

BEFORE THE PUBLIC SERVICE COMMISSION
COMMONWEALTH OF KENTUCKY

RECEIVED

JAN 24 2008

PUBLIC SERVICE
COMMISSION

In the Matter of:

THE APPLICATION OF AUXIER WATER)	
CO., FLOYD COUNTY, KENTUCKY FOR)	
AUTHORIZATION OF ITS PROPOSED SALE)	CASE NO.
AND CONVEYANCE OF ALL OF ITS WATER)	2007-00488
DISTRIBUTION SYSTEM AND CUSTOMER)	
DEPOSITS TO THE CITY OF PRESTONSBURG,)	
KENTUCKY)	

**APPLICANTS' RESPONSES TO COMMISSION STAFF'S
FIRST DATA REQUEST**

****CERTIFICATION****

The undersigned, David M. Ellis, being first duly sworn, state that he is the Superintendent of Prestonsburg City's Utilities Commission (herein after "Prestonsburg"), and certifies that he supervised the preparation of the following responses to First Data Request of the Commission Staff and that they are true and accurate to the best of his knowledge, information and belief formed after a reasonable inquiry.



David M. Ellis, Superintendent

Subscribed and sworn to before me, this 22nd day of January, 2008


Notary Public

My Commission expires on: 9/26/09

**PRESTONSBURG'S RESPONSES TO COMMISSION STAFF'S FIRST DATA
REQUEST**

Comes Prestonsburg, by counsel, and for its Response to the Commission Staff's First Data Request in the above-captioned matter, states:

1. For its water distribution system and customer deposits, Auxier will receive \$2,650,000 and other valuable consideration, including commitments of Prestonsburg respecting water service in Auxier's service territory.¹

a. Explain the term "other valuable consideration."

RESPONSE: Prestonsburg will supply potable water directly to Auxier's customers. Prestonsburg will charge Auxier's customers for water delivered at the same rates that Auxier had been charging (Auxier's latest approved tariff) until: 1) the Acquisition Debt is satisfied per Contract; 2) Prestonsburg outside City rates are higher; or 3) until the customer's property is annexed by the City. In addition, Prestonsburg will provide operations and maintenance services for the distribution system previously owned and operated by Auxier.

WITNESS: David M. Ellis

b. Describe the water service commitments that Auxier will receive.

RESPONSE: Pursuant to Commission approved wholesale contract between Prestonsburg and Auxier, Auxier has provided potable water to its customers. Prestonsburg will continue to deliver potable water through existing customer meters, and provide operations and maintenance services for existing facilities.

WITNESS: David M. Ellis

2. KRS 278.020(6) provides that the Commission must find that the proposed transaction "[i]s to be made in accordance with law, for a proper purpose and is consistent with the public interest." Explain how the proposed transaction benefits the public.

RESPONSE: Prestonsburg is a municipally owned utility system that is operated to provide low-cost utility services to its citizens and customers of surrounding environs. Prestonsburg operates a potable water treatment plant and distribution system. Prestonsburg will integrate Auxier's distribution facilities into its distribution system.

Previously, Auxier has received a deviation from satisfying the Commission's storage requirements. Prestonsburg has established substantial storage facilities that can serve Auxier.

Prestonsburg has previously constructed a water main through the territory served by Auxier to serve customers in Martin County, Kentucky. Auxier has established numerous taps for both commercial and residential customers on this

¹ Application at 2.

water main. Prestonsburg believes that it can sustain customer service and security over its distribution system by the support of the entire management and work force of the utilities system.

The Auxier distribution system is geographically divided into two systems by the Levisa Fork of the Big Sandy River. On the west side is the mining camp known as "Old Auxier". The water distribution system was laid in Old Auxier in excess of fifty (50) years ago and is in need of replacement. Prestonsburg intends to upgrade the portion of the distribution system in Old Auxier serving approximately 800 customers at a total projected cost of \$464,000.00, using the latest technology available. Prestonsburg intends to use Ductile Iron Pipe. See Exhibit "A" attached hereto for an estimated cost prepared by Kenvirons, Inc.

By Order dated May 29, 2007 in Case No. 2007-00095, the Commission approved Prestonsburg's proposed increase in water rates to its wholesale customers, including Auxier. Auxier has not filed for a purchased water adjustment due to the increased cost of its water supply in anticipation of the sale and transfer of its system to Prestonsburg. Consequently, the customers of Auxier will not have an increase in their water rates that otherwise would be implemented pursuant to a water purchase adjustment.

Effective December 11, 1967, Prestonsburg became the sole supplier of potable water to Auxier, and has continued to do so without interruption until the present time. The latest extension of the water purchase contract with Auxier will expire on February 11, 2008, and Prestonsburg has previously given Auxier a notice of termination in anticipation of negotiating a new water supply contract. Auxier will avoid the expenses associated with a full rate proceeding before the Commission. The avoidance of the costs that would necessarily be recovered from Auxier's and Prestonsburg's customers benefits the public.

Prestonsburg has obtained a favorable commitment from the Kentucky Infrastructure Authority ("KIA") at the favorable rate of seven-tenth of one percent (.7%). Please see Exhibit "B" attached hereto for a loan commitment from KIA. The favorable terms of the financing benefits the public.

The transfer of the distribution system of Auxier to Prestonsburg accomplishes a legislative mandate given to the KIA, which "...encourages the regionalization, merger, and consolidation of water systems and elimination of structural and administrative duplication." See KRS 224.310. KIA has an incentive program to facilitate regionalization. Prestonsburg has received the KIA loan commitment pursuant to this incentive program.

Prestonsburg has long-term plans to construct a new water treatment plant near Old Auxier, and the transfer and control of the customer load served by Auxier is a critical component of evaluating the need for a new water treatment

plant. Clearly, a modern water treatment plant to serve the customers is a benefit to the public.

WITNESS: David M. Ellis

3. According to the Acquisition Contract dated September 24, 2007, Auxier will “deliver to the City and its Utilities Commission (a) all sums of money which it then holds, representing deposits made by Auxier’s water users as security for the payment of water bills.”²

a. Identify the amount of the customer deposit liability that Auxier has outstanding as of December 31, 2007, that will be transferred to Prestonsburg.

RESPONSE: Please see Auxier’s separate response.

WITNESS:

b. Identify any of Auxier’s outstanding customer deposit liabilities that will be refunded to customers prior to the proposed transfer.

RESPONSE: Please see Auxier’s separate response.

WITNESS:

4. Commission regulations require that interest be paid on customer deposits annually. Auxier’s annual report to the Commission for the Calendar Year Ending December 31, 2006 indicates that Auxier did not accrue interest on its customer deposits. Provide the amount of accrued interest on customer deposits Auxier owes as of December 31, 2007.

RESPONSE: Please see Auxier’s separate response.

WITNESS:

5. The Acquisition Contract states that the future accrual of interest on Auxier’s customer deposits will conform to, “[w]hatever policies and practices the City has established.”³

a. Describe the policies and practices Prestonsburg has regarding the accrual and payment of interest on customer deposits.

RESPONSE: Prestonsburg does not pay interest on deposits.

² Acquisition Contract at 6.

³ Id.

WITNESS: David M. Ellis

b. Describe the differences between Prestonsburg's policies regarding interest on customer deposits with the requirements contained in the Commission regulations.

RESPONSE: Prestonsburg does not pay interest on deposits.

WITNESS: David M. Ellis

6. Provide the proposed journal entry that Auxier will use to record the transfer.

RESPONSE: Please see Auxier's separate response.

WITNESS:

7. Provide the proposed journal entry that Prestonsburg will use to record the transfer.

**RESPONSE: 1) Cash – PCUC Operating x,xxx,xxx.xx
Note/Bond Payable**

(To record the funding liability)

**2) Water Plant/Lines – Auxier x,xxx,xxx.xx
Cash – PCUC Operating x,xxx,xxx.xx**

(To record the asset transfer)

WITNESS: Turner E Campbell

8. Exhibit B of the Application is the Report on Audit of Financial Statement for the years ended June 30, 2006 and 2005 for the Prestonsburg City Utilities Commission. Provide a copy of the Water Division's balance sheet, income statement, and statement of retained earnings for the 12-month period ending December 31, 2007.

RESPONSE: Prestonsburg's balance sheet accounts are not set-up by utility service (i.e. water, sewer, natural gas). Prestonsburg, as required by state law, is on a fiscal year that ends June 30th. Prestonsburg believes that a more appropriate reflection of its financial picture is its most recent audit report for the year ending June 30, 2007. See attached Exhibit "C".

WITNESS: Turner E Campbell

9. Provide a copy of Auxier's balance sheet, income statement, and statement of retained earnings for the 12-month period ending December 31, 2007.

RESPONSE: Please see Auxier's separate response.

WITNESS:

10. Identify the Prestonsburg employees who will manage and operate Auxier's water system and describe each person's qualifications to operate and manage a water distribution system.

RESPONSE: Prestonsburg presently employs nine (9) class IID (3-D) certified distribution system operators. All operators share responsibilities throughout our entire distribution system. The operator certification numbers are as follows:

**David M. Ellis.....2916
Brian Music.....3163
William Campbell.....2021
Donald Compton.....2498
Turner E. Campbell.....16401
Rickey E. Lemaster.....3591
David S. Meade.....17031
Jeff Holbrook.....17085
Timothy A. Goble.....17280**

The contacts for distribution operations are as follows:

**David M. Ellis – Superintendent
Brian Music – Water Quality / Distribution System Supervisor
Tony Hall – Field System Supervisor
Michael Campbell – Administrative Specialist
Rickey L. Lemaster – Field Foreman
David S. Meade – Field Foreman
All contacts can be reached at (606) 886-6871 or (606) 886-2900**

WITNESS: David M. Ellis

11. a. Describe the internal standards and policies of Prestonsburg regarding service reliability and quality of its water utility operations.

RESPONSE: Prestonsburg presently operates its accounting system following AICPA standards. Prestonsburg complies with all Federal and State standards set forth by the Environmental and Public Protection Cabinet.

PRESTONSBURG CITY'S UTILITIES COMMISSION MISSION STATEMENT

To provide the highest quality of utility services to the community, while enhancing the quality of life and economic environment, and promoting the restoration of our natural resources for the area as a whole.

Prestonsburg does not have internal policies related to service quality and reliability of water utility operations. However, Prestonsburg follows the Division of Water's detailed regulations regarding water treatment and operation of facilities as required by 401 KAR Chapter 8 and 902 KAR Chapter 115, and applicable state statutes.

WITNESS: David M. Ellis

- b. Provide all written standards or policies related to service quality and reliability of water utility operations.

RESPONSE: N/A

WITNESS: David M. Ellis

- 12. Provide in table format an analysis of the number and type of consumer complaints that Prestonsburg received during the period from 2000 to 2005 and of how such complaints were resolved.

RESPONSE: All customer concerns are addressed as a work order issued by clerical employees of Prestonsburg. Work orders are then distributed to the appropriate department for immediate response. The work orders are then returned upon completion. Prestonsburg Utilities strives to address each customer concern as expediently as possible. Each concern is given attention to the extent of the policies and procedures adopted by the Utilities Commission.

WITNESS:

- 13. a. List all of Auxier's current employees.

RESPONSE: Please see Auxier's separate response.

WITNESS:

b. Identify each Auxier employee that Prestonsburg will not retain after the acquisition is completed, explain why he or she will not be retained, and describe the severance package, if any, that he or she will receive.

RESPONSE: Prestonsburg has recently employed a field representative of Auxier Water Company. This representative is a full-time employee of Prestonsburg at this time. No other employees will be retained by Prestonsburg.

WITNESS: David M. Ellis

c. Provide the job duties and salary of each Auxier employee to be hired by Prestonsburg.

RESPONSE: N/A

WITNESS: David M. Ellis

d. Will the hiring of any Auxier employee fill a current vacancy at Prestonsburg? If yes, state the current vacant position and how long that position has been vacant.

RESPONSE: No vacancies presently exist at Prestonsburg.

WITNESS: David M. Ellis

e. Who will supervise the Auxier employees hired by Prestonsburg?

RESPONSE: N/A

WITNESS: David M. Ellis

Respectfully submitted,



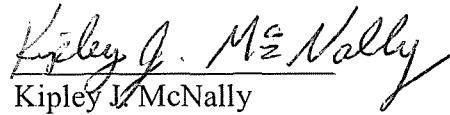
Kipley J. McNally, Esq.
Kipley J. McNally, PLC
2527 Nelson Miller Parkway, Ste. 104
Louisville, Kentucky 40223
Telephone: (502) 245-6133
Fax: (502) 245-1974

Counsel for Prestonsburg City's
Utilities Commission

Date submitted: January ^{13th} 2008

CERTIFICATE OF SERVICE

I hereby certify that the foregoing has been served by electronic mail without exhibits on Bruce F. Clark, Esq., Stites & Harbison, PLLC, 421 West Main Street, Frankfort, Kentucky 40601, on the 23rd day of January, 2008, and with exhibits via hand delivery on the 24th day of January, 2008.


Kipley J. McNally

INDEX TO EXHIBITS
PRESTONSBURG CITY'S UTILITIES COMMISSION

- A. Cost Estimate Prepared by Kenvirons, Inc.
- B. Loan Commitment from Kentucky Infrastructure Authority
- C. Audit Report for the fiscal year ending June 30, 2007



Kenvirons, Inc.

452 Versailles Road • Frankfort, KY 40601 • Phone: (502) 695-4357 • Fax: (502) 695-4363
Civil & Environmental Engineering and Laboratory Services

January 18, 2008

Mr David M. Ellis, Superintendent
Prestonsburg City's Utilities Commission
2560 South Lake Drive
Prestonsburg, Kentucky 41653

RE: Auxier Water System

Dear Dave:

In response to your request, the estimated cost of the proposed upgrades to the above referenced system is as follows:

5,200 LF 6-In Ductile Iron Pipe @ \$20 00/LF	\$	104,000
800 EA Replacement Residential Meter Services @ \$450 00/EA	\$	360,000

Please contact me should you have any questions.

Sincerely,

Douglas C. Griffin, P.E.
Vice President

DCCG/cag

December 13, 2007

Mr. Jimmy Calhoun, Chairman
Prestonsburg City's Utilities Commission
2560 South Lake Drive
Prestonsburg, Kentucky 41653

**KENTUCKY INFRASTRUCTURE AUTHORITY
INFRASTRUCTURE REVOLVING LOAN FUND
CONDITIONAL LOAN COMMITMENT B07-10**

Dear Mr. Calhoun:

The Kentucky Infrastructure Authority (the "Authority") commends your efforts to improve public service facilities in your community. On December 6, 2007 the Authority approved your loan for a water system acquisition subject to the conditions stated below. The total cost of the project shall not exceed \$2,700,000 of which the Authority loan shall provide up to \$2,700,000. Other anticipated funding for the project is reflected in Attachment A. The final loan amount will be equal to the Authority's portion of estimated project amount applied to the actual project cost. Attachment A incorporated herein by reference fully describes the project.

An assistance agreement will be executed between the Authority and the Prestonsburg City's Utilities Commission upon satisfactory performance of the conditions set forth in this letter. A period of twelve months from the date of this letter December 13, 2007 will be allowed for you to meet the conditions set forth in this letter and enter into an assistance agreement. A one-time extension up to six months may be granted for applicants that experience extenuating circumstances. Funds will be available for disbursement only after execution of the assistance agreement.

The assistance agreement and this commitment shall be subject, but not limited to the following terms:

1. The Authority project loan shall not exceed \$2,700,000.

2. The loan shall bear interest at the rate of 0.7% per annum commencing with the first draw of funds.
3. The loan shall be repaid over a period of twenty (20) years from the date of project completion.
4. Interest shall be payable on the amount of actual funds received. The first payment shall be due on June 1 or December 1 immediately succeeding the date of the initial draw of funds, provided that if such June 1 or December 1 shall be less than three months since the date of the initial draw of funds, then the first interest payment date shall be the June 1 or December 1 which is at least six months from the date of the initial draw of funds. Interest payments will be due each six months thereafter until the loan is repaid.
5. Full principal payments will commence on June 1 or December 1 immediately succeeding the date of the last draw of funds, provided that if such June 1 or December 1 shall be less than three months since the date of the last draw of funds, then the first principal payment date shall be the June 1 or December 1 which is at least six months from the date of the last draw of funds. Full payments will be due each six months thereafter until the loan is repaid.
6. A loan servicing fee of two-tenths of one percent of the annual outstanding loan balance shall be payable to the Authority as a part of each interest payment.
7. Loan funds will be disbursed after execution of the assistance agreement as project costs are incurred.
8. The final assistance agreement must be approved by ordinance or resolution, as applicable, of the city council or appropriate governing board.

The following is a list of the standard conditions to be satisfied prior to execution of the assistance agreement or incorporated in the assistance agreement. Any required documentation shall be provided directly to the Authority.

1. Upon completion of final design of the facilities in the attached project description, favorable approval shall be obtained of such design by all appropriate parties as required by Kentucky statute or administrative regulation.
2. Applicant must provide certification from their legal counsel stating that they have prepared construction specifications in accordance with all applicable

state or federal wage rate laws, and that the procurement procedures, including those for construction, land, equipment and professional services that are a part of the project, are in compliance with applicable federal, state and local procurement laws.

3. Documentation of final funding commitments from all parties other than the Authority as reflected in the Attachment A description shall be provided to the Authority prior to the pre-closing of the Authority loan and disbursement of the loan moneys. Rejections of any anticipated project funding or any new sources of funding not reflected in Attachment A shall be immediately reported to the Authority and cause this loan to be subject to further consideration.
4. Upon receipt of construction bids a tabulation of such bids and engineer's recommendations on compliance with bid specifications and recommendation for award, shall be forwarded to the Authority for final approval and sizing of this loan and the project.
5. Based on the final "as bid" project budget, the community must provide satisfactory proof, based on then existing conditions, that the revenue projections in the attached descriptions are still obtainable and that projections of operating expenses have not materially changed. This shall be reviewed and approved by your consultant engineer.
6. Any required adjustment in utility service rates shall be adopted by ordinance, municipal order or resolution by the city council or appropriate governing board. Public hearings as required by law shall be held prior to the adoption of the service rate ordinance or resolution. Any required approvals by the Kentucky Public Service Commission shall be obtained.
7. All easements or purchases of land shall be completed prior to commencement of construction. Certification of said acquisitions shall be provided to the Authority.
8. The loan must undergo review by the Capital Projects and Bond Oversight Committee of the Kentucky Legislature prior to the state's execution of the Assistance Agreement. The committee meets monthly on the third Tuesday. At this time we know of no further submission required for their review; however, they may request information as needed.
9. Documentation of Clearinghouse Endorsement and Clearinghouse Comments.

Mr. Jimmy Calhoun
December 13, 2007
Page 4

10. Complete and return to the Authority the attached "Authorization For Electronic Deposit of Vendor Payment" Form.
11. Implement the Kentucky Uniform System of Accounting (KUSoA), or an alternative approved by the Authority and assure that rates and charges for service are based upon the cost of providing such service.
12. Final Design Plans in an AutoCAD Drawing File Format (DWG), referenced to the appropriate (North, South or Single) Kentucky State Plane Coordinate System (NAD83-Survey Feet) on a Compact Disc (CD). If there is a significant deviation from the Final Design Plan during construction, As-built plans shall also be provided to the Authority in the same format.

Please inform the Authority of any changes in your financing plan as soon as possible. We will assist you in a final evaluation of the financing plan when construction bids are available. We wish you every success for this project which will benefit both your community and the Commonwealth as a whole.

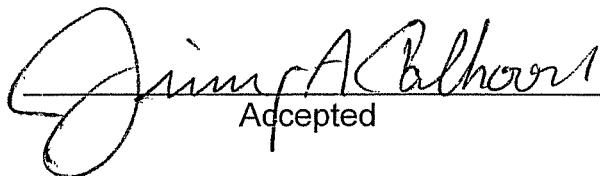
Sincerely,


John E. Covington, III
Financial Analyst

Attachment

c: Mr. Andrew Dorton, Public Finance Group, LLC
Mr. David Ellis, Prestonsburg City's Utilities Commission
Mr. Dirk Bedarff, Peck Shaffer & Williams, LLP
Mr. Dan Waits, State Local Debt Officer, GOLD

Please sign and return a copy of this letter indicating your acceptance of this commitment and its terms.


Accepted


Date

ATTACHMENT A

Michael R. Spears, CPA, PSC

Certified Public Accountant

PRESTONSBURG CITY UTILITIES COMMISSION

**REPORT ON AUDIT OF FINANCIAL STATEMENTS
for the years ended June 30, 2007 & 2006**

CONTENTS

Independent Auditor's Report	1-2
Management Discussion And Analysis	3-6
Basic Financial Statements	
Statements Of Net Assets	7-8
Statements Of Revenues, Expenses And Changes In Net Assets	9-10
Statements Of Cash Flows	11-12
Notes To Basic Financial Statements	13-22
Required Supplementary Information	
Budgetary Comparison Schedule	23-24
Report On Internal Control Over Financial Reporting and on Compliance and Other Matters Based On An Audit Of Financial Statements Performed In Accordance With <i>Government Auditing Standards</i>	25-26
Schedule Of Expenditures Of Federal Awards	27
Notes To Schedule Of Expenditures Of Federal Awards	28
Report On Compliance With Requirements Applicable To Each Major Program And On Internal Control Over Compliance In Accordance With OMB Circular A-133	29-30
Schedule Of Findings And Questioned Costs	31
Other Supplementary Information	
Comparative Analysis Of Revenues And Expenses	32
Schedule Of Plant, Equipment And Depreciation	33

Michael R. Spears, C.P.A., P.S.C.

Certified Public Accountant

Independent Auditor's Report

To the Board of Commissioners
Prestonsburg City's Utilities Commissions
Prestonsburg, Kentucky

We have audited the accompanying financial statements of the business-type activities of Prestonsburg City's Utilities Commission, component unit of the City of Prestonsburg, Kentucky, as of and for the years ended June 30, 2007 and June 30, 2006, which collectively comprise the Prestonsburg City's Utilities Commission's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the Prestonsburg City's Utilities Commission's 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 audit provides a reasonable basis for our opinion.


As discussed in Note A, the financial statements present only the activities of the Prestonsburg City's Utilities Commission, and are not intended to present fairly the financial position and result of operations of the City of Prestonsburg, Kentucky, and the results of its operations and its cash flows of its proprietary fund types in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the business-type activities of Prestonsburg City's Utilities Commission of the City of Prestonsburg as of June 30, 2007 and June 30, 2006, and the respective changes in financial position, and, where applicable, cash flows thereof for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated January 15, 2008, on our consideration of Prestonsburg City's Utilities Commission's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. 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 and budgetary comparison information on pages 3 through 6 and pages 22 and 23, are not a required part of the basic financial statements but are 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 methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audits were conducted for the purpose of forming opinions on the financial statements that collectively comprise the Prestonsburg City's Utilities Commission's basic financial statements. The introductory section and accompanying supplementary financial information as listed in the table of contents, are presented for purposes of additional analysis and are not a required part of the basic financial statements. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is also not a required part of the basic financial statements of the Prestonsburg City's Utilities Commission. The schedule of expenditures of federal awards has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the financial statements taken as a whole. The introductory section and accompanying supplementary financial information as listed in the table of contents, have not been subjected to the auditing procedures applied to the audit of the basic financial statements and, accordingly, we express no opinion on them.


Michael R. Spears, CPA, PSC
January 15, 2008

MANAGEMENT DISCUSSION AND ANALYSIS

Our discussion and analysis of the Prestonsburg City's Utilities Commission's financial performance provides an overview of the Commission's financial activities for the year ended June 30, 2007. Please read it in conjunction with the Commission's financial statements, which begin on page 10.

USING THIS ANNUAL REPORT

This annual report consists of a series of financial statements. The Statements of Net Assets and the Statements of Revenues, Expenses and Changes in Net Assets (pages 7-10) report the Commission's operations in detail. The Commission is a component unit of the City of Prestonsburg and presents only fund financial statements.

Reporting the Commission as a Whole

The Statement of Net Assets and the Statement of Revenues, Expenses and Changes in Net Assets

Our analysis of the Commission as a whole begins on page 4. One of the most important questions asked about the Commission's finances is, "Is the Commission as a whole better off or worse off as a result of the year's activities?" The Statement of Net Assets and the Statement of Revenues, Expenses, and Changes in Net Assets report information about the Commission as a whole and about its activities in a way that helps answer this question. These statements include all assets and liabilities using the accrual basis of accounting, which is similar to the accounting used by most private-sector companies. All of the current year's revenues and expenses are taken into account regardless of when cash is received or paid.

These two statements report the Commission's net assets and changes in them. You can think of the Commission's net assets—the difference between assets and liabilities—as one way to measure the Commission's financial health, or financial position. Over time, increases or decreases in the City's net assets are one indicator of whether its financial health is improving or deteriorating. You will need to consider other non-financial factors, however, such as changes in the Commission's service area and condition of existing water, sewer, and gas lines, to assess the overall health of the Commission.

In the Statement of Net Assets and the Statement of Revenues, Expenses and Changes in Net Assets, the Commission reports only one type of activity:

- Business-type activity—The Commission charges a fee to customers to help it cover all or most of the cost of certain services it provides. The City of Prestonsburg's water, sewer, and natural gas systems are reported here.

Reporting the Commission's Most Significant Funds

Fund Financial Statements

The fund financial statements begin on page 7 and provide detailed information about the fund. The Commission has only one fund type:

- Proprietary funds—When the Commission charges customers for the services it provides these services are generally reported in proprietary funds. Proprietary funds are reported in the same way that all activities are reported in the Statement of Net Assets and the Statement of Revenues, Expenses, and Changes in Net Assets.

PRESTONSBURG CITY'S UTILITIES COMMISSION
 MANAGEMENT'S DISCUSSION AND ANALYSIS
 FOR THE YEAR ENDED JUNE 30, 2007

The Commission As A Whole

The Commission's net assets changed slightly from a year ago, increasing from 19.7 million to 20.3 million. For the years ending June 30, 2007 and June 30, 2006, net assets changed as follows:

	Business-type Activities	
	<u>2007</u>	<u>2006</u>
Beginning net assets	\$ 19.7	\$ 20.7
Increase (decrease) in net assets	.6	(1.0)
Ending net assets	<u>\$ 20.3</u>	<u>\$ 19.7</u>

This reflects an increase of 3.04%. The Commission generally can only use these net assets to finance the expansion and continuing operations of the water, gas and sewer system.

Business-type Activities

Water rates were increased by 9.2% effective February 1, 2007. Gas rates were increased 3.7% effective February 1, 2007. The rates were increased due to the Commission's rising cost to obtain natural gas and increased costs to expand the water and sewer system throughout the service area.

GENERAL FUND BUDGETARY HIGHLIGHTS

The original budget, final budget and actual results are as follows:

	Budget Basis Original	Actual Amount GAAP Basis
Operating Revenue	\$ 5,360,779	\$ 5,701,794
Operating Expenses	5,404,759	6,863,636
Non-Operating Revenue/Expenses	(51,080)	58,389
Capital Contributions	1,200,000	1,759,556
Change in Net Assets	<u>\$ 1,104,940</u>	<u>\$ 656,103</u>

Operating revenue was budgeted based upon prevailing rates at June 30, 2006. Actual operating revenues billed varied from the original budget by 6.4%. This variance was due in part to increases in water and gas billing rates. Actual operating expenses varied from the original budget by 26.99%. This variance was due in large part to increases in natural gas purchase prices. The variance in non-operating revenues net of non-operating expenses is due primarily to a conservative estimate of interest income. Actual capital contributions were over budget. The increase in capital contributions accounts for the Commission closing the year with an increase in net assets.

PRESTONSBURG CITY'S UTILITIES COMMISSION
 MANAGEMENT'S DISCUSSION AND ANALYSIS
 FOR THE YEAR ENDED JUNE 30, 2007

CAPITAL ASSET AND DEBT ADMINISTRATION

Capital Assets

At the end of June 30, 2007, the Commission had \$39.3 million invested in capital assets including land, buildings and improvements, machinery and equipment and water, sewer, and gas lines, compared to \$36.6 million at June 30, 2006. This represents a net increase of \$2.7 million, or a 7.4% increase over last year.

	Business-Type Activities	
	2007	2006
Land	\$ 323,521	\$ 287,832
Buildings	561,114	561,114
Improvements	29,777	29,777
Vehicles	1,280,542	1,170,727
Office and other equipment	648,182	529,241
Water, sewer and gas lines	36,109,152	34,053,743
Construction in progress	312,259	0
TOTALS	\$ 39,264,547	\$ 36,632,434

This year's major additions included:

Water line extensions	\$ 963,025
Sewer line extensions	740,910
Totals	\$ 1,703,935

Debt

At year-end, the Commission had \$5.13 million in outstanding bonds, notes and capital leases compared to \$5.38 million last year. That is a decrease of approximately 4.6% as shown in the following table.

	2007	2006
Revenue notes (backed by system revenues)	\$ 2,346,500	\$ 2,375,000
KIA loans (backed by system revenues)	2,405,890	2,619,463
Capital lease obligations (secured by asset purchased)	373,205	389,871
TOTALS	\$ 5,125,595	\$ 5,384,334

New debt issued this year consisted of 4 notes totaling \$133,020. These notes were used to purchase vehicles. Other obligations of the Commission included accrued compensated absences and a line of credit. More detailed information about the Commission's long-term liabilities is presented in Note H to the basic financial statements.

PRESTONSBURG CITY'S UTILITIES COMMISSION
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED JUNE 30, 2007

ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES

The Commission's business-type activities will see a substantial change due to both water and gas rate increases. Water rates were increased effective February 1, 2007. The increase in rates amounted to approximately 9.2% across the board for residential customers and 2% for wholesale customers currently served. Gas rates were increased effective May 1, 2007 and amounted to an increase of approximately 3% across the board. The effects of both increases are reflected in the operating budget for Fiscal Year 2008.

Major capital additions budgeted for the Commission includes the construction of a 10" waterline and booster station along the east side of KY Route 321 from the north side of Prestonsburg to the new tank at Highlands Regional Medical Center and also to construct a water tank at Lancer with a cost basis of \$982,000. Other major capital additions included the construction of sewer lines in Town Branch with a cost basis of \$702,000.

CONTACTING THE COMMISSION'S FINANCIAL MANAGEMENT

This financial report is designed to provide our citizens, taxpayers, customers, and creditors with a general overview of the Commission's finances and to show the Commission's accountability for the money it receives. If you have questions about this report or need additional information, contact the Prestonsburg City's Utilities Commission Office at 2560 South Lake Drive, Prestonsburg, Kentucky 41653.

Turner E, Campbell

Prestonsburg City's Utilities Commission

Chief Financial Officer

PRESTONSBURG CITY UTILITIES COMMISSION
STATEMENT OF NET ASSETS
JUNE 30, 2007 and 2006

	<u>2007</u>	<u>2006</u>
ASSETS		
Current Assets		
Cash - (Note A)	\$ 885,428	\$ 992,461
Cash - restricted (Notes A and B)	-	-
Accounts receivable, net - (Note C)	841,299	622,957
Due from other funds	482,521	437,359
Inventory	106,518	99,928
Other current assets - (Note D)	<u>72,963</u>	<u>9,155</u>
Total Current Assets	2,388,729	2,161,860
Noncurrent Assets		
Investments - (Notes A and B)	1,856,085	1,779,741
Investments - restricted (Notes A and B)	<u>150,216</u>	<u>1,220,259</u>
Total Noncurrent Assets	2,006,301	3,000,000
Capital Assets - (Note E)		
Construction in progress	312,259	-
Land and land improvements	353,298	317,609
Buildings	561,114	561,114
Office and other equipment	648,182	529,241
Water plant and equipment	20,551,980	19,281,302
Sewer plant and equipment	14,779,670	14,000,574
Gas distribution system	777,502	771,867
Motor vehicles	<u>1,280,542</u>	<u>1,170,727</u>
	39,264,547	36,632,434
Less: accumulated depreciation	(17,451,168)	(15,899,514)
Capital assets, net	<u>21,813,379</u>	<u>20,732,920</u>
Total Assets	<u>\$ 26,208,409</u>	<u>\$ 25,894,780</u>

The accompanying notes are an integral part of these financial statements.

PRESTONSBURG CITY UTILITIES COMMISSION
 STATEMENT OF NET ASSETS
 JUNE 30, 2007 and 2006

	2007	2006
LIABILITIES AND NET ASSETS		
Current Liabilities		
Accounts payable (Note F)	\$ 299,383	\$ 451,289
Customer meter deposits	256,852	247,737
Current maturities of long-term debt	370,253	348,063
Current maturities of bonds payable	30,000	28,500
Construction contracts payable	30,186	9,500
Unearned revenue	13,300	15,100
Accrued expenses - (Note G)	156,995	116,825
Total Current Liabilities	1,156,969	1,217,014
Noncurrent Liabilities		
Bonds, notes, and leases payable	4,725,342	5,007,771
Total Liabilities	5,882,311	6,224,785
NET ASSETS		
Investment in capital assets, net of related debt	16,687,784	15,348,586
Unrestricted	3,638,314	4,321,409
Total Net Assets	20,326,098	19,669,995
Total Liabilities and Net Assets	\$ 26,208,409	\$ 25,894,780

The accompanying notes are an integral part of these financial statements.

PRESTONSBURG CITY UTILITIES COMMISSION
 STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS
 FOR THE YEARS ENDED JUNE 30, 2007 AND JUNE 30, 2006

	<u>2007</u>	<u>2006</u>
OPERATING REVENUES:		
Charges for services:		
Water sales	\$ 2,818,318	\$ 2,509,134
Gas sales	1,675,285	1,587,528
Sewer service	1,023,346	786,407
Tap fees	53,300	48,536
Penalties and arrears	116,227	126,728
Reconnection and collection fees	15,318	8,395
Total Operating Revenues	<u>5,701,794</u>	<u>5,066,728</u>
 OPERATING EXPENSES:		
Gas purchases	1,414,768	1,381,524
Water purchases	25,694	43,381
Maintenance materials and supplies	593,565	596,414
Lab testing fees	19,693	16,864
Electric power	361,670	291,816
Uniforms	-	-
Salaries and wages	1,418,055	1,374,289
Maintenance labor	-	-
Motor vehicle expense	79,281	78,615
Depreciation	1,596,077	1,544,560
Bad debts	16,978	8,368
Insurance	112,843	139,404
Hospitalization insurance	345,229	296,313
Other employee benefits	179,935	145,792
Legal and professional services	48,224	58,150
Engineering, easements and recording fees	88,256	50,594
Postage	52,940	23,735
Equipment rent	56,920	38,435
Office expense	53,007	77,470
Freight	3,011	6,025
Telephone	28,809	26,397
Advertising	4,127	6,012
Sewer sludge disposal	13,036	12,958
Educational and training expense	26,215	16,611
Travel	849	49
Dues and subscriptions	2,307	4,339
Payroll taxes	88,991	110,285
Miscellaneous tax and licenses	7,626	2,586
Directors fees	2,160	2,160
Gasoline and diesel fuel	94,121	88,724
Janitorial and grounds expense	83,979	62,240
Small tools	15,749	14,491
Miscellaneous	29,521	17,500
Total Operating Expenses	<u>6,863,636</u>	<u>6,536,101</u>
Operating Income (Loss)	<u>\$ (1,161,842)</u>	<u>\$ (1,469,373)</u>

The accompanying notes are an integral part of these financial statements.

PRESTONSBURG CITY UTILITIES COMMISSION
 STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS
 FOR THE YEARS ENDED JUNE 30, 2007 AND JUNE 30, 2006

	<u>2007</u>	<u>2006</u>
NONOPERATING REVENUES (EXPENSES)		
Miscellaneous income	\$ 88,915	\$ 183,245
Rent income	1,800	-
Gain on sale of capital assets	15,000	58,861
Interest income	134,797	115,163
Interest expense	<u>(182,123)</u>	<u>(187,407)</u>
Total Nonoperating Revenues (Expenses)	<u>58,389</u>	<u>169,862</u>
Income (loss) before contributions	<u>(1,103,453)</u>	<u>(1,299,511)</u>
CAPITAL CONTRIBUTIONS	<u>1,759,556</u>	<u>261,703</u>
Change in net assets	656,103	(1,037,808)
Total net assets - beginning	19,669,995	20,707,803
Total net assets - ending	<u>\$ 20,326,098</u>	<u>\$ 19,669,995</u>

The accompanying notes are an integral part of these financial statements.

PRESTONSBURG CITY UTILITIES COMMISSION
STATEMENT OF CASH FLOWS
FOR THE YEARS ENDED JUNE 30, 2007 AND JUNE 30, 2006

	<u>2007</u>	<u>2006</u>
CASH FLOWS FROM OPERATING ACTIVITIES		
Receipts from customers	\$ 5,422,073	\$ 5,125,038
Payments to suppliers	(4,058,149)	(3,629,957)
Payments to employees	(1,358,013)	(1,374,289)
Other receipts (payments)	92,287	447,065
Customer meter deposits	9,115	(7,433)
Net Cash Provided (Used) for Operating Activities	<u>107,313</u>	<u>560,424</u>
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Proceeds from capital debt	133,020	71,194
Capital contributions	1,759,556	261,703
Purchases of capital assets	(2,676,536)	(678,718)
Principal paid on capital debt	(391,759)	(357,537)
Interest paid on capital debt	(182,123)	(187,901)
Proceeds from sale of capital assets	15,000	72,119
Net cash (used) by capital and related financing activities	<u>(1,342,842)</u>	<u>(819,140)</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Proceeds from investments redeemed	993,699	678,835
Interest	134,797	115,163
Net cash (used) by investing activities	<u>1,128,496</u>	<u>793,998</u>
Net increase (decrease) in cash and cash equivalents	<u>(107,033)</u>	<u>535,282</u>
Balances - beginning of year	<u>992,461</u>	<u>457,179</u>
Balances - end of year	<u>\$ 885,428</u>	<u>\$ 992,461</u>

The accompanying notes are an integral part of these financial statements.

PRESTONSBURG CITY UTILITIES COMMISSION
 STATEMENT OF CASH FLOWS
 FOR THE YEARS ENDED JUNE 30, 2007 AND JUNE 30, 2006

	<u>2007</u>	<u>2006</u>
RECONCILIATION OF OPERATING INCOME (LOSS) TO NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES		
Operating Income (Loss)	\$ (1,161,842)	\$ (1,469,373)
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation Expense	1,596,077	1,544,560
Miscellaneous Income (Expense)	90,715	183,245
 Change in Net Assets and Liabilities:		
Receivables, net	(218,342)	58,310
Inventories	(6,590)	(12,705)
Other current assets	(108,970)	113,940
Accounts and other payables	(122,105)	129,142
Accrued expenses	40,170	13,305
Unearned revenue	(1,800)	-
Net cash provided (used) by operating activities	<u>\$ 107,313</u>	<u>\$ 560,424</u>

The accompanying notes are an integral part of these financial statements.

PRESTONSBURG CITY UTILITIES COMMISSION
NOTES TO BASIC FINANCIAL STATEMENTS
JUNE 30, 2007 and 2006

NOTE A: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

ORGANIZATION

The Prestonsburg City's Utilities Commission (the "Commission") is a municipally owned gas, water and sewer facility created as a public project in 1956 by ordinance of the City of Prestonsburg, Kentucky. The facility is supervised and managed by three commission members each with staggered six-year terms, who are appointed by the Mayor. Gas and sewage services are provided in Prestonsburg, and local surrounding areas; water services are provided in Prestonsburg and extend throughout most of Floyd County, either directly or indirectly through sales to wholesale water customers.

The Commission's financial statements are prepared in accordance with generally accepted accounting principles (GAAP). The Governmental Accounting Standards Board (GASB) is responsible for establishing GAAP for state and local governments through its pronouncements (Statements and Interpretations). Governments are also required to follow the pronouncements of the Financial Accounting Standards Board (FASB) issued through November 30, 1989 (when applicable) that do not conflict with or contradict GASB pronouncements. In June 1999, the Governmental Accounting Standards Board (GASB) unanimously approved Statement No. 34 *Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments*. Certain of the significant changes in the Statement include the following:

1. Reporting Entity

The Commission is a component unit of the City of Prestonsburg and maintains separate and distinct accounting records. The City of Prestonsburg transferred to the Commission, by Ordinance in 1956, all powers of the City to improve, operate and maintain the utility systems, including the power to determine utility rates and financial practices.

2. Basic Financial Statements—Fund Financial Statements

The financial transactions of the Commission are reported as a single fund, accounted for by a separate set of self-balancing accounts that comprise its assets, liabilities, reserves, fund equity, revenues and expenditures/expenses. The Commission uses the following fund type:

- Proprietary Funds

The focus of proprietary fund measurement is based upon determination of operating income, changes in net assets, financial position and cash flows. The generally accepted accounting principles applicable are those similar to businesses in the private sector. The Commission is an Enterprise fund which is required to account for operations for which a fee is charged to external users for goods and services and the activity (a) is financed with debt that is solely secured by a pledge of the net revenues, (b) has third party requirements that the cost of providing services, including capital costs, be recovered with fees and charges or (c) establishes fees and charges based on a pricing policy designed to recover similar costs.

3. Basis of Accounting

Basis of accounting refers to the point at which revenues or expenditures/expenses are recognized in the accounts and reported in the financial statements. It relates to the timing of the measurements made regardless of the measurement focus applied. The accounting records are maintained on the accrual basis of accounting. Using this method, revenues are recognized when earned and expenses are recognized when incurred.

PRESTONSBURG CITY UTILITIES COMMISSION
 NOTES TO BASIC FINANCIAL STATEMENTS
 JUNE 30, 2007 and 2006

NOTE A: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Proprietary funds distinguish operating revenues and expenses from non-operating revenue items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. The principal operating revenues of the Commission are for sales of water and natural gas to customers; charges for sewer services; and related tap and connection fees in addition to late payment charges. Operating expenses include the cost of sales, wages, operating and administrative expenses and depreciation of capital assets. All revenue and expenses not meeting this definition are reported as non-operating revenues and expenses.

4. Financial Statement Amounts

a) Cash and cash equivalents

For purposes of reporting cash flows, the Commission considers all cash on hand, cash accounts which are not subject to withdrawal restrictions or penalties and certificates of deposit with original maturities of 90 days or less to be cash or cash equivalents. All cash accounts are insured and collateralized.

b) Restricted cash and investments

Prestonsburg City's Utilities Commission is required by various bond agreements and ordinances to restrict cash amounts as mandated to meet funding requirements by those agreements and ordinances. The policy of the Commission regarding improvements, expansion and major renovation projects is to restrict an amount of cash to adequately fund the projects. As of June 30, Prestonsburg City's Utilities Commission had the following cash and investment amounts restricted:

	<u>2007</u>	<u>2006</u>
Customer Meter Deposits	\$ 256,852	\$ 247,736
Depreciation Reserve Fund	286,113	256,768
Unearned Sewer Tap Fees	13,300	15,100
Operation & Maintenance Reserve Fund	702,990	702,990
Construction Commitments		
Debt Service Fund	566,643	547,647
Retainage – Construction Contractors	<u>30,187</u>	<u>9,500</u>
	<u>\$ 1,856,085</u>	<u>\$ 1,779,741</u>

The restricted amounts consist of cash, current investments (securities with less than one-year maturity from balance sheet date) and non-current investments. The restricted amount at June 30, 2007 of \$150,216 consists of non-current investments. The restricted amount at June 30, 2006 of \$1,220,259 consists of non-current investments. The Depreciation Reserve Fund includes the restricted amounts required by USDA Rural Development and KIA.

- (1) \$ 8,640 - 1998 US 23/Cow Creek Project
- (2) \$ 10,920 - Buffalo Project
- (3) \$ 36,720 - 2001 Mountaintop Bond Issue
- (4) \$ 7,470 - Raw Water Intake Project
- (5) \$222,363 – KIA

PRESTONSBURG CITY UTILITIES COMMISSION
NOTES TO BASIC FINANCIAL STATEMENTS
JUNE 30, 2007 and 2006

NOTE A: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

c) Inventory

Inventory is stated at the lower of cost or market value, cost being computed on a first-in, first-out basis.

d) Capital Assets

Capital assets purchased or acquired are reported at historical cost. Contributed assets are reported at fair market value as of the date received. Additions, improvements and other capital outlays that significantly extend the useful life of an asset are capitalized. Other costs incurred for repairs and maintenance are expensed as incurred. Depreciation on all assets is provided on the straight-line basis over their useful lives ranging from 5 to 50 years.

e) Revenues

All revenues are accrued when earned. Utility service charges are billed monthly and collected in the following month. Grants to proprietary funds, which finance either capital or current operations, are reported as non-operating revenue based on GASBS No. 33. In applying GASBS No. 33 to grant revenues, the provider recognizes liabilities and expenses and the recipient recognizes receivables and revenues when the applicable eligibility requirements, including time requirements, are met. Resources transmitted before the eligibility requirements have been met are reported as advances by the provider and as deferred revenue by the recipient.

f) Expenditures

Expenses are recognized when incurred. Inventory costs are reported in the period when the inventory items are used, rather than in the period purchased.

g) Compensated absences

After completion of one (1) year of continuous service each full-time regular employee is granted vacation benefits and sick leave in varying amounts to specified maximums depending on their tenure with the Commission. Employees shall not be compensated for accrued sick leave upon termination or resignation of employment. Employees earn 80 hours of vacation time per year for each year of employment between years one and seven and 120 hours for each year after seven years. Employees may have no more than 40 hours accrued vacation at December 31st that can be carried over to the following calendar year. Once each calendar year, eligible employees may, upon request, be paid for a maximum of 40 hours of unused vacation time. All vacation time is paid at the employee's regular rate of pay. Full-time regular employees are entitled to all accrued vacation leave benefits if they terminate their employment in good standing.

h) Use 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.

PRESTONSBURG CITY UTILITIES COMMISSION
NOTES TO BASIC FINANCIAL STATEMENTS
JUNE 30, 2007 and 2006

NOTE A: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

- i) Income taxes
The organization was granted tax-exempt status under Section 501(c)(3) of the Internal Revenue Code. Therefore, no provision for income taxes has been made in these financial statements.
- j) Advertising
Advertising costs are charged to operations in the year incurred and totaled \$4,127 and \$6,012 for the years ended June 30, 2007 and 2006, respectively.

NOTE B: DEPOSITS AND INVESTMENTS

Deposits

The Commission's deposits are categorized to give an indication of the level of risk assumed by the Commission at fiscal year end. The categories are described as follows:

Category 1 - Insured or collateralized with securities held by the Commission or by its agent in the Commission's name.

Category 2 - Collateralized with securities held by the pledging financial institution's trust department or agent in the Commission's name.

Category 3 - Uncollateralized

The Commission's deposits are all considered to be in the Category 1 level of risk for June 30, 2007 and 2006.

At June 30, 2007 the carrying amount of the Commission's deposits was \$883,817 and the bank balances totaled \$947,304. The difference between the carrying amounts and bank balances was due to items in transit. Of the bank balances, \$307,185 was covered by the Bank Insurance Fund and \$640,119 was uninsured but collateralized with pledged securities held by the depositories in the Commission's name.

At June 30, 2006 the carrying amount of the Commission's deposits was \$990,850 and the bank balances totaled \$1,198,102. The difference between the carrying amounts and the bank balances was due to items in transit. Of the bank balances, \$207,188 was covered by the Bank Insurance Fund and \$990,914 was uninsured but collateralized with pledged securities held by the depositories in the Commission's name.

Investments

The Commission's investments are categorized to give an indication of the level of risk assumed by the Commission at fiscal year end. The categories are described as follows:

Category 1 - Insured, registered or securities held by the Commission or by its agent in the Commission's name.

Category 2 - Uninsured and unregistered, with securities held by the counter party's trust department or agent in the Commission's name.

Category 3 - Uninsured and unregistered, with securities held by the counter party, or its trust department or agent but not in the Commission's name.

PRESTONSBURG CITY UTILITIES COMMISSION
 NOTES TO BASIC FINANCIAL STATEMENTS
 JUNE 30, 2007 and 2006

NOTE B: DEPOSITS AND INVESTMENTS (Continued)

Investing is performed in accordance with investment policies complying with State Statutes and a resolution adopted by the Commission. The following is a summary of the Commission's investments at June 30, 2007 and 2006. These investments are either insured or collateralized with pledged securities held by the depositories in the Commission's name.

	<u>2007</u>		<u>2006</u>
Certificates of Deposit (Non-current) \$	2,006,301	\$	3,000,000
	<u>2,006,301</u>	\$	<u>3,000,000</u>

The Commission's investments are all considered to be in the Category 1 level of risk for June 30, 2007 and 2006.

NOTE C: ACCOUNTS RECEIVABLE AND BAD DEBTS

Accounts receivable are summarized as follows:

	<u>2007</u>		<u>2006</u>
Customer Accounts Receivable \$	875,620	\$	776,404
Miscellaneous Accounts Receivable	16,046		3,414
Total Accounts Receivable	891,666		779,818
Less: Allowance for Doubtful Accounts	<u>(50,367)</u>		<u>(156,861)</u>
Accounts Receivable, net \$	<u>841,299</u>	\$	<u>622,957</u>

Bad debts are recognized utilizing the allowance method. The provision for bad debts charged to operations is the amount deemed sufficient to bring the balance of the reserve to an adequate level to absorb future losses based on the Commission's past loss experience and other factors, which, in management's judgment, are necessary in estimating possible bad debts. Bad debt expense recognized for the fiscal years ended June 30, 2007 and 2006 was \$16,978 and \$8,368, respectively. Miscellaneous accounts receivable at June 30, 2007 consisted of miscellaneous sales of water and related supplies. Miscellaneous accounts receivable at June 30, 2006 consisted of miscellaneous sales of water and related supplies.

NOTE D: OTHER CURRENT ASSETS

The other assets account consists of:

- (1) \$1,100 equipment deposit; \$4,300 interest receivable; \$16 accounts receivable employee; and \$67,547 prepaid insurance at June 30, 2007.
- (2) \$1,100 equipment deposit and \$8,055 interest receivable at June 30, 2006.

PRESTONSBURG CITY UTILITIES COMMISSION
 NOTES TO BASIC FINANCIAL STATEMENTS
 JUNE 30, 2007 and 2006

NOTE E: PLANT AND EQUIPMENT

Plant and equipment are stated at cost less accumulated depreciation. Depreciation has been provided over the estimated useful lives of the assets on the straight-line method of cost allocation. Maintenance, repairs and minor replacements are charged to expense as incurred; major renewals and betterments are capitalized. At June 30, 2007 and 2006, plant and equipment consisted of the following:

		<u>2007</u>	<u>2006</u>
Water Plant and Distribution System	5-40 Yrs.	\$ 20,551,980	\$ 19,288,390
Sewer Plant and Collection System	5-50 Yrs.	14,779,670	14,000,643
Gas Distribution System	5-50 Yrs.	777,502	764,710
Motor Vehicles	4-5 Yrs.	671,739	625,887
Office and Other Equipment	5-10 Yrs.	648,182	529,241
Office Buildings and Improvements	5-40 Yrs.	561,114	561,114
Land Improvements	20 Yrs.	29,777	29,777
Land		323,521	287,832
Construction in progress		312,259	
Rental Property Improvements	5-20 Yrs.	0	0
Equipment Acquired by Capital Lease	5 Yrs.	608,803	544,840
Land Acquired by Capital Lease		<u>0</u>	<u>0</u>
Total Cost		39,264,547	36,632,434
Less: Accumulated Depreciation		(17,148,913)	(15,682,534)
Less: Accumulated Depreciation – Capital Leases		<u>(302,255)</u>	<u>(216,980)</u>
Net Plant and Equipment		\$ <u>21,813,379</u>	\$ <u>20,732,920</u>

Depreciation expense charged to operations in fiscal year ended June 30, 2007, amounted to \$1,596,077 of this amount \$85,275 was depreciation for equipment obtained by capital lease. Depreciation expense charged to operations for fiscal year June 30, 2006 was \$1,544,560 of this amount \$84,165 was depreciation for equipment obtained by capital lease. A detailed summary of changes in Plant and Equipment for the year ended June 30, 2007 is included as supplementary information on page 33 of this report.

NOTE F: ACCOUNTS PAYABLE

Accounts payable at June 30 consists of:

	<u>2007</u>	<u>2006</u>
Various Trade Vendors	\$ 191,993	\$ 253,524
City of Prestonsburg & Floyd County for collection of sanitation fees	<u>107,390</u>	<u>197,765</u>
Total Accounts Payable	\$ <u>299,383</u>	\$ <u>451,289</u>

PRESTONSBURG CITY UTILITIES COMMISSION
 NOTES TO BASIC FINANCIAL STATEMENTS
 JUNE 30, 2007 and 2006

NOTE G: ACCRUED EXPENSES

Accrued expenses as shown on the balance sheet at June 30 consist of the following accounts:

	<u>2007</u>	<u>2006</u>
Accrued Payroll Taxes and Withholding	\$ 11,419	\$ 25,860
Compensated Absences	117,532	57,474
Retirement Payable	19,222	25,047
Accrued Sales Tax	4,584	3,823
Accrued Bond and Note Interest	3,638	4,021
Rent Deposit Payable	<u>600</u>	<u>600</u>
Total Accrued Expenses	<u>\$ 156,995</u>	<u>\$ 116,825</u>

NOTE H: LONG-TERM DEBT

The Commission's outstanding lease agreements include the acquisition of four vehicles in the current year and land, a sewer cleaning machine, construction equipment and a Chevy Tahoe in prior years. These leases qualify as capital leases. The lease term will terminate upon final payment. Outstanding bond and notes payable represent acquisition of water systems and expansion of water and sewer lines in prior years. Bonds, notes and leases payable are summarized as follows:

	Rate	Maturity Date	Beginning Balance	Additions	Reductions	Ending Balance	Current Portion
Bonds Payable:							
USDA/RD (1998)	4.50%	01/01/38	\$ 173,500	\$ 0	\$ 2,500	\$ 171,000	\$ 2,500
USDA/RD (1999)	4.75%	01/01/27	255,500		3,500	252,000	3,500
USDA/RD (2001)	4.50%	01/01/41	1,065,000		13,000	1,052,000	14,000
USDA/RD (91-23)	4.50%	01/01/44	732,500		8,000	724,500	8,500
USDA/RD (91-25)	4.50%	01/01/44	148,500		1,500	147,000	1,500
Total Bonds Payable			<u>2,375,000</u>	<u>0</u>	<u>28,500</u>	<u>2,346,500</u>	<u>30,000</u>
Notes Payable:							
KIA – (B291-11)	2.90%	06/01/14	921,256		103,892	817,364	106,927
KIA – (B98-01)	1.30%	06/01/19	407,436		28,962	378,474	29,340
KIA – (A98-03)	1.80%	12/01/20	698,385		42,558	655,827	43,327
KIA – (B99-01)	1.00%	12/01/20	592,386		38,161	554,225	38,543
Daimler-Chrysler	4.91%	9/19/08	29,437		12,685	16,752	13,320
Community Trust	4.99%	9/2/08	25,980		25,980	0	0
Community Trust	6.67%	6/27/10	0	22,380	2,389	19,991	7,077
Community Trust	6.72%	6/27/10	0	24,631	0	24,631	7,670
Community Trust	6.77%	2/11/10	0	22,046	0	22,046	6,863
Total Notes Payable			<u>2,674,880</u>	<u>69,057</u>	<u>254,627</u>	<u>2,489,310</u>	<u>253,067</u>
Leases Payable:							
KADD2003_045B	3.59%	04/20/10	230,000		55,000	175,000	55,000
Leasing One Corp.	4.78%	04/06/05	36,487		36,487	0	0
Leasing One Corp.	5.27%	6/01/12	67,967	63,963	17,145	114,785	62,186
Total Leases Payable			<u>334,454</u>	<u>63,963</u>	<u>108,632</u>	<u>289,785</u>	<u>117,186</u>
Total Long-Term Debt			<u>\$ 5,384,334</u>	<u>\$ 133,020</u>	<u>\$ 391,759</u>	<u>\$ 5,125,595</u>	<u>\$ 400,253</u>

PRESTONSBURG CITY UTILITIES COMMISSION
 NOTES TO BASIC FINANCIAL STATEMENTS
 JUNE 30, 2007 and 2006

NOTE H: LONG-TERM DEBT (Continued)

The annual debt service requirements to maturity for long-term debt are as follows:

	BONDS		NOTES PAYABLE	
	Principal	Interest	Principal	Interest
June 30, 2009	\$ 31,500	\$ 104,399	\$ 249,356	\$ 42,506
June 30, 2010	33,000	102,939	249,552	36,095
June 30, 2011	33,500	101,444	232,511	30,443
June 30, 2012	35,000	99,904	237,539	25,414
June 30, 2013	37,500	98,520	242,691	20,264
June 30, 2014-2018	213,500	463,972	748,701	46,627
June 30, 2019-2023	266,500	410,205	275,893	5,592
June 30, 2024-2028	332,500	343,199		
June 30, 2029-2033	413,000	259,718		
June 30, 2034-2038	519,500	155,245		
June 30, 2039-2043	401,000	41,905		
June 30, 2044-2048				
	\$ <u>2,316,500</u>	\$ <u>2,181,450</u>	\$ <u>2,236,243</u>	\$ <u>206,941</u>

	LEASES PAYABLE	
	Principal	Interest
June 30, 2009	\$ 72,035	\$ 7,464
June 30, 2010	72,750	4,377
June 30, 2011	13,506	1,187
June 30, 2012	14,308	383
June 30, 2013		
	\$ <u>172,599</u>	\$ <u>13,411</u>

NOTE I: RETIREMENT PLAN

On August 18, 1988, the Commission and City of Prestonsburg by Ordinance No. 11-88 as prescribed by the House Bill 398 and KRS Statute 18.510 to 78.852, created the "Prestonsburg City Utilities Commission Retirement System", which is a participant in the County Employees Retirement System. This is a multiple employer public retirement system, providing retirement benefits for all full-time employees. This retirement plan, administered by Kentucky Retirement Systems, was for all electing employees as of August 1, 1988, and any future employees. Employees are vested in the plan after completion of (5) years of service.

PRESTONSBURG CITY UTILITIES COMMISSION
NOTES TO BASIC FINANCIAL STATEMENTS
JUNE 30, 2007 and 2006

NOTE I: RETIREMENT PLAN (Continued)

Benefit contributions and provisions are established by statute. Normal annual funding is computed at a percentage of gross wages, the percentage to be withheld is 5% and the percentage to be paid by the employer was 13.19% for the year ended June 30, 2007. Employer contributions for retirement were \$176,700 and \$145,614 for the years ending June 30, 2007 and 2006, respectively. Historical trend information showing the CERS' progress in accumulating sufficient assets to pay benefits when due is presented in the Kentucky Retirement System's annual financial report (which is a matter of public record).

NOTE J: CONSTRUCTION COMMITMENTS

Sanitary Sewer Extension - Big Branch Abbott

On September 7, 1995, the Commission accepted a check in the amount of \$40,000 from Big Branch Development Corporation, a construction company planning to build new houses in the Big Branch Abbott Creek area near Prestonsburg, Kentucky. This check was recorded as unearned sewer tap fees and income is being recognized as the taps are made. At June 30, 2007 and 2006, the balance of this account was \$13,300 and \$15,100, respectively.

Kentucky 321 Waterline Reinforcement Project

The Commission serves the water demands of the northern area of the city and county as well as the new Big Sandy Federal Prison Complex and parts of Martin County via a line that crosses the Big Sandy River four times between the northern most area of the city and Highlands Regional Medical Center. The Commission plans to replace this line, thus, eliminating the river crossings. Phase I of this project was completed during Fiscal Year 2004 when the 1,000,000-gallon water storage tank at the Highlands Regional Medical Center was constructed. Phase II of the project involves the construction of the new 10" waterline and booster station along the east side of KY Route 321 from the north side of Prestonsburg to the new tank near Highlands Regional Medical Center. The estimated cost of Phase II is \$800,000. Advertising for bids for Phase II is anticipated for the early spring of 2006 with construction expected to commence shortly thereafter. Both state and federal funding assistance is anticipated by the Commission for this project. This scope of this project was expanded during the year ended June 30, 2007 and Phase III should be completed during fiscal year 2008. Phase II of the project was completed during the year ended June 30, 2007 and was capitalized in the amount of \$982,285..

Town Branch PRIDE 2005 Sewer Project

During Fiscal Year 2006 the Commission will advertise for both engineering services and construction contractors with the intention of extending force main sewer service to the Town Branch area of Prestonsburg. The estimated cost of this project is \$700,000. It is anticipated that the cost will be funded with Federal PRIDE Program dollars. This project was completed during the year ended June 30, 2007, and was capitalized in the amount of \$702,559.

Construction in progress – Elevator and Office Improvement Project

Construction in progress during the year included the addition of an elevator and related office remodeling. The amount of expenditures in this account at June 30, 2007 was \$312,259. The project should be completed during the 2008 fiscal year.

PRESTONSBURG CITY UTILITIES COMMISSION
NOTES TO BASIC FINANCIAL STATEMENTS
JUNE 30, 2007 and 2006

NOTE K: COMMITMENTS AND CONTINGENCIES

The Commission is involved in legal action arising in the ordinary course of business. In the opinion of management, the Commission has adequate legal defenses or insurance coverage with respect to each of these actions and does not believe that they will materially affect the company's results of operations or financial position.

NOTE L: RELATED PARTY TRANSACTIONS

Board of Commissioners' Chairman, Jimmy Calhoun is president of Calhoun's Garage, Inc. Calhoun's Garage, Inc. occasionally performs vehicle repairs for the Commission. There were no material transactions individually or in the aggregate.

REQUIRED SUPPLEMENTARY INFORMATION

PRESTONSBURG CITY UTILITIES COMMISSION
 BUDGETARY COMPARISON SCHEDULE
 FOR THE YEAR ENDED JUNE 30, 2007

	Budgeted Basis <u>Original</u>	Actual Amount - <u>GAAP Basis</u>
OPERATING REVENUES:		
Charges for services:		
Water sales	\$ 2,584,754	\$ 2,818,318
Gas sales	1,793,856	1,675,285
Sewer service	820,545	1,023,346
Tap fees	38,000	53,300
Penalties and arrears	111,125	116,227
Reconnection and collection fees	12,499	15,318
Total Operating Revenues	<u>5,360,779</u>	<u>5,701,794</u>
OPERATING EXPENSES:		
Gas purchases	1,225,000	1,414,768
Water purchases	5,500	25,694
Maintenance materials and supplies	446,500	593,565
Lab testing fees	17,050	19,693
Electric power	231,200	361,670
Uniforms	7,255	-
Salaries and wages	1,351,000	1,418,055
Maintenance labor	7,575	-
Motor vehicle expense	42,750	79,281
Depreciation	1,302,000	1,596,077
Bad debts	-	16,978
Insurance	81,075	112,843
Hospitalization insurance	256,780	345,229
Other employee benefits	137,899	179,935
Legal and professional services	22,900	48,224
Engineering, easements and recording fees	16,025	88,256
Postage	23,275	52,940
Equipment rent	15,100	56,920
Office expense	41,000	53,007
Freight	4,150	3,011
Telephone	16,850	28,809
Advertising	2,955	4,127
Sewer sludge disposal	13,505	13,036
Educational and training expense	8,255	26,215
Travel	750	849
Dues and subscriptions	3,195	2,307
Payroll taxes	84,150	88,991
Miscellaneous tax and licenses	905	7,626
Directors fees	2,160	2,160
Bond Issue Costs	3,250	94,121
Gasoline and diesel fuel	-	83,979
Janitorial and grounds expense	24,895	15,749
Small tools	-	29,521
Miscellaneous	9,855	-
Total Operating Expenses	<u>5,404,759</u>	<u>6,863,636</u>
Operating Income (Loss)	\$ <u>(43,980)</u>	\$ <u>(1,161,842)</u>

The accompanying notes are an integral part of these financial statements.

PRESTONSBURG CITY UTILITIES COMMISSION
 BUDGETARY COMPARISON SCHEDULE
 FOR THE YEAR ENDED JUNE 30, 2007

	Budgeted Basis <u>Original</u>	Actual Amount - <u>GAAP Basis</u>
NON-OPERATING REVENUES (EXPENSES):		
Miscellaneous Income	\$ 48,000	\$ 88,915
Rent Income	-	1,800
Gain on sale of capital assets	5,000	15,000
Interest Income	71,346	134,797
Interest Expense	<u>(175,426)</u>	<u>(182,123)</u>
Total Non-operating Revenues (Expenses)	<u>(51,080)</u>	<u>58,389</u>
Income (loss) before contributions	<u>(95,060)</u>	<u>(1,103,453)</u>
CAPITAL CONTRIBUTIONS	<u>1,200,000</u>	<u>1,759,556</u>
Change in Net Assets	1,104,940	656,103
Total net assets - beginning		19,669,995
Total net assets - ending	<u>\$ 1,104,940</u>	<u>\$ 20,326,098</u>

The accompanying notes are an integral part of these financial statements.

Michael R. Spears, C.P.A., P.S.C.

Certified Public Accountant

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 Board of Commissioners
Prestonsburg City's Utilities Commission

We have audited the financial statements of the business-type activities of Prestonsburg City's Utilities Commission as of and for the years ended June 30, 2007 and June 30, 2006, which collectively comprise the Prestonsburg City's Utilities Commission's basic financial statements and have issued our report thereon dated January 15, 2008. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered Prestonsburg City's Utilities Commission's 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 Prestonsburg City's Utilities Commission's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Prestonsburg City's Utilities Commission's internal control over financial reporting.

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


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

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

Compliance and Other Matters

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

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


Michael R. Spears, CPA, PSC
January 15, 2008

PRESTONSBURG CITY UTILITIES COMMISSION
 SCHEDULE OF FEDERAL AWARDS
 FOR THE YEAR ENDED JUNE 30, 2007

Federal Grantor/Pass-through Grantor/Program Title	Federal CFDA Number	Total Program or Award Amount	Federal Expenditures
U.S. ENVIRONMENTAL PROTECTION AGENCY - Special Purpose Grant - Rt. 321/Lancer Tank	66.606	650,500	\$ 497,044
U.S. DEPARTMENT OF COMMERCE - Passed through the USDA Rural Development - Pride Grant - Town Branch Project	11.469	691,210	691,210
Total Expenditures of Federal Awards			<u>\$ 1,188,254</u>

PRESTONSBURG CITY'S UTILITIES COMMISSION
NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
JUNE 30, 2007

NOTE 1 - BASIS OF PRESENTATION

The accompanying schedule of expenditures of federal awards includes the federal grant activity of Prestonsburg City's Utilities Commission 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 Organizations*. Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of the basic financial statements.

Michael R. Spears, C.P.A., P.S.C.

Certified Public Accountant

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 Board of Commissioners
Prestonsburg City's Utilities Commission

Compliance

We have audited the compliance of Prestonsburg City's Utilities Commission 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, 2007. Prestonsburg City's Utilities Commission's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to each of its major federal programs is the responsibility of Prestonsburg City's Utilities Commission's management. Our responsibility is to express an opinion on Prestonsburg City's Utilities Commission's compliance based on our audit.

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

In our opinion, Prestonsburg City's Utilities Commission 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, 2007.

Internal Control Over Compliance

The management of Prestonsburg City's Utilities Commission 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 Prestonsburg City's Utilities Commission's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance, 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 Prestonsburg City's Utilities Commission's 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.

Prestonsburg City's Utilities Commission's response to the findings identified in our audit are described in the accompanying schedule of findings and questioned costs. We did not audit Prestonsburg City's Utilities Commission's response and, accordingly, we express no opinion on it.

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



Michael R. Spears, CPA, PSC
January 15, 2008

PRESTONSBURG CITY'S UTILITIES COMMISSION
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
YEAR ENDED JUNE 30, 2007

A. SUMMARY OF AUDIT RESULTS

1. The auditor's report expresses an unqualified opinion on the financial statements of Prestonsburg City's Utilities Commission.
2. No reportable conditions material to the financial statements of Prestonsburg City's Utilities Commission were disclosed during the audit.
3. No instances of non-compliance material to the financial statements of Prestonsburg City's Utilities Commission were disclosed during the audit.
4. No reportable conditions material to the financial statements of Prestonsburg City's Utilities Commission were disclosed during the audit of the major federal award programs.
5. The auditor's report on compliance for the major federal award programs for Prestonsburg City's Utilities Commission expresses an unqualified opinion on all major federal programs.
6. There were no audit findings relative to the major federal programs for Prestonsburg City's Utilities Commission to be reported.
7. The programs tested as major programs included:

	<u>CFDA</u>
U.S. Environmental Protection Agency:	
- Special Purpose Grant	66.606
U.S. Department of Commerce:	
- Passed through USDA Rural Development	
- Pride Grant	11.469

8. The threshold for distinguishing Types A and B programs was \$500,000.
9. Prestonsburg City's Utilities Commission was determined to be a low-risk auditee.

B. FINDINGS - FINANCIAL STATEMENTS AUDIT

REPORTABLE CONDITIONS

NONE.

C. FINDINGS AND QUESTIONED COSTS - MAJOR FEDERAL AWARD PROGRAMS AUDIT

REPORTABLE CONDITIONS

NONE.

QUESTIONED COSTS

NONE.

OTHER SUPPLEMENTARY INFORMATION

	June 30, 2007	June 30, 2006	June 30, 2005	June 30, 2004	June 30, 2003
OPERATING REVENUES:					
Sales - net	5,701,794	5,066,728	4,990,811	4,726,510	4,346,705
	100.00%	100.00%	100.00%	100.00%	100.00%
OPERATING EXPENSES:					
Gas purchases	1,414,768	1,381,524	1,327,078	1,191,417	1,226,913
Water purchases	26,694	43,381	20,923	15,851	16,851
Maintenance materials and supplies	593,565	596,414	542,377	501,508	448,258
Lab testing fees	19,693	16,864	18,758	18,056	19,807
Electric power	361,670	291,816	277,822	236,049	215,442
Uniforms	-	-	9,891	9,912	9,106
Salaries and wages	1,418,055	1,374,289	1,263,334	1,322,919	1,264,898
Maintenance labor	-	-	68	10,782	18,515
Motor vehicle expense	79,251	78,615	40,992	71,971	88,789
Depreciation	1,596,077	1,544,560	1,431,545	1,341,235	1,299,520
Bad debts	16,978	8,368	21,766	-	7,396
Insurance	112,843	139,404	106,774	113,509	94,447
Hospitalization insurance	345,229	296,313	237,113	281,262	289,309
Other employee benefits	179,935	145,792	115,720	98,396	80,845
Legal and professional services	48,224	58,150	34,284	33,227	63,587
Engineering, easements and recording fees	88,256	50,594	24,979	4,375	37,747
Postage	52,940	23,735	22,613	24,509	24,001
Equipment rent	56,920	38,435	13,837	35,094	49,546
Office expense	53,007	77,470	39,666	46,809	44,356
Freight	3,011	6,025	4,737	3,841	5,217
Telephone	28,809	26,397	20,539	17,431	18,446
Advertising	4,127	6,012	4,252	2,951	3,045
Sewer sludge disposal	13,036	12,958	12,992	16,893	12,430
Educational and training expense	26,215	16,611	8,213	8,213	6,291
Dues and subscriptions	2,307	4,339	3,135	3,691	5,223
Payroll taxes	88,991	110,285	91,539	95,822	90,663
Miscellaneous tax and licenses	7,626	2,586	521	645	3,385
Property Taxes	-	-	-	-	-
Directors fees	2,160	2,160	2,495	2,160	2,160
Gasoline and diesel fuel	94,121	88,724	74,065	47,085	2,160
Junitorial and grounds expense	83,979	62,240	35,802	21,742	-
Small tools	15,749	14,491	9,998	1,578	-
Miscellaneous	29,521	17,500	10,161	14,214	11,698
Fines & Penalties	-	-	-	-	-
Bond issue costs	-	-	-	250	15,020
Travel	849	49	324	156	331
Total Operating Expenses	6,863,636	6,536,101	5,827,754	5,598,625	5,471,941
	120.38%	129.00%	116.77%	118.45%	125.89%
Operating Income (Loss)	(1,161,842)	(1,469,373)	(836,943)	(872,115)	(1,125,236)
	-20.38%	-29.00%	-16.77%	-18.45%	-25.89%
NON-OPERATING REVENUES (EXPENSES):					
Miscellaneous income	88,915	183,245	61,956	119,125	105,355
Industrial customer connection fee	-	-	-	-	-
Interest income	134,797	115,163	102,476	120,760	140,884
Interest Expense	(182,123)	(187,407)	(186,713)	(162,670)	(163,736)
Rental Income	1,800	-	4,800	9,000	7,200
Gain on Sale of Fixed Assets	15,000	58,861	48,464	3,335	20,998
Total Non-operating Revenues (Expenses)	58,389	169,862	30,983	89,540	110,701
	1.02%	3.35%	0.62%	1.89%	2.55%
NET INCOME (LOSS)	(1,103,453)	(1,299,511)	(805,960)	(782,575)	(1,014,535)
	-19.35%	-25.65%	-16.16%	-18.56%	-23.34%

PRESTONSBURG CITY UTILITIES COMMISSION
 SCHEDULE OF PLANT, EQUIPMENT AND DEPRECIATION
 FOR THE YEAR ENDED JUNE 30, 2007

	PLANT AND EQUIPMENT				ALLOWANCE FOR DEPRECIATION			
	Balance 6/30/2006	Additions	Deletions	Balance 6/30/2007	Balance 6/30/2006	Additions	Deletions	Balance 6/30/2007
WATER SYSTEM								
Plant, equipment, storage tanks and service lines	\$ 15,142,582	\$ 1,139,400	\$ -	\$ 16,281,982	\$ 7,288,065	\$ 522,407	\$ -	\$ 7,810,472
Meters	926,958	131,280	-	1,058,238	556,946	75,221	-	632,167
Plant expansion	2,061,451	-	-	2,061,451	873,538	69,102	-	942,640
David Water	136,861	-	-	136,861	70,268	3,422	-	73,690
Prater Creek Water	1,013,449	-	-	1,013,449	481,737	25,336	-	507,073
SEWER SYSTEM								
Equipment and service lines	12,708,981	779,095	-	13,488,076	4,222,345	560,298	-	4,782,643
Plant expansion and renovation	1,291,594	-	-	1,291,594	556,470	63,651	-	620,121
GAS SYSTEM								
Transmission and service lines	651,431	5,635	-	651,431	344,562	20,894	-	365,456
Meters and regulators	120,436	-	-	126,071	84,999	5,755	-	90,754
MOTOR VEHICLES								
	1,170,727	154,238	44,423	1,280,542	668,151	170,191	44,423	793,919
OFFICE AND OTHER EQUIPMENT								
	529,241	118,941	-	648,182	403,786	47,321	-	451,107
OFFICE BUILDING AND IMPROVEMENTS								
	620,750	35,688	-	656,438	333,062	30,493	-	363,555
LAND								
	228,196	-	-	228,196	-	-	-	-
LAND ACQUIRED BY CAPITAL LEASE								
	-	-	-	-	-	-	-	-
RENTAL PROPERTY AND IMPROVEMENTS								
	-	-	-	-	-	-	-	-
LAND IMPROVEMENTS								
	29,777	-	-	29,777	15,585	1,986	-	17,571
CONSTRUCTION IN PROGRESS								
	-	312,259	-	312,259	-	-	-	-
TOTAL	<u>\$ 36,632,434</u>	<u>\$ 2,676,536</u>	<u>\$ 44,423</u>	<u>\$ 39,264,547</u>	<u>\$ 15,899,514</u>	<u>\$ 1,596,077</u>	<u>\$ 44,423</u>	<u>\$ 17,451,168</u>