

CITY OF WINCHESTER, KENTUCKY
AUDITED BASIC FINANCIAL STATEMENTS
INCLUDING SUPPLEMENTARY DATA
AND INDEPENDENT AUDITOR'S REPORTS
FOR THE YEAR ENDED JUNE 30, 2013

**CITY OF WINCHESTER, KENTUCKY
JUNE 30, 2013**

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PROFILE OF GOVERNMENT

The City of Winchester, Kentucky was incorporated in 1793. The City is the county seat of Clark County, which is in central Kentucky, commonly referred to as the Bluegrass Region. The City currently occupies 8.4 square miles (5,377 acres) and serves a population of 18,368 (2010 census).

The City of Winchester elected to operate under the City Manager plan of government, pursuant to KRS 83A.150, in 1968. Executive, legislative, and policy-making authority are vested in a governing council consisting of the Mayor and four Commissioners. The Board of Commissioners is elected on a non-partisan basis. The Mayor serves a four-year term, while Commissioners serve a two-year term. The Board of Commissioners is responsible for passing ordinances, setting tax rates, adopting a budget, hiring, and making appointments.

The City Manager is responsible for carrying out the policies, orders, and ordinances of the Board and for overseeing the day-to-day operations of the City. The City Manager supervises Administration, which consists of the Legal, City Manager, Finance, Planning, Main Street, Engineering, and Administration departments. He also supervises the Central Communications, Police, Fire, Emergency Services (EMS), and Public Works departments. (The City of Winchester provides county-wide services, by agreement with the county, for Dispatch and EMS.)

The City of Winchester is also responsible for water and sewer services. In 1958, the City established Winchester Municipal Utilities (WMU) as a public project to oversee water, sewer, and garbage disposal. WMU has full control over the supervision and management of these activities. WMU is considered a business-type activity because it charges fees for its services. WMU is separate in that it has its own budget, accounts, revenues, expenses, and its own audit. However, WMU is considered a component unit of the City of Winchester because the Winchester Board of Commissioners appoints members to the WMU Commission, sets rates, and approves bond issuances. Land is owned in the name of the City of Winchester. Therefore, WMU's audit is incorporated into the City's. Contact information for WMU is listed at the end of this report.

WMU is a municipal utility enterprise fund separate from the City and which has been separately audited. A full discussion of WMU's financial activities can be found in that audit. WMU's audit was prepared by Summers, McCrary, and Sparks, PSC and was accepted by the utility commission on November 7, 2013.

The City's fiscal year begins July 1 and ends June 30, according to state statute. An annual budget, based on the fiscal year, is prepared by fund and department. Budget-to-actual comparisons are provided in this report.

The annual budget serves as the foundation for financial planning and control. All departments are required to submit budget requests in the early spring. The City Manager then uses these figures as a starting point for developing a draft budget. The draft budget is then submitted to the Board of Commissioners for first and second readings. The City is required to have a final budget in place before June 30.

CITY OF WINCHESTER, KENTUCKY
JUNE 30, 2013

OTHER INFORMATION

Emergencies

The City did not declare any emergencies.

Elected Officials

In the November 2012 election, the citizens voted Kenny Book, Shannon Cox, Rick Beach, and Kitty Strode as commissioners (two-year term) effective January 1, 2013.

Retirements

The City recognized two retirements this past year. Communications Officer Donna Estes retired after 10 years of service. City Manager Ken Kerns retired after 6 years of service.

ELECTED OFFICIALS

The following elected officials are dedicated to improvement of services to the citizens of Winchester. They can be reached at the City Manager's office.

Mayor Edallen York Burtner
Commissioner Kenny Book
Commissioner Rick Beach
Commissioner Shannon Cox
Commissioner Kitty Strode

CITY OF WINCHESTER, KENTUCKY
JUNE 30, 2013

CONTACT INFORMATION

If you have any questions about this report or need additional information, the following people will be happy to help you.

Debbie Bailey
City Treasurer
32 Wall Street, P.O. Box 4135
Winchester, KY 40392-4135
859-744-1660
dbailey@winchesterky.com

Matthew Belcher
City Manager
32 Wall Street, P. O. Box 40
Winchester, KY 40392-0040
859-744-2821
mbelcher@winchesterky.com

Information about Winchester Municipal Utilities can be obtained from their separately issued financial statements or by contacting these individuals:

Jennifer Sparks
Supervisor of Finance and Accounting
Winchester Municipal Utilities
150 North Main Street, P. O. Box 4177
Winchester, KY 40392-4177
859-744-5434
jennifers@wmutilities.com

Mike Flynn
General Manager
Winchester Municipal Utilities
150 North Main Street, P.O. Box 4177
Winchester, KY 40392-4177
859-744-5434

Additional information about the economic environment in Winchester and Clark County can be obtained from:

Todd Denham
W/CC Industrial Development Authority
2 South Maple Street
Winchester, KY 40391
859-744-5627

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

MEMBERS:

AMERICAN INSTITUTE
OF CERTIFIED PUBLIC ACCOUNTANTS

KENTUCKY SOCIETY
OF CERTIFIED PUBLIC ACCOUNTANTS

PRIVATE COMPANIES
PRACTICE SECTION OF THE AMERICAN INSTITUTE
OF CERTIFIED PUBLIC ACCOUNTANTS

STUART K. MCCRARY, JR., CPA
THOMAS S. SPARKS, CPA
JAMES R. WHITTEN, CPA

SUSAN A. LACY, CPA
DEBORAH L. MAYNARD, CPA
RYAN R. LASKI, CPA

LAURENCE T. SUMMERS
1961-1992

INDEPENDENT AUDITOR'S REPORT

To the City Commissioners
City of Winchester, Kentucky

We have audited the accompanying financial statements of the governmental activities, the business-type activities, the aggregate discretely presented component unit, each major fund, and the aggregate remaining fund information of City of Winchester, Kentucky as of and for the year ended June 30, 2013, and the related notes to the financial statements, which collectively comprise the City's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express opinions on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the City of Winchester, Kentucky, as of June 30, 2013, and the respective changes in financial position and, where applicable, cash flows thereof and the respective budgetary comparisons for the general fund and capital equipment and federal grant funds for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and police and firefighter's pension fund on pages 7-28 and 74 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the City of Winchester, Kentucky's basic financial statements. The introductory section and combining nonmajor fund financial statements 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 is presented for purposes of additional analysis as required by the U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is also not required part of the basic financial statements

The combining nonmajor fund financial statements and the schedule of expenditures of federal awards are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the combining and individual nonmajor fund financial statements are fairly stated, in all material respects, in relation to the basic financial statements as a whole.

The introductory sections have not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we do not express an opinion or provide any assurance on them.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated February 10, 2014, on our consideration of the City of Winchester, Kentucky's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering City of Winchester, Kentucky's internal control over financial reporting and compliance.

Summers, McCrary & Sparks, PSC

Winchester, Kentucky
February 10, 2014

MANAGEMENT DISCUSSION AND ANALYSIS

CITY OF WINCHESTER, KENTUCKY
MANAGEMENT DISCUSSION AND ANALYSIS
JUNE 30, 2013

The management team of the City of Winchester presents this Management Discussion and Analysis to outline the financial highlights and provide their analysis of the financial reports by explaining changes in the financial data. This narrative is intended to disclose any known significant events or decisions that affect the financial condition of the City. In addition, supplementary information has been included that we hope will help our citizens understand the City's operations.

EXECUTIVE SUMMARY

We at the City continually strive to serve the citizens of this community. It is important to remember that serving our citizens requires both manpower and money to fund the day-to-day operations that improve the quality of life in our community.

Money is provided through taxes, fees, licenses, permits, investments, charges for services, intergovernmental revenue, and grants. Collection of funds is performed mainly by the Finance Department. Every effort is made to collect funds fairly, equitably, and efficiently. The four main revenues are occupational license fees, insurance premium taxes, property taxes, and EMS revenue.

Service to our citizens includes central dispatching (county-wide), police, fire, emergency medical services (county-wide), public works, and administrative departments. All departments make every effort to use financial resources effectively and efficiently. It must be noted, however, that about 75% of general fund expenses are in the form of manpower (personnel costs) and that most of these personnel costs relate to public safety.

The City makes every effort to hire and retain qualified people who deliver services to our citizens. To insure these services, employee wages and benefits are a vital component of the City's financial operations.

Personnel costs include wages, taxes, retirement, and insurance. The City granted a 3% cost-of-living adjustment (COLA) for FY 2013, and a 2% COLA for FY 2014. The City's self-insured employee health insurance plan continues to help manage the City's health care costs and keep those benefits on a sustainable level to protect both taxpayers and employees.

Retirement costs are mandated by the state. These rates are what the City pays on employee wages to the state-run retirement system (CERS-County Employees Retirement System). The table below shows how these rates had been increasing. For FY 2014, the state granted a temporary one-year reduction. The decrease for FY 2015 reflects changes made by the 2013 Kentucky legislature that reset the amortization period of the pension obligations.

CERS RATES

| | | |
|---------|--------|--------|
| FY 2015 | 17.67% | 34.31% |
| FY 2014 | 18.89% | 35.70% |
| FY 2013 | 19.55% | 37.60% |
| FY 2012 | 18.96% | 35.76% |
| FY 2011 | 16.93% | 33.25% |

CITY OF WINCHESTER, KENTUCKY
MANAGEMENT DISCUSSION AND ANALYSIS
JUNE 30, 2013

The total the City paid for retirement costs in FY 2013 was approximately \$1.9 million. We estimate that retirement costs in FY 2014 will be about \$2.2 million. In FY 2014, local government employers benefitted from the first decrease in employer contribution rates since 2008. Lower rates reflect improved investment performance, changes in health insurance administration, and retirement benefit changes for the County Employees Retirement System.

These costs affect the goods and services that the City purchases to provide public services. The City, like any person or business, must pay for the things we use every day and the services that we have to buy from someone else. Some of the things we use every day are evident (paper, computers, uniforms, vehicles). But other things are not seen, like paying for gasoline or electricity. What is important, though, is that these costs are also increasing.

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OVERVIEW OF THE FINANCIAL STATEMENTS

The basic financial statements include two kinds of statements that present different views of the City: government-wide financial statements and fund financial statements.

The government-wide financial statements include a *Statement of Net Position* and a *Statement of Activities*. These two statements provide both short-term and long-term information about the City's overall financial status. The government-wide financial statements have been prepared using the full accrual basis of accounting versus the modified accrual method used in the fund financial statements. A reconciliation report is provided as a key to understanding the changes between the two reporting methods.

These two statements divide the City of Winchester into two types of activities. Governmental activities include basic services, such as general administration, police, fire, and public works. Payroll taxes, insurance premiums taxes, property taxes, licenses, and state and federal grants finance most of these activities. Business-type activities include services for which fees are charged to customers to help cover all or most of the cost of certain services.

Government-wide statements present capital assets on the *Statement of Net Position*, including infrastructure assets. This is a significant difference between the government-wide statements and the fund statements. The infrastructure component of the standard is intended to provide financial information about the City's roads, bridges, storm sewers, and other infrastructure assets.

The *Statement of Net Position* provides information on all the City's assets and liabilities, including long-term debt and capital assets. The difference between assets and liabilities is reported as net position. Increases or decreases in net position will be analyzed to determine whether the financial position of the City is improving or deteriorating.

CITY OF WINCHESTER, KENTUCKY
MANAGEMENT DISCUSSION AND ANALYSIS
JUNE 30, 2013

The *Statement of Activities* provides information on how the City's net position changed during the most recent year. Amounts reported on this statement include depreciation of capital assets, rather than the purchase of capital assets which are reported in the fund statements (and our budgetary process). Depreciation provides a measure of how much of our capital assets have been used in the operation. Comparing depreciation expense to our capital purchases can give us an indicator of whether our capital investments are keeping pace with the use of these assets.

The remaining statements are fund financial statements that focus on the individual parts of City government. These statements report the City's operations in more detail than the government-wide statements. There are three types of fund financial statements.

- 1) The governmental funds statements tell how general government's basic services were financed and spent in the short term, as well as what remains for future spending. They focus on the City's most significant or "major" funds and groups of funds, not the City as a whole.
- 2) The proprietary funds statements tell how Winchester Municipal Utilities (WMU is the City's water, sewer, and solid waste component) services and activities were financed and spent in the short term, as well as what remains for future spending.
- 3) The fiduciary funds statements provide financial information about the local Winchester Police and Firefighter's Pension Fund and an agency fund. The pension fund can only be used for the trust beneficiaries. In addition, the City provides administrative services for the Bluegrass Regional Cable Commission. These activities are reported in the agency fund. The City is responsible for ensuring that the assets reported in these funds are used for their intended purposes. These activities are excluded from the City's government-wide financial statements because the City cannot use these assets to finance its operations.

Following the fund financial statements are *Notes to the Financial Statements*. The note disclosures explain some of the information in the financial statements and provide more detailed data. Notes are an integral component of the basic financial statements.

Following the notes is the required supplementary information about the local pension fund (fiduciary fund).

The final part of the basic financial statements includes other supplementary information that includes combining schedules for the non-major governmental funds and the *Schedule of Expenditures of Federal Awards*. The City established these additional special revenue funds to control and manage money for particular purposes or to show that it is properly using certain taxes and grants. The *Schedule of Expenditures of Federal Awards* outlines the federal grants awarded to the City and expenditures during the year for each of those programs.

CITY OF WINCHESTER, KENTUCKY
MANAGEMENT DISCUSSION AND ANALYSIS
 JUNE 30, 2013

FINANCIAL HIGHLIGHTS

Statement of Net Position

The Statement of Net Position provides a long-term view of the City's financial position. This report includes both capital assets and long term liabilities that outline a more comprehensive view of the City's financial resources. *Net Position* is the difference between total assets and deferred outflows of resources less total liabilities and deferred inflows of resources. This section is further divided into three components: net investment in capital assets, restricted, and unrestricted. *Net investment in capital assets* reflects real estate and personal property less depreciation and the amounts borrowed to purchase those assets. The *restricted* component is subject to constraints imposed by legal restrictions, for specific funds or projects. And, the *unrestricted* component represents those financial resources that are available for future programs and services, Changes in all three of these categories can help our readers understand how the City's financial picture is changing.

The following table summarizes the Statement of Net Position as of June 20, 2013 and 2012.

| | Governmental Activities | |
|----------------------------------|--------------------------------|--------------------|
| | <u>2013</u> | <u>2012</u> |
| Current and other assets | \$ 8,414,403 | \$ 7,708,925 |
| Capital assets | 13,670,839 | 13,044,006 |
| Total assets | 22,085,242 | 20,752,931 |
| Long-term debt outstanding | 2,640,935 | 2,709,912 |
| Other liabilities | 1,626,085 | 1,883,425 |
| Total liabilities | 4,267,019 | 4,593,337 |
| Net position: | | |
| Net investment in capital assets | 11,291,681 | 10,557,540 |
| Restricted | 769,542 | 633,150 |
| Unrestricted | 5,757,000 | 4,968,904 |
| Total Net Position | \$ 17,818,222 | \$ 16,159,594 |

Current and other assets significantly increased about \$705,500. Most of this increase was in the General Fund where cash increased because revenues exceeded expenses. This means that we continued to increase our cash reserves. Capital Equipment cash increased about \$28,000, also because revenues exceeded expenses. Non-major governmental fund cash increased overall about \$277,000. About half of this increase, \$136,000, is in the Municipal Aid Program Fund and about \$100,000 is in the Federal Forfeiture Fund. Accounts Receivable decreased about \$53,000.

Capital assets increased by about \$627,000. Acquisitions totaled \$1,929,319 and depreciation of \$1,252,302 was recorded (difference of \$677,017). During this fiscal year, the City purchased a new ambulance (\$205,000) and continued construction on the Depot Street project (\$853,000). Depreciation is a measure of how asset value declines as the asset is used. In addition, street and public work project improvements totaled nearly \$250,000.

At year-end, on-going engineering costs for the Fulton Road and Seventh Street projects are still in construction. These projects are still in the engineering and design stage.

CITY OF WINCHESTER, KENTUCKY
MANAGEMENT DISCUSSION AND ANALYSIS
JUNE 30, 2013

Long-term debt decreased because we paid more on debt service than the new debt incurred to purchase the new ambulance.

Other liabilities decreased only slightly. Accounts Payable increased about \$17,000. Accrued Payroll and Related Liabilities decreased about \$289,000. This is because the entire payroll for June 17-30, 2012 was paid July 6, 2012 (which was why FY 2012 payroll liabilities were so high). However, the first payroll in FY 2014 only included one day (June 30) accrual for FY 2013 payroll liabilities.

Payroll and Related Liabilities still includes about \$741,000 attributable to an issue with firefighter overtime and state incentive pay. In 2007, the KY Court of Appeals ruled that the City of Louisville had to pay overtime on the state supplement based on a 40-hour work week. This ruling was in contradiction to the directions that had been provided by the KY Department of Labor. Winchester, along with several other cities, filed a lawsuit challenging the authority of the KY Department of Labor to enforce the Louisville decision. In August, 2012, the KY Supreme Court rejected those arguments.

On December 21, 2012, the Kentucky Labor Cabinet notified the City, that during its ongoing investigation into the City Fire Department's compliance with the Kentucky wage and hour laws, the Fire Department failed to compensate employees time and one-half. On January 12, 2013, the City issued payment for back wages totaling \$62,526 to employees specified by the Kentucky Labor Cabinet.

The City's estimated liability for back-pay, retirement, and taxes is now estimated at about \$741,000. This liability is included on the government-wide financial statements, but not on the fund-wide statements. The City is still exploring legislative options and/or funding sources to pay for this liability. As such, it is uncertain at this time when this issue will be resolved.

Net Investment in Capital Assets increased about \$734,000 with the additional capital construction and acquisitions funded with cash rather than debt. Construction in progress decreased about \$50,000. Construction was completed on two major projects – the Depot Street restoration and a renovation of the City Hall bell tower. Fulton Road and Seventh Street are still in the engineering phases of construction in progress.

The City's unrestricted net position is finally recovering from the economic downturn and increased over \$788,000 by the end of FY 2013. This represents 53% of the City's annual net program expenses, a significant improvement in the City's financial position.

Statement of Activities

The Statement of Activities provides the operating results for all funds of the City, plus the component unit, Winchester Municipal Utilities, again using the accrual basis of accounting. This statement adds depreciation expense for each department but excludes the capital asset purchases. Another important feature of this report is the emphasis on *programs*. Line-items highlight the major components of the City's governmental operations and the columns present expenses, charges for services, grants, and general revenues. This format allows our readers to assess how the general resources are allocated to programs and the amounts that each program generates for their own services.

CITY OF WINCHESTER, KENTUCKY
MANAGEMENT DISCUSSION AND ANALYSIS
 JUNE 30, 2013

The following table summarizes the Statement of Activities for 2013 and 2012.

| | Governmental Activities | |
|--|--------------------------------|--------------------|
| | <u>2013</u> | <u>2012</u> |
| Revenues: | | |
| Program revenues: | | |
| Charges for services | \$ 1,369,373 | \$ 1,687,503 |
| Grant funding | 2,130,241 | 2,544,323 |
| Capital contributions | 8,375,299 | 4,422,014 |
| General revenues: | | |
| Property taxes | 2,274,389 | 2,078,336 |
| License fees and permits | 951,110 | 941,061 |
| Payroll taxes | 6,733,146 | 6,128,629 |
| Insurance premium tax | 2,026,521 | 1,929,212 |
| Transient room tax | 117,236 | 109,894 |
| Other taxes | 116,344 | 117,879 |
| Interest and investment earnings | 43,374 | 40,540 |
| Parking fines | 2,055 | 1,990 |
| Other local revenues | 231,817 | 214,552 |
| Total Revenues | 24,370,905 | 20,215,933 |
| Program Expenses: | | |
| General government | 3,066,235 | 3,419,226 |
| Public Protection | | |
| Dispatch | 753,168 | 701,604 |
| Police | 3,517,036 | 3,470,291 |
| Fire | 3,713,273 | 3,536,712 |
| EMS | 2,201,436 | 2,266,538 |
| Public Services | 1,290,571 | 1,404,842 |
| Intergovernmental services | 8,077,790 | 4,597,752 |
| Interest on long-term debt | 92,768 | 95,246 |
| Total Expenses | 22,712,277 | 19,492,211 |
| Excess (deficiency) before transfers and special items | 1,658,628 | 723,722 |
| Net increase (decrease) in net position | \$ 1,658,628 | \$ 723,722 |

Charges for Services decreased about \$318,000. This is EMS revenue for ambulance transports. EMS revenue has decreased significantly, mostly because the number of transports has decreased. The revenue will also fluctuate because of accounts receivable and provider payments.

Several major grant projects were completed in the prior year, so grant funding, except for the water and sewer projects, decreased \$414,000 from FY 2012 to FY 2013. Water and sewer funding for the Winchester Municipal Utilities are included in the capital contributions since the City receives these funds from the Kentucky Infrastructure Authority and transfers to WMU for plant and utility improvements. Those projects increased \$3.4 million over last year. The transfer to WMU is included in *Intergovernmental services* expenses and explains the significant increase in that cost category.

CITY OF WINCHESTER, KENTUCKY
MANAGEMENT DISCUSSION AND ANALYSIS
 JUNE 30, 2013

All Property taxes increased nearly \$200,000. Ad valorem taxes increased about \$84,000. Delinquent property taxes increased about \$37,000. Omitted Tangible taxes increased about \$45,000. Motor Vehicle taxes and Delinquent Property taxes each increased about \$11,000. Payroll taxes continued to grow, reflecting the rate increase from 1.5 to 2% effective October 1, 2012 and continued improvements in the economy.

General Government expenditures decreased about \$352,000. This was mainly because of the CDBG Walle grant (\$600,000) in FY 2012. However, the decrease was offset by payments for the Winchester Plaza TIF payment, the Amazon economic development bond payment, and the hospital revenue sharing payment to the Clark County Fiscal Court (total was \$180,000). Other departmental costs held steady as the City continued to watch operating costs carefully to ensure continued fiscal growth.

Intergovernmental Services increased due to an increase in grant activity. The Kentucky Infrastructure Loan for the Lower Howard's Creek project accounts for most of the grant activity.

Governmental Funds Balance Sheet

The following table summarizes the Governmental Funds Balance Sheet for 2013 and 2012.

| | <u>2013</u> | <u>2012</u> |
|---------------------------------------|---------------------|---------------------|
| Assets: | | |
| Cash and Cash Equivalents | \$ 6,440,066 | \$ 5,673,623 |
| Accounts Receivable | 1,990,694 | 2,092,558 |
| Prepaid Expenses | 6,574 | 16,587 |
| Other Assets | 0 | 0 |
| Total Assets | <u>\$ 8,437,334</u> | <u>\$ 7,782,768</u> |
| Liabilities: | | |
| Accounts Payable | \$ 119,982 | \$ 188,778 |
| Accrued Payroll & Related Liabilities | 199,550 | 488,443 |
| Total Liabilities | <u>319,532</u> | <u>677,221</u> |
| Fund Balances: | | |
| Restricted | 769,542 | 633,150 |
| Committed | 2,424,607 | 2,279,405 |
| Assigned | 406,280 | 49,703 |
| Unassigned | 4,517,375 | 4,143,289 |
| Total Fund Balances | <u>8,117,802</u> | <u>7,105,547</u> |
| Total Liabilities & Fund Balance | <u>\$ 8,437,334</u> | <u>\$ 7,782,768</u> |

As we noted earlier, cash and cash equivalents increased \$766,000, reflecting the City's continued improvement in cash reserves and financial position. Current liabilities decreased \$358,000, including the payment of the prior year retirement contribution and lower accounts payable for other operating expenditures.

Restricted funds increased \$136,000, representing obligations for grant projects that have not been completed. Committed funds increased primarily because of increases in federal and state forfeitures added to the Police Special Fund and Police Federal Forfeiture. Assigned funds include the self-insured health programs and these funds increased \$357,000, part of the overall cash increases. Unassigned funds increased \$374,000 with another operating surplus in FY 2013.

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Restricted fund balance includes those amounts that are subject to constraints imposed by third parties. Committed fund balance indicates reserves that the City Commission has set aside for specific purposes through the adoption of ordinance. Assigned fund balance describes amounts that management or the Commission have designated for specific purposes. Unassigned fund balance amounts are not constrained by any specific project restrictions.

For the City of Winchester, these balances include the following types of projects.

- Restricted – grant funds from federal, state, or local sources
- Committed – capital equipment fund and public safety special projects
- Assigned – self-insurance fund for health care benefits
- Unassigned – residual balance in General Fund

Governmental Funds Statement of Revenues, Expenditures and Changes in Fund Balance

The Governmental Funds Statement of Revenues, Expenditures and Changes in Fund Balances show revenues and expenses using the modified accrual basis of accounting. Results of operations are very similar to the statement of activities—revenues continue to lag the costs of operations.

The following table summarizes the *Statement of Revenues, Expenditures, and Changes in Fund Balance* for 2013 and 2012.

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| | Governmental Activities | |
|--|-----------------------------------|-----------------------------------|
| | <u>2013</u> | <u>2012</u> |
| REVENUES: | | |
| Taxes | \$ 11,267,637 | \$ 10,363,951 |
| Licenses & Permits | 951,110 | 941,061 |
| Charges for Services | 1,369,373 | 1,687,503 |
| Fines | 2,055 | 1,990 |
| Intergovernmental | 10,505,540 | 6,966,338 |
| Investment Income | 43,374 | 40,540 |
| Other | 231,817 | 214,552 |
| TOTAL REVENUES | <u>24,370,905</u> | <u>20,215,935</u> |
| EXPENDITURES: | | |
| General Government | 3,626,050 | 2,769,505 |
| Public Safety | 10,034,970 | 9,597,982 |
| Public Works | 1,469,948 | 1,293,204 |
| Intergovernmental | 8,077,790 | 4,597,752 |
| Capital | 0 | 1,010,696 |
| Debt service principal | 261,908 | 227,094 |
| Debt service interest | 92,768 | 95,246 |
| TOTAL EXPENDITURES | <u>23,563,433</u> | <u>19,591,479</u> |
| Excess (Deficit) of Revenues over Expenditures | <u>807,472</u> | <u>624,456</u> |
| OTHER FINANCING SOURCES (USES): | | |
| Proceeds from long-term borrowing | 204,784 | 0 |
| Infrastructure contributions | 0 | 0 |
| Operating transfers in | 0 | 8,354 |
| Operating transfers out | 0 | (8,354) |
| TOTAL OTHER FINANCING SOURCES (USES): | <u>204,784</u> | <u>0</u> |
| Excess (Deficit) of Revenues and Other Financing Sources over Expenditures and Other Financing Uses | 1,012,256 | 624,456 |
| Fund Balance, beginning | 7,105,546 | 6,481,090 |
| Fund Balance, ending | <u><u>\$ 8,117,802</u></u> | <u><u>\$ 7,105,546</u></u> |

The difference between revenues and expenses show how total fund balance has changed since last year. Total fund balance increased about \$1,000,000. Operating surpluses continued to improve with the economy and cost-saving measures for public programs and services.

Total taxes increased about \$900,000, mainly as a result of the payroll tax rate increase. License and Permits includes our electric and gas utility franchises, which increased only \$10,000 because the 2012-2013 winter was another mild season. Charges for Services (EMS revenue) decreased \$318,000.

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The large increase in intergovernmental revenue and expenses is mostly because of the Kentucky Infrastructure Agency loan for the Lower Howards Creek sewershed project that we noted earlier.

The large decrease in General Government Expenditures reflects the Community Development Block Grant project for the Walle Corporation completed in FY 2012. Other operating costs held steady, while capital costs increased with additional expenditures for the City Hall renovation and the TEA-21 Depot Street project. Debt service costs held steady since the City added a new capital lease for an ambulance as another lease was paid in full.

Capital and Operating Activities

The following table separates capital revenues and expenditures from operating to highlight the results for each major category and demonstrates that operating revenues are finally recovering sufficient to finance the City's increasing costs of services.

| FY 2013 Governmental Activities | | | |
|--|----------------|------------------|---------------|
| | Capital | Operating | Total |
| Revenues | \$ 1,172,529 | \$ 23,403,160 | 24,575,689 |
| Expended | (1,157,618) | (22,405,815) | (23,563,433) |
| Net | \$ 14,911 | \$ 997,345 | 1,012,256 |
| | | | |
| FY 2012 Governmental Activities | | | |
| | Capital | Operating | Total |
| Revenues | \$ 804,211 | \$ 19,411,724 | \$ 20,215,935 |
| Expended | (745,279) | (18,846,199) | (19,591,478) |
| Net | \$ 58,932 | \$ 565,525 | \$ 624,457 |

Capital revenues are primarily occupational license fees and proceeds from long-term borrowing. Capital expenses increased with the TEA-21 Depot Street and City Hall expenditures as we discussed earlier. Operating revenues and expenses increased, mainly due to the additional KIA funding for WMU and the continued healthy growth in payroll taxes. Excluding the transfer to WMU, operating costs held steady compared to FY 2012.

This year, the City finished the year with a much healthier surplus. This is mainly due to the increase in tax revenues. The City is working very hard to address revenue and expense issues. We are also pursuing many economic development projects for our community.

BUDGETARY HIGHLIGHTS

This section explains significant changes between the original and final adopted budget. The Schedule of Revenues, Expenditures, Changes in Fund Balance Budget-To-Actual financial reports begin on Page 35 with reports for the General Fund and two major special revenue funds.

Actual General Fund revenue fell short of budget estimates by about \$888,000. Tax revenues exceeded budget by \$375,000 as property values improved and the rate increase for the

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Occupational License fee was fully implemented. License and Permits came in just under budget. Most of the general fund under-budget difference (under budget by \$1.5 million) is attributed to Charges for Services, which includes Reimbursable Grant Income and EMS Revenue.

A major component of the budgeted Reimbursable Grant Income is the Depot Street project for \$909,000. This project is budgeted in General Fund because it is a reimbursable grant. This is also why Public Works expenses came in under budget. At year end, reimbursable grants revenue and expenses are transferred to federal, state, and local grant financial statements.

Operating expenses were under budget by about 17%, mostly because Public Works expenses came in under budget because of Depot Street. Also, some of this is attributable to personnel. The Planning, Communications, Police, Fire, and EMS did not have all of their positions filled for the entire year.

There was a budgeted transfer of \$400,000 from Capital Equipment to General Fund that was put in place should general fund revenue expectations not be met. Fortunately, we did not need to make this transfer.

The City approved two budget amendments to add revenues and appropriations for additional grants awarded during the fiscal year. The most significant amendment was budgeting the KIA funding in the Federal Grant fund for WMU to authorize the annual transfers from KIA to WMU. The following list includes the major amendments. Most are self-explanatory.

The first budget amendment added the following:

1. Added \$205,000 to CEF revenue for capital financing of an ambulance.
2. Added \$264,000 to CEF expenses (Admin) for repairs to city hall bell tower.
3. Added \$205,000 to CEF expenses (EMS) for the purchase of an ambulance.

The second budget amendment added the following:

1. Added \$46,000 to GF expenses (Admin) for economic development payments.
2. Added \$1,000 to GF expenses (Transfers) to W/CC Parks and Recreation.
3. Added \$25,500 to CEF revenue (Intergovernmental) to grant reimbursements.
4. Added \$64,000 to CEF expenses (Fire) for an AFG grant and a payment for a human simulator.
5. Added \$9,900,000 to CDBG/Other Grants for KIA loan for Lower Howard's Creek, a WMU project.

MAJOR CAPITAL PROJECTS FOR THE YEAR

Capital assets provide an important resource for supporting a variety of governmental programs and services. The City uses local tax revenues as well as federal and state grant funding to help finance critical infrastructure and public property improvements. During FY 2013, the City was working on the following capital projects to enhance public programs and services.

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Buildings

In FY 2013, the City made various improvements/repairs to City Hall, the Police Department building, three Fire stations, and the Public Works buildings at a total cost of about \$50,035. Of this total, \$11,752 was partial payment on the roof replacement at City Hall.

The City finished the restoration of the bell tower on City Hall in November, 2012. This building is 100 years old. The tower was in very bad shape, with water leaks, bird damage, and loose bricks. In FY 2012, we spent \$65,465 and in FY2013, we spent \$266,973 for engineering and construction.

Curbs, Gutters, Sidewalks, Other

We repaired curbing at various sites on state roads (Boone Avenue – KY 627) within the City at a cost of \$26,548. The state reimbursed us \$10,000 through a curb replacement agreement.

Storm Sewer Projects

In 1992, the City of Winchester recognized that its storm sewer infrastructure system was beginning to show signs of deterioration. As of June 30, 2013, \$1,253,500 has been spent to replace and/or restore existing storm sewers.

The City spent \$3,929 to repair a storm drain on East Washington Street. The City has set aside \$50,000 in the Capital Equipment Fund to identify and pay for various stormwater projects that might arise from failures in the system.

Roads and Bridges

The City street system consists of approximately 80 miles of two-lane paved roads and alleys. The City also contains some state roads and it is the state's responsibility to maintain those roads. The City uses Municipal Aid Program Funds (from the state) to maintain City streets. The City spent \$216,200 maintaining City streets.

The City accepted several streets into the City street system. On December 14, 2012, the City accepted approximately 2,177 feet of Rose Mary Drive, Sir Edward Court, Old Garden Court, English Miss Court, and Royal Blush Court at an asset value of \$421,279 by Order #2012-150. Also on December 14, 2012, the City accepted approximately 1,997 feet of portions of Concord Avenue, Abbeywood Drive, Sheffield Way, and Dorset Lane at an asset value of \$175,009 by Order #2012-151. It is City policy to accept streets into the system on the condition that the developer is responsible for repairs to the streets for one year following acceptance.

Transportation Enhancement Act of the 21st Century (TEA-21)

In FY 2010, the City applied to the Kentucky Department of Transportation for a Transportation Equity Act (TEA-21) grant to help reconstruct Depot Street with new brick paving, street lighting, electric pedestals, replacement of sanitary sewer, and new fencing. This project is the second phase of the Farmers Market project. In FY 2011, the grant was approved. The total estimated cost is \$1,151,600. The grant portion is \$909,000 (federal funds). The City's matching portion is \$242,600.

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An architect was selected to proceed with the engineering and design phase of the project. At June 30, design, development, and construction were complete. In FY 2011, the engineering costs were \$58,120. In FY 2012, the engineering costs were \$14,955. Construction began January, 2013. In FY 2013, the engineering and construction costs were \$974,415. The total cost of the project was \$1,048,957.

KY Department of Transportation JL-04 Bond Fund

In FY 2011, the City applied to the Kentucky Department of Transportation for JL-04 bond funds for three projects: (1) Fulton Road Extension Project; (2) Seventh Street Relocation Project; and (3) Downtown Mast Arms. The state has approved \$585,000 for the Fulton Road project – design, right-of-way acquisition, and utility relocation. The state has approved \$240,000 for the Seventh Street project – design. Contracts for the first phase of these two projects (engineering) were awarded June, 2011. As of June 30, 2013, the engineering costs on these two projects were \$115,400 and \$197,829 respectively.

When these first phases are completed, the state will consider additional funding for the second phases of these projects (Fulton Road Phase II - \$415,000 and Seventh Street Phase II - \$260,000). We have requested \$160,000 for the Downtown Mast Arm Project, but have not yet received approval.

Franchise

There were no new franchise agreements during FY 2013.

Land

On November 13, 2012, the City accepted a vacant lot at 20 Lincoln Street via a quitclaim deed (for \$10) by Order No. 2012-137.

Annexation

There was no annexation during FY 2013.

Land Improvements

There were no major land improvements in FY 2013.

STATUS OF GRANTS

The City of Winchester vigorously pursues grant opportunities to aid in the development and improvement of its services, equipment, and infrastructure. During FY 2013, the City applied for several grants. Listed below is the status of grant applications.

1. KIA Infrastructure Grant, Belair/Westside Pump Stations, \$1,000,000, approved
2. CDBG Disaster Recovery Program Grant, \$621,000, culvert reconstruction, approved
3. Kentucky Nonpoint Source Pollution Control Grant (Lower Howard's Creek Watershed Improvement), \$182,225, subsequently approved

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4. Kentucky Energy Efficiency and Conservation Grant, \$141,792, denied
5. Kentucky Land and Water Conservation Fund Grant, \$75,000, renovation of soccer complex building, pending
6. Kentucky Office of Homeland Security, \$8,855, mobile data project, denied
7. U.S. Department of Homeland Security FEMA Assistance to Firefighters Grant, \$925,000, aerial apparatus, denied
8. U.S. Department of Homeland Security FEMA Staffing for Adequate Fire and Emergency Response, \$393,738, denied

All grants received prior to FY 2013 have been closed out.

The following grants were completed and closed out during FY 2013.

1. KIA Infrastructure Grant, Lower Howard's Creek Watershed Improvements, \$36,000,000
2. Kentucky Transportation Cabinet TEA-21 Grant, \$909,000, match 20%, Depot Street Restoration Project (improvements, landscaping, and lighting)
3. United States Department of Housing and Urban Development. Community Development Block Grant (CDBG) No. 09-066, \$750,000, Winchester Wastewater Improvements Project Forest Park Sanitary Sewer system
4. CDBG Grant, Walle Corporation Equipment Lease, \$600,000
5. Kentucky Nonpoint Source Pollution Control Grant, \$208,534
6. Kentucky Renaissance on Main Façade Grant, \$20,000
7. Kentucky Office of Homeland Security, \$1,500, Security Camera Police Department
8. Kentucky Office of Homeland Security, \$40,500, Mobile and Portable Radios, Joint Grant for Winchester Fire/EMS, Clark County Sheriff, and Clark County Fire Department
9. Kentucky Office of Homeland Security, \$23,000, Joint Grant for Mobile P25 Digital Radios
10. U.S. Department of Homeland Security FEMA grant, \$42,004, computer simulator and software

STORMWATER CONCERNS

The United States Environmental Protection Agency (EPA) requires Kentucky to issue permits for MS4 (Municipal Small Separate Stormwater System) projects to protect water quality. Winchester is a Phase II community. The Kentucky Division of Water (KDOW) issued our first NPDES (National Pollution Detection Elimination System) permit September 2003. Our second NPDES permit was issued April 2010.

The KDOW issued a Notice of Violation to Winchester in December 2010 for deficiencies identified in the Violation Referral Form as a result of an August 2010 inspection. The notice was subsequently lifted once the Kentucky Department for Environmental Protection determined that we had taken sufficient action to address the violations. One of these requirements is on-going public education for citizens and contractors. We are working with some of the major industries on stormwater agreements and also on a stormwater regulation manual that will help contractors meet the City's requirements.

To address these deficiencies, the City engaged the services of CDP Engineer's Inc (Order No. 2011-8) to achieve satisfactory compliance for Plan Year 1 (Phase II permit). The City approved

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an order on September 20, 2011 with CDP for Plan Years 2-5 for support and consulting services for compliance and achieving tasks and goals for this second permit term (program development, regulatory assistance, outfall mapping, data management, and assistance with meeting identified tasks). The City also engaged the services of CDP (Order No. 2013-81) for development of a stormwater quality management plan (Plan Years 2-5). The following ordinances were also adopted as part of this plan:

1. Ordinance #5-2011 Stating the Erosion and Sediment Control Requirements, March 15, 2011
2. Ordinance #9-2011 Establishing Illicit Discharge and Connector Requirements, May 2, 2011
3. Ordinance #14-2011 Stating the Post Construction Stormwater Runoff Requirement, June 28, 2011
4. Ordinance # 10-2013 Relating to Erosion Prevention and Sediment Control Requirements, first reading was on May 20, second reading was on 08-06-2013.

ECONOMIC DEVELOPMENT

The City has been fortunate in the development of the Industrial Park on the north side of town. The Winchester/Clark County Industrial Development Authority (WCC-IDA) oversees development of the Park. WCC-IDA is funded by the City and the County. The Industrial Park development began in 1980. Phase VI provided an additional 300 acres to be used for development. Approximately \$2.4 million of infrastructure improvements (water and sewer lines) have been installed in the Phase VI development.

The Kentucky Transportation Cabinet provided up to \$2.8 million in reimbursable funding to the Clark County Fiscal Court to construct a bridge over the CSX railroad tracks on Van Meter Road for access from Exit 94 on Interstate 64 into the Industrial Park. Construction for the road and bridge began April, 2008 and was completed during FY 2009. This has provided better access to the Bluegrass Community & Technical College (BCTCS) and another route for industrial traffic.

With almost 1/3 (31%) of the jobs in Clark County being in the manufacturing industry and 36% of the total wages paid in Clark County coming from manufacturing, the City of Winchester recognizes and appreciates the fact that stability and growth of industry is key to the overall economic well-being of Winchester and Clark County.

Economic development continues to increase. We began the fiscal year with an 8.2% unemployment rate (down from 9.3% at the same time last year) and ended the fiscal year with an 8.5% unemployment rate. WCC-IDA has filled all vacant buildings with new industry in the industrial park and will continue efforts throughout the community to put people back to work.

Business Incentive Projects

To encourage the investment and job growth in Winchester, the Kentucky Economic Development Finance Authority (KEFDA) has several economic tax incentive packages that companies can apply for to grow their businesses.

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The Kentucky Business Investment (KBI) program is a performance-based incentive that allows a company to keep a portion of its investment over the term of the agreement through corporate income tax credits and wage assessment by meeting job and investment targets. The Kentucky Industrial Development Act (KIDA) is the former KBI program. The maximum tax incentive authorized is for both local and state incentives combined. The term of the agreement begins on the date of final approval and when the City has an agreement with the business. These agreements work by pledging to the business a portion of the occupational license fees withheld from employees' wages. So far, we have only two local participation agreements – Alltech and Walle. Neither of these companies has activated their projects yet.

The Kentucky Enterprise Initiative Act (KEIA) allows approved companies to recoup Kentucky sales and use tax on construction costs, building fixtures, equipment used in research and development, and electronic processing equipment.

The Kentucky Economic Development Bond (EDB) program is used for extraordinary project financing not covered with other funds. This program can be funded by the state or the local district. The KEFDA approved (03-29-2012) an EDB of \$250,000, through the City of Winchester, for Amazon. This EDB grant was funded by the WCC-IDA. We have an agreement with the WCC-IDA to repay this \$250,000 to the Authority over a five-year period. In the past, Sekisui received final approval (12-07-2006) for EDB tax incentives of \$200,000. The KEFDA made this grant to the City, which we then passed on to Sekisui on 04-23-2008.

Community Development Block Grants (CDBG) are federally funded low-interest loans made available through the Department of Local Government. We have received several CDBG grants in the past for local industries. The most recent grant was \$600,000 for a Walle Corporation equipment lease that was done in FY 2013.

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Many projects listed below have received preliminary or final approval from the KEFDA for one or more of these programs. These programs have helped our economy tremendously.

| RECIPIENT | PROGRAM | TOTAL PROJECT COST | MAX TAX INCENTIVE AUTHORIZED | STARTING JOBS | ESTIMATED NEW JOBS | AGREEMENT DATE | OCC LICENSE TAX PLEDGED |
|--|---------|--------------------|------------------------------|---------------|--------------------|--|-------------------------|
| Advanced Green Components LLC | KBI | \$11,960,000 | \$750,000 | 80 | 40 | | |
| Alltech Inc | KBI | \$14,000,000 | \$3,000,000 | NA | 40 | Reso #R2012-6 6/19/2012 Term 10 yrs | 1% |
| AMZN wacs Inc | KBI | \$20,411,340 | \$10,250,000 | NA | 550 | | |
| Catalent Pharma Solutions LLC | KBI | \$46,800,000 | \$2,000,000 | 307 | 90 | | |
| Caudill Seed & Warehouse Co Inc | KBI | \$775,000 | \$300,000 | NA | 18 | | |
| Harry Gordon Steel Company | KBI | \$5,572,000 | \$300,000 | 20 | 24 | | |
| J&T Munitions Inc dba J&T Distributing | KBI | \$3,615,800 | \$200,000 | NA | 15 | | |
| J&T Munitions Inc dba J&T Distributing | KIDA | \$998,000 | \$240,000 | 24 | 15 | | |
| Sekisui S-LEC America, LLC | KIDA | \$43,240,000 | \$1,600,000 | NA | 80 | | |
| Senko (USA) Inc | KBI | \$7,575,000 | \$250,000 | NA | 16 | | |
| Taica Corporation | KBI | \$8,049,232 | \$500,000 | NA | 30 | | |
| The Freeman Corp | KBI | \$3,440,000 | \$500,000 | 202 | 32 | | |
| Vangent Inc dba General Dynamics | KBI | \$12,000,000 | \$2,500,000 | NA | 150 | | |
| Walle Corporation | KBI | \$4,135,000 | \$500,000 | 114 | 23 | Order #2012-117 10/12/2012 Term - 10 yrs | 1% |

KBI - Kentucky Business Investment Program
KIDA - KBI

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| RECIPIENT | PROGRAM | TOTAL | AUTHORIZED | STARTING | ESTIMATED | AGREEMENT |
|---|---------|--------------|------------|----------|-----------|--|
| | | PROJECT | LOAN | | | |
| | | COST | GRANT | JOBS | NEW JOBS | DATE |
| AMZN wacs Inc thru City of Winchester | EDB | \$3,300,000 | \$250,000 | NA | 550 | Order #2012- 155 12/4/2012 Term 5 yrs |
| Catalent Pharma Solutions LLC | KEIA | \$46,800,000 | \$860,000 | 313 | 90 | |
| J & T Munitions Inc dba J&T Distributing | KEIA | \$3,615,800 | \$50,000 | NA | 15 | |
| ----- | | | | | | |
| EDB - Economic Development Bonds KEIA - Kentucky Enterprise Initiative Act | | | | | | |

Industrial Park

Last year, we successfully recruited Amazon WACS, Inc., a subsidiary of Amazon, to locate in Winchester. Amazon received preliminary approval (03-29-2012) from the Kentucky Economic Development Finance Board (KEFDA) for building a customer support project that will invest over \$20 million. The approval is for up to \$10,250,000 in KBI state tax incentives. Amazon temporarily located in the Winchester Plaza and finished building an 80,000 square-foot building for their call center in June, 2013. Amazon has already hired over 200 people. Their goal is 550 full-time and 600 part-time/seasonal employees.

Several companies at the Industrial Park have invested in expansion projects or built new facilities, including:

1. Advanced Green Components (AGC)
2. Alltech
3. Catalent Pharma Solutions.
4. Harry Gordon Steel Company.
5. J & T Munitions, Inc., dba J & T Distributing
6. Royal DSM (formerly Martek Biosciences)
7. Rocky Mountain ATV
8. Sekisui S-LEC America, LLC
9. Senko (USA Inc.)
10. TAICA North American Corporation
11. Univance
12. Walle Corporation

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Other Development

Also, WCC-IDA is still focused on commercial, retail, and restaurant development. Our community continues to see results from our involvement with the Winchester Plaza redevelopment. About three years ago, the City and County created a TIF district in the area around Winchester Plaza. (See *Tax Increment Financing*) The new businesses that opened last year have continued to thrive. The TIF district has been a success.

Three years ago, a private company purchased the non-profit Clark Regional Medical Center and began construction of a new hospital. The new hospital is near Winchester Plaza. The City funded a much-needed traffic signal on U.S. 60 at this site. The City annexed this area and approved a joint revenue-sharing agreement with the Clark County Fiscal Court. Since then, the hospital has built a 4,600 square-foot medical office building. This new development continues to draw other business and we anticipate more new business opportunities in that area. The City is very optimistic about new development surrounding the hospital.

Vangent, Inc., dba General Dynamics, is a new customer support center for Medicare. Vangent purchased and renovated the vacant HP building. Vangent received preliminary approval for KBI state tax incentives. (See *Business Incentive Projects*)

The City finished the Depot Street Project. Depot Street was the last remaining brick paved street in the city. We applied for and received a Transportation Enhancement Grant for street improvements, lighting, and landscaping for Depot Street. The project was finished in June, 2013. The project greatly enhanced the area. The Farmer's Market Coalition has since relocated back to Depot Street.

The Daniel Boone Pioneer Festival has been in existence for 35 years. The festival is held on Labor Day weekend and it is a huge success every year. We are proud that the Southeast Tourism Association has named it as one of top 10 festivals in Southern United States.

The City continues efforts to strengthen the downtown area. The Winchester First Board, along with the Downtown Business Association, is striving to improve the downtown area. The City had its fifth Beer Cheese Festival on June 8, 2013. The festival has also been a huge success. Last year, Winchester First began a mural project for the downtown area. Last year, local artists painted an historical mural on the side of a hardware business. This year, those same artists painted another historical mural on the side of grocery store facing Depot Street. Both murals have improved our downtown beauty. Winchester First is also working on a loan program to aid downtown investment.

Tax Increment Financing

In 2000, the Kentucky General Assembly approved laws allowing tax increment financing (TIF). In 2007, there was a major overhaul to the existing laws. In essence, TIF incentives encourage involvement of private investment in development areas. Designating an area as a TIF district allows the owner/developer to finance improvements from future increases in the tax revenues.

In 2010, by Ordinance No. 1-2010, the City and County created a TIF district in the area around Winchester Plaza. The local participation agreement is for 20 years. The City pledged 100% of

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the incremental real ad valorem taxes and 50% of the incremental occupational license fees to the developer.

The Winchester Plaza renovations were completed about four years ago. Business activity in the area continues to thrive. Winchester Plaza is now a much-improved anchor for our community. The following table summarizes the City's pledge to date.

| WINCHESTER PLAZA TIF DISTRICT | |
|-------------------------------|--------------------|
| 2012 | \$39,667.40 |
| 2010-2011 | \$14,884.45 |
| Total Payments to Date | \$54,551.85 |

REVENUE SHARING

On January 17, 2012, by Order No. 2012-9, the City and the Clark County Fiscal Court executed an interlocal agreement for revenue sharing (payroll taxes) from the old hospital area site (A -Floyd Clay Drive and McCann Drive) and the new hospital area site (B - Hospital Drive). This agreement is effective for fifteen years. The following table summarizes the revenue we have committed to the Fiscal Court to date.

| Revenue Sharing | | |
|---------------------------|---------------------|-------------|
| | | <u>Paid</u> |
| 2012 - 1st qtr | \$6,641.27 | 6/14/2012 |
| 2012 - 2nd qtr | \$41,981.98 | 8/20/2012 |
| 2012 - 3rd qtr | \$39,243.32 | 11/5/2012 |
| 2012 - 4th qtr | \$40,152.55 | 2/11/2013 |
| 2013 - 1st qtr | \$34,639.60 | 5/9/2013 |
| Total Paid to Date | \$162,658.72 | |

ECONOMIC CONDITION AND OUTLOOK

The City of Winchester is located 15 miles east of Lexington. The City has experienced residential growth on the west side of Clark County, due to its proximity to the Bypass and the City of Lexington. The City anticipates that development of the eastern bypass will bring about balanced residential and business growth on the east side of Clark County.

The local economy has improved and continues to grow. We began the fiscal year with an 8.2% unemployment rate (down from 9.3% at the same time last year) and ended the fiscal year with an 8.5% unemployment rate. We have had huge success with existing industry, new industry,

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MANAGEMENT DISCUSSION AND ANALYSIS
JUNE 30, 2013

and new businesses. We have numerous inquiries from potential businesses. New companies, new investment, and new jobs have all contributed to economic stability.

The City, like most Kentucky communities, is highly dependent on occupations license fees, insurance premiums taxes, and property taxes for funding governmental services. Because the unemployment rate is decreasing, more people are working, which helps to improve the City's tax base.

The City did not approve the maximum allowable property tax rate for calendar year 2012 (FY 2013). The rates chosen for real and tangible property were the compensating rates, which only allows for the same amount of tax revenue received in FY 2012. The FY 2013 budget was based on the maximum allowable rate, so this revenue fell short of budget expectations.

The Commission approved a payroll tax increase that took effect October 1, 2011. This rate change is now yielding higher revenues. Cuts in the operating costs have brought the City's budget back to surplus funding, which will allow for enhancing services that were curtailed during the recession.

Our taxes and fees are dependent upon the economy, but we cannot decrease our very important services that our citizens depend upon. It is our mission to provide the same level of service to our citizens as we have in the past.

Personnel costs consume about 75% of the General Fund budget. These costs will continue to rise for two main reasons: (1) the state retirement system continues to increase mandated pension rates upon Kentucky cities that are not sustainable in the long-run for our community; and (2) health insurance costs continue to rise.

During our FY 2013 budget preparations, we based our revenue projections on some major private investments in our community. Every department had to cut expenses somewhere. However, based on better revenue projections for FY 2013, a 3% COLA was granted to employees. This was very important to each department head. We are a service organization and retaining qualified employees is essential for public safety and administration.

We had not anticipated structural repairs needed for the City Hall bell tower. We included this in the first budget amendment for FY 2013. The additional repairs cost \$264,000. These costs were expensed out of Capital Equipment Fund. Although the City approved indefinitely that 1/8 of the payroll tax goes to the Capital Equipment Fund, this expense had a major impact on this fund.

Management is concerned about the following issues, which need to be addressed before governmental services are affected:

1. Revenues are not keeping up with expenses.
2. Expenses will continue to use up cash reserves to fund future costs. All other funds are restricted, so they cannot be used to fund anticipated general fund deposits. If necessary, a transfer of cash from the Capital Equipment Fund to General Fund will be made.
3. The impact of unfunded federal mandates.
4. The impact of global economics.

CITY OF WINCHESTER, KENTUCKY
MANAGEMENT DISCUSSION AND ANALYSIS
JUNE 30, 2013

There have been no changes in funding policies since the Commission approved a motion on May 19, 2004 to maintain a general fund balance at \$2 million. For the months of September and October 2012, general fund cash fell below the \$2 million threshold. However, the rest of the fiscal year remained above that target, mainly as a result of the increase in the occupational license fee.

Recovery from the recent recession has been a slow process. Typically, in a recession, a City's tax stream will lag behind any improvement in the economy. We are confident that the economy will continue to improve. However, the future of yearly COLA's, retirement costs, and health insurance will still be problematic. These are some of the major issues that the City is confronted with and will be challenged with in the future.

We are committed to delivering quality services to our residents and visitors. Our mission is to provide our citizens with essential and important governmental services. We note that the Mayor and Commissioners' number one priority is bringing jobs back to our community and removing any barriers that are a hindrance to new or existing businesses. They have, and still are, working diligently toward that end.

CONTACTING THE CITY'S FINANCIAL TEAM

This financial report is designed to provide our citizens, taxpayers, customers, investors, and creditors with a general overview of the City's financial position. We are dedicated to demonstrating our accountability for the money we manage on their behalf. The economic development information was provided by Todd Denham, Winchester/Clark County Industrial Authority. If you have questions about this report or need additional financial information, please give us a call or visit us at City Hall.

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City Treasurer
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Winchester, KY 40392-4135
859-744-1660
[dbailey@winchesterky.com](mailto:d Bailey@winchesterky.com)

Matthew Belcher
City Manager
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Winchester, KY 40392-0040
859-744-2821
mbelcher@winchesterky.com

CITY OF WINCHESTER, KENTUCKY
STATEMENT OF NET POSITION
JUNE 30, 2013

| | PRIMARY GOVERNMENT | | COMPONENT UNIT |
|---|----------------------------|----------------------|-----------------------|
| | GOVERNMENTAL ACTIVITIES | TOTAL | |
| ASSETS: | | | |
| Current Assets | | | |
| Cash and Cash Equivalents | \$ 6,440,066 | \$ 6,440,066 | \$ 7,658,841 |
| Restricted Cash and Cash Equivalents | 0 | 0 | 351,373 |
| Restricted Investments | 0 | 0 | 4,729,869 |
| Accounts Receivable | | | |
| Taxes | 1,307,966 | 1,307,966 | 0 |
| Accounts, net | 351,597 | 351,597 | 1,718,516 |
| Intergovernmental | 306,551 | 306,551 | 0 |
| SDC Receivables | 0 | 0 | 940,509 |
| Other Accounts Receivables | 0 | 0 | 10,729 |
| Due from Other Governments | 0 | 0 | 0 |
| Due from Other Funds | 1,649 | 1,649 | 0 |
| Prepaid Expenses | 6,574 | 6,574 | 720,328 |
| Accrued Interest | 0 | 0 | 6,738 |
| Inventories | 0 | 0 | 351,665 |
| Total Current Assets | 8,414,403 | 8,414,403 | 16,488,568 |
| Restricted Assets | | | |
| Cash and Cash Equivalents | 0 | 0 | 8,136,845 |
| Total Restricted Assets | 0 | 0 | 8,136,845 |
| Noncurrent Assets | | | |
| Other Receivables | 0 | 0 | 0 |
| Bond Issuance Costs (unamortized) | 0 | 0 | 159,725 |
| Construction in Progress | 344,880 | 344,880 | 43,084,130 |
| Land | 1,986,538 | 1,986,538 | 1,051,011 |
| Net Capital Assets | 11,339,420 | 11,339,420 | 66,152,427 |
| Total Noncurrent Assets | 13,670,839 | 13,670,839 | 110,447,293 |
| TOTAL ASSETS | \$ 22,085,242 | \$ 22,085,242 | \$ 135,072,706 |
| LIABILITIES: | | | |
| Current Liabilities | | | |
| Accounts Payable | \$ 97,051 | \$ 97,051 | \$ 370,010 |
| Other Accrued Liabilities | 0 | 0 | 287,977 |
| Accrued Payroll & Related Liabilities | 941,024 | 941,024 | 0 |
| Incurred but Not Reported Health Claims | 109,611 | 109,611 | 0 |
| Current portion of Lease Obligations | 309,639 | 309,639 | 6,974 |
| Total Current Liabilities | 1,457,325 | 1,457,325 | 664,961 |
| Current Liabilities from Restricted Assets | | | |
| Accounts Payable - Construction | 0 | 0 | 25,275 |
| Accounts Payable - Retainage | 0 | 0 | 0 |
| Customer Deposits | 0 | 0 | 155,489 |
| Accrued Interest Payable | 0 | 0 | 106,671 |
| Current Portion of Bonds | 0 | 0 | 3,175,612 |
| Total Current Liabilities from Restricted Assets | 0 | 0 | 3,463,047 |
| Noncurrent Liabilities | | | |
| Net Pension Obligation | 478,399 | 478,399 | 0 |
| Noncurrent Portion of Lease Obligations | 1,724,638 | 1,724,638 | 0 |
| Noncurrent Portion of Bonds | 0 | 0 | 65,377,038 |
| Compensated Absences | 606,658 | 606,658 | 395,076 |
| Total Noncurrent Liabilities | 2,809,695 | 2,809,695 | 65,772,114 |
| TOTAL LIABILITIES | 4,267,019 | 4,267,019 | 69,900,122 |
| NET POSITION | | | |
| Net Investment in Capital Assets | 11,291,681 | 11,291,681 | 41,621,273 |
| Restricted | 769,542 | 769,542 | 0 |
| Restricted for Capital Projects | 0 | 0 | 12,158,802 |
| Restricted for Bond Debt Service | 0 | 0 | 890,442 |
| Unrestricted | 5,757,000 | 5,757,000 | 10,502,067 |
| TOTAL NET POSITION | 17,818,222 | 17,818,222 | 65,172,584 |
| TOTAL LIABILITIES AND NET POSITION | \$ 22,085,242 | \$ 22,085,242 | \$ 135,072,706 |

See Accompanying Notes to the Financial Statements

**CITY OF WINCHESTER, KENTUCKY
STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED JUNE 30, 2013**

| FUNCTIONS/PROGRAMS | PROGRAM REVENUES | | | | NET (EXPENSE) REVENUE AND CHANGES IN NET POSITION | | COMPONENT UNIT |
|--------------------------------|------------------------|-------------------------|--|--|--|------------------------|-------------------|
| | EXPENSES | CHARGES FOR SERVICES | OPERATING GRANTS AND CONTRIBUTIONS | CAPITAL GRANTS AND CONTRIBUTIONS | PRIMARY GOVERNMENT | | |
| | | | | | GOVERNMENTAL ACTIVITIES | TOTAL | |
| Primary Government | | | | | | | |
| Governmental Activities: | | | | | | | |
| General Government | \$ (3,066,235) | \$ 81,403 | \$ 42,656 | \$ 907,892 | \$ (2,034,284) | \$ (2,034,284) | |
| Public Safety: | | | | | | | |
| Dispatch | (753,168) | 0 | 567,254 | 432 | (185,481) | (185,481) | |
| Police | (3,517,036) | 0 | 359,602 | 24,500 | (3,132,934) | (3,132,934) | |
| Fire | (3,713,273) | 0 | 239,802 | 42,707 | (3,430,765) | (3,430,765) | |
| EMS | (2,201,436) | 1,287,970 | 340,996 | 48,345 | (524,125) | (524,125) | |
| Public Works | (1,290,571) | 0 | 507,750 | 170,696 | (612,126) | (612,126) | |
| Intergovernmental Services | (8,077,790) | 0 | 72,182 | 7,180,726 | (824,882) | (824,882) | |
| Interest on Long-Term Debt | (92,768) | 0 | 0 | 0 | (92,768) | (92,768) | |
| Total Governmental Activities | <u>(22,712,277)</u> | <u>1,369,373</u> | <u>2,130,241</u> | <u>8,375,299</u> | <u>(10,837,365)</u> | <u>(10,837,365)</u> | |
| Total Primary Government | <u>\$ (22,712,277)</u> | <u>\$ 1,369,373</u> | <u>\$ 2,130,241</u> | <u>\$ 8,375,299</u> | <u>\$ (10,837,365)</u> | <u>\$ (10,837,365)</u> | |
| Component Unit | | | | | | | |
| Winchester Municipal Utilities | \$ (12,415,900) | \$ 15,403,126 | \$ 83,506 | \$ 827,720 | | | \$ 3,898,452 |
| | | | General Revenues: | | | | |
| | | | Taxes: | | | | |
| | | | Property | \$ 2,274,389 | \$ 2,274,389 | \$ 0 | 0 |
| | | | Licenses & Permits | 951,110 | 951,110 | 0 | 0 |
| | | | Payroll | 6,733,146 | 6,733,146 | 0 | 0 |
| | | | Insurance Premium | 2,026,521 | 2,026,521 | 0 | 0 |
| | | | Hotel/Motel Room Tax | 117,236 | 117,236 | 0 | 0 |
| | | | Telecommunications Excise Tax | 116,344 | 116,344 | 0 | 0 |
| | | | Investment Income | 43,374 | 43,374 | 0 | 100,034 |
| | | | Parking Fines | 2,055 | 2,055 | 0 | 0 |
| | | | Gain (Loss) on Disposal of Fixed Assets | 0 | 0 | 0 | 53,789 |
| | | | Other Local Revenues | 231,817 | 231,817 | 0 | 222,464 |
| | | | Total General Revenues | <u>\$ 12,495,993</u> | <u>\$ 12,495,993</u> | <u>\$ 376,287</u> | |
| | | | Capital Contributions | 0 | 0 | 0 | 0 |
| | | | Change in Net Position | 1,658,628 | 1,658,628 | 4,274,739 | |
| | | | Net Position June 30, 2012 | <u>16,159,594</u> | <u>16,159,594</u> | <u>60,897,845</u> | |
| | | | Net Position June 30, 2013 | <u>\$ 17,818,222</u> | <u>\$ 17,818,222</u> | <u>\$ 65,172,584</u> | |

See Accompanying Notes to the Financial Statements
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**CITY OF WINCHESTER, KENTUCKY
BALANCE SHEET
GOVERNMENTAL FUNDS
JUNE 30, 2013**

| | GENERAL FUND | CAPITAL EQUIPMENT FUND | FEDERAL GRANT FUND | NONMAJOR GOVERNMENTAL FUNDS | TOTAL GOVERNMENTAL FUNDS |
|--|-------------------------|---------------------------------------|-----------------------------------|--|---|
| ASSETS: | | | | | |
| Cash and Cash Equivalents | \$ 3,268,582 | \$ 1,995,860 | \$ 0 | \$ 1,175,624 | \$ 6,440,066 |
| Accounts Receivable | | | | | |
| Taxes (Net of Allowance for Doubtful | | | | | |
| Accounts (\$91,995) | 1,307,966 | 0 | 0 | 0 | 1,307,966 |
| Accounts, Net of Allowance for Doubtful | | | | | |
| Accounts (\$209,124) | 351,597 | 0 | 0 | 0 | 351,597 |
| Intergovernmental | 255,799 | 27,820 | 22,931 | 0 | 306,551 |
| Due from Other Funds | 24,580 | 0 | 0 | 0 | 24,580 |
| Prepaid Expenses | 6,574 | 0 | 0 | 0 | 6,574 |
| Accrued Interest | 0 | 0 | 0 | 0 | 0 |
| TOTAL ASSETS | \$ 5,215,098 | \$ 2,023,680 | \$ 22,931 | \$ 1,175,624 | \$ 8,437,334 |
| LIABILITIES: | | | | | |
| Accounts Payable | \$ 91,895 | \$ 0 | \$ 0 | \$ 5,156 | \$ 97,051 |
| Due to Other Funds | 0 | 0 | 22,931 | 0 | 22,931 |
| Pension Contribution Payable | 0 | 0 | 0 | 0 | 0 |
| Accrued Payroll & Related Liabilities | 199,550 | 0 | 0 | 0 | 199,550 |
| TOTAL LIABILITIES | 291,444 | 0 | 22,931 | 5,156 | 319,532 |
| FUND BALANCES: | | | | | |
| Restricted Fund Balance | 0 | 0 | 0 | 769,542 | 769,542 |
| Committed Fund Balance | 0 | 2,023,680 | 0 | 400,926 | 2,424,607 |
| Assigned Fund Balance | 406,280 | 0 | 0 | 0 | 406,280 |
| Unassigned Fund Balance | 4,517,375 | 0 | 0 | 0 | 4,517,375 |
| TOTAL FUND BALANCES | 4,923,654 | 2,023,680 | 0 | 1,170,468 | 8,117,802 |
| TOTAL LIABILITIES AND FUND BALANCES | \$ 5,215,098 | \$ 2,023,680 | \$ 22,931 | \$ 1,175,624 | \$ 8,437,334 |

See Accompanying Notes to the Financial Statements

**CITY OF WINCHESTER, KENTUCKY
RECONCILIATION OF THE BALANCE SHEET - GOVERNMENTAL FUNDS
TO THE STATEMENT OF NET POSTION
JUNE 30, 2013**

| | | |
|---|----|--------------------------|
| Total Governmental Fund Balances | \$ | 8,117,802 |
| Amounts reported for governmental activities in the statement of net position are different because: | | |
| Capital assets are not reported in the fund financial statement because they are not current current financial resources, but they are reported in the statement of net position | | 13,670,839 |
| Certain liabilities are not reported in the fund statements because they are not due and payable, but these liabilities are included in the statement of net position | | |
| Long-Term Debt | | (2,034,277) |
| Incurred but Not Reported Health Claims | | (109,611) |
| Compensated absences liability | | (606,658) |
| Net Pension Obligation | | (478,399) |
| Long-Term Litigation Settlement | | (741,474) |
| Net Position of Governmental Activities | \$ | <u><u>17,818,222</u></u> |

CITY OF WINCHESTER, KENTUCKY
STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES
GOVERNMENTAL FUNDS
FOR THE YEAR ENDED JUNE 30, 2013

| | <u>GENERAL</u> | <u>CAPITAL EQUIPMENT</u> | <u>FEDERAL GRANT FUNDS</u> | <u>NONMAJOR GOVERNMENTAL FUNDS</u> | <u>TOTAL GOVERNMENTAL FUNDS</u> |
|--|---------------------|------------------------------|------------------------------------|--|---|
| REVENUES: | | | | | |
| Taxes | \$ 10,310,433 | \$ 839,974 | \$ 0 | \$ 117,229 | \$ 11,267,637 |
| Licenses & Permits | 951,110 | 0 | 0 | 0 | 951,110 |
| Charges for Services | 1,369,373 | 0 | 0 | 0 | 1,369,373 |
| Fines | 2,055 | 0 | 0 | 0 | 2,055 |
| Intergovernmental | 1,439,681 | 103,330 | 8,208,839 | 753,691 | 10,505,540 |
| Investment Income | 21,253 | 14,323 | 0 | 7,798 | 43,374 |
| Other | 152,563 | 10,118 | 0 | 69,136 | 231,817 |
| TOTAL REVENUES | <u>14,246,467</u> | <u>967,745</u> | <u>8,208,839</u> | <u>947,854</u> | <u>24,370,905</u> |
| EXPENDITURES: | | | | | |
| City Commission | 312,028 | 47,018 | 0 | 0 | 359,045 |
| City Attorney | 53,267 | 0 | 0 | 0 | 53,267 |
| City Manager | 422,299 | 3,234 | 0 | 0 | 425,533 |
| Finance Department | 341,863 | 4,182 | 0 | 0 | 346,045 |
| Planning Department | 358,126 | 1,023 | 0 | 5,542 | 364,691 |
| Main Street Department | 73,421 | 0 | 0 | 42,621 | 116,042 |
| Engineering | 98,938 | 0 | 0 | 0 | 98,938 |
| Conservancy | 19,689 | 0 | 0 | 0 | 19,689 |
| Administration | 691,874 | 297,585 | 853,340 | 0 | 1,842,799 |
| Central Communications | 752,930 | 1,729 | 0 | 0 | 754,659 |
| Police Department | 3,277,157 | 90,061 | 25,738 | 68,402 | 3,461,357 |
| Fire Department | 3,354,862 | 79,344 | 42,707 | 4,859 | 3,481,772 |
| EMS Division | 2,099,109 | 238,073 | 0 | 0 | 2,337,182 |
| Public Works | 988,164 | 40,692 | 0 | 441,091 | 1,469,948 |
| Intergovernmental | 672,078 | 0 | 7,287,054 | 118,658 | 8,077,790 |
| Capital | 0 | 0 | 0 | 0 | 0 |
| Debt Service Principal | 0 | 261,908 | 0 | 0 | 261,908 |
| Debt Service Interest | 0 | 92,768 | 0 | 0 | 92,768 |
| TOTAL EXPENDITURES | <u>13,515,805</u> | <u>1,157,618</u> | <u>8,208,839</u> | <u>681,172</u> | <u>23,563,433</u> |
| Excess (Deficit) of Revenues over Expenditures | <u>730,663</u> | <u>(189,873)</u> | <u>0</u> | <u>266,682</u> | <u>807,472</u> |
| OTHER FINANCING SOURCES (USES): | | | | | |
| Proceeds from long-term borrowing | 0 | 204,784 | 0 | 0 | 204,784 |
| Infrastructure contributions | 0 | 0 | 0 | 0 | 0 |
| Operating transfers in | 0 | 0 | 0 | 0 | 0 |
| Operating transfers out | 0 | 0 | 0 | 0 | 0 |
| TOTAL OTHER FINANCING SOURCES (USES): | <u>0</u> | <u>204,784</u> | <u>0</u> | <u>0</u> | <u>204,784</u> |
| Excess (Deficit) of Revenues and Other Financing Sources over Expenditures and Other Financing Uses | 730,663 | 14,911 | 0 | 266,682 | 1,012,256 |
| Fund Balance June 30, 2012 | <u>4,192,991</u> | <u>2,008,769</u> | <u>0</u> | <u>903,786</u> | <u>7,105,546</u> |
| Fund Balance June 30, 2013 | <u>\$ 4,923,654</u> | <u>\$ 2,023,680</u> | <u>\$ 0</u> | <u>\$ 1,170,468</u> | <u>\$ 8,117,802</u> |

See Accompanying Notes to the Financial Statements

**CITY OF WINCHESTER, KENTUCKY
RECONCILIATION OF THE STATEMENT OF REVENUES,
EXPENDITURES AND CHANGES IN FUND BALANCES OF
GOVERNMENTAL FUNDS TO THE STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED JUNE 30, 2013**

| | |
|--|--------------|
| Net Change in Fund Balances - Total Governmental Funds | \$ 1,012,256 |
| Amounts reported for governmental activities in the statement of activities are different because: | |
| Capital outlays are reported as expenditures in the fund financial statement because they are current financial resources, but they are presented as assets in the statement of activities and depreciated over their estimated economic lives. | 1,879,135 |
| Depreciation expense is reported in the statement of activities to recognize the cost of capital assets used to provide programs and services. | (1,252,302) |
| Proceeds of lease proceeds are reported as sources of funds in the fund statements and increases in long-term debt in the governmentwide statements. | (204,784) |
| Gain/loss on sale of capital assets is reported in the statement of activities to recognize the disposal of capital assets. | |
| Developer contributions of roads and infrastructure are reported in the statement of activities. | |
| Accrued litigation settlement was recognized in governmentwide statements in previous year and adjusted in the current year as a result of revised estimates. | |
| Pension liability costs are not reported in the fund financial statements because they are not due in the current period, but they are presented as long-term liabilities in the statement of net position. | (37,827) |
| Health insurance claims that have been incurred, but not reported as of June 30, are not reported in the fund financial statements because they are not due in the current period, but they are presented as long-term liabilities in the statement of net position. | (11,611) |
| Compensated absences are not reported in the fund financial statements because they are not due in the current period, but they are presented as long-term liabilities in the statement of net position. | 11,853 |
| Bond and lease payments are recognized as expenditures of current financial resources in the fund financial statement, but are reductions of liabilities in the statement of net position. | 261,908 |
| | _____ |
| Change in Net Position of Governmental Activities | \$ 1,658,628 |

See Accompanying Notes to the Financial Statements

CITY OF WINCHESTER, KENTUCKY
SCHEDULE OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES
BUDGET TO ACTUAL MAJOR GOVERNMENTAL FUNDS
FOR THE YEAR ENDED JUNE 30, 2013

| | GENERAL FUND | | | |
|--|---------------------|---------------------|---------------------|----------------------------|
| | BUDGETED AMOUNTS | | ACTUAL | VARIANCE |
| | ORIGINAL | FINAL | | Favorable (Unfavorable) |
| REVENUES: | | | | |
| Taxes | \$ 9,935,000 | \$ 9,935,000 | \$ 10,310,433 | \$ 375,433 |
| Licenses & Permits | 960,000 | 960,000 | 951,110 | (8,890) |
| Charges for Services | 2,865,000 | 2,865,000 | 1,369,373 | (1,495,627) |
| Fines | 0 | 0 | 2,055 | 2,055 |
| Intergovernmental | 1,375,000 | 1,375,000 | 1,439,681 | 64,681 |
| Investment Income | 0 | 0 | 21,253 | 21,253 |
| Other | 0 | 0 | 152,563 | 152,563 |
| TOTAL REVENUES | <u>15,135,000</u> | <u>15,135,000</u> | <u>14,246,467</u> | <u>(888,533)</u> |
| EXPENDITURES: | | | | |
| General Government | 2,660,000 | 2,706,000 | 2,371,505 | 334,495 |
| Central Communications | 843,300 | 843,300 | 752,930 | 90,370 |
| Police Department | 3,614,400 | 3,614,400 | 3,277,157 | 337,243 |
| Fire Department | 3,704,800 | 3,704,800 | 3,354,862 | 349,938 |
| EMS Division | 2,239,800 | 2,239,800 | 2,099,109 | 140,691 |
| Public Works | 2,517,200 | 2,517,200 | 988,164 | 1,529,036 |
| Intergovernmental | 684,100 | 685,100 | 672,078 | 13,022 |
| Capital | 0 | 0 | 0 | 0 |
| Debt Service Principal | 0 | 0 | 0 | 0 |
| Debt Service Interest | 0 | 0 | 0 | 0 |
| TOTAL EXPENDITURES | <u>16,263,600</u> | <u>16,310,600</u> | <u>13,515,805</u> | <u>2,794,795</u> |
| Excess (Deficit) of Revenues over Expenditures | <u>(1,128,600)</u> | <u>(1,175,600)</u> | <u>730,663</u> | <u>1,906,263</u> |
| OTHER FINANCING SOURCES (USES): | | | | |
| Proceeds of Long-Term Debt | 0 | 0 | 0 | 0 |
| Infrastructure Contributions | 0 | 0 | 0 | 0 |
| Operating Transfers In | 400,000 | 400,000 | 0 | 400,000 |
| Operating Transfers Out | 0 | 0 | 0 | 0 |
| TOTAL OTHER FINANCING SOURCES (USES): | <u>400,000</u> | <u>400,000</u> | <u>0</u> | <u>400,000</u> |
| Excess (Deficit) of Revenues and Other Financing Sources over Expenditures and Other Financing Uses | <u>(728,600)</u> | <u>(775,600)</u> | <u>730,663</u> | <u>2,306,263</u> |
| Fund Balance June 30, 2012 | <u>3,600,200</u> | <u>3,600,200</u> | <u>4,192,991</u> | <u>592,791</u> |
| Fund Balance June 30, 2013 | <u>\$ 2,871,600</u> | <u>\$ 2,824,600</u> | <u>\$ 4,923,654</u> | <u>\$ 2,899,054</u> |

See Accompanying Notes to the Financial Statements

CITY OF WINCHESTER, KENTUCKY
SCHEDULE OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES
BUDGET TO ACTUAL MAJOR GOVERNMENTAL FUNDS
FOR THE YEAR ENDED JUNE 30, 2013

| | SPECIAL REVENUE FUND (CAPITAL EQUIPMENT FUND) | | | |
|--|--|---------------------|---------------------|--|
| | BUDGETED AMOUNTS | | ACTUAL | VARIANCE Favorable (Unfavorable) |
| | ORIGINAL | FINAL | | |
| REVENUES: | | | | |
| Taxes | \$ 825,000 | \$ 825,000 | \$ 839,974 | \$ 14,974 |
| Licenses & Permits | 0 | 0 | 0 | 0 |
| Charges for Services | 0 | 0 | 0 | 0 |
| Fines | 0 | 0 | 0 | 0 |
| Intergovernmental | 100,900 | 165,400 | 103,330 | (62,070) |
| Investment Income | 15,000 | 15,000 | 14,323 | (677) |
| Other | 10,000 | 10,000 | 10,118 | 118 |
| TOTAL REVENUES | <u>950,900</u> | <u>1,015,400</u> | <u>967,745</u> | <u>(47,655)</u> |
| EXPENDITURES: | | | | |
| General Government | 335,960 | 599,952 | 353,042 | 246,910 |
| Central Communications | 2,300 | 2,300 | 1,729 | 571 |
| Police Department | 94,400 | 119,900 | 90,061 | 29,839 |
| Fire Department | 72,700 | 136,700 | 79,344 | 57,356 |
| EMS Division | 71,740 | 276,740 | 238,073 | 38,667 |
| Public Works | 53,200 | 53,200 | 40,692 | 12,508 |
| Intergovernmental | 0 | 0 | 0 | 0 |
| Capital | 0 | 0 | 0 | 0 |
| Debt Service Principal | 261,900 | 261,908 | 261,908 | 0 |
| Debt Service Interest | 92,800 | 92,800 | 92,768 | 32 |
| TOTAL EXPENDITURES | <u>985,000</u> | <u>1,543,500</u> | <u>1,157,618</u> | <u>385,883</u> |
| Excess (Deficit) of Revenues over Expenditures | <u>(34,100)</u> | <u>(528,100)</u> | <u>(189,873)</u> | <u>338,227</u> |
| OTHER FINANCING SOURCES (USES): | | | | |
| Proceeds of Long-Term Debt | 0 | 205,000 | 204,784 | (216) |
| Infrastructure Contributions | 0 | 0 | 0 | 0 |
| Operating Transfers In | (400,000) | (400,000) | 0 | 400,000 |
| Operating Transfers Out | 0 | 0 | 0 | 0 |
| TOTAL OTHER FINANCING SOURCES (USES): | <u>(400,000)</u> | <u>(195,000)</u> | <u>204,784</u> | <u>399,784</u> |
| Excess (Deficit) of Revenues and Other Financing Sources over Expenditures and Other Financing Uses | (434,100) | (723,100) | 14,911 | 738,011 |
| Fund Balance June 30, 2012 | <u>1,911,800</u> | <u>1,911,800</u> | <u>2,008,769</u> | <u>96,969</u> |
| Fund Balance June 30, 2013 | <u>\$ 1,477,700</u> | <u>\$ 1,188,700</u> | <u>\$ 2,023,680</u> | <u>\$ 834,980</u> |

See Accompanying Notes to the Financial Statements

CITY OF WINCHESTER, KENTUCKY
SCHEDULE OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES
BUDGET TO ACTUAL MAJOR GOVERNMENTAL FUNDS
FOR THE YEAR ENDED JUNE 30, 2013

| | SPECIAL REVENUE FUND (FEDERAL GRANT FUNDS) | | | |
|--|---|-------------------|------------------|--|
| | BUDGETED AMOUNTS | | ACTUAL | VARIANCE Favorable (Unfavorable) |
| | ORIGINAL | FINAL | | |
| REVENUES: | | | | |
| Taxes | \$ 0 | \$ 0 | \$ 0 | \$ 0 |
| Licenses & Permits | 0 | 0 | 0 | 0 |
| Charges for Services | 0 | 0 | 0 | 0 |
| Fines | 0 | 0 | 0 | 0 |
| Intergovernmental | 1,831,400 | 11,731,400 | 8,208,839 | (3,522,562) |
| Investment Income | 0 | 0 | 0 | 0 |
| Other | 0 | 0 | 0 | 0 |
| TOTAL REVENUES | 1,831,400 | 11,731,400 | 8,208,839 | (3,522,562) |
| EXPENDITURES: | | | | |
| General Government | 306,700 | 2,876,939 | 853,340 | 2,023,599 |
| Central Communications | 0 | 0 | 0 | 0 |
| Police Department | 42,000 | 42,000 | 25,738 | 16,263 |
| Fire Department | 0 | 42,707 | 42,707 | 0 |
| EMS Division | 0 | 0 | 0 | 0 |
| Public Works | 1,482,700 | 1,482,700 | 0 | 1,482,700 |
| Intergovernmental | 0 | 7,287,054 | 7,287,054 | 0 |
| Capital | 0 | 0 | 0 | 0 |
| Debt Service Principal | 0 | 0 | 0 | 0 |
| Debt Service Interest | 0 | 0 | 0 | 0 |
| TOTAL EXPENDITURES | 1,831,400 | 11,731,400 | 8,208,839 | 3,522,562 |
| Excess (Deficit) of Revenues over Expenditures | 0 | 0 | 0 | 0 |
| OTHER FINANCING SOURCES (USES): | | | | |
| Proceeds of Long-Term Debt | 0 | 0 | 0 | 0 |
| Infrastructure Contributions | 0 | 0 | 0 | 0 |
| Operating Transfers In | 0 | 0 | 0 | 0 |
| Operating Transfers Out | 0 | 0 | 0 | 0 |
| TOTAL OTHER FINANCING SOURCES (USES): | 0 | 0 | 0 | 0 |
| Excess (Deficit) of Revenues and Other Financing Sources over Expenditures and Other Financing Uses | 0 | 0 | 0 | 0 |
| Fund Balance June 30, 2012 | 0 | 0 | 0 | 0 |
| Fund Balance June 30, 2013 | \$ 0 | \$ 0 | \$ 0 | \$ 0 |

See Accompanying Notes to the Financial Statements

**CITY OF WINCHESTER, KENTUCKY
STATEMENT OF NET POSITION
PROPRIETARY FUND (COMPONENT UNIT)
JUNE 30, 2013**

| | ENTERPRISE FUND |
|--|-----------------------|
| ASSETS: | |
| Current Assets | |
| Cash and Cash Equivalents | \$ 7,658,841 |
| Restricted Cash and Cash Equivalents | 351,373 |
| Restricted Investments | 4,729,869 |
| Accounts Receivable, Customers, Net of Allowance of Doubtful Accounts, \$46,831 | 1,718,516 |
| SDC Assessments Receivable | 940,509 |
| Due From Other Governments | 0 |
| Other Accounts Receivables | 10,729 |
| Accrued Interest | 6,738 |
| Materials and Supplies | 351,665 |
| Prepaid Expenses | 720,328 |
| Total Current Assets | 16,488,568 |
| Restricted Assets | |
| Cash and Cash Equivalents | 8,136,845 |
| Total Restricted Assets | 8,136,845 |
| Property, Plant and Equipment | |
| Utility Systems, Net of Depreciation | 66,152,427 |
| Land | 1,051,011 |
| Construction in Progress | 43,084,130 |
| Total Property, Plant and Equipment | 110,287,568 |
| Other Assets, Unamortized | |
| Bond Issue Costs | 159,725 |
| Other Receivable | 0 |
| Total Other Assets | 159,725 |
| TOTAL ASSETS | \$ 135,072,706 |
| LIABILITIES: | |
| Current Liabilities | |
| Accounts Payable | \$ 370,010 |
| Other Accrued Liabilities | 287,977 |
| Compensated Absences | 0 |
| Current Portion of Capital Lease Payable | 6,974 |
| Total Current Liabilities | 664,961 |
| Current Liabilities Payable from Restricted Assets | |
| Accounts Payable - Construction | 25,275 |
| Accounts Payable - Retainage | 0 |
| Customer Deposits | 155,489 |
| Current Portion of Long-Term Debt | 3,282,283 |
| Total Current Liabilities from Restricted Assets | 3,463,047 |
| Long-Term Debt, Less Current Portion | |
| Long-Term Debt, Less Current Portion | 65,377,038 |
| Compensated Absences | 395,076 |
| Total Long-Term Debt, Less Current Portion | 65,772,114 |
| TOTAL LIABILITIES | 69,900,122 |
| NET POSITION | |
| Net Invested in Capital Assets | 41,621,273 |
| Restricted for Capital Projects (Expendable) | 12,158,802 |
| Restricted for Bond Debt Service (Expendable) | 890,442 |
| Unrestricted | 10,502,067 |
| TOTAL NET POSITION | 65,172,584 |
| TOTAL LIABILITIES AND NET POSITION | \$ 135,072,706 |

See Accompanying Notes to the Financial Statements

CITY OF WINCHESTER, KENTUCKY
STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET POSITION
PROPRIETARY FUND (COMPONENT UNIT)
FOR THE YEAR ENDED JUNE 30, 2013

| | <u>ENTERPRISE FUND</u> |
|--|-----------------------------|
| OPERATING REVENUES: | |
| Water | \$ 5,269,419 |
| Wastewater | 6,826,218 |
| Solid Waste | 3,260,013 |
| Transfer Station | 47,476 |
| Other Income | 0 |
| TOTAL OPERATING REVENUES | <u>15,403,126</u> |
| OPERATING EXPENSES: | |
| Administrative | 1,985,151 |
| Solid Waste | 1,755,845 |
| Water | 2,990,591 |
| Wastewater | 4,701,673 |
| Vehicle Maintenance | 150,255 |
| TOTAL OPERATING EXPENSES | <u>11,583,515</u> |
| Operating Income (Loss) | 3,819,611 |
| NON-OPERATING REVENUES (EXPENSES) | |
| Interest Income | 136,511 |
| Interest Expense | (804,569) |
| Other Income | 222,464 |
| Gain on Sale of Capital Assets | 53,789 |
| Investment Income | (36,477) |
| Federal and State Grants | 83,506 |
| Amortization Expense of Bond Issue Costs & Bond Discount | (27,816) |
| TOTAL NON-OPERATING REVENUES (EXPENSES) | <u>(372,592)</u> |
| Net Income (Loss) before Capital Grants & Contributions | 3,447,019 |
| Capital Grants and Contributions | <u>827,720</u> |
| Change in Net Position | <u>4,274,739</u> |
| Net Position, Beginning of Year | <u>60,897,845</u> |
| Net Position, End of Year | <u><u>\$ 65,172,584</u></u> |

See Accompanying Notes to the Financial Statements

**CITY OF WINCHESTER, KENTUCKY
STATEMENT OF CASH FLOWS
PROPRIETARY FUND (COMPONENT UNIT)
FOR THE YEAR ENDED JUNE 30, 2013**

| | ENTERPRISE FUND |
|--|----------------------------|
| CASH FLOWS FROM OPERATING ACTIVITIES | |
| Receipts from Customers | \$ 15,378,738 |
| Payments to Suppliers | (6,480,467) |
| Payments to Employees | (2,538,627) |
| Other Receipts (Payments) | <u>39,740</u> |
| Net Cash Provided (Used) by Operating Activities | <u>6,399,384</u> |
| CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES | |
| Proceeds from Sale of Equipment | 53,789 |
| Proceeds from Long-Term Debt | 9,371,490 |
| Principal Payments | (1,823,089) |
| Interest Payments | (1,432,763) |
| Purchase of Property, Plant and Equipment | (14,528,751) |
| Proceeds from Federal and State Grants - Capital Items | 83,506 |
| Contributed Capital Received | 827,720 |
| Cash from Other Income | <u>222,464</u> |
| Net Cash Provided (Used) by Capital and Related Financing Activities | <u>(7,225,634)</u> |
| CASH FLOWS FROM INVESTING ACTIVITIES | |
| Proceeds from Sales and Maturities of Investments | 1,401,256 |
| Purchase of Investments | (960,000) |
| Cash from Interest | <u>136,511</u> |
| Net Cash Provided (Used) by Investing Activities | <u>577,767</u> |
| Net Increase (Decrease) in Cash and Cash Equivalents | (248,483) |
| Cash and Cash Equivalents, Beginning of Year | <u>16,395,542</u> |
| Cash and Cash Equivalents, End of Year | <u>\$ 16,147,059</u> |
| Reconciliation of Cash and Cash Equivalents to the Statement of Net Assets: | |
| Cash and Cash Equivalents - Unrestricted | 7,658,841 |
| Cash and Cash Equivalents - Restricted | 351,373 |
| Restricted Assets - Cash and Cash Equivalents | <u>8,136,845</u> |
| Cash and Cash Equivalents, End of Year | <u>\$ 16,147,059</u> |
| Reconciliation of Operating Income (Loss) to Net Cash Provided by Operating Activities: | |
| Operating Income (Loss) | \$ 3,819,611 |
| Adjustments to Reconcile Net Income (Loss) to Net Cash from Operating Activities: | |
| Depreciation/Amortization | 3,386,759 |
| Changes in Assets and Liabilities: | |
| Accounts Receivable, Customers | (24,719) |
| SDC Assessments Receivable | 2,527 |
| Other Accounts Receivable | 39,974 |
| Other Receivable | (233) |
| Material and Supplies | (35,990) |
| Prepaid Expenses | (104,036) |
| Accounts Payable | (266,043) |
| Accounts Payable - Construction | (261,815) |
| Accounts Payable - Retainage | (75,126) |
| Accrued Liabilities | (73,103) |
| Accrued Payroll and Vacation | (6,226) |
| Customer Deposits | <u>(2,196)</u> |
| Net Cash Provided (Used) by Operating Activities | <u>\$ 6,399,384</u> |
| NONCASH TRANSACTIONS AFFECTING FINANCIAL POSITION | |
| Capital assets were acquired through contributions from Developers and Governmental Entities | \$ 300 |
| | <u>\$ 300</u> |

See Accompanying Notes to the Financial Statements

**CITY OF WINCHESTER, KENTUCKY
STATEMENT OF FIDUCIARY NET POSITION
FIDUCIARY FUND
JUNE 30, 2013**

| | <u>PENSION TRUST</u> | <u>AGENCY FUND</u> |
|-------------------------------|-----------------------------------|------------------------|
| ASSETS: | | |
| Cash and Cash Equivalents | \$ 12,493 | \$ 3,186 |
| Investments | 1,547,996 | |
| Accrued Investment Income | <u>8,454</u> | |
| TOTAL ASSETS | \$ <u>1,568,943</u> | \$ <u>3,186</u> |
| LIABILITIES: | | |
| Accounts Payable | | 1,895 |
| Due to General Fund | \$ 1,649 | |
| Due to Member Agencies | | <u>1,292</u> |
| TOTAL LIABILITIES | \$ <u>1,649</u> | \$ <u>3,186</u> |
| FIDUCIARY NET POSITION | \$ <u><u>1,567,294</u></u> | |

(1) A schedule of funding progress for the pension plan is presented in the Required Supplementary Information section of this report.

**CITY OF WINCHESTER, KENTUCKY
STATEMENT OF CHANGES IN FIDUCIARY NET POSITION
FIDUCIARY FUND
FOR THE YEAR ENDED JUNE 30, 2013**

| | <u>PENSION TRUST</u> | <u>AGENCY FUND</u> |
|--|----------------------------|------------------------|
| ADDITIONS: | | |
| Contributions | \$ 13,981 | \$ 23,500 |
| Other revenue | 0 | 0 |
| Investment Income: | | |
| Interest | 38,316 | 85 |
| Net Appreciation (Depreciation) in Fair Value of Investments | (4,641) | 0 |
| (Gain) Loss on Sale of Investments | (42,050) | 0 |
| Less: Investment Expense | <u>(6,032)</u> | <u>0</u> |
| Net Investment Income | <u>(14,408)</u> | <u>85</u> |
| Total Additions | (426) | 23,585 |
| DEDUCTIONS: | | |
| Benefits | 107,761 | 0 |
| Program Expenses | 0 | 31,677 |
| Due to Members | 0 | (8,092) |
| HRA Benefits | 8,981 | 0 |
| Taxes | <u>5,424</u> | <u>0</u> |
| Total Deductions | 122,166 | 23,585 |
| Change in Net Position | (122,592) | 0 |
| Net Position June 30, 2012 | <u>1,689,886</u> | <u>0</u> |
| Net Position June 30, 2013 | <u><u>\$ 1,567,294</u></u> | <u><u>\$ 0</u></u> |

See Accompanying Notes to the Financial Statements

**CITY OF WINCHESTER, KENTUCKY
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2013**

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The City of Winchester, Kentucky was incorporated and founded in 1793, and has a population of 18,368 based on the 2010 census and is the County Seat of Clark County, Kentucky. The City is a Kentucky Municipal Corporation governed and operated under a manager/commission form of Government with a five-member city commission comprised of the Mayor and four city commissioners.

The financial statements of the City of Winchester, Kentucky, (the City), have been prepared in conformity with accounting principles generally accepted in the United States as applied to governmental units. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. Significant accounting policies of the City are described below.

THE FINANCIAL REPORTING ENTITY

In evaluating the City as a reporting entity, management has addressed all potential component units (traditionally separate reporting entities) which may or may not fall within the City's oversight and control and, as such, be included within the City's financial statements. These determinations are based on the provisions of GASB Statement 14, *The Financial Reporting Entity*, amended by GASB Statement 61, *The Financial Reporting Entity: Omnibus*, which focus on the concept of financial accountability, fiscal dependence, and the financial benefits or burdens on the primary government. The basic criterion for including Winchester Municipal Utilities as a component unit within the City's reporting entity is the exercise of oversight responsibility by Winchester's Board of Commissioners and the City's potential obligation for the WMU bonded indebtedness.

The relative importance of fiscal accountability must be evaluated in light of specific circumstances. The following is a brief review of each of the potential component units addressed in defining the City's reporting entity:

1. INCLUDED WITHIN THE ENTITY - Winchester Municipal Utilities Commission (WMU) - The City has the following oversight responsibilities: Appointment and removal of Board members, approval of utility rates, approval of issuance and sale of bonds, and the sale or purchase of land. The basic financial statements have been included in the City's reporting entity as the component unit.
2. EXCLUDED FROM THE ENTITY:
 - (a) The following joint city/county entities are not included in the City's reporting entity because of shared oversight responsibilities: Winchester/Clark County Planning and Zoning Commission, Winchester/Clark County Parks and Recreation Board, Clark County/Winchester Heritage Commission, Winchester/Clark County Recreational, Tourist and Convention Commission, Winchester/Clark County Industrial Development Authority, Winchester/Clark County Board of Adjustment, Winchester Historic Presentation Commission, Winchester/Clark County Appeals Board and the Municipal Cemetery Board.

CITY OF WINCHESTER, KENTUCKY
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2013

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

- (b) Housing Authority of Winchester and Urban Renewal and Community Development Agency - The appointment of the Governing Boards and the scope of public service are not considered an adequate demonstration of oversight and control. The City has no responsibility for the budgets, debts or financing deficits for either the Housing Authority of Winchester or Urban Renewal and Community Development Agency.

Further information regarding these agencies, their financial statements, and/or operations may be obtained by contacting the agencies directly.

Component Unit - WMU

Winchester Municipal Utilities (WMU) is a component unit of the City of Winchester, Kentucky and is accounted for as a governmental enterprise fund. The purpose of WMU is to operate the City's water, sewer and solid waste utility services. It is financed and operated in a manner similar to a private business enterprise where the intent of the governing body is that costs (expenses, including depreciation) of providing goods or services to the general public on a continuing basis are financed primarily through user charges. The financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. The accounts are maintained on the accrual basis of accounting. Revenues are recognized when earned and expenses are recognized when incurred.

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

BASIS OF PRESENTATION

Government-wide Financial Statements - The statement of net position and the statement of activities display information about the City as a whole. They include all funds of the reporting entity except for fiduciary funds. The statements distinguish between governmental and business-type activities. Governmental activities generally are financed through taxes, intergovernmental revenues, and other non-exchange revenues. Business-type activities are financed in whole or in part by fees charged to external parties for goods or services.

The government-wide statement of activities presents a comparison between direct expenses and program revenues for each segment of the business-type activities of the City and for each function or program of the City's governmental activities. Direct expenses are those that are specifically associated with a service, program or department and are therefore clearly identifiable to a particular function. Program revenues include charges paid by the recipient of the goods or services offered by the program and grants and contributions that are restricted to meeting the operational or capital requirements of a particular program. Revenues that are not classified as program revenues are presented as general revenues of the City, with certain limited exceptions. The comparison of direct expenses with program revenues identifies the extent to which each business segment or governmental function is self-financing or draws from the general revenues of the City.

CITY OF WINCHESTER, KENTUCKY
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2013

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Fund Financial Statements - Fund financial statements report detailed information about the City. The focus of governmental and enterprise fund financial statements is on major funds rather than reporting funds by type. Each major fund is presented in a separate column. Non-major funds are aggregated and presented in a single column. Fiduciary funds are reported by fund type.

Fund Accounting

The City maintains its accounting records in accordance with the principles of “fund” accounting. Fund accounting is a concept developed to meet the needs of governmental entities in which legal or other restraints require the recording of specific receipts and disbursements. The transactions of each fund are reflected in a self-balancing group of accounts which stands separate from the activities reported in other funds. A description along with the restrictions associated with each class of funds is as follows:

A. Governmental Fund Types

The General Fund is the main operating fund of the City. It accounts for financial resources used for general types of operations. This is a budgeted fund, and any fund balances are considered as resources available for use.

The special revenue funds account for proceeds of specific revenue sources (other than special assessments, or major capital projects) that are legally restricted to expenditures for specified purposes. The City’s special revenue funds include funds for tax resources that are restricted to specific purposes as well as the sources and uses of federal, state, and local intergovernmental programs and grants.

B. Proprietary Funds (Enterprise Fund)

The enterprise fund is used to account for operations (a) that are financed and operated in a manner similar to private business enterprises - where the intent of the governing body is that the costs (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 City’s enterprise fund is used to account for the operations of the component unit, Winchester Municipal Utilities.

C. Fiduciary Fund Type (includes Pension Trust and Agency Funds).

The measurement focus of the pension trust fund is similar to proprietary funds, using the accrual basis of accounting. The agency fund is purely custodial (assets equal liabilities) and thus, do not involve measurement of results of operations.

The pension trust fund is used to account for assets held by the City in a trustee capacity for former employees. The agency fund accounts for revenues and expenses of the Kentucky Regional Cable Commission (KRCC) and the City of Winchester provides the administrative bookkeeping services for the KRCC.

CITY OF WINCHESTER, KENTUCKY
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2013

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Measurement Focus and Basis of Accounting

Measurement focus is a term used to describe “which” transactions are recorded within the various financial statements. Basis of accounting refers to “when” transactions are recorded regardless of the measurement focus applied.

On the government-wide statement of net position and the statement of activities, both governmental and business-like activities are presented using the economic resources measurement focus. The accounting objectives of this measurement focus are the determination of operating income, changes in net position (or cost recovery), financial position, and cash flows. All assets and liabilities (whether current or noncurrent) associated with their activities are reported.

In the fund financial statements, the “current financial resources” measurement focus or the “economic resources” measurement focus is used as appropriate:

1. All governmental funds utilize a “current financial resources” measurement focus. Only current financial assets and liabilities are generally included on their balance sheets. Their operating statements present sources and uses of available spendable financial resources during a given period. These funds use fund balance as their measure of available spendable financial resources at the end of the period.
2. The proprietary fund utilizes an “economic resources” measurement focus.

BASIS OF ACCOUNTING

Basis of accounting determines when transactions are recorded in the financial records and reported on the financial statements.

In the government-wide statement of net position and statement of activities, both governmental and business-like activities are presented using the accrual basis of accounting. Under the accrual basis of accounting, revenues are recognized when earned and expenses are recorded 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. Non-exchange transactions, in which the City receives value without directly giving equal value in return, include property taxes, grants, entitlements and donations.

On an accrual basis, revenue from property taxes is recognized in the fiscal year for which the taxes are levied. Revenue from grants, entitlements and donations is recognized in the fiscal year in which all eligibility requirements have been satisfied.

In the fund financial statements, governmental funds and agency funds are presented on the modified accrual basis of accounting. Under this modified accrual basis of accounting, revenues are recognized when “measurable and available.” Measurable means knowing or being able to reasonably estimate the amount. Available means collectible within the current period or within sixty days after year end. Expenditures (including capital outlay) are recorded when the related fund liability is incurred, except for general obligation bond principal and interest which are reported when due.

CITY OF WINCHESTER, KENTUCKY
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2013

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

The proprietary fund utilizes the accrual basis of accounting. Under the accrual basis of accounting, revenues are recognized when earned and expenses are recorded when the liability is incurred or economic asset used.

Revenues from local sources consist primarily of payroll, insurance premium and property taxes. Property taxes collected are recorded as revenues in the fund for which they were levied. These revenues are recognized when susceptible to accrual. Miscellaneous revenues are recorded on the same basis, if measurable. Investment earnings are recorded as earned since they are measurable and available.

Grant funds which are recorded in the special revenue fund as restricted funds are considered to be earned to the extent of expenditures made under the provisions of the grant and, accordingly, when such funds are received they are recorded as deferred revenues until earned.

BUDGETARY PROCESS

The City Commission annually adopts the Budget Ordinance for General Fund, Capital Equipment Fund, Municipal Road Aid Fund, LGEA Fund and Pass Thru Grant Funds. Budgetary control is legally maintained at the department level. In the accompanying financial statements and supplementary information, the following line items are grouped for budget purposes under the Administration Department: City Commission, City Attorney, City Manager, Finance Department, Planning Department, Engineering, Administration, and Main Street.

The City's budget ordinance provides transfer authority to the City Manager for budgeted amounts within departments of any fund. Any revisions that alter the total expenditures of any department of any fund must be approved by the City Commission.

All budget amounts presented in the accompanying financial statements have been adjusted for legally authorized revisions of the annual budgets during the year. The budgets adopted for the above funds are on the modified accrual basis which is a method that is consistent with generally accepted account principles (GAAP). All appropriations lapse at year-end.

CASH, CASH EQUIVALENTS AND INVESTMENTS

The City considers demand deposits, money market funds, and other investments with an original maturity of 90 days or less, to be cash equivalents.

Managed funds related to the retirement systems not listed on an established market are reported at estimated fair value as determined by the respective fund managers based on quoted sales prices of the underlying securities.

All investments are stated at fair value. Investment fair values are based on quoted market prices. All investments are restricted as to use.

CITY OF WINCHESTER, KENTUCKY
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2013

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

ACCOUNTS RECEIVABLE-COMPONENT UNIT (WMU)

Accounts Receivable, Customers is stated at the amount management expects to collect from outstanding balances. Management provides for probable uncollectible amounts through a provision for bad debt expense. An adjustment to an allowance for doubtful accounts is based on its assessment of the current status of individual accounts. Balances that are still outstanding after management has used reasonable collection efforts are written off through a charge to the valuation allowance and a credit to accounts receivable. As of June 30, 2013 and 2012, \$34,730 and \$53,973 were written off as uncollectible, respectively.

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

INVENTORIES AND PREPAIDS

Materials and supplies of component unit (WMU) are stated at cost. Cost is determined using the "first-in, first-out" method.

Prepaid expenses record payments to vendors that benefit future reporting periods on the consumption basis. Both inventories and prepaids are similarly reported in government-wide and fund financial statements.

RESTRICTED ASSETS- COMPONENT UNIT (WMU)

The use of certain assets of enterprise funds is restricted by specific provisions of bond resolutions and agreements with various parties. Assets so designated are identified as restricted assets on the statement of net position. When both restricted and unrestricted resources are available for use, it is WMU's policy to use restricted resources first, and then unrestricted resources as they are needed. Restricted assets are classified as noncurrent if they are for acquisition or construction of capital assets, for liquidation of long-term debt, or are for other current operations.

CAPITAL ASSETS

Capital assets are defined by the City as assets with an initial, individual cost of \$500 or more and an estimated useful life in excess of one year. General capital assets are those assets not specifically related to activities reported in the proprietary funds. These assets generally result from expenditures in the governmental funds. These assets are reported in the governmental activities column of the government-wide statement of net position, but are not reported in the fund financial statements. Capital assets utilized by the proprietary funds are reported in the component unit column of the government-wide statement of net position.

All capital assets are capitalized at cost (or estimated historical costs) and updated for additions and retirements during the year. Donated fixed assets are recorded at their fair market values as of the date received. Improvements are capitalized; however, the cost of normal maintenance and repairs that do not add to the value of the asset or materially extend an asset's life are expensed.

All reported capital assets are depreciated. Improvements are depreciated over the remaining useful lives of the related capital assets.

CITY OF WINCHESTER, KENTUCKY
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2013

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

PROPERTY, PLANT AND EQUIPMENT – COMPONENT UNIT (WMU)

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

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

The costs of normal maintenance and repairs that do not add to the value of the asset or materially extend assets' lives are not capitalized

Assets under capitalized lease obligations are recorded at the discounted present value of the future minimum lease payments at the inception of the respective leases. The amounts capitalized are being amortized by the straight-line method over the lesser of the term of the lease or the estimated life of the asset. Amortization of these assets is included in depreciation expense.

ESTIMATES

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect reported amounts of assets, liabilities, designated fund balances, and disclosure of contingent assets and liabilities at the date of the governmental financial statements, and the reported amounts of revenues and expenditures during the reporting period. Actual results could differ from those estimates.

BOND AMORTIZATION COSTS-COMPONENT UNIT (WMU)

Bond premiums and discounts, as well as issuance costs, are deferred and amortized over the life of the bonds. Bonds payable are reported net of the applicable bond premium or discount. Bond issuance costs are reported as deferred charges and amortized over the term of the related debt.

Amortization expense for bond issue costs as of June 30, 2013 and 2012 was \$8,628 and \$59,709, respectively. Amortization expense for bond discount as of June 30, 2013 and 2012 was \$19,187 and \$112,536, respectively.

COMPENSATED ABSENCES

It is the City's policy to permit employees to accumulate earned, but unused sick leave which will be paid to employees upon separation from the City's service. In governmental funds, the cost of sick leave is recognized when payments are made to employees. In the government-wide financial statements, a long-term liability for accrued sick leave has been recorded representing the City's commitment to fund such costs from future operations.

The component unit's (WMU) accumulated vacation, sick leave and compensatory time are recorded as an expense and liability as these benefits accrue to employees in accordance with the provisions of Statement No. 16 of the Governmental Accounting Standards Board.

CITY OF WINCHESTER, KENTUCKY
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2013

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

LONG-TERM DEBT

The accounting treatment of long-term debt depends on whether the assets are used in governmental fund operations or proprietary fund operations and whether they are reported in the government-wide or fund financial statements.

All long-term debt to be repaid from governmental and business-type resources are reported as liabilities in the government-wide statements. The long-term debt consists primarily of notes payable, accrued compensated absences, retirement benefits and capital lease obligations.

Long-term debt for governmental funds is not reported as liabilities in the fund financial statements. The debt proceeds are reported as other financing sources and payment of principal and interest reported as expenditures. The accounting for proprietary fund is the same in the fund statements as it is in the government-wide statements.

INTERFUND TRANSFERS

Exchange transactions between funds are reported as revenues in the seller funds and as expenditures/expenses in the purchaser funds. Permanent reallocations of resources between funds of the reporting entity are classified as interfund transfers. For the purposes of the Statement of Activities, all interfund transfers between individual governmental funds have been eliminated. Repayments from funds responsible for particular expenditures/expenses to the funds that initially paid for them are not presented on the financial statements.

EQUITY CLASSIFICATIONS

Government-wide Statements - Equity is classified as net position. Net position is the difference between total assets and deferred outflows of resources less total liabilities and deferred inflows of resources. Proprietary fund equity is reported as net position. Net position is displayed in three components:

1. Net investment in capital assets—Consists of capital assets including restricted capital assets, net of accumulated depreciation and reduced by the outstanding balances of any bonds, mortgages, notes, or other borrowings that are attributable to the acquisition, construction, or improvement of those assets.
2. Restricted net position—Consists of net position with constraints placed on the use either by (1) external groups such as creditors, grantors, contributors, or laws or regulations of other governments; or (2) law through constitutional provisions or enabling legislation.
3. Unrestricted net position—All other net position that does not meet the definition of “restricted” or “invested in capital assets, net of related debt.”

Fund Statements - Governmental fund equity is classified as fund balance. Fund balance is further classified as nonspendable, restricted, committed, assigned or unassigned. Proprietary fund equity is classified the same as balances reported in the government-wide statements.

CITY OF WINCHESTER, KENTUCKY
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2013

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

REVENUE RECOGNITION – PROPERTY TAXES - Property taxes for 2012 were levied on the assessed property located in the City of Winchester as of the preceding January 1. The assessments are determined by the Clark County Property Valuation Administrator in accordance with Kentucky Revised Statutes. Taxes were levied on October 16, 2012 and were due December 7, 2012. Taxes unpaid after December 7, 2012 were delinquent and were subject to a 10% penalty, and interest of ½ of 1% per month.

Property tax revenues are recognized when they become available. Available includes those property tax receivables expected to be collected within sixty days after year end.

Based on collection histories, the City has provided at June 30, 2013, an allowance for uncollectible property taxes of 100% of delinquent accounts.

OPERATING AND NONOPERATING REVENUES AND EXPENSES - COMPONENT UNIT (WMU)

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

NONMONETARY TRANSACTION – COMPONENT UNIT (WMU)

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

CAPITAL AND OPERATING GRANTS AND SUBSIDIES – COMPONENT UNIT (WMU)

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

TAP FEES – COMPONENT UNIT (WMU)

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

SYSTEM DEVELOPMENT CHARGES - COMPONENT UNIT (WMU)

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

JOINT VENTURE – COMPONENT UNIT (WMU)

A joint venture is a legal entity or other organization that results from a contractual agreement and that is owned, operated or governed by two or more participants as a separate and specific activity subject to joint control in which the participants retain (a) an ongoing financial interest or (b) an ongoing financial responsibility. WMU participates in the following joint venture:

CITY OF WINCHESTER, KENTUCKY
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2013

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

JOINT VENTURE – COMPONENT UNIT (WMU) (CONTINUED)

Clark County Geographic Information System Consortium (CCGIS), is a governmental agency created by an inter-local agreement between the Clark County PVA, City of Winchester and WMU. CCGIS was created to provide a geographic system to serve the needs of Winchester and Clark County. The operations are funded by the City, WMU and the Clark County Fiscal Court. WMU provides management services for CCGIS. WMU contributed \$76,958 and \$64,782 for the years ended 2013 and 2012, respectively. CCGIS had accounts payables to WMU of \$0 and \$18,892 for the years ended 2013 and 2012, respectively, for reimbursements of payroll and other expenses. CCGIS had accounts receivable from WMU of \$0 and \$8,105 for the years ended 2013 and 2012, respectively, for excess reimbursements of payroll and other expenses. Complete financial statements for CCGIS can be obtained from WMU's Director of Finance.

IMPLEMENTATION OF GASB STANDARDS

The City implemented GASB Statement No. 62, Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989, FASB and AICPA Pronouncements, effective for periods beginning after December 15, 2011. GASB Statement No. 65 provides the accounting guidance for recognition of deferred inflows or outflows of resources. The City implemented this guidance as of June 30, 2012.

The City implemented GASB Statement No. 63, Financial Reporting of Deferred Outflows or Resources, Deferred Inflows of Resources and Net Position, effective for periods beginning after December 15, 2011, provides financial reporting guidance for deferred outflows of resources and deferred inflows of resources.

WMU has not yet implemented GASB Statement No. 65 and will expense \$58,097 of bond issuance costs recorded in prior years during FY 2014 to implement this guidance.

NOTE 2 - DEPOSITS AND INVESTMENTS

1. **DEPOSITS** - It is the City's policy for deposits to be 100% secured by collateral valued at market or par, whichever is lower, less the amount of the Federal Deposit Insurance Corporation insurance. All of the City's deposits were insured or collateralized with securities held by the City, its agent, or by the pledging financial institution's trust department or agent in the name of the City.

Kentucky Revised Statutes authorize municipalities to invest in obligations of the United States and its agencies, obligations of the Commonwealth of Kentucky and its agencies, shares in savings and loan associations insured by federal agencies and deposits in national or state chartered banks insured by federal agencies. Larger amounts can be deposited in savings and loan associations and banks providing such institutions pledge obligations of the United States government or its agencies as security. As of June 30, 2013, the City is in compliance with this requirement.

**CITY OF WINCHESTER, KENTUCKY
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2013**

NOTE 2 - DEPOSITS AND INVESTMENTS (CONTINUED)

2. INVESTMENTS - The City reports its' Pension Fund Investments under the provisions of Government Auditing Standards Board Statement No. 25, "Financial Reporting for Defined Benefit Plans and Note Disclosures for Defined Contribution Plans." The provisions of this statement require investments to be reported at fair value.

| <u>Investments</u> | <u>Fair Value</u> | <u>Cost</u> |
|----------------------------|--------------------|--------------------|
| Money Market Mutual Fund | \$ 110,323 | \$ 110,323 |
| U.S. Government Securities | 1,437,673 | 1,347,996 |
| Total Investments | <u>\$1,547,996</u> | <u>\$1,458,319</u> |

Custodial Credit Risk

Custodial credit risk for investments is the risk that, in the event of a failure of the counterparty to a transaction, the City will not be able to recover the value of the investments or collateral securities that are in possession of an outside party. The City does not have a formal policy for custodial credit risk. However, all investments are held in safekeeping by an external custodian, PNC Bank in Louisville, KY in the City's name.

Credit Risk

State law limits investments in accordance with KRS 95.600 "Pension Fund Investments". The City has no investment policy that would further limit its investment choices. As of June 30, 2013, the City's investments in money market mutual funds were unrated.

3. DEPOSITS AND INVESTMENTS (WMU) -The component unit's (WMU) investment policy conforms to state statutes. WMU deposits its funds in banks insured by FDIC. Investments include short term cash securities and United States backed securities. Collateral is required for all deposits in excess of FDIC at 100% of the carrying amount at the bank. Collateral consists of obligations of the United States and Kentucky municipal bonds.

Interest Rate Risk

This is the risk that changes in market interest rates will adversely affect the fair value of an investment. Generally, the longer the maturity of an investment, the greater the sensitivity of its fair value to changes in market interest rates. WMU does not have a formal investment policy that limits investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates. Information about the exposure of WMU's deposits and investments to this risk, using the segmented time distribution model is as follows:

| <u>06/30/13</u> | | <u>Maturities (in Years)</u> | | | |
|----------------------------|----------------------|------------------------------|--------------|---------------|---------------------|
| <u>Type</u> | <u>Fair Value</u> | <u>< Than 1</u> | <u>1 - 5</u> | <u>6 - 10</u> | <u>> Than 10</u> |
| Cash and Cash Equivalents | \$ 16,147,059 | \$ 16,147,059 | \$ 0 | \$ 0 | \$ 0 |
| U.S. Treasury Obligations | 4,332,646 | 4,332,646 | 0 | 0 | 0 |
| Federal Home Loan Mtg Corp | 185,316 | 185,316 | 0 | 0 | 0 |
| Federal Home Loan Bank | 211,907 | 211,907 | 0 | 0 | 0 |
| Total | <u>\$ 20,876,928</u> | <u>\$ 20,876,928</u> | <u>\$ 0</u> | <u>\$ 0</u> | <u>\$ 0</u> |

**CITY OF WINCHESTER, KENTUCKY
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2013**

NOTE 2 - DEPOSITS AND INVESTMENTS (CONTINUED)

Credit Risk

This risk is the risk that an issuer of a debt type investment will not fulfill its obligation to the holder of the investment. This is measured by assignment of a rating by a nationally recognized rating organization. U.S. Government securities or obligations explicitly guaranteed by the U.S. Government are not considered to have credit risk exposure. WMU has no formal policy on managing credit risk; however, Kentucky Revised Statutes authorize municipalities to invest in obligations of the United States and its agencies, obligations of the Commonwealth of Kentucky and its agencies and shares in savings and loan associations insured by federal agencies. Larger amounts can be deposited in savings and loan associations and banks provided such institutions pledge obligations of the United States government or its agencies as security. Presented below is the minimum rating required for each type of deposit and investment:

| 06/30/13 Type | Fair Value | Ratings | | | |
|----------------------------|---------------|--------------|------|------|---------------|
| | | AAA | AA | A | Unrated |
| Cash and Cash Equivalents | \$ 16,147,059 | \$ 0 | \$ 0 | \$ 0 | \$ 16,147,059 |
| U.S. Treasury Obligations | 4,332,646 | 4,332,646 | 0 | 0 | 0 |
| Federal Home Loan Mtg Corp | 185,316 | 185,316 | 0 | 0 | 0 |
| Federal Home Loan Bank | 211,907 | 211,907 | 0 | 0 | 0 |
| Total | \$ 20,876,928 | \$ 4,729,869 | \$ 0 | \$ 0 | \$ 16,147,059 |

Custodial Credit Risk

Custodial credit risk for investments is the risk that, in the event of a failure of the counterparty to a transaction, WMU will not be able to recover the value of deposits and investments or collateral securities that are in possession of an outside party. WMU has no formal policy for custodial credit risk; however, as of June 30, 2013 and 2012, all deposits and investments were either fully collateralized by federal depository insurance or by the pledging institution in WMU's name or were held in a bank's trust department in the City of Winchester's name, the primary government of the component unit, WMU.

NOTE 3 – CREATION OF ACCOUNTS AND RESTRICTED ASSETS - COMPONENT UNIT (WMU)

The Bond Ordinances require the creation of various separate deposit accounts designated for a specific purpose in accordance with the ordinance. A brief description of each required account is as follows:

Revenue Account

All income to WMU is deposited to the Revenue Account and then transferred to the other ordinance accounts as listed below.

Bond Redemption Account

The Bond Redemption Account was established to provide a source of funds for the payment of the bond principal and interest due within the current year. By the 20th day of each month funds equal to the total of one-sixth of the semiannual interest payment plus one-twelfth of the next annual bond principal payment are to be transferred to the account.

Reserve Account

The Reserve Account was established to provide funds for the payment of debt based on the least of three provisions: 1) maximum annual principal and interest, 2) 125% of the average annual principal and interest or 3) 10% of bond proceeds.

**CITY OF WINCHESTER, KENTUCKY
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2013**

NOTE 3 – CREATION OF ACCOUNTS AND RESTRICTED ASSETS - COMPONENT UNIT (WMU) (CONTINUED)

Depreciation Account

The Depreciation Account was established to provide funds for extraordinary repairs, improvements and expansion. WMU is required to fund 12% of the annual gross revenues or \$42,000 whichever is greater annually into the account.

Operation and Maintenance Account

The Operation and Maintenance Account was established to pay the reasonable necessary costs of operating, maintaining and repairing of the systems.

The restricted assets in the accompanying financial statements are restricted as to use by ordinance or by external parties. A schedule of restricted assets at June 30, 2013, follows:

| <u>06/30/13</u> | <u>Cash</u> | <u>Investments</u> | <u>Accrued Interest</u> | <u>Total</u> |
|-----------------------------------|---------------------|---------------------|-------------------------|----------------------|
| Restricted by Ordinance: | | | | |
| Bond Redemption Account | \$ 351,373 | \$ 0 | \$ 0 | \$ 351,373 |
| Reserve Accounts | 528,400 | 0 | 0 | 528,400 |
| Depreciation Account | 2,326,421 | 0 | 0 | 2,326,421 |
| Subtotal | <u>3,206,194</u> | <u>0</u> | <u>0</u> | <u>3,206,194</u> |
| Other Restricted Accounts: | | | | |
| SDC Water Fund | 2,623,222 | 0 | 0 | 2,623,222 |
| SDC Wastewater Fund | 1,376,260 | 0 | 0 | 1,376,260 |
| Customer Deposits | 175,581 | 0 | 0 | 175,581 |
| KIA Reserve | 10,669 | 0 | 0 | 10,669 |
| Water Improvements | 772,333 | 0 | 0 | 772,333 |
| 2011 Bond Funds | 0 | 4,729,869 | 6,595 | 4,736,464 |
| Capital Accum-Water | 231,409 | 0 | 102 | 231,511 |
| Capital Accum-Wastewater | 92,550 | 0 | 41 | 92,591 |
| Total | <u>\$ 8,488,218</u> | <u>\$ 4,729,869</u> | <u>\$ 6,738</u> | <u>\$ 13,224,825</u> |

CITY OF WINCHESTER, KENTUCKY
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2013

NOTE 4 – NET CAPITAL ASSETS AND PROPERTY PLANT AND EQUIPMENT

The following is a summary of changes in capital assets during the fiscal year:

| | Beginning Balance | Additions | Transfers & Retirements | Ending Balance |
|---|----------------------|--------------------|----------------------------|----------------------|
| Governmental activities: | | | | |
| Non-depreciable capital assets: | | | | |
| Construction in progress | \$ 395,064 | \$ (50,184) | \$ 0 | \$ 344,880 |
| Land | 1,986,538 | 0 | 0 | 1,986,538 |
| Total Non-depreciable capital assets | <u>2,381,602</u> | <u>(50,184)</u> | <u>0</u> | <u>2,331,418</u> |
| Depreciable capital assets: | | | | |
| Buildings | 5,492,818 | 1,998 | 0 | 5,494,816 |
| Vehicles | 5,271,923 | 312,804 | (180,328) | 5,404,399 |
| Computers | 398,845 | 1,197 | (350) | 399,692 |
| Equipment | 3,595,089 | 141,137 | (35,605) | 3,700,621 |
| Infrastructure | 20,715,865 | 1,472,183 | 0 | 22,188,048 |
| Total depreciable capital assets | <u>35,474,540</u> | <u>1,929,319</u> | <u>(216,283)</u> | <u>37,187,576</u> |
| Less accumulated depreciation | | | | |
| Buildings | (2,005,799) | (212,377) | 0 | (2,218,176) |
| Vehicles | (3,706,704) | (448,780) | 180,328 | (3,975,156) |
| Computers | (282,335) | (24,941) | 350 | (306,926) |
| Equipment | (2,777,321) | (272,382) | 35,605 | (3,014,098) |
| Infrastructure | (16,039,978) | (293,822) | 0 | (16,333,800) |
| Total accumulated depreciation | <u>(24,812,137)</u> | <u>(1,252,302)</u> | <u>216,283</u> | <u>(25,848,156)</u> |
| Total depreciable capital assets, net | <u>10,662,403</u> | <u>677,017</u> | <u>0</u> | <u>11,339,420</u> |
| Governmental activities capital assets, net | <u>\$ 13,044,005</u> | <u>\$ 626,833</u> | <u>\$ 0</u> | <u>\$ 13,670,839</u> |

Depreciation is computed using the straight-line method over the following useful lives for both general capital assets and proprietary fund assets:

| | |
|------------------------|-------------|
| Building | 5-45 years |
| Infrastructure | 20-35 years |
| Machinery & Equipment | 5-30 years |
| Transport Equipment | 5-28 years |
| Furniture and Fixtures | 5-48 years |

Depreciation expense for governmental activities was charged to the following functions:

| | |
|----------------------------|---------------------|
| General Government | \$ 581,951 |
| Public Protection | |
| Police | 143,695 |
| Fire Protection | 310,156 |
| EMS | 107,381 |
| Public Works | 109,119 |
| Total Depreciation Expense | <u>\$ 1,252,302</u> |

CITY OF WINCHESTER, KENTUCKY
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2013

**NOTE 4 – NET CAPITAL ASSETS AND PROPERTY PLANT AND EQUIPMENT
(CONTINUED)**

PROPERTY, PLANT AND EQUIPMENT – WMU

WMU's systems consist of the following:

| <u>06/30/13</u> | <u>Beginning</u> | <u>Additions</u> | <u>Disposals</u> | <u>Ending</u> |
|--|----------------------|----------------------|------------------------|----------------------|
| Non-depreciable Assets: | | | | |
| Land | \$ 1,051,011 | \$ 0 | \$ 0 | \$ 1,051,011 |
| Construction in Progress | 32,771,273 | 20,707,549 | (10,394,692) | 43,084,130 |
| Total Non-depreciable Assets | \$ 33,822,284 | \$ 20,707,549 | \$ (10,394,692) | \$ 44,135,141 |
| Depreciable Assets: | | | | |
| Administrative | \$ 3,083,795 | \$ 197,828 | \$ (20,807) | \$ 3,260,817 |
| Water System | 39,393,715 | 1,170,413 | (35,713) | 40,528,415 |
| Wastewater System | 65,690,211 | 3,387,040 | (419,965) | 68,657,286 |
| Solid Waste | 6,117,911 | 370,524 | (199,801) | 6,288,634 |
| Vehicle Maintenance | 440,980 | 2,288 | 0 | 443,268 |
| Equipment Capital Lease | 82,927 | 0 | 0 | 82,927 |
| Subtotal | 114,809,539 | 5,128,093 | (676,286) | 119,261,346 |
| Accumulated Depreciation: | | | | |
| Administrative | (1,354,420) | (167,189) | 17,819 | (1,503,790) |
| Water System | (10,468,292) | (931,153) | 0 | (11,399,445) |
| Wastewater System | (17,262,834) | (1,983,188) | 154,717 | (19,091,305) |
| Solid Waste | (1,474,628) | (281,432) | 197,288 | (1,558,772) |
| Vehicle Maintenance | (301,054) | (23,797) | 0 | (324,851) |
| Prior Years Accumulated | (19,230,756) | 0 | 0 | (19,230,756) |
| Subtotal | (50,091,984) | (3,386,759) | 369,824 | (53,108,919) |
| Total Net Property, Plant and Equipment | \$ 64,717,555 | \$ 1,741,334 | \$ (306,462) | \$ 66,152,427 |

Depreciation is recorded on a straight-line basis over the useful lives of the assets as follows:

| | |
|--------------------------|-------------|
| Buildings and Concrete | 40-50 years |
| Main Replacement Program | 40 years |
| Equipment | 2-7 years |
| Vehicles | 5-10 years |

Depreciation expense in total and by function follows:

| <u>Function</u> | <u>2013</u> |
|-----------------------------------|---------------------|
| Administrative | \$ 167,189 |
| Water System | 931,153 |
| Wastewater System | 1,983,188 |
| Solid Waste | 281,432 |
| Vehicle Maintenance | 23,797 |
| Total Depreciation Expense | \$ 3,386,759 |

NOTE 5 – CAPITALIZED INTEREST - WMU

Winchester Municipal Utilities follows the policy of capitalizing interest as a component of construction in progress. For the year ended June 30, 2013, total interest incurred was \$1,449,319, of which \$644,750 was capitalized and \$804,569 was expensed.

**CITY OF WINCHESTER, KENTUCKY
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2013**

NOTE 6 - INTERFUND RECEIVABLES AND PAYABLES

Interfund receivables and payables during the year ending June 30, 2013 were as follows.

| <u>Fund</u> | <u>Receivable</u> | <u>Payable</u> |
|---------------------|-------------------|------------------|
| General Fund | \$ 24,580 | \$ 0 |
| Federal Grant Funds | 0 | 22,931 |
| Fiduciary Funds | 0 | 1,649 |
| Total | <u>\$ 24,580</u> | <u>\$ 24,580</u> |

NOTE 7 – OPERATING LEASES

The City had five operating leases for copiers at June 30, 2013. Terms of the operating leases are as follows:

| <u>Date</u> | <u>Description</u> | <u>Payment</u> | <u>Months</u> | <u>Location</u> |
|-------------|--------------------|----------------|---------------|-----------------|
| 03/06/13 | IM440WP5 Copier | \$254 | 59 | City Hall |
| 10/30/12 | MP5002SP Copier | \$227 | 48 | Fire Department |
| 10/30/12 | MP4002SP Copier | \$227 | 48 | Fire-EMS |
| 10/22/12 | MPC5502 Copier | \$316 | 48 | City Hall |
| 08/01/11 | Toshiba Copier | \$74 | 48 | Police |

Rental expense for the current fiscal year was \$10,799. The future minimum payments are as follows:

| <u>Year</u> | <u>Amount</u> |
|-------------|------------------|
| 2014 | \$ 13,181 |
| 2015 | 13,181 |
| 2016 | 12,369 |
| 2017 | 6,132 |
| 2018 | 1,779 |
| Total | <u>\$ 46,643</u> |

NOTE 8 - CONSTRUCTION IN PROGRESS

Construction in progress at June 30, 2013 consists of the following:

| <u>Description</u> | <u>Balance June 30, 2012</u> | <u>Additions</u> | <u>Placed in Service</u> | <u>Balance June 30, 2013</u> |
|------------------------|----------------------------------|---------------------|------------------------------|----------------------------------|
| Depot Street | \$ 69,575 | \$ 974,786 | \$ 1,044,361 | \$ 0 |
| Bell Tower | 65,465 | 266,972 | 332,437 | 0 |
| US60 Traffic Signal | 44,463 | 30,612 | 75,075 | 0 |
| 7 th Street | 116,462 | 81,368 | 0 | 197,830 |
| Fulton Road | 99,100 | 47,950 | 0 | 147,050 |
| | <u>\$ 395,065</u> | <u>\$ 1,401,688</u> | <u>\$ 1,451,873</u> | <u>\$ 344,880</u> |

**CITY OF WINCHESTER, KENTUCKY
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2013**

NOTE 8 - CONSTRUCTION IN PROGRESS (CONTINUED)

COMPONENT UNIT (WMU)

Various construction projects in progress at June 30, 2013 are as follows:

| Balance June 30, 2012 | Additions | Placed in Service | Balance June 30, 2013 |
|--------------------------|---------------|----------------------|--------------------------|
| \$ 32,771,273 | \$ 20,707,549 | \$ (10,394,692) | \$ 43,084,130 |

NOTE 9 - LONG-TERM DEBT

CHANGES IN LONG-TERM DEBT

Governmental long-term liability activity was as follows:

| | Beginning Balance | Additions | Deletions | Ending Balance | Due Within One Year |
|--------------------|----------------------|-------------------|-------------------|---------------------|------------------------|
| Capital Leases | \$ 2,091,401 | \$ 204,784 | \$ 261,908 | \$ 2,034,277 | \$ 309,639 |
| Sick Leave | 618,511 | 0 | 11,853 | 606,658 | 0 |
| Total Governmental | <u>\$ 2,709,912</u> | <u>\$ 204,784</u> | <u>\$ 273,761</u> | <u>\$ 2,640,935</u> | <u>\$ 309,639</u> |

CAPITAL LEASES

The City has five capital leases as of June 30, 2013. The liability for the lease obligations have been recorded in the government-wide financial statements. Details of the leases are presented below.

| Purpose | Date | Interest Rate | Term | Annual Payment |
|-----------------------------|-----------|---------------|----------|-------------------|
| Horton Ambulance (EMS) | 2/26/2013 | 1.77% | 4 years | \$ 42,697 |
| Fire Truck (Fire) | 10/03/06 | 4.10% | 7 years | \$ 226,253 |
| Horton Ambulance | 06/03/10 | 3.29% | 5 years | \$ 201,942 |
| Pierce Pumper Fire Truck | 11/19/09 | 3.94% | 7 years | \$ 74,030 |
| Winchester Community Center | 05/21/10 | 3.48% | 20 years | \$ 152,277 |

Capital assets and related accumulated amortization under capital leases are as follows:

| Description | Amount |
|--------------------------------|---------------------|
| Safety Vehicles | \$ 1,268,552 |
| Building | 3,213,430 |
| Less: Accumulated Depreciation | <u>(1,156,841)</u> |
| Net Value | <u>\$ 3,325,141</u> |

CITY OF WINCHESTER, KENTUCKY
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2013

NOTE 9 - LONG-TERM DEBT (CONTINUED)

These leases qualify as capital leases for accounting purposes and, therefore, have been recorded at the present value of their future minimum lease payments as of the inception date. Capital leasing commitments to maturity for the year ending June 30, 2013:

| | | | |
|---|------------|----|-------------------------|
| | 2014 | \$ | 322,449 |
| | 2015 | | 293,531 |
| | 2016 | | 262,114 |
| | 2017 | | 204,758 |
| | 2018 | | 163,164 |
| | Thereafter | | <u>1,476,372</u> |
| Total Minimum Lease Payments | | | <u>2,722,388</u> |
| Less interest payments | | | <u>688,111</u> |
| Present Value of Minimum Lease Payments | | \$ | <u><u>2,034,277</u></u> |

NOTES PAYABLE—WMU

WMU issues revenue bonds to finance improvements and extensions to the water and sewer systems. The Winchester Municipal Utilities bonded indebtedness and other long-term notes at June 30, 2013 are summarized as follows:

| Description | Rate | Maturity | Original Issue | 2013 Total |
|--------------------------|------------|----------|----------------|----------------------|
| 2011 Issue | 5.27% | 01/01/31 | 9,010,000 | \$ 8,352,500 |
| 2012 Issue | 2.00-3.75% | | 7,495,000 | 7,115,000 |
| Less: Unamort. Discount | | | | <u>(186,077)</u> |
| Total Bonds | | | | <u>15,281,423</u> |
| KIA Loan | 1.00% | 12/01/28 | 21,000,000 | 16,637,036 |
| KIA-Lower Howards Creek | 2.00% | 01/01/31 | 36,600,000 | 35,600,004 |
| | | Estimate | | |
| KIA-Bel-Air | 2.00% | 01/01/31 | 1,000,000 | 478,140 |
| KIA-Ind. Storage tanks | 2.00% | 12/01/30 | 340,326 | 304,814 |
| KIA-Vaught Court | 2.00% | 06/01/31 | 287,400 | 251,233 |
| Total Kia Loans | | | | <u>53,271,227</u> |
| Less: Current Maturities | | | | <u>(3,175,612)</u> |
| Total | | | | <u>\$ 65,377,038</u> |

**CITY OF WINCHESTER, KENTUCKY
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2013**

NOTE 9 - LONG-TERM DEBT (CONTINUED)

The annual bond and long-term debt service requirements, as of June 30, 2013, are as follows:

| Fiscal Year | Principal | Interest | Total |
|-------------|---------------|---------------|---------------|
| 2014 | \$ 3,177,855 | \$ 1,514,000 | \$ 4,691,855 |
| 2015 | 3,237,304 | 1,455,176 | 4,692,480 |
| 2016 | 3,303,259 | 1,396,657 | 4,699,916 |
| 2017 | 3,362,062 | 1,336,807 | 4,698,869 |
| 2018 | 3,428,729 | 1,275,799 | 4,704,528 |
| 2019-2023 | 18,207,264 | 5,016,606 | 23,223,870 |
| 2024-2028 | 18,413,458 | 3,271,214 | 21,684,672 |
| 2029-2033 | 15,422,719 | 991,955 | 16,414,674 |
| | \$ 68,552,650 | \$ 16,258,214 | \$ 84,810,864 |

The above schedule includes estimated future payments towards the KIA-Lower Howards Creek and KIA-Bel-Air financing. At year end, the related projects were not completed, but are expected to be completed in the subsequent period, and KIA has provided WMU with estimated payment amounts.

Series 2002 Bonds

On March 1, 2002, the City issued \$9,025,000 of utilities revenue bonds for WMU secured by a first pledge of a fixed portion of the gross revenues to be derived from the operation of the system, which fixed portion shall be sufficient to pay the principal and interest of the bonds. The 2002 bond issue financed the acquisition, construction and installation of major new municipal sanitary sewer (wastewater) facilities and paying and discharging the outstanding Utilities Revenue Bond Anticipation Note, Series 1997. The bonds carry interest rates of 4.5% to 5.125% and mature on July 1, 2032. The interest payments are to be made on July 1 and January 1 and the principal payments are to be made on July 1. The bonds were paid in full during the 2011-2012 fiscal year by a refunding, Series 2012 Bonds issuance (See Refunding, Series 2012 Bonds below).

Series 2011 Bonds

On April 14, 2011, the City issued \$9,010,000 of utilities revenue bonds for WMU secured by a first and prior security interest in any and all right, title and interest of WMU in the portions of the Project (extensions and improvements of the System) that constitute personal property and in all additions, attachments, accessions, and substitutions thereto, and any proceeds therefrom. The 2011 bond issues financed the extensions and improvements to the combined and consolidated municipal waterworks, sanitary sewer and solid waste disposal system. The bonds carry an interest rate of 5.2656174% and mature on January 1, 2031. The interest and principal payments are to be made monthly.

CITY OF WINCHESTER, KENTUCKY
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2013

NOTE 9 - LONG-TERM DEBT (CONTINUED)

Refunding, Series 2012 Bonds

On April 19, 2012, the City issued \$7,495,000 of utilities refunding revenue bonds for WMU to pay off the Series 2002 Bonds (See Series 2002 Bonds above). The bonds were secured by a first pledge of a fixed portion of the gross revenues to be derived from the operation of the system, which fixed portion shall be sufficient to pay the principal and interest of the bonds. The 2002 bond issue financed the acquisition, construction and installation of major new municipal sanitary sewer (wastewater) facilities and paying and discharging the outstanding Utilities Revenue Bond Anticipation Note, Series 1997. The bonds carry interest rates of 2.0% to 3.75% and mature on July 1, 2021. The interest payments are to be made on July 1 and January 1 and the principal payments are to be made on July 1.

KIA Loan

On July 1, 2005, Winchester Municipal Utilities entered into an "Assistance Agreement" with the Kentucky Infrastructure Authority (KIA), to provide funds for the construction of a new wastewater treatment plant, \$21,000,000. This agreement calls for interest to be paid every six months starting December 1, 2005 at the rate of 1% of the outstanding balance. The amount of interest due will vary from due date to due date based upon the amount of funds drawn down to fund construction of the wastewater treatment plant. Principal payments are due to be paid every December 1 and June 1 starting after the wastewater treatment plant goes online. The online date for the plant was July, 2008, with principal payments due to begin on June 1, 2009, and be due every December 1 and June 1 thereafter until maturity on December 1, 2028.

KIA – Vaught Court Loan

On December 1, 2009, Winchester Municipal Utilities entered into an "Assistance Agreement" with the Kentucky Infrastructure Authority (KIA), to provide funds for construction of the Vaught Court Outfall Sewer Project, \$600,000 with a principal forgiveness of \$312,600 and a loan amount of \$287,400. This agreement calls for interest payments to commence within six months from the first draw of funds on June 1, 2010 with full principal and interest payments to commence within one year of initiation of operation on June 1, 2011. During the year ended June 30, 2010, \$312,600 of principal was forgiven and \$69,320 of the loan amount was drawn down. During the year ended June 30, 2011, \$218,080 was drawn down, and the project was completed. The loan carries a 2.00% interest rate, with principal and interest payments due on December 1 and June 1 every year until maturity on June 1, 2030. The loan is required to establish a replacement reserve account where \$1,500 is to be added to the account each December 1 until the balance reaches \$15,000 and is to be maintained for the life of the loan.

KIA – Lower Howards Creek

On February 5, 2010, Winchester Municipal Utilities entered into an "Assistance Agreement" with the Kentucky Infrastructure Authority (KIA), to provide funds for the Lower Howards Creek Sewershed project, \$36,600,000. This agreement calls for interest payments to commence within six months from the first draw of funds with full principal and interest payments to commence within one year of initiation of operation, which was on February 12, 2013. During the current year, \$8,893,350 of the loan was drawn down. Upon completion of the project, the loan will carry a 2.00% interest rate and mature in twenty years. The loan is required to establish a replacement reserve account where \$91,500 is to be added to the account each December 1 until the balance reaches \$915,000 and is to be maintained for the life of the loan.

**CITY OF WINCHESTER, KENTUCKY
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2013**

NOTE 9 - LONG-TERM DEBT (CONTINUED)

KIA – Industrial Elevated Storage Tank

On December 1, 2009, Winchester Municipal Utilities entered into an “Assistance Agreement” with the Kentucky Infrastructure Authority (KIA), to provide funds for construction of an Elevated Storage Tank Rehabilitation, \$741,450 with a principal forgiveness of \$401,124 and a loan amount of \$340,326. This agreement calls for interest payments to commence within six months from the first draw of funds on June 1, 2010 with full principal and interest payments to commence within one year of initiation of operation on June 1, 2011. During the year ended June 30, 2010, \$401,124 of principal was forgiven. During the year ended June 30, 2011, \$340,326 was drawn down, and the project was completed. The loan carries a 2.00% interest rate, with principal and interest payments due on December 1 and June 1 every year until maturity on December 1, 2030. The loan is required to establish a replacement reserve account where \$2,000 is to be added to the account each December 1 until the balance reaches \$20,000 and is to be maintained for the life of the loan.

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

KIA – Bel-Air Sanitary

On October 1, 2012, Winchester Municipal Utilities entered into an “Assistance Agreement” with the Kentucky Infrastructure Authority (KIA), to provide funds for the Bel-Air and Westside pump station projects, \$1,000,000. This agreement calls for interest payments to commence within six months from the first draw of funds with full principal and interest payments to commence within one year of initiation of operation estimated to be December 1, 2013. During the current year, \$478,140 of the loan was drawn down. Upon completion of the project, the loan will carry a 2.00% interest rate and mature in twenty years. The loan is required to establish a replacement reserve account where \$2,500 is to be added to the account each December 1 until the balance reaches \$25,000 and is to be maintained for the life of the loan.

Capital Lease

On September 30, 2011, the Utility entered into a new capital lease agreement with Oce’ Financial Services, Inc. for two new copiers in the amount of \$20,923. Payments are for \$648 for 36 months at an interest rate of 7.20%. The assets held under capital leases are included in equipment and total \$20,923 less accumulated depreciation of \$6,974 and \$2,790, as of June 30, 2013 and 2012, respectively.

The following reflects future minimum lease payments at June 30, 2013 as follows:

| | | | |
|---|--|----|--------------|
| 6/30/14 | | \$ | 7,272 |
| Less: Interest | | | (298) |
| Present Value of Minimum Lease Payments | | \$ | <u>6,974</u> |

Amortization of leased equipment under capital leases is included with depreciation expense.

**CITY OF WINCHESTER, KENTUCKY
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2013**

NOTE 9 - LONG-TERM DEBT (CONTINUED)

Long-Term Debt consists of bonds and other indebtedness for which the changes in the years ended June 30, 2013 are as follows:

| Description | Beginning | Borrowings Additions | Repayments Reductions | 2013 Ending | Current |
|-----------------------------|----------------------|-------------------------|--------------------------|----------------------|---------------------|
| Compensated Absences | \$ 401,302 | \$ 46,173 | \$ 52,399 | \$ 395,076 | \$ 0 |
| Bonds | 15,871,401 | 0 | 589,978 | 15,281,423 | 605,751 |
| KIA Loan | 17,817,272 | 0 | 1,180,235 | 16,637,037 | 997,483 |
| Capital Lease | 13,950 | 0 | 6,976 | 6,974 | 6,974 |
| KIA – Lower Howards | 26,706,654 | 8,893,350 | 0 | 35,600,004 | 1,504,837 |
| KIA – Bel-Air | 0 | 478,140 | 0 | 478,140 | 40,290 |
| KIA – Storage Tank | 319,231 | 0 | 14,416 | 304,815 | 14,707 |
| KIA – Vaught Court | 263,529 | 0 | 12,296 | 251,233 | 12,544 |
| Total Long-Term Debt | \$ 61,393,339 | \$ 9,417,663 | \$ 1,856,300 | \$ 68,954,700 | \$ 3,182,586 |

NOTE 10 – COMPLIANCE WITH BOND ORDINANCE COMPONENT UNIT (WMU)

The bonds and KIA loans require WMU to establish and maintain certain reserves and restricted assets as follows:

Bond Debt Service - Bonds

Monthly deposits equal to one-sixth of the next interest payment and one-twelfth of the next principal payment shall be set aside monthly so as to accumulate in the Bond Fund in order to pay interest and principal on the bonds. In addition, the Bond Ordinance requires that a specific amount be maintained in the Debt Service Reserve Account defined as the "Reserve Amount." The account is to be reviewed each year and funded based on the least of three factors: 1) maximum annual principal and interest requirement, 2) 125% of the average annual principal and interest requirement or 3) 10% of the outstanding loan proceeds. The first factor was applicable for June 30, 2013 and 2012, and required a balance of \$507,944.

Depreciation Reserve – Bonds and KIA Loan

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

Interest Coverage Ratio – Bonds and KIA Loan

On April 3, 2012, a new general bond ordinance was adopted that requires Winchester Municipal Utilities to maintain an interest coverage ratio of 1.2 times - annual debt service requirements for bonds and 1.0 times - annual debt service requirements for bonds and KIA loans. Other changes in coverage ratio are noted below in calculation of ratios as shown. The City of Winchester is required by bond ordinance to adjust rates as necessary to maintain such minimum coverage. Computed as follows:

**CITY OF WINCHESTER, KENTUCKY
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2013**

**NOTE 10 – COMPLIANCE WITH BOND ORDINANCE COMPONENT UNIT (WMU)
(CONTINUED)**

Interest Coverage Ratio – Bonds and KIA Loan (CONTINUED)

| | |
|--------------------------------------|--------------|
| Bonds: | 2013 |
| Income Available for Debt Service | \$ 4,178,586 |
| Add: Depreciation | 3,386,759 |
| Cash Available for Bond Debt Service | \$ 7,565,345 |
| Annual Debt Service on Bonds | 1,210,429 |
| Coverage Ratio | 6.25 |

| | |
|-----------------------------------|--------------|
| KIA: | 2013 |
| Income Available for Debt Service | \$ 4,178,586 |
| Add: Depreciation | 3,386,759 |
| Cash Available for Debt Service | \$ 7,565,345 |
| Annual Debt Service on all Debt | 2,604,128 |
| Coverage Ratio | 2.91 |

Winchester Municipal Utilities is in compliance with all of the covenants of the bond ordinance and KIA loan agreements as of June 30, 2013.

**NOTE 11 – FIVE-YEAR CAPITAL CONSTRUCTION PLAN – COMPONENT UNIT
(WMU)**

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

| | |
|---------------------------------------|----------------------|
| Water Utility Improvements | \$ 60,672,000 |
| Wastewater Utility Improvements | 22,616,000 |
| Total projected financing requirement | \$ <u>83,288,000</u> |

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

**CITY OF WINCHESTER, KENTUCKY
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2013**

NOTE 11 – FIVE-YEAR CAPITAL CONSTRUCTION PLAN – COMPONENT UNIT (WMU) (CONTINUED)

| | |
|--|---------------------|
| Finance and Administration: | |
| Copiers | \$ 8,000 |
| Upgrade/Renew Network Virus Protection | 1,600 |
| Upgrade Local Area Network | 8,000 |
| Replace Microcomputers | 8,000 |
| Engineering Software Upgrades | 2,500 |
| Field Operation Vehicles | 385,000 |
| Solid Waste Collection: | |
| Cubit Replacement | 30,000 |
| Container Replacement | 35,000 |
| Replace Compactor Ejector Box | 10,000 |
| Solid Waste Recycling | 100,000 |
| Water Treatment Plant Equipment Improvements | 233,000 |
| Water System Improvements | 710,000 |
| Water Distribution: | |
| Main Replacement | 125,000 |
| Fire Hydrant Replacement | 10,000 |
| Gate Value Box Adjustment – New Paving | 5,000 |
| Gate Value Replacement | 10,000 |
| Elevated Storage Tank Rehabilitation | 400,000 |
| Meter Change-Out/AMR Equipment | 125,000 |
| New Meter Services | 40,000 |
| Wastewater Collection: | |
| Main Replacement Program | 125,000 |
| Manhole Grade Adjustment – New Paving | 10,000 |
| I&I Rehabilitation | 25,000 |
| Rehabilitation of Private Sewers | 20,000 |
| Flow Meters | 35,000 |
| Infrastructure Rehabilitation Program | 25,000 |
| System Capacity Assurance Program | 18,000 |
| Routine Hydraulic Cleaning | 60,000 |
| Wastewater Treatment Plant: | |
| Replacement of Laboratory Equipment | 2,000 |
| WWTP Equipment Improvements | 100,000 |
| Solids Processing Improvements | 304,000 |
| Total Annual Allocations for Infrastructure Investment | <u>\$ 2,970,100</u> |

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

NOTE 12 – UTILITY REVENUES PLEDGED – COMPONENT UNIT (WMU)

WMU has pledged future revenues from water, wastewater and solid waste to repay the 2011 and 2012 bonds and KIA outstanding debt referenced in Note 9. Proceeds from these debt obligations provided financing of the water and wastewater infrastructure, including a new wastewater treatment plant. The debt obligations will be repaid from the previously mentioned utility revenues through the year 2032.

**CITY OF WINCHESTER, KENTUCKY
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2013**

NOTE 13 – PENSION PLANS

The City participates in two separate defined benefit plans for full-time employees. The Police and Firefighter's Pension Fund is a single-employer plan and is presented in the financial statements as the Pension Trust Fund. The other pension plan is a multiple-employer cost-sharing plan maintained by the Kentucky Retirement Systems in the County Employees Retirement System (CERS).

A – POLICEMEN'S AND FIREMEN'S PENSION FUND

Plan Description. The City of Winchester Police and Firefighter's Pension Plan is a single-Employer defined benefit pension plan administered by the City of Winchester Police and Firefighter's Pension Board. The Plan provides retirement, disability, and death benefits to plan members and beneficiaries. It was established pursuant to KRS Sections 95.520 to 95.620. The Plan covered substantially all employees of the City's police and fire departments prior to August 1, 1988. On July 26, 1988, the City adopted Ordinance 18-88, which phased out the Police and Firefighter's Pension Plan by restricting future participation to those existing employees electing to remain in the plan who were active as of August 1, 1988, and to employees who were already drawing retirement or disability payments as of August 1, 1988.

On February 16, 1989, the City was accepted into the County Employees' Retirement System of the Commonwealth of Kentucky which was enacted by House Bill 398 during the 1988 General Assembly. This acceptance was retroactive to an effective date of August 1, 1988. The Police and Firefighter's Pension Plan's actuarial valuation was performed on July 1, 2013, and the report issued by the firm of Bryan, Pendleton, Swats & McAllister, LLC. A copy of the report may be obtained from the City of Winchester Police and Firefighter's Pension Board.

Annual Pension Cost and Net Pension Obligation. The City's annual pension cost and net pension obligation to the Police and Firefighter's Pension Fund for the following years were:

| | <u>6/30/2013</u> | <u>6/30/2012</u> | <u>6/30/2011</u> |
|---|-------------------|-------------------|-------------------|
| Annual required contribution | \$ 122,559 | \$ 105,609 | \$ 114,664 |
| Interest on net pension obligation | 22,029 | 20,754 | 18,645 |
| Adjustment to annual required contribution | <u>(101,761)</u> | <u>(95,873)</u> | <u>(86,131)</u> |
| Annual Pension Cost | <u>42,827</u> | <u>30,490</u> | <u>47,178</u> |
| | | | |
| Contributions Made | <u>(5,000)</u> | <u>(5,000)</u> | <u>(5,000)</u> |
| Increase (decrease) in net pension obligation | <u>37,827</u> | <u>25,490</u> | <u>42,178</u> |
| | | | |
| Net pension obligation beginning of year | <u>440,572</u> | <u>415,082</u> | <u>372,904</u> |
| Net pension obligation end of year | <u>\$ 478,399</u> | <u>\$ 440,572</u> | <u>\$ 415,082</u> |

As of June 30, 2013, the total actuarial unfunded liability was \$660,135 if retirees are granted a 3% annual cost of living adjustment. If this COLA is not implemented, assets available for benefits (\$1,568,940) exceed the actuarial liability (\$1,550,761) by \$18,179.

**CITY OF WINCHESTER, KENTUCKY
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2013**

NOTE 13 – PENSION PLANS (CONTINUED)

A – POLICEMEN’S AND FIREMEN’S PENSION FUND (CONTINUED)

Normal retirement period applied to employees who had completed 20 years of service and obtained the age of 55. The benefit was 50% of monthly salary at time of retirement. The plan does have provisions for disability and death benefits. The annual required contribution for the current year was determined as part of the July 1, 2013 actuarial valuation using the entry age normal cost funding method. The actuarial assumptions included (a) 5% per annum assumed rate of return and (b) projected salary increases of 3% per year. Both (a) and (b) included future cost of living increases at a maximum of 3%. The actuarial value of assets was determined at the market value as reported by PNC Bank, Kentucky, Inc. plus a checking account balance.

Starting with the year 2001, the unfunded actuarial accrued liabilities are assumed to be amortized by 2012 (closed basis), but with any unfunded actuarial accrued liability after 2007 being amortized over five years (open basis). As of June 30, 2013, the plan’s funded ratio was 70.4% (actuarial value of assets compared to actuarial accrued liability).

Membership Data.

| | |
|---|---|
| Inactive Plan Participants- | |
| Retirees and beneficiaries currently receiving benefits | 8 |
| Active Plan Participants-Nonvested | 0 |

B - COUNTY EMPLOYEES RETIREMENT SYSTEM

Plan Description. The City of Winchester contributes to the County Employees Retirement System (CERS), a cost-sharing multiple-employer defined benefit pension plan administered by Kentucky Retirement Systems. CERS was established in 1958 under Kentucky Revised Statutes 78.510 to 78.852. The Plan provides retirement, disability, and death benefits to plan members and beneficiaries with annual cost-of-living adjustments. The retirement benefits are guaranteed by state law and cannot be reduced. By contributing to the retirement systems, the employee is assured a percentage of average salary for each year he is employed. The employee’s contributions are currently tax-deferred. The Kentucky Retirement Systems issues a publicly available financial report that includes financial statements and required supplementary information for CERS. That report may be obtained by writing to Kentucky Retirement Systems, Perimeter Park West, 1260 Louisville Road, Frankfort, KY 40601. The valuation date is as of June 30, 2013.

Funding Policy. Plan members are required to contribute 5%, or 6% if hire date was after September 1, 2008, of their gross salary to the system; however, if they are covered under hazardous coverage, it is 8%, or 9% if hire date was after September 1, 2008. The City is required to contribute at an actuarially determined rate. For fiscal year 2012, the KRS Board of Trustees established contribution rates of 19.55% of gross pay for regular employees and 37.6% of gross pay for hazardous employees. The contribution requirements of plan members and the City of Winchester are established and may be amended by the CERS Board of Trustees. Employer contributions for the years ended June 30, 2013, 2012 and 2011, under the current plan amounted to \$2,038,353, \$1,864,646 and \$1,725,644, respectively.

**CITY OF WINCHESTER, KENTUCKY
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2013**

NOTE 13 – PENSION PLANS (CONTINUED)

B - COUNTY EMPLOYEES RETIREMENT SYSTEM (CONTINUED)

Kentucky Retirement Systems Insurance Fund. Employee and employer contribution rates outlined above include an amount designated to fund health insurance benefits for retirees. The allocation of insurance premiums paid by this Fund and amounts withheld from members' benefits is based on years of service with the Systems.

The KRS Board is required by KRS 61.565(6) to establish the employer contribution rates for CERS that will phase in to the full actuarially required contribution for the health insurance fund over a ten (10) year period using the 2007 - 2008 fiscal year contribution rates as the base rates.

Legislative Revisions in 2009. In August 2008, the Kentucky General Assembly revised the benefit provisions, employer contribution rates, and provisions for retirees returning to service with employers participating in any of the Kentucky Retirement System pension plans. These revisions will be effective for employees hired after September 1, 2008. Kentucky Retirement Systems has developed the revised plan description documents to outline these changes. More information is available on the KRS website at <http://www.kyret.com/>.

C - PENSION PLAN - WMU

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

Retirement benefits are provided for through legislative action of the Kentucky General Assembly and are funded by employee contributions which are deducted from employees' wages and by employer paid contributions. The General Assembly sets the employee contribution rates, currently 5% or 6% for fiscal year ending 2013 and 2012, and the Retirement Systems' Board of Trustees sets the employer contribution rates, currently 19.55% and 18.96% for fiscal year ending 2013 and 2012, respectively. Each employer is notified prior to each fiscal year of any change in the contribution rates. The Retirement System's administrative expenses are subject to approval by the Kentucky General Assembly and are paid from the State's Retirement Allowance Account.

Employer contributions for the years ended June 30, 2013, 2012 and 2011, under the current plan amounted to \$500,979, \$505,126 and \$432,605, respectively, which represents 100% of the required contributions.

**CITY OF WINCHESTER, KENTUCKY
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2013**

NOTE 13 – PENSION PLANS (CONTINUED)

C - PENSION PLAN – WMU (CONTINUED)

In a prior year, the WMU Commission agreed to pay \$381,296 in prior service costs. This cost will be expensed equally over 19 years, based upon the average remaining service lives of all involved employees. Prior service costs expensed amounted to \$21,934 and \$21,934 for the years ended June 30, 2013 and 2012, respectively.

WMU offers employees the option to participate in a defined contribution plan under Section 403(B) and 401(K) of the Internal Revenue Code. All regular full time and part time employees are eligible to participate and may contribute up to the maximum amount allowable by law.

Also, WMU offers its employees a deferred compensation plan created in accordance with Internal Revenue Code Section 457. The plan, available to all employees, permits them to defer a portion of their salary until future years. This deferred compensation is not available to employees until their termination, retirement, death or unforeseeable emergency.

GASB Statement No. 32, Accounting and Financial Reporting for Internal Revenue Code Section 457 Deferred Compensation Plans, allows entities with little or no administrative involvement and who do not perform the investing function for these plans to omit plan assets and related liabilities from their financial statements. WMU, therefore, does not report these assets and liabilities on its financial statements.

Employee contributions made to the 401k and 457 plans as of June 30, 2013 and 2012 were \$44,771 and \$47,650, respectively. WMU does not contribute to these plans.

NOTE 14 – CONTINGENCIES

A – INDUSTRIAL DEVELOPMENT BONDS

The City has the following Industrial building Revenue Bonds outstanding at year end:

| | Origination Date | Maturity Date | Outstanding Balance |
|-------------------------------------|------------------|-----------------|---------------------|
| Industrial Facility-Leggett & Platt | October 20, 1988 | October 1, 2018 | \$ 2,400,000 |

B – LITIGATION

City of Winchester, KY v. Kentucky Labor Cabinet – the City is asking the Franklin Circuit Court for a declaration of rights that the City is not responsible for the payment of the firefighter's back pay. The Supreme Court of Kentucky has ruled against all of the City plaintiffs who brought the suit and the City of Winchester is currently set for trial. It is anticipated that this matter will be settled during the upcoming fiscal year.

In regards to the above, the City has accrued a payroll liability for the firefighter's overtime on state provided incentive pay in the amount of \$741,474 as of June 30, 2013. It is recorded in the government-wide financial statements as part of accrued payroll and related liabilities.

**CITY OF WINCHESTER, KENTUCKY
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2013**

NOTE 15 – LANDFILL POST-CLOSURE COSTS - COMPONENT UNIT (WMU)

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

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

The Division of Waste Management has finished construction of a new wetlands treatment system for treating the landfill leachate at the WMU and Clark County Landfills. With construction of this treatment facility a new Kentucky Pollution Discharge Elimination System (KPDES) Permit was required. Laboratory testing/Monitoring required as part of the conditions of this permit were unexpectedly more stringent than the previous permit resulting in a higher monthly cost for operation.

NOTE 16 –ECONOMIC DEPENDENCY-COMPONENT UNIT (WMU)

The following four entities provide a significant portion of the revenues for WMU:

| Name | Amount |
|----------------------|--------------|
| Sekisui | \$ 744,656 |
| Alltech | 504,423 |
| The Kroger Company | 559,965 |
| East Clark County WD | 318,513 |
| Total | \$ 2,127,557 |

NOTE 17 –COMMITMENTS- COMPONENT UNIT (WMU)

As of June 30, 2013, WMU had several uncompleted construction contracts. The remaining commitment on these construction contracts was approximately \$2,418,023 financed with KIA loans.

**CITY OF WINCHESTER, KENTUCKY
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2013**

NOTE 18 – RISK MANAGEMENT

The City and its component unit (WMU) are exposed to various risks of loss related to torts; theft of, damage to and destruction of assets; errors and omissions; injuries to employees and natural disasters. The City carries commercial insurance for the risks of loss, including worker's compensation, and property and casualty loss insurance.

CITY – SELF-INSURANCE

In 2009, the City initiated a self-insured health insurance plan to provide employees with traditional healthcare insurance that covers hospitalization and major medical expenses with specific limits.

The plan is administered by a third-party administrator. The City pays the administrator a monthly fixed fee for various claim administration services, plus premiums for excess coverage insurance to cover claims that exceed \$35,000 per participant. Monthly payments also include a specified amount to set aside funds for the payment of claims that do not exceed the \$35,000 amount. The third party administrator pays these claims from the funds set aside by the City and bills the City for additional funds if the amounts in the healthcare checking accounts are not sufficient to pay claims. Amounts held in the healthcare checking accounts are also reported as *assigned* fund balance in the General Fund.

| <u>Fiscal Year Ended June 30,</u> | <u>Claims Payable July 1,</u> | <u>Claims and Changes in Estimates</u> | <u>Claims Paid</u> | <u>Claims Payable June 30,</u> |
|---------------------------------------|---------------------------------------|--|------------------------|--|
| 2012 | \$ 221,300 | \$ 1,093,578 | \$ 1,216,878 | \$ 98,000 |
| 2013 | \$ 98,000 | \$ 1,102,777 | \$ 1,310,388 | \$ 109,611 |

NOTE 19 – FUND BALANCE CLASSIFICATION POLICIES AND PROCEDURES

In accordance with the guidance in GASB Statement 54, the City has classified ending fund balance based on the availability of funds for expenditure on programs and services. Restricted fund balance reflects funds that are limited to projects funded by federal, state, or local grants (\$12,743) and shared revenues (\$756,797) from the Commonwealth of Kentucky. Committed fund balance includes amounts set aside by the City Commission for special projects (\$400,926) and capital acquisitions (\$2,023,680). The City Commission is the highest level of decision-making authority of the City. Assigned fund balance includes balances (\$406,280) held by a third-party administrator to pay future employee health care claims. Under the City's adopted policy, only the City Commission may assign amounts for specific purposes.

NOTE 20 – LOCAL GOVERNMENT ECONOMIC ASSISTANCE FUNDS

The City received \$23,546 in LGEA Funds during the current fiscal year. The City is in a non-coal producing county and is required to expend these funds in accordance with KRS 42.470, which limits the expenditures to public transportation, including mass transit systems, streets and roads. During fiscal year 2013, the City spent \$28,500.

CITY OF WINCHESTER, KENTUCKY
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2013

NOTE 21 – RELATED ORGANIZATIONS

The City participates with the County to provide a variety of services with joint funding from both organizations. All entities operate independently with separate management personnel. In most cases, the city and county contribute equal funding for operations. The following table outlines these organizations and the City's contribution during fiscal year 2013.

| | |
|--|-------------------|
| Winchester/Clark County Planning & Zoning | \$ 7,000 |
| Winchester/Clark County Parks & Recreation | 254,300 |
| Clark County/Winchester Heritage Commission | 12,000 |
| Winchester/Clark County Recreation | 55,000 |
| Winchester/Clark County Industrial Development Authority | 110,500 |
| Winchester/Clark County Board of Adjustment | 1,500 |
| Clark County GIS | 79,111 |
| Total Contributions | <u>\$ 519,411</u> |

NOTE 22 – SUBSEQUENT EVENTS

The City has evaluated all subsequent events through February 10, 2014, the date the financial statements were available to be issued.

REQUIRED SUPPLEMENTARY INFORMATION

**CITY OF WINCHESTER, KENTUCKY
POLICE AND FIREFIGHTERS PENSION FUND
REQUIRED SUPPLEMENTARY INFORMATION
FOR THE YEAR ENDED JUNE 30, 2013**

Primary Government - City of Winchester, Kentucky Police & Firefighters Pension Fund

1. SCHEDULES OF FUNDING PROGRESS

| Actuarial Valuation Date | Actuarial Value of Assets (a) | Actuarial Accrued Liability (AAL) - Entry Age (b) | Unfunded Actuarial Accrued Liability (UAAL) (b-a) | Funded Ratio (a/b) | Covered Payroll (c) | UAAL as a Percentage of Covered Payroll (b-a)/(c) |
|--------------------------------|--|--|--|--------------------------|---------------------------|--|
| 7/1/1993 | \$ 1,913,034 | \$ 3,970,903 | \$ 2,057,869 | 48.2 % | \$ 81,842 | 2,514.4 % |
| 7/1/1994 | 1,882,229 | 3,733,210 | 1,850,981 | 50.4 | 63,961 | 2,893.9 |
| 7/1/1995 | 1,941,892 | 3,721,659 | 1,779,767 | 52.2 | 67,225 | 2,647.5 |
| 7/1/1996 | 1,970,044 | 3,594,044 | 1,624,000 | 54.8 | 72,020 | 2,254.9 |
| 7/1/1997 | 2,024,274 | 3,210,316 | 1,186,042 | 63.1 | 76,100 | 1,558.5 |
| 7/1/1998 | 2,079,719 | 2,661,949 | 582,230 | 78.1 | 80,110 | 726.8 |
| 7/1/1999 | 2,048,729 | 2,631,557 | 582,828 | 77.9 | 84,169 | 692.4 |
| 7/1/2000 | 2,063,927 | 2,823,325 | 759,398 | 73.1 | 88,438 | 858.7 |
| 7/1/2001 | 2,158,847 | 2,832,626 | 673,779 | 76.2 | 91,533 | 736.1 |
| 7/1/2002 | 2,216,339 | 3,503,625 | 1,287,286 | 63.3 | 98,583 | 1,305.8 |
| 7/1/2003 | 2,171,382 | 2,478,417 | 307,035 | 87.6 | | N/A |
| 7/1/2004 | 2,081,329 | 2,414,957 | 333,628 | 86.2 | | N/A |
| 7/1/2005 | 2,018,329 | 2,431,405 | 413,166 | 83.0 | | N/A |
| 7/1/2006 | 1,923,066 | 2,419,380 | 496,314 | 79.5 | | N/A |
| 7/1/2007 | 1,893,689 | 2,352,971 | 459,282 | 80.5 | | N/A |
| 7/1/2008 | 1,893,689 | 2,352,971 | 459,282 | 80.5 | | N/A |
| 7/1/2009 | 1,807,674 | 2,307,890 | 500,216 | 78.3 | | N/A |
| 7/1/2010 | 1,782,234 | 2,303,493 | 521,259 | 77.4 | | N/A |
| 7/1/2011 | 1,717,389 | 2,197,484 | 480,095 | 78.2 | | N/A |
| 7/1/2012 | 1,689,894 | 2,247,041 | 557,147 | 75.2 | | N/A |
| 7/1/2013 | 1,568,940 | 2,229,075 | 660,135 | 70.4 | | N/A |

2. SCHEDULE OF EMPLOYER CONTRIBUTIONS

| Fiscal Year End | Annual Required Contribution | Amount Contributed | Percentage Contributed |
|--------------------|------------------------------------|-----------------------|---------------------------|
| 1988 | \$ 174,698 | \$ 5,000 | 2.9% |
| 1989 | 43,829 | 800 | 1.8% |
| 1990 | 51,582 | 1,000 | 1.9% |
| 1991 | 72,574 | 72,500 | 99.9% |
| 1992 | 165,693 | 165,693 | 100.0% |
| 1993 | 144,128 | 160,000 | 111.0% |
| 1994 | 175,093 | 150,000 | 85.7% |
| 1995 | 152,600 | 140,000 | 91.7% |
| 1996 | 148,997 | 141,363 | 94.9% |
| 1997 | 147,374 | 155,000 | 105.2% |
| 1998 | 106,823 | 155,000 | 145.1% |
| 1999 | 64,471 | 105,000 | 162.9% |
| 2000 | 65,687 | 105,000 | 159.8% |
| 2001 | 112,413 | 135,000 | 120.1% |
| 2002 | 108,221 | 132,500 | 122.4% |
| 2003 | 195,216 | 36,000 | 18.4% |
| 2004 | 41,140 | 35,000 | 85.1% |
| 2005 | 49,161 | 18,000 | 36.6% |
| 2006 | 68,003 | 5,000 | 7.4% |
| 2007 | 93,126 | 5,000 | 5.4% |
| 2008 | 101,031 | 10,000 | 9.9% |
| 2009 | 109,390 | 5,000 | 4.6% |
| 2010 | 110,036 | 5,000 | 4.5% |
| 2011 | 114,664 | 5,000 | 4.4% |
| 2012 | 105,609 | 5,000 | 4.7% |
| 2013 | 122,559 | 5,000 | 4.1% |

3. NOTES TO REQUIRED SUPPLEMENTARY INFORMATION

| | |
|----------------------------------|--|
| Valuation Date | 7/1/2013 |
| Actuarial Cost Method | Entry age |
| Amortization Method | Level percentage of payroll |
| Amortization Period | 2012, closed |
| Actuarial Asset Valuation Method | Market Value as reported by PNC Bank, Kentucky, Inc., with adjustments as reported by City Treasurer |
| Actuarial Assumptions: | |
| Investment rate of return | 5% |
| Inflation | 3% |
| Other | RP-2000 Mortality Table (Static) |

OTHER SUPPLEMENTARY INFORMATION

CITY OF WINCHESTER, KENTUCKY
 COMBINING BALANCE SHEET
 NONMAJOR GOVERNMENTAL FUNDS
 JUNE 30, 2013

| | MUNICIPAL AID FUND | LOCAL GOVERNMENT ECONOMIC ASSISTANCE FUND | ROOM TAX FUND | ADMINISTRATION SPECIAL PROJECTS FUND | MAIN STREET FUND | POLICE SPECIAL PROJECTS FUND | POLICE FEDERAL FORFEITURE FUND | FIRE SPECIAL PROJECTS FUND | STATE ASAP FUNDS | STATE GRANT FUNDS | TOTAL NONMAJOR GOVERNMENTAL FUNDS |
|--|--------------------------|--|---------------------|---|---------------------|---------------------------------------|---|-------------------------------------|------------------------|-------------------------|--|
| ASSETS: | | | | | | | | | | | |
| Cash and Cash Equivalents | \$ 710,343 | \$ 50,712 | \$ 2 | \$ 39,984 | \$ 70,468 | \$ 69,038 | \$ 172,318 | \$ 18,609 | \$ 31,409 | \$ 12,743 | \$ 1,175,624 |
| Accounts Receivable | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Due from Other Funds | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| TOTAL ASSETS | \$ 710,343 | \$ 50,712 | \$ 2 | \$ 39,984 | \$ 70,468 | \$ 69,038 | \$ 172,318 | \$ 18,609 | \$ 31,409 | \$ 12,743 | \$ 1,175,624 |
| LIABILITIES: | | | | | | | | | | | |
| Accounts Payable | \$ 4,258 | \$ 0 | \$ 0 | \$ 32 | \$ 229 | \$ 0 | \$ 0 | \$ 0 | \$ 637 | \$ 0 | \$ 5,156 |
| Deferred Grant Revenue | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Due to Other Funds | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| TOTAL LIABILITIES | 4,258 | 0 | 0 | 32 | 229 | 0 | 0 | 0 | 637 | 0 | 5,156 |
| FUND BALANCES: | | | | | | | | | | | |
| Restricted Fund Balance | 706,085 | 50,712 | 2 | 0 | 0 | 0 | 0 | 0 | 0 | 12,743 | 769,542 |
| Committed Fund Balance | 0 | 0 | 0 | 39,952 | 70,238 | 69,038 | 172,318 | 18,609 | 30,771 | 0 | 400,926 |
| TOTAL FUND BALANCES | 706,085 | 50,712 | 2 | 39,952 | 70,238 | 69,038 | 172,318 | 18,609 | 30,771 | 12,743 | 1,170,468 |
| TOTAL LIABILITIES AND FUND BALANCES | \$ 710,343 | \$ 50,712 | \$ 2 | \$ 39,984 | \$ 70,468 | \$ 69,038 | \$ 172,318 | \$ 18,609 | \$ 31,409 | \$ 12,743 | \$ 1,175,624 |

CITY OF WINCHESTER, KENTUCKY
 COMBINING STATEMENT OF REVENUES, EXPENDITURES
 AND CHANGES IN FUND BALANCES
 NONMAJOR GOVERNMENTAL FUNDS
 FOR THE YEAR ENDED JUNE 30, 2013

| | MUNICIPAL AID FUND | LOCAL GOVERNMENT ECONOMIC ASSISTANCE FUND | ROOM TAX FUND | ADMINISTRATION SPECIAL PROJECTS FUND | MAIN STREET FUND | POLICE SPECIAL PROJECTS FUND | POLICE FEDERAL FORFEITURE FUND | FIRE SPECIAL PROJECTS FUND | STATE ASAP FUND | STATE GRANT FUNDS | TOTAL NONMAJOR GOVERNMENTAL FUNDS |
|--|-----------------------|--|---------------------|---|---------------------|---------------------------------------|---|-------------------------------------|-----------------------|-------------------------|--|
| REVENUES: | | | | | | | | | | | |
| Taxes | \$ 0 | \$ 0 | \$ 117,236 | \$ (7) | \$ 0 | \$ 0 | \$ 0 | \$ 0 | \$ 0 | \$ 0 | \$ 117,229 |
| Intergovernmental | 548,572 | 23,546 | 0 | 5,200 | 0 | 17,410 | 145,063 | 0 | 13,900 | 0 | 753,691 |
| Investment Income | 4,863 | 407 | 77 | 320 | 476 | 473 | 766 | 112 | 208 | 95 | 7,798 |
| Other | 0 | 0 | 1,344 | 2,600 | 42,728 | 9,032 | | 12,451 | 980 | 0 | 69,136 |
| TOTAL REVENUES | 553,436 | 23,952 | 118,658 | 8,113 | 43,205 | 26,915 | 145,829 | 12,564 | 15,088 | 95 | 947,854 |
| EXPENDITURES: | | | | | | | | | | | |
| Main Street Department | 0 | 0 | 0 | 1,175 | 41,446 | 0 | 0 | 0 | 0 | 0 | 42,621 |
| Planning | 0 | 0 | 0 | 5,542 | 0 | 0 | 0 | 0 | 0 | 0 | 5,542 |
| Police Department | 0 | 0 | 0 | 0 | 0 | 15,363 | 41,346 | 0 | 11,693 | 0 | 68,402 |
| Fire Department | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 4,859 | 0 | 0 | 4,859 |
| Public Works | 412,591 | 28,500 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 441,091 |
| Intergovernmental | 0 | 0 | 118,658 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 118,658 |
| Capital | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| TOTAL EXPENDITURES | 412,591 | 28,500 | 118,658 | 6,717 | 41,446 | 15,363 | 41,346 | 4,859 | 11,693 | 0 | 681,172 |
| Excess (Deficit) of Revenues over Expenditures | 140,845 | (4,548) | 0 | 1,396 | 1,759 | 11,552 | 104,484 | 7,705 | 3,395 | 95 | 266,682 |
| Fund Balance June 30, 2012 | 565,241 | 55,259 | 2 | 38,556 | 68,480 | 57,486 | 67,834 | 10,905 | 27,376 | 12,647 | 903,786 |
| Fund Balance June 30, 2013 | \$ 706,085 | \$ 50,712 | \$ 2 | \$ 39,952 | \$ 70,238 | \$ 69,038 | \$ 172,318 | \$ 18,609 | \$ 30,771 | \$ 12,743 | \$ 1,170,468 |

**CITY OF WINCHESTER, KENTUCKY
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED JUNE 30, 2013**

| <u>Federal Grantor/Pass-Through Grantor/ Program Title</u> | <u>Federal CFDA Number</u> | <u>Grant Number</u> | <u>Federal Expenditures</u> |
|---|------------------------------------|---------------------------------------|---------------------------------|
| HOUSING & URBAN DEVELOPMENT | | | |
| Passed Through Commonwealth of Kentucky: Community Development Block Grant | 14.228 | 09-066 | \$ 41,378 |
| TOTAL HOUSING & URBAN DEVELOPMENT | | | 41,378 |
| U.S. DEPT. OF TRANSPORTATION | | | |
| Passed Through Commonwealth of Kentucky : Depot Street | 20.205 | PO2-628-1000004390 | 853,340 |
| TOTAL U.S. DEPT. OF TRANSPORTATION | | | 853,340 |
| U.S. DEPT. OF JUSTICE | | | |
| Federal Forfeiture | 16.922 | | 41,346 |
| Bulletproof Vest | 16.800 | | 1,238 |
| TOTAL U.S. DEPT. OF JUSTICE | | | 42,583 |
| EPA | | | |
| Passed Through Commonwealth of Kentucky: | | | |
| Pollution Control | 66.460 | C9994861-04 | 64,950 |
| Wastewater Revolving Loan Program | 66.458 | A10-03 | 7,044,958 |
| Wastewater Revolving Loan Program | 66.458 | A 12-05 | 135,768 |
| TOTAL EPA | | | 7,245,676 |
| HOMELAND SECURITY | | | |
| Assistance to Firefighters Grant | 97.044 | EMW-2009-FO-09285 | 2,803 |
| Assistance to Firefighters Grant | 97.044 | EMW-2012-FO-04731 | 39,904 |
| Passed Through Commonwealth of Kentucky: | | | |
| Homeland Security Grant | 97.067 | #P02-094-1200003006-1 Project #11-260 | 1,500 |
| Homeland Security Grant | 97.067 | #P02-094-1300003022-1 Project #12-117 | 23,000 |
| TOTAL HOMELAND SECURITY | | | 67,207 |
| TOTAL FEDERAL FINANCIAL ASSISTANCE | | | \$ 8,250,184 |

CITY OF WINCHESTER, KENTUCKY
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
For the Year Ended June 30, 2013

NOTE A – BASIS OF PRESENTATION

This schedule of expenditures of federal awards includes the federal grant activity of the City of Winchester, Kentucky and is presented on the modified 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

Of the federal expenditures presented in the Schedule, the City of Winchester provided awards to subrecipients as follows:

| | |
|---|-------------|
| #66.458 Capitalization Grants for Clean Water Revolving | \$7,180,726 |
|---|-------------|

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

MEMBERS:

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OF CERTIFIED PUBLIC ACCOUNTANTS

KENTUCKY SOCIETY
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PRIVATE COMPANIES
PRACTICE SECTION OF THE AMERICAN INSTITUTE
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DEBORAH L. MAYNARD, CPA
RYAN R. LASKI, CPA

LAURENCE T. SUMMERS
1961-1992

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

To the City Commissioners
City of Winchester, Kentucky

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the governmental activities, the business-type activities, the aggregate discretely presented component unit, each major fund, and the aggregate remaining fund information of City of Winchester, Kentucky, as of and for the year ended June 30, 2013, and the related notes to the financial statements, which collectively comprise City of Winchester, Kentucky's basic financial statements, and have issued our report thereon dated February 10, 2014.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered City of Winchester, Kentucky's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of City of Winchester, Kentucky's internal control. Accordingly, we do not express an opinion on the effectiveness of City of Winchester, Kentucky's internal control.

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 and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or, significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified. We did identify a certain deficiency in internal control, described in the accompanying schedule of findings and questioned costs that we consider to be a significant deficiency. (2013-01)

Compliance and Other Matters

As part of obtaining reasonable assurance about whether City of Winchester, Kentucky's financial statements are free from 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*.

City of Winchester, Kentucky's Response to Findings

City of Winchester, Kentucky's response to the findings identified in our audit is described in the accompanying schedule of findings and questioned costs. City of Winchester's response was not subjected to the auditing procedures applied in the audit of the financial statements and accordingly, we express no opinion on it.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Summers, McCrary & Sparks, PSC

Winchester, Kentucky
February 10, 2014

SUMMERS, MCCRARY & SPARKS, P.S.C.
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1961-1992

**INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE FOR EACH MAJOR PROGRAM
AND ON INTERNAL CONTROL OVER COMPLIANCE REQUIRED BY OMB CIRCULAR A-133**

To the City Commissioners
City of Winchester, Kentucky

Report on Compliance for Each Major Federal Program

We have audited City of Winchester, Kentucky's compliance with the types of compliance requirements described in the *OMB Circular A-133 Compliance Supplement* that could have a direct and material effect on each of City of Winchester, Kentucky's major federal programs for the year ended June 30, 2013. City of Winchester, Kentucky's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs.

Management's Responsibility

Management is responsible for compliance with the requirements of laws, regulations, contracts, and grants applicable to its federal programs.

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for each of City of Winchester, Kentucky's major federal programs based on our audit of the types of compliance requirements referred to above. 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 City of Winchester, Kentucky'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 on compliance for each major federal program. However, our audit does not provide a legal determination of City of Winchester, Kentucky's compliance.

Opinion on Each Major Federal Program

In our opinion, City of Winchester, Kentucky, complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended June 30, 2013.

Report on Internal Control Over Compliance

Management of City of Winchester, Kentucky, is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered City of Winchester, Kentucky's internal control over compliance with the types of requirements that could have a direct and material effect on each major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major federal program and to test and report on internal control over compliance in accordance with OMB Circular A-133, 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 City of Winchester, Kentucky's internal control over compliance.

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. *A material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. *A significant deficiency in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of OMB Circular A-133. Accordingly, this report is not suitable for any other purpose.

Summers, McCrary & Sparks, PSC

Winchester, Kentucky
February 10, 2014

CITY OF WINCHESTER, KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
For the Year Ended June 30, 2013

SUMMARY OF AUDIT RESULTS

1. The auditor's report expresses an unqualified opinion on the financial statements of the City of Winchester, Kentucky.
2. One significant deficiency disclosed during the audit of the financial statements is reported in the "Independent Auditor's Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards*." No material weaknesses are reported
3. No instances of noncompliance material to the financial statements of the City of Winchester, Kentucky, which would be required to be reported in accordance with *Government Auditing Standards*, were disclosed during the audit.
4. No significant deficiencies relating to the audit of the major federal awards programs are reported in the "Independent Auditor's Report on Compliance for each Major Program and on Internal Control over Compliance Required by OMB Circular A-133". No material weaknesses are reported.
5. The auditor's report on compliance for the major federal award programs for the City of Winchester, Kentucky expresses an unqualified opinion on all major federal programs.
6. No audit findings that are required to be reported in accordance with Section 510(a) of OMB Circular A-133 are reported in this Schedule.
7. The programs tested as a major program includes: CFDA #20.205 Highway Planning and Construction; CFDA #66.458 Capitalization Grants for Clean Water State Revolving Funds
8. The threshold for distinguishing Types A and B programs was \$300,000.
9. The City of Winchester, Kentucky was determined to be a low-risk auditee.

FINDINGS – FINANCIAL STATEMENT AUDIT

SIGNIFICANT DEFICIENCY:

2013-01: Purchase Orders

Condition: Purchase order procedures are not consistently being followed. The purchase requisitions are not always being dated prior to the date of the vendor invoice.

Criteria: Internal controls require a purchase requisition to be obtained before any items/services are ordered.

Cause: The City's employees are not following the purchasing manual.

Effect: Potential exists for a department to exceed budget.

Recommendation: We recommend management review purchasing procedures with each employee and stress the importance they have with internal control over disbursements.

Management Response and Corrective Action: The City will review its internal controls over purchase orders and meet with all personnel involved in the purchasing process to address these issues. Also, the City is pursuing new software that will allow departments read-only access to their accounts and the ability to create their own reports.

FINDINGS AND QUESTIONS COSTS – MAJOR FEDERAL AWARD PROGRAMS

NONE

CITY OF WINCHESTER, KENTUCKY
SCHEDULE OF PRIOR YEAR FINDINGS AND QUESTIONED COSTS
For the Year Ended June 30, 2013

SECTION I – FINDINGS – FINANCIAL STATEMENT FINDINGS

2012-01 Condition: Purchase order procedures are not consistently being followed by purchasing employees.

Status: Similar condition found in the current year

2012-02 Condition: The City did not include in the Federal grants budget all of the Federal Grant Funds.

Status: The condition was not repeated in the current year.