

2007-473

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November 6, 2007

**HENRY M. REED III**  
**LOUISVILLE, KENTUCKY**

**GILLARD B. JOHNSON III**  
**LEXINGTON, KENTUCKY**

**RECEIVED**  
NOV 07 2007  
**PUBLIC SERVICE  
COMMISSION**

**VIA UPS**

Ms. Beth A. O'Donnell  
Executive Director  
Public Service Commission  
211 Sower Boulevard  
P.O. Box 615  
Frankfort, Kentucky 40602-0615

**In re: Application of Adair County Water District for Approval of Loan to District**

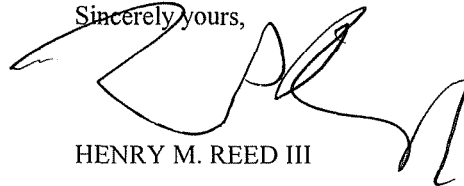
Ms. O'Donnell:

Enclosed herewith please find ten (10) copies of the Petition of the Adair County Water District seeking the Commission's approval of a Loan to the District from the Kentucky Infrastructure Authority.

I request that the Petition be filed with the Commission pursuant to the provisions of KRS 278.300.

Thank you.

Sincerely yours,



HENRY M. REED III

cc: Mr. David M. Bowles, P.E.  
Monarch Engineering, Inc.  
556 Carlton Dr.  
Lawrenceburg, Kentucky 40342

Mr. Lennon Stone, Manager  
Adair County Water District  
P.O. Box 567  
Columbia, Kentucky 42728

BEFORE THE PUBLIC SERVICE COMMISSION OF KENTUCKY

RECEIVED

NOV 07 2007

PUBLIC SERVICE COMMISSION

CASE NO.

2007-473

IN THE MATTER OF THE APPLICATION )  
OF THE ADAIR COUNTY WATER DISTRICT, A )  
WATER DISTRICT ORGANIZED PURSUANT TO )  
CHAPTER 74 OF THE KENTUCKY REVISED )  
STATUTES, IN ADAIR COUNTY, KENTUCKY, )  
FOR THE APPROVAL OF A PLAN OF FINANCING )  
IMPROVMENTS TO THE DISTRICT'S WATER )  
DISTRIBUTION SYSTEM. )

PETITION

Pursuant to KRS 278.300, this Petition of the Adair County Water District ("District" or "Petitioner"), respectfully states:

1. That Petitioner is a Water District in Adair County, created and existing under and by virtue of Chapter 74 of the Kentucky Revised Statutes, pursuant to an Order of the County Court of said County, following the requisite procedure prescribed in said Chapter 74.

2. That the Post Office address of said District is "Adair County Water District, Doug Sapp, Vice-Chairman, P.O. Box 567, Columbia, Kentucky 42728".

3. That the formation of the District, its present tariff of rates, and the issuance of its outstanding long term indebtedness have been previously approved by Orders of the Public Service Commission of Kentucky ("PSC" or "Commission").

4. That on May 16, 2007 the District filed a Petition seeking (1) a Certificate of Public Convenience and Necessity approving the construction of extensions, additions and improvements to the District's Water System, consisting of (a) 39,800 linear feet of 12-inch water line and (b) a 500,000 gallon elevated water storage tank (the "Phase I Project"), (2) approval of increased rates and charges for water service and (3) approval of the plan of financing said Phase I Project.

5. That on June 14, 2007 the Commission entered its Order granting all of the District's requests as set forth in its original Petition.

6. That the District has applied to the Kentucky Infrastructure Authority ("KIA") for a Loan in the principal amount of \$1,000,000 bearing interest at the rate of 1% per annum (the "KIA Loan") repayable over a 20-year term which it desires to apply to the construction of additional improvements as well as the Phase I Project previously approved by the Commission; said additional improvements consisting of (a) water system improvements; (b) water system extensions and; (c) radio read metering system improvements (the "Phase II Project"). The District requests a waiver from the Commission of deficiencies in Engineering data regarding the Phase II Project.

7. That the District does not now anticipate that it will let construction contracts for the Phase II Project until June of 2008, since additional engineering work and governmental approvals are required; however, the District does wish the Commission's approval for the KIA Loan, the proceeds of which Loan may be applied in part to the Phase I Project as well as the Phase II Project.

8. That the District fully understands and agrees that upon receipt of construction bids for the Phase II Project it will file with the Commission an application with necessary exhibits in order to seek a Certificate of Public Convenience and Necessity for the Phase II Project.

9. That no increase in the rates and charges for water service supplied by the District will be required as a result of the KIA Loan.

10. That there is attached hereto and made a part of this Petition an Audit of the District's financial operations for the year ending December 31, 2006. The District requests a waiver of the 90-day deficiency by the Commission for said Audit.

11. That the approval of the Public Service Commission is urgently required in order to enable the District to proceed to utilize the KIA Loan in order to provide for the needs of the District.

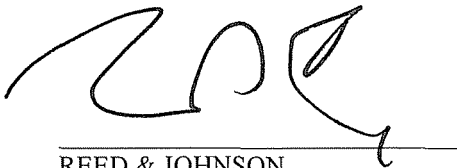
WHEREFORE, Petitioner prays that the Public Service Commission of Kentucky grant to the Petitioner the following:

An Order approving the KIA Loan in the principal amount of \$1,000,000 and the application thereof to the costs incident to the Phase I Project and the Phase II Project; all subject to the subsequent granting by the Commission of a Certificate of Public Convenience and Necessity as to the Phase II Project.

Dated at Columbia, Kentucky as of this 2 day of November, 2007.

ADAIR COUNTY WATER DISTRICT

By Doug Dapp  
Vice Chairman



REED & JOHNSON  
Henry M. Reed III, Bond Counsel  
2218 Frankfort Avenue  
Louisville, Kentucky 40206

Marshall F. Loy  
Marshall F. Loy, Esquire  
Attorney for the District  
116 Public Square  
Columbia, Kentucky 42728

STATE OF KENTUCKY            )  
                                          ) SS  
COUNTY OF ADAIR            )

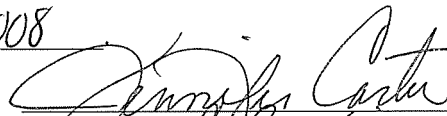
The undersigned Doug Sapp, being first duly sworn, deposes and states: That he is the Vice-Chairman of Adair County Water District of Adair County, Kentucky, Petitioner in the above Petition; that he has read the foregoing Petition and has noted the contents thereof; that the same is true of his own knowledge, except as to matters which are therein stated on information or belief, and that as to those matters, he believes same to be true.

IN TESTIMONY WHEREOF, witness the signature of the undersigned on the 2 day of November, 2007.

  
\_\_\_\_\_  
Doug Sapp

2 Acknowledged before me by Doug Sapp, Vice-Chairman of the Adair County Water District, on this day of November, 2007.

My Commission expires 2-28-2008

  
\_\_\_\_\_  
Notary Public, Columbus  
Kentucky

(Seal of Notary)

ADAIR COUNTY WATER DISTRICT

FINANCIAL STATEMENTS

For the Years Ended December 31, 2006 and 2005

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INDEPENDENT AUDITOR'S REPORT

To the Commissioners  
Adair County Water District  
Columbia, Kentucky

We have audited the accompanying financial statements of the business-type activities of and each major fund of Adair County Water District, as of and for the years then ended December 31, 2006 and 2005, which collectively comprise the Adair County Water District's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the Adair County Water District's management. Our responsibility is to express an opinion on these basic 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; the provisions of *Office of Management and Budget Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations*. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the business-type activities and each major fund of Adair County Water District, as of December 31, 2006 and 2005, 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 a report dated March 23, 2007, on our consideration of Adair County Water District's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grants. Those reports are an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

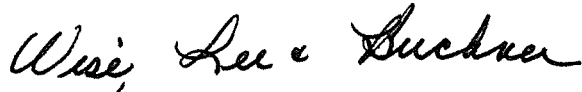
The Management's Discussion and Analysis and other required supplementary information on pages 3 through 6 and pages 19 through 21 are not a required part of the basic financial statements but are supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Adair County Water District's basic financial statements. The accompanying schedule of expenditures of federal awards on page 19 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 Adair County Water District. Such information has

To the Commissioners  
Adair County Water District  
Page 2

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 basic financial statements taken as a whole.

This report is intended for the information of the commissioners, management, United States Department of Agriculture Rural Development, federal awarding agencies, and Kentucky Public Service Commission, and is not intended to be and should not be used by anyone other than these specified parties.

A handwritten signature in cursive script that reads "Wise, Lee & Buckner".

Wise, Lee & Buckner, PLLC  
Certified Public Accountants

Campbellsville, Kentucky  
March 23, 2007





## **ADAIR COUNTY WATER DISTRICT Management's Discussion and Analysis**

This section of the Adair County Water District's annual financial report presents an analysis of the District's financial performance during the fiscal year ended December 31, 2006. This information is presented in conjunction with the audited basic financial statements, which follow.

### **Overview of the Financial Statements**

This annual report consists of the following three parts: Management's Discussion and Analysis, Basic Financial Statements and Other Required Supplementary information. The MD&A is intended to explain the significant changes in financial position and differences in operation between the current and prior years. Significant changes from the prior year are explained in the following paragraphs. The Financial Statements include notes which explain in detail some of the information included in the basic financial statements.

### **Required Financial Statements**

The Financial Statements of the District report information utilizing the full accrual basis of accounting. The Financial Statements conform to accounting principals which are generally accepted in the United States of America. The statements of Net Assets include information on the District's assets and liabilities and provide information about the nature and amounts of investments in resources (assets) and the obligations to Districts creditors (liabilities). The Statement of Revenues, Expense and Changes in Net Assets identify the District's revenues and expenses for the year ended December 31, 2006. This statement normally provides information on the District's operations and can be used to determine whether the District has recovered all of its actual and projected costs through user fees and other charges. The third financial statement is the Statements of Cash Flows. This statement provides information on the District's cash receipts, cash payments and changes in cash resulting from operations, investments and financing activities. From the Statements of Cash Flows, the reader can obtain information on the source and use of cash and the change in the cash and cash equivalents balance.

### **Financial Analysis of the District**

A condensed version of the Statement of Net Assets at December 31, 2006 and 2005 follows:

**Net Assets**

A summary of the District's Statements of Net Assets is presented below.

Condensed Statement of Net Assets

	<u>2006</u>	<u>2005</u>
Cash and Investments	\$ 1,050,729	\$ 1,139,054
Other Assets	300,179	227,285
Capital Assets	<u>12,129,711</u>	<u>11,436,522</u>
 Total Assets	 13,480,619	 12,802,861
 Current Liabilities	 121,444	 107,559
Other Liabilities	253,986	253,596
Long-Term Outstanding	<u>4,461,000</u>	<u>4,548,000</u>
 Total Liabilities	 4,836,430	 4,909,155
 Net Assets:		
Invested in Capital Assets (Net of Related Debt)	7,581,711	6,804,522
Restricted	507,678	498,086
Unrestricted	<u>554,801</u>	<u>591,098</u>
 Total Net Assets	 <u>\$ 8,644,190</u>	 <u>\$ 7,893,706</u>

**Capital Assets and Debt Administration**

Capital Assets

At December 31, 2006 the District had \$17,056,840 invested in capital assets, consisting primarily of plant and equipment. The most significant change in capital assets during the year was an increase of \$1,653,233 with the completion of Phase V construction.

Capital Assets at Year End

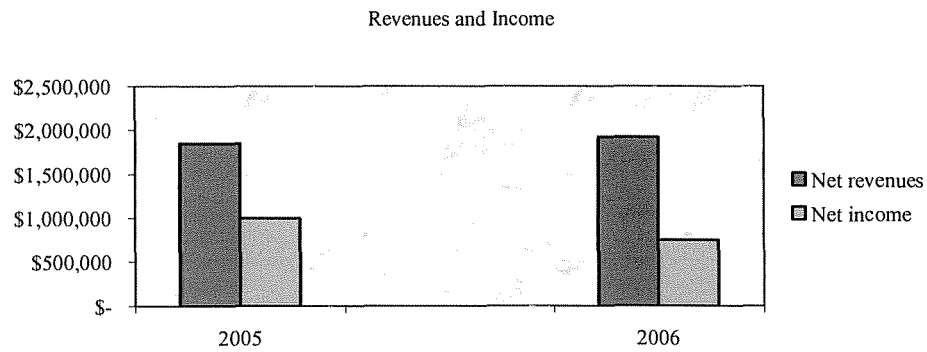
	<u>2006</u>	<u>2005</u>
Land	\$ 105,729	\$ 101,639
Construction-in-Progress	80,163	704,678
Buildings	342,827	325,746
Plant & Equipment	<u>16,528,121</u>	<u>14,858,222</u>
Subtotal	17,056,840	15,990,285
Accumulated Depreciation	<u>(4,927,129)</u>	<u>(4,553,763)</u>
Capital Assets, Net	<u>\$ 12,129,711</u>	<u>\$ 11,436,522</u>

**Revenues and Income**

A comparison of the District's revenues and net income for the years ended December 31, 2006 and 2005 is as follows:

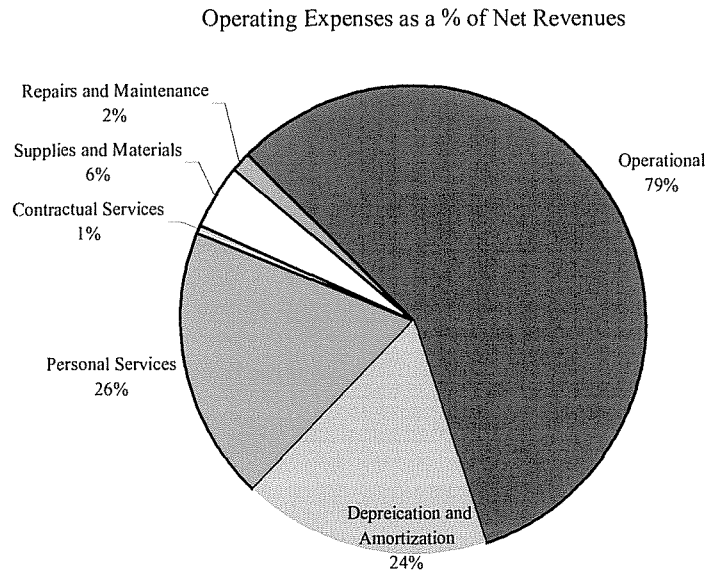
	2005	2006
Net revenues	\$ 1,844,943	\$ 1,918,701
Net income	999,017	750,483

The following graph shows the District's 2005 revenues and income in comparison to the District's 2006 revenues and income.



**Expenses as a Percentage of Revenues**

The following pie chart shows the District's expenses as a percentage of revenues.



**Debt Outstanding**

At December 31, 2006, the District had \$4,548,000 in notes outstanding versus \$4,632,000 for December 31, 2005.

**Financial Contact**

The District's financial statements are designed to provide the District's customers, commissioners, creditors and other interested parties with a general overview of the District's financial operations and financial condition. If you have questions about the report or need additional financial information, please contact the District's Manager, Lennon Stone at 270-384-2181 or 109 Grant Lane, Columbia, KY 42728.

ADAIR COUNTY WATER DISTRICT  
STATEMENT OF NET ASSETS  
December 31, 2006 and 2005

ASSETS	2006	2005
<b>CURRENT ASSETS</b>		
Cash and Cash Equivalents	\$ 269,554	\$ 380,258
Short-Term Investments	273,497	260,710
Customer & Other Accounts Receivable	197,758	151,526
Inventory	69,095	45,487
Prepaid Expenses	26,564	22,665
Interest Receivable	3,698	2,489
Total Unrestricted Current Assets	840,166	863,135
Restricted Cash and Investments	507,678	498,086
TOTAL CURRENT ASSETS	1,347,844	1,361,221
<b>NON-CURRENT ASSETS</b>		
Debt Issuance Cost (net of accumulated amortization)	3,064	5,118
Capital Assets:		
Land and Construction in Progress	185,892	806,317
Other Capital Assets (net of accumulated depreciation)	11,943,819	10,630,205
TOTAL NON-CURRENT ASSETS	12,132,775	11,441,640
TOTAL ASSETS	\$ 13,480,619	\$ 12,802,861

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

ADAIR COUNTY WATER DISTRICT  
STATEMENT OF NET ASSETS  
December 31, 2006 and 2005

	2006	2005
LIABILITIES		
CURRENT LIABILITIES		
Accounts Payable - Trade	\$ 99,762	\$ 78,610
Accrued and Withheld Taxes	3,410	12,690
Customer Deposits	11,818	11,389
Deferred Revenue	-	-
Accrued Payroll	6,453	4,870
Liabilities Payable from Restricted Assets:		
Interest Payable	166,986	169,596
Current Portion of Long-term Debt	87,000	84,000
Note Payable	-	-
TOTAL CURRENT LIABILITIES	375,429	361,155
NON-CURRENT LIABILITIES		
Long-term Liabilities (Excluding Current Portion):		
Revenue Bonds Payable	4,461,000	4,548,000
TOTAL LIABILITIES	4,836,429	4,909,155
NET ASSETS		
Invested in Capital Assets, Net of Related Debt	7,581,711	6,804,522
Restricted	507,678	498,086
Unrestricted	554,801	591,098
TOTAL NET ASSETS	8,644,190	7,893,706
TOTAL LIABILITIES AND NET ASSETS	\$ 13,480,619	\$ 12,802,861

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

ADAIR COUNTY WATER DISTRICT  
STATEMENTS OF REVENUE, EXPENSES AND CHANGES IN NET ASSETS  
Years Ended December 31, 2006 and 2005

	<u>2006</u>	<u>2005</u>
OPERATING REVENUES		
Water Sales	\$ 1,843,127	\$ 1,767,566
Service Charges and Other	<u>75,574</u>	<u>77,377</u>
TOTAL OPERATING REVENUES	1,918,701	1,844,943
OPERATING EXPENSES		
Personal Service	495,161	459,022
Contractual Services	15,457	12,333
Supplies and Materials	113,941	62,439
Repairs and Maintenance	40,767	64,814
Operational	846,009	760,814
Depreciation and Amortization	<u>451,402</u>	<u>400,288</u>
TOTAL OPERATING EXPENSES	<u>1,962,737</u>	<u>1,759,710</u>
OPERATING INCOME/(LOSS)	(44,036)	85,233
NON-OPERATING REVENUES (EXPENSES)		
Other Non-utility Income	2,919	14,685
Interest Income	33,834	22,260
Interest Expenses and Fiscal Charges	<u>(214,510)</u>	<u>(176,988)</u>
TOTAL NON-OPERATING REVENUES (EXPENSES)	<u>(177,757)</u>	<u>(140,043)</u>
INCOME (LOSS) BEFORE CAPITAL CONTRIBUTIONS	(221,793)	(54,810)
Capital Contributions	429,376	543,978
Grants	<u>542,900</u>	<u>509,849</u>
INCREASE (DECREASE) IN NET ASSETS	750,483	999,017
NET ASSETS		
Beginning of Year	7,893,706	6,894,689
End of Year	<u>\$ 8,644,190</u>	<u>\$ 7,893,706</u>

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

ADAIR COUNTY WATER DISTRICT  
STATEMENT OF CASH FLOWS  
Years Ended December 31, 2006 and 2005

	2006	2005
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Cash Received From Customers	\$ 1,872,469	\$ 1,845,419
Cash Payments to Employees for Services	(493,578)	(459,844)
Cash Payments to Suppliers for Goods and Services	(1,031,808)	(825,581)
Customer Deposits Received	9,959	10,556
Customer Deposits Returned	(9,530)	(9,124)
NET CASH PROVIDED/(USED) BY OPERATING ACTIVITIES	347,512	561,426
<b>CASH FLOWS FROM NON-CAPITAL AND RELATED FINANCING ACTIVITIES</b>		
Transfer to Sinking Fund	-	(4,258)
NET CASH PROVIDED/(USED) BY NON-CAPITAL AND RELATED FINANCING ACTIVITIES	-	(4,258)
<b>CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES</b>		
Principal Paid on Debt	(84,000)	(66,500)
Interest Paid on Debt	(217,120)	(176,348)
Bank Borrowings	-	(1,171,914)
Acquisition of Capital Assets	(1,140,827)	(1,619,005)
Proceeds from Grants	542,900	509,849
Contributed Capital	429,376	543,978
Deferred Revenue	-	-
Bond Proceeds	-	1,238,000
NET CASH PROVIDED/(USED) BY CAPITAL AND RELATED FINANCING ACTIVITIES	(469,671)	(741,940)
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Interest	33,834	22,249
NET CASH PROVIDED/(USED) BY INVESTING ACTIVITIES	33,834	22,249
NET INCREASE/(DECREASE) IN CASH AND CASH EQUIVALENTS	(88,325)	(162,523)
CASH AND CASH EQUIVALENTS - BEGINNING OF YEAR	1,139,054	1,301,577
CASH AND CASH EQUIVALENTS - END OF YEAR	\$ 1,050,729	\$ 1,139,054
<b>RECONCILIATION OF CASH AND CASH EQUIVALENTS TO THE STATEMENT OF NET ASSETS</b>		
Cash and Cash Equivalents	\$ 269,554	\$ 380,258
Short-Term Investments	273,497	260,710
Restricted Cash	507,678	498,086
TOTAL CASH AND CASH EQUIVALENTS	\$ 1,050,729	\$ 1,139,054

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



ADAIR COUNTY WATER DISTRICT  
STATEMENT OF CASH FLOWS (CONTINUED)  
Years Ended December 31, 2006 and 2005

	2006	2005
RECONCILIATION OF OPERATING INCOME/(LOSS) TO NET CASH PROVIDED/(USED) FOR OPERATING ACTIVITIES		
Operating Margin	\$ (44,036)	\$ 85,232
ADJUSTMENTS TO RECONCILE OPERATING INCOME/(LOSS) TO NET CASH PROVIDED/(USED) FOR OPERATING ACTIVITIES		
Depreciation	451,402	400,288
Change in Assets and Liabilities:		
(Increase)/Decrease in Accounts Receivable	(46,232)	476
(Increase)/Decrease in Inventory	(23,608)	62,169
(Increase)/Decrease in Prepaid Expenses	(3,899)	(937)
Increase/(Decrease) in Accounts Payable	21,152	5,548
Increase/(Decrease) in Salaries and Wages Payable	1,583	(823)
Increase/(Decrease) in Customer Deposits	429	1,435
Increase/(Decrease) in Accrued and Withheld Taxes	(9,279)	8,038
TOTAL RECONCILING ADJUSTMENTS	391,548	476,194
NET CASH PROVIDED/(USED) BY OPERATING ACTIVITIES	\$ 347,512	\$ 561,426

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

ADAIR COUNTY WATER DISTRICT  
NOTES TO FINANCIAL STATEMENTS  
Years Ended December 31, 2006 and 2005

NOTE 1: DESCRIPTION OF ENTITY

Reporting Entity - The Adair County Water District Commissioners have financial accountability and control over all activities related to the water district. The district's primary source of income is derived from water sales. The district also receives funding from federal government sources and must comply with the requirements of those funding source entities.

NOTE 2: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Accounting - The accounts of Adair County Water District are maintained in accordance with the principles of fund accounting. Under fund accounting, resources for various purposes are classified for accounting and reporting purposes into funds established according to their nature and purpose. Separate accounts are maintained for each fund; however, the district uses only one fund type known as a proprietary fund type.

The proprietary fund type is accounted for on a flow of economic resources measurement focus. With this measurement focus, all assets and all liabilities associated with the operation of this fund are included on the statement of net assets. Net assets (i.e., net of total liabilities) is segregated into invested in capital assets, net of related debt; restricted and unrestricted.

FASB Pronouncements - Since the District uses a proprietary fund, it applies all applicable Financial Accounting Board (FASB) Statements and Interpretations, Accounting Principles Board (APB) Opinions and Accounting Research Bulletins (ARB's) of the Committee on Accounting Procedures. The only exception in use of the aforementioned pronouncements is those that conflict with or contradict Governmental Accounting Standard's Board (GASB) pronouncements.

Cash Equivalents and Investments - The District considers all highly liquid investments with a remaining maturity of 90 days or less when purchased to be cash equivalents.

Investments are presented at fair value. Short-term investments generally mature or are otherwise available for withdrawal in less than one year. Investments for the District are certificates of deposits maturing after 90 days with interest rates ranging from 4.95% to 5.50%.

Inventory - Materials and supplies inventory consists principally of spare parts that are recorded when purchased and expensed when used. Inventory is stated at the lower of cost or market value. Cost is generally determined on a first-in, first-out basis.

Capital Assets and Related Depreciation - The utility plant and equipment was recorded at cost. Depreciation is computed using the straight-line method over the plant's estimated useful life of 40 years. The office building is depreciated on a straight-line basis over an estimated useful life of 20 years. Machinery, office equipment and service vehicles are depreciated on a straight-line basis over their estimated useful life ranging from 5 to 10 years.

Bond Issue Costs - Bond Issue Costs are being amortized and charged to expense over the term of the outstanding revenue bonds by use of the straight-line method.

Net Assets

Net assets comprise the various net earnings from operating income, non-operating revenues and expenses, and capital contributions. Net assets are classified in the following three components:

ADAIR COUNTY WATER DISTRICT  
NOTES TO FINANCIAL STATEMENTS  
Years Ended December 31, 2006 and 2005

NOTE 2: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

*Invested in capital assets, net of related debt*—This component of net assets consists of capital assets, net of accumulated depreciation and reduced by the outstanding balances of any bonds, mortgages, notes or other borrowings that are attributable to the acquisition, construction or improvement of those assets.

*Restricted*—This component of net assets consists of constraints imposed by creditors (such as through debt covenants), grantors, contributors, or laws or regulations of other governments or constraints imposed by law through constitutional provisions or enabling legislation.

*Unrestricted net assets*—This component of net assets consists of net assets that do not meet the definition of “restricted” or “invested in capital assets, net of related debt.”

NOTE 3: CASH AND CASH EQUIVALENTS AND INVESTMENTS

A summary of the District’s cash and investments is shown below:

	December 31, 2006	December 31, 2005
Unrestricted:		
Cash	\$ 269,554	\$ 380,258
Certificates of Deposit and Savings	273,497	260,710
Total Unrestricted	543,051	640,968
Restricted:		
Cash	271,041	272,718
Certificates of Deposit and Savings	236,637	225,368
Total Restricted	507,678	498,086
Total Cash and Cash Equivalents	\$ 1,050,729	\$ 1,139,054

There are three categories of credit risk that apply to the government’s bank balance:

1. Insured or collateralized with securities held by the government or by the government’s agent in the government’s name.
2. Collateralized with securities held by the pledging financial institution’s trust department or the government’s agent in the government’s name.
3. Uncollateralized.

	2006	2005
Insured (FDIC) or Collateral Held by Pledging Bank Securities in District's Name	\$ 1,121,424	\$ 1,142,978
Uninsured or Uncollateralized	23,535	-
Total (Memorandum Only)	\$ 1,144,959	\$ 1,142,978

ADAIR COUNTY WATER DISTRICT  
NOTES TO FINANCIAL STATEMENTS  
Years Ended December 31, 2006 and 2005

NOTE 3: CASH AND CASH EQUIVALENTS AND INVESTMENTS (CONTINUED)

Deposits

The carrying amount of the District's deposits at December 31, 2006 was \$1,050,129 and the bank balance was \$1,144,959. The difference between the bank balance and the carrying amount represents outstanding checks and deposits in transit. Of the bank balance, \$200,000 was insured by federal depository insurance and all but \$23,535 was collateralized by the pledging financial institutions.

Restricted Assets

These assets consist of cash restricted in a sinking fund and depreciation reserve fund as required by the revenue bonds plus cash received from the United States Fidelity and Guaranty Company for repairs to the system constructed by Roy Brothers.

NOTE 4: CUSTOMER AND OTHER ACCOUNTS RECEIVABLES

Customer and other accounts receivables were as follows:

	<u>2006</u>	<u>2005</u>
Accounts Receivable - Trade	\$ 251,084	\$ 180,041
Accounts Receivable - Returned Checks	1,155	643
Allowance for Doubtful Accounts	<u>(54,742)</u>	<u>(29,157)</u>
Net	<u>\$ 197,497</u>	<u>\$ 151,527</u>

NOTE 5: CAPITAL ASSETS

Capital asset activity for the years ended December 31, 2006 and 2005 was as follows:

	<u>Balance</u> <u>12/31/05</u>	<u>Additions</u>	<u>Deletions</u>	<u>Balance</u> <u>12/31/06</u>
Capital Assets				
Land and Land Rights	\$ 101,639	\$ 4,090	\$ -	\$ 105,729
Office Equipment	106,286	7,419	4,149	109,557
Service Equipment	402,135	85,467	72,071	415,530
Building	325,746	17,081		342,827
Plant and Equipment	14,349,801	1,653,233	-	16,003,034
Construction in Progress	<u>704,678</u>	<u>80,163</u>	<u>704,678</u>	<u>80,163</u>
Total Capital Assets	15,990,285	1,847,453	780,898	17,056,840
Less: Accumulated Depreciation				
Office Equipment	53,554	16,423	4,003	65,974
Service Equipment	274,872	30,952	72,071	233,753
Plant and Equipment	<u>4,225,429</u>	<u>401,973</u>		<u>4,627,402</u>
Total Accumulated Depreciation	<u>4,553,855</u>	<u>449,348</u>	<u>76,074</u>	<u>4,927,129</u>
Net Capital Assets	<u>\$ 11,436,430</u>	<u>\$ 1,398,105</u>	<u>\$ 704,824</u>	<u>\$ 12,129,711</u>

Depreciation expense for the year ended December 31, 2006 was \$449,348.

ADAIR COUNTY WATER DISTRICT  
NOTES TO FINANCIAL STATEMENTS  
Years Ended December 31, 2006 and 2005

NOTE 6: LONG-TERM OBLIGATIONS

Revenue Bonds payable with principal payments due annually on January 1 are detailed as follows:

	2006
1974 Waterworks Revenue Bond, original amount \$80,000 maturing January 1, 2014, with interest payments due semi-annually on January 1, and July 1, at a rate of 5%	\$ 28,500
1978 Waterworks Revenue Bond, original amount \$363,000 maturing January 1, 2018 with interest payments due semi-annually on January 1, July 1, at a rate of 5%	198,000
1985 Water District Water Revenue Bond, original amount \$1,155,000 maturing January 1, 2025, with interest payments due annually on January 1 at a rate of 5%	925,000
1989 Water District Water Revenue Bond, original amount \$200,000 maturing January 1, 2022, with interest payments due annually on January 1 at a rate of 6%	146,000
1992 Water District Water Revenue Bond, original amount \$745,000 maturing January 1, 2032, with interest payments due annually on January 1 at a rate of 5%	635,000
1995 Water District Water Revenue Bond, original amount \$428,000 maturing January 1, 2035, with interest payments due annually on January 1 at a rate of 4.5%	380,000
1998 Water District Water Revenue Bond, original amount \$427,000 maturing January 1, 2035, with interest payments due annually on January 1 at a rate of 4.5%	397,000
2003 Water District Water Revenue Bond, original amount \$627,000 maturing January 1, 2042, with interest payments due annually on January 1 at a rate of 4.5%	613,500
2005 Water District Water Revenue Bond, original amount \$1,238,000 maturing January 1, 2045, with interest payments due annually on January 1 at a rate of 4.25%	1,225,000
Total Debt	4,548,000
Payments Due in Less Than One Year	87,000
Total Long-Term Obligations	\$ 4,461,000

ADAIR COUNTY WATER DISTRICT  
 NOTES TO FINANCIAL STATEMENTS  
 Years Ended December 31, 2006 and 2005

NOTE 6: LONG-TERM OBLIGATIONS (CONTINUED)

The annual requirements to amortize all bonded debt outstanding as of December 31, 2006 are as follows:

	Principal	Interest	Total
2007	\$ 87,000	\$ 211,937	\$ 298,937
2008	92,500	207,703	300,203
2009	98,500	203,156	301,656
2010	103,500	198,388	301,888
2011	110,000	193,287	303,287
2012-2016	652,500	879,091	1,531,591
2017-2021	784,000	705,261	1,489,261
2022-2026	807,500	507,631	1,315,131
2027-2031	611,500	344,239	955,739
2032-2036	1,201,000	278,159	1,479,159
	\$ 4,548,000	\$ 3,728,852	\$ 8,276,852

NOTE 7: BONDING COMPANY SETTLEMENT

A summary of the guaranteed payments from the United States Fidelity and Guaranty Company resulting from the settlement with the district regarding leakage of lines and repairs to those lines.

	<u>TOTALS</u>
Repairs: \$8,000 per year, starting November 1, 1984, for a period of 15 years	\$ 120,000
Leakage: \$5,280 per year, starting November 1, 1984, for a period of 37 years	195,360
<u>LUMP SUM PAYMENTS</u>	
November 1, 1994	50,000
November 1, 2000	50,000
November 1, 2004	50,000
November 1, 2009	50,000
November 1, 2014	100,000
November 1, 2019	100,000
Total Guaranteed Payments	\$ 715,360

NOTE 8: RISK MANAGEMENT

The Adair County Water District is exposed to various risks of losses related to torts; theft of, damage to, and destruction of assets; injuries to employees; errors and omissions and natural disasters. The District purchases commercial insurance to cover any of these instances. The District did not have settled claims that exceeded the District's commercial insurance coverage in any of the past three years.

ADAIR COUNTY WATER DISTRICT  
NOTES TO FINANCIAL STATEMENTS  
Years Ended December 31, 2006 and 2005

NOTE 9: PENSION PLAN

The County Employees Retirement System of Kentucky (CERS) is a cost-sharing multiple-employer defined benefit pension plan that covers substantially all regular full-time members employed in non-hazardous duty positions of each county and school board, and any additional eligible local agencies electing to participate in the System. The plan provides for retirement, disability, and death benefits to plan members. Retirement benefits may be extended to beneficiaries of plan members under circumstances. Cost-of-living adjustments are provided at the discretion of the State legislature.

For the year ended December 31, 2006, plan members were required to contribute 5% of their annual creditable compensation. Participating employers were required to contribute at an actuarially determined rate. Per Kentucky Revised Statute Section 61.565 (3), normal contribution and past service contribution rates shall be determined by the CERS Board on the basis of an annual valuation last preceding the July 1 of a new biennium. The Board may amend contribution rates as of the first day of July of the second year of a biennium, if it is determined on the basis of a subsequent actuarial valuation that amended contribution rates are necessary to satisfy requirements determined in accordance with actuarial bases adopted by the Board. From January through June 2006, participating employers contributed 10.98% of member's non-hazardous compensation. The rate used by participating employers from July through December 2006, was 13.19% of members non-hazardous compensation. The Adair County Water District's total payroll for 2006 and 2005 was \$356,803 and \$336,908 and the amount covered by CERS was \$339,701 and \$320,490 respectively.

The following table presents certain information regarding the plans' status as a whole, derived from actuarial valuations performed as of the dates indicated:

	CERS as of June 30, 2005	CERS as of June 30, 2004 (In Thousands)	CERS as of June 30, 2003
Assets available for benefits, at fair value	\$ 6,511,562	\$ 6,645,464	\$ 6,753,585
Pension benefit obligation (Under funded) / over funded	7,180,774	6,577,290	5,917,227
pension benefit obligation	\$ (669,212)	\$ 68,174	\$ 836,358

The following table presents the last three years of the total of all employer contributions to CERS and the District's contributions for the years ending December 31:

Total Plan Contributions - CERS

Fiscal Year Ended	Annual Required Contributions	Actual Contributions	Percentage Contributed
2005	\$ 159,730,588	\$ 161,255,053	100.95%
2004	\$ 132,401,025	\$ 133,372,706	100.73%
2003	\$ 110,720,684	\$ 111,090,537	100.33%

ADAIR COUNTY WATER DISTRICT  
 NOTES TO FINANCIAL STATEMENTS  
 Years Ended December 31, 2006 and 2005

NOTE 9: PENSION PLAN (CONTINUED)

District Contribution - CERS

Fiscal Year Ended	Annual Required Contributions	Actual Contributions	Percentage Contributed
2006	\$ 40,504	\$ 40,504	100%
2005	\$ 46,352	\$ 46,352	100%
2004	\$ 38,533	\$ 38,533	100%

Vesting in a retirement benefit begins immediately upon entry into the System. The participant has a fully vested interest after the completion of sixty months of service, twelve of which are current service.

At a minimum, terminated employees are refunded their contributions with credited interest at 3% compounded annually through June 30, 1980, 6% thereafter through June 30, 1986, and 4% thereafter.

The pension benefit obligation is a standardized disclosure measure of the present value of pension benefits which is adjusted for the effects of projected salary increases and step-rate benefits that are estimated to be payable in the future as a result of employee service-to-date. The measure, which is the actuarial present value of credited projected benefits, is intended to help users assess the pensions' funding status on a going-concern basis, assess progress made in accumulating sufficient assets to pay benefits when due, and make comparisons among the plans and employers.

The County Employees Retirement System does not make separate measurements of assets and pension benefit obligation for individual employers.

Ten-year historical trend information showing the County Employees Retirement System's progress in accumulating sufficient assets to pay benefits when due is presented in their June 30, 2005, comprehensive annual financial reports. Copies of these reports can be obtained from CERS.

As the District is only one of several employers participating in the plan, it is not practical to determine the District's portion of the unfunded past service cost or the vested benefits of the District's portion of the plan assets.



SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

ADAIR COUNTY WATER DISTRICT  
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS  
For The Year Ended December 31, 2006

	<u>Federal CFDA Number</u>	<u>Disbursements</u>
<u>U. S. Department of Agriculture</u>		
Passed through Rural Utility Services:		
Water and Waste Disposal System for Rural Communities	10.760	<u>542,900</u>
 Total Federal Financial Assistance		 <u>\$ 542,900</u>

SCHEDULE OF FINDINGS AND QUESTIONED COSTS

ADAIR COUNTY WATER DISTRICT  
Schedule of Findings and Questioned Costs  
For the Year Ended December 31, 2006

I. SUMMARY OF AUDITORS' RESULTS

- a. As detailed on page one, an unqualified report was issued on the financial statements.
- b. The audit disclosed no areas of noncompliance which were material to the financial statements.
- c. As detailed on page 23 and 24, an unqualified report was issued on compliance for major programs.
- d. The audit disclosed no audit findings reportable under section 510(a) of OMB Circular A-133.
- e. Major programs consisted of grants received from Waste Water Disposal System for Rural Communities (CFDA #10.760).
- f. The dollar threshold used to distinguish between Type A and Type B programs was \$300,000.
- g. Adair County Water District qualified as a high-risk auditee in accordance with OMB Circular A-133.

II. FINDINGS RELATING TO FINANCIAL STATEMENTS REQUIRED TO BE REPORTED IN ACCORDANCE WITH GAGAS

- a. None.

III. FINDINGS AND QUESTIONED COSTS FOR FEDERAL AWARDS

- a. None.

ADAIR COUNTY WATER DISTRICT  
SCHEDULE OF PRIOR YEAR AUDIT FINDINGS  
December 31, 2006

The audit of Adair County Water District for the year ended December 31, 2005, revealed no audit findings requiring corrective action.



REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING  
AND COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT  
OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE  
WITH *GOVERNMENTAL AUDITING STANDARDS*

To the Commissioners  
Adair County Water District  
Columbia, KY

We have audited the accompanying financial statements of the business-type activities and each major fund of Adair County Water District as of and for the year ended December 31, 2006, which collectively comprise the Adair County Water District's basis financial statements and have issued our report thereon dated March 23, 2007. 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 and state audit requirements.

INTERNAL CONTROL OVER FINANCIAL REPORTING

In planning and performing our audit, we considered Adair County Water District's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinions 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 errors 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 Adair County Water District'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* or state audit requirements.

Adair County Water District  
Columbia, KY  
Page 2

We noted certain matters that we reported to the management of Adair County Water District in a separate letter dated March 23, 2007.

This report is intended for the information of the commissioners, management, United States Department of Agriculture Rural Development, federal awarding agencies, and Kentucky Public Service Commission, and is not intended to be and should not be used by anyone other than these specified parties.

A handwritten signature in cursive script that reads "Wise, Lee & Buckner".

Wise, Lee & Buckner, PLLC  
Certified Public Accountants

Campbellsville, Kentucky  
March 23, 2007



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

To the Commissioners  
Adair County Water District  
Columbia, KY

COMPLIANCE

We have audited the compliance of Adair County Water District 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 December 31, 2006. Adair County Water District'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 Adair County Water District's management. Our responsibility is to express an opinion on Adair County Water District'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, OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations* and state audit requirements. 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 Adair County Water District's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on Adair County Water District's compliance with those requirements.

In our opinion, Adair County Water District 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 December 31, 2006.

INTERNAL CONTROL OVER COMPLIANCE

The management of Adair County Water District is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts and grants applicable to federal programs. In planning and performing our audit, we considered Adair County Water District'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 and to test and report on internal control over compliance in accordance with OMB Circular A-133.



Adair County Water District  
Columbia, KY  
Page 2

Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be a material weakness. 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 noncompliance with applicable requirements of laws, regulations, contracts and grants caused by error or fraud that would be material in relation to a major federal program 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 compliance and its operation that we consider to be material weaknesses.

This report is intended for the information of the commissioners, management, United States Department of Agriculture Rural Development, federal awarding agencies, and Kentucky Public Service Commission, and is not intended to be and should not be used by anyone other than these specified parties.



Wise, Lee & Buckner, PLLC  
Certified Public Accountants

Campbellsville, Kentucky  
March 23, 2007