

**WINCHESTER MUNICIPAL UTILITIES
WINCHESTER, KENTUCKY**

AUDITED FINANCIAL STATEMENTS

YEARS ENDED JUNE 30, 2009 and 2008

**WINCHESTER MUNICIPAL UTILITIES
WINCHESTER, KENTUCKY
JUNE 30, 2009 and 2008**

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SUMMERS, MCCRARY & SPARKS, P.S.C.

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INDEPENDENT AUDITOR'S REPORT

To the Commissioners
Winchester Municipal Utilities
Winchester, KY

We have audited the accompanying financial statements of Winchester Municipal Utilities, a component unit of the City of Winchester, Kentucky, as of and for the years ended June 30, 2009 and 2008, which collectively comprise the Utilities' basic financial statements as listed in the table of contents. These financial statements are the responsibility of the Utilities' management. 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 of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and the significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As discussed in Note 1, the financial statements present only the Winchester Municipal Utilities and do not purport to, and do not, present fairly the financial position of the City of Winchester, Kentucky, as of June 30, 2009 and 2008.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of Winchester Municipal Utilities, a component unit of the City of Winchester, Kentucky, as of June 30, 2009 and 2008, and the respective changes in financial position and cash flows thereof for the years then ended in conformity with accounting principles generally accepted in the United States of America.

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In accordance with *Government Auditing Standards*, we have also issued our report dated October 30, 2009, on our consideration of Winchester Municipal Utilities', a component unit of the City of Winchester, Kentucky, internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

The management's discussion and analysis on pages 3 through 15, is not a required part of the basic financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming opinions on the Winchester Municipal Utilities', a component unit of the City of Winchester, Kentucky, basic financial statements. The Department expense and Revenue Bond Debt Schedules shown on pages 38 through 40 is presented for purposes of additional analysis and is not a required part of the basic financial statements. The accompanying schedule of expenditures of federal awards is presented for the purpose of additional analysis as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is also not a required part of the basic financial statements of Winchester Municipal Utilities, a component unit of the City of Winchester, Kentucky. The Department expense and Revenue Bond Debt Schedules, including the schedule of expenditures of federal awards, have been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, are fairly stated in all material respects in relation to the basic financial statements taken as a whole.

Summers, McCrary & Sparks, PSC

Summers, McCrary & Sparks, PSC
Winchester, Kentucky
October 30, 2009

**MANAGEMENT'S DISCUSSION AND ANALYSIS
WINCHESTER MUNICIPAL UTILITIES
JUNE 30, 2009**

UTILITY PROFILE

Winchester Municipal Utilities (WMU), an enterprise fund of the city of Winchester, Kentucky (City), was established in 1958 by ordinance of the City to provide water, sanitary sewer (wastewater) and solid waste services for the City and portions of Clark County. WMU is governed by a Board of Commissioners appointed by the Mayor with approval of the Board of Commission of the City. The Winchester Municipal Utilities Commission (WMUC) provides direction and oversight of the utility and its operations, adopts the budget, sets the operating policies, hires the General Manager and Counsel of the utility, and recommends to the City utility rates necessary to support the operations of the utility, repair and replacement of the utility's assets, and the utility's debt service.

WMU has 11,761 water customers, 11,442 wastewater customers, and 8,926 solid waste customers.

Fiscal Year 2009/2010 budget reflects annual revenue of \$11,269,000 and annual debt service of \$2,094,410.

• **Water System**

WMU has two sources of raw water – pool No. 10 of the Kentucky River and the Carroll Ecton Reservoir (Reservoir). WMU's primary source of water is Pool No. 10, a 25-mile pool of the river. WMU is the only water utility withdrawing water from this source. WMU is permitted to withdraw up to 15 million gallons per day (MGD) from pool No. 10 under normal river flow conditions, with restrictions being imposed during times of below normal river flow. The Reservoir impounds approximately 500,000,000 gallons of water on an unnamed tributary of Lower Howards Creek. There are no withdrawal restrictions on the Reservoir.

The water treatment plant is rated to produce 6.0 million gallons per day (MGD). Clearwell storage is 1,000,000 gallons; elevated storage totals 3,500,000 gallons.

There are approximately 164.3 miles of waterlines in the system.

Average day water production for FY 2008/2009 was 4.07 MGD. In addition to the provision of service to its retail customers, WMU provides water for resale to the East Clark County Water District (ECCWD) and the Kentucky American Water Company (KAWC).

• **Wastewater System**

WMU maintains approximately 150.9 miles of gravity and force main sanitary sewers, 17 sewage-pumping stations, and a new wastewater treatment plant (WWTP) rated at 7.2 MGD. The WWTP is designed to handle a biological load approximately four times greater than typical domestic sewage. In addition, WMU operates a solids processing

facility producing and distributing for beneficial reuse Class A biosolids in compliance with 40 Code of Federal Regulations (CFR) §503.

Average day wastewater treatment for FY 2008/2009 was 4.01 MGD. Average day production of Class A biosolids for FY 2008/2009 was 12.7 dry tons.

- **Solid Waste System**

WMU is responsible for the daily collection of solid waste generated within the City and transportation for ultimate disposal in a privately owned and permitted solid waste landfill. In addition, WMU collects and grinds yard waste for beneficial reuse, operates and maintains a voluntary recycling operation for newspaper, white and mixed paper, cardboard, glass, plastics, tin, and aluminum, and maintains a 20-acre, non-operating landfill that is classified as *in post-closure care*.

Average day solid waste collection and disposal for FY 2008/2009 was 58.1 tons and average day yard waste collection for FY 2008/2009 was 8.26 tons.

SIGNIFICANT ISSUES

- **Consent Decree**

The Consent Decree is the settlement agreement between the United States Environmental Agency (EPA), the Kentucky Energy and Environment Cabinet (EEC, formerly known as the Environmental and Public Protection Cabinet), the City and WMU detailing actions to be taken by the City and WMU for violations of the Clean Water Act , 33 U.S.C. § 1319. The basic tenants of the Consent Decree call for the City and WMU to:

- Eliminate existing and recurring sanitary sewer overflows (SSOs)
- Reduce the potential for future SSOs

Such is to be achieved through a defined capital program and structured operation and maintenance (O&M) program.

Deadlines for capital projects to eliminate SSO's are shown in the chart below:

Project Area		Proposed Date for Removal from Service
Forest Park Sanitary Sewer Improvements	Maryland Avenue Wabash Smith Manor	July 31, 2012
Lower Howards Creek Sanitary Sewer Improvements	Snowfall Stoneybrook	January 31, 2013
Bel-Air Sanitary Sewer Improvements	Bel-Air Westside	January 31, 2021

The Lower Howards Creek Project involves a facilities plan update, construction of sanitary sewer interceptors and construction of a new wastewater treatment plant. Both the Forest Park and Bel-Air Sanitary Sewer Improvements projects will involve construction of a interstate road bore and new interceptor sewers.

The structured O&M programs have been developed and submitted to the EPA as the Capacity, Management, Operation and Maintenance (CMOM) program. WMU developed 14 required CMOM programs seven of which must be reviewed and approved by EPA. The following programs have been completed and submitted:

- Sewer Overflow Response Plan (SORP)
- Inter Jurisdictional Agreement Program
- Public Education Program
- Spill Impact Water Quality Monitoring Program
- Corrosion Control Program
- Routine Hydraulic Cleaning Program
- Root Control Program
- Capacity Assurance Program (CAP)
- Acquisition Consideration Program
- Infrastructure Rehabilitation Program (IRP)
- Sewer System Assessment Program (CSSAP)
- Sewer System Inventory Program
- Fats, Oils, and Grease Control Program (FOG)
- Financial and Cost Analysis Program

WMU has monitored the “First Flush” of the Town Branch storm system as part of the supplemental environmental project (SEP) required by EPA. Monitoring has determined that constituents of concern are not present at levels to warrant construction of a treatment system. WMU intends to review other alternatives for compliance with the SEP.

- **Water Supply**

WMU faces a critical need with respect to water supply. Normal growth pattern projections indicate the need for additional potable water capacity in 2011 or 2012. The timeframe for that need has been accelerated with the location of Sekisui S-LEC America (Sekisui) in Winchester. Sekisui has outlined plans for its Phase II construction in the calendar year 2012 which will increase its water demand from 300,000 gallons per day to 1,300,000 gallons per day – an increase of 433%.

WMU’s current permitted capacity is 6.0 million gallons per day (MGD) with current average day demand of 4.0 MGD and peak day demand of 5.0 MGD. Projections of WMU’s 20-year demand are 12.0 MGD based upon normal growth patterns which can be skewed with the addition of any significant industrial or other large user.

Discussions in 2008 between the WMU and City Commission led to a decision to construct a new water treatment plant. Construction will be phased with the initial capacity being 6.0 MGD to operate in concert with the existing water treatment plant yielding an effective capacity of 8.0 – 9.0 MGD. The final effective capacity will be

determined by the Division of Water (DOW). In addition water transmission improvements are being planned to insure the delivery of the additional capacity. Over time, the existing water treatment plant will be phased out of service and the planned water treatment plant expanded to 12.0 MGD. The total estimated cost of the initial phase of improvements is \$55,000,000.

- **Kentucky River Lock and Dam No. 10**

Construction of the Kentucky River Lock and Dam No. 10 were completed in 1905. The lock and dam were owned and operated by the United States Army Corps of Engineers (COE) until 1996 at which time ownership and the responsibility for maintenance and replacement of the lock and dam were transferred to the Commonwealth of Kentucky. The General Assembly created by statute the Kentucky River Authority (KRA) to oversee the operation, maintenance and replacement of the 14 locks and dams on the Kentucky River. Implicit in that charge of authority is the maintenance of the 14 pools of water for water supply. The Kentucky River supplies water to approximately 22% of Kentucky's population. WMU, like all other water utilities that withdraw water from the Kentucky River, pays a withdrawal fee for each gallon of water withdrawn from the Kentucky River and the reservoir and passes that cost to its customers. The withdrawal fees are used by KRA for repair and replacement of the 14 locks and dams.

Dam No. 10 was built as a timber crib dam with a plain concrete face, i.e., the dam is a series of timber boxes, stacked and filled with large rock and covered with a concrete skin that has no reinforcement. The dam is over 100 years old and has had no substantial rehabilitation during its service life. The dam impounds pool No. 10 which creates the water supply for Winchester and most of Clark County.

Pool No. 10 is the longest pool on the Kentucky River stretching 25 miles. The East Kentucky Power (EKP) J. K. Smith Generating Plant and the Dale Generating Plant withdraw cooling water for the two power generating plants. Approximately 95% of that cooling water is returned to the river. The two EKP withdrawals and the WMU withdrawal are the only permitted withdrawals from pool No. 10. The city of Richmond Utilities has constructed a new wastewater treatment plant (WWTP) which will discharge to Otter Creek in Madison County. Otter Creek discharges to pool No. 10. The permitted WWTP discharge meets the Kentucky, five-mile separation rule between a WWTP discharge and a WTP intake.

The Kentucky River is subject to wide variations in flow from 0 flows to 1 billion gallons per day. The wide variations in flow and resulting stress on the dam and scour below the dam make dam No. 10 vulnerable to overturning. KRA has ranked replacement of dam No. 10 as its number one priority but does not show the dam on its list of priorities as the financing for the dam replacement is encumbered by a federal appropriation. The appropriation is stalled due to requirements of COE. A failed dam would leave Winchester without its primary water supply. WMU's reservoir would yield, without mandatory conservation measures, approximately a 60-75 day supply of water.

The Kentucky River is a non-protected watershed. It is subject to contamination from straight pipes (unauthorized sewer discharges), agricultural runoff (chemical contamination), chemical spills, and drought. Yet approximately 22% of the state's population relies upon the river for water supply.

- **Affordability**

Affordability is a major concern to the City Commission, the Utility Commission and to management. The WMU service area population is approximately 27,000 of which 51% fall in the low to moderate income (LMI) level. A depressed world-wide economy further impacts the affordability of WMU's service.

The primary costs in WMU's budget are capital costs including renewals and replacements. The cost of compliance with the Consent Decree and the cost for upgrading and expanding WMU's water system capacity will exceed \$90 million. Renewals and replacements exceed \$1,000,000 each year. The driving factors in WMU's operations and maintenance budget are power costs, fuel costs, and personnel costs. WMU's personnel and related benefit costs total 53% of the total budget.

The City and WMU Commission, in concert with management, continuously work to reduce the financial burden of rate increases. Cost-effective decisions must be considered and made with respect to capital needs. Management must be focused on cost-effective operations and yet be aware of the high level of service demanded by WMU's customers.

The City and WMU Commission passed an annual adjustment to the rate structure tied to the Consumer Price Index (CPI). This adjustment will allow WMU to maintain its operating and maintenance budget current with the cost of living through annual adjustments to the rate versus the historical flat line approach with infrequent but significant adjustments. This approach was favored in a community survey by 73.5 % of the respondents.

The City and WMU Commissions, in concert with the Fiscal Court, have adopted legislation that will ensure that the costs of growth for WMU's sanitary sewer system are apportioned to all benefitted properties versus supported by the existing customer base. This approach is favored for its equity and for the benefit to the community by insuring that sanitary sewers are sized on a watershed basis versus the historical "first in, one size fits all approach".

The City and WMU Commission have secured grants and sought the best possible financing for WMU's capital needs. The city and WMU have applied for and been conditionally approved for a \$36,600,000 low interest (2.2%; 20 years) loan for the wastewater system improvements. The likelihood for financing of the water system improvements will be the sale of revenue bonds in the range of 4-5% for 20 years.

Rate increases for WMU's customers are inevitable. Rate increases for WMU's customers will be significant – likely in the range of 20-25% per year for a number of consecutive years. Rate increases must be put in place despite a depressed economy, high unemployment, and a declining stock market. Compliance with the Consent Decree, upgrading and improving WMU's water system capacity, and replacement of WMU's aging infrastructure to ensure service to existing customers and to position the community to be able to attract and retain residential, commercial, and industrial development while balancing the affordability of providing a prescribed level of service is and will be a challenge to WMU, the City, and the community.

BUSINESS FACTORS

• Facilities Plan Update

WMU is required by federal and state regulation to maintain a Facilities Plan that outlines the long-term plan for growth of the sanitary sewer system and treatment works. A Facilities Plan Update was completed and approved by the EEC for the upgrade of the Strodes Creek Wastewater Treatment Plant. The last Facilities Plan with respect to the collection system was completed in 1973. The plan should be updated on a minimum 20-year cycle. The WMU Commission authorized a Facilities Plan Update for the sanitary sewer collection system in August 2008. The Facilities Plan Update was necessary to determine the recommended end-of-pipe sewage management plan for the Lower Howards Creek Sanitary Sewer Improvements as is being required by the Consent Decree. The Facilities Plan Update, being completed at a cost of \$135,000, will identify and address sanitary sewer collection recommendations for WMU's 14 sub-watersheds listed below:

- Strodes Creek Basins A, B, C, and D
- Lower Howards Creek Basins A, B, and C
- Hancock Creek Basins A, B, and C
- Hoods Creek
- Four Mile Creek Basins A, B, and C

• Rate Studies

The WMU Commission authorized, at a cost of \$110,000, rate studies of WMU's three utility functions. The rate studies will propose cost of service rates to support WMU's operations, including the expanded operations as required by CMOM, the operations of the Strodes Creek WWTP and the planned WTP, the capital needs as required by the Consent Decree and the planned water system improvements. Included with the rate studies will be a revised schedule of System Development Charges (SDCs) and a schedule of pretreatment surcharges.

• Work Force

Key issues facing WMU in the coming years with respect to workforce include *Baby Boomer* retirements, loss of institutional and industry knowledge, finding and attracting qualified replacement employees, and training of employees to meet the increasingly sophisticated needs of water, wastewater, and solid waste utility operations including customer service, finance, information systems, administrative services and engineering.

WMU has 79 budgeted staff positions of which 76 are filled. The average age for WMU employees is 39 years. The number of eligible retirements at WMU over the next five years, due to age, years of service, or both, is seven or 9% of the workforce. Since 2002, there have been 19 retirements or 25% of the WMU workforce. Large scale retirement numbers often enable entities to renew and refresh operations, systems, and business philosophies. Transition planning has been successful for most key positions, however, such changeover carries the load of loss of institutional and industry

knowledge, and challenges management to find, attract, train, and retain replacements particularly for supervisory positions.

WMU's attractiveness as an employer is its benefits package. Salaries average below the private sector and other government utilities. Training for utility operations is typically on-the-job. Certification in operations and driver's licensing (commercial) is a job requirement for all three utility functions. Support functions, customer service and vehicle maintenance, as well as engineering and finance, will require on-the-job training specific to WMU's business operations. Workforce development will be key in maintaining the quality of service delivered by WMU and for compliance with enforcement and regulatory activities.

- **Infrastructure Renewal**

A structured approach for infrastructure renewal spreads costs over the long-term and can increase the service life of assets. WMU is a leader in Kentucky in the area of asset management and infrastructure renewal. WMU's infrastructure renewal program includes a prioritization methodology to maximize capital investment, and annual allocations for defined asset categories. WMU annually allocates an average of \$1,284,000 of its capital investment for this effort. Program elements include:

- Main Replacement Program
- Fire hydrant Replacement
- Gate Valve Box Adjustment – Pavement Overlay
- Elevated Storage Tank Rehabilitation
- Meter Change Out
- Main Replacement Program – Sewer
- Private Sewer Replacement
- Manhole Grade Adjustment – Pavement Overlay
- Inflow and Inflow (I/I) Rehabilitation
- Curbit Replacement
- Container Replacement
- Vehicles
- Plant & Equipment Improvements

While WMU's program of infrastructure renewal is a model for other utilities and public works agencies in Kentucky, the program is limited in its scope by funding.

Infrastructure renewal funding should be based upon a mathematical model that addresses asset category inventory and asset category service life. WMU's program is based upon funds available. As an example and simply stated, for the waterline asset category, funding for waterline replacement should be based upon the cost for replacing the number of miles of waterline divided by the service life of the pipe. In this example, if WMU owns and maintains 160.8 miles of waterline with the waterlines having a service life of 60 years, the allocation for waterline replacement should be the average cost of replacing 2.68 miles of waterline per year. At \$60 per foot for replacement of a waterline this calculates to an annual allocation of \$849,025. WMU allocates \$125,000. Likewise, if WMU owns and maintains 147.5 miles of sanitary sewer lines having a service life of 60 years, the allocation for sewer line replacement should be the average cost of replacing 2.45 miles of sewer line per year. At \$70 per foot for replacement of a sewer line, the annual allocation calculates to be \$924,000. WMU allocates \$125,000.

- **Regulations**

WMU and its utility functions are highly regulated. Regulation is a necessary part of the business to ensure a service delivery level and to protect the public's safety, health, and welfare. Regulations serve to protect the environment for future generations. Regulations ensure conservation and protection of our natural resources.

Regulations are regularly considered and promulgated by state and federal governments. WMU staff is active in monitoring proposed regulations and the impacts such regulations have on a local basis. Comment and impact on the promulgation of regulations on a federal level is limited, however, WMU staff communicate state and national industry organizations and through direct contact with federal officials elected from Kentucky. On a state level, WMU staff participates on numerous committees and task forces to provide a voice for city-owned water, wastewater, and solid waste utilities.

State regulations typically result as mandates on state regulatory agencies from federal legislation. Kentucky is a primacy state meaning that the state is responsible for implementing and enforcing federal regulation. WMU staff works to ensure that state regulations, when promulgated, are reasonable and practicable.

- **Vulnerability**

The impacts of 9/11 and the resulting passage of the Bioterrorism Act in 2002 required utilities to consider their vulnerabilities as a primary consideration versus a secondary consideration. For mid-size and smaller utilities such as WMU, the probability of an act of international violence or terrorism is extremely low.

However, WMU's vulnerabilities are real and must be considered. Planning must be in place to address catastrophic events, violence, or contamination. Potential threats to WMU include severe weather (tornado, lightning, ice or snow), earthquake, prolonged power outage, contamination of the raw or potable water supply, workplace or customer violence, hazardous chemical spills, contamination or contact, and regular job safety hazards including confined space, vehicular accidents, and personal injury accidents.

- **Growth**

It has been the policy of the WMU Commission to be neither pro nor con with respect to growth. Rather the Commission has placed as a part of its mission to accommodate growth as approved by the Planning Commission, the City Commission and the Fiscal Court with specified required levels of service. WMU and the City continue to examine and develop policies that provide for growth and that protect the existing customer base from the costs of serving growth.

The Consent Decree will impact extensions to the sanitary sewer system as a detailed, engineering-capacity analysis will be required for each extension. The capacity analysis will thus become a defacto growth management tool.

WMU avails itself of every opportunity to add to and to strengthen the water transmission system and backbone sanitary sewer system taking into consideration long range growth needs.

UTILITY HIGHLIGHTS

• Renewals and Replacements

WMU began its program of infrastructure renewals in 1996 with emphasis on improving service delivery and ensuring that all customers are afforded a comparable level of service delivery. Historically, WMU never attempted these types of improvements without incurring new debt. The infrastructure renewal program has been implemented and managed without additional funding allocations or rate increases. Funding for the program was achieved through management of WMU's depreciation funds. To date, this program has resulted in the following replacement totals:

• Waterline Replacements	24,197 feet
• Sanitary Sewer Replacements	23,312 feet
• Fire Hydrant Replacements	40
• Gate Valve Replacements	121
• Elevated Storage Tank Rehabilitations	2

UTILITY HIGHLIGHTS: FINANCIAL

Total Assets increased from \$85,879,540, June 30, 2008, to \$88,844,252 June 30, 2009, a net increase of \$2,964,712 or 3.45%. A new wastewater treatment plant was completed and placed in service as well as other smaller construction projects which account for the large increase in Utility Systems. The increase is also partly due to the donated capital of ownership and perpetual maintenance of system water and sewer lines and related appurtenances.

Operating Revenues decreased from \$9,803,920, June 30, 2008, to \$9,664,848, June 30, 2009, a net decrease of \$139,072 or 1.42%. The decrease in revenues was attributable to decreased water demand and accompanying sewer charges by industrial customers. The decrease in Wastewater Revenues of \$192,659 or 4.44% was the largest decrease as compared to Water Revenues at a decrease of \$3,378 or 0.10%. The Solid Waste revenues increased \$56,965 or 2.82%.

Operating Expenses increased from \$9,158,472, June 30, 2008, to \$10,405,368, June 30, 2009, a net increase of \$1,246,896 or 13.61%. The increase in Operating Expense is due to an increase in depreciation expense and electricity costs associated the operation of the new wastewater treatment plant. The Wastewater expenses increased \$1,308,286 or 44.53% for the year. Water expenses increased \$61,410 or 2.40%. Solid Waste expenses decreased \$114,138 or 6.53%.

Net Income to Retained Earnings decreased from \$937,711, June 30, 2008, to a net loss of \$884,541, June 30, 2009, a net decrease of \$1,822,252 or 194.33%. The decrease in Net Income to Retained Earnings is due to decreased industrial water and sewer revenue and the increase in operating expenses and interest expense associated with the KIA loan for the wastewater treatment plant.

- **Balance Sheet**

Condensed Balance Sheet - Assets

	2009	2008	Difference	Percent
Current Assets:				
Cash and equivalents	\$1,340,694	\$1,247,424	\$93,270	7.48
Accounts Receivable, Customers	\$1,064,963	\$1,086,683	\$(21,720)	(2.00)
Other Acct. Receivable	\$936,993	\$1,156,177	\$(219,184)	(18.96)
Materials & Prepaid Expenses	\$982,183	\$1,095,279	\$(113,096)	(10.33)
Total Current Assets	\$4,324,833	\$4,585,563	\$(260,730)	(5.69)
Restricted Assets:				
Cash and equivalents	\$5,114,094	\$5,555,442	\$(441,348)	(7.94)
Investments	\$9,508,869	\$10,772,155	\$(1,263,286)	(11.73)
Accrued Interest	\$156,559	\$81,595	\$74,964	91.87
Total Restricted Assets	\$14,779,522	\$16,409,192	\$(1,629,670)	(9.93)
Property, Plant & Equip:				
Utility Systems, net of Depr.	\$60,421,815	\$35,807,286	\$24,614,529	68.74
Land	\$1,051,011	\$1,051,011		0
Construction in Progress	\$7,837,161	\$27,535,651	\$(19,698,490)	(71.54)
Total Property, Plant & Equip	\$69,309,987	\$64,393,948	\$4,916,039	7.63
Other Assets	\$429,910	\$490,837	\$(60,927)	(12.41)
Total Assets	\$88,844,252	\$85,879,540	\$2,964,712	3.45

Condensed Balance Sheet – Liabilities

	2009	2008	Difference	Percent
Current Liabilities:				
Current Liabilities	\$1,276,766	\$1,053,045	\$223,721	21.25
Current Liabilities payable from Restricted Liabilities	\$3,001,607	\$2,491,182	\$510,425	20.49
Total Current Liabilities	\$4,278,373	\$3,544,227	\$734,146	20.71
Long-term Debt, less current portion	\$32,415,833	\$32,857,150	\$(441,317)	(1.34)
Total Liabilities	\$36,694,206	\$36,401,377	\$292,829	0.80
Net Assets:	\$52,150,046	\$49,478,163	\$2,671,883	5.40
Invested in Capital Assets, Net of Related Debt	\$34,522,429	\$29,456,439	\$5,065,990	17.19
Restricted Net Assets	\$14,612,955	\$16,234,206	\$(1,621,251)	(9.98)
Unrestricted Net Assets	\$3,014,662	\$3,787,518	\$(772,856)	(20.4)
Total Net Assets	\$52,150,046	\$49,478,163	\$2,671,883	5.4
Total Liabilities & Net Assets	\$88,844,252	\$85,879,540	\$2,964,712	3.45

- **Income Statement**

Condensed Statement of Revenues and Expenses

	2009	2008	Difference	Percent
Operating Revenues:				
Water	\$3,439,492	\$3,442,870	\$(3,378)	(0.10)
Wastewater	\$4,147,585	\$4,340,244	\$(192,659)	(4.44)
Solid waste	\$2,077,771	\$2,020,806	\$56,965	2.82
Total Revenues	\$9,664,848	\$9,803,920	\$(139,072)	(1.42)
Operating Expenses including Depreciation:				
Administration	\$1,777,949	\$1,788,174	\$(10,225)	(.57)
Solid Waste	\$1,634,134	\$1,748,272	\$(114,138)	(6.53)
Water	\$2,622,639	\$2,561,229	\$61,410	2.40
Wastewater	\$4,246,483	\$2,938,197	\$1,308,286	44.53
Vehicle Maintenance	\$124,163	\$122,600	\$1,563	1.27
Total Operating Expenses	\$10,405,368	\$9,158,472	\$1,246,896	13.61
Operating Income	\$(740,520)	\$645,448	\$(1,385,968)	(214.73)
Non-Operating Income	\$580,483	\$853,728	\$(273,245)	(32.01)
Interest Expense	\$(724,504)	\$(561,465)	\$(163,039)	29.04
Net Income to Retained Earnings	\$(884,541)	\$937,711	\$(1,822,252)	(194.33)
Grants and Capital Contributions	\$3,556,424	\$3,879,605	\$(323,181)	(8.33)
Change in Net Assets	\$2,671,883	\$4,817,316	\$(2,145,433)	(44.53)
Net Assets, Beginning of Year	\$49,478,163	\$44,660,847	\$4,817,316	10.78
Net Assets, End of Year	\$52,150,046	\$49,478,163	\$2,671,883	5.12

- **Five-Year Capital Plan**

The WMU Commission maintains and annually updates a five-year capital plan that identifies and prioritizes the capital requirements of WMU necessary for customer service, regulatory compliance, and to accommodate growth. The five-year investment totals in excess of \$6,832,100. Of these planned expenditures, \$6,000,000 will be invested in infrastructure renewal and administrative support with the remaining \$323,600 allocated for one-time, and intermittent investments. Additionally \$275,000 is reserved for emergency and / or unexpected expenditures.

- **Debt Administration**

As of July 1, 2009, WMU maintained the following debt:

- Series 2002 Bonds \$7,895,000
- Series 2003 Bonds \$1,470,000
- KIA loan \$20,528,943

The Debt Service coverage factor of 1.32 in FY 2008/2009 is unfavorable to the required 1.4 coverage limit. Debt Service coverage is based upon the revenue of the combined utility functions – Water, Sewer, and Solid Waste. WMU currently maintains an A2 bond rating by Moody's Investor Services. The Series 2003 Bonds will retire in 2010 and Series 2002 will retire in 2032.

WMU has a KIA loan connected to the construction of the new WWTP. The City and the WCCIDA will be sharing payment of the principal and interest until WMU assumes full responsibility of the debt after the Series 2003 Bonds are retired in 2010.

- **FY 2009/2010 Budget Assumptions**

Total Combined Revenues for FY 2009/2010 are projected to increase from FY 2008/2009 Total Combined Revenues by 9.96%. No annual adjustment to rates based upon the CPI index is expected this year, however, a rate increase is budgeted in October for Capital needs. Operating Expenses excluding depreciation for FY 2009/2010 are projected to decrease over FY 2008/2009 by approximately 0.43%. Operating expenses will be impacted by increased power and employee benefit costs and decreased by chemical, insurance, and fuel costs.

As has been the case in prior budgets and in actual results, utility operating revenues typically are not sufficient to meet the operations and maintenance expense, depreciation, and debt service needs of the utility. For these periods, non-operating interest and other income, which is added to utility operating revenues, will offset operating losses to produce a positive net income.

CONTACTING THE COMPANY'S FINANCIAL MANAGEMENT

This report is designed to provide the WMU Commission, the City Commission, the customers of WMU, and WMU's creditors a general overview of WMU's finances and to demonstrate WMU's financial accountability. Questions should be addressed to:

Mike Flynn
Director of Engineering & Operations

Or

Jennifer Sparks
Director of Finance and Accounting
150 North Main Street
P.O. Box 4177
Winchester, KY 40392-4177
859-744-5434

**WINCHESTER MUNICIPAL UTILITIES
STATEMENTS OF NET ASSETS
JUNE 30, 2009 AND 2008**

ASSETS	<u>2009</u>	<u>2008</u>
CURRENT ASSETS		
Cash and Cash Equivalents	\$ 1,340,694	\$ 1,247,424
Accounts Receivable, Customers (Net of allowance for Doubtful Accounts, 2009 and 2008, \$22,194 and \$20,708)	1,064,963	1,086,683
SDC Assessments Receivable	884,680	1,118,110
Other Accounts Receivable	52,313	38,067
Materials and Supplies	346,333	343,561
Prepaid Expenses	<u>635,850</u>	<u>751,718</u>
Total Current Assets	<u>4,324,833</u>	<u>4,585,563</u>
RESTRICTED ASSETS		
Cash and Cash Equivalents	5,114,094	5,555,442
Investments	9,508,869	10,772,155
Accrued Interest	<u>156,559</u>	<u>81,595</u>
Total Restricted Assets	<u>14,779,522</u>	<u>16,409,192</u>
PROPERTY, PLANT AND EQUIPMENT		
Utility Systems, net of depreciation	60,421,815	35,807,286
Land	1,051,011	1,051,011
Construction in Progress	<u>7,837,161</u>	<u>27,535,651</u>
Total Property, Plant and Equipment	<u>69,309,987</u>	<u>64,393,948</u>
OTHER ASSETS		
Bond Issue Costs	96,137	134,177
Other Receivable	<u>333,773</u>	<u>356,660</u>
Total Other Assets	<u>429,910</u>	<u>490,837</u>
TOTAL ASSETS	<u><u>\$ 88,844,252</u></u>	<u><u>\$ 85,879,540</u></u>

See Auditor's Report and Accompanying Notes

**WINCHESTER MUNICIPAL UTILITIES
STATEMENTS OF NET ASSETS (CONTINUED)
JUNE 30, 2009 AND 2008**

LIABILITIES AND NET ASSETS	<u>2009</u>	<u>2008</u>
CURRENT LIABILITIES		
Accounts Payable	\$ 606,591	\$ 268,894
Other Accrued Liabilities	377,192	413,087
Compensated Absences	286,926	368,834
Current Portion of Capital Lease Payable	6,057	2,230
	<u>1,276,766</u>	<u>1,053,045</u>
Total Current Liabilities		
CURRENT LIABILITIES PAYABLE FROM RESTRICTED ASSETS		
Accounts Payable - Construction	389,963	-
Accounts Payable - Retainage	93,381	250,000
Customer Deposits	152,595	163,053
Current Portion of Long-Term Debt	2,365,668	2,078,129
	<u>3,001,607</u>	<u>2,491,182</u>
Total Current Liabilities Payable from Restricted Assets		
LONG-TERM DEBT, Less Current Portion		
Long-Term Debt, Less Current Portion	32,409,273	32,841,211
Capital Lease Payable, Less Current Portion	6,560	15,939
	<u>32,415,833</u>	<u>32,857,150</u>
Total Long-Term Debt, Less Current Portion		
TOTAL LIABILITIES	<u>36,694,206</u>	<u>36,401,377</u>
NET ASSETS		
Invested in Capital Assets, Net of Related Debt	34,522,429	29,456,439
Restricted for Capital Projects	12,378,335	13,530,539
Restricted for Bond Debt Service	2,234,620	2,576,658
Restricted for Self Insurance	-	127,009
Unrestricted	3,014,662	3,787,518
	<u>52,150,046</u>	<u>49,478,163</u>
TOTAL NET ASSETS	<u>52,150,046</u>	<u>49,478,163</u>
TOTAL LIABILITIES AND NET ASSETS	<u>\$ 88,844,252</u>	<u>\$ 85,879,540</u>

See Auditor's Report and Accompanying Notes

WINCHESTER MUNICIPAL UTILITIES
STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS
FOR THE YEARS ENDED JUNE 30, 2009 AND 2008

	<u>2009</u>	<u>2008</u>
OPERATING REVENUES		
Water	\$ 3,439,492	\$ 3,442,870
Wastewater	4,147,585	4,340,244
Solid Waste	2,032,227	1,967,288
Transfer Station	<u>45,544</u>	<u>53,518</u>
Total Operating Revenues	<u>9,664,848</u>	<u>9,803,920</u>
OPERATING EXPENSES		
Administrative	1,777,949	1,788,174
Solid Waste	1,634,134	1,748,272
Water	2,622,639	2,561,229
Wastewater	4,246,483	2,938,197
Vehicle Maintenance	<u>124,163</u>	<u>122,600</u>
Total Operating Expenses	<u>10,405,368</u>	<u>9,158,472</u>
OPERATING INCOME (LOSS)	(740,520)	645,448
NONOPERATING REVENUES (EXPENSES)		
Interest Income	357,388	592,882
Other Income	223,095	260,846
Interest Expense	(673,420)	(505,998)
Amortization Expense of bond issue costs & bond discount	<u>(51,084)</u>	<u>(55,467)</u>
Total Nonoperating Revenues (Expenses)	<u>(144,021)</u>	<u>292,263</u>
NET INCOME (LOSS) BEFORE GRANTS & CONTRIBUTIONS	(884,541)	937,711
GRANTS AND CAPITAL CONTRIBUTIONS	<u>3,556,424</u>	<u>3,879,605</u>
CHANGE IN NET ASSETS	<u>2,671,883</u>	<u>4,817,316</u>
NET ASSETS, BEGINNING OF YEAR	<u>49,478,163</u>	<u>44,660,847</u>
NET ASSETS, END OF YEAR	<u>\$ 52,150,046</u>	<u>\$ 49,478,163</u>

See Auditor's Report and Accompanying Notes

**WINCHESTER MUNICIPAL UTILITIES
STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED JUNE 30, 2009 AND 2008**

	2009	2008
CASH FLOWS FROM OPERATING ACTIVITIES		
Receipts from Customers	\$ 9,909,540	\$ 9,681,170
Payments to Suppliers	(4,254,390)	(6,589,046)
Payments to Employees	(2,599,871)	(2,452,316)
Other Receipts (Payments)	58,668	724,446
Net Cash Provided (Used) by Operating Activities	3,113,947	1,364,254
CASH PROVIDED (USED) BY CAPITAL AND RELATED FINANCING ACTIVITIES		
Proceeds from Sale of Equipment	29,431	30,000
Proceeds from Long-Term Debt	1,933,613	7,620,385
Principal Payments	(1,625,552)	(3,117,573)
Interest Payments	(832,920)	(951,292)
Purchase of Property, Plant and Equipment	(7,109,308)	(3,793,773)
Proceeds from Federal and State Grants - Capital items	2,387,461	787,523
Contributed Capital Received	134,576	985,990
Net Cash Provided (Used) by Capital and Related Financing Activities	(5,082,699)	1,561,260
CASH PROVIDED (USED) BY INVESTING ACTIVITIES		
Cash from Interest	357,388	589,906
Net Cash Provided (Used) by Investing Activities	357,388	589,906
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(1,611,364)	3,515,420
CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR	17,575,021	14,059,601
CASH AND CASH EQUIVALENTS, END OF YEAR	\$ 15,963,657	\$ 17,575,021
Reconciliation of Cash and Cash Equivalents to the Statement of Net Assets:		
Cash and Cash Equivalents - unrestricted	\$ 1,340,694	\$ 1,247,424
Cash and Cash Equivalents - restricted	5,114,094	5,555,442
Investments - Restricted	9,508,869	10,772,155
Cash and Cash Equivalents, End of Year	\$ 15,963,657	\$ 17,575,021

See Auditor's Report and Accompanying Notes

**WINCHESTER MUNICIPAL UTILITIES
STATEMENTS OF CASH FLOWS (CONTINUED)
FOR THE YEARS ENDED JUNE 30, 2009 AND 2008**

	<u>2009</u>	<u>2008</u>
RECONCILIATION OF OPERATING INCOME (LOSS) TO NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES		
Operating Income (Loss)	\$ (740,520)	\$ 645,448
Adjustments to Reconcile Operating Income (Loss) to Net Cash Provided (Used) by Operating Activities:		
Depreciation	2,984,774	2,067,818
Amortization	38,040	38,040
(Gain) Loss on Sale of Equipment	11,987	-
(Increase) Decrease in Current Assets:		
Accounts Receivable, Customers	21,720	(59,727)
SDC Receivables	233,430	(76,619)
Other Accounts Receivable	8,641	78,407
Grants Receivable	-	608,000
Material and Supplies	(2,772)	(69,726)
Prepaid Expenses	115,867	(48,527)
Increase (Decrease) in Current Liabilities:		
Accounts Payable	337,697	(485,479)
Accounts Payable - Construction	389,963	(340,288)
Accounts Payable - Retainage	(156,619)	(851,229)
Accrued Liabilities	(35,895)	61,342
Accrued Vacation	(81,908)	53,871
Accrued Interest on Bonds	-	(270,674)
Customer Deposits	<u>(10,458)</u>	<u>13,597</u>
 Net Cash Provided (Used) by Operating Activities	 <u>\$ 3,113,947</u>	 <u>\$ 1,364,254</u>
 NONCASH TRANSACTIONS AFFECTING FINANCIAL POSITION		
Capital Contributions from Developers and Government Entities	\$ 1,034,687	\$ 2,714,092
Purchase of Capital Asset through a Capital Lease	-	18,169
	<u>\$ 1,034,687</u>	<u>\$ 2,732,261</u>

See Auditor's Report and Accompanying Notes

**WINCHESTER MUNICIPAL UTILITIES
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEARS ENDED JUNE 30, 2009 AND 2008**

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Introduction

Winchester Municipal Utilities (WMU), is a component of the City of Winchester, Kentucky, and is accounted for as a governmental enterprise fund. It is financed and operated in a manner similar to a private business enterprise where the intent of the governing body is that costs (expenses, including depreciation) of providing goods or services to the general public on a continuing basis are financed primarily through user charges. The accounts are maintained on the accrual basis of accounting.

In accordance with paragraph 7 of Governmental Accounting Standards Board (GASB) Statement No. 20, WMU applies all applicable GASB pronouncements as well as the following pronouncements issued on or before November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements: Financial Accounting Standards Board (FASB) Statements and Interpretations, Accounting Principles Board Opinions, and Accounting Research Bulletins of the Committee on Accounting Procedure.

Cash and Cash Equivalents

All cash and investments, unrestricted and restricted, are considered cash and cash equivalents for the purpose of the Statements of Cash Flows. The composition of these cash and investments is as follows:

	<u>2009</u>		<u>2008</u>
Cash - Unrestricted	\$ 1,340,694	\$	1,247,424
Cash - Restricted	5,114,094		5,555,442
Investments	9,508,869		10,772,155
Total	<u>\$ 15,963,657</u>	\$	<u>17,575,021</u>

Investments

Investments consist principally of certificates of deposit and are carried at cost. Other investments are carried at fair market value, based upon quoted market prices and do not differ materially from cost. The majority of the investments are restricted as to use.

Type	<u>2009</u>		<u>2008</u>
Certificates of Deposit	\$ 9,480,303	\$	10,703,824
Government Income Fund	28,566		28,062
Government Securities	0		40,269
Total	<u>\$ 9,508,869</u>	\$	<u>10,772,155</u>

**WINCHESTER MUNICIPAL UTILITIES
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEARS ENDED JUNE 30, 2009 AND 2008**

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Accounts Receivable

Accounts receivable - Customers, are stated at the amount management expects to collect from outstanding balances. Management provides for probable uncollectible amounts through a provision for bad debt expense, instead of netting with revenues because of immateriality, and an adjustment to an allowance for doubtful accounts based on its assessment of the current status of individual accounts. Balances that are still outstanding after management has used reasonable collection efforts are written off through a charge to the valuation allowance and a credit to accounts receivable.

SDC assessments and other receivables are stated at the amount management expects to collect from outstanding balances and management expects to fully collect all of these receivables.

Other receivable consists of a note receivable dated April 20, 2005 from a Corporation in the amount of \$603,000. As of June 30, 2009 and 2008, the balance was \$333,773 and \$356,660, respectively. The note receivable bears an interest rate of 5.00% and matures on April 20, 2020. Interest income received as of June 30, 2009 and 2008 was \$17,313 and \$18,427, respectively.

Materials and Supplies

Materials and supplies are stated at cost. Cost is determined using the “first-in, first-out” method.

Prepaid Expenses

Certain payments to vendors reflect costs applicable to future accounting periods and are recorded as prepaid expenses.

Property, Plant and Equipment

Property, plant, and equipment are stated at cost and depreciated over their estimated useful lives using the straight-line method. Donated capital assets are recorded at estimated fair market value at the date of donation. WMU’s capitalization policy is \$500.

Major outlays for capital assets and improvements are capitalized when assets constructed are completed. Interest incurred during the construction phase of capital assets is included as part of the capitalized value of the assets constructed.

Accrued Compensated Absences

Accumulated vacation, sick leave and compensatory time are recorded as an expense and liability as these benefits accrue to employees in accordance with the provisions of Statement No. 16 of the Governmental Accounting Standards Board.

**WINCHESTER MUNICIPAL UTILITIES
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEARS ENDED JUNE 30, 2009 AND 2008**

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Long-Term Debt

Bond premiums and discounts, as well as issuance costs, are deferred and amortized over the life of the bonds. Bonds payable are reported net of the applicable bond premium or discount. Bond issuance costs are reported as deferred charges and amortized over the term of the related debt. Amortization expense for bond issue costs as of June 30, 2009 and 2008 was \$38,040 and \$38,040, respectively. Amortization expense for bond discount was \$13,044 and \$17,427, respectively.

Net Assets

Net assets are comprised of three categories: net assets invested in capital assets, net of related debt; restricted net assets; and unrestricted net assets. The first category 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 unspent related debt proceeds at year-end, the portion of the debt attributable to the unspent proceeds are not included in the calculation of invested in capital assets, net of related debt. Rather, that portion of the debt is included in the same net assets component as the unspent proceeds. The second category consists of constraints placed on net asset use 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. The third category consists of net assets that do not meet the definition of “restricted” or “invested in capital assets, net of related debt”.

When both restricted and unrestricted resources are available for use, it is WMU’s policy to use restricted resources first, and then unrestricted resources as they are needed.

Revenues and Expenses

Revenues and expenses are distinguished between operating and non-operating items. Operating revenues generally result from providing services and producing, and delivering goods in connection with WMU’s principal ongoing operations. The principal operating revenues of WMU are charges to customers for sales and services. Operating expenses for enterprise funds include the cost of sales and services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

Nonmonetary Transaction

WMU accepts utility installations built by contractors upon inspection. The utility installations are added to fixed assets and contributed capital at contractor’s cost.

**WINCHESTER MUNICIPAL UTILITIES
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEARS ENDED JUNE 30, 2009 AND 2008**

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Capital and Operating Grants and Subsidies

Operating grants and subsidies that may be used to pay operating expenses are recorded as other income. Grants that are restricted to the purchase of property, plant and equipment are recorded as contributed capital.

Tap Fees

Tap Fees are restricted by ordinance for the use of capital improvements.

System Development Charges

WMU assesses system development charges to developers as a means to help finance new construction of systems required to facilitate growth. The charges are restricted by ordinance for capital construction.

Self-Insurance

In fiscal year ended June 30, 1987, the Winchester Municipal Utilities Board of Commissioners approved a resolution establishing a self-insurance fund for all liability and property damage claims. On January 16, 1996, management determined that the program did not provide adequate protection and currently obtains insurance coverage from outside sources. During the current fiscal year, the Board voted to dissolve the fund and deposit any remaining monies into the Operations and Maintenance cash account.

Basis of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

Reclassifications

Certain reclassifications have been made to the prior year financial statements in order for them to be in conformity with the current year presentation.

Joint Venture

Clark County Geographic Information System Consortium (CCGIS), is a governmental agency created by an inter-local agreement between the Clark County PVA, City of Winchester (City) and WMU. CCGIS was created to provide a geographic system to serve the needs of Winchester and Clark County. The operations are funded by the City and WMU and WMU provides management services. WMU contributed \$87,065 and \$72,290 for the years ended 2009 and 2008. CCGIS had accounts payables to WMU of \$12,198 and \$13,919 for they years ended 2009 and 2008. Complete financial statements for CCGIS can be obtained from WMU's Director of Finance.

**WINCHESTER MUNICIPAL UTILITIES
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEARS ENDED JUNE 30, 2009 AND 2008**

NOTE 2 – RESTRICTED ASSETS

The restricted assets in the accompanying financial statements are restricted as to use by bond ordinance or by external parties at June 30, 2009 and 2008 follows:

	<u>Cash</u>	<u>Investments at Cost</u>	<u>Accrued Interest</u>	<u>Total 2009</u>
Restricted by Ordinance				
With Paying Agents	\$ 276,206	\$ 0	\$ 0	\$ 276,206
Reserve Accounts	603	1,925,000	32,811	1,958,414
Depreciation Account	3,398,342	28,566	0	3,426,908
Subtotal	<u>3,675,151</u>	<u>1,953,566</u>	<u>32,811</u>	<u>5,661,528</u>
Other Restricted Assets				
SDC Water Fund	772,990	1,800,000	0	2,572,990
SDC Wastewater Fund	296,648	1,574,937	0	1,871,585
Customer Deposits	64,861	100,000	1,704	166,565
WWTP Construction Fund	198,700	0	0	198,700
2008 BAN	105,743	3,500,000	122,044	3,727,787
Capital Accum-water	0	376,661	0	376,661
Capital Accum- Wastewater	0	203,705	0	203,705
Total	<u>\$ 5,114,094</u>	<u>\$ 9,508,869</u>	<u>\$ 156,559</u>	<u>\$ 14,779,522</u>
	<u>Cash</u>	<u>Investments at Cost</u>	<u>Accrued Interest</u>	<u>Total 2008</u>
Restricted by Ordinance				
With Paying Agents	\$ 596,018	\$ 0	\$ 0	\$ 596,018
Reserve Accounts	627	1,925,000	55,013	1,980,640
Depreciation Account	3,192,608	68,330	753	3,261,691
Subtotal	<u>3,789,253</u>	<u>1,993,330</u>	<u>55,766</u>	<u>5,838,349</u>
Other Restricted Assets				
SDC Water Fund	658,872	1,800,000	0	2,458,872
SDC Wastewater Fund	533,613	1,800,000	0	2,333,613
Customer Deposits	72,129	100,000	2,858	174,987
Self-Insurance Fund	1,317	121,394	4,298	127,009
2008 BAN	500,258	4,500,000	4,068	5,004,326
Capital Accum-water	0	300,735	9,588	310,323
Capital Accum-wastewater	0	156,696	5,017	161,713
Total	<u>\$ 5,555,442</u>	<u>\$ 10,772,155</u>	<u>\$ 81,595</u>	<u>\$ 16,409,192</u>

NOTE 3 – CASH AND INVESTMENTS

Kentucky Revised Statutes authorize municipalities to invest in obligations of the United States and its agencies, obligations of the Commonwealth of Kentucky and its agencies and shares in savings and loan associations insured by federal agencies. Larger amounts can be deposited in savings and loan associations and banks provided such institutions pledge obligations of the United States government or its agencies as security. As of June 30, 2009 and 2008, WMU was in compliance with this requirement.

**WINCHESTER MUNICIPAL UTILITIES
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEARS ENDED JUNE 30, 2009 AND 2008**

NOTE 3 – CASH AND INVESTMENTS (continued)

Custodial credit risk is the risk that, in the event of the failure of the counterparty, WMU will not be able to recover the value of its cash and investments that are in possession of an outside party. Consistent with WMU's investment policy, all cash and investments are either fully collateralized by federal depository insurance or by the pledging institution in WMU's name or obligations of the U. S. Government.

NOTE 4 – PROPERTY, PLANT AND EQUIPMENT

WMU's systems consist of the following:

	<u>Beginning</u>	<u>Additions</u>	<u>Disposals</u>	<u>2008</u>
Land (non-depreciable)	\$ 1,051,012	\$ 0	\$ 0	\$ 1,051,012
Construction in Progress (non-depreciable)	24,784,061	3,727,815	(976,225)	27,535,651
Administrative	2,722,285	32,495	0	2,754,780
Water System	30,174,941	2,660,068	0	32,835,009
Wastewater System	32,273,922	862,505	0	33,136,427
Solid Waste	4,812,797	213,877	(43,459)	4,983,215
Vehicle Maintenance	402,741	0	0	402,741
Equipment Capital Lease	43,835	18,169	0	62,004
	<u>96,265,594</u>	<u>7,514,929</u>	<u>(1,019,684)</u>	<u>102,760,839</u>
(Total Accumulated Depreciation)	<u>(36,342,532)</u>	<u>(2,067,818)</u>	<u>43,459</u>	<u>(38,366,891)</u>
	<u>\$ 59,923,062</u>	<u>\$ 5,447,111</u>	<u>\$ (976,225)</u>	<u>\$ 64,393,948</u>
	<u>Beginning</u>	<u>Additions</u>	<u>Disposals</u>	<u>2009</u>
Land (non-depreciable)	\$ 1,051,012	\$ 0	\$ 0	\$ 1,051,012
Construction in Progress (non-dep.)	27,535,651	7,703,473	(27,401,962)	7,837,161
Administrative	2,754,780	99,538	0	2,854,318
Water System	32,835,009	1,875,391	0	34,710,400
Wastewater System	33,136,427	25,308,501	(53,347)	58,391,581
Solid Waste	4,983,215	324,269	0	5,307,484
Vehicle Maintenance	402,741	6,053	0	408,794
Equipment Capital Lease	62,004	0	0	62,004
	<u>102,760,839</u>	<u>35,317,225</u>	<u>(27,455,309)</u>	<u>110,622,755</u>
(Total Accumulated Depreciation)	<u>(38,366,891)</u>	<u>(2,984,774)</u>	<u>38,899</u>	<u>(41,312,767)</u>
	<u>\$ 64,393,948</u>	<u>\$ 32,332,451</u>	<u>\$ (27,416,410)</u>	<u>\$ 69,309,987</u>

**WINCHESTER MUNICIPAL UTILITIES
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEARS ENDED JUNE 30, 2009 AND 2008**

NOTE 4 – PROPERTY, PLANT AND EQUIPMENT (continued)

Depreciation expense in total and per function follows:

<u>Function</u>	<u>2009</u>	<u>2008</u>
Administrative	\$ 117,050	\$ 125,215
Water System	776,619	771,151
Wastewater System	1,878,519	902,387
Solid Waste	190,618	248,346
Vehicle Maintenance	21,968	20,720
Total Depreciation Expense	<u>\$ 2,984,774</u>	<u>\$ 2,067,818</u>

NOTE 5 – LONG-TERM DEBT

Long-Term Debt consists of bonds and other indebtedness for which the changes in the years ended June 30, 2009 and 2008 are as follows:

<u>Description</u>	<u>Beginning</u>	<u>Borrowings Additions</u>	<u>Repayments Reductions</u>	<u>2009 Ending</u>	<u>Current</u>
Compensated Absences	\$ 368,834	\$ 24,315	\$ (106,223)	\$ 286,926	\$ 0
Bonds	10,852,954	0	(1,606,956)	9,245,998	1,647,573
KIA Loan	19,066,386	1,933,613	(471,056)	20,528,943	718,095
2008 BAN	5,000,000	0	0	5,000,000	0
Capital Lease	18,169	0	(5,552)	12,617	6,057
Total Long-Term Debt	<u>\$ 35,306,343</u>	<u>\$ 1,957,928</u>	<u>\$ (2,189,787)</u>	<u>\$ 35,074,484</u>	<u>\$ 2,371,725</u>
<u>Description</u>	<u>Beginning</u>	<u>Borrowings Additions</u>	<u>Repayments Reductions</u>	<u>2008 Ending</u>	<u>Current</u>
Compensated Absences	\$ 314,963	\$ 100,140	\$ (46,269)	\$ 368,834	\$ 0
Bonds	13,970,527	0	(3,117,573)	10,852,954	1,602,573
KIA WWTP Construction Loan	16,446,002	2,620,384	0	19,066,386	475,556
2008 BAN	0	5,000,000	0	5,000,000	0
Capital Lease	0	18,169	0	18,169	2,230
Total Long-Term Debt	<u>\$ 30,731,492</u>	<u>\$ 7,738,693</u>	<u>\$ (3,163,842)</u>	<u>\$ 35,306,343</u>	<u>\$ 2,080,359</u>

**WINCHESTER MUNICIPAL UTILITIES
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEARS ENDED JUNE 30, 2009 AND 2008**

NOTE 5 – LONG-TERM DEBT (Continued)

The Winchester Municipal Utilities bonded indebtedness and other long-term notes at June 30, 2009 and 2008, are summarized as follows:

	<u>Rate</u>	<u>Maturity</u>	<u>Original Issue</u>	<u>Total 2009</u>	<u>Total 2008</u>
2002 Issue	4.50 – 5.125%	07/01/32	\$ 9,025,000	\$ 7,895,000	\$ 8,080,000
2003 Issue	2.00 – 2.50%	07/01/10	9,070,000	1,470,000	2,905,000
				<u>9,365,000</u>	<u>10,985,000</u>
Less unamortized bond discount				119,002	132,046
				<u>9,245,998</u>	<u>10,852,954</u>
KIA WWTP Construction Loan	1.00%	12/01/28	21,000,000	20,528,944	19,066,386
2008 Bond Anticipation Note	3.19%	06/15/11	5,000,000	5,000,000	5,000,000
				<u>34,774,941</u>	<u>34,919,340</u>
Less current maturities				<u>2,365,668</u>	<u>2,078,129</u>
				<u>\$ 32,409,273</u>	<u>\$ 32,841,211</u>

KIA interest and principal payments are due on December 1st and June 1st. Other bond interest is payable on July 1st and January 1st and the bond principal is payable on July 1st.

The bond debt service requirements, as of June 30, 2009, are as follows:

<u>Fiscal Year</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2010	\$2,365,668	\$632,265	\$2,997,933
2011	6,005,379	580,742	6,586,121
2012	1,362,749	561,801	1,924,550
2013	1,382,549	540,625	1,923,174
2014	1,209,838	519,382	1,729,220
2015-2019	6,436,440	2,272,094	8,708,534
2020-2024	7,101,080	1,648,409	8,749,489
2025-2029	7,296,238	891,122	8,187,360
2030-2032	1,615,000	168,356	1,783,356
	<u>\$34,774,941</u>	<u>\$7,814,796</u>	<u>\$42,589,737</u>

**WINCHESTER MUNICIPAL UTILITIES
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEARS ENDED JUNE 30, 2009 AND 2008**

NOTE 5 – LONG-TERM DEBT (Continued)

KIA Loan

On July 1, 2005, Winchester Municipal Utilities entered into an “Assistance Agreement” with the Kentucky Infrastructure Authority (KIA), to provide funds for the construction of a new wastewater treatment plant. This agreement calls for interest to be paid every six months starting December 1, 2005 at the rate of 1% of the outstanding balance. The amount of interest due will vary from due date to due date based upon the amount of funds drawn down to fund construction of the wastewater treatment plant. Principal payments are due to be paid every December 1 and June 1 starting after the wastewater treatment plant goes online. The online date for the plant was July, 2008, with principal payments due to begin on June 1, 2009, and be due every December 1 and June 1 thereafter.

Due to Winchester Municipal Utilities current rate structure and debt service availability, the Winchester/Clark County Industrial Authority and the City of Winchester have agreed to provide Winchester Municipal Utilities with interim financing. The Industrial Authority will be contributing a portion of the amounts necessary to pay all principal payments due June 1, 2009 through June 1, 2010, not to exceed \$1,435,000. While, the City of Winchester will contribute the monies necessary to pay the interest expense from inception of the loan through June 1, 2010, and any principal amounts left unpaid through June 1, 2010.

The Kentucky Infrastructure Authority has made the loan inferior and subordinate to the security interest and source of payment for the Debt Obligations of Winchester Municipal Utilities payable from the revenues of the System outstanding at the time of the execution of the “Assistance Agreement”. The Agreement also further states that the Kentucky Infrastructure Authority must be notified no less than thirty days (30), in writing, prior to the issuance of any further debt obligations on parity with the current debt obligations.

2008 Bond Anticipation Note

On June 19, 2008, the Utility entered into a Series 2008 Combined Utilities Revenue Bond Anticipation Note with Branch Banking and Trust Company for \$5,000,000. The bond anticipation note matures on June 15, 2011 at which time the principal is to be paid and the interest payments are to begin December 15, 2008 and are payable on each June 15 and December 15 to maturity at an interest rate of 3.19%. The note is issued in anticipation of the issuance of the City of Winchester, Kentucky’s Combined Utilities Revenue Bonds, Series 2008, for the purpose of providing interim financing of certain capital costs related to the City’s combined municipal waterworks, sanitary sewer and solid waste disposal system (the “System”).

**WINCHESTER MUNICIPAL UTILITIES
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEARS ENDED JUNE 30, 2009 AND 2008**

NOTE 5 – LONG-TERM DEBT (Continued)

2008 Bond Anticipation Note (continued)

Pledged against this note as the sources of payment of the principal of and the interest on the Note (a) the proceeds of the Bonds, when sold and issued, and (b) the income and revenues of the System, but on a basis subordinate and subject in all respects to the prior and superior pledges, liens, rights and contractual commitments securing the WMU's outstanding bonds and Kentucky Infrastructure Authority loan payable from the income and revenues of the System.

Capital Lease

On May 14, 2008, the Utility entered into a capital lease agreement with Océ Financial Services, Inc. for 2 copiers in the amount of \$18,169. Payments are for \$561 per month for 36 months at an interest rate of 7.00%. Following is a schedule of future minimum lease payments:

<u>Year</u>	<u>Amount</u>
2010	\$ 6,732
2011	6,732
2012	<u>561</u>
	<u>14,025</u>
Less amount representing interest	<u>(1,408)</u>
Total	<u>\$12,617</u>

The assets held under capital leases as of June 30, 2009 and 2008 are included in Equipment and total \$62,004 less accumulated depreciation of \$45,812 and \$39,118 as of the end of 2009 and 2008.

NOTE 6 – COMPLIANCE WITH BOND ORDINANCE

The 2003 bonds are on parity with the prior bonds and require WMU to establish and maintain certain reserves and restricted assets as follows:

Bond Debt Service

Monthly deposits equal to one-sixth of the next interest payment and one-twelfth of the next principal payment shall be set aside monthly so as to accumulate in the Bond Fund in order to pay interest and principal on the bonds. In addition, the Bond Ordinance requires that a specific amount be maintained in the Debt Service Reserve Account defined as the "Reserve Amount." The account is to be reviewed each year and funded based on the least of three factors: 1) maximum annual principal and interest requirement, 2) 125% of the average annual principal and interest requirement or 3) 10% of the outstanding loan proceeds. The third factor was applicable for June 30, 2009 and required a balance of \$968,222.

**WINCHESTER MUNICIPAL UTILITIES
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEARS ENDED JUNE 30, 2009 AND 2008**

NOTE 6 – COMPLIANCE WITH BOND ORDINANCE (continued)

Depreciation Reserve

The Winchester Municipal Utilities is required to transfer 12% of annual gross revenues or \$42,000, whichever is greater, in equal monthly installments to the Depreciation Fund. These funds are to be used for renewals, replacements and/or additions to property, plant and equipment.

Interest Coverage Ratio

The Winchester Municipal Utilities is required to maintain an interest coverage ratio of 1.4 times – annual debt service requirements. The City of Winchester is required by bond ordinance to adjust rates as necessary to maintain such minimum coverage.

Computed as follows:

	<u>2009</u>	<u>2008</u>
Net Income (Loss)		
Before Contributions	\$ (884,541)	\$ 937,711
Add:		
Depreciation	2,984,775	2,067,819
Interest Expense		
On Bonds	<u>678,345</u>	<u>505,998</u>
Income available for		
Debt Service	\$ <u>2,778,579</u>	\$ <u>3,511,528</u>
Maximum Debt Service		
On Bonds	<u>2,094,410</u>	<u>2,094,410</u>
Coverage Ratio	1.32	1.7

The Winchester Municipal Utilities is not in compliance with all of the covenants of this bond ordinance as of June 30, 2009; however, they were in compliance with the interest coverage ratio as of June 30, 2008.

NOTE 7 – CAPITALIZED INTEREST

WMU follows the policy of capitalizing interest as a component of construction in progress. For the years ended June 30, 2009 and 2008, total interest incurred was \$832,920 and \$680,619, respectively, of which \$159,500 and \$174,621 was capitalized and \$673,420 and \$505,998 was expensed, respectively.

**WINCHESTER MUNICIPAL UTILITIES
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEARS ENDED JUNE 30, 2009 AND 2008**

NOTE 8 – FIVE YEAR CAPITAL CONSTRUCTION PLAN

Winchester Municipal Utilities' five year capital plan includes major capital construction of new wastewater treatment plant, pump station and force mains which are projected to be funded as follows:

Water System Improvements	\$55,000,000
Wastewater System Improvements	37,000,000
Total projected financing requirement	\$92,000,000

Winchester Municipal Utilities' five year capital plan of depreciation funded projects consists of the following annual allocations in addition to other specifically identified projects:

Finance and Administration:	
Copiers	\$8,000
Upgrade local area network	2,500
Replace microcomputers	11,000
Engineering Software Upgrades	12,500
Field Operation vehicles	290,000
Solid Waste Collection:	
Curbit inventory	42,500
Container replacement	15,000
Replace compactor ejector box	12,000
Water Treatment Plant Equipment Improvements	100,000
Water Distribution:	
Main replacement	125,000
Meter Change-Out/AMR Equipment	145,000
Elevated tank rehabilitation	90,000
Meter change-out	50,000
Gate valve replacement	1,000
Gate valve grade adjustment	8,000
Fire hydrant replacement	15,000
Wastewater Collection:	
Manhole grade adjustment	125,000
Manhole Grade Adjustment – New Paving	25,000
I&I Rehabilitation	35,000
Rehabilitation of Private Sewers	35,000
Flow Meters	20,000
Infrastructure Rehabilitation Program	75,000
Wastewater Treatment Plant:	
Replacement of Laboratory Equipment	2,000
WWTP Equipment Improvements	15,000
Solids Processing Improvements	25,000
Total annual allocations for infrastructure investment	\$1,284,500

All annual allocation programs are funded in each year of the five year capital plan.

**WINCHESTER MUNICIPAL UTILITIES
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEARS ENDED JUNE 30, 2009 AND 2008**

NOTE 9 – PENSION FUND

The Winchester Municipal Utilities Commission adopted a resolution authorizing participation in the Kentucky Retirement Systems sponsored retirement program for County Employees Retirement System (CERS) effective July 1, 1998. The County Employees Retirement System (CERS) is a cost-sharing multiple-employer defined benefit pension plan administered by Kentucky Retirement Systems. CERS was established in 1958 under Kentucky Revised Statutes 78.510 to 78.852. The Plan provides retirement, disability, and death benefits to plan members and beneficiaries with annual cost-of-living adjustments. The retirement benefits are guaranteed by state law and cannot be reduced. By contributing to the retirement systems, the employee is assured a percentage of average salary for each year he is employed. The employee's contributions are currently tax-deferred. The Kentucky Retirement Systems issues a publicly available financial report that includes financial statements and required supplementary information for CERS. That report may be obtained by writing to Kentucky Retirement Systems, Perimeter Park West, 1260 Louisville Road, Frankfort, KY 40601.

Retirement benefits are provided for through legislative action of the Kentucky General Assembly and are funded by employee contributions which are deducted from employees' wages and by employer-paid contributions. The General Assembly sets the employee contribution rates, currently 5%, and the Retirement Systems' Board of Trustees sets the employer contribution rates, currently 16.17%. Each employer is notified prior to each fiscal year of any change in the contribution rates. The Retirement System's administrative expenses are subject to approval by the Kentucky General Assembly and are paid from the State's Retirement Allowance Account.

Employer contributions for the years ended June 30, 2009, 2008 and 2007, under the current plan amounted to \$389,350, \$422,012 and \$329,930, respectively which represents 100% of the required contributions. The previous plan's termination procedures and the subsequent distribution of excess assets were completed during the fiscal year ended June 30, 1999.

In a prior year, the WMU Commission agreed to pay \$381,296 in prior service costs. This cost will be expensed equally over 19 years, based upon the average remaining service lives of all involved employees. Prior service costs amounted to \$21,934 and \$21,934 for the years ended June 30, 2009 and 2008, respectively.

**WINCHESTER MUNICIPAL UTILITIES
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEARS ENDED JUNE 30, 2009 AND 2008**

NOTE 10 – CONTINGENCIES

- 1) On April 7, 2006, The United States of America and the Commonwealth of Kentucky filed suit, No. 06-102-KSF, in the United States District Court, Eastern District of Kentucky against Winchester Municipal Utilities. Shortly thereafter the City of Winchester, Kentucky became an unnamed party for the purposes of negotiation with the intention of later naming it as a party. A confidentiality agreement was entered in to by all parties including the City.

Essentially the action was an enforcement action seeking penalties and injunctive relief for violations of the Clean Water Act. The Complaint alleged that WMU, as a permitted owner of its wastewater treatment plant and system, has violated the Clean Water Act and as a result thereof is subject to injunctive relief to bring its facilities into compliance with the Act and to the penalties provided therein for past violations. The Complaint also alleged that WMU has failed to properly maintain and operate its facilities as required by its permit and has failed to properly monitor sanitary sewer discharges and prevent overflows.

After the filing of the Complaint, WMU staff and counsel along with City staff and counsel had a series of meetings with the EPA and State and negotiated regarding an agreement to settle the issues raised in the Complaint. The decree was approved by these two entities, the EPA and the Department of Justice was lodged with the Court in accordance with the Law for a period of public review. On April 6, 2007, the decree was signed by the Court and became final.

The settlement of the issues raised in the Complaint will have a substantial impact upon WMU and the City. The settlement requires WMU to take certain remedial measures to improve its system including the implementation of a Capacity Management Operations and Maintenance Program. These programs have several elements which are required to be implemented over a two year period. The cost of implementing these programs has been estimated to be \$935,000 over a two year period. In addition, the recurring capital cost over the 20 year life of the Decree is estimated to be \$1,334,000 and the annual Operations and Maintenance cost of the program is estimated to be \$385,000.

The Decree also requires the implementation of a System Capacity Assurance Program including the submission of a plan for the program within a two year period and full implementation of a program by January 31, 2010. The Capacity Assurance Program is to assure that future connections to WMU's system after the implementation of the program will not result in any further sanitary sewer overflows.

**WINCHESTER MUNICIPAL UTILITIES
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEARS ENDED JUNE 30, 2009 AND 2008**

NOTE 10 – CONTINGENCIES (continued)

The Decree also required WMU to undertake certain actions to bring its system into compliance with the Clean Water Act by ridding its system of Sanitary Sewer Overflows (SSO). WMU has started part of the goals of the Consent Decree which previously committed programs have an estimated cost of \$37,000,000 over the next four years to do improvements in the Lower Howard Creek watershed to eliminate the SSOs at the Stoneybrook and Snowfall pump stations. The Consent Decree also identifies other sanitary sewer overflows and capital projects to address same for the time period beginning January 31, 2010 and ending January 31, 2025, with an estimated capital cost of \$12,980,000.

The Consent Decree also provided for a civil monetary penalty of \$75,000, which has been paid. The Decree also requires WMU and the City to expend \$230,000 over the next five years on supplemental programs to improve water quality in Clark County, Kentucky. It also provided stipulated penalties in the event that the City and WMU fail to comply with the terms of the Decree or if there are no further SSOs after the work under the Decree is completed.

All in all, the total estimated financial impact to the city and WMU of the Consent Decree if implemented through 2027 will be \$64,222,836 exclusive of interest and outside funding, such as grants. The total estimated financial impact including interest at a present bond rate through 2027 is \$75,173,138. The bond payments would continue until the year 2040. The Capacity, Management, Operations and Maintenance Programs required by the proposed Decree will have an estimated ongoing escalating cost of at least \$570,000 annually.

The final judgment was entered into in April 2007 which will have a financial impact on the Utility for the next 25 years for curative work and potential fines and penalties, but there are no outstanding matters pending at this time.

- 2) Kentucky-American Water Company v. Natural Resources and Environmental Protection Cabinet (NREPC) and WMU. This is an administrative proceeding brought by Kentucky American against the NREPC as a result of its refusal to reissue the operating permit for the Rockwell Village treatment plant. WMU was added as a party, and Kentucky American claims that WMU is attaching unreasonable conditions in order for it to allow the connection. WMU has answered, stating its position that it will allow the connection to its system on the same terms and conditions that apply to all of its customers. The Cabinet issued a ruling on September 2, 1999, denying the requests of Kentucky American that it determine that WMU must make the connection, and that it determine the terms of the connection finding that it does not have the jurisdiction to make that

**WINCHESTER MUNICIPAL UTILITIES
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEARS ENDED JUNE 30, 2009 AND 2008**

NOTE 10 – CONTINGENCIES (continued)

determination. Kentucky American filed exceptions to the hearing officer's report, which were overruled. Kentucky American appealed the matter to the Franklin Circuit Court who referred the matter to mediation which was unsuccessful. The matter of connection only has been presented to the Franklin Circuit Court and an Order was entered directing Kentucky American to make the connection at its expense and WMU to allow the connection, but reserving the issue of payment to tap fees and SDC fees.

The connection was to be made in July 2002, but still has not been made due to design problems. WMU has approved the design plan of Kentucky American to connect, but the Plan has not been approved by the Division of Water and Kentucky American has not agree to pay its prorated share of the necessary line upgrade expense which has yet to be exactly determined. The Court also still needs to rule whether WMU can collect its tap on and SDC fees totaling \$175,000. As of this time the case is still pending and WMU will make every effort to collect all fees due when the connection is finally made to it's system.

NOTE 11 – COMMITMENTS

WMU has the following commitments which had not begun as of June 30, 2009:

<u>Project No.</u>	<u>Contractor</u>	<u>Amount</u>
2499	Conn Hurst LLC	\$ 177,034
2492	Frei Plumbing, Inc.	287,700
		<u>\$ 464,734</u>

NOTE 12 – RISK OF LOSS

WMU is exposed to various risks of loss related to torts; theft of, damage to and destruction of assets; errors and omissions; injuries to employees and natural disasters. WMU carries commercial insurance for the risks of loss, including worker's compensation, and property and casualty loss insurance.

NOTE 13 – ECONOMIC DEPENDENCY

WMU is economically dependent for revenues from the following four entities:

<u>Name</u>	<u>2009</u>	<u>2008</u>
Martek	\$ 223,753	\$ 260,449
Sekisui	333,063	386,080
Winchester Farms	310,863	457,314
East Clark County WD	319,234	281,997
	<u>\$ 1,186,913</u>	<u>\$ 1,385,840</u>

**WINCHESTER MUNICIPAL UTILITIES
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEARS ENDED JUNE 30, 2009 AND 2008**

NOTE 14 – LANDFILL POST-CLOSURE COSTS

In 1992, WMU discontinued its landfill operations and ceased accepting solid waste. Under 401 KAR 47:080, WMU presented a closure plan. The final cap, leachate collection systems, surface water drainage systems, gas vent systems and groundwater monitoring systems have been constructed. On June 4, 1998, the Clark County Fiscal Court entered into a lease agreement with WMU for the rental of county property upon which the County and WMU formerly operated landfills, the term of the lease was for 20 years at \$1 per year. The lease provides provision for the post-closure monitoring requirements of state and federal law to be provided by WMU. The post-closure costs are allocated 30% WMU and 70% Clark County Fiscal Court. The state and federal monitoring and maintenance regulations must be performed at the site for 30 years after closure. A liability was not recorded on WMU's general ledger in the year of closure, instead the actual post-closure expenses have been recorded in operations each year.

On October 16, 2008, WMU received notice from the Kentucky Division of Waste Management that the site had been released from groundwater monitoring. In applying GASB 18, WMU believes these costs were the most significant of the post-closure expenses. The effect of any remaining projected costs will be offset by the lease agreement with Clark County.

NOTE 15 – UTILITY REVENUES PLEDGED

WMU has pledged future revenues from water, wastewater and solid waste to repay the 2002, 2003 and KIA outstanding debt reference in Note 5. Proceeds from these debt obligations provided financing of the water and wastewater infrastructure, including a new wastewater treatment plant. The debt obligations will be repaid from the previously mentioned utility revenues through the year 2032. Principal and interest paid and total customer revenues for each year were as follows: 2009 year, \$2,069,716 and \$7,587,077 and 2008 year, \$3,815,618 and \$7,783,114, respectively.

NOTE 16 – SUBSEQUENT EVENTS

As required by SFAS No. 165, Subsequent Events, the School has reviewed events subsequent to the statement of financial position date of the accompanying financial statements through October 30, 2009 and determined that no events have occurred which would render the accompanying financial statements misleading.

**WINCHESTER MUNICIPAL UTILITIES
SCHEDULE 1 - DEPARTMENT EXPENSES (CONTINUED)
FOR THE YEARS ENDED JUNE 30, 2009 AND 2008**

	<u>2009</u>	<u>2008</u>
ADMINISTRATIVE		
Salaries	\$ 926,058	\$ 907,551
Employee Benefits	346,145	346,729
Repairs and Maintenance	47,671	48,889
Supplies	30,650	32,372
Small Tools	1,943	4,349
Utilities and Telephone	30,588	30,441
Property Insurance	46,609	60,678
Other	26,572	35,257
Postage and Freight	52,313	54,129
Bad Debts	15,000	15,000
Professional Fees	137,350	127,564
Depreciation	117,050	125,215
	<u>1,777,949</u>	<u>1,788,174</u>
 SOLID WASTE		
Salaries	468,777	519,100
Employee Benefits	293,208	286,115
Repairs and Maintenance	327,749	315,842
Supplies	14,059	16,926
Small Tools	4,374	4,168
Utilities and Telephone	14,027	14,469
Property Insurance	74,570	83,874
Other	28,592	44,137
Postage	-	31
Depreciation	190,618	248,346
Landfill Charges	218,160	215,264
	<u>1,634,134</u>	<u>1,748,272</u>
 WATER		
Salaries	556,695	579,640
Employee Benefits	263,547	268,193
Repairs and Maintenance	169,734	162,804
Supplies	327,028	275,333
Small Tools	8,163	6,697
Utilities and Telephone	403,203	356,108
Property Insurance	74,523	75,099
Other	33,251	41,798
Postage	408	194
Professional Fees	1,005	6,676
Depreciation	776,619	771,151
New Services	8,463	16,513
Meter Replacements	-	1,023
	<u>2,622,639</u>	<u>2,561,229</u>
	\$	\$

**WINCHESTER MUNICIPAL UTILITIES
SCHEDULE 1 - DEPARTMENT EXPENSES (CONTINUED)
FOR THE YEARS ENDED JUNE 30, 2009 AND 2008**

	<u>2009</u>	<u>2008</u>
WASTEWATER		
Salaries	\$ 578,835	\$ 512,302
Employee Benefits	311,365	247,809
Repairs and Maintenance	225,415	288,102
Supplies	300,527	280,620
Small Tools	8,595	13,889
Utilities and Telephone	602,051	473,632
Property Insurance	133,759	88,985
Other	49,786	25,778
Postage	269	330
Professional Fees	157,190	104,363
Depreciation	1,878,519	902,387
New Services	172	-
	<u>4,246,483</u>	<u>2,938,197</u>
 VEHICLE MAINTENANCE		
Salaries	9,532	16,884
Employee Benefits	45,834	43,003
Repairs and Maintenance	5,468	2,764
Supplies	3,107	3,585
Small Tools	1,642	622
Utilities and Telephone	21,891	16,505
Property Insurance	14,318	17,520
Other	403	997
Depreciation	21,968	20,720
	<u>124,163</u>	<u>122,600</u>
 TOTAL OPERATING EXPENSES	 <u>\$ 10,405,368</u>	 <u>\$ 9,158,472</u>

**WINCHESTER MUNICIPAL UTILITIES
SCHEDULE II - REVENUE BOND DEBT SERVICES
FOR THE YEAR ENDED JUNE 30, 2009**

Maturity Date	2003 Issue		2002 Issue		Total	
	Principal	Interest	Principal	Interest	Principal	Interest
2010-2011	\$ 1,470,000	\$ 18,375	\$ 195,000	\$ 388,273	\$ 1,665,000	\$ 406,648
2011-2012	-	-	200,000	379,385	200,000	379,385
2012-2013	-	-	210,000	370,160	210,000	370,160
2013-2014	-	-	220,000	360,485	220,000	360,485
2014-2015	-	-	230,000	350,245	230,000	350,245
2015-2016	-	-	240,000	339,315	240,000	339,315
2016-2017	-	-	255,000	327,619	255,000	327,619
2017-2018	-	-	265,000	315,269	265,000	315,269
2018-2019	-	-	280,000	302,325	280,000	302,325
2019-2020	-	-	290,000	288,425	290,000	288,425
2020-2021	-	-	305,000	273,550	305,000	273,550
2021-2022	-	-	325,000	257,800	325,000	257,800
2022-2023	-	-	340,000	241,175	340,000	241,175
2023-2024	-	-	355,000	223,578	355,000	223,578
2024-2025	-	-	375,000	204,872	375,000	204,872
2025-2026	-	-	395,000	185,141	395,000	185,141
2026-2027	-	-	415,000	164,384	415,000	164,384
2027-2028	-	-	440,000	142,475	440,000	142,475
2028-2029	-	-	460,000	119,413	460,000	119,413
2029-2030	-	-	485,000	95,197	485,000	95,197
2030-2031	-	-	510,000	69,700	510,000	69,700
2031-2032	-	-	540,000	42,794	540,000	42,794
2032-2033	-	-	565,000	14,474	565,000	14,474
	<u>\$ 1,470,000</u>	<u>\$ 18,375</u>	<u>\$ 7,895,000</u>	<u>\$ 5,456,054</u>	<u>\$ 9,365,000</u>	<u>\$ 5,474,429</u>

**WINCHESTER MUNICIPAL UTILITIES
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED JUNE 30, 2009**

<u>Federal Grantor/Pass Through Grantor/Program Title</u>	<u>Federal CFDA Number</u>	<u>Pass-Through Entity Identifying Number</u>	<u>Federal Expenditures</u>
<u>U.S. Environmental Protection Agency</u>			
Passed through state:			
Federal revolving funds	66.458	A05-02	1,612,393
Total Federal Awards			\$ <u>1,612,393</u>

The above schedule of expenditures of federal awards includes the federal grant activity of WMU and is presented on the accrual basis of accounting. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, Audits of States, Local Governments, and Non-Profit Organization.

SUMMERS, MCCRARY & SPARKS, P.S.C.
CERTIFIED PUBLIC ACCOUNTANTS

MEMBERS:

AMERICAN INSTITUTE
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KENTUCKY SOCIETY
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**REPORT 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***

To the Commissioners
Winchester Municipal Utilities
Winchester, KY

We have audited the financial statements of Winchester Municipal Utilities as of and for the year ended June 30, 2009, which comprise the Winchester Municipal Utilities', a component unit of the City of Winchester, Kentucky, basic financial statements and have issued our report thereon dated October 30, 2009. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered Winchester Municipal Utilities', a component unit of the City of Winchester, Kentucky, internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Winchester Municipal Utilities', a component unit of the City of Winchester, Kentucky, internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Winchester Municipal Utilities', a component unit of the City of Winchester, Kentucky, internal control over financial reporting.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the Winchester Municipal Utilities', a component unit of the City of Winchester, Kentucky, ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the Winchester Municipal Utilities', a component unit of

the City of Winchester, Kentucky, financial statements that is more than inconsequential will not be prevented or detected by the Winchester Municipal Utilities', a component unit of the City of Winchester, Kentucky, internal control.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the Winchester Municipal Utilities', a component unit of the City of Winchester, Kentucky, internal control.

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

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Winchester Municipal Utilities', a component unit of the City of Winchester, Kentucky, financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

We noted certain matters that we reported to management of Winchester Municipal Utilities in a separate letter dated October 30, 2009.

This report is intended solely for the information and use of the Commissioners, management, others within the organization, federal awarding agencies and pass through entities and is not intended to be and should not be used by anyone other than these specified parties.

Summers, McCrary & Sparks, PSC

Summers, McCrary & Sparks, PSC
Winchester, Kentucky
October 30, 2009

SUMMERS, MCCRARY & SPARKS, P.S.C.
CERTIFIED PUBLIC ACCOUNTANTS

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

To the Commissioners
Winchester Municipal Utilities
Winchester, Kentucky

Compliance

We have audited the compliance of the Winchester Municipal Utilities, a component unit of the City of Winchester, Kentucky, with the types of compliance requirements described in the U. S. Office of Management and Budget (OMB) Circular A-133 *Compliance Supplement* that are applicable to each of its major federal programs for the year ended June 30, 2009. Winchester Municipal Utilities', a component unit of the City of Winchester, Kentucky, major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs is the responsibility of Winchester Municipal Utilities', a component unit of the City of Winchester, Kentucky, management. Our responsibility is to express an opinion on Winchester Municipal Utilities', a component unit of the City of Winchester, Kentucky, compliance based on our audit.

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

In our opinion, Winchester Municipal Utilities, a component unit of the City of Winchester, Kentucky, complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended June 30, 2009.

Internal Control Over Compliance

The management of Winchester Municipal Utilities, a component unit of the City of Winchester, Kentucky, is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered Winchester Municipal Utilities', a component unit of the City of Winchester, Kentucky, internal control over compliance with the requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of Winchester Municipal Utilities', a component unit of the City of Winchester, Kentucky, internal control over compliance.

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

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

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

This report is intended solely for the information and use of management, Commissioners, others within the entity, federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Summers, McCrary & Sparks, PSC
Winchester, Kentucky
October 30, 2009

WINCHESTER MUNICIPAL UTILITIES
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
JUNE 30, 2009

Section I - Summary of Auditor's Results

1. The auditor's report expresses an unqualified opinion on the financial statements of Winchester Municipal Utilities, a component unit of the City of Winchester, Kentucky.
2. No significant deficiencies were disclosed during the audit of the financial statements.
3. No instances of noncompliance material to the financial statements of Winchester Municipal Utilities, a component unit of the City of Winchester, Kentucky, were disclosed during the audit.
4. No significant deficiencies were reported in the Report on Compliance with Requirements Applicable to Each Major Program and Internal Controls Over Compliance in Accordance with OMB Circular A-133.
5. The auditor's report on compliance for the major federal awards programs for Winchester Municipal Utilities, a component unit of the City of Winchester, Kentucky, expresses an unqualified opinion.
6. No audit findings that are required to be reported in accordance with Section 510(a) of OMB Circular A-133 are reported in this Schedule.
7. The programs tested as major programs includes: EPA Federal Revolving Funds CFDA #66.458.
8. The threshold for distinguishing Types A and B programs was \$300,000.
9. Winchester Municipal Utilities, a component unit of the City of Winchester, Kentucky, was determined to be a low-risk auditee.

Section II – Financial Statement Findings

No Findings

Section III – Federal Award Findings and Questioned Costs

No Findings