KENTUCKY INFRASTRUCTURE AUTHORITY

FINANCIAL STATEMENTS

AND

SUPPLEMENTARY INFORMATION

JUNE 30, 2018

KENTUCKY INFRASTRUCTURE AUTHORITY

TABLE OF CONTENTS
JUNE 30, 2018

DEANDORTON
DEAN DORTON ALLEN FORD, PLLC

Report of Independent Auditors

Board of Directors
Kentucky Infrastructure Authority
Frankfort, Kentucky

Report on the Financial Statements

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, 2018, and the related notes to the financial statements, which collectively comprise the Authority's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. 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 from material misstatement.

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

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

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, 2018, and the changes in financial position and cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis on pages 4 to 8, the Schedule of Proportionate Share of Net Pension Liability on page 36, the Schedule of Pension Contributions on page 37, the Schedule of Proportionate Share of Net OPEB Liability on page 38 and the Schedule of OPEB Contributions on page 39 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information

Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise the Authority's basic financial statements. The accompanying Supplementary Schedule of Expenditures of Federal Awards on pages 40 to 42, as required by Title 2 U.S. *Code of Federal Regulations* (CFR) Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards*, Combining Statement of Net Position on page 43 and Combining Statement of Revenues, Expenses and Changes in Net Position on page 44 (the Supplementary Information) are presented for purposes of additional analysis and are not a required part of the basic financial statements.

The Supplementary Information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the Supplementary Information is fairly stated, in all material respects, in relation to the basic financial statements as a whole.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated November 19, 2018 on our consideration of the Authority's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is solely 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 effectiveness of the Authority's internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Authority's internal control over financial reporting and compliance.

Dean Dorton Allen Ford, PLLC

November 19, 2018
Louisville, Kentucky

As management of the Kentucky Infrastructure Authority (the Authority), a component unit of the Commonwealth of Kentucky (the Commonwealth), 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 year ended June 30, 2018. We encourage readers to read it in conjunction with the Authority's audited financial statements and the accompanying notes.

FINANCIAL HIGHLIGHTS

- As of the close of fiscal year 2018, the Authority reported an ending net position of $1,137,549,155, an increase of $36,540,978 (3.3%) compared to the prior year.
- The Authority's total liabilities at June 30, 2018 increased $923,385 (0.3%) compared to the prior year.
- During the year ended June 30, 2018 the Authority disbursed $120,783,256 to borrowers for eligible expenditures under loan assistance agreements and $5,552,914 to local governmental entities for state grants.
- During the year ended June 30, 2018, principal and interest in the amount of $79,389,698 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 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 position presents information on all of the Authority's assets and deferred outflows less its liabilities and deferred inflows, with the difference between the two reported as net position. Over time, increases or decreases in net position 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 position shows how the Authority's net position changed during the most recent fiscal year. All changes in net position are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of the related cash flows. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods.

The statement of cash flows provides relevant information about the cash receipts and cash payments of the Authority during the fiscal year. The statement shows the differences between actual cash receipts and 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 through 35.

FINANCIAL ANALYSIS OF THE AUTHORITY

Condensed Financial Information
Statements of Net Position
As of June 30

	2018	Increase (Decrease)	2017
Assets:			
Current assets	$ 367,386,946	-1.4%	$ 372,559,492
Long-term investments	1,043,055	-85.0%	6,945,000
Long-term receivables	1,041,396,479	5.0%	991,447,812
Capital assets, net	8,530	-45.2%	15,554
Total assets	1,409,835,010	2.8%	1,370,967,858
Deferred outflows of resources	7,054,968	-6.8%	7,572,724
Liabilities:			
Current liabilities	28,113,006	-9.7%	31,134,997
Long-term debt	249,958,958	1.6%	246,012,982
Total liabilities	278,071,964	0.3%	277,147,979
Deferred inflows of resources	1,268,859	230.1%	384,426
Net position:			
Net investment in capital assets	8,530	-45.2%	15,554
Restricted net position	1,137,540,625	3.3%	1,100,992,623
Total net position	$ 1,137,549,155	3.32%	$ 1,101,008,177

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

During 2018, the Authority's total cash and cash equivalents and investments decreased $12,492,189.

At June 30, 2018, investments consist of a current portion of $297,628,241 and a non-current portion of $1,043,055. The current portion is composed of U.S. Government Agency debt securities with maturities longer than three months when purchased, but also having maturities prior to June 30, 2019. The non-current portion is composed 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 primarily consist of a concentration of investments with a maturity of six months or less when purchased (cash equivalents) in order to maintain sufficient liquidity.

During fiscal year 2018, payments to borrowers for eligible expenditures under assistance agreements were $120,783,256, which exceeded repayments of assistance agreements receivable of $62,499,921 and forgiveness of loan principal of $4,662,136 contributing to the $53,681,594 (5.1%) increase in net assistance agreements receivable.

Total liabilities consist of bonds payable and related accrued interest; miscellaneous accounts and state grants payable, and accrued pension liabilities.

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

	2018	Increase (Decrease)	2017
Operating revenues	$ 19,241,581	5.4%	$ 18,263,606
Operating expenses	21,285,325	-7.4%	22,987,381
Operating loss	(2,043,744)	-56.7%	(4,723,775)
Non-operating revenues (expenses):			
Investment Income	3,521,472	80.6%	1,950,279
Federal grants and reimbursements	29,669,934	-12.9%	34,057,992
Provision for losses on assistance agreements	0	100.0%	(2,000,000)
Loan subsidy required by federal capitalization grants	(4,662,136)	-40.7%	(7,867,718)
Intergovernmental revenue from the Commonwealth	9,609,701	-10.8%	10,776,399
State appropriations	1,141,979	-4.8%	1,200,000
Change in net position	$ 37,237,206	11.5%	$ 33,393,177

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 $975,611 (5.3%) from fiscal year 2017 due to the increase in assistance agreements receivable.

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 to local taxing districts of the Commonwealth as appropriated by the General Assembly. Current year state grant expenditures decreased $686,264 (10.7%) from 2017 due to continued budgetary constraints of the Commonwealth. Interest expense on revenue bonds decreased $774,744 (6.7%). General and administrative costs decreased $867,241 inclusive of a $690,955 decrease in net changes due to pension expenses under Governmental Accounting Standards Board (GASB) 68, Accounting and Financial Reporting for Pensions. Additionally $31,000 expense was recorded in 2018 due to the implementation of GASB 75, Accounting and Financial Reporting for Post-Employment Benefits Other Than Pensions (OPEB) which was implemented at the beginning of fiscal 2018.

Non-operating revenues and expenses consist of income from investments, net changes in the fair market value of investments, debt issue costs, federal grant revenues and required principal forgiveness, provisions for losses on assistance agreements, intergovernmental revenues and state appropriations. Federal grant revenues and expenditures totaled $29,669,934 for loans made to municipalities under federal programs and the cost of administration of the programs. A portion of these funds was awarded under federal regulations that required additional subsidization which the Authority chose to provide as principal forgiveness. For 2018, $4,662,136 in loan principal forgiveness was recorded as an expense in the statement of revenues, expenses, and changes in net position. The Authority did not record any additional provision for loan losses during the year. For details related to intergovernmental revenues, refer to Note 9 of the financial statements. For details on state appropriations, refer to Note 10 of the financial statements.

LONG-TERM DEBT

At June 30, 2018, the Authority had $230,435,000 in bond principal outstanding which is an increase of 0.6% from last year. In March 2018 the Authority defeased $38,490,000 of Series 2010A and 2012A bonds with existing cash. In April 2018 the Authority issued $60,000,000 in Series 2018A Revenue bonds to fund additional loan commitments. More detailed information about the Authority's long-term liabilities is presented in Note 7 of the financial statements.

Bond Ratings. As of June 30, 2018, the Wastewater and Drinking Water program supported debt rating is Aaa from Moody's and AAA from Standard & Poor's and Fitch. The Governmental Agencies program revenue bonds of the Authority are rated AA by Standard & Poor's. The Authority has no appropriation supported debt outstanding.

Limitations on Debt. The Authority is required by Kentucky Revised Statute (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 five hundred million dollars ($500,000,000) (KRS 224A. 165 (2) (b). The Authority's outstanding debt, which meets this criterion, is significantly below this limit.

Outstanding debt at June 30 consists of the following:

	2018	Increase (Decrease)	2017
Program revenue supported debt	$ 230,435,000	0.6%	$ 228,985,000

CURRENTLY KNOWN FACTS, DECISIONS, OR CONDITIONS

The Authority administers grants under numerous House Bills. At June 30, 2018 approximately $11,545,000 remained to be disbursed as outlined in Note 8 of the financial statements.

CONTACTING THE AUTHORITY'S FINANCIAL MANAGEMENT

This report is designed to provide our stakeholders with information needed to understand the Authority's financial condition and results of operations for the fiscal year ended June 30, 2018. For questions about this report or for additional financial information, contact Kentucky Infrastructure Authority, Fiscal Officer, 1024 Capital Center Drive, Suite 340, Frankfort, Kentucky 40601.

KENTUCKY INFRASTRUCTURE AUTHORITY

STATEMENT OF NET POSITION

JUNE 30, 2018

ASSETS	
Current assets:	
Cash and cash equivalents	$ 4,377,397
Investments, current portion	297,628,241
Intergovernmental receivables	463,614
Accrued interest receivable, investments	265,745
Accrued interest receivable, assistance agreements	1,433,949
Current maturities of long-term receivables	63,218,000
Total current assets	367,386,946
Investments	432,555
Investments, restricted for debt service	610,500
Total noncurrent investments	1,043,055
Long-term receivables:	
Assistance agreements receivable	
Principal	1,043,653,199
Allowance for losses on assistance agreements	(2,000,000)
Unamortized discounts	(256,720)
Total long-term receivables	1,041,396,479
Capital assets, net	8,530
Total assets	1,409,835,010
Deferred outflows of resources:	
Pension related	920,001
Post-employment benefits other than pension	171,054
Unamortized deferred amount on refunding	5,963,913
Total deferred outflows of resources	7,054,968
LIABILITIES	
Current liabilities:	
Current maturities of revenue bonds payable, net of unamortized premiums and discounts	$ 23,445,921
Accrued interest payable	3,984,699
State treasury advances for capitalization grant matching funds	288,384
Grants payable	391,927
Other payables	2,075
Total current liabilities	28,113,006
Long-term liabilities:	
Revenue bonds payable, less current maturities and unamortized premiums and discounts	243,966,282
Net pension liability	4,644,598
Net post-employment benefits other than pension liability	879,752
Other payables	468,326
Total liabilities	278,071,964
Deferred inflows of resources:	
Pension related	1,118,059
Post-employment benefits other than pension	18,932
Unamortized deferred amount on refunding	131,868
Total deferred inflows of resources	1,268,859
NET POSITION	
Net investment in capital assets	8,530
Restricted net position	1,137,540,625
Total net position	$1,137,549,155

See accompanying notes to the financial statements.

KENTUCKY INFRASTRUCTURE AUTHORITY

STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET POSITION
FOR THE YEAR ENDED JUNE 30, 2018

Operating revenues:	
Assistance agreements:	
Servicing fee	$ 2,225,575
Interest income	17,016,006
Total operating revenues	19,241,581
Operating expenses:	
General and administrative	2,399,692
Intergovernmental administrative expense reimbursement	7,544,939
State grant expenditures	5,727,841
Revenue bonds:	
Amortization of bond premiums	(3,494,940)
Interest	10,863,048
Arbitrage expense	33,477
Gain on early extinguishment of bonds payable	(2,254,088)
Bond issuance cost	465,356
Total operating expenses	21,285,325
Operating loss	(2,043,744)
Non-operating gain / (loss):	
Investment income	3,521,472
Federal grants	29,669,934
Loan subsidy required by federal capitalization grants	(4,662,136)
Intergovernmental revenue from the Commonwealth	9,609,701
State appropriations	1,141,979
Total non-operating revenues	39,280,950
Change in net position	$ 37,237,206
Net position, beginning of year (as previously stated)	1,101,008,177
Cumulative effect on prior years (to June 30, 2017) resulting from the retroactive change in accounting for postemployment benefits other than pensions (See Note 2)	(696,228)
Net position, beginning of year (as adjusted)	1,100,311,949
Net position, end of year	$ 1,137,549,155

See accompanying notes to the financial statements.

KENTUCKY INFRASTRUCTURE AUTHORITY

STATEMENT OF CASH FLOWS

FOR THE YEARS ENDED JUNE 30, 2018

Cash flows from operating activities:	
Administrative fees received	$ 2,225,575
Collections on assistance agreements	62,499,921
Advances on assistance agreements	(120,783,256)
Interest received on assistance agreements	16,889,777
Cash payments for grants	(5,552,914)
Cash payments for personnel expenses	(1,121,852)
Cash payments to suppliers for goods and services	(11,407,943)
Net cash used in operating activities	(57,250,692)
Cash flows from noncapital financing activities:	
Principal payments on long-term debt	(20,060,000)
Interest paid on long-term debt	(10,585,394)
Payments to refund and defease debt	(41,508,664)
Bond issuance cost	(465,356)
Proceeds from new debt issuance	70,993,064
Receipt of federal grants	29,669,934
State appropriations	1,141,979
Payments from the Commonwealth	12,296,036
Net cash provided by noncapital financing activities	41,481,599
Cash flows from noncapital financing activities:	
Purchase of capital assets	0
Cash flows from investing activities:	
Purchase of investment securities	(958,027,913)
Proceeds from sale and maturities of investment securities	971,322,097
Interest and other investment income received	5,085,424
Net cash provided by investing activities	18,379,608
Net change in cash and cash equivalents	2,610,515
Cash and cash equivalents, beginning of year	1,766,882
Cash and cash equivalents, end of year	$ 4,377,397

See accompanying notes to the financial statements.

KENTUCKY INFRASTRUCTURE AUTHORITY

STATEMENT OF CASH FLOWS

FOR THE YEARS ENDED JUNE 30, 2018

Reconciliation of operating loss to net cash used in operating activities:		
Operating loss	$	(2,043,744)
Adjustments to reconcile operating loss to net cash used in operating activities:		
Gain on early extinguishment of bonds payable		(2,254,088)
Amortization of bond premium		(3,494,940)
Amortization of assistance agreements discounts		(60,280)
Amortization of bond defeasance		690,955
Loss on early extinguishment of bonds payable		
Interest paid on long-term debt		10,585,394
Bond issue cost		465,356
Depreciation		6,470
Changes in assets and liabilities:		
Accrued interest receivable		(65,949)
Assistance agreements receivable		(58,283,335)
Accrued interest payable		(413,301)
State treasury advances for capitalized grant matching fund		(2,008,616)
Local Government		
Grants payable		174,927
Other payables		(577,599)
Deferred outflow		(205,055)
Deferred inflow		916,991
Net pension liability		(867,402)
Net OPEB liability		183,524
Net cash used in operating activities	$	(57,250,692)

See accompanying notes to the financial statements.

1. DESCRIPTION OF ORGANIZATION

In 1972, the General Assembly of Kentucky established the Kentucky Pollution Abatement Authority (KPAA) after determining that pollution was seriously harming the Commonwealth of Kentucky's (the Commonwealth) 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. KPAA was created to maximize federal grant participation in the Commonwealth in respect to 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 to remove the prior requirement that federal grant participation be obtained by local units of government as a condition precedent to KPAA aid. The Act was further amended in 1978 to grant to KPAA 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 KPAA 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 KPAA 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 agency'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 agency to the "Kentucky Infrastructure Authority" (the 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.

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 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 Kentucky Revised Statute (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 restrict the amount of notes and bonds the Authority can have outstanding. The purpose of the loans is to assist eligible entities in financing the construction of infrastructure projects. The following provides a description of the Authority's various programs:

Fund A - Clean Water State Revolving Fund Loan Program

Wastewater treatment, collection, and storm water projects that qualify under the U.S. Environmental Protection Agency (EPA) requirements can be financed through this program. Projects must be ranked on the Priority List using the Kentucky Division of Water Priority System Guidance and must be financially feasible as determined by the Authority's staff. Loans are provided at below-market interest rates with repayments not to exceed thirty years. Loan funds are available on short terms for planning and design activities. The state's share of construction (state match funds) is funded with state appropriation – supported bonds for which the Commonwealth appropriates an amount equal to the related debt.

Fund B - Infrastructure Revolving Loan Program

The Infrastructure Revolving Fund (Fund B) was created by KRS 224A.112 for the construction and acquisition of infrastructure projects. Infrastructure projects are defined in KRS 224A.011 as "any construction or acquisition of treatment works, facilities related to the collection, transportation, and treatment of wastewater as defined in KRS 65.8903, distribution facilities, or water resources projects instituted by a governmental agency or an investor-owned water utility which is approved by the authority and, if required, by the Energy and Environment Cabinet, Public Service Commission, or other agency; solid waste projects; dams; storm water control and treatment systems; gas or electric utility; broadband deployment project; or any other public utility or public service project which the authority finds would assist in carrying out the purposes set out in KRS 224A.300".

Loans are provided at or below market rates with repayments not to exceed thirty years. Grants are available, but are reserved for borrowers where the Authority determines both a hardship and extreme health hazard exist.

As part of this program, a 2020 water service fund was established to assist in making potable water available to all Kentuckians by the year 2020.

The General Assembly has periodically appropriated funds to be administered by the Authority in the form of water and wastewater grants. Activities for these grants are accounted for in Fund B.

Fund C - Governmental Agencies Program

This program provides local governmental agencies access to funding through the municipal bond market at better terms than could be obtained on an individual basis. Financial assistance is available in the form of loans with repayment terms not to exceed thirty years for the construction or acquisition of infrastructure projects by governmental entities in the Commonwealth.

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 EPA requirements. Projects must be ranked on the Priority List using the Kentucky Division of Water Priority System Guidance and must be financially feasible as determined by the Authority's staff. Loans are provided at below-market interest rates with repayments not to exceed thirty years. Loans funds are available on short terms for planning and design activities. The state's share of construction (state match funds) is funded with state appropriation-supported bonds for which the Commonwealth appropriates an amount equal to the related debt service.

2. SIGNIFICANT ACCOUNTING POLICIES

This summary of significant accounting policies of the Authority is presented to assist in understanding the financial statements. The financial statements and notes are representations of the 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 financial statements.

Basis of Accounting

The activities of the Authority are accounted for as an enterprise fund on the accrual basis of accounting. Accordingly, revenues are recognized when they are earned and expenditures are recognized when they are incurred.

Change in Accounting Principle

Effective July 1, 2017, the Authority was required to adopt Governmental Accounting Standards Board (GASB) Statement No. 75, Accounting and Financial Reporting for Post-employment Benefits Other than Pensions (OPEB) (Statement 75). Statement 75 replaces the requirement of GASB Statements No. 45, Accounting and Financial Reporting by Employers for Post-employment Benefits Other Than Pensions, as amended, and No. 57, OPEB Measurements by Agent Employers and Agent Multiple-Employer Plans. Statement 75 is applicable for government agencies that provide defined benefit OPEB to recognize their long-term obligation for OPEB as a liability to more comprehensively and comparably measure the annual cost. The Authority participates in the Kentucky Employees Retirement System OPEB plan administered by the Board of Trustees of the Kentucky Retirement Systems. This is a cost- sharing, multiple-employer defined benefit OEPB plan, which covers all eligible full-time employees and provides health insurance benefits. Cost-sharing governmental employers, such as the Authority, are required to report a net OPEB liability, OPEB expense, and OPEB-related deferred outflow and inflows of resources based on their proportionate share of the collective amounts for all government agencies in the plan. Net position as of the beginning of the year was reduced by $696,228 to reflect the adoption of Statement 75.

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. Actual results may differ from those estimates.

Cash and Cash Equivalents

The Authority reports all highly liquid investments with a maturity of three months or less when purchased as cash equivalents.

Investments

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

Description of Net Position Classes

Accounting principles generally accepted in the United States of America require the classification of net position into three components – net investment in capital assets; restricted; and unrestricted. These classifications are defined as follows:

Net investment in capital assets – This component of net position consists of capital assets, including restricted capital assets, net of accumulated depreciation and reduced by the outstanding balances of any bonds, mortgages, notes, or other borrowings that are attributable to the acquisition, construction, or improvement of those assets. If there are significant unspent related debt proceeds at year end, the portion of the debt attributable to the unspent proceeds are not included in the calculation of net investment in capital assets. Rather, that portion of the debt is included in the same net position component as unspent proceeds.

Restricted – This component of net position consists of constraints placed on the use of net position through external constraints imposed by creditors (such as through debt covenants), grantors, contributors, or laws or regulations of other governments or constraints imposed by law through constitutional provisions or enabling legislation.

Unrestricted – This component of net position consists of net position that does not meet the definition of “restricted” or “net investment in capital assets.”

Assistance Agreements Receivable and Allowance for Loan Losses

Assistance agreements receivable are stated at their outstanding principal balances net of allowances for loan losses. The allowance for loan losses is evaluated at least annually and is established through a provision for loan Losses and is charged to expense. Loans are charged against the allowance for loan losses when management believes that the collectability of the principal is unlikely. The allowance is an amount that management believes will be adequate to absorb losses on existing loans that may become uncollectible and is based on individual assessments of their collectability. The Authority has never incurred a loss of principal on a loan. Therefore, prior loan loss experience is not considered in the evaluation. Management believes the allowance for loan losses is adequate. While management uses available information and considers potential remedies to recognize the amount of losses on loans, these evaluations are subjective and future adjustments to the allowance may be necessary if the results of mitigation efforts differ substantially from the original loss estimates.

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. The results of this method do not materially differ from those that would be obtained by applying the effective interest method.

Amortization of Bond Premium

Bond premiums are amortized on the straight-line method over the life of the bond issue. The results of this method do not materially differ from those that would be obtained by applying the effective interest method.

Deferred Gain or Loss on Early Retirement of Debt

Gain or loss on early retirement of debt utilizing external funds is reported as deferred outflow and deferred inflow and amortized on the straight-line method over the original remaining life of the old debt or the life of the new debt, whichever is shorter. The results of this method do not materially differ from those that would be obtained by applying the effective interest method. Gain or loss on early retirement of debt utilizing existing Authority funds is recognized in the period of the defeasance transaction.

Operating Revenues and Expenses

The Authority reports service fees and interest income received on loans as operating revenue. General and administrative expenses, the cost of services provided by the Commonwealth Energy and Environment Cabinet's Division of Water related to federal grant compliance and project administration, and net expenses on leverage bonds that are issued to fund the Authority's loans are reported as operating expense.

Pensions and Other Post-Employment Benefits (OPEB)

For purposes of measuring the net pension and other post-employment benefits liabilities, deferred outflows of resources, deferred inflows of resources related to pension and OPEB expenses, information about the fiduciary net position of Kentucky Employees' Retirement Systems (KERS) and addition to/deduction from KERS's fiduciary net position have been determined on the same basis as they are reported by KERS.

3. CASH, CASH EQUIVALENTS, AND INVESTMENTS

All cash and investments of the Authority, except for cash deposited with the state, are held by a trustee bank. Most of these assets are either pledged as collateral for bond indebtedness, have certain investment restrictions as outlined in the bond indentures, or both.

As of June 30, 2018 cash and cash equivalents consist of the following:

First American Government Obligation Fund	$ 3,452,824
State cash and investment pool	924,573
Total cash and cash equivalents	$ 4,377,397

The following schedule presents the carrying amounts of investments by maturity at June 30, 2018:

Investment	Fair Value	Maturity	Rate	Credit Rating
U S Treasury Bill	$ 24,569,448	07/12/18	1.75%	N/A
Federal Home Loan Bank Discount Notes	51,059,879	07/13/18	0.00%	AAA
FNMA Discount Notes	11,608,379	07/13/18	0.00%	AAA
Federal Home Loan Bank Discount Notes	19,684,620	07/16/18	0.00%	AAA
U S Treasury Notes	37,460,250	08/15/18	1.00%	AAA
U S Treasury Bill	1,010,690	08/16/18	1.85%	N/A
U S Treasury Notes	27,186,520	08/31/18	0.75%	AAA
Federal Home Loan Bank Discount Notes	54,219,053	09/17/18	0.00%	AAA
Federal Home Loan Bank Discount Notes	10,520,942	10/15/18	0.00%	AAA
U S Treasury Bill	56,640,606	12/13/18	0.00%	N/A
U S Treasury Notes	432,555	01/15/19	1.13%	AAA
U S Treasury Notes State & Local Government Securities	610,500	08/01/22	5.12%	N/A
	295,003,442			
Investment in state pool	3,667,854			
Total	298,671,296			
Less current portion	(297,628,241)			
Long-term investments	$ 1,043,055			

At June 30, 2018 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 AA+.

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, 2018, 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
- obligations of government sponsored entities
- 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 it 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 (Finance and Administration Cabinet) to determine suitable investments.

At June 30, 2018 the Authority maintained $4,592,427 of cash and investments with the State Investment Pool of the State Investment Commission of the Commonwealth of Kentucky. The State Investment Commission (the Commission) is charged with the oversight of the Commonwealth's investment programs pursuant to KRS 42.500. The Commission delegates the day to day management of the Commonwealth's investments to the Office of Financial Management (OFM). The purpose of the investment pools is to provide: economies of scale that enhance yield, ease of administration for both the user agencies and OFM, and increase accountability and control. All investments shall be permitted investments as defined in KRS 42.500 and as further limited by 200 Kentucky Administrative Regulation (KAR) Chapter 14. Funds in the pools are available to be spent at any time. The Authority had no collateral or insurance as security for the balances with the Commission at June 30, 2018, but they own a proportionate interest in the securities held in the respective pools.

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.

4. REVENUE BOND FUND ACCOUNTS

Components of the Revenue Bond Fund accounts by cash and cash equivalents, and investments at June 30, 2018 are summarized below:

	Cash and Cash Equivalents	Investments	Total
Operating Fund	$ 749,021	$ 11,818,958	$ 12,567,979
Revolving Fund	2,024,489	127,985,104	130,009,593
Debt Service Reserve Fund	9,049	0	9,049
Revenue Fund	900	2,521,397	2,522,297
Arbitrage Rebate Fund	2,893	432,555	435,448
Surplus Fund	666,472	152,245,428	152,911,900
Funds in state pool	924,573	3,667,854	4,592,427
	$ 4,377,397	$ 298,671,296	$ 303,048,693

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. Debt Service Reserve Fund - designated as an allowance or reserve for the payment of principal and interest on revenue bonds for which there would otherwise be a default in payment.

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

E. Arbitrage Rebate Fund – designated for reserves to rebate the United States Treasury for interest earned in excess of the maximum yield rate set for each bond issue.

F. Surplus Fund - designated reserve for advances to municipalities in anticipation of new bond issues, transfers to other funds to cover deficiencies, and other lawful purposes of the Authority.

5. INTERGOVERNMENTAL RECEIVABLES

Intergovernmental receivables consist of the following reimbursements for expenditures incurred prior to June 30, 2018:

State Property and Building Commission bond issue - funding of the state match for the KIA Fund F Federally Assisted Wastewater Program (*)	$ 288,384
State Property and Building Commission bond issue - funding of water and sewer projects under various House Bills	175,230
Total receivable from the Commonwealth	$ 463,614

* The State Treasury periodically authorizes disbursement of funds by the Authority representing the state match for awarded EPA capitalization grants. The disbursements are recorded as a current liability, "State Treasury Advances for Capitalization Grant Matching Funds", until the State Property and Building Commission issues bonds as the final funding source for the state match. Income as well as a receivable from the State Property and Building Commission are recorded by the Authority at the time of the original disbursement.

6. 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 meet the principal and interest requirements of the Authority's revenue bonds or fund additional projects. Assistance Agreements Receivable balances, net of allowance for loan losses, at June 30, 2018 were as follows:

Fund A - Clean Water State Revolving Fund Loan Program	$ 784,878,156
Fund B - Infrastructure Revolving Loan Program	63,312,509
Fund C - Governmental Agencies Program	32,746,525
Fund F - Drinking Water State Revolving Fund Loan Program	225,934,009
Sub total	1,106,871,199
Allowance for loan loss	(2,000,000)
Net assistance agreement receivable	1,104,871,199
Current maturities	(63,218,000)
Unamortized discounts	(256,720)
Long-term receivables	$ 1,041,396,479

During the year ended June 30, 2017, the Authority recorded a provision for loan losses of $2,000,000. No additional provision was recorded during the year ended June 30, 2018 and no loan balances were charged against the allowance for loan loss. The Authority continues to work with borrowers and other interested parties toward a resolution. If a resolution is not reached, the Authority will pursue remedies of default which include the declaration of all balances being due and payable, appointment of a receiver, and all remedies as permitted by KRS 224A.070.

In addition to the net assistance agreements receivable, the Authority has commitments remaining to disburse funds as summarized below:

Fund A - Clean Water State Revolving Fund Loan Program	$ 174,324,000
Fund B - Infrastructure Revolving Loan Program	12,739,000
Fund C - Governmental Agencies Program	11,309,000
Fund F - Drinking Water State Revolving Fund Loan Program	66,001,000
Total commitments outstanding	$ 264,373,000

7. LONG-TERM DEBT, REVENUE BONDS PAYABLE

Long-term debt consists of the following at June 30, 2018:

Description	Balance	Current	Long-term
Series 2004A Revenue and Revenue Refunding Bonds, interest 4.25% to 4.625%, due semi-annually, principal due annually to August 1, 2022 (Fund C)	$ 3,015,000	$ 1,390,000	$ 1,625,000
Series 2010A Revenue and Revenue Refunding Bonds, interest 3.00% to 5.00%, due semi-annually, principal due annually to February 1, 2020 (Funds A and F)	22,980,000	11,560,000	11,420,000
Series 2012A Revenue and Revenue Refunding Bonds, interest 3.00% to 5.00%, due semi-annually, principal due annually to February 1, 2032 (Funds A and F)	28,770,000	6,355,000	22,415,000
Series 2015 Revenue Bonds, interest 2.25% to 4.00%, due semi-annually, principal due annually to August 1, 2021 (Fund C)	3,090,000	410,000	2,680,000
Series 2015A Revenue and Refunding Bonds, interest 4.00% to 5.00%, due semi-annually, principal due annually to February 1, 2026 (Funds A and F)	63,510,000	0	63,510,000
Series 2016A Revenue and Refunding Bonds, interest 2.00% to 5.00%, due semi-annually, principal due annually to February 1, 2028 (Funds A and F)	49,070,000	0	49,070,000
Series 2018A Revenue and Revenue Bonds, interest 3.00% to 5.00%, due semi-annually, principal due annually to February 1, 2031 (Funds A and F)	60,000,000	0	60,000,000
Bond principal payable	230,435,000	19,715,000	210,720,000
Unamortized bond premiums	36,977,203	3,730,921	33,246,282
Total	$267,412,203	$ 23,445,921	$ 243,966,282

The required annual payments for all debt for each of the years ended June 30 are as follows:

	Principal	Interest	Total
2019	$ 19,715,000	$ 10,330,190	$ 30,045,190
2020	19,485,000	9,930,475	29,415,475
2021	19,405,000	9,138,613	28,543,613
2022	18,725,000	8,255,200	26,980,200
2023	20,430,000	7,426,388	27,856,388
2024 - 2028	91,810,000	23,261,838	115,071,838
2029 - 2032	40,865,000	3,909,400	44,774,400
	$ 230,435,000	$ 72,252,104	$ 302,687,104

The following summarizes long-term debt activity of the Authority for the year ended June 30, 2018:

	Balance June 30, 2017	Increases	Decreases	Balance June 30, 2018
Bond principal payable	$ 228,985,000	$ 60,000,000	$ 58,550,000	$ 230,435,000
Unamortized bond premiums	34,691,426	10,993,064	8,707,287	36,977,203
Total	$ 263,676,426	$ 70,993,064	$ 67,257,287	$ 267,412,203

In March 2018, the Authority utilized existing funds to advance refund $10,645,000 and $27,845,000 of outstanding Series 2010A and 2012A bonds, respectively. To accomplish the refunding, the Authority purchased, at par, certain direct obligations of the United States of America which bear interest and mature in such a manner as to pay the debt service of the defeased bonds. These direct obligations of the United States of America were deposited with the Trustee in a refunding escrow account and pledged to pay debt service and interest when due, through the February 1, 2020 and February 1, 2022 redemption dates on the 2010A and 2012A bonds to be refunded, respectively. Upon deposit of the escrow securities, the bonds to be refunded were considered defeased and the Authority removed the liabilities from its accounts. The cash flow required to service the refunded 2010A and 2012A bonds is $44,828,826. A gain of $2,254,088 was recorded on the transaction.

As of June 30, 2018, $155,085,000 of defeased bonds were outstanding of which $104,090,000 will be redeemed in February 2020 and $50,995,000 will be redeemed in February 2022.

In April 2018, the Authority issued $60,000,000 in Series 2018A Revenue Bonds with a premium of $10,993,064. The proceeds after payment of issue costs were used to reimburse the Authority for prior eligible disbursements to borrowers. These funds will be used to fund additional loan commitments.

8. STATE GRANT COMMITMENTS

The Authority has outstanding commitments for state grant expenditures as follows:

2020 Program Funds	$ 2,000
Funded by bond funds:	
2005 HB267	100,000
2006 HB380	283,000
2008 HB406 / 608	2,236,000
2016 HB303 Reallocated	5,081,000
Total funded by bond funds	7,700,000
2008 HB410; 2010 HB1; 2012 HB365; 2014 HB235; HB 303 (reallocated) Coal Severance	3,843,000
Total grant commitments	$ 11,545,000

The primary funding sources for the 2020 program 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.

The funding source of the coal severance projects is from Local Government Economic Development Fund (KRS 42.4592) monies from the single county fund. Administration of the projects has been designated to the Authority by the enumerated General Assembly. The total shown above represents the amount left to disburse for projects with grant assistance agreements at year end.

9. INTERGOVERNMENTAL REVENUE

Intergovernmental revenue from the Commonwealth during the fiscal year ended June 30, 2018 is as follows:

State Property and Building Commission bond issue - funding of the state match for the KIA Fund A Federally Assisted Wastewater Program	$ 3,374,800
State Property and Building Commission bond issue - funding of the state match for the KIA Fund F Federally Assisted Drinking Water Program	2,566,000
State Grant Funding Under Previous Authorizations	3,668,901
Total intergovernmental revenue from the Commonwealth	$ 9,609,701

10. STATE APPROPRIATIONS

Appropriations from the Commonwealth for administrative costs were $1,141,979.

11. RESTRICTED NET POSITION

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

Restricted by law	$ 1,136,938,655
Restricted for debt service	610,500
Total restricted net position	$ 1,137,549,155

12. INTERGOVERNMENTAL EXPENSE

Intergovernmental expense for the year ended June 30, 2018 totaled $7,544,939 for services provided by the Commonwealth Energy and Environment Cabinet’s Division of Water related to federal grant compliance for the federal funds administered under the Clean Water State Revolving Program (Fund A) and the Drinking Water State Revolving Program (Fund F).

13. RELATED PARTY TRANSACTIONS

The Authority incurred expenses for information technology support received from the Commonwealth Office of Technology (COT) in the amount of $37,405 for the year ending June 30, 2018.

14. RETIREMENT AND OTHER POST EMPLOYMENT BENEFIT PLANS

KERS Plan

Plan description and benefits provided - Under the provisions of KRS Section 61.645, the Board of Trustees of Kentucky Retirement Systems administers the Kentucky Employees Retirement System (KERS), County Employees Retirement System (CERS), and State Police Retirement System (SPRS). These are cost sharing, multiple employer defined benefit pension plans. Although the assets of the systems are invested as a whole, each system’s assets are used only for the payment of benefits to the members of that plan and the administrative costs incurred by those receiving a benefit, in accordance with the provisions of KRS Sections 16.510, 61.515, 61.702, 78.520, and 78.630. Under the provisions of KRS Section 61.701, the Board of Trustees of Kentucky Retirement Systems administers the Kentucky Retirement Systems’ Insurance Fund (Insurance Fund). The statutes provide for a single insurance fund to provide group hospital and medical benefits to retirees drawing a benefit from the three pension funds administered by Kentucky Retirement Systems: (1) KERS; (2) CERS; and (3) SPRS. The assets of the Insurance Fund are also segregated by plan.

The KERS Pension Fund and KERS Insurance Fund cover all eligible full-time employees and provide retirement, disability and death benefits, and health insurance benefits. Benefit contributions and provisions are established by statute. KERS issues a publicly available financial report that includes financial statements and required supplementary information. That report may be obtained by writing to Kentucky Retirement Systems, Perimeter Park West, 1260 Louisville Road, Frankfort, Kentucky 40601-6124 or by calling (502) 696-8800.

Non-hazardous employees can retire with full retirement benefits after 27 years of service or age 65. Non-hazardous employees who begin participation on or after September 1, 2008 must meet the rule of 87 (members age plus years of service credit must equal 87, and the member must be a minimum of 57 years of age) or the member is age 65, with a minimum of 60 months service credit. Retirement benefits are determined based upon a maximum of 2.2 percent of the employee's years of service multiplied by their Final Compensation. Final Compensation is calculated based upon the average of the five highest fiscal years (or last five fiscal years for employees who begin participation on or after September 1, 2008) of salary prior to attainment of KERS specified age (or age and service combinations).

KERS allows non-hazardous and hazardous employees to retire prior to meeting the requirements above and receive partial benefits, providing they meet certain age and service related criteria. Employees are eligible for service-related disability benefits regardless of length of service. Five years of service is required for nonservice-related disability eligibility. Disability benefits are determined in the same manner as retirement benefits but are payable immediately without an actuarial reduction. Death benefits equal the employee's final full-year salary.

KERS also provides post-retirement health care coverage as follows:

For members participating prior to July 1, 2003, years of service and respective percentages of the maximum contribution are as follows:

Years of Service	% Paid by Insurance Fund	% Paid by Member through Payroll Deduction
20 or more	100%	0%
15 - 19	75%	25%
14 - 10	50%	50%
4 - 9	25%	75%
Less than 4	0%	100%

As a result of House Bill 290 (2004 General Assembly), medical insurance benefits are calculated differently for members who began participation on or after July 1, 2003. Once members reach a minimum vesting period of ten years, non-hazardous employees whose participation began on or after July 1, 2003, earn ten dollars per month for insurance benefits at retirement for every year of earned service without regard to a maximum dollar amount. This dollar amount is subject to adjustment annually based on the retiree cost of living adjustment, which is updated annually due to changes in the Consumer Price Index.

Contributions – Benefit and contribution rates are established by state statute. Non-hazardous covered employees are required to contribute 5.00% of their salary to the plan. Non-hazardous covered employees who begin participation on or after September 1, 2008, are required to contribute 6.00% of their salary to the plan. The Authority's contribution rate for non-hazardous employees was 49.47%, 48.59% and 38.77% for the years ended June 30, 2018, 2017 and 2016, respectively.

In accordance with Senate Bill 2, signed by the Governor on April 4, 2013, plan members who began participating on, or after, January 1, 2014, are required to contribute to the Cash Balance Plan. The Cash Balance Plan is known as a hybrid plan because it has characteristics of both a defined benefit plan and a defined contribution plan. Members in the plan contribute 5% (non-hazardous) and 8% (hazardous) of their creditable compensation each month to their own account, and 1% to the Insurance Fund which is not credited to the member's account and is not refundable. The employer contribution rate is set annually by the Board of Trustees of the Kentucky Retirement Systems based on an actuarial valuation. The employer contributes a set percentage of the member's salary. Each month, when employer contributions are received, an employer pay credit is deposited to the member's account. A member's account is credited with a 4% (non-hazardous) and 7.5% (hazardous) employer pay credit. The employer pay credit represents a portion of the employer contribution.

Pension Plan

Pension Liabilities, Pension Expense, and Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions – At June 30, 2018, the Authority reported a liability of $4,644,598 for its proportionate share of the net pension liability. The net pension liability was measured as of June 30, 2017, and the total pension liability used to calculate the net pension liability was determined by an actuarial valuation as of that date. The Authority's proportion of the net pension liability was based on the Authority's actual contributions to the pension plan relative to the actual contributions of all participating organizations.

The complete actuarial valuation report including all actuarial assumptions and methods is publicly available on the website at www.kyret.ky.gov or can be obtained as described in the paragraph above.

For the year ended June 30, 2018, the Authority recognized pension expense of $236,926. At June 30, 2018, the Authority reported deferred outflows and inflows of resources related to pensions from the following sources:

	Deferred Outflows of Resources	Deferred Inflows of Resources
Difference between expected and actual experience	$ 826	$ 29,909
Net difference between projected and actual earnings on investments	58,045	35,585
Change of assumption	589,273	0
Changes in proportion and difference between employer contributions and proportionate share of contributions	32,540	1,052,565
Contributions subsequent to the measurement date of June 30, 2017	239,317	0
Total	$ 920,001	$ 1,118,059

The deferred outflows of resources related to the Authority's contributions to the KERS pension plan subsequent to the measurement date will be recognized as a reduction of the net pension liability in the year ending June 30, 2019. The deferred outflows of resources related to the net difference between projected and actual earnings on pension plan investments are amortized and recognized in pension expense over five years. All other amounts reported as deferred outflows of resources related to pensions are amortized and recognized in pension expense over the average expected remaining service life of the entire plan membership, which is 3.41 years for non-hazardous employees. The net increase (decrease) by fiscal year in pension expense related to the amortization of these deferred outflows of resources is as follows:

2019	$ (205,947)
2020	(231,334)
2021	6,300
2022	(6,394)
Total	$ (437,375)

Actuarial assumptions – For financial reporting the actuarial valuation as of June 30, 2017, was performed by Gabriel Roeder Smith (GRS). The total pension liability, net pension liability, and sensitivity information as of June 30, 2017, were based on an actuarial valuation date of June 30, 2016. The total pension liability was rolled-forward from the valuation date (June 30, 2016) to the plan's fiscal year ending June 30, 2017, using generally accepted actuarial principles. GRS did not perform the actuarial valuation as of June 30, 2016, but did replicate the prior actuary's valuations results on the same assumption, methods, and data, as of that date. The roll-forward is based on the results of GRS' replication. Subsequent to the actuarial valuation date (June 30, 2016), but prior to the measurement date, and before the required 2019 experience study, the Kentucky Retirement Systems Board of Trustees reviewed investment trends, inflation, and payroll growth historical trends. Based on this review the Board of Trustees adopted the following updated actuarial assumptions which were used in performing the actuarial valuation as of June 30, 2017:

Inflation	2.30 percent (3.25 percent in previous measurement date)
Salary increases	4.0 percent, average, including inflation
Investment rate of return	6.25 percent (7.50 percent in previous measurement date), net of pension plan investment expense, including inflation

The mortality table used for active members is RP-2000 Combined Mortality Table projected with Scale BB to 2013 (multiplied by 50% for males and 30% for females). For healthy retired members and beneficiaries, the mortality table used is the RP-2000 Combined Mortality Table projected with Scale BB to 2013 (set-back for one year for females). For disabled members, the RP-2000 Combined Disabled Mortality Table projected with Scale BB to 2013 (set back four years for males) is used for the period after disability retirement.

The long-term expected rate of return on pension plan investments was determined using a building-block method in which best-estimate ranges of expected future real rates of return (expected returns, net of pension plan investment expense and inflation) are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and by adding expected inflation. The target allocation and best estimates of arithmetic real rates of return for each major asset class are summarized in the following table:

Asset Class	Target Allocation	Long-Term Nominal Rate of Return
US Equity	17.50%	5.75%
International Equity	17.50%	7.38%
Global Bonds	10.00%	2.63%
Global Credit	17.00%	3.63%
Real Estate	5.00%	6.63%
Absolute Return	10.00%	5.63%
Real Return	10.00%	5.13%
Private Equity	10.00%	8.25%
Cash	3.00%	1.88%
	100.00%	5.46%

Discount rate – The discount rate used to measure the total pension liability was 5.25 percent. The projection of cash flows used to determine the discount rate assumed that contributions from plan members and employers will be made at statutory contribution rates. Based on those assumptions, the pension plan's fiduciary net position was projected to be available to make all projected future benefit payment of current active and inactive employees. Therefore, the long-term expected rate of return on pension plan investments was applied to all periods of projected benefit payments to determine the total pension liability.

Sensitivity of the Authority's proportionate share of the net pension liability to changes in the discount rate – The following presents the Authority's proportionate share of the net pension liability calculated using the discount rate of 5.25 percent, as well as what the Authority's proportionate share of the net pension liability would be if it were calculated using a discount rate that is 1 percentage point lower (4.25 percent) or 1 percentage point higher (6.25 percent) than the current rate:

	Discount Rate Less 1.00%	Discount Rate (5.25%)	Discount Rate Plus 1.00% (6.25%)
Authority's proportionate share	$ 5,303,021	$ 4,644,598	$ 4,097,060

<u>OPEB Plan</u>

OPEB Liabilities, OPEB Expense, and Deferred Outflows of Resources and Deferred Inflows of Resources Related to OPEB - At June 30, 2018, the Authority reported a liability of $879,752 for its proportionate share of the net OPEB liability. The net OPEB liability was measured as of June 30, 2017, and the total OPEB liability used to calculate the net OPEB liability was determined by an actuarial valuation as of that date. The Authority's proportion of the net OPEB liability was based on the Authority's actual contributions to the OPEB plan relative to the actual contributions of all participating organizations.

The complete actuarial valuation report including all actuarial assumptions and methods is publicly available on the website at www.kyret.ky.gov or can be obtained as described in the paragraph above.

For the year ended June 30, 2018, the Authority recognized OPEB expense of $87,272. At June 30, 2018, the Authority reported deferred outflows of resources and deferred inflows of resources related to OPEB from the following sources:

	Deferred Outflows of Resources	Deferred Inflows of Resources
Difference between expected and actual experience	$ -	$ 1,089
Net difference between projected and actual earnings on investments	0	11,387
Change of assumption	115,186	0
Changes in proportion and difference between employer contributions and proportionate share of contributions	0	6,456
Contributions subsequent to the measurement date of June 30, 2017	55,868	0
Total	$ 171,054	$ 18,932

The deferred outflows of resources related to the Authority's contributions to the OPEB plan subsequent to the measurement date will be recognized as a reduction of the net OPEB liability in the year ending June 30, 2019. The deferred inflows of resources related to the net difference between projected and actual earnings on OPEB plan investments are amortized and recognized in OPEB expense over five years. All other amounts reported as deferred outflows of resources and deferred inflows of resources are amortized and recognized in OPEB expense over the average of the expected remaining service lives of all employees that are provided OPEB through the OPEB plan which is determined to be approximately 6.25 years for non-hazardous employees. The net increase (decrease) in OPEB expense for future fiscal years related to the amortization of deferred inflows and outflows of resources is as follows:

2019	$ 23,997
2020	23,997
2021	23,997
2022	23,997
2023	266
Total	$ 96,254

Actuarial assumptions - for financial reporting the actuarial valuation as of June 30, 2017, was performed by GRS. The total OPEB liability, net OPEB liability, and sensitivity information as of June 30, 2017, were based on an actuarial valuation date of June 30, 2016. The total OPEB liability was rolled-forward from the valuation date (June 30, 2016) to the plan's fiscal year ending June 30, 2017, using generally accepted actuarial principles. GRS did not perform the actuarial valuation as of June 30, 2016, but did replicate the prior actuary's valuations results on the same assumption, methods, and data, as of that date. The roll-forward is based on the results of GRS' replication. Subsequent to the actuarial valuation date (June 30, 2016), but prior to the measurement date, and before the required 2019 experience study, the Kentucky Retirement Systems Board of Trustees reviewed investment trends, inflation, and payroll growth historical trends. Based on this review the Board of Trustees adopted the following updated actuarial assumptions which were used in performing the actuarial valuation as of June 30, 2017:

Inflation	2.30%
Payroll growth rate	0.0% for KERS non-hazardous and hazardous
Salary increase	3.05%, average
Investment rate of return	6.25%
Healthcare trend rates:	
Pre – 65	Initial trend starting at 7.25% at January 1, 2019, and gradually decreasing to an ultimate trend rate of 4.05% over a period of 13 years.
Post-65	Initial trend starting at 5.10% at January 1, 2019, and gradually decreasing to an ultimate trend rate of 4.05% over a period of 11 years.

The mortality table used for active members is RP-2000 Combined Mortality Table projected with Scale BB to 2013 (multiplied by 50% for males and 30% for females). For healthy retired members and beneficiaries, the mortality table used is the RP-2000 Combined Mortality Table projected with Scale BB to 2013 (set-back for one year for females). For disabled members, the RP-2000 Combined Disabled Mortality Table projected with Scale BB to 2013 (set back four years for males) is used for the period after disability retirement.

Discount Rate - The projection of cash flows used to determine the discount rate of 5.83% for non-hazardous and 5.96% for hazardous assumed that local employers would contribute the actuarially determined contribution rate of projected compensation over the remaining 26 years (closed) amortization period of the unfunded actuarial accrued liability. The discount rate determination used an expected rate of return of 6.25%, and a municipal bond rate of 3.56%, as reported in Fidelity Index's "20 –Year Municipal GO AA Index" as of June 30, 2017. However, the cost associated with the implicit employer subsidy was not included in the calculation of the Kentucky Retirement System's actuarial determined contributions, and any cost associated with the implicit subsidy will not be paid out of the Kentucky Retirement System's trusts. Therefore, the municipal bond rate was applied to future expected benefit payments associated with the implicit subsidy. The target asset allocation and best estimates of arithmetic nominal rates of return for each major asset class are summarized in the pension section above.

Sensitivity of the Authority's proportionate share of the net OPEB liability to changes in the discount rate - The following presents the Authority's proportionate share of the net OPEB liability, as well as what the Authority's proportionate share of the net OPEB liability would be if it were calculated using a discount rate that is 1 percentage point lower or 1 percentage point higher than the current discount rate:

	Discount Rate Less 1.00%	Discount Rate (5.83%)	Discount Rate Plus 1.00% (6.83%)
Authority's proportionate share	$ 1,028,535	$ 879,752	$ 756,102

Sensitivity of the Authority's proportionate share of the net OPEB liability to changes in the healthcare cost trend rates - The following presents the Authority's proportionate share of the net OPEB liability, as well as what the Authority's proportionate share of the net OPEB liability would be if it were calculated using healthcare cost trend rates that are 1 percentage point lower or 1 percentage point higher than the current healthcare cost trend rates:

	Healthcare Trend Rate Less 1.00%	Current Trend Rate	Healthcare Trend Rate Plus 1.00%
Authority's proportionate share	$ 747,503	$ 879,752	$ 1,045,811

<u>Deferred Compensation Plans</u>

The Authority's employees may elect to participate in two deferred compensation plans offered by the Kentucky Public Employees Deferred Compensation Authority under sections 401(k) and 457 of the Internal Revenue Code. Under the plans, employees may defer up to 100% of their compensation after deducting required contributions to the KERS plan. The Authority does not make matching contributions to these plans.

15. RISK MANAGEMENT

The Authority is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; and errors and omissions. The Authority utilizes the Commonwealth of Kentucky's Risk Management Fund to cover the exposure to these potential losses. The Commonwealth of Kentucky's Comprehensive Annual Financial Report should be referred to for additional disclosures related to the Risk Management Fund.

16. FAIR VALUE MEASUREMENTS

The framework for measuring fair value provides a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3). The three levels of the fair value hierarchy are described as follows:

- Level 1: Inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets that the Authority has the ability to access.
- Level 2: Inputs to the valuation methodology include quoted prices for similar assets or liabilities in active markets; inputs other than quoted prices that are observable for the asset or liability; inputs that are derived principally from or corroborated by observable market data by correlation or other means. If an asset or liability has a specified (contractual) term, the level 2 inputs must be observable for substantially the full term of the asset or liability.
- Level 3: Inputs to the valuation methodology are unobservable and significant to the fair value measurements.

The asset or liability's fair value measurement level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. Valuation techniques maximize the use of relevant observable inputs and minimize the use of unobservable inputs.

Following is a description of the valuation methodologies used for assets and liabilities measured at fair value. There have been no changes in the methodologies used at June 30, 2018.

- *U.S. Treasury and U.S Agency Securities*: Valued using quoted prices in active markets for similar securities and interest rates.

The following table sets forth by level within hierarchy, the Authority's investment at fair value for June 30, 2018:

	Assets at Fair Value as of June 30, 2018			
	Level 1	*Level 2*	*Level 3*	*Total*
Investment in State Pool	$ 46,357	$ 3,621,497	$ -	$ 3,667,854
Federal Home Loan Bank Discount Notes	0	135,484,495	0	135,484,495
Federal Home Loan Mortgage Corporation Discount Notes	0	11,608,379	0	11,608,379
U.S Treasury Bill	0	82,220,743	0	82,220,743
U.S Treasury Notes	0	65,689,825	0	65,689,825
	$ 46,357	$ 298,624,939	$ -	$ 298,671,296

The Authority's policy is to recognize transfers between levels as of the actual date of the event or change in circumstances. There were no transfers between levels during the year ended June 30, 2018.

17. RECENT GASB PRONOUNCEMENTS

Management has not currently determined what, if any, effects of implementation of the following statements may have on the financial statements:

GASB Statement No. 87, *Leases,* will be effective for periods beginning after December 15, 2019. This Statement increases the usefulness of governments' financial statements by requiring recognition of certain lease assets and liabilities for leases that previously were classified as operating leases and recognized as inflows of resources or outflows of resources based on the payment provisions of the contract. It establishes a single model for lease accounting based on the foundational principle that leases are financings of the right to use an underlying asset. Under this Statement, a lessee is required to recognize a lease liability and an intangible right-to-use lease asset, and a lessor is required to recognize a lease receivable and a deferred inflow of resources.

REQUIRED SUPPLEMENTARY INFORMATION

KENTUCKY INFRASTRUCTURE AUTHORITY

SCHEDULE OF PROPORTIONATE SHARE OF NET PENSION LIABILITY
JUNE 30, 2018

	2018	2017	2016	2015
Proportion of the net pension liability	0.0347%	0.0484%	0.0516%	0.0497%
Proportionate share of the net pension liability	$ 4,644,598	$ 5,511,653	$ 5,178,848	$ 4,214,000
Covered payroll *	$ 536,379	$ 781,651	$ 828,620	$ 772,709
Proportionate share of the net pension liability as a percentage of its covered payroll	865.92%	705.13%	625.00%	545.35%
Pension plan fiduciary net position as a percentage of the total pension liability	13.30%	14.80%	18.83%	22.32%

* The amounts presented for each fiscal year were determined as of the measurement date of the net pension liability, which is as of the Authority's prior fiscal year end.

This schedule is intended to present 10 years of the proportionate share of the net pension liability. Additional years will be displayed as they become available.

KENTUCKY INFRASTRUCTURE AUTHORITY

SCHEDULE OF PENSION CONTRIBUTIONS
JUNE 30, 2018

	2018	2017	2016	2015
Statutorily required contribution	$ 266,046	$ 215,839	$ 241,061	$ 255,559
Contribution in relation to the statutorily required	266,046	215,839	241,061	255,559
Contribution deficiency (excess)	$ -	$ -	$ -	$ -
Covered payroll	$ 647,943	$ 536,379	$ 781,651	$ 828,620
Contribution as a percentage of covered payroll	41.06%	40.24%	30.84%	30.84%

This schedule is intended to present 10 years of the contributions and related ratios. Additional years will be displayed as they become available.

KENTUCKY INFRASTRUCTURE AUTHORITY

SCHEDULE OF PROPORTIONATE SHARE OF NET OPEB LIABILITY
JUNE 30, 2018

	2018
Proportion of the net OPEB liability	0.0347%
Proportionate share of the net OPEB liability	$ 879,752
Covered payroll *	$ 536,379
Proportionate share of the net OPEB liability as a percentage of its covered payroll	164.02%
Plan fiduciary net position as a percentage of the total OPEB liability	24.37%

* The amounts presented for each fiscal year were determined as of the measurement date of the net OPEB liability, which is as of the Authority's prior fiscal year end.

This schedule is intended to present 10 years of the contributions and related ratios. Additional years will be displayed as they become available.

KENTUCKY INFRASTRUCTURE AUTHORITY

SCHEDULE OF OPEB CONTRIBUTIONS
JUNE 30, 2018

	2018
Statutorily required contribution	$ 54,492
Contribution in relation to the statutorily required	54,492
Contribution deficiency (excess)	$ -
Covered payroll	$ 647,943
Contribution as a percentage of covered payroll	8.41%

This schedule is intended to present 10 years of the contributions and related ratios. Additional years will be displayed as they become available.

SUPPLEMENTARY INFORMATION

KENTUCKY INFRASTRUCTURE AUTHORITY

SUPPLEMENTARY SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED JUNE 30, 2018

Grant Name	Federal CFDA No.	Grant Number	Grant Period	Expenditures	Passed through to other agencies (including revenue redistribution)
U.S. Environmental Protection Agency					
Major Program:					
Capitalization Grants for Clean Water State Revolving Fund	66.458	CS210001-16	7/2016 - 9/2019	$ 2,835,888	$ 241,219
Capitalization Grants for Clean Water State Revolving Fund	66.458	CS210001-17	7/2017 - 9/2020	16,168,247	473,423
Total Capitalization Grants for Clean Water State Revolving Fund				19,004,135	714,642
Non-Major Program:					
Capitalization Grants for Drinking Water State Revolving Fund	66.468	FS984547-15	7/2015 - 9/2018	1,778,118	1,778,118
Capitalization Grants for Drinking Water State Revolving Fund	66.468	FS984547-16	7/2016 - 9/2018	3,460,555	3,460,555
Capitalization Grants for Drinking Water State Revolving Fund	66.468	FS984547-17	7/2017 - 9/2019	5,427,126	1,591,624
Total Capitalization Grants for Clean Water State Revolving Fund				10,665,799	6,830,297
Total all programs				$ 29,669,934	$ 7,544,939

See report of independent auditors and accompanying notes to the schedule.

NOTES TO THE SUPPLEMENTARY SCHEDULE OF
EXPENDITURES OF FEDERAL AWARDS
YEAR ENDED JUNE 30, 2018

1. BASIS OF ACCOUNTING

The accompanying supplementary schedule of expenditures of federal awards includes the federal grant activity of the Authority and is presented on the cash basis of accounting. The information in this schedule is presented in accordance with the requirements of Title 2 U.S. *Code of Federal Regulations* Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards*. Therefore, some amounts in this schedule may differ from amounts presented in, or used in the preparation of, the basic financial statements.

The award revenues received and expended are subject to audit and adjustment. If any expenditures are disallowed by the grantor as a result of such an audit, any claim for reimbursement to the grantor would become a liability of the Authority. In the opinion of management, all grant expenditures are in compliance with the terms of the grant agreements and applicable federal laws and regulations. The authority did not elect to use the 10% de minimis indirect cost rate.

2. PASSED THROUGH TO OTHER AGENCY

CFDA No.	Name of Grant	Amount	Pass Through Entity
66.458	Clean Water State Revolving Fund	$ 714,642	Energy and Environment Cabinet
66.468	Drinking Water State Revolving Fund	6,830,297	Energy and Environment Cabinet
	Total	$ 7,544,939	

3. LOANS OUTSTANDING

CFDA No.	Name of Grant	Amount
66.458	Clean Water State Revolving Fund	$ 784,878,156
66.468	Drinking Water State Revolving Fund	225,934,009
	Total	$ 1,010,812,165

4. LOAN PRINCIPAL FORGIVENESS

CFDA No.	Name of Grant		Amount
66.458	Clean Water State Revolving Fund	$	2,204,239
66.468	Drinking Water State Revolving Fund		2,450,104
	Total	$	4,654,343

5. SUB-RECIPIENTS

The accompanying supplementary schedule of expenditures of federal awards includes expenditures consisting of federal awards provided to sub-recipients as follows:

CFDA No.	Name of Grant		Amount
66.458	Clean Water State Revolving Fund	$	18,289,493
66.468	Drinking Water State Revolving Fund		6,830,296
	Total	$	25,119,789

KENTUCKY INFRASTRUCTURE AUTHORITY

COMBINING STATEMENT OF NET POSITION

JUNE 30, 2018

	Fund A	Fund B	Fund C	Fund F	Total
ASSETS					
Current assets:					
Cash and cash equivalents	$ 2,187,007	$ 1,508,820	$ 52,873	$ 628,697	$ 4,377,397
Investments, current portion	183,219,447	18,669,211	13,536,382	82,203,201	297,628,241
Intergovernmental receivables	288,384	175,230	0	0	463,614
Accrued interest receivable, investments	129,619	14,268	16,111	105,747	265,745
Accrued interest receivable, assistance agreements	973,157	89,950	101,212	269,630	1,433,949
Current maturities of long-term receivables	43,828,000	4,245,000	2,934,000	12,211,000	63,218,000
Total current assets	230,625,614	24,702,479	16,640,578	95,418,275	367,386,946
Investments	0	0	432,555	0	432,555
Investments, restricted for debt service	0	0	610,500	0	610,500
Total noncurrent investments	0	0	1,043,055	0	1,043,055
Long-term receivables:					
Assistance agreements receivable:					
Principal	741,050,156	59,067,509	29,812,525	213,723,009	1,043,653,199
Allowance for losses on assistance agreements	0	(2,000,000)	0	0	(2,000,000)
Unamortized discounts	0	0	(256,720)	0	(256,720)
Total long-term receivables	741,050,156	57,067,509	29,555,805	213,723,009	1,041,396,479
Capital assets, net	0	8,530	0	0	8,530
Total assets	971,675,770	81,778,518	47,239,438	309,141,284	1,409,835,010
Deferred outflows of resources:					
Pension related	433,233	36,357	55,308	395,103	920,001
Post-employment benefits other than pension	81,251	7,184	9,579	73,040	171,054
Unamortized deferred amount on refunding	4,937,639	0	0	1,026,274	5,963,913
Total deferred outflows of resources	$ 5,452,123	$ 43,541	$ 64,887	$ 1,494,417	$ 7,054,968
LIABILITIES					
Current liabilities:					
Current maturities of revenue bonds payable, net of unamortized premiums and discounts	$ 17,968,145	$ -	$ 1,847,838	$ 3,629,938	$ 23,445,921
Accrued interest payable	3,070,016	0	96,250	818,433	3,984,699
State treasury advances for capitalization grant matching funds	288,384	0	0	0	288,384
Grants payable	0	391,927	0	0	391,927
Other payables	2,075	0	0	0	2,075
Total current liabilities	21,328,620	391,927	1,944,088	4,448,371	28,113,006
Long-term liabilities:					
Revenue bonds payable, less current maturities and unamortized premiums and discounts	182,146,224	0	4,408,650	57,411,408	243,966,282
Net pension liability	2,199,922	194,792	264,458	1,985,426	4,644,598
Net post-employment benefits other than pension liability	417,882	36,950	49,266	375,654	879,752
Other payables	0	0	468,326	0	468,326
Total liabilities	206,092,648	623,669	7,134,788	64,220,859	278,071,964
Deferred inflows of resources:					
Pension related	529,858	46,848	63,063	478,290	1,118,059
Post-employment benefits other than pension	8,993	795	1,060	8,084	18,932
Unamortized deferred amount on refunding	0	0	131,868	0	131,868
Total deferred inflows of resources	$ 538,851	$ 47,643	$ 195,991	$ 486,374	$ 1,268,859
NET POSITION					
Net investment in capital assets	$ -	$ 8,530	$ -	$ -	$ 8,530
Restricted net position	770,496,394	81,142,217	39,973,546	245,928,468	1,137,540,625
Total net position	$ 770,496,394	$ 81,150,747	$ 39,973,546	$ 245,928,468	$ 1,137,549,155

See report of independent auditors.

KENTUCKY INFRASTRUCTURE AUTHORITY

COMBINING STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET POSITION
FOR THE YEAR ENDED JUNE 30, 2018

	Fund A	Fund B	Fund C	Fund F	Total
Operating revenues:					
Assistance agreements:					
Servicing fee	$ 1,484,684	$ 120,043	$ 55,016	$ 565,832	$ 2,225,575
Interest income	11,679,626	898,236	890,308	3,547,836	17,016,006
Total operating revenues	13,164,310	1,018,279	945,324	4,113,668	19,241,581
Operating expenses:					
General and administrative	717,393	1,086,273	40,313	555,713	2,399,692
Intergovernmental administrative expense reimbursement	714,642	0	0	6,830,297	7,544,939
State grant expenditures	0	5,727,841	0	0	5,727,841
Revenue bonds:					
Amortization of bond premiums	(2,794,607)	0	(108,243)	(592,090)	(3,494,940)
Interest	8,717,930	0	207,111	1,938,007	10,863,048
Arbitrage expense	0	0	33,477	0	33,477
Gain on early extinguishment of bonds payable	(1,992,410)	0	0	(261,678)	(2,254,088)
Bond issuance cost	272,747	0	0	192,609	465,356
Total operating expenses	5,635,695	6,814,114	172,658	8,662,858	21,285,325
Operating loss	7,528,615	(5,795,835)	772,666	(4,549,190)	(2,043,744)
Non-operating gain / (loss):					
Investment income	2,296,628	197,022	275,612	752,210	3,521,472
Federal grants	19,004,135	0	0	10,665,799	29,669,934
Loan subsidy required by federal capitalization grants	(2,204,239)	(7,793)	0	(2,450,104)	(4,662,136)
Intergovernmental revenue from the Commonwealth	3,374,800	3,668,901	0	2,566,000	9,609,701
State appropriations	0	1,141,979	0	0	1,141,979
Total non-operating revenues	22,471,324	5,000,109	275,612	11,533,905	39,280,950
Change in net position	$ 29,999,939	$ (795,726)	$ 1,048,278	$ 6,984,715	$ 37,237,206
Net position, beginning of year (as previously stated)	740,827,159	81,975,716	38,964,256	239,241,046	1,101,008,177
Cumulative effect on prior years (to June 30, 2017) resulting from the retroactive change in accounting for postemployment benefits other than pensions (See Note 2)	(330,708)	(29,242)	(38,989)	(297,289)	(696,228)
Net position, beginning of year (as adjusted)	740,496,451	81,946,474	38,925,267	238,943,757	1,100,311,949
Net position, end of year	$ 770,496,390	$ 81,150,748	$ 39,973,545	$ 245,928,472	$ 1,137,549,155

See report of independent auditors.

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Report of Independent Auditors on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards*

Board of Directors
Kentucky Infrastructure Authority
Frankfort, Kentucky

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, the 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, 2018, and the related notes to the financial statements, which collectively comprise the Authority's basic financial statements, and have issued our report thereon dated November 19, 2018.

Internal Control over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Authority's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Authority's internal control. Accordingly, we do not express an opinion on the effectiveness of the Authority's internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that have not been identified. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. We did identify a deficiency in internal control, described in the accompanying Schedule of Findings and Questioned Costs as item 2018-001, that we consider to be a significant deficiency.

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Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Authority's financial statements are free from 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*.

The Authority's Response to Findings

The Authority's response to the finding identified in our audit is described in the accompanying Schedule of Findings and Questioned Costs. The Authority's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

Purpose of this Report

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

Dean Dorton Allen Ford, PLLC

November 19, 2018
Louisville, Kentucky

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Report of Independent Auditors on Compliance for Each Major Federal Program; Report on Internal Control Over Compliance Required by the Uniform Guidance

Board of Directors
Kentucky Infrastructure Authority
Frankfort, Kentucky

Report on Compliance for Each Major Federal Program

We have audited the Kentucky Infrastructure Authority's (the Authority), a component unit of the Commonwealth of Kentucky, compliance with the types of compliance requirements described in the *OMB Compliance Supplement* that could have a direct and material effect on each of the Authority's major federal programs for the year ended June 30, 2018. The Authority's major federal programs are identified in the summary of auditors' results section of the accompanying Schedule of Findings and Questioned Costs.

Management's Responsibility

Management is responsible for compliance with federal statutes, regulations, and the terms and conditions of its federal awards applicable to its federal programs.

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for each of the Authority's major federal programs based on our audit of the types of compliance requirements referred to above. 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 the audit requirements of Title 2 U.S. *Code of Federal Regulations* Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance). Those standards and the Uniform Guidance 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 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 on compliance for each major federal program. However, our audit does not provide a legal determination of the Authority's compliance.

Opinion on Each Major Federal Program

In our opinion, the Authority complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended June 30, 2018.

Report on Internal Control Over Compliance

Management of the Authority is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered the Authority's internal control over compliance with the types of requirements that could have a direct and material effect on each major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major federal program and to test and report on internal control over compliance in accordance with the Uniform Guidance, 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.

A *deficiency in internal control over compliance* exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. A *material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. A *significant deficiency in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of the Uniform Guidance. Accordingly, this report is not suitable for any other purpose.

Dean Dorton Allen Ford, PLLC

November 19, 2018
Louisville, Kentucky

KENTUCKY INFRASTRUCTURE AUTHORITY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
YEAR ENDED JUNE 30, 2018

Section I. SUMMARY OF AUDITOR'S RESULTS

Financial Statements

Type of report the auditor issued on whether the financial statements audited were prepared in accordance with GAAP: *Unmodified*

Internal control over financial reporting:

Material weakness(es) identified?		Yes	X	No
Significant deficiency(ies) identified?	X	Yes		None Reported
Noncompliance material to financial statements noted?		Yes	X	No

Federal Awards

Internal control over major programs:

Material weakness(es) identified?		Yes	X	No
Significant deficiency(ies) identified?		Yes	X	None Reported

Type of auditor's report issued on compliance for major federal programs: *Unmodified*

Any audit findings disclosed that are required to be reported in accordance with section 2 CFR 200.516(a)?		Yes	X	No

Identification of major programs:

CFDA Number(s)	Name of Federal Program or Cluster [D]
66.458	Capitalization Grants for Clean Water State Revolving Funds

Dollar threshold used to distinguish between type A and type B programs		$ 890,098		
Auditee qualified as low-risk auditee?	X	Yes		No

Section II. FINANCIAL STATEMENT FINDINGS

<u>Finding 2018-001: Lack of Segregation of Duties</u>

Criteria

A governmental agency's internal controls should be in compliance with guidance in ''Standards for Internal Control in the Federal Government'' (the Green Book) issued by the Comptroller General of the United States and the ''Internal Control Integrated Framework'', issued by the Committee of Sponsoring Organizations of the Treadway Commission (the COSO framework).

The Uniform Guidance, in 2 CFR 200 section 200.303, states that a non-Federal entity must establish and maintain effective internal control over Federal awards that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should be in compliance with guidance in the Green Book and the COSO framework.

Both the Green Book and the COSO framework identify proper segregation of duties as an essential element of an entity's internal control environment, as it forms the basic building block of sustainable risk management and internal controls. The Green Book states "Management divides or segregates key duties and responsibilities among different people to reduce the risk of error, misuse, or fraud. This includes separating the responsibilities for authorizing transactions, processing and recording them, reviewing the transactions, and handling any related assets so that no one individual controls all key aspects of a transaction or event."

Condition

During our audit we noted that there is limited segregation of duties in the accounting department. The Fiscal Officer has the ability to both post and approve journal entries. The Fiscal Officer is also responsible for reconciliation of account balances. There is little to no supervision or approval of entries or reconciliations performed by the Fiscal Officer.

Cause

The segregation of duties weakness results from the small accounting department.

Effect or Potential Effect

The lack of segregation of duties with regards to key processes of the accounting function exposes the Authority to greater risk of misstatement due to human error and fraud.

Recommendation

We suggest the Authority take steps to establish procedures to strengthen the segregation of duties within the accounting department. This would mitigate the risk of misstatement due to human error and fraud. Such procedures would include the following:

- A robust review of the accounting and financial reporting functions, including the supervision of various activities.
- Evaluate the need for additional resources within the accounting department, or identify areas where current staff members could be assigned duties to strengthen segregation of duties.
- Establish workflows to allow for review and approval procedures over transactions and reconciliations.

Management Response

The Authority previously recognized segregation of duties concerns and a need for cross training in the financial reporting area due to its significant complexity and staffing was adjusted accordingly. As a result of ongoing turnover of staff, existing resources have continually been realigned to accommodate immediate organization priorities until replacement staff can be hired and trained. This has extended the time needed to address both segregation of duties and cross training efforts. Workflows and organization structure are being evaluated in an effort to mitigate the noted deficiency.

Section III. FINDINGS AND QUESTIONED COSTS FOR FEDERAL AWARDS

None identified.

Section IV. PRIOR AUDIT FINDINGS

Finding 2017-001

The Authority did not submit its SF-425 - Federal Financial Report and the Federal Funding and Accountability and Transparency Act (FFATA) reporting timely during the year which is required under the Uniform Guidance.

This finding was resolved in the current year.