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DAMON R. TALLEY

ATTORNEY AT LAW

April 13, 2005

Ms. Beth O'Donnell
Executive Director
Public Service Commission
P.O. Box 615
Frankfort, KY 40602

RECEIVED

APR 13 2005

PUBLIC SERVICE
COMMISSION

RE: Hardin County Water District No. 2
Bond Refunding

Case No. 2005-00158

Dear Ms O'Donnell:

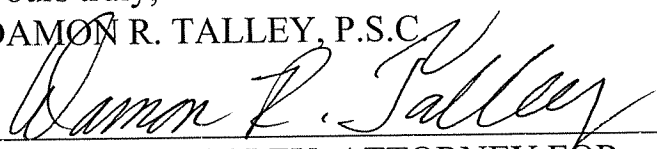
Enclosed are the original and ten (10) copies of the Application of the Hardin County Water District No. 2 to issue securities pursuant to KRS 278.300 for the purpose of refunding certain high interest Bonds of the Applicant.

No rate increase will be required.

The tentative closing date is **May 17, 2005.**

Should you need any additional information, please let me know.

Yours truly,
DAMON R. TALLEY, P.S.C.


DAMON R. TALLEY, ATTORNEY FOR
HARDIN COUNTY WATER DISTRICT
NO. 2

DRT/ms

Enclosures

cc: Hardin County Water District No. 2

COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

IN THE MATTER OF:

RECEIVED

APR 13 2005

PUBLIC SERVICE
COMMISSION

THE APPLICATION OF THE HARDIN)
COUNTY WATER DISTRICT NO. 2 TO)
ISSUE SECURITIES IN THE APPROXIMATE)
PRINCIPAL AMOUNT OF \$1,775,000 FOR)
THE PURPOSE OF ADVANCE REFUNDING)
CERTAIN OUTSTANDING REVENUE)
BONDS OF THE DISTRICT PURSUANT)
TO THE PROVISIONS OF KRS 278.300)
AND 807 KAR 5:001)

CASE NO. 2005-00158

** *** **** ***** **

APPLICATION

The Applicant, Hardin County Water District No.2, (the "District"), files this Petition and Application, pursuant to KRS 278.300, 807 KAR 5:001, and all other applicable laws and regulations, and requests that the Public Service Commission of Kentucky (the "Commission") enter an Order authorizing the District to issue certain securities in the approximate principal amount of \$1,775,000 for the purpose of refunding certain outstanding water system revenue bonds of the District. In support of the Petition and Application, and in compliance with the rules and regulations of the Commission, the District states as follows:

1. The District was established by the Order of the County Court of Hardin County entered on June 23, 1965, pursuant to the provisions of KRS Chapter 74. The District is now, and has been since its inception, regulated by the Commission, and all records and proceedings of the Commission with reference to the District are incorporated in this Application by reference.

2. The governing body of the District is its Board of Commissioners. The District is a public body corporate, with power to make contracts in furtherance of its lawful and proper purposes as provided in KRS 74.070 and all other applicable laws.

3. The mailing address of the District is as follows:

Hardin County Water District No.2
360 Ring Road
P.O. Box 970
Elizabethtown, KY 42702
Attn: Barry DeWitt, Manager
Telephone: (270) 737-1056

4. A general description of the District's water system property, together with a statement of the original cost, is contained in the District's Annual Report for 2004 which is on file with the Commission. The Annual Report is incorporated herein by reference.

5. The District proposes to issue new securities, to be designated as Water System Refunding Revenue Bonds, Series 2005B (the "2005B Bonds"), in the principal amount of \$1,785,000 for the purpose of currently refunding the unrefunded

portion of the following revenue bonds:

Water System Revenue Bonds, 1995 Series A in the outstanding principal amount of \$1,680,000 (the "1995A Bonds") which bear interest at rates ranging from 5.50% to 5.90% per annum.

6. The actual Debt Service Schedule for the proposed 2005B Bonds is shown in **Exhibit 1**, which is attached hereto and incorporated herein by reference. **Exhibit 1** also shows the actual coupon rate for each maturity and the actual average coupon rate. **Exhibit 1** was prepared after competitive bids for the proposed 2005B Bonds were received on April 12, 2005. Consequently, **Exhibit 1** reflects the actual interest rates and the actual Debt Service Schedule for the proposed 2005B Bonds. The 2005B Bonds were sold pursuant to public advertisement soliciting competitive bids according to Kentucky law.

7. As shown in **Exhibit 1**, the proposed 2005B Bonds will bear interest at a rate of 4.10 %.

8. The issuance of the 2005B Bonds will provide the District with the funds necessary: (a) to allow it to currently refund the unrefunded portion of the 1995A Bonds; and (b) to pay the fees and expenses incident to the issuance of the 2005B Bonds.

9. The Sources and Uses of the funds to be obtained from the issuance of the 2005B Bonds are detailed in **Exhibit 2**, which is attached hereto and incorporated herein by reference.

10. The proposed refinancing of the 1995A Bonds will result in total gross savings of approximately \$299,119 and a net present value savings of \$126,794. This represents a net present value savings of approximately 7.55%. These savings are shown in the Gross Debt Service Comparison schedule, which is attached hereto and incorporated herein by reference as **Exhibit 3**.

11. The Debt Service Schedule of the 1995A Bonds which are being currently refunded is set forth in **Exhibit 4**, which is attached hereto and incorporated herein by reference.

12. The District represents that the issuance of the 2005B Bonds will be in the public interest and is intended to accomplish the purpose of strengthening the financial condition of the District by producing substantial debt service savings. This is a lawful object within the corporate purposes of the District's utility operations. The issuance of the 2005B Bonds is necessary, appropriate for, and consistent with the proper performance by the District of its service to the public and will not impair its ability to perform that service.

13. The District represents that it will, as soon as reasonably possible after the issuance of the 2005B Bonds, file with the Commission a statement setting forth the date of issuance of the 2005B Bonds, the price paid, the fees and expenses incurred in the issuance of the 2005B Bonds, and the terms and interest rates of the 2005B Bonds.

14. The detailed Income Statement and Balance Sheet for the twelve (12) month period ending on December 31, 2004 are attached hereto and incorporated herein by reference as **Exhibits 5 and 6** respectively.

15. The remaining financial schedules and other information necessary for the Financial Exhibit required by 807 KAR 5:001, Section 6 and Section 11 (2) (a) are contained in the 2004 Annual Report which is on file with the Commission. The Annual Report is incorporated herein by reference.

16. Pursuant to KAR 5:001, the District hereby states as follows:

- A. Section 6(4) Mortgages: The District does not have any mortgages in effect as of the date hereof;
- B. Section 6(5) Bonds: The 2005B Bonds will be secured by a pledge of the revenues of the District's System;
- C. Section 11(2)(b): The District does not have any trust deeds in effect as of the date hereof; and
- D. Section 11(2)(c): No property is being acquired as the proceeds of the securities are being used for the purpose of currently refunding the unrefunded portion of the 1995A Bonds.

17. A copy of the District's audited financial statements for the years ended December 31, 2004 and 2003 is attached hereto and incorporated herein by reference as **Exhibit 7**.

18. The District hereby requests and moves for a deviation, pursuant to 807 KAR 5:001, Section 14, from the requirements of 807 KAR 5:001, Section 6, which requires that the financial data filed with the Application be for a twelve (12) month period ending within ninety (90) days of the filing of the Application. The District states that there has been no material change in the financial condition or operation of the District since December 31, 2004. The financial data filed with this Application is for the twelve (12) month period ending December 31, 2004. This is the most recent published financial data available. Because of the volatility of the bond market, the District cannot run the risk of delaying the sale of the 2005B Bonds while more current financial data is compiled. The current, favorable market conditions could disappear overnight.

19. The District believes that the financial information submitted with this Application is sufficient to enable the Commission to adequately, effectively and efficiently review this Application to issue securities.

20. The sale of the proposed 2005B Bonds was held on April 12, 2005, and the closing is tentatively scheduled for **May 17, 2005**.

21. No rate adjustment will be necessary.

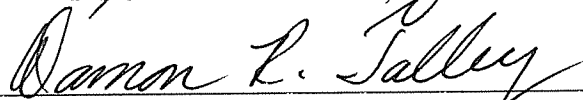
WHEREFORE, the District respectfully requests that the Commission take the following actions:

1. Place this Application to issue securities at the head of the docket as provided by KRS 278.300(2);
2. Authorize the issuance of the securities requested in the Application prior to the proposed closing date of **May 17, 2005**;
3. Grant the District a deviation, to the extent necessary, from 807 KAR 5:001, Section 6 to allow the submission of the District's Audit for the twelve (12) month period ending December 31, 2004 in lieu of more recent financial data; and
4. Process this Application without a formal hearing in order to save time and expense. The District will promptly respond to any inquiries or information requests by the Commission's staff.

This April 12, 2005.

Respectfully submitted,
HARDIN COUNTY WATER
DISTRICT NO. 2

BY: 
MICHAEL L. BELL, CHAIRMAN


DAMON R. TALLEY, P.S.C.
Counsel for Applicant
P.O. Box 150
Hodgenville, KY 42748-0150
(270) 358-3187 FAX (270) 358-9560

COMMONWEALTH OF KENTUCKY)
) SS:
COUNTY OF HARDIN)

The undersigned, MICHAEL L. BELL, being first duly sworn, deposes and states that he is the Chairman of the Commission of the Hardin County Water District No. 2 of Hardin County and LaRue County Kentucky; that he has read the foregoing Application and has noted the contents thereof; and that the statements of fact set forth therein are true and correct.

IN TESTIMONY WHEREOF, witness the signature of the undersigned on this April 12, 2005.

HARDIN COUNTY WATER
DISTRICT NO. 2

BY: 
MICHAEL L. BELL, CHAIRMAN

Subscribed and sworn to before me by Michael L. Bell, in his capacity as Chairman of the Commission of the Hardin County Water District No. 2, on this April 12, 2005.


NOTARY PUBLIC, STATE AT LARGE

MY COMMISSION EXPIRES: 6-9-07

EXHIBIT LIST

1. DEBT SERVICE SCHEDULE FOR 2005B BONDS
2. SOURCES AND USES FOR 2005B BONDS
3. GROSS DEBT SERVICE COMPARISON
(2005B AND PRIOR BONDS BEING REFUNDED)
4. DEBT SERVICE SCHEDULE FOR 1995A BONDS BEING
REFUNDED
5. INCOME STATEMENT
6. BALANCE SHEET
7. 2004 AUDIT

Hardin County (Kentucky)

Water District #2

Water System Refunding Revenue Bonds,
Series 2005B**EXHIBIT 1****Debt Service Schedule**

Part 1 of 2

Date	Principal	Coupon	Interest	Total P+I	Fiscal Total
05/17/2005	-	-	-	-	-
07/01/2005	-	-	18,193.75	18,193.75	-
12/31/2005	-	-	-	-	18,193.75
01/01/2006	55,000.00	4.100%	36,387.50	91,387.50	-
07/01/2006	-	-	35,260.00	35,260.00	-
12/31/2006	-	-	-	-	126,647.50
01/01/2007	50,000.00	4.100%	35,260.00	85,260.00	-
07/01/2007	-	-	34,235.00	34,235.00	-
12/31/2007	-	-	-	-	119,495.00
01/01/2008	55,000.00	4.100%	34,235.00	89,235.00	-
07/01/2008	-	-	33,107.50	33,107.50	-
12/31/2008	-	-	-	-	122,342.50
01/01/2009	55,000.00	4.100%	33,107.50	88,107.50	-
07/01/2009	-	-	31,980.00	31,980.00	-
12/31/2009	-	-	-	-	120,087.50
01/01/2010	60,000.00	4.100%	31,980.00	91,980.00	-
07/01/2010	-	-	30,750.00	30,750.00	-
12/31/2010	-	-	-	-	122,730.00
01/01/2011	65,000.00	4.100%	30,750.00	95,750.00	-
07/01/2011	-	-	29,417.50	29,417.50	-
12/31/2011	-	-	-	-	125,167.50
01/01/2012	70,000.00	4.100%	29,417.50	99,417.50	-
07/01/2012	-	-	27,982.50	27,982.50	-
12/31/2012	-	-	-	-	127,400.00
01/01/2013	75,000.00	4.100%	27,982.50	102,982.50	-
07/01/2013	-	-	26,445.00	26,445.00	-
12/31/2013	-	-	-	-	129,427.50
01/01/2014	80,000.00	4.100%	26,445.00	106,445.00	-
07/01/2014	-	-	24,805.00	24,805.00	-
12/31/2014	-	-	-	-	131,250.00
01/01/2015	85,000.00	4.100%	24,805.00	109,805.00	-
07/01/2015	-	-	23,062.50	23,062.50	-
12/31/2015	-	-	-	-	132,867.50
01/01/2016	85,000.00	4.100%	23,062.50	108,062.50	-
07/01/2016	-	-	21,320.00	21,320.00	-
12/31/2016	-	-	-	-	129,382.50
01/01/2017	90,000.00	4.100%	21,320.00	111,320.00	-
07/01/2017	-	-	19,475.00	19,475.00	-
12/31/2017	-	-	-	-	130,795.00
01/01/2018	95,000.00	4.100%	19,475.00	114,475.00	-
07/01/2018	-	-	17,527.50	17,527.50	-
12/31/2018	-	-	-	-	132,002.50
01/01/2019	105,000.00	4.100%	17,527.50	122,527.50	-

Hardin County (Kentucky)

Water District #2

Water System Refunding Revenue Bonds,
Series 2005B

Debt Service Schedule

Part 2 of 2

Date	Principal	Coupon	Interest	Total P+I	Fiscal Total
07/01/2019	-	-	15,375.00	15,375.00	-
12/31/2019	-	-	-	-	137,902.50
01/01/2020	105,000.00	4.100%	15,375.00	120,375.00	-
07/01/2020	-	-	13,222.50	13,222.50	-
12/31/2020	-	-	-	-	133,597.50
01/01/2021	115,000.00	4.100%	13,222.50	128,222.50	-
07/01/2021	-	-	10,865.00	10,865.00	-
12/31/2021	-	-	-	-	139,087.50
01/01/2022	120,000.00	4.100%	10,865.00	130,865.00	-
07/01/2022	-	-	8,405.00	8,405.00	-
12/31/2022	-	-	-	-	139,270.00
01/01/2023	130,000.00	4.100%	8,405.00	138,405.00	-
07/01/2023	-	-	5,740.00	5,740.00	-
12/31/2023	-	-	-	-	144,145.00
01/01/2024	135,000.00	4.100%	5,740.00	140,740.00	-
07/01/2024	-	-	2,972.50	2,972.50	-
12/31/2024	-	-	-	-	143,712.50
01/01/2025	145,000.00	4.100%	2,972.50	147,972.50	-
12/31/2025	-	-	-	-	147,972.50
Total	\$1,775,000.00	-	\$878,476.25	\$2,653,476.25	-

Yield Statistics

Accrued Interest from 04/01/2005 to 05/17/2005	9,299.03
Bond Year Dollars	\$21,426.25
Average Life	12.071 Years
Average Coupon	4.100000%
Net Interest Cost (NIC)	4.2656846%
True Interest Cost (TIC)	4.3264953%
Bond Yield for Arbitrage Purposes	4.2124882%
All Inclusive Cost (AIC)	4.7969111%

IRS Form 8038

Net Interest Cost	4.2259885%
Weighted Average Maturity	11.943 Years

Hardin County (Kentucky)

Water District #2

Water System Refunding Revenue Bonds,
Series 2005B

EXHIBIT 2

Sources & Uses

Dated 04/01/2005 | Delivered 05/17/2005

Sources Of Funds

Par Amount of Bonds	\$1,775,000.00
Release from DSR Fund	39,042.86
1995A Sinking Fund Accruals	57,557.30
Accrued Interest from 04/01/2005 to 05/17/2005	9,299.03
Total Sources	\$1,880,899.19

Uses Of Funds

Deposit to Current Refunding Fund	1,761,351.19
Hilliard Lyons	20,000.00
Ogden, Newell & Welch	20,000.00
Damon Talley	20,000.00
Original Issue Discount (OID)	17,750.00
Total Underwriter's Discount (1.000%)	17,750.00
Deposit to Debt Service Fund	9,299.03
Rounding Amount	4,198.97
Moody's	4,000.00
Paying Agent	3,750.00
Ogden, Newell & Welch (expenses)	2,500.00
Escrow Agent	300.00
Total Uses	\$1,880,899.19

Note: (1) The release from the Debt Service Reserve equals the current DSR requirement of \$1,255,499.60 less the DSR after issuance of the 2005 refunding (\$1,216,456.74), for a net release of \$39,042.86.

Hardin County (Kentucky)

Water District #2

Water System Refunding Revenue Bonds,

Series 2005B

EXHIBIT 3**Gross Debt Service Comparison**

Date	Principal	Coupon	Interest	New D/S	OLD D/S	Savings
12/31/2005	-	-	18,193.75	18,193.75	49,068.75	30,875.00
12/31/2006	55,000.00	-	71,647.50	126,647.50	137,037.50	10,390.00
12/31/2007	50,000.00	-	69,495.00	119,495.00	134,837.50	15,342.50
12/31/2008	55,000.00	-	67,342.50	122,342.50	137,500.00	15,157.50
12/31/2009	55,000.00	-	65,087.50	120,087.50	135,013.75	14,926.25
12/31/2010	60,000.00	-	62,730.00	122,730.00	137,365.00	14,635.00
12/31/2011	65,000.00	-	60,167.50	125,167.50	139,383.75	14,216.25
12/31/2012	70,000.00	-	57,400.00	127,400.00	141,062.50	13,662.50
12/31/2013	75,000.00	-	54,427.50	129,427.50	142,421.25	12,993.75
12/31/2014	80,000.00	-	51,250.00	131,250.00	143,455.00	12,205.00
12/31/2015	85,000.00	-	47,867.50	132,867.50	144,177.50	11,310.00
12/31/2016	85,000.00	-	44,382.50	129,382.50	144,605.00	15,222.50
12/31/2017	90,000.00	-	40,795.00	130,795.00	144,737.50	13,942.50
12/31/2018	95,000.00	-	37,002.50	132,002.50	144,575.00	12,572.50
12/31/2019	105,000.00	-	32,902.50	137,902.50	148,970.00	11,067.50
12/31/2020	105,000.00	-	28,597.50	133,597.50	147,922.50	14,325.00
12/31/2021	115,000.00	-	24,087.50	139,087.50	151,432.50	12,345.00
12/31/2022	120,000.00	-	19,270.00	139,270.00	154,352.50	15,082.50
12/31/2023	130,000.00	-	14,145.00	144,145.00	156,682.50	12,537.50
12/31/2024	135,000.00	-	8,712.50	143,712.50	158,422.50	14,710.00
12/31/2025	145,000.00	-	2,972.50	147,972.50	159,572.50	11,600.00
Total	\$1,775,000.00	-	\$878,476.25	\$2,653,476.25	\$2,952,595.00	\$299,118.75

PV Analysis Summary (Gross to Gross)

Gross PV Debt Service Savings	209,895.84
Accrued Interest Credit to Debt Service Fund	9,299.03
Transfers from Prior Issue Debt Service Fund	(1,255,499.60)
Transfers from Prior Issue DSR Fund	(57,557.30)
Amount deposited into new DSR Fund	1,216,456.74
Contingency or Rounding Amount	4,198.97
Net Present Value Benefit	\$126,793.68
Net PV Benefit / \$1,680,000 Refunded Principal	7.547%
Net PV Benefit / \$1,775,000 Refunding Principal	7.143%

Refunding Bond Information

Refunding Dated Date	4/01/2005
Refunding Delivery Date	5/17/2005

Hardin County (Kentucky)

Water District #2

Water System Refunding Revenue Bonds,
Series 1995A (1985 Bonds only) rounded nearest**EXHIBIT 4****Total Refunded Debt Service**

Part 1 of 2

Date	Principal	Coupon	Interest	Total P+i	Fiscal Total
07/01/2005	-	-	49,068.75	49,068.75	-
12/31/2005	-	-	-	-	49,068.75
01/01/2006	40,000.00	5.500%	49,068.75	89,068.75	-
07/01/2006	-	-	47,968.75	47,968.75	-
12/31/2006	-	-	-	-	137,037.50
01/01/2007	40,000.00	5.500%	47,968.75	87,968.75	-
07/01/2007	-	-	46,868.75	46,868.75	-
12/31/2007	-	-	-	-	134,837.50
01/01/2008	45,000.00	5.500%	46,868.75	91,868.75	-
07/01/2008	-	-	45,631.25	45,631.25	-
12/31/2008	-	-	-	-	137,500.00
01/01/2009	45,000.00	5.550%	45,631.25	90,631.25	-
07/01/2009	-	-	44,382.50	44,382.50	-
12/31/2009	-	-	-	-	135,013.75
01/01/2010	50,000.00	5.600%	44,382.50	94,382.50	-
07/01/2010	-	-	42,982.50	42,982.50	-
12/31/2010	-	-	-	-	137,365.00
01/01/2011	55,000.00	5.750%	42,982.50	97,982.50	-
07/01/2011	-	-	41,401.25	41,401.25	-
12/31/2011	-	-	-	-	139,383.75
01/01/2012	60,000.00	5.800%	41,401.25	101,401.25	-
07/01/2012	-	-	39,661.25	39,661.25	-
12/31/2012	-	-	-	-	141,062.50
01/01/2013	65,000.00	5.850%	39,661.25	104,661.25	-
07/01/2013	-	-	37,760.00	37,760.00	-
12/31/2013	-	-	-	-	142,421.25
01/01/2014	70,000.00	5.900%	37,760.00	107,760.00	-
07/01/2014	-	-	35,695.00	35,695.00	-
12/31/2014	-	-	-	-	143,455.00
01/01/2015	75,000.00	5.900%	35,695.00	110,695.00	-
07/01/2015	-	-	33,482.50	33,482.50	-
12/31/2015	-	-	-	-	144,177.50
01/01/2016	80,000.00	5.900%	33,482.50	113,482.50	-
07/01/2016	-	-	31,122.50	31,122.50	-
12/31/2016	-	-	-	-	144,605.00
01/01/2017	85,000.00	5.900%	31,122.50	116,122.50	-
07/01/2017	-	-	28,615.00	28,615.00	-
12/31/2017	-	-	-	-	144,737.50
01/01/2018	90,000.00	5.900%	28,615.00	118,615.00	-
07/01/2018	-	-	25,960.00	25,960.00	-
12/31/2018	-	-	-	-	144,575.00
01/01/2019	100,000.00	5.900%	25,960.00	125,960.00	-
07/01/2019	-	-	23,010.00	23,010.00	-

Hardin County (Kentucky)

Water District #2

Water System Refunding Revenue Bonds,

Series 1995A (1985 Bonds only) rounded nearest

Total Refunded Debt Service

Part 2 of 2

Date	Principal	Coupon	Interest	Total P+i	Fiscal Total
12/31/2019	-	-	-	-	148,970.00
01/01/2020	105,000.00	5.900%	23,010.00	128,010.00	-
07/01/2020	-	-	19,912.50	19,912.50	-
12/31/2020	-	-	-	-	147,922.50
01/01/2021	115,000.00	5.900%	19,912.50	134,912.50	-
07/01/2021	-	-	16,520.00	16,520.00	-
12/31/2021	-	-	-	-	151,432.50
01/01/2022	125,000.00	5.900%	16,520.00	141,520.00	-
07/01/2022	-	-	12,832.50	12,832.50	-
12/31/2022	-	-	-	-	154,352.50
01/01/2023	135,000.00	5.900%	12,832.50	147,832.50	-
07/01/2023	-	-	8,850.00	8,850.00	-
12/31/2023	-	-	-	-	156,682.50
01/01/2024	145,000.00	5.900%	8,850.00	153,850.00	-
07/01/2024	-	-	4,572.50	4,572.50	-
12/31/2024	-	-	-	-	158,422.50
01/01/2025	155,000.00	5.900%	4,572.50	159,572.50	-
12/31/2025	-	-	-	-	159,572.50
Total	\$1,680,000.00	-	\$1,272,595.00	\$2,952,595.00	-

Yield Statistics

Average Life	12.625 Years
Weighted Average Maturity (Par Basis)	12.497 Years
Average Coupon	5.8843028%

Refunding Bond Information

Refunding Dated Date	4/01/2005
Refunding Delivery Date	5/17/2005

HARDIN COUNTY WATER DISTRICT NO. 2

EXHIBIT 5

STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS

YEARS ENDED DECEMBER 31, 2004 AND 2003

	2004	2003
OPERATING REVENUES:		
Water sales	\$ 6,065,406	\$ 5,745,272
Other operating income	303,259	253,485
	6,368,665	5,998,757
TOTAL OPERATING REVENUES		
OPERATING EXPENSES:		
Power and water purchased	314,427	246,688
Pumping and treatment labor	319,546	247,749
Purification supplies and expense	313,624	323,633
Transmission and distribution labor	565,239	524,279
Transmission and distribution supplies and expense	518,976	502,943
Transmission and distribution maintenance and repairs	74,118	82,295
Equipment rental	1,055	1,089
Transportation expense	108,334	78,910
Water treatment maintenance and expense	91,488	74,456
General and administrative expenses	1,370,656	1,237,777
Depreciation	1,016,269	983,638
	4,693,732	4,303,457
TOTAL OPERATING EXPENSES		
OPERATING INCOME	1,674,933	1,695,300
NON-OPERATING REVENUES (EXPENSES):		
Interest income	284,790	299,534
Gain (loss) on disposal of asset	28,972	(78,669)
Interest expense on long-term debt	(873,569)	(989,917)
Interest expense on customer deposits	(8,875)	(7,526)
Amortization of bond discount and expense	(185,207)	(153,724)
	(753,889)	(930,302)
TOTAL NON-OPERATING REVENUES (EXPENSES)		
CAPITAL CONTRIBUTIONS	821,264	2,476,532
CHANGE IN NET ASSETS	1,742,308	3,241,530
NET ASSETS, beginning of year	22,597,389	19,355,859
NET ASSETS, end of year	\$ 24,339,697	\$ 22,597,389

See accompanying notes to financial statements.

HARDIN COUNTY WATER DISTRICT NO. 2

STATEMENTS OF NET ASSETS

EXHIBIT 6

DECEMBER 31, 2004 AND 2003

<u>ASSETS</u>	<u>2004</u>	<u>2003</u>
CURRENT ASSETS:		
Cash and cash equivalents	\$ 4,894,827	\$ 5,038,128
Accounts receivable, net	455,843	487,863
Prepaid insurance	32,810	26,522
State grants receivable	-	27,580
Tap fees receivable	36,434	36,349
Inventory	606,360	153,989
TOTAL CURRENT ASSETS	6,026,274	5,770,431
NONCURRENT ASSETS:		
Restricted cash and cash equivalents	6,349,577	5,924,177
Loan receivable	44,000	-
Capital assets:		
Land	532,983	532,983
Constuction in progress	3,679,091	3,275,258
Buildings and equipment	41,004,305	40,094,597
Less: accumulated depreciation	(10,360,495)	(9,344,226)
TOTAL NONCURRENT ASSETS	41,249,461	40,482,789
TOTAL ASSETS	47,275,735	46,253,220
 <u>LIABILITIES</u>		
CURRENT LIABILITIES:		
Accounts payable	341,264	177,114
Accrued taxes	22,616	17,450
Accrued liabilities	27,308	20,744
Accrued vacation	6,134	5,400
Accrued interest	-	32,823
Customer deposits	47,406	50,144
Customer advances for construction	35,000	35,000
Notes payable	-	733,881
Bonds payable	985,000	976,823
TOTAL CURRENT LIABILITIES	1,464,728	2,049,379
NONCURRENT LIABILITIES:		
Customer deposits	426,657	451,297
Accrued vacation	55,246	48,523
Customer advances for construction	653,739	746,356
Notes payable	700,000	700,000
Bonds payable	20,963,500	20,764,299
Less: bond discount and deferred amount on refundings	(1,327,832)	(1,104,023)
TOTAL NONCURRENT LIABILITIES	21,471,310	21,606,452
TOTAL LIABILITIES	22,936,038	23,655,831
 <u>NET ASSETS</u>		
Invested in capital assets, net of related debt	13,535,216	12,487,632
Restricted for debt service	2,414,829	3,210,075
Unrestricted	8,389,652	6,899,682
TOTAL NET ASSETS	\$ 24,339,697	\$ 22,597,389

See accompanying notes to financial statements.

EXHIBIT 7

HARDIN COUNTY WATER DISTRICT NO. 2

INDEPENDENT AUDITOR'S REPORT ON FINANCIAL
STATEMENTS AND SUPPLEMENTARY INFORMATION

YEARS ENDED DECEMBER 31, 2004 AND 2003



STILES, CARTER & ASSOCIATES, P.S.C.
CERTIFIED PUBLIC ACCOUNTANTS

HARDIN COUNTY WATER DISTRICT NO. 2

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YEARS ENDED DECEMBER 31, 2004 AND 2003

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INDEPENDENT AUDITOR'S REPORT

Board of Commissioners
Hardin County Water District No. 2
Elizabethtown, Kentucky

We have audited the accompanying basic financial statements of Hardin County Water District No. 2 as of and for the years ended December 31, 2004 and 2003, as listed in the Table of Contents. These basic financial statements are the responsibility of the District's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Hardin County Water District No. 2, as of December 31, 2004 and 2003, and its changes in financial position and cash flows 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 a report dated March 3, 2005, on our consideration of Hardin County Water District No. 2's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, 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 audits.

Management's Discussion and Analysis on pages 3 through 7 is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

Our audits were performed for the purpose of forming an opinion on the basic financial statements taken as a whole. The accompanying Schedules I through III are presented for purposes of additional analysis and are not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audits of the financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

Stiles, Carter & Associates

Certified Public Accountants

March 3, 2005

HARDIN COUNTY WATER DISTRICT NO. 2
MANAGEMENT'S DISCUSSION AND ANALYSIS (MD&A)
YEAR ENDED DECEMBER 31, 2004

The discussion and analysis of Hardin County Water District No. 2's financial performance provides an overall review of the District's financial activities for the year ended December 31, 2004. The intent of this discussion and analysis is to review the District's financial performance as a whole. Readers should also review the basic financial statements and notes to the basic financial statements to enhance their understanding of the District's financial performance.

The Management's Discussion and Analysis (MD&A) is an element of the new reporting model adopted by the Governmental Accounting Standards Board (GASB) in the Statement No. 34 *Basic Financial Statements-and Management's Discussion and Analysis-for State and Local Governments* issued in June 1999.

FINANCIAL HIGHLIGHTS

- The ending cash balance for the District was \$11.2 million. The balance at December 31, 2003, was \$10.9 million. This reflects an increase in cash during the year of \$300 thousand.
- The District neared completion its work on the Phase I Waterline Extension Project. The District also continued construction on its Phase II Waterline Extension Project and continued in the planning process for its Phase III Waterline Extension Project. The District began the planning on its Phase IV and V Waterline Extension Projects.
- The District invested approximately \$1.3 million in capital assets during the year.
- The District issued \$2.94 million in 2004 Series Refunding Revenue bonds to partially advance refund the outstanding principal of the 1995A bond issue. The refunding reduced the District's total debt service payments over the next 20 years by \$418 thousand and resulted in a net present value savings of \$295 thousand. The District also issued the 2002A bonds to convert its rural development loan for the Phase I project to permanent financing.

USING THIS ANNUAL REPORT

The basic financial statements report information about the District using full accrual accounting methods as utilized by similar business activities in the private sector. The basic financial statements include a balance sheet; a statement of revenues, expenses, and changes in net assets; a statement of cash flows; and notes to the basic financial statements.

The *statement of net assets* presents the financial position of the District on a full accrual historical cost basis. The statement presents information on all of the District's assets and liabilities, with the difference reported as net assets. Over time, increases and decreases in net assets are one indicator of whether the financial position of the District is improving or deteriorating.

While the statement of net assets provides information about the nature and amount of resources and obligations at year-end, the *statement of revenues, expenses, and changes in net assets* presents the results of the business activities over the course of the fiscal year and information as to how the net assets changed during the year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of the related cash flows. This statement also provides certain information about the District's recovery of its costs. Rate setting policies use different methods of cost recovery not fully provided for by generally accepted accounting principles. The primary objectives of the rate model are to improve equity among customer classes and to ensure that capital costs are allocated on the basis of long-term capacity needs, ensuring that growth pays for growth.

The *statement of cash flows* presents changes in cash and cash equivalents, resulting from operational, financing, and investing activities. This statement presents cash receipts and cash disbursement information, without consideration of the earnings event, when an obligation arises, or depreciation of capital assets.

The *notes to the basic financial statements* provide required disclosures and other information that are essential to a full understanding of material data provided in the statements. The notes present information about the District's accounting policies, significant account balances and activities, material risks, obligations, commitments, contingencies and subsequent events, if any.

ENTITY-WIDE FINANCIAL ANALYSIS

Net assets may serve over time as a useful indicator of a government's financial position. In the case of the District, assets exceeded liabilities by \$24.3 and \$22.5 million as of December 31, 2004 and 2003.

The largest portion of the District's net assets reflects its investment in infrastructure and capital assets (e.g., land, buildings, vehicles, equipment, transmission and distribution systems and construction in progress), less any related debt used to acquire those assets that is outstanding. The District uses these capital assets to provide services to its customers; consequently, these assets are not available for future spending. Although the District's investment in its capital assets is reported net of related debt, it should be noted that the resources needed to repay this debt must be provided from other sources, since the capital assets themselves cannot be used to liquidate these liabilities.

The District's financial position is the product of several financial transactions including the net results of activities, the acquisition and payment of debt, the acquisition and disposal of capital assets, and the depreciation of capital assets.

(Table 1)
Summary of Net Assets
as of December 31, 2004 and 2003

	<u>2004</u>	<u>2003</u>
Assets		
Current and		
Other Assets	\$ 12,419,851	\$ 11,694,608
Capital Assets	34,855,884	34,558,612
Total Assets	<u>47,275,735</u>	<u>46,253,220</u>
Liabilities		
Long-term liabilities	21,471,310	21,606,452
Other Liabilities	1,464,728	2,049,379
Total Liabilities	<u>22,936,038</u>	<u>23,655,831</u>
Net Assets		
Invested in capital assets, net of related debt	13,535,216	12,487,632
Restricted for debt service	2,414,829	3,210,075
Unrestricted	8,389,652	6,899,682
Total Net Assets	<u>\$ 24,339,697</u>	<u>\$ 22,597,389</u>

Unrestricted net assets, the portion of net assets that can be used to finance day-to-day operations (without constraints established by debt covenants, enabling legislation or other legal requirements), increased by 21.6% from \$6.9 million to \$8.4 million at December 31, 2004. Restricted net assets decreased \$795 thousand (24.8%). Investment in governmental capital assets, net of related debt increased by \$1.1 million (8.4%).

(Table 2)
Changes in Net Assets
Years Ended December 31, 2004 and 2003

	2004	2003
OPERATING REVENUES:		
Water sales	\$ 6,065,406	\$ 5,745,272
Other operating income	303,259	253,485
Total operating revenues	<u>6,368,665</u>	<u>5,998,757</u>
OPERATING EXPENSES:		
Power and water purchased	314,427	246,688
Pumping and treatment labor	319,546	247,749
Purification supplies and expense	313,624	323,633
Transmission and distribution labor	565,239	524,279
Transmission and distribution supplies and expense	518,976	502,943
Transmission and distribution maintenance and repairs	74,118	82,295
Equipment rental	1,055	1,089
Transportation expense	108,334	78,910
Water treatment maintenance and expense	91,488	74,456
General and administrative expenses	1,370,656	1,237,777
Depreciation	1,016,269	983,638
Total operating expenses	<u>4,693,732</u>	<u>4,303,457</u>
OPERATING INCOME	1,674,933	1,695,300
NON-OPERATING REVENUES (EXPENSES)		
Interest income	284,790	299,534
Gain (loss) on disposal of asset	28,972	(78,669)
Interest expense on long-term debt	(873,569)	(989,917)
Interest expense on customer deposits	(8,875)	(7,526)
Amortization of bond discount and expense	(185,207)	(153,724)
TOTAL NON-OPERATING REVENUES (EXPENSES)	(753,889)	(930,302)
Capital contributions	<u>821,264</u>	<u>2,476,532</u>
Increase in net assets	<u>\$ 1,742,308</u>	<u>\$ 3,241,530</u>

Operating revenue increased 6.2% compared to the prior year. Operating expenses increased 9.1%. The primary increase is due to payroll expenses, health insurance, and depreciation. Interest expense on long-term debt decreased by 11.7%, which is a result of the District's refunding of bonds in prior years and the current year to obtain more favorable interest rates. The bond discount amortization increased due to the deferred amount on refundings that is being written off on the 2002B, 2002C, 2003 and 2004A Series bonds. The District continues to receive capital contributions through the State of Kentucky, counties the District works with and individual developers.

Capital Assets and Debt Administration

Capital Assets

At December 31, 2004 and 2003, the District had \$34.9 million and \$34.6 million invested in a variety of capital assets, as reflected in the following table:

(Table 3)
Capital Assets (Net of Depreciation)
 as of December 31, 2004 and 2003

	2004	2003
Non-Depreciable Assets:		
Land and land rights	\$ 532,983	\$ 532,983
Depreciable Assets:		
Structures and improvements	2,674,826	2,706,742
Supply mains	1,235,357	1,279,456
Water treatment plant	9,161,302	9,383,332
Standpipes, tanks and foundations	4,516,391	4,652,648
Transmission and distribution mains	10,496,879	10,543,903
Services	1,970,051	1,622,930
Hydrants	41,197	31,830
Office furniture and fixtures	77,847	102,048
Transportation equipment	356,170	263,893
Communication equipment	2,741	4,053
Other property and equipment	111,049	159,536
Capital assets in service	31,176,793	31,283,354
Construction in progress	3,679,091	3,275,258
Total capital assets, net of depreciation	<u>\$ 34,855,884</u>	<u>\$ 34,558,612</u>

(Table 4)
Changes in Capital Assets
 Years Ended December 31, 2004 and 2003

	2004	2003
Beginning balance	\$ 34,558,612	\$ 32,487,324
Additions	1,313,541	3,133,595
Retirements	-	(78,669)
Depreciation	(1,016,269)	(983,638)
Ending balance	<u>\$ 34,855,884</u>	<u>\$ 34,558,612</u>

Construction was nearly completed on the Phase I Waterline Extension Project and continued on the Phase II Waterline Extension Project. Also, planning began on the Phase III and Phase III Waterline Extension Projects. These unfinished project costs are in construction in progress at December 31, 2004.

Debt

At December 31, 2004 and 2003, the District had \$22.6 million and \$23.2 million, in bonds and notes outstanding. A total of \$985 thousand is due within the 2004 calendar year.

(Table 5)
Outstanding Debt
 as of December 31, 2004 and 2003

	<u>2004</u>	<u>2003</u>
Revenue bonds	\$ 21,948,500	\$ 21,741,122
Notes	<u>700,000</u>	<u>1,433,881</u>
Total	<u>\$ 22,648,500</u>	<u>\$ 23,175,003</u>

The District partially advance refunded \$2.94 million of its 1995A bonds with the 2004A bond issue and issued the 2002A bonds for \$1.013 million to convert its Phase I rural development loan to permanent financing.

District Challenges for the Future

The District continues to be financially sound. However, the current state and national financial climate requires the District to remain prudent. The State of Kentucky has experienced a shortfall in revenue for the 2002-2004 biennium. The state's response to this shortfall has been to reduce expenditures.

The District will continue to use careful planning and monitoring of finances to provide quality services to its customers.

Contacting the District's Financial Management

This financial report is designed to provide our customers, investors and creditors with a general overview of the District's finances and to show the District's accountability for the money it receives and spends. If you have questions about this report or need additional financial information, contact Barry DeWitt, General Manager, 360 Ring Road, Elizabethtown, Kentucky 42701, (270) 737-1056.

HARDIN COUNTY WATER DISTRICT NO. 2

STATEMENTS OF NET ASSETS

DECEMBER 31, 2004 AND 2003

<u>ASSETS</u>	<u>2004</u>	<u>2003</u>
CURRENT ASSETS:		
Cash and cash equivalents	\$ 4,894,827	\$ 5,038,128
Accounts receivable, net	455,843	487,863
Prepaid insurance	32,810	26,522
State grants receivable	-	27,580
Tap fees receivable	36,434	36,349
Inventory	606,360	153,989
TOTAL CURRENT ASSETS	6,026,274	5,770,431
NONCURRENT ASSETS:		
Restricted cash and cash equivalents	6,349,577	5,924,177
Loan receivable	44,000	-
Capital assets:		
Land	532,983	532,983
Constuction in progress	3,679,091	3,275,258
Buildings and equipment	41,004,305	40,094,597
Less: accumulated depreciation	(10,360,495)	(9,344,226)
TOTAL NONCURRENT ASSETS	41,249,461	40,482,789
TOTAL ASSETS	47,275,735	46,253,220
<u>LIABILITIES</u>		
CURRENT LIABILITIES:		
Accounts payable	341,264	177,114
Accrued taxes	22,616	17,450
Accrued liabilities	27,308	20,744
Accrued vacation	6,134	5,400
Accrued interest	-	32,823
Customer deposits	47,406	50,144
Customer advances for construction	35,000	35,000
Notes payable	-	733,881
Bonds payable	985,000	976,823
TOTAL CURRENT LIABILITIES	1,464,728	2,049,379
NONCURRENT LIABILITIES:		
Customer deposits	426,657	451,297
Accrued vacation	55,246	48,523
Customer advances for construction	653,739	746,356
Notes payable	700,000	700,000
Bonds payable	20,963,500	20,764,299
Less: bond discount and deferred amount on refundings	(1,327,832)	(1,104,023)
TOTAL NONCURRENT LIABILITIES	21,471,310	21,606,452
TOTAL LIABILITIES	22,936,038	23,655,831
<u>NET ASSETS</u>		
Invested in capital assets, net of related debt	13,535,216	12,487,632
Restricted for debt service	2,414,829	3,210,075
Unrestricted	8,389,652	6,899,682
TOTAL NET ASSETS	\$ 24,339,697	\$ 22,597,389

See accompanying notes to financial statements.

HARDIN COUNTY WATER DISTRICT NO. 2

STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS

YEARS ENDED DECEMBER 31, 2004 AND 2003

	<u>2004</u>	<u>2003</u>
OPERATING REVENUES:		
Water sales	\$ 6,065,406	\$ 5,745,272
Other operating income	303,259	253,485
TOTAL OPERATING REVENUES	<u>6,368,665</u>	<u>5,998,757</u>
OPERATING EXPENSES:		
Power and water purchased	314,427	246,688
Pumping and treatment labor	319,546	247,749
Purification supplies and expense	313,624	323,633
Transmission and distribution labor	565,239	524,279
Transmission and distribution supplies and expense	518,976	502,943
Transmission and distribution maintenance and repairs	74,118	82,295
Equipment rental	1,055	1,089
Transportation expense	108,334	78,910
Water treatment maintenance and expense	91,488	74,456
General and administrative expenses	1,370,656	1,237,777
Depreciation	1,016,269	983,638
TOTAL OPERATING EXPENSES	<u>4,693,732</u>	<u>4,303,457</u>
OPERATING INCOME	1,674,933	1,695,300
NON-OPERATING REVENUES (EXPENSES):		
Interest income	284,790	299,534
Gain (loss) on disposal of asset	28,972	(78,669)
Interest expense on long-term debt	(873,569)	(989,917)
Interest expense on customer deposits	(8,875)	(7,526)
Amortization of bond discount and expense	(185,207)	(153,724)
TOTAL NON-OPERATING REVENUES (EXPENSES)	<u>(753,889)</u>	<u>(930,302)</u>
CAPITAL CONTRIBUTIONS	<u>821,264</u>	<u>2,476,532</u>
CHANGE IN NET ASSETS	1,742,308	3,241,530
NET ASSETS, beginning of year	<u>22,597,389</u>	<u>19,355,859</u>
NET ASSETS, end of year	<u>\$ 24,339,697</u>	<u>\$ 22,597,389</u>

See accompanying notes to financial statements.

HARDIN COUNTY WATER DISTRICT NO. 2

STATEMENTS OF CASH FLOWS

YEARS ENDED DECEMBER 31, 2004 AND 2003

	2004	2003
CASH FLOWS FROM OPERATING ACTIVITIES:		
Receipts from customers	\$ 6,400,685	\$ 5,846,220
Payments to suppliers	(2,438,483)	(1,529,313)
Payments to employees	(1,501,761)	(1,348,055)
NET CASH PROVIDED BY OPERATING ACTIVITIES	2,460,441	2,968,852
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES:		
Principal payments on bonds	(3,745,622)	(4,926,208)
Principal payments on notes	(823,687)	-
Acquisition of capital assets	(1,298,541)	(1,816,755)
Contribution in aid of construction	474,157	1,128,018
Interest on long-term debt	(921,236)	(989,917)
Bond proceeds	3,953,000	4,485,000
Grant proceeds	333,431	192,117
Issuance of loan receivable	(44,000)	-
Bond issuance costs	(510,099)	(310,567)
Note proceeds	89,807	163,871
Sale of capital assets	28,972	-
Customer deposit interest	(8,875)	(7,523)
NET CASH USED BY CAPITAL AND RELATED FINANCING ACTIVITIES	(2,472,693)	(2,081,964)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchase of investments	(2,788,864)	(3,734,334)
Proceeds from investments	2,798,425	3,810,092
Interest income	284,790	299,534
NET CASH PROVIDED BY INVESTING ACTIVITIES	294,351	375,292
NET INCREASE IN CASH AND CASH EQUIVALENTS	282,099	1,262,180
CASH AND CASH EQUIVALENTS, beginning of year	10,962,305	9,700,125
CASH AND CASH EQUIVALENTS, end of year	\$ 11,244,404	\$ 10,962,305
SUPPLEMENTAL DISCLOSURES OF CASH FLOWS INFORMATION:		
Interest paid during the year	\$ 930,111	\$ 997,440
RECONCILIATION OF OPERATING INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES:		
Operating income	\$ 1,674,933	\$ 1,695,300
Adjustments to reconcile net operating income to net cash provided by operating activities:		
Depreciation	1,016,269	983,638
Bad debts	40,000	-
Decrease in accounts receivable	32,020	55,948
(Increase) in prepaid insurance	(6,288)	(4,613)
(Increase) in tap fees receivable	(85)	(7,100)
Increase in accounts payable	164,150	168,583
Increase (decrease) in customer deposits	(27,378)	53,734
Increase in accrued taxes payable	5,166	1,043
(Increase) decrease in inventory	(452,371)	17,994
Increase in other current payables	6,564	4,148
Increase in accrued vacation	7,461	177
NET CASH PROVIDED BY OPERATING ACTIVITIES	\$ 2,460,441	\$ 2,968,852

See accompanying notes to financial statements.

HARDIN COUNTY WATER DISTRICT NO. 2NOTES TO FINANCIAL STATEMENTSYEARS ENDED DECEMBER 31, 2004 AND 2003

Brief history - The Hardin County Water District No. 2 was organized pursuant to the provisions of Kentucky Revised Statutes KRS 74.010 and KRS 44.020 in order to provide a water supply for the residents of Hardin County, Kentucky.

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIESBasis of Accounting

The District's financial statements are presented in accordance with the accrual basis of accounting. As allowed in Section P80 of Governmental Accounting Standards Board's (GASB) Codification of Governmental Accounting and Financial Reporting Standards, the District has elected not to apply to its proprietary activities Financial Accounting Standards Board Statements and Interpretations, Accounting Principles Board Opinions, and Accounting Research Bulletins of the Committee of Accounting Procedure issued after November 30, 1989. The District follows the accounting policies and procedures set forth by the National Association of Regulatory Utility Commissioners and the guidance provided by the American Water Works Association in *Water Utility Accounting*.

All activities of the District are accounted for within a single proprietary (enterprise) fund. Proprietary funds are used to account for operations that are (a) financed and operated in a manner similar to private business enterprises where the intent of the governing body is that the cost (expenses, including depreciation) of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges; or (b) where the governing body has decided that periodic determination of revenues earned, expenses incurred, and/or net income is appropriate for capital maintenance, public policy, management control, accountability, or other purposes.

The accounting and financial reporting treatment applied to the District is determined by its measurement focus. The transactions of the District are accounted for on a flow of economic resources measurement focus. With this measurement focus, all assets and all liabilities associated with the operations are included on the balance sheet. Net assets (i.e., total assets net of total liabilities) are segregated into "invested in capital assets, net of related liabilities"; "restricted for capital activity and debt service"; and "unrestricted" components.

- (1) Accounts Receivable - The allowance method is used to record uncollectible accounts. At December 31, 2004 and 2003, accounts receivable was stated net of an allowance for uncollectible accounts of \$120,000 and \$80,000. Bad debt expense for the years ended December 31, 2004 and 2003 was \$40,000 and \$-0-. The District does not believe there is any credit risk associated with these receivables due to the large customer base and small individual account balances.
- (2) Inventory - Inventory is composed of equipment and supply type items used for routine maintenance and repairs. Inventory is stated at the lower of cost (first-in, first-out method) or market.
- (3) Restricted Assets - Restricted assets consist of demand deposit savings accounts and certificates of deposit plus accrued interest. The cost basis approximates market value.

(Continued next page)

HARDIN COUNTY WATER DISTRICT NO. 2NOTES TO FINANCIAL STATEMENTSYEARS ENDED DECEMBER 31, 2004 AND 2003

- (4) Property and Equipment - Property, plant and equipment in service and construction in progress are recorded at cost, if purchased or constructed. Assets acquired through contributions from developers or other customers are capitalized at their estimated fair market value, if available, or at engineers' estimated fair market value or cost to construct at the date of the contribution. Maintenance and repairs, which do not significantly extend the value or life of property, plant and equipment, are expensed as incurred.

Assets are depreciated on the straight-line method. Depreciation is calculated using the following estimated useful lives:

	<u>Years</u>
Source of supply equipment	15-50
Water treatment plant	10-40
Transmission and distribution systems	10-50
Equipment	3-20
Structures and improvements, including buildings	10-50
Office furniture, equipment and vehicles	3-20
Meters	10-20

- (5) Amortization - Bond discounts, expenses and deferred amounts on refundings are being amortized using the straight-line method over the life of each respective bond issue.
- (6) Cash Equivalents - For purposes of the statements of cash flows, the District considers cash on deposit and certificates of deposit to be cash equivalents.
- (7) Compensation for Future Absences - Accumulated vacation to be paid to employees is recorded as an expense and liability as the benefit is earned.
- (8) Claims and Judgments - These events and obligations are recorded on the accrual basis, when the event occurs and the obligation arises.
- (9) Revenues and Rate Structure - Revenues from water services are recognized on the accrual basis and as earned. Services are supplied to customers under a rate structure designed to produce revenues sufficient to provide for operating and maintenance costs, capital outlay, debt service, reserves and debt service coverage.
- (10) Capital Contributions - Contributions are recognized in the Statement of Revenues, Expenses and Changes in Net Assets when earned. Contributions include capacity fees, capital grants, and other supplemental support by other utilities and industrial customers and federal, state and local grants in support of system improvements.
- (11) Long-term obligations are reported at face value, net of applicable premiums and discounts. Premiums and discounts, issuance costs, and gains or losses on advance refundings and defeasances are deferred and amortized over the life of the bonds.
- (12) Restricted assets are used to fund appropriations only after unrestricted resources are depleted except for appropriations related to a project/debt requirement for which the assets are restricted.

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HARDIN COUNTY WATER DISTRICT NO. 2NOTES TO FINANCIAL STATEMENTSYEARS ENDED DECEMBER 31, 2004 AND 2003

- (13) Net Assets - Net assets comprise the various net earnings from operating and non-operating revenues, expenses and contributions of capital. Net assets are classified in the following three components: invested in capital assets, net of related liabilities; restricted for debt service; and unrestricted net assets. Invested in capital assets, net of related debt, consists of all capital assets, net of accumulated depreciation and reduced by outstanding debt that is attributable to the acquisition, construction and improvement of those assets; debt related to unspent proceeds or other restricted cash and investments is excluded from the determination. Restricted for debt service consists of net assets for which constraints are placed thereon by external parties, such as lenders, grantors, contributors, laws, regulations and enabling legislation, including self-imposed legal mandates, less any related liabilities. Unrestricted consists of all other net assets not included in the above categories.
- (14) Use of Estimates - The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect reported amounts of assets, liabilities, net assets, and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenditures during the reporting period. Actual results could differ from those estimates.

NOTE B - TAP FEES RECEIVABLE

The District has entered into short-term notes receivable with a portion of its customers for tap fees related to the Phase I, Phase II and Phase III Water Line Projects. The notes are scheduled to be collected during the 2004 calendar year. The balances at December 31, 2004 and 2003 were \$36,434 and \$36,349.

NOTE C - NOTE RECEIVABLE

On October 14, 2004, the District agreed to loan the Lincoln Trail Regional Water Commission up to \$50,000 at an annual interest rate of 3%. At December 31, 2004, the outstanding balance was \$44,000. The note matures October 14, 2006 and is collateralized by water sales to Fort Knox, Hardin County Water District No. 1 and the City of Muldraugh.

NOTE D - DEPOSITS

The District's deposits are categorized to give an indication of the level of risk assumed by the District at December 31, 2004 and 2003. The categories are described as follows:

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

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

Category 3 - Uncollateralized, including any bank balance that is collateralized with securities held by the pledging financial institution, or by its trust department or agent but not in the entity's name.

(Continued next page)

HARDIN COUNTY WATER DISTRICT NO. 2

NOTES TO FINANCIAL STATEMENTS

YEARS ENDED DECEMBER 31, 2004 AND 2003

The following schedules represent the District's deposits at December 31, 2004 and 2003:

December 31, 2004

NON-POOLED DEPOSITS	CATEGORY			BANK
	1	2	3	BALANCES
Revenue fund	\$ 540,043	\$ -	\$ -	\$ 540,043
Operation and maintenance	4,354,142	-	-	4,354,142
Other operating funds	102,671	-	-	102,671
Customer deposit fund	540,338	-	-	540,338
Bond funds	1,657,461	757,367	-	2,414,828
Depreciation fund	414,616	-	-	414,616
Escrow accounts	100,231	-	-	100,231
Construction accounts	2,922,661	-	-	2,922,661
	<u>\$ 10,632,163</u>	<u>\$ 757,367</u>	<u>\$ -</u>	<u>\$ 11,389,530</u>

December 31, 2003

NON-POOLED DEPOSITS	CATEGORY			BANK
	1	2	3	BALANCES
Revenue fund	\$ 466,546	\$ -	\$ -	\$ 466,546
Operation and maintenance	4,462,045	-	-	4,462,045
Other operating funds	45,190	-	-	45,190
Customer deposit fund	526,572	-	-	526,572
Bond funds	2,344,601	895,716	-	3,240,317
Depreciation fund	427,536	-	-	427,536
Escrow accounts	97,344	-	-	97,344
Construction accounts	1,717,264	4,789	-	1,722,053
	<u>\$ 10,087,098</u>	<u>\$ 900,505</u>	<u>\$ -</u>	<u>\$ 10,987,603</u>

The carrying balances at December 31, 2004 and 2003 were \$11,244,404, and \$10,962,305.

NOTE E - RESTRICTED CASH

The District has restricted cash for various purposes including debt service, future construction and customer deposits. The following schedule represents restricted cash at December 31, 2004 and 2003:

<u>Restricted For</u>	<u>December 31, 2004</u>	<u>December 31, 2003</u>
Debt service	\$ 2,414,829	\$ 3,210,075
Depreciation fund	405,993	431,136
Escrow	99,434	95,113
Construction	2,922,213	1,668,635
Customer deposits	507,108	519,218
	<u>\$ 6,349,577</u>	<u>\$ 5,924,177</u>

(Continued next page)

HARDIN COUNTY WATER DISTRICT NO. 2

NOTES TO FINANCIAL STATEMENTS

YEARS ENDED DECEMBER 31, 2004 AND 2003

NOTE F - CAPITAL ASSETS

Capital assets are recorded at cost.

Capital asset activity for the year ended December 31, 2004 follows.

	Balance at December 31, 2003	Additions	Retirements	Balance at December 31, 2004
Non-Depreciable Assets:				
Land and land rights	\$ 532,983	\$ -	\$ -	\$ 532,983
Depreciable Assets:				
Structures and improvements	3,115,387	47,000	-	3,162,387
Supply mains	1,763,965	-	-	1,763,965
Water treatment plant	10,983,191	-	-	10,983,191
Standpipes, tanks and foundations	5,450,253	-	-	5,450,253
Transmission and distribution mains	14,651,158	248,482	-	14,899,640
Services	2,507,934	415,008	-	2,922,942
Hydrants	173,327	15,087	-	188,414
Office furniture and fixtures	342,761	6,264	-	349,025
Transportation equipment	664,695	177,867	-	842,562
Communication equipment	58,962	-	-	58,962
Other property and equipment	382,964	-	-	382,964
Capital assets in service	40,627,580	909,708	-	41,537,288
Construction in progress	3,275,258	403,833	-	3,679,091
Total capital assets	43,902,838	1,313,541	-	45,216,379
Less accumulated depreciation for:				
Structures and improvements	408,645	78,916	-	487,561
Supply mains	484,509	44,099	-	528,608
Water treatment plant	1,599,859	222,030	-	1,821,889
Standpipes, tanks and foundations	797,605	136,257	-	933,862
Transmission and distribution mains	4,107,255	295,506	-	4,402,761
Services	885,004	67,887	-	952,891
Hydrants	141,497	5,721	-	147,218
Office furniture and fixtures	240,713	30,465	-	271,178
Transportation equipment	400,802	85,590	-	486,392
Communication equipment	54,909	1,312	-	56,221
Other property and equipment	223,428	48,486	-	271,914
Total accumulated depreciation	9,344,226	1,016,269	-	10,360,495
Net capital assets	\$ 34,558,612	\$ 297,272	\$ -	\$ 34,855,884

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HARDIN COUNTY WATER DISTRICT NO. 2NOTES TO FINANCIAL STATEMENTSYEARS ENDED DECEMBER 31, 2004 AND 2003

Capital asset activity for the year ended December 31, 2003 follows.

	Balance at December 31, 2002	Additions	Retirements	Balance at December 31, 2003
Non-Depreciable Assets:				
Land and land rights	\$ 482,839	\$ 50,144	\$ -	\$ 532,983
Depreciable Assets:				
Structures and improvements	2,886,135	229,252	-	3,115,387
Supply mains	1,763,965	-		1,763,965
Water treatment plant	10,953,605	29,586		10,983,191
Standpipes, tanks and foundations	5,517,510	56,550	(123,807)	5,450,253
Transmission and distribution mains	14,240,043	411,115		14,651,158
Services	2,357,927	150,007		2,507,934
Hydrants	173,327	-		173,327
Office furniture and fixtures	324,966	17,795		342,761
Transportation equipment	650,011	14,684		664,695
Communication equipment	58,962	-		58,962
Other property and equipment	233,178	149,786		382,964
Capital assets in service	39,642,468	1,108,919	(123,807)	40,627,580
Construction in progress	1,250,582	2,024,676	-	3,275,258
Total capital assets	40,893,050	3,133,595	(123,807)	43,902,838
Less accumulated depreciation for:				
Structures and improvements	335,976	72,669	-	408,645
Supply mains	440,410	44,099	-	484,509
Water treatment plant	1,380,245	219,614	-	1,599,859
Standpipes, tanks and foundations	704,799	137,944	(45,138)	797,605
Transmission and distribution mains	3,818,345	288,910	-	4,107,255
Services	824,180	60,824	-	885,004
Hydrants	136,530	4,967	-	141,497
Office furniture and fixtures	206,004	34,709	-	240,713
Transportation equipment	324,659	76,143	-	400,802
Communication equipment	53,597	1,312	-	54,909
Other property and equipment	180,981	42,447	-	223,428
Total accumulated depreciation	8,405,726	983,638	(45,138)	9,344,226
Net capital assets	\$ 32,487,324	\$ 2,149,957	\$ (78,669)	\$ 34,558,612

During the years ended December 31, 2004 and 2003, the District capitalized \$14,844 and \$23,935 of interest and expensed \$882,444 and \$997,443.

NOTE G - LONG-TERM OBLIGATIONS

The construction cost of the District's water facilities have been financed by issuance of revenue bonds authorized under Kentucky Revised Statutes and a long-term note with the City of Elizabethtown. All assets of the District are pledged as collateral for these bonds. Information relating to the outstanding bond issues is summarized below:

Issue Date	Interest Rate	Face Amount of Each Issue	Bonds Due 12/31/04	Bonds Due 12/31/03
1994 Series B	5.6%-5.7%	\$5,135,000	\$ 265,000	\$ 515,000
1995 Series A	5.5%-5.9%	4,940,000	1,680,000	4,350,000
1995 KIA	5.50%	1,053,951	140,000	406,122
1999 Series A	3.7%-5.0%	7,005,000	6,655,000	6,775,000
2002 Series A	4.375%	1,013,000	1,003,500	-0-
2002 Series B	1.75%-3.5%	2,190,000	1,935,000	2,190,000
2002 Series C	2.0%-3.75%	3,020,000	2,980,000	3,020,000
2003 Series	3.5%-4.625%	4,485,000	4,350,000	4,485,000
2004 Series A	2.0% - 4.0%	2,940,000	2,940,000	-0-

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HARDIN COUNTY WATER DISTRICT NO. 2

NOTES TO FINANCIAL STATEMENTS

YEARS ENDED DECEMBER 31, 2004 AND 2003

On January 8, 2002, the District entered into an agreement with the City of Elizabethtown, Kentucky, to borrow the sum of \$700,000 for construction of water lines. The note is non-interest bearing and is due and payable on or before two years from the date of the note. The note is automatically renewed at maturity for two additional years unless the Water District notifies the City in writing thirty days prior to the maturity date. At the end of the renewal period, the note is automatically renewed for one year unless the Water District notifies the City in the manner previously mentioned. The Water District may make installment payments or pay the entire loan at any time. No payments were made during 2004 or 2003.

The District requires new customers to provide a \$60 deposit for initial water service.

Full-time employees of the District are entitled to paid vacation and paid personal days depending upon length of service. Personal days must be used within the calendar year earned. Vacation days may be carried forward.

Customers' advances for construction are payments by customers to extend water lines to areas not presently served by the District. These funds are repaid by refunding a percentage of future service connection fees collected by the District.

Long-term liability activity for the year ended December 31, 2004, was as follows:

	Balance at December 31, 2003	Additions	Reductions	Balance at December 31, 2004	Amount Due Within One Year
Bonds and notes payable:					
Revenue bonds	\$ 21,741,122	\$ 3,953,000	\$ (3,745,622)	\$ 21,948,500	\$ 985,000
Notes payable	1,433,881	89,806	(823,687)	700,000	-
Total bonds and notes payable	23,175,003	4,042,806	(4,569,309)	22,648,500	985,000
Other liabilities:					
Customer deposits	501,441	51,960	(79,338)	474,063	47,406
Accrued vacation	53,923	7,457	-	61,380	6,134
Customer advances for construction	781,356	20,500	(113,117)	688,739	35,000
Total other liabilities	1,336,720	79,917	(192,455)	1,224,182	88,540
Long-term liabilities	\$ 24,511,723	\$ 4,122,723	\$ (4,761,764)	\$ 23,872,682	\$ 1,073,540

Long-term liability activity for the year ended December 31, 2003, was as follows:

	Balance at December 31, 2002	Additions	Reductions	Balance at December 31, 2003	Amount Due Within One Year
Bonds and notes payable:					
Revenue bonds	\$ 22,182,330	\$ 4,485,000	\$ (4,926,208)	\$ 21,741,122	\$ 976,823
Notes payable	1,275,715	158,166	-	1,433,881	733,881
Total bonds and notes payable	23,458,045	4,643,166	(4,926,208)	23,175,003	1,710,704
Other liabilities:					
Customer deposits	447,707	113,520	(59,786)	501,441	50,144
Accrued vacation	53,746	177	-	53,923	5,400
Customer advances for construction	793,950	21,909	(34,503)	781,356	35,000
Total other liabilities	1,295,403	135,606	(94,289)	1,336,720	90,544
Long-term liabilities	\$ 24,753,448	\$ 4,778,772	\$ (5,020,497)	\$ 24,511,723	\$ 1,801,248

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HARDIN COUNTY WATER DISTRICT NO. 2

NOTES TO FINANCIAL STATEMENTS

YEARS ENDED DECEMBER 31, 2004 AND 2003

Bond maturities and Sinking Fund requirements in each of the next five years and in five year increments thereafter are as follows at December 31, 2004:

Year	Revenue Bonds		Notes Payable		Totals
	Principal	Interest	Principal	Interest	
2005	\$ 985,000	\$ 916,016	\$ -	\$ -	\$ 1,901,016
2006	740,000	921,470	-	-	1,661,470
2007	1,050,500	892,529	-	-	1,943,029
2008	1,071,000	836,761	700,000	-	2,607,761
2009	1,091,500	779,051	-	-	1,870,551
2010-2014	4,856,500	3,311,112	-	-	8,167,612
2015-2019	2,830,000	2,562,533	-	-	5,392,533
2020-2024	3,698,000	1,826,404	-	-	5,524,404
2025-2029	2,873,500	988,468	-	-	3,861,968
2030-2034	1,871,500	355,508	-	-	2,227,008
2035-2039	720,000	108,081	-	-	828,081
2040-2044	161,000	10,675	-	-	171,675
Total	\$ 21,948,500	\$ 13,508,608	\$ 700,000	\$ -	\$ 36,157,108

Year	Sinking Fund Requirements
2005	\$ 1,901,016
2006	1,661,470
2007	1,943,029
2008	1,907,761
2009	1,870,551
2010-2014	8,167,612
2015-2019	5,392,533
2020-2024	5,524,404
2025-2029	3,861,968
2030-2034	2,227,008
2035-2039	828,081
2040-2044	171,675
Total	\$ 35,457,108

On April 8, 2004, the District issued \$2,940,000 in 2004 Series A Refunding Revenue Bonds with an average interest rate of 3.4 percent to refund \$2,635,000 of outstanding 1995 A Series bonds with an average interest rate of 4 percent. The refunding was a partial advance refunding and \$1,715,000 of the 1995 A Series bonds remained outstanding. The net proceeds of \$2,885,770 (after \$151,934 in bond discount and \$10,320 in accrued interest) plus an additional \$97,704 of sinking fund monies were used to purchase U.S. Government securities. These securities were deposited in an irrevocable trust to provide for all future debt service on the refunded portion of the 1995 Series A bonds. As a result, that portion of the 1995 Series A bonds is considered defeased and the District has removed the liability from its accounts. The outstanding principal of the defeased bonds is \$2,940,000 at December 31, 2004.

The refunding resulted in a difference between the reacquisition price and the net carrying amount of the old debt of \$351,853. This difference, reported in the accompanying financial statements as a deduction from bonds payable, is being charged to operations through the year 2024 using the effective-interest method.

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HARDIN COUNTY WATER DISTRICT NO. 2NOTES TO FINANCIAL STATEMENTSYEARS ENDED DECEMBER 31, 2004 AND 2003

The District completed the refunding to reduce its total debt service payments over the next 20 years by \$418,776 and to obtain an economic gain (difference between the present values of the old and new debt service payments) of \$294,870.

On June 7, 2004, the District issued \$1,013,000 in 2002 Series A bonds to convert its United States Department of Agriculture, Rural Development loan to permanent financing. The bonds carry an average interest rate of 4.375% and mature in annual installments through January 1, 2025.

Under covenants of the bond ordinances, certain funds have been established. These funds and their current financial requirements are presented as follows:

Revenue Fund

All receipts for services are deposited into this fund and, subsequently, disbursed into the following required funds:

Bond and Interest Redemption Funds

There is to be a monthly deposit of an amount equal to 1/12 of the next ensuing principal payment due and 1/6 of the next ensuing interest payment due for the 1994 B, 1995 Series A, 1995 KIA, 1999 Series A, 2002 Series A, B and C, 2003 Series and 2004 Series A issues.

Depreciation Fund

This fund receives, on a monthly basis, \$15,000. This fund also receives the proceeds from the sale of any property or equipment. This fund may be used to purchase new or replacement property and equipment.

Operation and Maintenance Fund

This fund receives, on a monthly basis, sufficient amounts to pay current expenses from the Revenue Fund after the above transfers have been made. This fund is used to pay operating expenditures. This account is funded until it reaches 2 months of forecasted operating expenses. Any surplus left may be added to the Bond and Interest Redemption Fund.

NOTE H - SHORT-TERM NOTES PAYABLE

On June 13, 2002, the District entered into an agreement with the Kentucky Rural Water Finance Corporation to borrow up to \$1,013,000 at 4.5% interest per annum as a short-term source of funds for construction on the Phase I Construction Project. The loan was renegotiated on October 14, 2003, for the same total principal amount with a 3.4% per annum interest rate. The total draws on the loan were during 2004 and 2003 were \$89,806 and \$158,166. The principal amount was repaid as described in Note G. The principal balance at December 31, 2003 was \$733,881. Total interest accrued during 2004 and 2003 was \$14,844 and \$23,935. Interest paid when the loan was repaid was \$47,667.

NOTE I - RETIREMENT PLAN

Plan Description - The District participates in the County Employees Retirement System (CERS), a cost-sharing multiple-employer defined benefit pension plan administered by the Kentucky Retirement System's Board of Trustees. CERS provides benefits to its participants upon retirement. CERS issues a publicly available financial report that includes financial statements and required supplementary information for the retirement plan. That report may be obtained by writing to Kentucky Retirement Systems, Perimeter Park West, 1260 Louisville Road, Frankfort, Kentucky 40601 or by calling 502-564-4646. Funding Policy - Plan members are required to contribute 5.00% of their annual covered salary and the District is required to contribute at an actuarially determined rate. The current rate is 8.48% of covered payroll. The contribution requirements of the District

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HARDIN COUNTY WATER DISTRICT NO. 2NOTES TO FINANCIAL STATEMENTSYEARS ENDED DECEMBER 31, 2004 AND 2003(CONCLUDED)

are established and may be amended by the Kentucky Retirement System's Board of Trustees. The District's contributions to CERS for the years ended December 31, 2004 and 2003 were \$112,422 and \$89,190. Employee contributions were \$72,310 and \$65,089 and covered payroll was \$1,447,338 and \$1,301,770.

NOTE J - CAPITAL CONTRIBUTIONS

The following schedule details the sources of capital contributions for the years ended December 31, 2004 and 2003:

Source	2004	2003
State of Kentucky	\$ 320,891	\$ 877,575
Tap Fees	400,674	337,525
Developers	84,699	27,949
Hardin County Fiscal Court	15,000	262,985
Hart County Fiscal Court	-	970,498
	\$ 821,264	\$ 2,476,532

NOTE K - COMMITMENTS

The District has entered into construction commitments toward its Phase I and Phase II Waterline Extension Projects. Also, the District has received certain funding commitments from federal and state agencies for current and planned construction projects.

NOTE L - RISK MANAGEMENT

The District is exposed to various risks of loss related to torts; theft of, damage to and destruction of assets; errors and omissions; and natural disasters. The City was insured for workers' compensation, general liability and automobile liability coverage under a retrospectively rated commercial policy.

NOTE M - CORRECTION OF AN ERROR

The District made an adjustment to accounts receivable and water sales revenue, for the year ended December 31, 2003, for unbilled accounts receivable that were not recorded. The effect of this correction of an error was to increase the change in net assets for the year ended December 31, 2003, by \$92,964.

OTHER SUPPLEMENTARY INFORMATION

HARDIN COUNTY WATER DISTRICT NO. 2

SCHEDULE I - BOND AND INTEREST REQUIREMENTS

YEAR ENDED DECEMBER 31, 2004

	<u>\$ 750,000</u>		<u>\$ 4,940,000</u>		<u>\$ 1,000,750</u>	
	<u>1994 SERIES B</u>		<u>1995 SERIES A</u>		<u>1995 KIA</u>	
	<u>BOND</u>	<u>INTEREST</u>	<u>BOND</u>	<u>INTEREST</u>	<u>BOND</u>	<u>INTEREST</u>
2005	\$ 265,000	\$ 7,453	\$ 35,000	\$ 99,100	\$ 40,000	\$ 24,781
2006			40,000	97,037	40,000	43,684
2007			40,000	94,837	40,000	42,334
2008			45,000	92,500	20,000	20,808
2009			45,000	90,014		
2010			50,000	87,365		
2011			55,000	84,384		
2012			60,000	81,063		
2013			65,000	77,421		
2014			70,000	73,455		
2015			75,000	69,178		
2016			80,000	64,605		
2017			85,000	59,738		
2018			90,000	54,575		
2019			100,000	48,970		
2020			105,000	42,923		
2021			115,000	36,433		
2022			125,000	29,353		
2023			135,000	21,683		
2024			145,000	13,423		
2025			155,000	4,573		
2026						
2027						
2028						
2029						
2030						
2031						
2032						
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2036						
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2038						
2039						
2040						
2041						
2042						
	<u>\$ 265,000</u>	<u>\$ 7,453</u>	<u>\$ 1,715,000</u>	<u>\$ 1,322,630</u>	<u>\$ 140,000</u>	<u>\$ 131,607</u>

(Continued next page)

HARDIN COUNTY WATER DISTRICT NO. 2

SCHEDULE I - BOND AND INTEREST REQUIREMENTS

YEAR ENDED DECEMBER 31, 2004

\$ 7,005,000 1999 SERIES A		\$ 1,013,000 2002 SERIES A		\$ 2,190,000 2002 SERIES B	
BOND	INTEREST	BOND	INTEREST	BOND	INTEREST
\$ 125,000	\$ 317,069	\$ -	\$ 21,952	\$ 250,000	\$ 55,045
130,000	311,905	10,000	43,684	255,000	49,358
140,000	306,438	10,500	43,236	270,000	42,120
145,000	300,666	11,000	42,766	275,000	33,945
150,000	294,205	11,500	42,274	285,000	25,189
155,000	287,038	12,000	41,759	295,000	15,616
165,000	279,476	12,500	41,223	305,000	5,338
170,000	271,520	13,500	40,655		
180,000	263,207	14,000	40,053		
190,000	254,420	14,500	39,430		
200,000	245,158	15,500	38,774		
210,000	235,420	16,000	38,084		
220,000	225,207	17,000	37,362		
230,000	214,520	17,500	36,608		
240,000	203,358	19,000	35,809		
250,000	191,720	19,500	34,967		
265,000	179,489	20,500	34,092		
275,000	166,526	21,500	33,173		
290,000	152,825	22,500	32,211		
305,000	138,396	24,000	31,194		
320,000	123,000	25,000	30,122		
335,000	106,625	26,500	28,995		
355,000	89,375	27,500	27,814		
375,000	71,125	29,000	26,578		
390,000	52,000	30,500	25,276		
410,000	32,000	32,000	23,909		
435,000	10,875	33,500	22,477		
		35,000	20,978		
		37,000	19,403		
		39,000	17,740		
		40,500	16,001		
		43,000	14,175		
		45,000	12,250		
		47,000	10,237		
		49,500	8,127		
		52,000	5,906		
		54,500	3,576		
		54,500	1,192		
<u>\$ 6,655,000</u>	<u>\$ 5,323,563</u>	<u>\$ 1,003,500</u>	<u>\$ 1,064,062</u>	<u>\$ 1,935,000</u>	<u>\$ 226,611</u>

(Continued next page)

HARDIN COUNTY WATER DISTRICT NO. 2SCHEDULE I - BOND AND INTEREST REQUIREMENTSYEAR ENDED DECEMBER 31, 2004(CONCLUDED)

<u>\$ 3,020,000</u>		<u>\$ 4,485,000</u>		<u>\$ 2,940,000</u>	
<u>2002 SERIES C</u>		<u>2003 SERIES A</u>		<u>2004 SERIES A</u>	
<u>BOND</u>	<u>INTEREST</u>	<u>BOND</u>	<u>INTEREST</u>	<u>BOND</u>	<u>INTEREST</u>
\$ 45,000	\$ 100,073	\$ 130,000	\$ 180,796	\$ 90,000	\$ 102,295
45,000	99,060	130,000	176,246	90,000	100,495
320,000	93,698	130,000	171,696	95,000	98,170
330,000	83,947	145,000	166,884	100,000	95,245
345,000	73,391	145,000	161,809	105,000	92,170
350,000	61,922	145,000	156,643	105,000	89,020
365,000	49,673	160,000	151,015	110,000	85,795
380,000	36,445	75,000	146,609	115,000	82,420
395,000	22,396	80,000	143,703	115,000	78,826
405,000	7,594	80,000	140,703	125,000	74,926
		85,000	137,609	125,000	70,708
		90,000	134,283	135,000	66,158
		95,000	130,650	145,000	61,113
		95,000	126,779	155,000	55,563
		100,000	122,733	160,000	49,575
		105,000	118,479	170,000	43,140
		110,000	114,018	175,000	36,413
		115,000	109,349	190,000	29,200
		120,000	104,263	200,000	21,400
		130,000	98,638	215,000	13,100
		135,000	92,675	220,000	4,400
		140,000	86,488		
		145,000	80,075		
		155,000	73,325		
		165,000	66,022		
		170,000	58,275		
		180,000	50,181		
		190,000	41,625		
		200,000	32,606		
		110,000	25,438		
		115,000	20,234		
		120,000	14,800		
		125,000	9,134		
		135,000	3,122		
<u>\$ 2,980,000</u>	<u>\$ 628,199</u>	<u>\$ 4,350,000</u>	<u>\$ 3,446,905</u>	<u>\$ 2,940,000</u>	<u>\$ 1,350,132</u>

HARDIN COUNTY WATER DISTRICT NO. 2SCHEDULE II - GENERAL AND ADMINISTRATIVE EXPENSESYEARS ENDED DECEMBER 31, 2004 AND 2003

	<u>2004</u>	<u>2003</u>
Salaries	\$ 586,583	\$ 545,342
Commissioner's salaries	30,392	30,861
Employee benefits	313,224	277,685
Materials and supplies	64,421	60,426
Professional fees	16,200	16,450
Insurance	135,459	138,136
Advertising	3,994	4,598
Bad debts	40,000	-
Other general and administrative	180,383	164,279
	<u>\$ 1,370,656</u>	<u>\$ 1,237,777</u>

HARDIN COUNTY WATER DISTRICT NO. 2SCHEDULE III - ORGANIZATION DATADECEMBER 31, 2004WATER COMMISSIONERS

Michael Bell - Chairman
Coleman Crady - Secretary/Treasurer
Garland Carter - Member
Cordell Tabb - Member
John Effinger - Member

ATTORNEY

Damon R. Talley - Hodgenville, Kentucky

CALENDAR YEAR

January 1 to December 31

INTERNAL CONTROL AND FISCAL COMPLIANCE

THEODORE C. STILES, CPA
BENJAMIN E. CARTER, CPA
JOHN R. ASHCRAFT, CPA
J. SCOTT KISSELBAUGH, CPA
BRIAN S. WOOSLEY, CPA
CHRIS R. CARTER, CPA
CHERYLE L. BEAUCHAMP, CPA
J. ALTON PIKE, CPA



STILES, CARTER & ASSOCIATES, P.S.C.

CERTIFIED PUBLIC ACCOUNTANTS

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INDEPENDENT AUDITOR'S 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

Board of Commissioners
Hardin County Water District No. 2
Elizabethtown, Kentucky

We have audited the financial statements of the Hardin County Water District No. 2, as of and for the year ended December 31, 2004, and have issued our report thereon dated March 3, 2005. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered Hardin County Water District No. 2's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide an opinion on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be material weaknesses. A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Hardin County Water District No. 2'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 that are required to be reported under *Government Auditing Standards*.

This report is intended solely for the information and use of the commissioners, management, federal agencies, and the Kentucky Public Service Commission and is not intended to be and should not be used by anyone other than those specified parties.

Shiles, Carter & Associates

Certified Public Accountants

March 3, 2005

THEODORE C. STILES, CPA
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Board of Commissioners
Hardin County Water District No. 2
Elizabethtown, Kentucky

We have audited the basic financial statements of Hardin County Water District No. 2 as of and for the year ended December 31, 2004 and have issued our report thereon dated March 3, 2005. Professional standards require that we provide you with the following information related to our audit.

Our responsibility under auditing standards generally accepted in the United States of America and the standards applicable to financial statement audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States

As stated in our engagement letter dated February 7, 2005, our responsibility, as described by professional standards, is to plan and perform our audit to obtain reasonable, but not absolute, assurance about whether the basic financial statements are free of material misstatement and are fairly presented in accordance with accounting principles generally accepted in the United States of America. Because an audit is designed to provide reasonable, but not absolute, assurance and because we did not perform a detailed examination of all transactions, there is a risk that material errors, fraud or illegal acts may exist and not be detected by us.

In planning and performing our audit, we considered the District's internal control over financial reporting in order to determine our audit procedures for the purpose of expressing our opinion on the basic financial statements and not to provide assurance on the internal control over financial reporting.

As part of obtaining reasonable assurance about whether the District's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, grant agreements and other matters. However, the objective of our tests was not to provide an opinion on compliance with such provisions.

Significant Accounting Policies

Management has the responsibility for selection and use of appropriate accounting policies. In accordance with the terms of our engagement letter, we will advise management about the appropriateness of accounting policies and their application. The significant accounting policies used by the District are described in Note A to the financial statements. We noted no transactions entered into by the District during the year that were both significant and unusual, and of which, under professional standards, we are required to inform you, or transactions which there is a lack of authoritative guidance or consensus.

Accounting Estimates

Accounting estimates are an integral part of the financial statements prepared by management and are based on management's knowledge and experience about past and current events and assumptions about future events. Certain

accounting estimates are particularly sensitive because of their significance to the financial statements and because of the possibility that future events affecting them may differ significantly from those expected. The most sensitive estimate affecting the financial statements was the allowance for doubtful accounts.

Significant Audit Adjustments

For purposes of this letter, professional standards define a significant audit adjustment as a proposed correction of the financial statements that, in our judgment, may not have been detected except through our auditing procedures. An audit adjustment may or may not indicate matters that could have a significant effect on the District's financial reporting process (that is, cause future financial statements to be materially misstated). The audit adjustments, in our judgment, do not indicate matters that could have a significant effect on the District's financial reporting process. In addition, management has made all adjustments proposed by us.

Disagreements With Management

For purposes of this letter, professional standards define a disagreement with management as a matter, whether or not resolved to our satisfaction, concerning a financial accounting, reporting, or auditing matter that could be significant to the financial statements or the auditor's report. There have been no disagreements during the course of our audit.

Consultations With Other Independent Accountants

In some cases, management may decide to consult with other accountants about auditing and accounting matters. If a consultation involves application of an accounting principle to the

District's financial statements or a determination of the type of auditor's opinion that may be expressed on those statements, our professional standards require the consulting accountant to contact us to determine that the consultant has all the relevant facts. To our knowledge, there were no such consultations with other accountants.

Issues Discussed Prior to Retention of Independent Auditors

We generally discuss a variety of matters, including the application of accounting principles and auditing standards, with management each year prior to retention as the District's auditor. However, these discussions occurred in the normal course of our professional relationship and our responses were not a condition to our retention.

Difficulties Encountered in Performing the Audit

We encountered no significant difficulties in dealing with management in performing our audit.

This report is intended solely for the information and use of the commissioners, management, federal agencies, and the Kentucky Public Service Commission and is not intended to be and should not be used by anyone other than those specified parties.

Stiles, Carter & Associates

Certified Public Accountants

March 3, 2005

