780	68,174
Total operating revenues	<u>12,064,607</u>	<u>11,473,876</u>
Operating expenses:		
General and administrative	3,676,864	2,696,036
Intergovernmental administrative expense reimbursement	1,671,970	2,223,049
Grants	131,641,342	107,260,239
Revenue bonds payable:		
Amortization of discount	26,604	32,420
Amortization of costs of issuance	138,756	140,093
Interest	7,601,740	8,481,947
Total operating expenses	<u>144,757,276</u>	<u>120,833,784</u>
Operating loss	(132,692,669)	(109,359,908)
Nonoperating revenues (expenses):		
Income from investments	13,701,326	11,570,691
Net increase (decrease) in fair market value of investments	(3,287,986)	2,577,660
Federal grants and reimbursements	32,107,111	43,070,404
Net payments from the Commonwealth	130,599,320	69,787,596
State appropriations	20,757,820	19,986,884
Total nonoperating revenues	<u>193,877,591</u>	<u>146,993,235</u>
Change in net assets	61,184,922	37,633,327
Net assets, beginning of year	<u>587,351,605</u>	<u>549,718,278</u>
Net assets, end of year	<u>\$ 648,536,527</u>	<u>\$ 587,351,605</u>

KENTUCKY INFRASTRUCTURE AUTHORITY
STATEMENTS OF CASH FLOWS
Years ended June 30, 2008 and 2007

	<u>2008</u>	<u>2007</u>
Cash flows from operating activities:		
Administrative fees received	\$ 1,555,288	\$ 1,330,620
Collections on assistance agreements	32,219,352	31,380,760
Advances on assistance agreements	(55,201,024)	(67,337,478)
Interest received on assistance agreements	10,039,741	10,235,386
Cash payments for grants	(131,641,342)	(107,260,239)
Cash payments for personnel expenses	(1,134,305)	(1,060,977)
Cash payments to suppliers for goods and services	<u>(4,093,630)</u>	<u>(3,659,716)</u>
Net cash used in operating activities	<u>(148,255,920)</u>	<u>(136,371,644)</u>
Cash flows from noncapital financing activities:		
Receipt of federal grants, net	58,410,014	13,953,784
State appropriation	20,437,045	18,186,959
Payments from the Commonwealth	130,599,320	71,587,521
Receipt of deposit reserve funds from borrowers	<u>412,597</u>	<u>647,739</u>
Net cash provided by noncapital financing activities	<u>209,858,976</u>	<u>104,376,003</u>
Cash flows from financing activities:		
Principal payments on long-term debt	(15,515,000)	(14,840,000)
Interest paid on long-term debt	<u>(7,552,219)</u>	<u>(8,198,080)</u>
Net cash used in financing activities	<u>(23,067,219)</u>	<u>(23,038,080)</u>
Cash flows from investing activities:		
Purchase of investment securities	(226,087,911)	(283,028,622)
Proceeds from sale and maturities of investment securities	122,378,368	335,718,438
Interest and other investment income received	<u>17,004,104</u>	<u>11,325,841</u>
Net cash provided by (used in) investing activities	<u>(86,705,439)</u>	<u>64,015,657</u>
Increase (decrease) in cash and cash equivalents	(48,169,602)	8,981,936
Cash and cash equivalents at beginning of year	<u>55,741,925</u>	<u>46,759,989</u>
Cash and cash equivalents at end of year	<u>\$ 7,572,323</u>	<u>\$ 55,741,925</u>
Reconciliation of cash and cash equivalents to the statements of net assets:		
Cash and cash equivalents	7,268,530	50,951,811
Cash and cash equivalents, restricted for debt service	<u>303,793</u>	<u>4,790,114</u>
Total cash and cash equivalents	<u>\$ 7,572,323</u>	<u>\$ 55,741,925</u>
Reconciliation of operating loss to net cash used in operating activities:		
Operating loss	(132,692,669)	(109,359,908)
Adjustments to reconcile operating loss to net cash used in operating activities:		
Amortization of bond discount and cost of issuance	165,360	172,513
Amortization of bond premium	(106,780)	(68,174)
Amortization of assistance agreements discount	(60,054)	(97,863)
Amortization of bond defeasance included in interest	140,733	367,004
Interest paid on long-term debt	7,552,219	8,198,080
Change in assets and liabilities:		
(Increase) decrease in accrued interest receivable	(302,744)	258,167
Increase in assistance agreements receivable	(22,981,674)	(35,956,718)
Decrease in accrued interest payable	(91,208)	(83,137)
Increase (decrease) in due to Division of Water	(431,286)	198,392
Increase in due to the Department of Local Government	1,183	0
Increase in other payables	<u>551,000</u>	<u>0</u>
Net cash used in operating activities	<u>\$ (148,255,920)</u>	<u>\$ (136,371,644)</u>
Supplemental disclosure of noncash investing activities:		
Purchase of capital asset included in accounts payable	<u>\$ 19,354</u>	<u>\$ 0</u>

KENTUCKY INFRASTRUCTURE AUTHORITY
NOTES TO THE FINANCIAL STATEMENTS
June 30, 2008 and 2007

NOTE 1 - DESCRIPTION OF ORGANIZATION

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: In 2004, the Governor of the Commonwealth issued an Executive Order which attached the Authority to the Governor's Office for Local Development (GOLD) for administrative purposes. By Executive Order issued in 2008, the GOLD was reorganized as the Department for Local Government (DLG).

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.

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, 2008 and 2007

NOTE 1 - DESCRIPTION OF ORGANIZATION (CONTINUED)

Fund A - Clean Water State Revolving Fund 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 Authority and the Energy and Environment 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 the construction or acquisition of infrastructure projects. 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.

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 2007 and 2008, projects were being administered from the 2003 General Assembly, the 2005 General Assembly and the 2006 General Assembly. Activities for these grants are accounted for in Fund B.

The Fund E Solid Waste Revolving Loan Program was established to assist local government units in the financing of solid waste projects. The 2002 General Assembly abolished the legal authority for the Authority's solid waste program. On February 8, 2007, the Authority's Board approved a resolution to authorize the transfer of the Fund E (solid waste revolving) program assets to the appropriate accounts in Fund B (infrastructure revolving) program.

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 the construction or acquisition of infrastructure projects 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.

KENTUCKY INFRASTRUCTURE AUTHORITY
NOTES TO THE FINANCIAL STATEMENTS
June 30, 2008 and 2007

NOTE 1 - DESCRIPTION OF ORGANIZATION (CONTINUED)

Fund F - Drinking Water State Revolving Fund Loan Program:

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 the Authority's 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 2 - 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 generally accepted accounting principles and have been consistently applied in the preparation of the combined financial statements.

Basis of Accounting:

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. Under the provisions of GASB Statement No. 20, the Division has elected not to follow FASB pronouncements issued after November 30, 1989.

Basis of Presentation:

The Authority follows the provisions of the Governmental Accounting Standards Board Statement No. 34, *Basic Financial Statements – and Management's Discussions and Analysis – for State and Local Governments*, Statement No. 37, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments: Omnibus*, and Statement No. 38, *Certain Financial Statement Note Disclosures*, which establish the financial reporting standards for all state and local government entities.

KENTUCKY INFRASTRUCTURE AUTHORITY
NOTES TO THE FINANCIAL STATEMENTS
June 30, 2008 and 2007

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

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.

Investments:

Investments in marketable securities with readily determinable fair values and all investments in debt securities are reported at their fair values in the statement of financial position. Unrealized gains and losses are included in the change in net assets in the accompanying statement of revenues, expenses and changes in net assets.

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.

Capital Assets:

The Authority's policy is to capitalize purchases of assets over \$5,000 with a useful life of more than one year. All capital assets are valued at cost, less accumulated depreciation. Depreciation is calculated using the straight-line method over the estimated useful lives of the assets, ranging from five to ten years, and is recorded in the statement of activities. The cost of normal maintenance and repairs that do not add to the value of the assets or materially extend assets' lives are reported as expenditures.

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.

KENTUCKY INFRASTRUCTURE AUTHORITY
NOTES TO THE FINANCIAL STATEMENTS
June 30, 2008 and 2007

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

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 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.

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.

Restricted assets:

Certain proceeds from revenue bonds, as well as resources set aside for their repayment, are classified as restricted assets on the statement of net assets because their use is limited by applicable bond covenants.

NOTE 3 - CASH, CASH EQUIVALENTS, AND INVESTMENTS

As of June 30, 2008 and 2007, cash and cash equivalents consist of the following:

	<u>2008</u>		<u>2007</u>
First American Government Obligation Fund	\$ 7,248,543	\$	68,601,510
State cash and investment pool	323,780		(12,859,585)
Total cash and cash equivalents	<u>\$ 7,572,323</u>	<u>\$</u>	<u>55,741,925</u>

KENTUCKY INFRASTRUCTURE AUTHORITY
NOTES TO THE FINANCIAL STATEMENTS
June 30, 2008 and 2007

NOTE 3 - CASH, CASH EQUIVALENTS, AND INVESTMENTS (CONTINUED)

The following schedule presents the carrying amounts of investments by maturity at June 30, 2008:

<u>Investment</u>	<u>Fair Value</u>	<u>Maturity</u>	<u>Rate</u>
FNMA MTN	\$ 9,971,278	07/15/08	3.875
FNMA MTN	19,970,755	08/15/08	3.250
FNMA MTN	19,402,385	09/15/08	3.750
Federal Home Loan Bank	60,509,609	10/14/08	4.500
Federal Home Loan Bank	31,868,179	11/13/08	4.250
U.S. Treasury Security Stripped Interest Payment	45,660	11/15/08	n/a
FNMA Debenture	32,157,139	12/15/08	3.375
Federal Home Loan Bank	29,102,159	01/14/09	3.250
FNMA MTN	29,440,418	02/15/09	3.250
FHLMC Debenture	29,320,648	03/15/09	5.750
U.S. Treasury Security Stripped Interest Payment	20,307	11/15/09	n/a
U.S. Treasury Bond Stripped Principal Payment	108,089	11/15/10	9.875
U.S. Treasury Security Stripped Interest Payment	1,441,779	05/15/11	n/a
U.S. Treasury Security Stripped Interest Payment	261,444	11/15/11	n/a
U.S. Treasury Security Stripped Interest Payment	170,659	11/15/12	n/a
U.S. Treasury Security Stripped Interest Payment	1,265,736	05/15/13	n/a
U.S. Treasury Notes State and Local Governments Series	2,300,209	08/01/14	4.450
U.S. Treasury Notes State and Local Governments Series	1,314,791	08/01/14	4.450
U.S. Treasury Notes State and Local Governments Series	2,481,106	08/01/22	5.120
	<u>271,152,350</u>		
State cash and investment pool	23,698,312		
Total	294,850,662		
Less: current portion	261,788,230		
Long-term investments	\$ <u>33,062,432</u>		

KENTUCKY INFRASTRUCTURE AUTHORITY
NOTES TO THE FINANCIAL STATEMENTS
June 30, 2008 and 2007

NOTE 3 - CASH, CASH EQUIVALENTS, AND INVESTMENTS (CONTINUED)

The following schedule presents the carrying amounts of investments by maturity at June 30, 2007:

<u>Investment</u>	<u>Fair Value</u>	<u>Maturity</u>	<u>Rate</u>
FNMA MTN	\$ 15,093,093	10/15/07	6.625
Federal Home Loan Bank	15,909,942	11/15/07	3.500
Federal Home Loan Bank	15,710,954	12/14/07	4.500
FNMA MTN	5,455,759	01/15/08	4.630
Federal Home Loan Bank	8,076,883	02/15/08	4.500
FHLMC MTN	8,098,460	03/06/08	4.450
FNMA MTN	8,109,009	04/10/08	4.875
FHLMC Debenture	7,345,847	05/05/08	4.300
U.S. Treasury Security Stripped Interest Payment	7,425,132	05/15/08	n/a
FNMA MTN	32,779,664	06/15/08	5.250
FNMA MTN	9,824,892	07/15/08	3.875
FNMA MTN	19,515,650	08/15/08	3.250
FNMA MTN	19,015,305	09/15/08	3.750
U.S. Treasury Security Stripped Interest Payment	43,038	11/15/08	n/a
U.S. Treasury Security Stripped Interest Payment	18,750	11/15/09	n/a
U.S Treasury Bond Stripped Principal Payment	97,917	11/15/10	n/a
U.S. Treasury Security Stripped Interest Payment	1,304,961	05/15/11	n/a
U.S. Treasury Security Stripped Interest Payment	236,368	11/15/11	n/a
U.S. Treasury Security Stripped Interest Payment	151,749	11/15/12	n/a
U.S. Treasury Security Stripped Interest Payment	1,123,406	05/15/13	n/a
U.S. Treasury Notes State and Local Governments Series	1,314,791	08/01/14	4.450
U.S. Treasury Notes State and Local Governments Series	2,300,209	08/01/14	4.450
U.S. Treasury Notes State and Local Governments Series	2,481,108	08/01/22	5.120
U.S. Treasury Notes State and Local Governments Series	3,405,933	08/01/22	5.120
	<u>184,838,820</u>		
State cash and investment pool	<u>9,590,285</u>		
Total	194,429,105		
Less: current portion	<u>124,123,851</u>		
Long-term investments	\$ <u>70,305,254</u>		

At June 30, 2008 and 2007, all of the Authority's investments other than those in U.S. Treasury securities possess a Moody's rating of Aaa or a Standard and Poor's rating of AAA.

KENTUCKY INFRASTRUCTURE AUTHORITY
NOTES TO THE FINANCIAL STATEMENTS
June 30, 2008 and 2007

NOTE 3 - CASH, CASH EQUIVALENTS, AND INVESTMENTS (CONTINUED)

Custodial Credit Risk: For an investment, custodial credit risk is the risk that in the event of the failure of the counterparty, the Authority will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. As of June 30, 2008 and 2007, the Authority's investments are neither insured nor registered, but are held by the Authority's custodial agent in the Authority's name.

Credit Risk: Under State statutes, the Authority is permitted to invest in the following:

- obligations backed by the full faith and credit of the United States
- obligations of any corporation of the United States Government
- collateralized or uncollateralized certificates of deposit issued by banks or other interest-bearing accounts in depository institutions chartered by Kentucky or by the United States
- bankers acceptances
- commercial paper
- securities issued by a state or local government, or any instrumentality or agency thereof in the United States
- United States denominated corporate, Yankee, and Eurodollar securities, excluding corporate stocks, issued by foreign and domestic issuers
- asset-backed securities
- shares of mutual funds, not to exceed 10% of the total funds available for investment
- State and local delinquent property tax claims

Concentration of Credit Risk: The Authority places no limit on the amount the Authority may invest in any one issuer, with the exception of investments in mutual funds as indicated above. The Authority's trustee consults with the Office of Financial Management (within the Finance and Administration Cabinet) to determine suitable investments.

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 arising from increasing interest rates.

KENTUCKY INFRASTRUCTURE AUTHORITY
NOTES TO THE FINANCIAL STATEMENTS
June 30, 2008 and 2007

NOTE 4 - REVENUE BOND FUND ACCOUNTS

Components of the Revenue Bond Fund accounts by cash, cash equivalents and investments at June 30, 2008 are summarized below:

	<u>Cash and cash equivalents</u>	<u>Investments</u>	<u>Total</u>
Operating fund	\$ 10,298	\$ 5,454,629	\$ 5,464,927
Revolving fund	407,666	231,480,446	231,888,112
Government agency fund	6,515,154	599,558	7,114,712
Debt service reserve fund	411	6,096,108	6,096,519
Debt service fund	303,382	0	303,382
Revenue fund	1,914	3,982,986	3,984,900
Surplus fund	9,718	23,538,623	23,548,341
Funds in state pool	323,780	23,698,312	24,022,092
Total	<u>\$ 7,572,323</u>	<u>\$ 294,850,662</u>	<u>\$ 302,422,985</u>

Components of the Revenue Bond Fund accounts by cash, cash equivalents and investments at June 30, 2007 are summarized below:

	<u>Cash and cash equivalents</u>	<u>Investments</u>	<u>Total</u>
Operating fund	\$ 1,139,175	\$ 3,381,662	\$ 4,520,837
Revolving fund	51,965,458	153,675,118	205,640,576
Government agency fund	8,128,532	3,464,274	11,592,806
Debt service reserve fund	146,544	6,096,108	6,242,652
Debt service fund	4,643,570	0	4,643,570
Revenue fund	8,444	0	8,444
Surplus fund	2,569,787	18,221,658	20,791,445
Rebate fund	0	0	0
Funds in state pool	(12,859,585)	9,590,285	(3,269,300)
Total	<u>\$ 55,741,925</u>	<u>\$ 194,429,105</u>	<u>\$ 250,171,030</u>

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.

KENTUCKY INFRASTRUCTURE AUTHORITY
NOTES TO THE FINANCIAL STATEMENTS
June 30, 2008 and 2007

NOTE 4 - REVENUE BOND FUND ACCOUNTS (CONTINUED)

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.

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 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, 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.

KENTUCKY INFRASTRUCTURE AUTHORITY
NOTES TO THE FINANCIAL STATEMENTS
June 30, 2008 and 2007

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 \$483,359,128 in assistance agreements receivable at June 30, 2008, the Authority has commitments remaining to disburse funds summarized as follows:

Fund A - Clean Water State Revolving Fund Loan Program	\$ 250,061,078
Fund B - Infrastructure Revolving Loan Program	12,650,692
Fund C - Governmental Agencies Program	8,518,718
Fund F - Drinking Water State Revolving Fund Loan Program	50,110,740
Total commitments outstanding	<u>\$ 321,341,228</u>

NOTE 6 - CAPITAL ASSETS

Capital asset activity during the year ended June 30, 2008 is as follows:

	Balance June 30, 2007	Increases	Decreases	Balance June 30, 2008
Office equipment	\$ 84,288	\$ 19,354	\$ 0	\$ 103,642
Less accumulated depreciation	84,288	0		84,288
Capital assets - net	\$ 0	\$ 19,354	\$ 0	\$ 19,354

NOTE 7 - 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 fiscal year 2005, 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.

KENTUCKY INFRASTRUCTURE AUTHORITY
NOTES TO THE FINANCIAL STATEMENTS
June 30, 2008 and 2007

NOTE 8 - LONG-TERM DEBT, REVENUE BONDS PAYABLE

Long-term debt consists of the following at June 30, 2008:

	<u>Balance</u>	<u>Current</u>	<u>Long-term</u>
Fund A, Waste Water Revolving Fund Revenue and Revenue Refunding Bonds, interest 2.50% to 6.00%, due semi-annually, principal due annually to June 1, 2024	\$ 31,905,000	\$ 3,465,000	\$ 28,440,000
Fund B, Infrastructure Revolving Fund Revenue Bonds, interest 2.75% to 5.95%, due semi-annually, principal due annually to June 1, 2021	61,295,000	7,970,000	53,325,000
Fund B, Solid Waste Revolving Fund Revenue and Revenue Refunding Bonds, interest 2.50% to 5.50%, due semi-annually, principal due annually to June 1, 2015	3,120,000	570,000	2,550,000
Fund C, Governmental Agencies Program Revenue and Revenue Refunding Bonds, interest 2.25% to 5.50%, due semi-annually, principal due annually to August 1, 2022	33,675,000	3,415,000	30,260,000
Fund F, Drinking Water Revolving Fund Revenue Bonds, interest 3.00% to 6.00%, due semi-annually, principal due annually to June 1, 2024	<u>12,035,000</u>	<u>675,000</u>	<u>11,360,000</u>
Total	142,030,000	16,095,000	125,935,000
Plus: unamortized premium	1,157,795	106,780	1,051,015
Less: unamortized discount	109,773	25,266	84,507
Less: unamortized deferred loss on early retirement of debt	<u>869,045</u>	<u>140,729</u>	<u>728,316</u>
	<u>\$ 142,208,977</u>	<u>\$ 16,035,785</u>	<u>\$ 126,173,192</u>

KENTUCKY INFRASTRUCTURE AUTHORITY
NOTES TO THE FINANCIAL STATEMENTS
June 30, 2008 and 2007

NOTE 8 - LONG-TERM DEBT, REVENUE BONDS PAYABLE (CONTINUED)

Long-term debt consists of the following at June 30, 2007:

	<u>Balance</u>	<u>Current</u>	<u>Long-term</u>
Fund A, Waste Water Revolving Fund Revenue and Revenue Refunding Bonds, interest 2.50% to 6.00%, due semi-annually, principal due annually to June 1, 2024	\$ 35,210,000	\$ 3,305,000	\$ 31,905,000
Fund B, Infrastructure Revolving Fund Revenue Bonds, interest 2.75% to 5.95%, due semi-annually, principal due annually to June 1, 2021	69,040,000	7,745,000	61,295,000
Fund B, Solid Waste Revolving Fund Revenue and Revenue Refunding Bonds, interest 2.50% to 5.50%, due semi-annually, principal due annually to June 1, 2015	3,660,000	540,000	3,120,000
Fund C, Governmental Agencies Program Revenue and Revenue Refunding Bonds, interest 2.25% to 5.50%, due semi-annually, principal due annually to August 1, 2022	36,950,000	3,275,000	33,675,000
Fund F, Drinking Water Revolving Fund Revenue Bonds, interest 3.00% to 6.00%, due semi-annually, principal due annually to June 1, 2024	<u>12,685,000</u>	<u>650,000</u>	<u>12,035,000</u>
Total	157,545,000	15,515,000	142,030,000
Plus: unamortized premium	1,264,574	105,984	1,158,590
Less: unamortized discount	136,378	32,420	103,958
Less: unamortized deferred loss on early retirement of debt	<u>1,009,776</u>	<u>367,004</u>	<u>642,772</u>
	<u>\$ 157,663,420</u>	<u>\$ 15,221,560</u>	<u>\$ 142,441,860</u>

KENTUCKY INFRASTRUCTURE AUTHORITY
NOTES TO THE FINANCIAL STATEMENTS
June 30, 2008 and 2007

NOTE 8 - LONG-TERM DEBT, REVENUE BONDS PAYABLE (CONTINUED)

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

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

	<u>Interest</u>	<u>Principal</u>	<u>Total</u>
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	4,790,323	12,910,000	17,700,323
2013	4,192,851	11,230,000	15,422,851
2014 - 2018	11,964,619	49,685,000	61,649,619
2019 - 2023	2,605,525	22,330,000	24,935,525
2024	42,000	840,000	882,000
	<u>\$ 42,129,419</u>	<u>\$ 142,030,000</u>	<u>\$ 184,159,419</u>

The following summarizes long-term debt activity of the Authority for the year ended June 30, 2008:

	<u>Balance June 30, 2007</u>	<u>Increases</u>	<u>Decreases</u>	<u>Balance June 30, 2008</u>
Bond principal payable	\$ 157,545,000	\$	\$ 15,515,000	\$ 142,030,000
Unamortized premiums	1,264,574		106,780	1,157,794
Less unamortized discounts	136,378		26,604	109,774
Less unamortized gain on defeasance	<u>1,009,776</u>		<u>140,733</u>	<u>869,043</u>
Total	<u>\$ 157,663,420</u>	<u>\$ 0</u>	<u>\$ 15,454,443</u>	<u>\$ 142,208,977</u>

The following summarizes long-term debt activity of the Authority for the year ended June 30, 2007:

	<u>Balance June 30, 2006</u>	<u>Increases</u>	<u>Decreases</u>	<u>Balance June 30, 2007</u>
Bond principal payable	\$ 172,385,000	\$	\$ 14,840,000	\$ 157,545,000
Unamortized premiums	1,370,557		105,983	1,264,574
Less unamortized discounts	168,796		32,418	136,378
Less unamortized gain on defeasance	<u>1,376,780</u>		<u>367,004</u>	<u>1,009,776</u>
Total	<u>\$ 172,209,981</u>	<u>\$ 0</u>	<u>\$ 14,546,561</u>	<u>\$ 157,663,420</u>

KENTUCKY INFRASTRUCTURE AUTHORITY
NOTES TO THE FINANCIAL STATEMENTS
June 30, 2008 and 2007

NOTE 9 - GRANT COMMITMENTS

The Authority has committed to disburse grant funds as follows:

		<u>Amount</u>
Fund B	\$	2,265,652
Fund B - 2020		5,759,001
Total funded by agency funds		<u>8,024,653</u>
Fund B - 2003 HB 269 Coal Development		3,617,906
Fund B - 2003 HB 269 Tobacco Development		7,260,065
Fund B - 2005 HB 267 Coal IEDF		19,889,638
Fund B - 2005 HB 267 Tobacco IEDF		32,550,476
Fund B - 2006 HB 380 Coal		40,032,119
Fund B - 2006 HB 380 Non Coal		88,463,447
Fund B - 2006 HB 380 Community Development		777,062
Fund B - 2008 HB 406 Coal		79,240,000
Fund B - 2008 HB 406 Non Coal		160,584,650
Total funded by bond funds		<u>432,415,363</u>
Total grant commitments	\$	<u>440,440,016</u>

The primary funding sources for Fund B and Fund B - 2020 are from the Authority's revolving funds and the primary source of funds for the remaining commitments are provided from bond funds made available by specific General Assembly House Bills as listed above. Funds committed under House Bill No. 406 above were appropriated during the 2008 session of the General Assembly and are committed to be disbursed during fiscal years 2009 and 2010.

KENTUCKY INFRASTRUCTURE AUTHORITY
NOTES TO THE FINANCIAL STATEMENTS
June 30, 2008 and 2007

NOTE 10 - PAYMENTS FROM THE COMMONWEALTH

Net payments from the Commonwealth during the fiscal years ended June 30, 2008 and 2007 are as follows:

	<u>2008</u>	<u>2007</u>
State Property and Building Commission bond issue - funding of the state match for the KIA Fund A Federally Assisted Wastewater Program per 2005 House Bill 267 and 2006 House Bill 380	\$ 6,200,000	\$ 0
State Property and Building Commission bond issue - funding of the state match for the KIA Fund F Federally Assisted Drinking Water Program per 2005 House Bill 267 and 2006 House Bill 380	6,600,000	0
State Property and Building Commission bond issue - funding of the Infrastructure for Economic Development Fund for Coal Counties per 2005 House Bill 267	17,243,345	22,867,017
State Property and Building Commission bond issue - funding of the Infrastructure for Economic Development Fund for Tobacco Counties per 2005 House Bill 267	29,115,785	29,408,964
State Property and Building Commission bond issue - funding of the Infrastructure for Economic Development Fund for Coal Producing Counties per 2006 House Bill 380	23,259,409	6,867,424
State Property and Building Commission bond issue - funding of the Infrastructure for Economic Development Fund for Non-Coal Producing Counties per 2006 House Bill 380	47,417,842	10,444,191
State Property and Building Commission bond issue - funding of the water and sewer projects from the Community Development Projects per 2006 House Bill 380	<u>762,939</u>	<u>200,000</u>
Total payments from the Commonwealth	\$ <u>130,599,320</u>	\$ <u>69,787,596</u>

KENTUCKY INFRASTRUCTURE AUTHORITY
NOTES TO THE FINANCIAL STATEMENTS
June 30, 2008 and 2007

NOTE 11 - GENERAL FUND APPROPRIATIONS

General Fund appropriations from the Commonwealth during the fiscal years ended June 30, 2008 and 2007 are as follows:

	<u>2008</u>	<u>2007</u>
Appropriations for debt service	\$ 18,188,744	\$ 18,186,960
Appropriations for general and administrative costs	<u>2,569,076</u>	<u>1,799,924</u>
Total general fund appropriations	<u>\$ 20,757,820</u>	<u>\$ 19,986,884</u>

NOTE 12 - RESTRICTED NET ASSETS

Since the use of the Authority's resources is mandated by Kentucky Revised Statute 224A, the Authority considers all net assets other than those invested in capital net of related debt, and restricted for debt service, to be restricted by enabling legislation. Restricted net assets consist of the following at June 30:

	<u>2008</u>	<u>2007</u>
Restricted by enabling legislation	\$ 642,117,272	\$ 576,465,383
Restricted for debt service	<u>6,399,901</u>	<u>10,886,222</u>
Total restricted net assets	<u>\$ 648,517,173</u>	<u>\$ 587,351,605</u>

NOTE 13 - 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 debt 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, 2008 is \$17,003,707.

NOTE 14 - INTERGOVERNMENTAL EXPENSE

Intergovernmental expense for the years ended June 30, 2008 and 2007 totaled \$1,671,970 and \$2,223,049, respectively for services provided by the Commonwealth's Energy and Environment Cabinet, Division of Water related to federal grant compliance for the federal funds administered under Funds A and Funds F.

KENTUCKY INFRASTRUCTURE AUTHORITY
NOTES TO THE FINANCIAL STATEMENTS
June 30, 2008 and 2007

NOTE 15 - RELATED PARTY TRANSACTIONS

The Authority incurred expenses for utilities and office space received from DLG in the amounts of \$29,867 and \$29,700 for the years ending June 30, 2008 and 2007, respectively. The Authority also received the benefit of administrative services from DLG for 2008 and 2007 for which no fee was assessed. Amounts due to DLG at June 30, 2008 and 2007 totaled \$14,880 and \$13,697, respectively.

NOTE 16 - RETIREMENT PLANS

The employees of the Kentucky Infrastructure Authority providing services to the Authority participate in the Kentucky Employees Retirement Systems (KERS) of the Commonwealth of Kentucky, which is a cost-sharing multiple-employer defined benefit pension plan. The plan provides retirement, disability and death benefits to plan members. The KERS provides for cost-of-living adjustments at the discretion of the Kentucky legislature.

Employees who retire at or after age 65 with 48 months of credited services are entitled to a retirement benefit, payable monthly for life, equal to 1.97% to 2.20% of their final-average salary multiplied by their years of service. Final-average salary is the employee's average of the five fiscal years during which the employee had the highest average monthly salary. Benefits fully vest upon reaching five years of service. Vested employees may retire after 27 years of service and receive full retirement benefits or after age 55 and receive reduced retirement benefits. The KERS also provides death and disability benefits. Benefits are established by State statute.

The payroll for employees covered by the KERS for the year ended June 30, 2008 totals approximately \$893,000. The Authority's total payroll totals approximately \$908,000. Covered employees are required by State statute to contribute 5.00% of their salary to the KERS. The Authority is required by the same statute to contribute 8.50% of the covered employees' salaries. The contribution requirement for the year ended June 30, 2008 totals approximately \$79,000. The Authority's contributions for the year ended June 30, 2007 totaled approximately \$63,000.

Ten-year historical trend information showing the KERS' progress in accumulating sufficient assets to pay benefits when due is presented in the Kentucky Employees Retirement System's Annual Financial Reports (which are a matter of public record). The most recent actuarial valuation was as of June 30, 2007. The Commonwealth of Kentucky's Comprehensive Annual Financial Report should be referred to for additional disclosures related to the Kentucky Employees Retirement System.

KENTUCKY INFRASTRUCTURE AUTHORITY
NOTES TO THE FINANCIAL STATEMENTS
June 30, 2008 and 2007

NOTE 16 - RETIREMENT PLANS (CONTINUED)

In addition to the above defined benefit pension plan, the Authority's employees are also eligible to participate in two deferred compensation plans sponsored by the Commonwealth of Kentucky. These plans are organized as a Section 457 plan and as a Section 401(k) plan under the Internal Revenue Code. Both plans permit employees to defer a portion of their salary until future years. Deferred compensation is not available to employees until termination, retirement, death, or financial hardship. The Commonwealth of Kentucky's Comprehensive Annual Financial Report should be referred to for additional disclosures related to the deferred compensation plans.

NOTE 17 - RECLASSIFICATIONS

Certain amounts in the prior-year financial statements have been reclassified for comparative purposes to conform with the presentation in the current-year financial statements.

KENTUCKY INFRASTRUCTURE AUTHORITY
SUPPLEMENTARY SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
 Year ended June 30, 2008

<u>Grant Name</u>	<u>Federal CFDA No.</u>	<u>Grant Number</u>	<u>Grant Period</u>	<u>Expenditures</u>	<u>Passed through to other agencies (including revenue redistributions)</u>
<u>U.S. Environmental Protection Agency</u>					
Direct Programs:					
Capitalization Grants for Clean Water State Revolving Fund	66.458	CS210001-02	10/2003 - 6/2007	\$ 0	\$ 0
Capitalization Grants for Clean Water State Revolving Fund	66.458	CS210001-03	9/2004 - 9/2008	89,389	0
Capitalization Grants for Clean Water State Revolving Fund	66.458	CS210001-04	9/2005 - 9/2007	2,765,046	386,484
Capitalization Grants for Clean Water State Revolving Fund	66.458	CS210001-05	9/2006 - 9/2008	13,166,082	74,174
Capitalization Grants for Clean Water State Revolving Fund	66.458	CS210001-06	7/2007 - 7/2012	2,750,539	0
Capitalization Grants for Clean Water State Revolving Fund	66.458	CS210001-07	6/2008 - 11/2009	0	0
Capitalization Grants for Clean Water State Revolving Fund	66.458	CS210001-08	6/2008 - 6/2010	0	0
Total Capitalization Grants for Clean Water State Revolving Fund				<u>18,771,056</u>	<u>460,658</u>
Capitalization Grants for Drinking Water State Revolving Fund	66.468	FS984547-97	9/1998 - 10/2006	0	0
Capitalization Grants for Drinking Water State Revolving Fund	66.468	FS984547-99	7/2000 - 9/2006	139,105	211,513
Capitalization Grants for Drinking Water State Revolving Fund	66.468	FS984547-00	10/2000 - 9/2005	457,907	0
Capitalization Grants for Drinking Water State Revolving Fund	66.468	FS984547-01	1/2002 - 3/2005	0	156,160
Capitalization Grants for Drinking Water State Revolving Fund	66.468	FS984547-02	1/2002 - 9/2005	20,102	185,575
Capitalization Grants for Drinking Water State Revolving Fund	66.468	FS984547-03	9/2004 - 9/2008	178,898	83,252
Capitalization Grants for Drinking Water State Revolving Fund	66.468	FS984547-04	9/2004 - 9/2009	4,937,942	45,839
Capitalization Grants for Drinking Water State Revolving Fund	66.468	FS984547-05	10/2006 - 9/2008	5,843,828	356,481
Capitalization Grants for Drinking Water State Revolving Fund	66.468	FS984547-06	7/2007 - 7/2012	86,303	172,494
Capitalization Grants for Drinking Water State Revolving Fund	66.468	FS984547-07	6/2008 - 11/2012	0	0
Total Capitalization Grants for Drinking Water State Revolving Fund				<u>11,664,085</u>	<u>1,211,314</u>
Total all programs				<u>\$ 30,435,141</u>	<u>\$ 1,671,972</u>

KENTUCKY INFRASTRUCTURE AUTHORITY
NOTES TO THE SUPPLEMENTARY SCHEDULE OF
EXPENDITURES OF FEDERAL AWARDS
Year ended June 30, 2008

NOTE 1 - BASIS OF ACCOUNTING

The accompanying schedule of expenditures of federal awards includes the federal grant activity of the Authority and is presented on the accrual basis of accounting. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, *Audits of State, Local Governments, and Non-Profit Organizations*. Therefore, some amounts in this schedule may differ from amounts presented in, or used in the preparation of, the basic financial statements.

NOTE 2 - PASSED THROUGH TO OTHER ENTITY

<u>CFDA No.</u>	<u>Name of Grant</u>	<u>Amount</u>	<u>Pass Through Entity</u>
66.458	Clean Water State Revolving Funds	\$ 460,658	Environmental and Public Protection Cabinet
66.468	Drinking Water State Revolving Funds	\$ 1,211,314	Environmental and Public Protection Cabinet

KENTUCKY INFRASTRUCTURE AUTHORITY
COMBINING STATEMENT OF NET ASSETS

June 30, 2008

A S S E T S

	Fund A	Fund B	Fund C	Fund F	Total
Current assets:					
Cash and cash equivalents	\$ (801,398)	\$ 7,144,275	\$ 11,710	\$ 913,943	\$ 7,268,530
Cash and cash equivalents, restricted for debt service	0	68	303,725	0	303,793
Investments, current portion	198,500,147	18,591,801	24,414,464	20,281,818	261,788,230
Federal funds receivable	3,054,386	0	0	389,772	3,444,158
General fund appropriations receivable		320,766			320,766
Accrued interest receivable, investments	348,573	75,863	330,583	36,439	791,458
Accrued interest receivable, loans	539,374	163,453	328,896	199,815	1,231,538
Current maturities of long-term receivables	21,758,915	3,748,851	4,830,145	3,989,016	34,326,927
Total current assets	<u>223,399,997</u>	<u>30,045,077</u>	<u>30,219,523</u>	<u>25,810,803</u>	<u>309,475,400</u>
Investments	4,389,559	15,999,734	3,268,014	3,309,017	26,966,324
Investments, restricted for debt service	0	0	6,096,108	0	6,096,108
Total noncurrent investments	<u>4,389,559</u>	<u>15,999,734</u>	<u>9,364,122</u>	<u>3,309,017</u>	<u>33,062,432</u>
Long-term receivables:					
Assistance agreements receivable:					
Principal	306,056,047	53,768,643	37,947,015	88,239,135	486,010,840
Less:					
Current maturities	(21,758,915)	(3,748,851)	(4,830,145)	(3,989,016)	(34,326,927)
Deposit reserve			(1,762,826)		(1,762,826)
Unamortized premiums			(860,770)		(860,770)
Funds held for governmental agencies			(28,116)		(28,116)
Total long-term receivables	<u>284,297,132</u>	<u>50,019,792</u>	<u>30,465,158</u>	<u>84,250,119</u>	<u>449,032,201</u>
Capital assets, net		19,354			19,354
Other assets:					
Unamortized costs of issuance	323,014	545,571	245,966	129,331	1,243,882
Total assets	<u>\$ 512,409,702</u>	<u>\$ 96,629,528</u>	<u>\$ 70,294,769</u>	<u>\$ 113,499,270</u>	<u>\$ 792,833,269</u>

L I A B I L I T I E S

Current liabilities:					
Current maturities of revenue bonds payable, less unamortized discounts and deferred loss on early retirement of debt	\$ 3,383,962	\$ 8,461,755	\$ 3,516,044	\$ 674,024	\$ 16,035,785
Accrued interest payable	126,725	272,117	645,753	49,825	1,094,420
Due to Division of Water	94,077	0	0	303,470	397,547
Due to the Department of Local Governments		14,880			14,880
Other payables		580,918			580,918
Total current liabilities	<u>3,604,764</u>	<u>9,329,670</u>	<u>4,161,797</u>	<u>1,027,319</u>	<u>18,123,550</u>
Long-term debt:					
Revenue bonds payable, less current maturities and unamortized discounts and deferred loss on early retirement of debt	28,083,741	55,710,781	31,028,043	11,350,627	126,173,192
Total liabilities	<u>31,688,505</u>	<u>65,040,451</u>	<u>35,189,840</u>	<u>12,377,946</u>	<u>144,296,742</u>
Invested in capital net of related debt		19,354			19,354
Restricted net assets	480,721,197	31,569,723	35,104,929	101,121,324	648,517,173
Total net assets	<u>\$ 480,721,197</u>	<u>\$ 31,569,077</u>	<u>\$ 35,104,929</u>	<u>\$ 101,121,324</u>	<u>\$ 648,536,527</u>

KENTUCKY INFRASTRUCTURE AUTHORITY
COMBINING STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NETS ASSETS
 Year ended June 30, 2008

	Fund A	Fund B	Fund C	Fund F	Total
Operating revenues:					
Assistance agreements:					
Servicing fee	\$ 495,965	\$ 100,404	\$ 71,961	\$ 144,378	\$ 812,708
Interest	5,722,691	1,272,839		1,642,487	8,638,017
Interest received securing revenue bonds			1,704,468		1,704,468
Amortization of premium		742,580	60,054		802,634
Grant administration fee	38,194	67,882		704	742,580
Amortization of bond premium					106,780
Total operating revenues	<u>6,256,850</u>	<u>2,183,705</u>	<u>1,836,483</u>	<u>1,787,569</u>	<u>12,064,607</u>
Operating expenses:					
General and administrative	204,489	3,073,865	10,416	388,094	3,676,864
Intergovernmental administrative expense reimbursement	460,657			1,211,313	1,671,970
Grants		131,641,342			131,641,342
Revenue bonds payable:					
Amortization of discount	18,456	6,468		1,680	26,604
Amortization of costs of issuance	45,348	58,836	24,804	9,768	138,756
Interest	1,756,307	3,765,399	1,457,579	622,455	7,601,740
Total operating expenses	<u>2,485,257</u>	<u>138,545,910</u>	<u>1,492,799</u>	<u>2,233,310</u>	<u>144,757,276</u>
Operating income (loss)	<u>3,771,593</u>	<u>(136,362,205)</u>	<u>343,684</u>	<u>(445,741)</u>	<u>(132,692,669)</u>
Nonoperating revenues:					
Income from investments	7,896,522	2,189,311	2,792,323	823,170	13,701,326
Net increase (decrease) in fair market value of investments	(1,703,127)	(53,886)	(1,355,954)	(175,019)	(3,287,986)
Federal grants and reimbursements	19,231,713			12,875,398	32,107,111
Net payments from the Commonwealth	6,200,000	117,799,320		6,600,000	130,599,320
State appropriations	4,972,789	14,510,431		1,274,600	20,757,820
Total nonoperating revenues	<u>36,597,897</u>	<u>134,445,176</u>	<u>1,436,369</u>	<u>21,398,149</u>	<u>193,877,591</u>
Change in net assets	<u>40,369,490</u>	<u>(1,917,029)</u>	<u>1,780,053</u>	<u>20,952,408</u>	<u>61,184,922</u>
Net assets, beginning of year	<u>440,351,707</u>	<u>33,506,106</u>	<u>33,324,876</u>	<u>80,168,916</u>	<u>587,351,605</u>
Net assets, end of year	<u>\$ 480,721,197</u>	<u>\$ 31,589,077</u>	<u>\$ 35,104,929</u>	<u>\$ 101,121,324</u>	<u>\$ 648,536,527</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 (Authority) as of and for the year ended June 30, 2008, and have issued our report thereon dated December 9, 2008. 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.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Kentucky Infrastructure Authority's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Authority's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Authority's internal control over financial reporting.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the Authority's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the Authority's financial statements that is more than inconsequential will not be prevented or detected by the Authority's internal control.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the Authority's internal control.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

To the Board of Directors
Kentucky Infrastructure Authority
Frankfort, Kentucky

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Compliance and Other Matters

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 grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

We noted certain matters that we reported to management of the Authority in a separate letter dated December 9, 2008.

This report is intended solely for the information and use of the Board of Directors, management, the Auditor of Public Accounts of the Commonwealth of Kentucky, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties. However, this report is a matter of public record and its distribution is not limited.

Potter & Company, LLP

POTTER & COMPANY, LLP
December 9, 2008



**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 (Authority) with the types of compliance requirements described in the U. S. Office of Management and Budget (OMB) Circular A-133 *Compliance Supplement* that are applicable to its major federal program for the year ended June 30, 2008. 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 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 the 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, 2008.

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 the 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, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the Authority's internal control over compliance.

To the Board of Directors
Kentucky Infrastructure Authority
Frankfort, Kentucky

Page Two

A control deficiency in an entity's internal control over compliance exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect noncompliance with a type of compliance requirement of a federal program on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to administer a federal program such that there is more than a remote likelihood that noncompliance with a type of compliance requirement of a federal program that is more than inconsequential will not be prevented or detected by the entity's internal control.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that material noncompliance with a type of compliance requirement of a federal program will not be prevented or detected by the entity's internal control.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses, as defined above.

This report is intended solely for the information and use of the Board of Directors, management, the Auditor of Public Accounts of the Commonwealth of Kentucky, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties. However, this report is a matter of public record and its distribution is not limited.

Potter & Company, LLP

POTTER & COMPANY, LLP
December 9, 2008



KENTUCKY INFRASTRUCTURE AUTHORITY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
Year ended June 30, 2008

Summary of auditor's results

We have issued an unqualified opinion, dated December 9, 2008, on the financial statements of Kentucky Infrastructure Authority as of and for the year ended June 30, 2008.

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 December 9, 2008, 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, 2008, were the U.S. Environmental Protection Agency, CFDA No. 66.458 and CFDA No. 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, 2007

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

