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DAMON R. TALLEY

ATTORNEY AT LAW

June 25, 2010

Mr. Jeff Derouen
Executive Director
Public Service Commission
PO Box 615
Frankfort, KY 40602

RECEIVED

JUN 28 2010

PUBLIC SERVICE
COMMISSION

RE: Hardin County Water District No. 2
Bond Refunding

Dear Mr. Derouen:

2010-00256

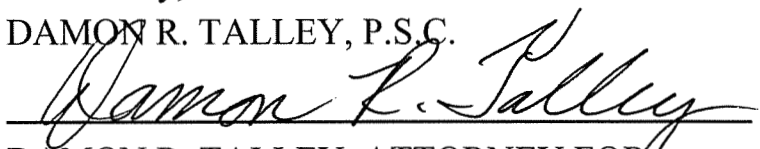
Enclosed for filing are the original and ten (10) copies of the Application of the Hardin County Water District No. 2 to issue securities pursuant to KRS 278.300 for the purpose of refunding certain high interest Bonds of the Applicant

No rate increase will be required.

The tentative Closing date is **July 27, 2010.**

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:

THE APPLICATION OF THE HARDIN)
COUNTY WATER DISTRICT NO. 2 TO ISSUE)
SECURITIES IN THE APPROXIMATE)
PRINCIPAL AMOUNT OF \$5,625,000 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. 2010-00256

RECEIVED
JUN 28 2010
PUBLIC SERVICE
COMMISSION

** **

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 \$5,625,000 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: James R. Jeffries, 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 2009 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 2010A (the "2010A Bonds"), in the principal amount of \$5,625,000 for the purpose of currently refunding the

following revenue bonds:

Water System Revenue Bonds, 1999 Series A in the outstanding principal amount of \$5,810,000 (the "1999A Bonds") which bear interest at rates ranging from 4.75% to 5.00% per annum.

6. The actual Debt Service Schedule for the proposed 2010A 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 2010A Bonds were received on June 24, 2010. Consequently, **Exhibit 1** reflects the actual interest rates and the actual Debt Service Schedule for the proposed 2010A Bonds. The 2010A Bonds were sold pursuant to public advertisement soliciting competitive bids according to Kentucky law.

7. As shown in **Exhibit 1**, the proposed 2010A Bonds will bear interest at rates ranging from 2.00% to 4.125%.

8. The issuance of the 2010A Bonds will provide the District with the funds necessary: (a) to allow it to currently refund the 1999A Bonds; and (b) to pay the fees and expenses incident to the issuance of the 2010A Bonds.

9. The Sources and Uses of the funds to be obtained from the issuance of the 2010A Bonds are detailed in **Exhibit 2**, which is attached hereto and incorporated herein by reference.

10. The proposed refinancing of the 1999A Bonds will result in total gross savings of approximately \$1,283,778 and a net present value savings of \$536,176. This represents a net present value savings of approximately 9.23%. 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 1999A 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 2010A 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 2010A 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 2010A Bonds, file with the Commission a statement setting forth the date of issuance of the 2010A Bonds, the price paid, the fees and expenses incurred in the issuance of the 2010A Bonds, and the terms and interest rates of the 2010A Bonds.

14. The detailed Income Statement and Balance Sheet for the twelve (12) month period ending on December 31, 2009 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 2009 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 2010A 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 1999A Bonds.

17. A copy of the District's audited financial statements for the years ended December 31, 2009 and 2008 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, 2009. The financial data filed with this Application is for the twelve (12) month period ending December 31, 2009. 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 or the closing of the 2010A 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 2010A Bonds was held on June 24, 2010 and the closing is tentatively scheduled for **July 27, 2010**.

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 **July 27, 2010**.
3. Grant the District a deviation, to the extent necessary, from 801 KAR 5:001, Section 6 to allow the submission of the District's Audit for the twelve (12) month period ending December 31, 2009 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 June 24, 2010.

Respectfully submitted,
HARDIN COUNTY WATER
DISTRICT NO. 2

BY:


MICHAEL L. BELL, CHAIRMAN


DAMON R. TALLEY, P.S.C.

Counsel for Applicant

PO 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 June 24, 2010.

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 June 24, 2010.


NOTARY PUBLIC, STATE AT LARGE

MY COMMISSION EXPIRES: 6-9-2011

EXHIBIT LIST

1. DEBT SERVICE SCHEDULE FOR 2010A BONDS
2. SOURCES AND USES FOR 2010A BONDS
3. GROSS DEBT SERVICE COMPARISON
(2010A AND PRIOR BONDS BEING REFUNDED)
4. DEBT SERVICE SCHEDULE FOR 1999A BONDS BEING
REFUNDED
5. INCOME STATEMENT
6. BALANCE SHEET
7. 2009 AUDIT

Hardin County (Kentucky)

Water District #2

Water System Refunding Revenue Bonds,
Series 2010 (Refunding of 1999A)**EXHIBIT 1****Debt Service Schedule**

Part 1 of 2

Date	Principal	Coupon	Interest	Total P+I	Fiscal Total
07/28/2010	-	-	-	-	-
01/01/2011	140,000.00	2.000%	78,452.34	218,452.34	-
07/01/2011	-	-	90,896.88	90,896.88	-
12/31/2011	-	-	-	-	309,349.22
01/01/2012	205,000.00	2.000%	90,896.88	295,896.88	-
07/01/2012	-	-	88,846.88	88,846.88	-
12/31/2012	-	-	-	-	384,743.76
01/01/2013	210,000.00	2.000%	88,846.88	298,846.88	-
07/01/2013	-	-	86,746.88	86,746.88	-
12/31/2013	-	-	-	-	385,593.76
01/01/2014	215,000.00	2.000%	86,746.88	301,746.88	-
07/01/2014	-	-	84,596.88	84,596.88	-
12/31/2014	-	-	-	-	386,343.76
01/01/2015	220,000.00	2.000%	84,596.88	304,596.88	-
07/01/2015	-	-	82,396.88	82,396.88	-
12/31/2015	-	-	-	-	386,993.76
01/01/2016	225,000.00	2.375%	82,396.88	307,396.88	-
07/01/2016	-	-	79,725.00	79,725.00	-
12/31/2016	-	-	-	-	387,121.88
01/01/2017	230,000.00	2.750%	79,725.00	309,725.00	-
07/01/2017	-	-	76,562.50	76,562.50	-
12/31/2017	-	-	-	-	386,287.50
01/01/2018	235,000.00	2.750%	76,562.50	311,562.50	-
07/01/2018	-	-	73,331.25	73,331.25	-
12/31/2018	-	-	-	-	384,893.75
01/01/2019	245,000.00	3.000%	73,331.25	318,331.25	-
07/01/2019	-	-	69,656.25	69,656.25	-
12/31/2019	-	-	-	-	387,987.50
01/01/2020	250,000.00	3.250%	69,656.25	319,656.25	-
07/01/2020	-	-	65,593.75	65,593.75	-
12/31/2020	-	-	-	-	385,250.00
01/01/2021	260,000.00	3.375%	65,593.75	325,593.75	-
07/01/2021	-	-	61,206.25	61,206.25	-
12/31/2021	-	-	-	-	386,800.00
01/01/2022	265,000.00	3.375%	61,206.25	326,206.25	-
07/01/2022	-	-	56,734.38	56,734.38	-
12/31/2022	-	-	-	-	382,940.63
01/01/2023	275,000.00	3.500%	56,734.38	331,734.38	-
07/01/2023	-	-	51,921.88	51,921.88	-
12/31/2023	-	-	-	-	383,656.26
01/01/2024	290,000.00	3.625%	51,921.88	341,921.88	-
07/01/2024	-	-	46,665.63	46,665.63	-
12/31/2024	-	-	-	-	388,587.51

Hardin County (Kentucky)

Water District #2

Water System Refunding Revenue Bonds,
Series 2010 (Refunding of 1999A)**EXHIBIT 1****Debt Service Schedule**

Part 2 of 2

Date	Principal	Coupon	Interest	Total P+I	Fiscal Total
01/01/2025	300,000.00	3.750%	46,665.63	346,665.63	-
07/01/2025	-	-	41,040.63	41,040.63	-
12/31/2025	-	-	-	-	387,706.26
01/01/2026	310,000.00	3.875%	41,040.63	351,040.63	-
07/01/2026	-	-	35,034.38	35,034.38	-
12/31/2026	-	-	-	-	386,075.01
01/01/2027	325,000.00	3.875%	35,034.38	360,034.38	-
07/01/2027	-	-	28,737.50	28,737.50	-
12/31/2027	-	-	-	-	388,771.88
01/01/2028	340,000.00	4.000%	28,737.50	368,737.50	-
07/01/2028	-	-	21,937.50	21,937.50	-
12/31/2028	-	-	-	-	390,675.00
01/01/2029	345,000.00	4.000%	21,937.50	366,937.50	-
07/01/2029	-	-	15,037.50	15,037.50	-
12/31/2029	-	-	-	-	381,975.00
01/01/2030	360,000.00	4.000%	15,037.50	375,037.50	-
07/01/2030	-	-	7,837.50	7,837.50	-
12/31/2030	-	-	-	-	382,875.00
01/01/2031	380,000.00	4.125%	7,837.50	387,837.50	-
12/31/2031	-	-	-	-	387,837.50
Total	\$5,625,000.00	-	\$2,407,464.94	\$8,032,464.94	-

Yield Statistics

Bond Year Dollars	\$65,965.63
Average Life	11.727 Years
Average Coupon	3.6495750%
Net Interest Cost (NIC)	3.7077257%
True Interest Cost (TIC)	3.6839301%
Bond Yield for Arbitrage Purposes	3.6273362%
All Inclusive Cost (AIC)	3.8987318%

IRS Form 8038

Net Interest Cost	3.6797338%
Weighted Average Maturity	11.696 Years

Hardin County (Kentucky)

Water District #2

Water System Refunding Revenue Bonds,
Series 2010 (Refunding of 1999A)

EXHIBIT 2

Sources & Uses

Dated 07/28/2010 | Delivered 07/28/2010

Sources Of Funds

Par Amount of Bonds	\$5,625,000.00
Transfers from Prior Issue Debt Service Funds	119,866.25
Transfers from Prior Issue DSR Funds	1,226,138.61
Total Sources	\$6,971,004.86

Uses Of Funds

Original Issue Discount (OID)	9,361.70
Total Underwriter's Discount (0.516%)	28,997.77
Financial Advisor	30,000.00
Bond Counsel	30,000.00
Local Counsel	30,000.00
Trustee Origination	3,500.00
Rating Agency Fee	12,600.00
Publication and Bond Counsel Expenses	2,000.00
Deposit to Debt Service Reserve Fund (DSRF)	962,326.86
Deposit to Current Refunding Fund	5,861,091.83
Rounding Amount	1,126.70
Total Uses	\$6,971,004.86

Hardin County (Kentucky)

Water District #2

Water System Refunding Revenue Bonds,
Series 2010 (Refunding of 1999A)**EXHIBIT 3****Gross Debt Service Comparison**

Date	Principal	Coupon	Interest	New D/S	OLD D/S	Savings
12/31/2010	-	-	-	-	-	-
12/31/2011	140,000.00	-	169,349.22	309,349.22	444,476.25	135,127.03
12/31/2012	205,000.00	-	179,743.76	384,743.76	441,520.00	56,776.24
12/31/2013	210,000.00	-	175,593.76	385,593.76	443,207.50	57,613.74
12/31/2014	215,000.00	-	171,343.76	386,343.76	444,420.00	58,076.24
12/31/2015	220,000.00	-	166,993.76	386,993.76	445,157.50	58,163.74
12/31/2016	225,000.00	-	162,121.88	387,121.88	445,420.00	58,298.12
12/31/2017	230,000.00	-	156,287.50	386,287.50	445,207.50	58,920.00
12/31/2018	235,000.00	-	149,893.75	384,893.75	444,520.00	59,626.25
12/31/2019	245,000.00	-	142,987.50	387,987.50	443,357.50	55,370.00
12/31/2020	250,000.00	-	135,250.00	385,250.00	441,720.00	56,470.00
12/31/2021	260,000.00	-	126,800.00	386,800.00	444,488.75	57,688.75
12/31/2022	265,000.00	-	117,940.63	382,940.63	441,526.25	58,585.62
12/31/2023	275,000.00	-	108,656.26	383,656.26	442,825.00	59,168.74
12/31/2024	290,000.00	-	98,587.51	388,587.51	443,396.25	54,808.74
12/31/2025	300,000.00	-	87,706.26	387,706.26	443,000.00	55,293.74
12/31/2026	310,000.00	-	76,075.01	386,075.01	441,625.00	55,549.99
12/31/2027	325,000.00	-	63,771.88	388,771.88	444,375.00	55,603.12
12/31/2028	340,000.00	-	50,675.00	390,675.00	446,125.00	55,450.00
12/31/2029	345,000.00	-	36,975.00	381,975.00	442,000.00	60,025.00
12/31/2030	360,000.00	-	22,875.00	382,875.00	442,000.00	59,125.00
12/31/2031	380,000.00	-	7,837.50	387,837.50	445,875.00	58,037.50
Total	\$5,625,000.00	-	\$2,407,464.94	\$8,032,464.94	\$9,316,242.50	\$1,283,777.56

PV Analysis Summary (Gross to Gross)

Gross PV Debt Service Savings	918,727.36
Transfers from Prior Issue Debt Service Fund	(119,866.25)
Transfers from Prior Issue DSR Fund	(1,226,138.61)
Amount deposited into new DSR Fund	962,326.86
Contingency or Rounding Amount	1,126.70
Net Present Value Benefit	\$536,176.06
Net PV Benefit / \$5,810,000 Refunded Principal	9.229%
Net PV Benefit / \$5,625,000 Refunding Principal	9.532%

Refunding Bond Information

Refunding Dated Date	7/28/2010
Refunding Delivery Date	7/28/2010

Hardin County (Kentucky)

Water District #2

Water System Revenue Bonds,

Series 1999

EXHIBIT 4**Total Refunded Debt Service**

Part 1 of 2

Date	Principal	Coupon	Interest	Total P+I
01/01/2011	165,000.00	4.750%	141,697.50	306,697.50
07/01/2011	-	-	137,778.75	137,778.75
01/01/2012	170,000.00	4.750%	137,778.75	307,778.75
07/01/2012	-	-	133,741.25	133,741.25
01/01/2013	180,000.00	4.750%	133,741.25	313,741.25
07/01/2013	-	-	129,466.25	129,466.25
01/01/2014	190,000.00	4.750%	129,466.25	319,466.25
07/01/2014	-	-	124,953.75	124,953.75
01/01/2015	200,000.00	4.750%	124,953.75	324,953.75
07/01/2015	-	-	120,203.75	120,203.75
01/01/2016	210,000.00	4.750%	120,203.75	330,203.75
07/01/2016	-	-	115,216.25	115,216.25
01/01/2017	220,000.00	4.750%	115,216.25	335,216.25
07/01/2017	-	-	109,991.25	109,991.25
01/01/2018	230,000.00	4.750%	109,991.25	339,991.25
07/01/2018	-	-	104,528.75	104,528.75
01/01/2019	240,000.00	4.750%	104,528.75	344,528.75
07/01/2019	-	-	98,828.75	98,828.75
01/01/2020	250,000.00	4.750%	98,828.75	348,828.75
07/01/2020	-	-	92,891.25	92,891.25
01/01/2021	265,000.00	4.750%	92,891.25	357,891.25
07/01/2021	-	-	86,597.50	86,597.50
01/01/2022	275,000.00	4.850%	86,597.50	361,597.50
07/01/2022	-	-	79,928.75	79,928.75
01/01/2023	290,000.00	4.850%	79,928.75	369,928.75
07/01/2023	-	-	72,896.25	72,896.25
01/01/2024	305,000.00	4.850%	72,896.25	377,896.25
07/01/2024	-	-	65,500.00	65,500.00
01/01/2025	320,000.00	5.000%	65,500.00	385,500.00
07/01/2025	-	-	57,500.00	57,500.00
01/01/2026	335,000.00	5.000%	57,500.00	392,500.00
07/01/2026	-	-	49,125.00	49,125.00
01/01/2027	355,000.00	5.000%	49,125.00	404,125.00
07/01/2027	-	-	40,250.00	40,250.00
01/01/2028	375,000.00	5.000%	40,250.00	415,250.00
07/01/2028	-	-	30,875.00	30,875.00
01/01/2029	390,000.00	5.000%	30,875.00	420,875.00
07/01/2029	-	-	21,125.00	21,125.00
01/01/2030	410,000.00	5.000%	21,125.00	431,125.00
07/01/2030	-	-	10,875.00	10,875.00
01/01/2031	435,000.00	5.000%	10,875.00	445,875.00
Total	\$5,810,000.00	-	\$3,506,242.50	\$9,316,242.50

Hardin County (Kentucky)

Water District #2

Water System Revenue Bonds,

Series 1999

EXHIBIT 4

Total Refunded Debt Service

Part 2 of 2

Yield Statistics

Average Life	12.170 Years
Weighted Average Maturity (Par Basis)	12.170 Years
Average Coupon	4.9286167%

Refunding Bond Information

Refunding Dated Date	7/28/2010
Refunding Delivery Date	7/28/2010

EXHIBIT 5

HARDIN COUNTY WATER DISTRICT NO. 2

STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN FUND NET ASSETS

YEARS ENDED DECEMBER 31, 2009 AND 2008

	<u>2009</u>	<u>2008</u>
OPERATING REVENUES:		
Water sales	\$ 7,535,979	\$ 7,875,790
Other operating income	309,537	243,068
TOTAL OPERATING REVENUES	<u>7,845,516</u>	<u>8,118,858</u>
OPERATING EXPENSES:		
Power purchased	355,777	412,230
Pumping and treatment labor	413,838	381,767
Purification supplies and expense	429,116	408,134
Transmission and distribution labor	1,097,094	1,086,018
Transmission and distribution supplies and expense	319,188	211,247
Transmission and distribution maintenance and repairs	66,903	68,579
Equipment rental	16,912	5,561
Transportation expense	110,811	167,637
Water treatment maintenance and expense	174,657	112,975
General and administrative expenses	1,466,979	1,456,569
Depreciation	1,406,261	1,315,353
TOTAL OPERATING EXPENSES	<u>5,857,536</u>	<u>5,626,070</u>
OPERATING INCOME	1,987,980	2,492,788
NON-OPERATING REVENUES (EXPENSES):		
Interest income	338,461	405,501
Other income	103,150	92,446
Gain on disposal of assets	14,220	27,902
Interest expense on long-term debt	(881,306)	(920,283)
Interest expense on customer deposits	(1,895)	(5,629)
Amortization of bond discount and expense	(112,797)	(129,713)
TOTAL NON-OPERATING REVENUES (EXPENSES)	(540,167)	(529,776)
CAPITAL CONTRIBUTIONS	<u>1,541,139</u>	<u>3,232,543</u>
CHANGE IN NET ASSETS	2,988,952	5,195,555
NET ASSETS, beginning of year	<u>38,384,301</u>	<u>33,188,746</u>
NET ASSETS, end of year	<u>\$ 41,373,253</u>	<u>\$ 38,384,301</u>

See accompanying notes to financial statements.

HARDIN COUNTY WATER DISTRICT NO. 2

EXHIBIT 6

STATEMENTS OF NET ASSETS

DECEMBER 31, 2009 AND 2008

<u>ASSETS</u>	<u>2009</u>	<u>2008</u>
CURRENT ASSETS:		
Cash and cash equivalents	\$ 2,457,651	\$ 1,245,323
Investments	8,708,865	6,920,378
Accounts receivable, net	559,785	527,788
Prepaid insurance	32,988	37,033
State grants receivable	19,760	-
Federal grants receivable	-	72,103
Tap fees receivable	20,050	20,050
Inventory	386,455	481,263
TOTAL CURRENT ASSETS	12,185,554	9,303,938
NONCURRENT ASSETS:		
Restricted cash and cash equivalents	3,567,268	3,311,336
Investments	-	1,525,154
Restricted investments	1,221,392	1,222,362
Capital assets, net of accumulated depreciation	45,898,989	44,582,721
TOTAL NONCURRENT ASSETS	50,687,649	50,641,573
TOTAL ASSETS	62,873,203	59,945,511
 <u>LIABILITIES</u>		
CURRENT LIABILITIES:		
Accounts payable	313,692	238,965
Accrued taxes	20,475	22,346
Accrued liabilities	37,293	27,774
Accrued vacation	6,599	7,222
Customer deposits	44,893	42,058
Customer advances for construction	77,254	125,949
Accrued interest	30,240	-
Notes payable	1,113,769	171,802
Bonds payable	1,158,500	1,131,500
TOTAL CURRENT LIABILITIES	2,802,715	1,767,616
NONCURRENT LIABILITIES:		
Customer deposits	404,039	378,521
Accrued vacation	59,386	64,993
Customer advances for construction	172,721	243,288
Bonds payable	18,841,500	20,000,000
Less: bond discount and deferred amount on refundings	(780,411)	(893,208)
TOTAL NONCURRENT LIABILITIES	18,697,235	19,793,594
TOTAL LIABILITIES	21,499,950	21,561,210
 <u>NET ASSETS</u>		
Invested in capital assets, net of related debt	25,565,631	24,172,627
Restricted for debt service	2,863,767	2,857,995
Unrestricted	12,943,855	11,353,679
TOTAL NET ASSETS	\$ 41,373,253	\$ 38,384,301

See accompanying notes to financial statements.

EXHIBIT 7

2009 AUDIT

HARDIN COUNTY WATER DISTRICT NO. 2

INDEPENDENT AUDITOR'S REPORT ON FINANCIAL
STATEMENTS AND SUPPLEMENTARY INFORMATION
YEARS ENDED DECEMBER 31, 2009 AND 2008

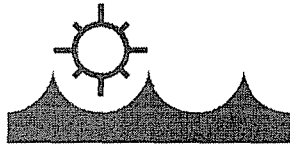
HARDIN COUNTY WATER DISTRICT NO. 2

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LETTER OF TRANSMITTAL



Hardin County Water District No. 2

360 Ring Road • P.O. Box 970 • Elizabethtown, KY 42702

Telephone (270) 737-1056 • Fax (270) 737-2301 • TTY 1-800-648-6956 or 711

www.hardincountywater2.org

Board of Commissioners: Mike Bell, Cordell Tabb, John Effinger, Morris Miller, Tim Davis

General Manager: James Jeffries

February 16, 2010

TO: Hardin County Water District No. 2 Board of Commissioners

We are pleased to submit the Financial Report for Hardin County Water District No. 2 for the year ended December 31, 2009. This report has been prepared in accordance with generally accepted accounting principles (GAAP), as set forth in the pronouncements of the Governmental Accounting Standards Board (GASB) and the Financial Accounting Standards Board.

Responsibility for both the accuracy of the data presented and the completeness and fairness of presentation, including all disclosures, rests with the District. We believe the data as presented is accurate, that it is presented in a manner designed to fairly set forth the financial position and the results of operations of the District as measured by its and that all disclosures necessary to enable the reader to gain maximum understanding of the District's financial affairs have been included.

District management's narrative on the financial activities of the District is in the Management's Discussion and Analysis (MD&A) section of this report, immediately following the Independent Auditor's Report. The letter of transmittal is written to complement the MD&A and the financial statements, and should be read from that perspective and in conjunction with all other sections of the report.

This report is a joint effort between our staff and Stiles, Carter, and Associates, Certified Public Accountants. I would like to recognize Mr. Scott Clark, Customer Service and Administrative Manager, for his role in leading the District in this effort. I also recognized Ms. Lea Ona Sims for her continued role in keeping the finances of the District. Mr. Brian Woosley was the lead auditor for Stiles, Carter, and Associates and our staff spent several hours working closely with Mr. Woosley to complete this report.

Financial Performance and Highlights

The District has historically enjoyed increasing revenues year over year throughout the decade. Average revenue growth from 2000 to 2008 was 6% compared to the 2009 result of -3.4% to \$7.8 million. This drop in revenue can be contributed to a combination of factors. The midyear of 2009, May through October, was unseasonably wet with total rainfall reaching 31.18 inches versus 18.05 inches for 2008 and 15.73 inches for 2007. This was a direct impact to the typical boost in demand that has been experienced in the past during the summer months. Swimming pools, landscaping, gardens, and front yards were not in need of assistance from District water supplies. The recession also played a role in the reduced water demand. As Hardin County's unemployment rate approached 10%, commercial and

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industrial activity was scaled back in the county. Revenue from these groups was off \$191,000 in 2009 compared to 2008. The third contributing factor is the low new customer growth experienced by the District. As developers in the area slowed expansion, new meter sales growth dropped to a three year low at 272 new taps. This represents a new customer growth rate of less than 1% while the District is accustomed to a rate of 3 – 4%.

While the District has little influence on revenue, the staff recognizes that we can control expenses. Total operating expenses for the year saw a modest increase of 4.1% to \$5.86 million. Depreciation contributed 1.6% or \$91,000 to the total increase. Total labor expenses rose by \$82,000, 3.3% over last year, and contributed another 1.4%. The District continued its practice of hiring employees through Express Personnel during 2009. After three years of this practice, we have 9 employees who have completed the process to fill permanent positions. The process reduces training costs and employee turnover. The employee base has also become more self sufficient within each department. Total payments to suppliers were flat for the year at \$2.55 million compared to \$2.54 million in 2008. The trend is evident of the expansion of our internal skills. Noteworthy examples include the construction crew, which completed the District's first rail road bore in-house, and the water treatment plant staff, which completed the rehabilitation of the Number 3 Claricone in-house.

Capital Improvement and Projects

The District continued its 2020 County Expansion Phase IV/V. After Twin States, Inc. completed construction of the initial selection of roads in 2008, additional roads were added to the contract. Twin States completed infrastructure upgrades on Rineyville Road west of Rineyville and on St. John Road leaving Elizabethtown. Funds were still available from the RD revenue bond of \$2.48 million and Kenvirons proceeded with the design of the Valley Creek pump station to replace the aging Springfield Road pump station. Plans were also laid to replace the Valley Creek stand pipe with a 150,000 gallon tank on the same site. These projects will be funded with the balance of the RD bonds.

The District's construction crew began construction of the Glendale section of the Loop Project. The crew laid over 20,000 feet of 24" ductile iron pipe intended to serve an eventual customer at the Glendale Industrial Site and to connect to the east side of the Elizabethtown Loop. The District drew over \$1.1 million in Kentucky State Appropriation KIA grant funds for material purchases for this project during the year. This was the main driver for the construction in process account expansion from \$115,000 in 2008 to \$2,311,000 in 2009.

The District received notice of grants from the Kentucky Cabinet for Economic Development in association with the expansion of Fort Knox through the BRAC process. Projects funded were: the Rineyville Wastewater Project at \$9.6 million; the Springfield Tank Project at \$2 million; and the final phase of the Elizabethtown Loop project at \$1.5 million. The District hired Strand and Associates to commence the Preliminary Engineering Report for the Rineyville Wastewater Project and \$10,000 was drawn on the wastewater grant to finance the study. The District staff worked diligently with Strand to frame the project scope for the wastewater project.

The District continued procurement of the Louisville Water Connection Project by petitioning property owners in the Pear Orchard Road Northwest area and along highway 434. Of the nine mile project, we project that another 4 miles of easements are required to complete the pipeline route.

Water Operations

The District water treatment plant treated and delivered 1.65 billion gallons during the year. This was off 9.8% from the 1.83 billion gallons delivered in 2008. Capacity utilization was an average of 59% as total gallons sold to customers finished at 1.41 billion gallons versus 1.52 billion gallons in 2008. The distribution leak percentage improved slightly from 12.8% in 2008 to 12.3% in 2009.

The District had no violations for water quality or reporting requirements. We experienced favorable audits in all areas including: workers compensation audit, inventory audit, DOW audit, PSC inspection, fire safety inspection, bacteriological laboratory inspection, and the fluoride inspection.

The 2009 Ice Storm significantly affected the water operations of the District. A District-wide boil water advisory was issued in cooperation with District No. 1. The water treatment plant was without power for the last week of January and other water systems were in similar situations. District staff responded by converting the board room to a 'war room', placing all personnel on-call, and working around the clock to recover. Generators were brought in to run the treatment plant and most customers who were affected were without water for 12 to 36 hours. The Hart County area was without water for a week. The event resulted in an unbudgeted expenditure totaling \$113,000. The District applied for FEMA disaster reimbursement and received a payment toward this application in the amount of \$75,000 in December. Efforts continue to collect the balance of this application.

Safety and Quality Recognition

The District was humbled by the constant recognition throughout the year for our excellence in operations, water quality and customer service.

In the area of Safety, the District was awarded the "Thoroughbred Award" from the Kentucky Department of Workplace Standards for 24 months without a lost time accident and the "Governor's Safety Award" from the Kentucky Labor Cabinet for 250,000 hours worked without a lost time accident. The District is still adding to these totals.

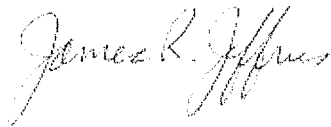
In the area of water quality, the District placed second in the Kentucky Rural Water Association "Best Tasting Water" contest in February. Then in June, the District took first place in the Kentucky-Tennessee Chapter of American Water Works Association "Best Tasting Water" contest. Mr. Shaun Youravich, Operations Manager, will represent the District at the national AWWA convention in Chicago in 2010.

In our operations area, the District was nominated by AWWA for the "Plant of the Year" Award. We also received the "Public Information Excellence in Service" Award from AWWA for our new customer information packets. Mr. Scott Clark, Customer Service Manager, was personally recognized by AWWA with the "Customer Service" Award.

Closing Remarks

Hardin County Water District No. 2 has had a banner year in the core areas of our operations in 2009. The District continues to show excellence in our water quality and customer service. While economic conditions at large resulted in an unfavorable revenue result, the staff responded by maintaining overall expenditures \$93,000 under budget. As water demand returns to growth, the fiscal position of the District will be even stronger as a result of these efforts.

It has been a pleasure for the staff to bring these results to the Board of Commissioners for their consideration and review. On behalf of all the employees of the District, it has been a pleasure to provide the highest quality service to our customers for another year.



James R. Jeffries
General Manager

INDEPENDENT AUDITOR'S REPORT

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
PHILIP A. LOGSDON, CPA



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

CERTIFIED PUBLIC ACCOUNTANTS

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INDEPENDENT AUDITOR'S REPORT

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

We have audited the accompanying financial statements of Hardin County Water District No. 2 as of and for the years ended December 31, 2009 and 2008, as listed in the table of contents. These 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 consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the District's internal control over financial reporting. Accordingly, we express no such opinion. 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, 2009 and 2008, 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 February 16, 2010, 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 7 through 11 is not a required part of the basic financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the 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 schedule of expenditures of federal awards on page 37 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 not a required part of the basic financial statements. Also, the accompanying Schedules I and II are presented for purposes of additional analysis and are not a required part of the basic financial statements. The schedule of expenditures of federal awards and Schedules I and II have 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. The letter of transmittal and Schedule III have not been subjected to the auditing procedures applied in the audit of the basic financial statements, and accordingly, we express no opinion on them.

Stiles, Carter & Associates
Certified Public Accountants
February 16, 2010

REQUIRED SUPPLEMENTARY INFORMATION

**HARDIN COUNTY WATER DISTRICT NO. 2
MANAGEMENT'S DISCUSSION AND ANALYSIS (MD&A)
YEAR ENDED DECEMBER 31, 2009**

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, 2009. 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.

FINANCIAL HIGHLIGHTS

- The ending cash and investment balance for the District was \$15.9 million. The balance at December 31, 2008, was \$14.2 million. This reflects an increase in cash and investments during the year of \$1.7 million.
- The District began the next portion of its 2020 County Expansion Project and E-town Loop Projects, started the Rineyville Sewer Project and continued work on the Glendale Project.
- The District invested approximately \$2.7 million in capital assets during the year.
- The District drew \$942 thousand on a \$2.5 million loan agreement that was entered into in 2007 for interim financing with Rural Development for the Phase IV project.

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 statement of net assets; a statement of revenues, expenses, and changes in fund 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 fund net assets** presents the results of the District's 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 \$41.4 million and \$38.4 million as of December 31, 2009 and 2008.

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, 2009 and 2008

	<u>2009</u>	<u>2008</u>
Assets		
Current and		
Other Assets	\$ 16,974,214	\$ 15,362,790
Capital Assets	<u>45,898,989</u>	<u>44,582,721</u>
Total Assets	<u>62,873,203</u>	<u>59,945,511</u>
Liabilities		
Long-term liabilities	18,697,235	19,793,594
Other Liabilities	<u>2,802,715</u>	<u>1,767,616</u>
Total Liabilities	<u>21,499,950</u>	<u>21,561,210</u>
Net Assets		
Invested in capital assets, net of related debt	25,565,631	24,172,627
Restricted for debt service	2,863,767	2,857,995
Unrestricted	<u>12,943,855</u>	<u>11,353,679</u>
Total Net Assets	<u>\$ 41,373,253</u>	<u>\$ 38,384,301</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 13.2% from \$11.4 million to \$12.9 million at December 31, 2009. Restricted net assets increased \$6 thousand (0.2%). Investment in governmental capital assets, net of related debt increased by \$1.4 million (5.8%).

(Table 2)
Changes in Net Assets
Years Ended December 31, 2009 and 2008

	2009	2008
OPERATING REVENUES:		
Water sales	\$ 7,535,979	\$ 7,875,790
Other operating income	309,537	243,068
Total operating revenues	7,845,516	8,118,858
OPERATING EXPENSES:		
Power purchased	355,777	412,230
Pumping and treatment labor	413,838	381,767
Purification supplies and expense	429,116	408,134
Transmission and distribution labor	1,097,094	1,086,018
Transmission and distribution supplies and expense	319,188	211,247
Transmission and distribution maintenance and repairs	66,903	68,579
Equipment rental	16,912	5,561
Transportation expense	110,811	167,637
Water treatment maintenance and expense	174,657	112,975
General and administrative expenses	1,466,979	1,456,569
Depreciation	1,406,261	1,315,353
Total operating expenses	5,857,536	5,626,070
OPERATING INCOME	1,987,980	2,492,788
NON-OPERATING REVENUES (EXPENSES):		
Interest income	338,461	405,501
Other income	103,150	92,446
Gain on disposal of assets	14,220	27,902
Interest expense on long-term debt	(881,306)	(920,283)
Interest expense on customer deposits	(1,895)	(5,629)
Amortization of bond discount and expense	(112,797)	(129,713)
TOTAL NON-OPERATING REVENUES (EXPENSES)	(540,167)	(529,776)
Capital contributions	1,541,139	3,232,543
Increase in net assets	\$ 2,988,952	\$ 5,195,555

Operating revenue decreased 3.4% compared to the prior year. The primary reason for the decrease is a decline in customer demand as the economy softened and the area experienced more rainfall than the previous year. Operating expenses increased by 4.1%, which includes a 1.6% increase in depreciation expense. Interest expense on long-term debt decreased 4.2%. The District continues to receive capital contributions through the State of Kentucky, the Federal government, other governments and individual developers.

Capital Assets and Debt Administration

Capital Assets

At December 31, 2009 and 2008, the District had \$45.9 million and \$44.6 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, 2009 and 2008

	2009	2008
Non-Depreciable Assets:		
Land and land rights	\$ 552,983	\$ 552,983
Depreciable Assets:		
Structures and improvements	2,283,324	2,360,390
Supply mains	1,014,861	1,058,960
Water treatment plant	8,051,151	8,273,181
Standpipes, tanks and foundations	4,118,581	4,263,902
Transmission and distribution mains	23,388,139	23,932,857
Services	3,732,616	3,535,860
Hydrants	84,225	94,548
Office furniture and fixtures	51,080	43,051
Transportation equipment	308,999	348,593
Communication equipment	-	-
Other property and equipment	2,183	3,252
Capital assets in service	43,588,142	44,467,577
Construction in progress	2,310,847	115,144
Total capital assets, net of depreciation	\$ 45,898,989	\$ 44,582,721

(Table 4)
Changes in Capital Assets
 Years Ended December 31, 2009 and 2008

	2009	2008
Beginning balance	\$ 44,582,721	\$ 42,732,694
Additions	2,722,529	4,520,370
Retirements	-	(1,354,990)
Depreciation	(1,406,261)	(1,315,353)
Ending balance	\$ 45,898,989	\$ 44,582,721

The District began the next portion of its 2020 County Expansion Project and E-town Loop Projects, started the Rineyville Sewer Project and continued work on the Glendale Project.

Debt

At December 31, 2009 and 2008, the District had \$21.1 million and \$21.3 million, in bonds and notes outstanding. A total of \$2.3 million is due within the 2010 calendar year.

(Table 5)
Outstanding Debt
as of December 31, 2009 and 2008

	<u>2009</u>	<u>2008</u>
Revenue bonds	\$ 20,000,000	\$ 21,131,500
Notes	<u>1,113,769</u>	<u>171,802</u>
Total	<u>\$ 21,113,769</u>	<u>\$ 21,303,302</u>

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 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 James Jeffries, General Manager, 360 Ring Road, Elizabethtown, Kentucky 42701, (270) 737-1056.

BASIC FINANCIAL STATEMENTS

HARDIN COUNTY WATER DISTRICT NO. 2STATEMENTS OF NET ASSETSDECEMBER 31, 2009 AND 2008

<u>ASSETS</u>	<u>2009</u>	<u>2008</u>
CURRENT ASSETS:		
Cash and cash equivalents	\$ 2,457,651	\$ 1,245,323
Investments	8,708,865	6,920,378
Accounts receivable, net	559,785	527,788
Prepaid insurance	32,988	37,033
State grants receivable	19,760	-
Federal grants receivable	-	72,103
Tap fees receivable	20,050	20,050
Inventory	386,455	481,263
TOTAL CURRENT ASSETS	12,185,554	9,303,938
NONCURRENT ASSETS:		
Restricted cash and cash equivalents	3,567,268	3,311,336
Investments	-	1,525,154
Restricted investments	1,221,392	1,222,362
Capital assets, net of accumulated depreciation	45,898,989	44,582,721
TOTAL NONCURRENT ASSETS	50,687,649	50,641,573
TOTAL ASSETS	62,873,203	59,945,511
 <u>LIABILITIES</u>		
CURRENT LIABILITIES:		
Accounts payable	313,692	238,965
Accrued taxes	20,475	22,346
Accrued liabilities	37,293	27,774
Accrued vacation	6,599	7,222
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Customer advances for construction	77,254	125,949
Accrued interest	30,240	-
Notes payable	1,113,769	171,802
Bonds payable	1,158,500	1,131,500
TOTAL CURRENT LIABILITIES	2,802,715	1,767,616
NONCURRENT LIABILITIES:		
Customer deposits	404,039	378,521
Accrued vacation	59,386	64,993
Customer advances for construction	172,721	243,288
Bonds payable	18,841,500	20,000,000
Less: bond discount and deferred amount on refundings	(780,411)	(893,208)
TOTAL NONCURRENT LIABILITIES	18,697,235	19,793,594
TOTAL LIABILITIES	21,499,950	21,561,210
 <u>NET ASSETS</u>		
Invested in capital assets, net of related debt	25,565,631	24,172,627
Restricted for debt service	2,863,767	2,857,995
Unrestricted	12,943,855	11,353,679
TOTAL NET ASSETS	\$ 41,373,253	\$ 38,384,301

See accompanying notes to financial statements.

HARDIN COUNTY WATER DISTRICT NO. 2

STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN FUND NET ASSETSYEARS ENDED DECEMBER 31, 2009 AND 2008

	<u>2009</u>	<u>2008</u>
OPERATING REVENUES:		
Water sales	\$ 7,535,979	\$ 7,875,790
Other operating income	309,537	243,068
TOTAL OPERATING REVENUES	<u>7,845,516</u>	<u>8,118,858</u>
OPERATING EXPENSES:		
Power purchased	355,777	412,230
Pumping and treatment labor	413,838	381,767
Purification supplies and expense	429,116	408,134
Transmission and distribution labor	1,097,094	1,086,018
Transmission and distribution supplies and expense	319,188	211,247
Transmission and distribution maintenance and repairs	66,903	68,579
Equipment rental	16,912	5,561
Transportation expense	110,811	167,637
Water treatment maintenance and expense	174,657	112,975
General and administrative expenses	1,466,979	1,456,569
Depreciation	1,406,261	1,315,353
TOTAL OPERATING EXPENSES	<u>5,857,536</u>	<u>5,626,070</u>
OPERATING INCOME	1,987,980	2,492,788
NON-OPERATING REVENUES (EXPENSES):		
Interest income	338,461	405,501
Other income	103,150	92,446
Gain on disposal of assets	14,220	27,902
Interest expense on long-term debt	(881,306)	(920,283)
Interest expense on customer deposits	(1,895)	(5,629)
Amortization of bond discount and expense	(112,797)	(129,713)
TOTAL NON-OPERATING REVENUES (EXPENSES)	<u>(540,167)</u>	<u>(529,776)</u>
CAPITAL CONTRIBUTIONS	<u>1,541,139</u>	<u>3,232,543</u>
CHANGE IN NET ASSETS	2,988,952	5,195,555
NET ASSETS, beginning of year	<u>38,384,301</u>	<u>33,188,746</u>
NET ASSETS, end of year	<u>\$ 41,373,253</u>	<u>\$ 38,384,301</u>

See accompanying notes to financial statements.

HARDIN COUNTY WATER DISTRICT NO. 2STATEMENTS OF CASH FLOWSYEARS ENDED DECEMBER 31, 2009 AND 2008

	<u>2009</u>	<u>2008</u>
CASH FLOWS FROM OPERATING ACTIVITIES:		
Receipts from customers	\$ 7,813,519	\$ 8,040,316
Payments to suppliers	(2,552,070)	(2,543,612)
Payments to employees	(1,695,854)	(1,634,020)
NET CASH PROVIDED BY OPERATING ACTIVITIES	3,565,595	3,862,684
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES:		
Principal payments on bonds	(1,131,500)	(1,114,500)
Proceeds from notes	941,967	171,802
Acquisition of capital assets	(2,582,643)	(3,165,380)
Contributions in aid of construction	1,593,482	3,160,440
Interest on long-term debt	(881,306)	(920,283)
Sale of capital assets	14,220	27,902
Customer deposit interest	(1,895)	(5,629)
NET CASH USED BY CAPITAL AND RELATED FINANCING ACTIVITIES	(2,047,675)	(1,845,648)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchase of investments	(6,028,402)	(5,712,525)
Proceeds from investments	5,811,993	2,696,145
Utility plant leased to others and other income	103,150	92,446
Interest income	63,599	83,917
NET CASH USED BY INVESTING ACTIVITIES	(49,660)	(2,840,017)
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	1,468,260	(822,981)
CASH AND CASH EQUIVALENTS, beginning of year	4,556,659	5,379,640
CASH AND CASH EQUIVALENTS, end of year	<u>\$ 6,024,919</u>	<u>\$ 4,556,659</u>
SUPPLEMENTAL DISCLOSURES OF CASH FLOWS INFORMATION:		
Interest paid during the year	<u>\$ 883,201</u>	<u>\$ 925,912</u>
RECONCILIATION OF OPERATING INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES:		
Operating income	\$ 1,987,980	\$ 2,492,788
Adjustments to reconcile net operating income to net cash provided by operating activities:		
Depreciation	1,406,261	1,315,353
Provision for loss on loan receivable	-	50,000
(Increase) in accounts receivable	(31,997)	(78,542)
Decrease in prepaid insurance	4,045	2,251
Decrease in tap fees receivable	-	25,265
(Increase) decrease in inventory	94,808	(40,485)
Increase in accounts payable	74,727	69,590
Increase in customer deposits	28,353	42,325
(Decrease) in accrued taxes payable	(1,871)	(6,949)
Increase (decrease) in accrued liabilities	9,519	(7,038)
(Decrease) in accrued vacation	(6,230)	(1,874)
NET CASH PROVIDED BY OPERATING ACTIVITIES	<u>\$ 3,565,595</u>	<u>\$ 3,862,684</u>

See accompanying notes to financial statements.

NOTES TO BASIC FINANCIAL STATEMENTS

HARDIN COUNTY WATER DISTRICT NO. 2NOTES TO FINANCIAL STATEMENTSDECEMBER 31, 2009 AND 2008

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* and is regulated by the Kentucky Public Service Commission.

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 and the accrual basis of accounting. 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 debt service"; and "unrestricted" components. Under the accrual basis of accounting, revenues are recognized when earned and expenses are recognized when the liability is incurred or economic asset used. Revenues, expenses, gains, losses, assets and liabilities resulting from exchange and exchange-like transactions are recognized when the exchange takes place.

- (1) Accounts Receivable - The allowance method is used to record uncollectible accounts. At December 31, 2009 and 2008, accounts receivable was stated net of an allowance for uncollectible accounts of \$60,000 and \$80,000. Bad debt expense for 2009 was \$4,101 and 2008 was \$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.

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HARDIN COUNTY WATER DISTRICT NO. 2NOTES TO FINANCIAL STATEMENTSDECEMBER 31, 2009 AND 2008NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

- (4) Capital assets - Capital assets 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 interest method over the life of each respective bond issue.
- (6) Cash Equivalents - For purposes of the statements of cash flows, the District considers all highly liquid debt instruments (including restricted assets) purchased with a maturity of three months or less 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, Expenses and Rate Structure - Revenues and expenses are recognized on the accrual basis as earned or incurred. The District distinguishes operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with the District's principal ongoing operations. The principal operating revenues of the District are charges to customers for sales and services. 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. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.
- (10) Capital Contributions - Contributions are recognized in the Statement of Revenues, Expenses and Changes in Fund 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.

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HARDIN COUNTY WATER DISTRICT NO. 2NOTES TO FINANCIAL STATEMENTSDECEMBER 31, 2009 AND 2008NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

- (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.
- (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 - 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 the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses 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, Phase III and Phase IV Water Line Projects. The notes are scheduled to be collected during the 2009 calendar year. The balances at December 31, 2009 and 2008 were \$20,050 and \$20,050.

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, 2007 and 2006, the outstanding balance was \$50,000. The note matured October 14, 2006, but the due date was extended until October 14, 2008. On November 15, 2007, the District agreed to extend the due date until November 15, 2009. Note collateral is water sales to Fort Knox, Hardin County Water District No. 1, the City of Muldraugh and any other entity. During 2008, the District determined that the loan would likely not be collected and established an allowance of \$50,000 against the loan. The loan was written off during 2009.

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HARDIN COUNTY WATER DISTRICT NO. 2NOTES TO FINANCIAL STATEMENTSDECEMBER 31, 2009 AND 2008NOTE D - DEPOSITS AND INVESTMENTS*DEPOSITS*

Custodial Credit Risk—Deposits. Custodial credit risk is the risk that in the event of a bank failure, the District's deposits may not be returned or that the District will not be able to recover collateral securities in the possession of an outside party. As of December 31, 2009 and 2008, \$12,988,526 and \$11,799,555 of the District's bank balance of \$14,566,682 and \$12,799,555 was exposed to custodial credit risk. The carrying amount of deposits at December 31, 2009 and 2008 was \$14,466,166 and \$12,743,635. For 2009, of the amount exposed to custodial credit risk, the entire amount was collateralized by securities held by the pledging financial institution. For 2008, of the amount exposed to custodial credit risk, \$12,695,076 was collateralized by securities held by the pledging financial institution and \$104,479 was uncollateralized.

INVESTMENTS

At December 31, 2009 and 2008, the District had the following investments and maturities:

	<u>12/31/2009</u> <u>Fair Value</u>	<u>Average Credit</u> <u>Quality/Ratings (1)</u>	<u>Less</u> <u>Than 1</u>
Treasury Money Market Fund	<u>\$ 1,486,932</u>	AAA/Aaa	<u>\$ 1,486,932</u>
Total Investments	<u><u>\$ 1,486,932</u></u>		<u><u>\$ 1,486,932</u></u>
	<u>12/31/2008</u> <u>Fair Value</u>	<u>Average Credit</u> <u>Quality/Ratings (1)</u>	<u>Less</u> <u>Than 1</u>
Treasury Money Market Fund	<u>\$ 1,480,912</u>	AAA/Aaa	<u>\$ 1,480,912</u>
Total Investments	<u><u>\$ 1,480,912</u></u>		<u><u>\$ 1,480,912</u></u>

(1) Ratings are provided to indicate associated *Credit Risk*. Ratings are from Standard & Poor's and Moody's Investors Service and are presented in that order.

*Investment Policies**District Policy*

Credit Risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. Generally, the District's investing activities are under the custody of the District Commissioners. Investing policies comply with the State Statutes. Kentucky Revised Statute 66.480 defines the following items as permissible investments:

- Obligations of the United States and of its agencies and instrumentalities;
- Obligations of any corporation of the United States Government;
- Obligations and contracts for future delivery or purchase of obligations backed by the full faith and credit of the United States or a United States government agency;
- Uncollateralized certificates of deposit issued by any bank or savings and loan institution rated in one (1) of the three (3) highest categories by a nationally recognized rating agency;

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HARDIN COUNTY WATER DISTRICT NO. 2NOTES TO FINANCIAL STATEMENTSDECEMBER 31, 2009 AND 2008NOTE D - DEPOSITS AND INVESTMENTS (CONTINUED)*INVESTMENTS (CONTINUED)*

- Certificates of deposit issued by or other interest-bearing accounts of any bank or savings and loan institution which are insured by the Federal Deposit Insurance Corporation or similar entity or which are collateralized, to the extent uninsured, by any obligations, including surety bonds, permitted by KRS 41.240(4)
- Bankers' acceptances for banks rated in one (1) of the three (3) highest categories by a nationally recognized rating agency;
- Commercial paper rated in the highest category by a nationally recognized rating agency;
- Bonds or certificates of indebtedness of this state and of its agencies and instrumentalities;
- Securities issued by a state or local government, or any instrumentality of agency thereof, in the United States, and rated in one (1) of the three (3) highest categories by a nationally recognized rating agency; and
- Shares of mutual funds, each of which shall have the following characteristics:
 1. The mutual fund shall be an open-end diversified investment company registered under the Federal Investment Company Act of 1940, as amended;
 2. The management company of the investment company shall have been in operation for at least five (5) years; and
 3. All of the securities in the mutual fund shall be eligible investments pursuant to this section.

Interest Rate Risk is the risk that changes in interest rates will adversely affect the fair value of an investment. Investments held for longer periods are subject to increased risk of adverse interest rate changes. The District policy provides that, to the extent practicable, investments are matched with anticipated cash flows. Investments are diversified to minimize the risk of loss resulting from over-concentration of assets in a specific maturity period, a single issuer, or an individual class of securities. **Concentration of Credit Risk** is the risk of loss attributed to the magnitude of the District's investment in a single issuer. U.S. Government securities and investments in mutual funds are excluded from this risk. The District does not have more than 5% or more of investments subject to the concentration of credit risk disclosure in any one issuer.

Custodial Credit Risk is the risk that, in the event of the failure of the counterparty, the District will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. The District did not have any investments in securities at December 31, 2009 and 2008.

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HARDIN COUNTY WATER DISTRICT NO. 2NOTES TO FINANCIAL STATEMENTSDECEMBER 31, 2009 AND 2008NOTE 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, 2009 and 2008:

<u>Restricted For</u>	<u>December 31, 2009</u>	<u>December 31, 2008</u>
Debt service	\$ 1,376,835	\$ 1,377,083
Depreciation fund	451,381	431,529
Escrow	132,381	124,079
Construction	814,270	652,549
Customer deposits	526,560	477,491
	<u>\$ 3,301,427</u>	<u>\$ 3,062,731</u>

NOTE F - CAPITAL ASSETS

Capital assets are recorded at cost.

Capital asset activity for the year ended December 31, 2009 follows.

	<u>Balance at</u>	<u>Additions</u>	<u>Retirements</u>	<u>Balance at</u>
	<u>December 31, 2008</u>			<u>December 31, 2009</u>
Non-Depreciable Assets:				
Land and land rights	\$ 552,983	\$ -	\$ -	\$ 552,983
Depreciable Assets:				
Structures and improvements	3,167,489	3,000	-	3,170,489
Supply mains	1,763,965	-	-	1,763,965
Water treatment plant	10,983,191	-	-	10,983,191
Standpipes, tanks and foundations	5,766,203	-	-	5,766,203
Transmission and distribution mains	30,157,163	65,977	-	30,223,140
Services	4,924,549	361,770	-	5,286,319
Hydrants	287,534	4,745	-	292,279
Office furniture and fixtures	319,380	24,398	-	343,778
Transportation equipment	988,766	66,436	(60,457)	994,745
Communication equipment	55,270	-	-	55,270
Other property and equipment	271,911	500	-	272,411
Capital assets in service	59,238,404	526,826	(60,457)	59,704,773
Construction in progress	115,144	2,195,703	-	2,310,847
Total capital assets	59,353,548	2,722,529	(60,457)	62,015,620
Less accumulated depreciation for:				
Structures and improvements	807,099	80,066	-	887,165
Supply mains	705,005	44,099	-	749,104
Water treatment plant	2,710,010	222,030	-	2,932,040
Standpipes, tanks and foundations	1,502,301	145,321	-	1,647,622
Transmission and distribution mains	6,224,306	610,695	-	6,835,001
Services	1,388,689	165,014	-	1,553,703
Hydrants	192,986	15,068	-	208,054
Office furniture and fixtures	276,329	16,369	-	292,698
Transportation equipment	640,173	106,030	(60,457)	685,746
Communication equipment	55,270	-	-	55,270
Other property and equipment	268,659	1,569	-	270,228
Total accumulated depreciation:	14,770,827	1,406,261	(60,457)	16,116,631
Net capital assets	\$ 44,582,721	\$ 1,316,268	\$ -	\$ 45,898,989

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HARDIN COUNTY WATER DISTRICT NO. 2

NOTES TO FINANCIAL STATEMENTS

DECEMBER 31, 2009 AND 2008

NOTE F - CAPITAL ASSETS (CONTINUED)

Capital asset activity for the year ended December 31, 2008 follows.

	Balance at December 31, 2007	Additions	Retirements	Balance at December 31, 2008
Non-Depreciable Assets:				
Land and land rights	\$ 532,983	\$ 20,000	\$ -	\$ 552,983
Depreciable Assets:				
Structures and improvements	3,167,489	-	-	3,167,489
Supply mains	1,763,965	-	-	1,763,965
Water treatment plant	10,983,191	-	-	10,983,191
Standpipes, tanks and foundations	5,766,203	-	-	5,766,203
Transmission and distribution mains	26,191,251	3,965,912	-	30,157,163
Services	4,619,668	304,881	-	4,924,549
Hydrants	268,348	19,186	-	287,534
Office furniture and fixtures	397,213	25,758	(103,591)	319,380
Transportation equipment	907,809	131,923	(50,966)	988,766
Communication equipment	58,962	-	(3,692)	55,270
Other property and equipment	389,660	900	(118,649)	271,911
Capital assets in service	55,046,742	4,468,560	(276,898)	59,238,404
Construction in progress	1,418,324	51,810	(1,354,990)	115,144
Total capital assets	56,465,066	4,520,370	(1,631,888)	59,353,548
Less accumulated depreciation for:				
Structures and improvements	727,182	79,917	-	807,099
Supply mains	660,905	44,100	-	705,005
Water treatment plant	2,487,979	222,031	-	2,710,010
Standpipes, tanks and foundations	1,356,978	145,323	-	1,502,301
Transmission and distribution mains	5,686,967	537,339	-	6,224,306
Services	1,248,457	140,232	-	1,388,689
Hydrants	178,036	14,950	-	192,986
Office furniture and fixtures	365,390	14,530	(103,591)	276,329
Transportation equipment	586,446	104,693	(50,966)	640,173
Communication equipment	58,962	-	(3,692)	55,270
Other property and equipment	375,070	12,238	(118,649)	268,659
Total accumulated depreciation	13,732,372	1,315,353	(276,898)	14,770,827
Net capital assets	\$ 42,732,694	\$ 3,205,017	\$ (1,354,990)	\$ 44,582,721

During the years ended December 31, 2009 and 2008, the District capitalized \$30,240 and \$0 of interest and expensed \$883,201 and \$925,912 of interest.

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HARDIN COUNTY WATER DISTRICT NO. 2NOTES TO FINANCIAL STATEMENTSDECEMBER 31, 2009 AND 2008NOTE G - LONG-TERM OBLIGATIONS

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

<u>Issue</u>	<u>Interest Rate</u>	<u>Face Amount</u>	<u>Bonds Due 12/31/2009</u>	<u>Bonds Due 12/31/2008</u>
1999 Series A	3.7% - 5.0%	7,005,000	5,965,000	6,115,000
2002 Series A	4.375%	1,013,000	960,500	972,000
2002 Series B	1.75% - 3.5%	2,190,000	600,000	885,000
2002 Series C	2.0% - 3.75%	3,020,000	1,895,000	2,240,000
2003 Series	3.5% - 4.625%	4,485,000	3,670,000	3,815,000
2004 Series A	2.0% - 4.0%	2,940,000	2,460,000	2,565,000
2005 Series A	4.375%	2,990,000	2,889,500	2,924,500
2005 Series B	4.1%	1,775,000	1,560,000	1,615,000

On December 18, 2007, the District entered into an interim financing agreement with the Kentucky Rural Water Finance Corporation to borrow up to \$2,480,000 for its Phase IV project. The loan initially carried an interest rate of 4.125%. The rate was changed to 3.7% in January 2009. The District borrowed \$941,967 during 2009 and \$171,802 during 2008. The loan will be converted to the 2007A bond issue when all draws have been completed.

The District requires new customers to provide a \$60 deposit for initial water service. Current customers in good standing who add additional service locations are not required to pay an additional deposit.

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.

(Continued next page)

HARDIN COUNTY WATER DISTRICT NO. 2

NOTES TO FINANCIAL STATEMENTS

DECEMBER 31, 2009 AND 2008

NOTE G - LONG-TERM OBLIGATIONS (CONTINUED)

Long-term liability activity for the year ended December 31, 2009, was as follows:

	Balance at December 31, 2008	Additions	Reductions	Balance at December 31, 2009	Amount Due Within One Year
Bonds and notes payable:					
Revenue bonds	\$ 21,131,500	\$ -	\$ (1,131,500)	\$ 20,000,000	\$ 1,158,500
Notes payable	171,802	941,967	-	1,113,769	1,113,769
Total bonds and notes payable	21,303,302	941,967	(1,131,500)	21,113,769	2,272,269
Other liabilities:					
Customer deposits	420,579	72,480	(44,127)	448,932	44,893
Accrued vacation	72,215	-	(6,230)	65,985	6,599
Customer advances for construction	369,237	9,939	(129,201)	249,975	77,254
Total other liabilities	862,031	82,419	(179,558)	764,892	128,746
Long-term liabilities	\$ 22,165,333	\$ 1,024,386	\$ (1,311,058)	\$ 21,878,661	\$ 2,401,015

Long-term liability activity for the year ended December 31, 2008, was as follows:

	Balance at December 31, 2007	Additions	Reductions	Balance at December 31, 2008	Amount Due Within One Year
Bonds and notes payable:					
Revenue bonds	\$ 22,246,000	\$ -	\$ (1,114,500)	\$ 21,131,500	\$ 1,131,500
Notes payable	-	171,802	-	171,802	171,802
Total bonds and notes payable	22,246,000	171,802	(1,114,500)	21,303,302	1,303,302
Other liabilities:					
Customer deposits	378,254	70,045	(27,720)	420,579	42,058
Accrued vacation	74,089	-	(1,874)	72,215	7,222
Customer advances for construction	453,538	9,992	(104,293)	369,237	125,949
Total other liabilities	915,881	80,037	(133,887)	862,031	175,229
Long-term liabilities	\$ 23,161,881	\$ 251,839	\$ (1,248,387)	\$ 22,165,333	\$ 1,478,531

(Continued next page)

HARDIN COUNTY WATER DISTRICT NO. 2NOTES TO FINANCIAL STATEMENTSDECEMBER 31, 2009 AND 2008NOTE G - LONG-TERM OBLIGATIONS (CONTINUED)

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, 2009:

Revenue Bonds			
<u>Year</u>	<u>Principal</u>	<u>Interest</u>	<u>Totals</u>
2010	\$ 1,158,500	\$ 841,406	\$ 1,999,906
2011	1,220,500	797,780	2,018,280
2012	863,000	758,500	1,621,500
2013	900,500	724,347	1,624,847
2014	937,500	688,252	1,625,752
2015-2019	3,075,500	3,038,377	6,113,877
2020-2024	3,933,500	2,289,129	6,222,629
2025-2029	3,395,500	1,426,860	4,822,360
2030-2034	2,339,000	705,869	3,044,869
2035-2039	1,299,000	347,897	1,646,897
2040-2044	877,500	110,885	988,385
Total	\$ 20,000,000	\$ 11,729,302	\$ 31,729,302

<u>Year</u>	<u>Sinking Fund Requirements</u>
2010	\$ 1,999,906
2011	2,018,280
2012	1,621,500
2013	1,624,847
2014	1,625,752
2015-2019	6,113,877
2020-2024	6,222,629
2025-2029	4,822,360
2030-2034	3,044,869
2035-2039	1,646,897
2040-2044	988,385
Total	\$ 31,729,302

(Continued next page)

HARDIN COUNTY WATER DISTRICT NO. 2NOTES TO FINANCIAL STATEMENTSDECEMBER 31, 2009 AND 2008NOTE G - LONG-TERM OBLIGATIONS (CONTINUED)

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 1999 Series A, 2002 Series A, B and C, 2003 Series, 2004 Series A, 2005 Series A and B issues.

Depreciation Fund

This fund receives, on a monthly basis, \$18,700. 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 - 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 employed before September 1, 2008, are required to contribute 5% of their annual covered salary and those hired on or after September 1, 2008, are required to contribute 6% of their annual covered salary. The District is required to contribute at an actuarially determined rate. The rate at December 31, 2009, was 16.16% of covered payroll. The contribution requirements of the District 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, 2009, 2008 and 2007 were \$327,279, \$233,064, and \$226,896. Employee contributions were \$81,071, \$78,782 and \$77,340 and covered payroll was \$1,655,839, \$1,574,409 and \$1,546,805. All payments were made to the retirement system in the amount of the annually required contributions.

(Continued next page)

HARDIN COUNTY WATER DISTRICT NO. 2NOTES TO FINANCIAL STATEMENTSDECEMBER 31, 2009 AND 2008(CONCLUDED)NOTE I - CAPITAL CONTRIBUTIONS

The following schedule details the sources of capital contributions for the years ended December 31, 2009 and 2008:

<u>Source</u>	<u>2009</u>	<u>2008</u>
State of Kentucky	\$ 1,108,042	\$ 2,020,380
Federal Government	120,546	645,847
Tap Fees	173,350	221,773
Developers	129,201	104,293
Hardin County Fiscal Court	10,000	240,250
	<u>\$ 1,541,139</u>	<u>\$ 3,232,543</u>

NOTE J - COMMITMENTS

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

NOTE K - 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 L - SUBSEQUENT EVENTS

In January 2010, the rate on the interim financing agreement with the Kentucky Rural Water Finance Corporation changed to 2.9%.

OTHER SUPPLEMENTARY INFORMATION

HARDIN COUNTY WATER DISTRICT NO. 2SCHEDULE I - BOND AND INTEREST REQUIREMENTSDECEMBER 31, 2009

	\$ 7,005,000 1999 SERIES A		\$ 1,013,000 2002 SERIES A	
	<u>BOND</u>	<u>INTEREST</u>	<u>BOND</u>	<u>INTEREST</u>
2010	\$ 155,000	\$ 287,038	\$ 12,000	\$ 42,021
2011	165,000	279,476	12,500	41,497
2012	170,000	271,520	13,500	40,950
2013	180,000	263,207	14,000	40,359
2014	190,000	254,420	14,500	39,747
2015	200,000	245,158	15,500	39,113
2016	210,000	235,420	16,000	38,434
2017	220,000	225,207	17,000	37,734
2018	230,000	214,520	17,500	36,991
2019	240,000	203,358	19,000	36,225
2020	250,000	191,720	19,500	35,394
2021	265,000	179,489	20,500	34,541
2022	275,000	166,526	21,500	33,644
2023	290,000	152,825	22,500	32,703
2024	305,000	138,396	24,000	31,719
2025	320,000	123,000	25,000	30,669
2026	335,000	106,625	26,500	29,575
2027	355,000	89,375	27,500	28,416
2028	375,000	71,125	29,000	27,213
2029	390,000	52,000	30,500	25,944
2030	410,000	32,000	32,000	24,609
2031	435,000	10,875	33,500	23,209
2032			35,000	21,744
2033			37,000	20,213
2034			39,000	18,594
2035			40,500	16,888
2036			43,000	15,116
2037			45,000	13,234
2038			47,000	11,266
2039			49,500	9,209
2040			52,000	7,044
2041			54,500	4,769
2042			54,500	2,384
2043				
2044				
	<u>\$ 5,965,000</u>	<u>\$ 3,793,280</u>	<u>\$ 960,500</u>	<u>\$ 891,168</u>

(Continued next page)

HARDIN COUNTY WATER DISTRICT NO. 2

SCHEDULE I - BOND AND INTEREST REQUIREMENTS

DECEMBER 31, 2009

(CONTINUED)

	\$ 2,190,000 2002 SERIES B		\$ 3,020,000 2002 SERIES C		\$ 4,485,000 2003 SERIES A	
	BOND	INTEREST	BOND	INTEREST	BOND	INTEREST
2010	\$ 295,000	\$ 15,616	\$ 350,000	\$ 61,922	\$ 145,000	\$ 156,643
2011	305,000	5,338	365,000	49,673	160,000	151,015
2012			380,000	36,445	75,000	146,609
2013			395,000	22,396	80,000	143,703
2014			405,000	7,594	80,000	140,703
2015					85,000	137,609
2016					90,000	134,283
2017					95,000	130,650
2018					95,000	126,779
2019					100,000	122,733
2020					105,000	118,479
2021					110,000	114,018
2022					115,000	109,349
2023					120,000	104,263
2024					130,000	98,638
2025					135,000	92,675
2026					140,000	86,488
2027					145,000	80,075
2028					155,000	73,325
2029					165,000	66,022
2030					170,000	58,275
2031					180,000	50,181
2032					190,000	41,625
2033					200,000	32,606
2034					110,000	25,438
2035					115,000	20,234
2036					120,000	14,800
2037					125,000	9,134
2038					135,000	3,122
2039						
2040						
2041						
2042						
2043						
2044						
	<u>\$ 600,000</u>	<u>\$ 20,954</u>	<u>\$ 1,895,000</u>	<u>\$ 178,030</u>	<u>\$ 3,670,000</u>	<u>\$ 2,589,474</u>

(Continued next page)

HARDIN COUNTY WATER DISTRICT NO. 2SCHEDULE I - BOND AND INTEREST REQUIREMENTSDECEMBER 31, 2009(CONTINUED)

	<u>\$ 2,940,000</u>		<u>\$ 2,990,000</u>		<u>\$ 1,775,000</u>	
	<u>2004 SERIES A</u>		<u>2005 SERIES A</u>		<u>2005 SERIES B</u>	
	<u>BOND</u>	<u>INTEREST</u>	<u>BOND</u>	<u>INTEREST</u>	<u>BOND</u>	<u>INTEREST</u>
2010	\$ 105,000	\$ 89,020	\$ 36,500	\$ 126,416	\$ 60,000	\$ 62,730
2011	110,000	85,795	38,000	124,818	65,000	60,168
2012	115,000	82,420	39,500	123,156	70,000	57,400
2013	115,000	78,826	41,500	121,428	75,000	54,428
2014	125,000	74,926	43,000	119,612	80,000	51,250
2015	125,000	70,708	45,000	117,732	85,000	47,868
2016	135,000	66,158	47,000	115,762	85,000	44,383
2017	145,000	61,113	49,000	113,706	90,000	40,795
2018	155,000	55,563	51,000	111,562	95,000	37,003
2019	160,000	49,575	53,500	109,332	105,000	32,903
2020	170,000	43,140	56,000	106,990	105,000	28,598
2021	175,000	36,413	58,500	104,540	115,000	24,088
2022	190,000	29,200	61,000	101,982	120,000	19,270
2023	200,000	21,400	63,500	99,312	130,000	14,145
2024	215,000	13,100	66,500	96,534	135,000	8,713
2025	220,000	4,400	69,000	93,626	145,000	2,973
2026			72,000	91,006		
2027			75,500	87,456		
2028			78,500	84,154		
2029			82,000	80,718		
2030			85,500	77,132		
2031			89,500	73,390		
2032			93,500	69,476		
2033			97,500	65,384		
2034			101,500	61,118		
2035			106,000	56,678		
2036			111,000	52,040		
2037			115,500	47,184		
2038			120,500	42,132		
2039			126,000	36,860		
2040			131,500	31,346		
2041			137,000	25,594		
2042			143,000	19,600		
2043			149,500	13,344		
2044			155,500	6,804		
	<u>\$ 2,460,000</u>	<u>\$ 861,757</u>	<u>\$ 2,889,500</u>	<u>\$ 2,807,924</u>	<u>\$ 1,560,000</u>	<u>\$ 586,715</u>

(Continued next page)

HARDIN COUNTY WATER DISTRICT NO. 2SCHEDULE I -- BOND AND INTEREST REQUIREMENTSDECEMBER 31, 2009(CONCLUDED)

TOTAL ALL ISSUES			
	<u>BOND</u>		<u>INTEREST</u>
2010	\$ 1,158,500	\$	841,406
2011	1,220,500		797,780
2012	863,000		758,500
2013	900,500		724,347
2014	937,500		688,252
2015	555,500		658,188
2016	583,000		634,440
2017	616,000		609,205
2018	643,500		582,418
2019	677,500		554,126
2020	705,500		524,321
2021	744,000		493,089
2022	782,500		459,971
2023	826,000		424,648
2024	875,500		387,100
2025	914,000		347,343
2026	573,500		313,694
2027	603,000		285,322
2028	637,500		255,817
2029	667,500		224,684
2030	697,500		192,016
2031	738,000		157,655
2032	318,500		132,845
2033	334,500		118,203
2034	250,500		105,150
2035	261,500		93,800
2036	274,000		81,956
2037	285,500		69,552
2038	302,500		56,520
2039	175,500		46,069
2040	183,500		38,390
2041	191,500		30,363
2042	197,500		21,984
2043	149,500		13,344
2044	155,500		6,804
	<u>\$ 20,000,000</u>	<u>\$</u>	<u>11,729,302</u>

HARDIN COUNTY WATER DISTRICT NO. 2SCHEDULE II - GENERAL AND ADMINISTRATIVE EXPENSESYEARS ENDED DECEMBER 31, 2009 AND 2008

	<u>2009</u>	<u>2008</u>
Salaries	\$ 552,884	\$ 533,996
Commissioner's salaries	30,340	31,630
Employee benefits	410,117	392,268
Materials and supplies	48,441	42,444
Professional fees	16,700	18,850
Insurance	118,794	95,198
Advertising	4,988	2,284
Loan bad debt	-	50,000
Other general and administrative	284,715	289,899
	<u>\$ 1,466,979</u>	<u>\$ 1,456,569</u>

HARDIN COUNTY WATER DISTRICT NO. 2

SCHEDULE III - ORGANIZATION DATA

DECEMBER 31, 2009

WATER COMMISSIONERS

Michael Bell - Chairman
Morris Miller - Secretary/Treasurer
Cordell Tabb - Member
John Effinger - Member
Tim Davis - Member

ATTORNEY

Damon R. Talley - Hodgenville, Kentucky

GENERAL MANAGER

James Jeffries

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
PHILIP A. LOGSDON, CPA



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

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

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, 2009, and have issued our report thereon dated February 16, 2010. 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 as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Hardin County Water District No. 2's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the District's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses and therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. However, as described in the accompanying schedule of findings and questioned costs, we identified certain deficiencies in internal control over financial reporting that we consider to be material weaknesses.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A material weakness is a deficiency, or combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the District's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiency described as item 2009-1 in the accompanying schedule of findings and questioned costs to be a material weakness.

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 or other matters that are required to be reported under *Government Auditing Standards*.

Hardin County Water District No. 2's response to the findings identified in our audit is described in the accompanying schedule of findings and responses. We did not audit Hardin County Water District No. 2's response and, accordingly, we express no opinion on it.

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
February 16, 2010

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

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

Compliance

We have audited the compliance of Hardin County Water District No. 2, 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, 2009. Hardin County Water District No. 2'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 Hardin County Water District No. 2's management. Our responsibility is to express an opinion on Hardin County Water District No. 2's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, and OMB Circular A-133 *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about Hardin County Water District No. 2'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 Hardin County Water District No. 2's compliance with those requirements.

In our opinion, Hardin County Water District No. 2, 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, 2009.

Internal Control Over Compliance

The management of Hardin County Water District No. 2, 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 Hardin County Water District No. 2's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the District's internal control over compliance.

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

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

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

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
February 16, 2010

HARDIN COUNTY WATER DISTRICT NO. 2
 SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
 YEAR ENDED DECEMBER 31, 2009

<u>FEDERAL GRANTOR/ PASS - THROUGH GRANTOR/ PROGRAM OR CLUSTER TITLE</u>	<u>FEDERAL CFDA NUMBER</u>	<u>PASS- THROUGH GRANTOR NUMBER</u>	<u>FEDERAL EXPENDITURES</u>
<u>U.S. DEPARTMENT OF AGRICULTURE</u>			
Passed Through Kentucky Rural Water Finance Corporation Rural Utilities Service - Water and Waste Disposal Systems For Rural Communities	10.760 *	N/A	<u>941,967</u>
TOTAL U.S. DEPARTMENT OF AGRICULTURE			<u>941,967</u>
<u>U.S. ENVIRONMENTAL PROTECTION AGENCY</u>			
Surveys, Studies, Investigations and Special Purpose Grants	66.606	N/A	<u>45,242</u>
TOTAL U.S. ENVIRONMENTAL PROTECTION AGENCY			<u>45,242</u>
<u>U.S. DEPARTMENT OF HOMELAND SECURITY</u>			
Passed Through Kentucky Office of Emergency Management: Disaster Grants - Public Assistance	97.036	FEMA-DR-1818-KY	<u>75,304</u>
TOTAL U.S. DEPARTMENT OF HOMELAND SECURITY			<u>75,304</u>
TOTAL EXPENDITURES OF FEDERAL AWARDS			<u>\$ 1,062,513</u>

* Denotes major federal program.

The accompanying notes are an integral part of this schedule.

HARDIN COUNTY WATER DISTRICT NO. 2

NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

YEAR ENDED DECEMBER 31, 2009

NOTE A - BASIS OF PRESENTATION

The accompanying schedule of expenditures of federal awards includes the federal grant activity of Hardin County Water District No. 2 and is presented on the accrual basis of accounting. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of, the basic financial statements.

NOTE B - SUBRECIPIENTS

There were no subrecipients during the fiscal year.

SCHEDULE OF FINDINGS AND QUESTIONED COSTS

HARDIN COUNTY WATER DISTRICT NO. 2
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED DECEMBER 31, 2009

Section I-Summary of Auditor's Results

Financial Statements

Type of auditor's report issued (unqualified):

Internal control over financial reporting:

- Material weakness(es) identified? yes no
- Significant deficiency(ies) identified
that are not considered to be material
weaknesses? yes none reported

Noncompliance material to financial
statements noted? yes no

Federal Awards

Internal control over major programs:

- Material weakness(es) identified? yes no
- Significant deficiency(ies) identified
that are not considered to be material
weaknesses? yes none reported

Type of auditor's report issued on compliance for major programs (unqualified):

Any audit findings disclosed that are
required to be reported in accordance
with section 510(a) of Circular A-133? yes no

Identification of major programs:

<u>CFDA Number(s)</u>	<u>Name of Federal Program or Cluster</u>
10.760	Water and Waste Disposal Systems for Rural Communities

Dollar threshold used to distinguish
Between type A and type B programs: \$ 300,000

Auditee qualified as low-risk auditee? yes no

Section II - Financial Statement Findings

MATERIAL WEAKNESS**REFERENCE NUMBER 2009-1 FINANCIAL STATEMENT PRESENTATION**

Criteria: The District's management is responsible for establishing and maintaining internal controls over the application of transactions and the preparation of financial statements.

Condition: As part of the audit we noted that material adjustments were not identified by the District's internal control.

Cause: The District did not make all necessary adjustments when closing the year.

Effect: The design of the internal controls over financial reporting limits the ability of the District to provide accurate financial information.

Recommendation: We recommend District management and financial personnel continue to increase their awareness and knowledge of all procedures and processes involved in preparing financial statements and develop internal control policies to ensure proper financial statement presentation.

Management Response: Management will review the options available to ensure that necessary adjustments are made in accordance with the normal closing process.

Section III - Federal Award Findings and Questioned Costs

No matters were reported.

SCHEDULE OF PRIOR YEAR AUDIT FINDINGS

HARDIN COUNTY WATER DISTRICT NO. 2

SCHEDULE OF PRIOR YEAR AUDIT FINDINGS

DECEMBER 31, 2009

There were no prior year audit findings.