

CITY OF WINCHESTER, KENTUCKY
AUDITED BASIC FINANCIAL STATEMENTS
INCLUDING SUPPLEMENTARY DATA
AND INDEPENDENT AUDITOR'S REPORTS
FOR THE YEAR ENDED JUNE 30, 2012

**CITY OF WINCHESTER, KENTUCKY
JUNE 30, 2012**

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CITY OF WINCHESTER, KENTUCKY
INFORMATIONAL REPORT
JUNE 30, 2012

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 December 6, 2012.

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.

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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.

OTHER INFORMATION

Emergencies

The City did not declare any emergencies.

Elected Officials

In the November 2010 election, the citizens voted in Ed Burtner for mayor (4-year term); and Kenny Book, Shannon Cox, Rick Beach, and Kitty Strode as commissioners (two-year term) effective January 1, 2011.

Retirements

The City recognized several retirements this past year. Communications Officer Ronnie Blakemore retired after 17 years of service. Police Sergeant Anthony Kirk retired after 11 years of service. Fire Department Battalion Chief Kenneth Williamson retired after 26 years of service. Fire Department Battalion Chief Raymond A. Tallent retired after 20 years of service.

Recognitions

The City presented a Certificate of Recognition to Major Greg Beam for saving a choking victim. The City recognized two officers for exemplary police service. Officer Travis Thompson and Sgt. William Mason were commended for their service to our citizens on April 3, 2012. The City recognized Joy Curtis on October 18, 2011 for earning her certified municipal clerk's designation from the International Institute of Municipal Clerks.

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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 or through the City's website, www.winchesterky.com.

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

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

J. R. Wilhite
Interim City Manager
32 Wall Street, P. O. Box 40
Winchester, KY 40392-0040
859-744-2821
jwilhite@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 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, 2012, which collectively comprise the City's basic financial statements as listed in the table of contents. These financial statements are the responsibility of City of Winchester, Kentucky's management. 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 of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and the significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our 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 aggregate discretely presented component unit, each major fund, and the aggregate remaining fund information of the City of Winchester, Kentucky, as of June 30, 2012, and the respective changes in financial position, and, where applicable, cash flows thereof, and the respective budgetary comparison for the general fund and capital equipment fund for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated January 25, 2013, 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* and should be considered in assessing the results of our audit.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and police and firefighter's pension fund on pages 6 through 26 and page 68 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.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the City of Winchester, Kentucky's financial statements as a whole. The introductory section and combining nonmajor fund financial statements are presented for purposes of additional analysis and are not a required part of the financial statements. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is also not a required part of the 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 financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole. The introductory section has 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.

Summers, McCrary & Sparks, PSC

Lexington, Kentucky
January 25, 2013

**CITY OF WINCHESTER, KENTUCKY
MANAGEMENT DISCUSSION AND ANALYSIS
JUNE 30, 2012**

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 ceaselessly 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 did not grant a cost-of-living adjustment (COLA) for FY2012, but did grant a 3% COLA for FY2013. The City still maintains a self-insured employee health insurance plan in order to keep costs down.

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 are increasing. For FY 2014 the state has granted a temporary one-year reduction.

<u>CERS RATES</u>		
FY2014	18.89%	35.70%
FY2013	19.55%	37.60%
FY2012	18.96%	35.76%
FY2011	16.93%	33.25%
FY2010	16.16%	32.97%

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The total the City paid for retirement costs in FY2012 was approximately \$1.86 million. We estimate that retirement costs in FY2013 will be about \$2.1 million. These rates continue to escalate at a faster pace than we can match. The Kentucky League of Cities, the Kentucky Retirement Systems, and the General Assembly are working to resolve these issues to improve local government's ability to meet commitments to their valued employees.

These pressures affect the goods and services the City pays for. 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.

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.

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

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MANAGEMENT DISCUSSION AND ANALYSIS
JUNE 30, 2012**

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 government-wide financial statements include not only the City itself (known as the primary government), but also its discretely presented component unit, Winchester Municipal Utilities (WMU). Financial information is presented separately from the financial information presented for the primary government. Other additional information about the City's component unit are presented in the notes to the financial statements. Contact information for WMU's financial statements are noted on Page 3.

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 Policemen's and Firemen'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*. The notes 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 non-major governmental funds and the *Schedule of Federal Financial Assistance*. 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 Federal Financial Assistance* lists federal grant expenditures.

**CITY OF WINCHESTER, KENTUCKY
MANAGEMENT DISCUSSION AND ANALYSIS
JUNE 30, 2012**

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 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 30, 2012 and 2011.

	Net Position	
	June 30,	
	Governmental Activities	
	<u>2012</u>	<u>2011</u>
Current and other assets	\$ 7,708,925	\$ 6,849,830
Capital assets	13,044,006	13,324,130
Total assets	20,752,931	20,173,960
Long-term debt outstanding	2,709,912	2,952,696
Other liabilities	1,883,425	1,785,392
Total liabilities	4,593,337	4,738,088
Net position:		
Net investment in capital assets	10,557,540	10,918,016
Restricted	633,150	619,026
Unrestricted	4,968,904	3,898,830
Total Net Position	\$ 16,159,594	\$ 15,435,872

Current and other assets significantly increased about \$859,000. Most of this increase was in the General Fund where cash increased because revenues exceeded expenses. This means that we increased our cash reserves. Expenses were kept low because there were no extraordinary events. Capital Equipment cash increased about \$36,000, also because revenues exceeded expenses, mostly because an ambulance that had been budgeted has not been purchased yet. Non-major governmental fund cash increased overall about \$31,000.

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Accounts Receivable increased about \$518,000. This increase is due to (1) an increase in the occupation license fee rate; (2) an increase in EMS accounts receivable; and (3) an increase in the county's payments for services and reimbursable grant activity.

Capital assets decreased by about \$280,000. Acquisitions totaled \$1,010,697 and depreciation of \$1,290,821 was recorded (difference of \$280,124). This means that asset purchases are lagging behind the "using up" of assets. Depreciation is a measure of how asset value declines as it is used. Not a perfect measure, but this relationship does indicate that the City is not yet replacing the assets as they are used.

At year-end, the traffic signal at U.S. 60 and the city hall bell tower were still in construction. Also, on-going engineering costs for the Fulton Road and Seventh Street projects are still in construction.

In addition, vehicle acquisitions for Police (\$89,600) and Fire (\$31,300) continued the fleet improvements for public safety. Technical equipment acquisitions included two homeland security grant projects for Fire (1) Bluegrass Emergency Response Team foam trailer \$240,000 and (2) fire department generator \$53,000. Remaining acquisitions provided equipment and software for several departments.

Long-term debt decreased by \$242,784 due to principal payments on the debt and no new debt was incurred during FY2012.

Other liabilities increased only slightly. Accounts Payable increased about \$50,000, mostly in the Municipal Aid Program Fund for Fulton Road engineering. Accrued Payroll and Related Liabilities increased about \$150,000 because June's state retirement payment was not made until July (last year, June's payment was made in June). However health insurance claims decreased about \$123,000 (there were several large claims in FY2011).

Payroll and Related Liabilities still includes about \$741,000 attributable to an issue with firefighter overtime and state incentive pay. In 2007, the Kentucky 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 Kentucky Department of Labor. Winchester, along with several other cities, filed a lawsuit challenging the authority of the Kentucky Department of Labor to enforce the Louisville decision. In August, 2011, the Kentucky Supreme Court rejected those arguments.

On December 21, 2011, 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 the correct time and one-half. On January 12, 2012, the City issued payment for back wages totaling \$62,526 to employees specified by the Kentucky Labor Cabinet.

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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 decreased about \$361,000 as annual depreciation expenses exceed the new additions to capital assts. Construction in progress increased about \$308,000 as work proceeds on four major projects – a renovation of the City Hall bell tower, construction of a traffic signal on U.S. 60, Fulton Road engineering phase, and Seventh Street engineering phase.

The City's unrestricted net position is finally recovering from the economic downturn and increased a little over \$1 million by the end of FY2012. This represents 44% of the City's annual net program expenses, a much healthier financial cushion than the prior year's 31%.

Statement of Activities

The Statement of activities provides the operating results for all funds of the City 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 represent 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. The following table summarizes the Statement of Activities for 2012 and 2011.

Operating Results for the Year Ended June 30,		Governmental Activities	
		<u>2012</u>	<u>2011</u>
Revenues:			
Program revenues:			
Charges for services	\$	1,687,503	\$ 1,549,935
Grant funding		2,544,323	2,063,809
Capital contributions		4,422,014	7,626,761
General revenues:			
Property taxes		2,078,336	2,048,831
License fees and permits		941,061	1,039,954
Payroll taxes		6,128,629	4,809,280
Insurance premium tax		1,929,212	1,998,440
Transient room tax		109,894	112,257
Other taxes		117,879	119,424
Interest and investment earnings		40,540	41,676
Parking fines		1,990	3,690
Other local revenues		214,552	189,560
Gain(Loss) on Disposal of Fixed Assets		-	647
Total Revenues		20,215,935	21,604,264

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Program Expenses:		
General government	3,419,226	3,350,847
Public Protection		
Dispatch	701,604	792,996
Police	3,470,291	3,571,543
Fire	3,536,712	4,274,932
EMS	2,266,538	2,398,244
Public Services	1,404,842	1,388,097
Intergovernmental services	4,597,752	7,889,669
Interest on long-term debt	95,246	111,549
Total Expenses	19,492,212	23,777,878
Excess (deficiency) before transfers and special items	723,723	(2,173,614)
Net increase (decrease) in net position	\$ 723,723	\$ (2,173,614)

Charges for Services include EMS revenue for ambulance transports. EMS revenue is up slightly, but will fluctuate because of accounts receivable. The number of transports has not increased that much, but claim processing may have improved.

Although there was less activity in some grants, grant funding increased about \$480,000, mainly because of the Homeland Security Grant for the BERT foam trailer and the CDBG Walle Corporation grant.

Property taxes did not increase much. The City Commission voted to levy the maximum rate allowed by state law (14.5 cents per hundred) for the 2011 calendar year. This rate allows for a four percent increase in revenue. Any rate higher than that is subject to voter recall. However, total assessments increased only slightly and there were no new additions. Payroll taxes increased significantly because the rate increased from 1.5 to 2% effective October 1, 2011 (the increase was effective only slightly, but the account receivable for it decreased because most payroll taxes are now collected on a monthly basis instead of a quarterly basis. Other taxes continue to reflect the downturn in the economy.

Capital Contributions decreased. The City did not accept any new streets this year and there were significant capital contributions from the Lower Howards Creek sewer project in the previous year.

Public Safety expenses were less in FY2012, in part, due to the recognition of the potential liability for firefighter overtime backpay that resulted from litigation. General government and public works expenses are higher, but the rest of the programs, public safety, are lower. This is due in part because all positions were not filled.

Intergovernmental Services decreased also due to the decrease in grant activity. These grants fluctuate with the projects on the drawing board in any given year.

**CITY OF WINCHESTER, KENTUCKY
MANAGEMENT DISCUSSION AND ANALYSIS
JUNE 30, 2012**

Governmental Funds Balance Sheet

The following table summarizes the Governmental Funds Balance Sheet for June 30, 2012 and 2011.

Governmental Funds Balance Sheet	<u>2012</u>	<u>2011</u>
Assets:		
Cash and Cash Equivalents	\$5,673,623	\$5,318,631
Accounts Receivable	2,092,558	1,543,980
Prepaid Expenses	16,587	7,100
Other Assets	0	0
Total Assets	<u>\$7,782,766</u>	<u>\$6,869,711</u>
Liabilities:		
Accounts Payable	\$188,777	\$113,163
Accrued Payroll & Related Liabilities	488,443	275,457
Total Liabilities	<u>677,220</u>	<u>388,621</u>
Fund Balances:		
Restricted	633,150	619,026
Committed	2,279,405	2,154,310
Assigned	49,703	53,721
Unassigned	4,143,289	3,654,034
Total Fund Balances	<u>7,105,546</u>	<u>6,481,090</u>
Total Liabilities & Fund Balance	<u>\$7,782,766</u>	<u>\$6,869,711</u>

Cash has increased about \$355,000. Revenues exceeded expenses in both the general fund and capital improvement fund. Expenses were kept low because there were no extraordinary events. Capital Equipment cash increased about \$36,000, also because revenues exceeded expenses. One-eighth of the payroll tax is transferred to the Capital Equipment Fund. Because the rate increased, the revenue increased. Also, an ambulance that had been budgeted has not been purchased yet. Non-major governmental fund cash increased overall about \$31,000.

Restricted funds increased only slightly, mostly in local project funds. Committed funds increased primarily because of fewer expenses in the Main Street Project, and increases in federal and state forfeitures added to the Police Special Fund and Police Federal Forfeiture. Assigned funds are the self-insured health programs and these funds decreased slightly. Unassigned funds increased because revenues exceeded expenses.

Non-spendable fund balance reflects those amounts that are not held in assets that can easily be converted to cash. 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.

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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 2012 and 2011.

Governmental Fund Operating Statement For the Year Ended June 30,		
	Governmental Activities	
	2012	2011
REVENUES:		
Taxes	\$10,363,951	\$9,088,232
Licenses & Permits	941,061	1,039,954
Charges for Services	1,687,503	1,549,935
Fines	1,990	3,690
Intergovernmental	6,966,338	9,459,420
Investment Income	40,540	41,676
Other	214,552	189,560
TOTAL REVENUES	20,215,935	20,372,466
EXPENDITURES:		
General Government	2,769,505	2,201,498
Public Safety	9,597,982	9,625,577
Public Works	1,293,204	1,269,703
Intergovernmental	4,597,752	7,889,669
Capital	1,010,696	1,007,992
Debt Service Principal	227,094	292,076
Debt Service Interest	95,246	111,549
TOTAL EXPENDITURES	19,591,478	22,398,065
Excess (Deficit) of Revenues over Expenditures	624,456	(1,025,598)
OTHER FINANCING SOURCES (USES):		
Proceeds from Long-term Borrowing		359,076
Operating Transfers In	8,354	11,780
Operating Transfers Out	(8,354)	(11,780)
TOTAL OTHER FINANCING SOURCES (USES):	(8,354)	359,076
Excess (Deficit) of Revenues and Other Financing Sources Over Expenditures and Other Financing Uses	624,456	(666,523)
Fund Balance, Beginning	6,481,090	7,175,720
Less Balance Transferred to Agency Fund		(28,107)
Fund Balance, Ending	\$7,105,546	\$6,481,090

The difference between revenues and expenses show how total fund balance has changed since last year. Total fund balance increased almost \$625,000. The operating deficit became an excess, which means our revenues exceeded our expenses.

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Total taxes increased about \$1.3 million, mainly as a result of the payroll tax rate increase. License and Permits includes our electric and gas utility franchises, which decreased because the 2011-2012 winter was very mild. Charges for Services (EMS revenue) increased slightly.

The large decrease in intergovernmental revenue and expenses is mostly because of the Kentucky Infrastructure Authority loan for the Lower Howards Creek sewershed project.

The large increase in General Government Expenditures is because of the inclusion of the Community Development Block Grant project for the Walle Corporation. The decrease in other operating costs is due to the fact that no COLA was granted for FY2012 and several positions were not filled for the entire year.

The City uses a capital improvements fund to manage fixed asset purchases and financing. The expenditures for capital increased only slightly. Debt service decreased because we did not finance any new items.

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 lagging the City's increasing costs of services.

	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	<u>\$58,932</u>	<u>\$565,525</u>	<u>\$624,456</u>

	FY 2011 GOVERNMENTAL ACTIVITIES		
	Capital	Operating	Total
Revenues	\$1,141,167	\$20,590,376	\$21,731,543
Expended	(1,139,353)	(21,258,711)	(22,398,064)
Net	<u>\$1,814</u>	<u>\$(668,335)</u>	<u>\$(666,523)</u>

Capital revenues are primarily occupational license fees and proceeds from long-term borrowing, but no additional debt was incurred in FY 2012. That is why Capital revenues decreased. Capital expenses decreased because: (1) We did not buy any large equipment; and (2) the aquatic center was finished in the previous year.

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Operating revenues and expenses decreased, mainly due to less grant activity. Also, the City did not grant a COLA for FY2012, several positions were not filled for the entire year, and there were no emergencies.

This year, the City finished the year with an excess. This is mainly due to the increase in tax revenues. The City is working very hard to address revenue and expense issues. One measure that came to fruition was the joint revenue-sharing project with the Clark County Fiscal Court that came about with annexation of the land on which the new hospital was being built. The City is also pursuing other joint agreements. The City is 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 report is on Page 33.

Actual General Fund revenue came in under budget by about \$334,000. Tax revenue came in just over budget. License and Permits came in just under budget. Most of the general fund under budget difference is attributed to Charges for Services, which include Reimbursable Grant Income and EMS Revenue.

A major component of the budgeted Reimbursable Grant Income is the Depot Street project for \$909,000, which was still in engineering design at year-end. We had only spent about \$15,000 for this project and the reimbursable part was only \$12,000. The project has been bid and construction is scheduled to begin January 2013. This project is budgeted in General Fund because it is a reimbursable grant. This is also why Public Works expenses came in under budget by about \$826,000.

EMS revenue increased about 9% over last year and came in over budget by about \$218,000. This increase can be attributed to an increase in ambulance runs and an increase in collections (Medicaid and Medicare payments and several insurance companies now pay by direct deposit instead of by check).

Operating expenses were under budget by about 11%. Some of the reduction is attributable to personnel. The Communications, Police, Fire, and EMS did not have all of their positions filled for the entire year.

Intergovernmental revenue Capital Equipment Fund budget include reimbursable grant projects. Three major grant items were finished at year-end: the Homeland Security Grant to the Bluegrass Emergency Response Team (BERT) for a high-volume multi-foam trailer (\$239,000), a Homeland Security FEMA Hazard Mitigation Grant for the fire department generator initiative, and a Homeland Security Grant for police radio equipment (\$41,000). These projects were moved to the grant portion of the financial statements, but were budgeted in Capital. So the capital revenue and expense items were under budget.

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Capital expenses were also under budget for another reason. We had budgeted \$200,000 for the firefighter overtime issue for debt service, but that issue has yet to be resolved.

Other capital budgeted revenue includes ambulance loan proceeds, but this item is listed under Other Financing Sources, so this was also under budget. At year-end, the ambulance was still in construction so that is why there are no financing proceeds. The ambulance is scheduled to be delivered in early 2013.

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. The original FY2012 budget was very lean. This discussion lists the important changes that were made to General Fund (GF) and Capital Equipment Fund (CEF). Some of the items are minor. Most are self-explanatory. Quite a few pertained to grants.

The first budget amendment added the following:

1. Added \$48,000 to GF expenses for various items
2. Added \$239,000 to CEF revenue for Kentucky Homeland Security reimbursable grant income (BERT foam trailer)
3. Added \$239,000 to CEF expenses for BERT foam trailer
4. Added \$97,000 to CEF expenses for Bell tower tuckpointing project
5. Added \$33,000 to CEF expenses for Fire Chief's vehicle
6. Added \$20,900 to CEF expenses for various items
7. Added \$647,800 to CDBG/Other Grants for CDBG Walle Coporation equipment lease project (\$600,000), KY Renaissance on Main Downtown grant (\$5,800), and two KY Office of Homeland Security grants (\$42,000)

The second budget amendment added the following:

1. Added \$25,000 to GF expenses for additional engineering
2. Added \$70,000 to GF expenses for repairs at police department building caused by lightning strike
3. Added \$150,000 to GF expenses for additional wages
4. Added \$100,000 to GF expenses for additional overtime
5. Added \$65,000 to CEF expenses for traffic signal on U.S. 60
6. Added \$41,000 to CEF expenses for a Kentucky Homeland Security grant for police radio equipment
7. Added \$10,000 to Other Funds for various items

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MAJOR CAPITAL PROJECTS FOR THE YEAR

INFRASTRUCTURE

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 FY2012, the City was working on the following capital projects to enhance public programs and services.

Buildings

In FY2012, 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 \$158,000. About \$60,000 of this total was for repairs due to a lightning strike at the police station. About \$58,100 of this total was for a back-up generator installed at Fire Station #1. Of that amount, \$52,833 was reimbursed to the City by FEMA and the Kentucky Division of Emergency Management.

The City is also in the process of restoring the bell tower on City Hall. This building is 100 years old. The tower was in very bad shape, with water leaks, bird damage, and loose bricks. At June 30, we had spent \$64,465. Complete restoration was finished November 2012 for a final cost of \$328,000.

Curbs, Gutters, Sidewalks, Other

The City built the first phase of a walking trail at Bluegrass Community & Technical College at a cost of \$36,525. Funding came from a Rails-To-Trails state grant. We also repaired curbing at various sites on state roads within the City at a cost of \$25,800. The City will be reimbursed \$10,000 for these repairs.

The City installed a traffic signal on U.S. 60 at the entrance to the new hospital at a cost of \$75,075 (FY2012 - \$44,463, FY2013 - \$30,612). The signal will facilitate traffic flow for the hospital, the planned development around it, and the Clark County Board of Education Central Office.

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, 2012, \$1,249,571 has been spent to replace and/or restore existing storm sewers.

The City spent \$4,701 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.

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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 about \$200,000 maintaining city streets.

The City did not accept any streets into the City street system. 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.

Municipal Aid Bond Program CC05 Bond Fund

The City filed an application to the Kentucky Transportation Cabinet for discretionary funding from the Road Aid Bond Program (CC05 Bond Fund). The application was approved and an agreement with the state was approved by Order Number 2007-183 in December, 2007 for \$225,000. Several streets were repaved with these funds at a cost of \$104,529. The City repaired the Mockingbird Valley Bridge at a total cost of \$57,028. The City repaired the Pearl Street culvert at a total cost of \$63,443 (\$48,924 was spent in FY2012). The agreement was fulfilled and the total spent for these three projects was \$225,000.

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

In FY2010, 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 FY2011, the grant was approved. The total estimated cost is \$1,151,600. The grant portion is \$909,000 (federal funds). The City's match portion is \$242,600.

An architect was selected to proceed with the engineering and design phase of the project. At June 30, design and development were complete. In FY2011, the engineering costs were \$58,120. In FY2012, the engineering costs were \$14,955. In FY2013, the project was put out to bid. Construction will begin January, 2013.

KY Department of Transportation JL-04 Bond Fund

In FY2011, 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, 2012, the engineering costs on these two projects were \$67,450 and \$116,462 respectively.

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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 FY2012.

Land

On December 12, 2011, the City accepted vacant property at 45 Sixth Street by Order No. 2011-187. The house was in poor shape and was subsequently demolished.

Annexation

The City annexed approximately 30 acres along U.S. 60, Caudill Drive, Brownland Way, and Croxton Way by Order No. 4-2012 on February 7, 2012. The new hospital was built at this site.

Land Improvements

There were no major land improvements in FY2012.

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 FY2012, the City applied for several grants. Listed below is the status of grant applications.

1. CDBG Disaster Recovery Program Grant, \$621,000, culvert reconstruction, pending
2. Winchester Youth Soccer Park Improvements, pending
3. Bluegrass Pride Community Grant, \$9,750, construction of wetlands, 50/50 match, approved
4. United States Department of Justice COPS Grant, \$182,531, Hiring Program, denied
5. Kentucky Office of Homeland Security, \$23,163, P25 Repeater, denied
6. Kentucky Office of Homeland Security, \$1,500, Security Camera Police Department, approved
7. 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, approved
8. Kentucky Office of Homeland Security, \$23,000, Joint Grant for Mobile P25 Digital Radios, approved
9. Kentucky Office of Homeland Security, \$69,387, P25 Repeaters/Microwave Links, denied
10. Kentucky Office of Homeland Security, \$8,855, Mobile Data Computers, denied

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11. Kentucky Office of Homeland Security, \$40,285, Rugged Notebook Computers and Printers, denied
12. United States Department of Homeland Security FEMA, \$127,204, Chest Compression Devices and Fire Ground Simulator, denied
13. United States Department of Homeland Security FEMA, \$993,000, Aerial Apparatus, denied
14. Assistance to Firefighters SAFER Grant, \$384,000, Staffing for Adequate Fire and Emergency Response, denied

The following grants were received prior to FY2012 and are still ongoing.

1. Kentucky Transportation Cabinet TEA-21 Grant, \$909,000, match 20%, Depot Street Restoration Project (improvements, landscaping, and lighting)
2. 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
3. Kentucky Nonpoint Source Pollution Control Grant, \$208,534
4. Kentucky Renaissance on Main Façade Grant, \$20,000
5. Kentucky Governor's Office of Local Development Rails-To-Trails Grant, \$39,800

The following grants were completed and closed out during FY2012.

1. CDBG Grant, Walle Corporation Equipment Lease, \$600,000
2. Kentucky Transportation Cabinet Highway Safety Grant, \$10,000, Operation Safe Winchester XII (10/2010 to 9/2011)
3. National Association of Drug Diversion Investigators (NADDI), \$5,000
4. United States Department of Homeland Security FEMA, Generator Initiative, \$45,619
5. Kentucky Homeland Security Grant, \$239,800, Bluegrass Emergency Response Team, high volume multi-foam suppression trailer

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. To address these deficiencies, the City engaged the services of CDP Engineers, Inc. (Order No. 2011-8) to achieve satisfactory compliance for Plan Year 1 (Phase II permit) and development of a stormwater quality management plan. The following ordinances were also adopted as part of this plan:

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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

The City approved 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).

On November 7, 2012 we received notification from the state that the notice of violation has been temporarily lifted. 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.

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 FY2009. This has provided better access to the Bluegrass Community & Technical College (BCTCS) and another route for industrial traffic.

Economic development increased much more during FY2012. We began the year with a 9.3% unemployment rate (down from 10.5% at the same time last year) and ended the fiscal year with an 8.2% unemployment rate. This can be attributed to the prior year's efforts with the recruitment of Senko and Alltech, as well as investment by existing industry such as Walle and Catalent.

Alltech received final approval for the Kentucky Economic Development Finance Board (KEDFA) in June 2012 indicating that they had hired the required 48 employees (average wage \$20.50) and invested about \$15 million in expansion efforts. Catalent received preliminary approval in October 2011 from the KEDFA for tax incentives on an expansion project that will invest \$45 million and hire 90 new people with an (average wage) of \$23 per hour.

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TAICA, a Japanese automotive supplier, was granted preliminary approval by the KEFDA for tax incentives in March of 2012. They will invest \$8 million in a vacant building and create 30 jobs (average wage \$20).

We also entered into another CDBG low-interest loan with the WCC-IDA for \$600,000 at 2% interest for the Walle Corporation for equipment purchases. This assistance helped Walle Corporation hire an additional 60 employees. These funds will go back into sewer projects for Rocky Mountain ATV and others. Rocky Mountain ATV is building a 65,000 square foot distribution center and will employ up to 80 people. They will build a parts and accessory distribution center on a 15-acre lot in the Industrial Park.

Another sign of growth is Senko Corporation. The WCC-IDA successfully recruited Senko to build a plant in the Industrial Park. Senko is a cold storage/dry goods logistics center. Senko has invested \$4.8 million for construction of the plant, which opened July 2011. Also, WCC-IDA and the City helped Senko secure \$500,000 in state tax incentives. Senko hired 12 employees as part of the tax incentive package.

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.

By far, the biggest achievement of the year was the successful recruitment of Amazon WACS, Inc, a subsidiary of Amazon. In March 2012, KEDFA granted preliminary approval to Amazon for a customer support project that will invest \$20 million. Amazon will hire 550 full-time and 600 part-time/seasonal employees (average wage \$15.74). Amazon will temporarily locate in the Winchester Plaza and ultimately build an 80,000 square-foot building for their call center. We are convinced that our previous efforts to get the Plaza renovated helped immensely in getting this project in our community.

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 two years ago, the city and county created a TIF district in the area around Winchester Plaza. A TIF is tax increment financing. Designating an area as a TIF district allows the owner/developer to finance improvements from future increases in the tax revenues. The new businesses that opened last year have continued to thrive. The TIF district has been a success. Winchester Plaza is now a much-improved anchor for our community.

Subway Sandwich renovated an existing building in another area of this major intersection. On the Bypass, the AT&T Store finished construction on a new building.

Two 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 annexed this area and approved a joint revenue-sharing agreement with the Clark County Fiscal Court.

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The new hospital opened this spring and a physician's office building opened later. The City funded a much-needed traffic signal on U.S. 60 at this site. Already, one local restaurant has moved to that new area. We anticipate more new business opportunities in that area. The City is very optimistic about new development surrounding the hospital.

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 fourth Beer Cheese Festival on June 9, 2012. The festival was a huge success. Winchester First is also working on a loan program to aid downtown investment.

The City had also applied for a Transportation Enhancement Grant for street improvements, lighting, and landscaping for Depot Street. Project funding has been approved. An architect has been selected and construction should begin in the spring of 2013.

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 Veterans Memorial Parkway (eastern bypass) will bring about balanced residential and business growth on the east side of Clark County.

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.

However, the economy has impacted the local unemployment rates. We began the year with a 9.3% unemployment rate. We have had some success with existing industry, new industry, and new businesses. We have numerous inquiries from potential businesses. The local unemployment rate has fallen to 8.2% at fiscal year end.

The City, like most Kentucky communities, is highly dependent on occupational 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 (FY2013). The rates chosen for real and tangible property were the compensating rates, which only allows for the same amount of tax revenue received in FY2012. The FY2013 budget was based on the maximum allowable rate, so this revenue will be down.

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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.

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 the summer of 2012, the Kentucky General Assembly appointed a tax force to research and evaluate potential reforms for the both the Kentucky Employees Retirement System and the County Employees Retirement System. Recommendations from the Pension Reform Task Force were delivered to the General Assembly in November 2012 in anticipation of legislative changes during the 2013 General Assembly. In general, the proposals include increased contributions, elimination of cost-of-living adjustments for retirees, limitation on returning to governmental service after retirement, and a shift to a defined contribution plan (with a guaranteed minimum return on investments) for new employees. The impact of any revisions cannot be estimated until the General Assembly takes final action on the recommendations.

During our FY2013 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 FY2013, 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 have included this in the first budget amendment for FY2013. 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 will have a major impact on this fund.

Our City revenue is not keeping up with expenses. In the coming year, management anticipates that general fund expenses will exceed general fund revenues (deficit). 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.

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. A sustained economic downturn will not support future debt for capital projects.

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3. 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.
4. The impact of unfunded federal mandates.

There have been no changes in funding policies since the Commission approved a motion on May 19, 2004 to maintain general fund balance at \$2 million. For the months of July, August, 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.

Hopefully we are on the recovery side of the recession. Recovery is 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 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.

Still, 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 Development Authority. If you have questions about this report or need additional financial information, please visit our website (www.winchesterky.com), give us a call, or visit us at City Hall.

Debbie Bailey
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Interim City Manager
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CITY OF WINCHESTER, KENTUCKY
STATEMENT OF NET POSITION
JUNE 30, 2012

	PRIMARY GOVERNMENT		COMPONENT UNIT
	GOVERNMENTAL ACTIVITIES	TOTAL	
ASSETS:			
Current Assets			
Cash and Cash Equivalents	\$ 5,673,623	\$ 5,673,623	\$ 5,386,377
Restricted Cash and Cash Equivalents	0	0	404,038
Restricted Investments	0	0	4,741,588
Accounts Receivable			
Taxes	1,318,222	1,318,222	0
Accounts, net	369,674	369,674	1,693,797
Intergovernmental	330,821	330,821	0
SDC Receivables	0	0	943,036
Other Accounts Receivables	0	0	50,470
Due from Other Governments	0	0	0
Prepaid Insurance	16,587	16,587	616,292
Restricted Accrued Interest	0	0	19,977
Inventories	0	0	315,675
Total Current Assets	7,708,925	7,708,925	14,171,250
Restricted Assets			
Cash and Cash Equivalents	0	0	10,605,127
Investments	0	0	413,765
Total Restricted Assets	0	0	11,018,892
Noncurrent Assets			
Construction in Progress	395,064	395,064	32,771,273
Land	1,986,538	1,986,538	1,051,011
Net Capital Assets	10,662,403	10,662,403	64,717,555
Bond Issue Costs	0	0	168,353
Total Noncurrent Assets	13,044,006	13,044,006	98,708,192
TOTAL ASSETS	\$ 20,752,931	\$ 20,752,931	\$ 123,898,334
LIABILITIES:			
Current Liabilities			
Accounts Payable	\$ 114,936	\$ 114,936	\$ 636,053
Other Accrued Liabilities	0	0	361,080
Accrued Payroll & Related Liabilities	1,229,917	1,229,917	0
Compensated Absences	0	0	401,302
Incurred but Not Reported Health Claims	98,000	98,000	0
Current Portion of Lease Obligations	317,498	317,498	6,975
Total Current Liabilities	1,760,351	1,760,351	1,405,410
Current Liabilities from Restricted Assets			
Customer Deposits	0	0	157,685
Current Portion of Bonds	0	0	1,816,115
Accrued Interest Payable	0	0	90,116
Accounts Payable - Construction	0	0	287,090
Accounts Payable - Retainage	0	0	75,126
Total Current Liabilities from Restricted Assets	0	0	2,426,132
Noncurrent Liabilities			
Net Pension Obligation	440,572	440,572	0
Noncurrent Portion of Lease Obligations	1,773,903	1,773,903	0
Noncurrent Portion of Lease Obligations	0	0	6,974
Noncurrent Portion of Bonds	0	0	59,161,973
Accrued Sick Leave	618,511	618,511	0
Total Noncurrent Liabilities	2,832,986	2,832,986	59,168,947
TOTAL LIABILITIES	4,593,337	4,593,337	63,000,489
NET POSITION			
Net Investment in Capital Assets	10,557,540	10,557,540	37,457,686
Restricted	633,150	633,150	0
Restricted for Capital Projects	0	0	9,991,337
Restricted for Bond Debt Service	0	0	840,983
Unrestricted	4,968,904	4,968,904	12,607,839
TOTAL NET POSITION	16,159,594	16,159,594	60,897,845
TOTAL LIABILITIES AND NET POSITION	\$ 20,752,931	\$ 20,752,931	\$ 123,898,334

**CITY OF WINCHESTER, KENTUCKY
STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED JUNE 30, 2012**

FUNCTIONS/PROGRAMS	PROGRAM REVENUES				NET (EXPENSE) REVENUE AND CHANGES IN NET ASSETS PRIMARY GOVERNMENT		COMPONENT UNIT
	EXPENSES	CHARGES FOR SERVICES	OPERATING GRANTS AND CONTRIBUTIONS	CAPITAL GRANTS AND CONTRIBUTIONS	GOVERNMENTAL ACTIVITIES	TOTAL	
Primary Government							
Governmental Activities:							
General Government	\$ (3,419,226)	\$ 69,148	\$ 707,440	\$ 52,650	\$ (2,589,988)	\$ (2,589,988)	
Public Safety:							
Dispatch	(701,604)	0	566,464	2,563	(132,577)	(132,577)	
Police	(3,470,291)	0	249,819	40,500	(3,179,972)	(3,179,972)	
Fire	(3,536,712)	0	200,148	292,522	(3,044,043)	(3,044,043)	
EMS	(2,266,538)	1,618,356	252,068	33,068	(363,047)	(363,047)	
Public Works	(1,404,842)	0	496,202	773,469	(135,170)	(135,170)	
Intergovernmental Services	(4,597,752)	0	72,182	3,227,241	(1,298,329)	(1,298,329)	
Interest on Long-Term Debt	(95,246)	0	0	0	(95,246)	(95,246)	
Total Governmental Activities	(19,492,212)	1,687,503	2,544,323	4,422,014	(10,838,371)	(10,838,371)	
Total Primary Government	\$ (19,492,212)	\$ 1,687,503	\$ 2,544,323	\$ 4,422,014	\$ (10,838,371)	\$ (10,838,371)	
Component Unit							
Winchester Municipal Utilities	\$ (12,806,771)	\$ 13,995,169	\$ 1,124,188	\$ 0			\$ 2,312,586
			General Revenues:				
			Taxes:				
			Property	\$ 2,078,336	\$ 2,078,336	\$ 0	0
			Licenses & Permits	941,061	941,061	0	0
			Payroll	6,128,629	6,128,629	0	0
			Insurance Premium	1,929,212	1,929,212	0	0
			Hotel/Motel Room Tax	109,894	109,894	0	0
			Telecommunications Excise Tax	117,879	117,879	0	0
			Investment Income	40,540	40,540		150,892
			Parking Fines	1,990	1,990		0
			Gain (Loss) on Disposal of Capital Assets	0	0		39,164
			Other Local Revenues	214,552	214,552		202,791
			Total General Revenues	\$ 11,562,094	\$ 11,562,094	\$ 392,847	
			Capital Contributions	0	0		206,733
			Change in Net Position	723,723	723,723		2,912,166
			Net Position June 30, 2011	15,435,872	15,435,872		57,985,679
			Net Position June 30, 2012	\$ 16,159,594	\$ 16,159,594	\$ 60,897,845	

See Auditor's Report and Accompanying Notes

**CITY OF WINCHESTER, KENTUCKY
BALANCE SHEET
GOVERNMENTAL FUNDS
JUNE 30, 2012**

	GENERAL FUND	CAPITAL EQUIPMENT FUND	FEDERAL GRANT FUND	NONMAJOR GOVERNMENTAL FUNDS	TOTAL GOVERNMENTAL FUNDS
ASSETS:					
Cash and Cash Equivalents	\$ 2,807,413	\$ 1,967,913	\$ 0	\$ 898,297	\$ 5,673,623
Accounts Receivable					
Taxes, Net of Allowance for Doubtful					
Accounts (\$108,133)	1,318,222	0	0	0	1,318,222
Accounts, Net of Allowance for Doubtful					
Accounts (\$327,489)	369,674	0	0	0	369,674
Intergovernmental	232,207	356	73,044	25,214	330,821
Due from Other Funds	18,018	40,500	0	15,324	73,841
Prepaid Expenses	16,587	0	0	0	16,587
Accrued Interest	0	0	0	0	0
TOTAL ASSETS	\$ 4,762,119	\$ 2,008,769	\$ 73,044	\$ 938,835	\$ 7,782,766
 LIABILITIES:					
Accounts Payable	\$ 80,684	\$ 0	\$ 0	\$ 34,252	\$ 114,936
Due to Other Funds	0	0	73,044	797	73,841
Pension Contribution Payable	0	0	0	0	0
Accrued Payroll & Related Liabilities	488,443	0	0	0	488,443
TOTAL LIABILITIES	569,128	0	73,044	35,049	677,220
 FUND BALANCES:					
Restricted Fund Balance	0	0	0	633,150	633,150
Committed Fund Balance	0	2,008,769	0	270,636	2,279,405
Assigned Fund Balance	49,703	0	0	0	49,703
Unassigned Fund Balance	4,143,289	0	0	0	4,143,289
TOTAL FUND BALANCES	4,192,991	2,008,769	0	903,786	7,105,546
TOTAL LIABILITIES AND FUND BALANCES	\$ 4,762,119	\$ 2,008,769	\$ 73,044	\$ 938,835	\$ 7,782,766

See Auditor's Report and Accompanying Notes

**CITY OF WINCHESTER, KENTUCKY
RECONCILIATION OF THE BALANCE SHEET - GOVERNMENTAL FUNDS
TO THE STATEMENT OF NET POSITION
JUNE 30, 2012**

Total Governmental Fund Balances	\$	7,105,546
Amounts reported for governmental activities in the statement of net assets are different because:		
Capital assets are not reported in the fund financial statement because they are not current financial resources, but they are reported in the statement of net assets.		13,044,006
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 assets.		
Long-term debt		(2,091,401)
Incurred but Not Reported Health Claims		(98,000)
Compensated absences liability		(618,511)
Net Pension Obligation		(440,572)
Long-term litigation settlement		(741,474)
Net Position of Governmental Activities	\$	<u><u>16,159,594</u></u>

See Auditor's Report and Accompanying Notes

CITY OF WINCHESTER, KENTUCKY
STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES
GOVERNMENTAL FUNDS
FOR THE YEAR ENDED JUNE 30, 2012

	<u>GENERAL</u>	<u>CAPITAL EQUIPMENT</u>	<u>FEDERAL GRANT FUNDS</u>	<u>NONMAJOR GOVERNMENTAL FUNDS</u>	<u>TOTAL GOVERNMENTAL FUNDS</u>
REVENUES:					
Taxes	\$ 9,533,159	\$ 720,721	\$ 0	\$ 110,071	\$ 10,363,951
Licenses & Permits	941,061	0	0	0	941,061
Charges for Services	1,687,503	0	0	0	1,687,503
Fines	1,990	0	0	0	1,990
Intergovernmental	1,365,807	70,570	4,844,402	685,558	6,966,338
Investment Income	19,669	14,734	0	6,137	40,540
Other	153,145	5,500	0	55,907	214,552
TOTAL REVENUES	<u>13,702,334</u>	<u>811,526</u>	<u>4,844,402</u>	<u>857,673</u>	<u>20,215,935</u>
EXPENDITURES:					
City Commission	105,781	8,193	0	0	113,974
City Attorney	31,890	0	0	0	31,890
City Manager	457,969	0	0	0	457,969
Finance Department	335,678	0	0	0	335,678
Planning Department	310,096	70	0	5,400	315,567
Main Street Department	72,735	0	0	18,107	90,842
Engineering	124,983	0	0	0	124,983
Conservancy	67,741	151	0	0	67,892
Administration	629,847	864	600,000	0	1,230,711
Central Communications	739,535	108	0	0	739,644
Police Department	3,280,997	3,446	42,030	30,465	3,356,938
Fire Department	3,326,810	6,509	0	6,381	3,339,700
EMS Division	2,160,868	833	0	0	2,161,701
Public Works	938,554	34,650	0	320,000	1,293,204
Intergovernmental	629,584	0	3,857,386	110,782	4,597,752
Capital	2,991	368,116	353,340	286,250	1,010,696
Debt Service Principal	0	227,094	0	0	227,094
Debt Service Interest	0	95,246	0	0	95,246
TOTAL EXPENDITURES	<u>13,216,059</u>	<u>745,279</u>	<u>4,852,755</u>	<u>777,385</u>	<u>19,591,478</u>
Excess (Deficit) of Revenues over Expenditures	<u>486,275</u>	<u>66,247</u>	<u>(8,354)</u>	<u>80,288</u>	<u>624,456</u>
OTHER FINANCING SOURCES (USES):					
Operating Transfers In	0	0	8,354	0	8,354
Operating Transfers Out	(1,039)	(7,315)	0	0	(8,354)
TOTAL OTHER FINANCING SOURCES (USES):	<u>(1,039)</u>	<u>(7,315)</u>	<u>8,354</u>	<u>0</u>	<u>0</u>
Excess (Deficit) of Revenues and Other Financing Sources over Expenditures and Other Financing Uses	<u>485,237</u>	<u>58,932</u>	<u>0</u>	<u>80,288</u>	<u>624,456</u>
Fund Balance June 30, 2011	<u>3,707,755</u>	<u>1,949,837</u>	<u>0</u>	<u>823,498</u>	<u>6,481,090</u>
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>

See Auditor's Report and Accompanying Notes

**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, 2012**

Net Change in Fund Balances - Total Governmental Funds	\$	624,456
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.		1,010,696
Depreciation expense is reported in the statement of activities to recognize the cost of capital assets used to provide programs and services.		(1,290,821)
Gain/loss on sale of fixed assets is reported in the statement of activities to recognize the disposal of fixed 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		62,526
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 assets.		(25,490)
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 assets.		123,300
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 assets.		15,691
Unamortized bond costs were capitalized in prior years and expensed in current year to implement GASB Statement No. 65		(23,729)
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 assets.		227,094
		<hr style="width: 100%;"/>
Change in Net Postion of Governmental Activities	\$	<u><u>723,723</u></u>

See Auditor's Report and Accompanying Notes

CITY OF WINCHESTER, KENTUCKY
SCHEDULE OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES
BUDGET TO ACTUAL (BUDGETARY BASIS) MAJOR GOVERNMENTAL FUNDS
FOR THE YEAR ENDED JUNE 30, 2012

	GENERAL FUND				SPECIAL REVENUE FUND (CAPITAL EQUIPMENT FUND)				SPECIAL REVENUE FUND (FEDERAL GRANTS FUND)			
	BUDGETED AMOUNTS		ACTUAL	VARIANCE Favorable (Unfavorable)	BUDGETED AMOUNTS		ACTUAL	VARIANCE Favorable (Unfavorable)	BUDGETED AMOUNTS		ACTUAL	VARIANCE Favorable (Unfavorable)
	ORIGINAL	FINAL			ORIGINAL	FINAL			ORIGINAL	FINAL		
REVENUES:												
Taxes	\$ 9,327,000	\$ 9,327,000	\$ 9,533,159	\$ 206,159	\$ 750,000	\$ 750,000	\$ 720,721	\$ (29,279)	\$ 0	\$ 0	\$ 0	\$ 0
Licenses & Permits	990,000	990,000	941,061	(48,939)	0	0	0	0	0	0	0	0
Charges for Services	2,279,500	2,279,500	1,687,503	(591,997)	0	0	0	0	0	0	0	0
Fines	0	0	1,990	1,990	0	0	0	0	0	0	0	0
Intergovernmental	1,439,500	1,439,500	1,365,807	(73,693)	165,000	404,000	70,570	(333,430)	2,091,000	2,738,800	4,844,402	2,105,602
Investment Income	0	0	19,669	19,669	224,500	224,500	14,734	(209,766)	0	0	0	0
Other	0	0	153,145	153,145	5,500	5,500	5,500	0	0	0	0	0
TOTAL REVENUES	14,036,000	14,036,000	13,702,334	(333,666)	1,145,000	1,384,000	811,526	(572,474)	2,091,000	2,738,800	4,844,402	2,105,602
EXPENDITURES:												
General Government	2,294,000	2,331,000	2,136,719	194,281	0	0	9,278	(9,278)	875,000	1,480,800	600,000	880,800
Central Communications	857,000	857,000	739,535	117,465	11,100	11,100	108	10,992	0	0	0	0
Police Department	3,325,000	3,395,000	3,280,997	114,003	4,000	4,000	3,446	554	9,000	10,500	42,030	(31,530)
Fire Department	3,280,000	3,430,000	3,326,810	103,190	0	0	6,509	(6,509)	0	0	0	0
EMS Division	2,178,000	2,311,000	2,160,868	150,132	0	0	833	(833)	0	0	0	0
Public Works	1,765,000	1,765,000	938,554	826,446	41,500	41,500	34,650	6,850	909,000	909,000	0	909,000
Intergovernmental	639,000	642,000	629,584	12,416	0	0	0	0	0	0	3,857,386	(3,857,386)
Capital	0	0	2,991	(2,991)	634,800	1,130,700	368,116	762,584	298,000	338,500	353,340	(14,840)
Debt Service Principal	0	0	0	0	225,000	225,000	227,094	(2,094)	0	0	0	0
Debt Service Interest	0	0	0	0	87,000	87,000	95,246	(8,246)	0	0	0	0
TOTAL EXPENDITURES	14,338,000	14,731,000	13,216,059	1,514,941	1,003,400	1,499,300	745,279	754,021	2,091,000	2,738,800	4,852,755	(2,113,956)
Excess (Deficit) of Revenues over Expenditures	(302,000)	(695,000)	486,275	1,181,275	141,600	(115,300)	66,247	181,547	0	0	(8,354)	(8,354)
OTHER FINANCING SOURCES (USES):												
Proceeds of Long-term Debt	0	0	0	0	0	0	0	0	0	0	0	0
Operating Transfers In	400,000	400,000	0	400,000	(400,000)	(400,000)	0	400,000	0	0	8,354	8,354
Operating Transfers Out	0	0	(1,039)	1,039	0	0	(7,315)	(7,315)	0	0	0	0
TOTAL OTHER FINANCING SOURCES (USES):	400,000	400,000	(1,039)	401,039	(400,000)	(400,000)	(7,315)	392,685	0	0	8,354	8,354
Excess (Deficit) of Revenues and Other Financing Sources over Expenditures and Other Financing Uses	98,000	(295,000)	485,237	1,582,314	(258,400)	(515,300)	58,932	574,232	0	0	(0)	(0)
Fund Balance June 30, 2011	2,928,000	2,928,000	3,707,755	779,755	1,907,000	1,907,000	1,949,837	42,837	0	0	0	0
Fund Balance June 30, 2012	\$ 3,026,000	\$ 2,633,000	\$ 4,192,991	\$ 2,362,069	\$ 1,648,600	\$ 1,391,700	\$ 2,008,769	\$ 617,069	\$ 0	\$ 0	\$ (0)	\$ (0)

See Auditor's Report and Accompanying Notes

**CITY OF WINCHESTER, KENTUCKY
STATEMENT OF NET POSITION
PROPRIETARY FUND (COMPONENT UNIT)
JUNE 30, 2012**

	ENTERPRISE FUND
ASSETS:	
Current Assets	
Cash and Cash Equivalents	\$ 5,386,377
Restricted Cash and Cash Equivalents	404,038
Restricted Investments	4,741,588
Accounts Receivable, Customers, Net of Allowance of Doubtful Accounts, \$20,361	1,693,797
SDC Assessments Receivable	943,036
Other Accounts Receivables	50,470
Prepaid Expenses	616,292
Restricted Accrued Interest	19,977
Inventories	315,675
Total Current Assets	14,171,250
Restricted Assets	
Cash and Cash Equivalents	10,605,127
Investments	413,765
Total Restricted Assets	11,018,892
Property, Plant and Equipment	
Utility Systems, Net of Depreciation	64,717,555
Land	1,051,011
Construction in Progress	32,771,273
Total Property, Plant and Equipment	98,539,839
Other Assets, unamortized	
Bond Issue Costs	168,353
Total Other Assets	168,353
TOTAL ASSETS	\$ 123,898,334
LIABILITIES:	
Current Liabilities	
Accounts Payable	\$ 636,053
Other Accrued Liabilities	361,080
Compensated Absences	401,302
Current Portion of Capital Lease Payable	6,975
Total Current Liabilities	1,405,410
Current Liabilities Payable from Restricted Assets	
Accounts Payable - Construction	287,090
Accounts Payable - Retainage	75,126
Accrued Interest Payable	90,116
Customer Deposits	157,685
Current Portion of Long-Term Debt	1,816,115
Total Current Liabilities from Restricted Assets	2,426,132
Long-Term Debt, Less Current Portion	
Long-Term Debt, Less Current Portion	59,161,973
Capital Lease Payable, Less Current Portion	6,974
Total Long-Term Debt, Less Current Portion	59,168,947
TOTAL LIABILITIES	63,000,489
NET POSITION:	
Net Investment of Capital Assets	37,457,686
Restricted for Capital Projects (Expendable)	9,991,337
Restricted for Bond Debt Service (Expendable)	840,983
Unrestricted	12,607,839
TOTAL NET POSITION	60,897,845
TOTAL LIABILITIES AND NET POSITION	\$ 123,898,334

See Auditor's Report and Accompanying Notes

CITY OF WINCHESTER, KENTUCKY
STATEMENT OF REVENUES, EXPENSES AND CHANGES IN FUND NET POSITION
PROPRIETARY FUND (COMPONENT UNIT)
FOR THE YEAR ENDED JUNE 30, 2012

	<u>ENTERPRISE FUND</u>
OPERATING REVENUES:	
Water	\$ 4,843,271
Wastewater	6,226,897
Solid Waste	2,868,726
Transfer Station	56,275
TOTAL OPERATING REVENUES	<u>13,995,169</u>
OPERATING EXPENSES:	
Administrative	1,896,651
Solid Waste	1,676,815
Water	3,061,054
Wastewater	4,848,891
Vehicle Maintenance	136,859
TOTAL OPERATING EXPENSES	<u>11,620,270</u>
Operating Income (Loss)	2,374,899
NON-OPERATING REVENUES (EXPENSES)	
Interest Income	223,376
Interest Expense	(1,014,251)
Other Income	202,791
Investment Income	(72,484)
Gain on Sale of Capital Assets	39,164
Amortization Expense of Bond Issue Costs & Bond Discount	(172,250)
Federal and State Grants	1,124,188
TOTAL NON-OPERATING REVENUES (EXPENSES)	<u>330,534</u>
Net Income (Loss) before Capital Grants & Contributions	2,705,433
Capital Grants and Contributions	<u>206,733</u>
Change in Net Position	<u>2,912,166</u>
Fund Net Position, Beginning of Year	<u>57,985,679</u>
Fund Net Position, End of Year	<u><u>\$ 60,897,845</u></u>

See Auditor's Report and Accompanying Notes

**CITY OF WINCHESTER, KENTUCKY
STATEMENT OF CASH FLOWS
PROPRIETARY FUND (COMPONENT UNIT)
FOR THE YEAR ENDED JUNE 30, 2012**

	ENTERPRISE FUND
CASH FLOWS FROM OPERATING ACTIVITIES	
Receipts from Customers	\$ 13,698,837
Payments to Suppliers	(5,017,062)
Payments to Employees	(2,498,862)
Other Receipts (Payments)	<u>(31,493)</u>
Net Cash Provided (Used) by Operating Activities	<u>6,151,420</u>
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES	
Proceeds from Sale of Equipment	49,858
Proceeds from Long-Term Debt	27,823,103
Bond Issue Costs/Discount on Long-Term Debt	(146,835)
Principal Payments	(9,087,484)
Interest Payments	(1,292,551)
Purchase of Property, Plant and Equipment	(24,639,267)
Proceeds from Federal and State Grants - Capital Items	1,124,188
Contributed Capital Received	149,890
Cash from Other Income	<u>202,791</u>
Net Cash Provided (Used) by Capital and Related Financing Activities	<u>(5,816,307)</u>
CASH FLOWS FROM INVESTING ACTIVITIES	
Proceeds from Sales and Maturities of Investments	3,329,581
Purchase of Investments	(2,174,995)
Cash from Interest in Investments	<u>141,587</u>
Net Cash Provided (Used) by Investing Activities	<u>1,296,173</u>
Net Increase (Decrease) in Cash and Cash Equivalents	1,631,286
Cash and Cash Equivalents, Beginning of Year	<u>14,764,256</u>
Cash and Cash Equivalents, End of Year	<u>\$ 16,395,542</u>
Reconciliation of Cash and Cash Equivalents to the Statement of Net Assets:	
Cash and Cash Equivalents - Unrestricted	5,386,377
Cash and Cash Equivalents - Restricted	404,038
Investments - Restricted	<u>10,605,127</u>
Cash and Cash Equivalents, End of Year	<u>\$ 16,395,542</u>
Reconciliation of Operating Income (Loss) to Net Cash Provided by Operating Activities:	
Operating Income (Loss)	\$ 2,374,899
Adjustments to Reconcile Net Income (Loss) to Net Cash from Operating Activities:	
Depreciation/Amortization	3,467,372
Changes in Assets and Liabilities:	
Accounts Receivable, Customers	(299,040)
SDC Receivable	2,119
Other Accounts Receivable	(34,968)
Other Receivable	3,474
Material and Supplies	(9,019)
Prepaid Expenses	(11,904)
Accounts Payable	413,768
Accounts Payable - Construction	189,902
Accounts Payable - Retainage	75,126
Accrued Liabilities	(23,775)
Accrued Vacation	2,877
Customer Deposits	<u>589</u>
Net Cash Provided by Operating Activities	<u>\$ 6,151,420</u>
NONCASH TRANSACTIONS AFFECTING FINANCIAL POSITION	
Capital assets were acquired through contributions from Developers Governmental Entities	\$ 56,843
	<u>\$ 56,843</u>

See Auditor's Report and Accompanying Notes

**CITY OF WINCHESTER, KENTUCKY
STATEMENT OF FIDUCIARY NET POSITION
FIDUCIARY FUND
JUNE 30, 2012**

	PENSION TRUST	AGENCY FUND
ASSETS		
Cash and Cash Equivalents	\$ 18,575	\$ 11,103
Investments	1,660,993	
Accrued Investment Income	10,319	
TOTAL ASSETS	\$ 1,689,886	\$ 11,103
LIABILITIES		
Accounts Payable	\$	\$ 1,719
Due to Member Agencies		9,384
TOTAL LIABILITIES	\$	\$ 11,103
 FIDUCIARY NET POSITION	 \$ 1,689,886	

(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, 2012**

	PENSION TRUST
ADDITIONS:	
Contributions	\$ 16,268
Other Revenue	
Investment Income:	
Interest	40,823
Net Appreciation (Depreciation) in Fair Value of Investments	
(Gain) Loss on Sale of Investments	39,218
Less: Investment Expense	(6,068)
Net Investment Income	73,973
Total Additions	90,241
DEDUCTIONS:	
Benefits	105,644
Program Expenses	
Due to Members	
HRA Benefits	11,268
Taxes	4,487
Total Deductions	121,399
Change in Net Assets	(31,158)
Net Position June 30, 2011	1,721,044
Net Position June 30, 2012	\$ 1,689,886

CITY OF WINCHESTER, KENTUCKY
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2012

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 and would not cause the City's financial statements to be misleading: 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 Preservation Commission, Winchester/Clark County Appeals Board and the Municipal Cemetery Board.

CITY OF WINCHESTER, KENTUCKY
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2012

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 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, 2012

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. Accordingly, it presents only a statement of fiduciary net position and does not present a statement of changes in fiduciary net position.

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, 2012

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. Nonexchange 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, 2012

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.

The Component Unit's investments are stated at fair value. Investment fair values are based on quoted market prices. The majority of the investments are restricted as to use (See Note 2)

CITY OF WINCHESTER, KENTUCKY
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2012

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

ACCOUNTS RECEIVABLE – COMPONENT UNIT (WMU)

Accounts receivable - Customers, are 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, 2012, \$53,973 was written off as uncollectible.

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. Prepaid items include only insurance premiums. 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 assets. 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 business-type activities 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, 2012

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Major outlays for the component unit's (WMU) capital assets and improvements are capitalized when assets constructed are completed. Interest incurred during the construction phase of capital assets is included as part of the capitalized value of the assets constructed.

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, 2012 was \$59,709. Amortization expense for bond discount as of June 30, 2012 was \$112,536.

ACCRUED SICK LEAVE

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.

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.

CITY OF WINCHESTER, KENTUCKY
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2012

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

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 do 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 the balances are reported in the government-wide statements.

REVENUE RECOGNITION – PROPERTY TAXES - Property taxes for 2011 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 18, 2011 and were due December 1, 2011. Taxes unpaid after December 1, 2011 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 an allowance for uncollectible property taxes for 100% of delinquent accounts.

CITY OF WINCHESTER, KENTUCKY
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2012

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

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 fixed assets and contributed capital at contractor's cost.

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

WMU's 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)

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:

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 and WMU and WMU provides management services. WMU contributed \$64,782 and \$70,555 for the years ended 2012 and 2011, respectively. CCGIS had accounts payables to WMU of \$18,892 and \$0 for they years ended 2012 and 2011, respectively, for reimbursements of payroll and other expenses. CCGIS had accounts receivable from WMU of \$8,105 and \$9,282 for they years ended 2012 and 2011, respectively, for excess reimbursements of payroll and other expenses. Complete financial statements for CCGIS can be obtained from WMU's Director of Finance.

**CITY OF WINCHESTER, KENTUCKY
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2012**

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

EARLY IMPLEMENTATION OF GASB STANDARDS—The City of Winchester has elected to early implement several new GASB accounting and reporting standards as of June 30, 2012. GASB Statement No. 61 revised guidance related to the recognition of component units, but did not affect how the City recognized its component unit or other related organizations. GASB Statement No. 62 incorporated a variety of FASB standards into the GASB Codification and did not affect the accounting and reporting used by the City or WMU prior to implementation.

GASB Statement No. 63 revised certain terms used in the statements of net position to incorporate the guidance from GASB Concepts Statement 4. GASB Statement No. 65 provided the accounting guidance for recognition of deferred inflows or outflows of resources. The City expensed \$23,729 of bond issuance costs recorded in prior years to implement GASB Statement No. 65. The Component Unit (WMU) did not adopt early implementation of GASB 65 and the effect of this statement would have been a reduction of net assets of \$168,360.

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, 2012, the City is in compliance with this requirement.

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>Investment</u>	<u>Fair Value</u>	<u>Cost</u>
Money Market Mutual Fund	\$ 127,348	\$ 127,348
U.S. Government Securities	<u>1,533,645</u>	<u>1,403,742</u>
Total Investments	<u>\$ 1,660,993</u>	<u>\$ 1,531,090</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.

CITY OF WINCHESTER, KENTUCKY
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2012

NOTE 2 - DEPOSITS AND INVESTMENTS (CONTINUED)

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, 2012, the City's investments in money market mutual funds were unrated.

3. 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:

06/30/12 Type	Fair Value	Maturities (in Years)			
		< Than 1	1 - 5	6 - 10	> Than 10
Cash and Cash Equivalents	\$ 16,395,542	\$ 16,395,542	\$ 0	\$ 0	\$ 0
U.S. Treasury Obligations	3,761,653	3,761,653	0	0	0
Federal Home Loan Mtg Corp	492,688	299,528	193,160	0	0
Federal National Mtg Assn	680,407	680,407	0	0	0
Federal Home Loan Bank	220,605	0	220,605	0	0
Total	\$ 21,550,895	\$ 21,137,130	\$ 413,765	\$ 0	\$ 0

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:

06/30/12 Type	Fair Value	Ratings			
		AAA	AA	A	Unrated
Cash and Cash Equivalents	\$ 16,395,542	\$ 0	\$ 0	\$ 0	\$ 16,395,542
U.S. Treasury Obligations	3,761,653	3,761,653	0	0	0
Federal Home Loan Mtg Corp	492,688	492,688	0	0	0
Federal National Mtg Assn	680,407	680,407	0	0	0
Federal Home Loan Bank	220,605	220,605	0	0	0
Total	\$ 21,550,895	\$ 5,155,353	\$ 0	\$ 0	\$ 16,395,542

**CITY OF WINCHESTER, KENTUCKY
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2012**

NOTE 2 - DEPOSITS AND INVESTMENTS (CONTINUED)

Custodial Credit Risk

Custodial credit risk is the risk that, in the event of the failure of the counterparty, WMU will not be able to recover the value of its deposits and investments that are in possession of an outside party. WMU has no formal policy for custodial credit risk; however, as of June 30, 2012 and 2011 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.

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.

CITY OF WINCHESTER, KENTUCKY
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2012

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

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, 2012, follows:

06/30/12	Cash	Investments	Accrued Interest	Total
Restricted by Ordinance:				
Bond Redemption Account	\$ 309,500	\$ 0	\$ 0	\$ 309,500
Reserve Accounts	524,392	0	0	524,392
Depreciation Account	5,358,163	0	0	5,358,163
Subtotal	<u>6,192,055</u>	<u>0</u>	<u>0</u>	<u>6,192,055</u>
Other Restricted Accounts:				
SDC Water Fund	2,559,083	0	0	2,559,083
SDC Wastewater Fund	1,794,265	0	0	1,794,265
Customer Deposits	176,845	0	0	176,845
KIA Reserve	7,091	0	0	7,091
2011 Bond Funds	0	5,155,353	19,860	5,175,213
2008 BAN	94,537	0	0	94,537
Capital Accum-Water	147,128	0	93	147,221
Capital Accum-Wastewater	38,161	0	24	38,185
Total	<u>\$ 11,009,165</u>	<u>\$ 5,155,353</u>	<u>\$ 19,977</u>	<u>\$ 16,184,495</u>

NOTE 4 – 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	\$ 87,620	\$ 307,444	\$ 0	\$ 395,064
Land	1,986,538	0	0	1,986,538
Total Non-depreciable capital assets	<u>2,074,158</u>	<u>307,444</u>	<u>0</u>	<u>2,381,602</u>
Depreciable capital assets:				
Buildings	5,492,818	0	0	5,492,818
Vehicles	5,151,027	120,897	0	5,271,924
Computers	397,080	1,764	0	398,844
Equipment	3,118,187	476,902	0	3,595,089
Infrastructure	20,612,177	103,688	0	20,715,865
Total depreciable capital assets	<u>34,771,289</u>	<u>703,251</u>	<u>0</u>	<u>35,474,540</u>
Less accumulated depreciation				
Buildings	(1,763,832)	(241,967)	0	(2,005,799)
Vehicles	(3,242,288)	(464,416)	0	(3,706,704)
Computers	(254,286)	(28,049)	0	(282,335)
Equipment	(2,526,975)	(250,346)	0	(2,777,321)
Infrastructure	(15,733,935)	(306,043)	0	(16,039,978)
Total accumulated depreciation	<u>(23,521,316)</u>	<u>(1,290,821)</u>	<u>0</u>	<u>(24,812,137)</u>
Total depreciable capital assets, net	<u>11,249,973</u>	<u>(587,570)</u>	<u>0</u>	<u>10,662,403</u>
Governmental activities capital assets, net	<u>\$ 13,324,131</u>	<u>\$ (280,126)</u>	<u>\$ 0</u>	<u>\$ 13,044,006</u>

CITY OF WINCHESTER, KENTUCKY
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2012

NOTE 4 – PROPERTY PLANT AND EQUIPMENT (CONTINUED)

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 in total and by function follows:

<u>Function</u>	<u>2012</u>
General Government	\$ 623,507
Public Protection:	
Police	155,256
Fire Protection	278,914
EMS	120,663
Public Works	112,481
Total Depreciation Expense	\$ <u>1,290,821</u>

PROPERTY, PLANT AND EQUIPMENT - WMU

WMU's property, plant and equipment as of June 30, 2012 is as follows:

<u>06/30/12</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	12,856,597	26,940,271	(7,025,595)	32,771,273
Total Non-depreciable Assets	\$ <u>13,907,608</u>	\$ <u>296,940,271</u>	\$ <u>(7,025,595)</u>	\$ <u>33,822,284</u>
Depreciable Assets:				
Administrative	\$ 3,030,966	\$ 72,349	\$ (19,520)	\$ 3,083,795
Water System	37,499,778	1,931,060	(37,123)	39,393,715
Wastewater System	63,167,584	2,546,890	(24,263)	65,690,211
Solid Waste	5,814,764	476,552	(173,405)	6,117,911
Vehicle Maintenance	428,994	13,708	(1,722)	440,980
Equipment Capital Lease	62,004	20,923	0	82,927
Subtotal	<u>110,004,090,</u>	<u>5,061,482</u>	<u>(256,033)</u>	<u>114,809,539</u>
Accumulated Depreciation:				
Administrative	(1,199,279)	(173,371)	18,230	(1,354,420)
Water System	(9,619,472)	(875,516)	26,696	(10,468,292)
Wastewater System	(15,147,785)	(2,137,591)	22,542	(17,262,834)
Solid Waste	(1,389,023)	(259,010)	173,405	(1,474,628)
Vehicle Maintenance	(280,892)	(21,884)	1,722	(301,054)
Prior Years Accumulated	(19,230,756)	0	0	(19,230,756)
Subtotal	<u>(46,867,207)</u>	<u>(3,467,372)</u>	<u>242,595</u>	<u>(50,091,984)</u>
Total Net Property, Plant and Equipment	\$ <u>63,136,883</u>	\$ <u>1,594,110</u>	\$ <u>(13,438)</u>	\$ <u>64,717,555</u>

CITY OF WINCHESTER, KENTUCKY
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2012

NOTE 4 – PROPERTY PLANT AND EQUIPMENT (CONTINUED)

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>2012</u>
Administrative	\$ 173,371
Water System	875,516
Wastewater System	2,137,591
Solid Waste	259,010
Vehicle Maintenance	21,884
Total Depreciation Expense	<u>\$ 3,467,372</u>

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, 2012, total interest incurred was \$1,294,299, of which \$280,048 was capitalized and \$1,014,251 was expensed.

NOTE 6 - INTERFUND RECEIVABLES AND PAYABLES

Interfund receivables and payables during the year ending June 30, 2012 were as follows.

<u>Fund</u>	<u>Receivable</u>	<u>Payable</u>
General Fund	\$ 18,018	\$ -
Capital Equipment Fund	40,500	-
Special Revenue Funds	-	-
Local Grant Funds	15,324	-
State Grant Funds	-	797
Federal Grant Funds	-	73,044
Total	<u>\$ 73,841</u>	<u>\$ 73,841</u>

NOTE 7 – OPERATING LEASES

The City had three operating leases for copiers at June 30, 2012. Terms of the operating leases are as follows:

<u>Date</u>	<u>Vendor</u>	<u>Description</u>	<u>Payment</u>	<u>Months</u>	<u>Location</u>
10/13/08	IKON	Cannon 32451I (2)	\$541	48	Fire St. #1 & #3
10/22/08	IKON	Cannon IR1023IF	\$370	48	City Hall
07/01/10	Toshiba	Toshiba E-450U	\$219	36	Police Dept

CITY OF WINCHESTER, KENTUCKY
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2012

NOTE 7 – OPERATING LEASES (CONTINUED)

Rental expense for the current fiscal year was \$13,861. The future minimum payments are as follows:

<u>Year</u>	<u>Amount</u>
2013	\$2,733

NOTE 8 – FIVE YEAR CAPITAL CONSTRUCTION PLAN – COMPONENT UNIT (WMU)

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

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	40,000
Container Replacement	10,000
Replace Compactor Ejector Box	10,000
Solid Waste Recycling	15,000
Water Treatment Plant Equipment Improvements	150,000
Water System Improvements	770,000
Water Distribution:	
Main Replacement	200,000
Fire Hydrant Replacement	10,000
Gate Value Box Adjustment – New Paving	5,000
Gate Value Replacement	10,000
Elevated Storage Tank Rehabilitation	210,000
Meter Change-Out/AMR Equipment	125,000
New Meter Services	40,000
Wastewater Collection:	
Manhole Grade Adjustment	200,000
Manhole Grade Adjustment – New Paving	10,000
I&I Rehabilitation	25,000
Rehabilitation of Private Sewers	20,000
Flow Meters	5,000
Infrastructure Rehabilitation Program	25,000
System Capacity Assurance Program	18,000
Continuous Sewer System Assessment Program	7,000
Routine Hydraulic Cleaning	60,000
Wastewater Treatment Plant:	
Replacement of Laboratory Equipment	2,000
WWTP Equipment Improvements	45,000
Solids Processing Improvements	200,000
Total Annual Allocations for Infrastructure Investment	\$ 2,668,100

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

CITY OF WINCHESTER, KENTUCKY
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2012

NOTE 8 – FIVE YEAR CAPITAL CONSTRUCTION PLAN – COMPONENT UNIT (WMU)
(CONTINUED)

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	\$	60,600,000
Wastewater Utility Improvements		<u>57,821,000</u>
Total projected financing requirement	\$	<u><u>118,421,000</u></u>

NOTE 9 - CONSTRUCTION IN PROGRESS

Construction in progress at June 30, 2012 consists of the following:

Description	Balance June 30, 2011	Additions	Placed in Service	Balance June 30, 2012
Depot Street	\$ 54,620	\$ 14,955	\$ 0	\$ 69,575
Pearl Street	17,920	49,243	67,163	0
Bell Tower	0	65,465	0	65,465
US60 Traffic Signal	0	44,463	0	44,463
7 th Street	0	116,461	0	116,461
Fulton Road	15,080	84,020	0	99,100
Total	<u>\$ 87,620</u>	<u>\$ 374,607</u>	<u>\$ 67,163</u>	<u>\$ 395,064</u>

COMPONENT UNIT (WMU)

Various construction projects in progress at June 30, 2012 are as follows:

Balance June 30, 2011	Additions	Placed in Service	Balance June 30, 2012
<u>\$12,856,597</u>	<u>\$26,940,271</u>	<u>\$7,025,595</u>	<u>\$32,771,273</u>

NOTE 10 - LONG-TERM DEBT

CHANGES IN LONG-TERM DEBT

Long-term liability activity was as follows:

Describe	Beginning Balance	Additions	Deletions	Ending Balance	Due Within One Year
Capital Leases	\$ 2,318,495	\$	\$ 227,094	\$ 2,091,401	\$ 317,498
Sick Leave	634,201		15,691	618,511	
Total Governmental	<u>\$ 2,952,696</u>	<u>\$</u>	<u>\$ 242,785</u>	<u>\$ 2,709,912</u>	<u>\$ 317,498</u>

**CITY OF WINCHESTER, KENTUCKY
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2012**

NOTE 10 - LONG-TERM DEBT (CONTINUED)

CAPITAL LEASES

The City has four capital leases as of June 30, 2012. The liability for the lease obligations have been recorded in the government-wide financial statements. Details of the leases are presented below:

<u>Purpose</u>	<u>Date</u>	<u>Interest Rate</u>	<u>Term</u>	<u>Annual Payment</u>
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:

<u>Description</u>	<u>Amount</u>
Automobiles	\$ 1,063,768
Building	3,213,430
Less: Accumulated Depreciation	(820,179)
Net Value	<u>\$ 3,457,019</u>

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, 2012:

<u>Year Ending June 30,</u>	<u>Amount</u>
2013	\$ 345,741
2014	279,618
2015	250,696
2016	219,270
2017	161,921
2018-2022	689,484
2023-2027	638,346
2028-2029	278,500
Total Minimum Lease Payments	<u>2,863,576</u>
Less: Interest Payments	<u>(772,175)</u>
Present Value of Minimum Lease Payments	<u>\$ 2,091,401</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, 2012 are summarized as follows:

CITY OF WINCHESTER, KENTUCKY
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2012

NOTE 10 - LONG-TERM DEBT (CONTINUED)

Description	Rate	Maturity	Original Issue	2012 Total
2002 Issue	4.50-5.13%	07/01/32	\$ 9,025,000	\$ 0
2011 Issue	5.27%	01/01/31	9,010,000	8,676,667
2012 Issue	2.00-3.75%	07/01/32	7,495,000	7,400,000
Less: Unamort. Discount				(205,266)
Total Bonds				<u>15,871,401</u>
KIA Loan	1.00%	12/01/28 Estimate	21,000,000	17,817,272
KIA-Lower Howards Creek	2.00%	01/01/31	36,600,000	26,706,654
KIA-Ind. Storage Tanks	2.00%	12/01/30	340,326	319,231
KIA-Vaught Court	2.00%	06/01/31	287,400	263,529
Total KIA Loans				<u>45,106,686</u>
Less: Current Maturities				<u>(1,816,115)</u>
Total				<u><u>59,161,973</u></u>

The annual bond and long-term debt service requirements, as of June 30, 2012, are as follows:

Fiscal Year	Principal	Interest	Total
2013	\$ 1,796,928	\$ 788,013	\$ 2,584,941
2014	1,630,485	760,706	2,391,191
2015	1,658,899	734,333	2,393,233
2016	1,693,283	707,387	2,400,669
2017	1,719,881	679,741	2,399,621
2018-2022	9,122,944	2,911,673	12,034,617
2023-2027	10,222,203	1,873,355	12,095,558
2028-2032	6,426,810	572,562	6,999,374
	<u>\$ 34,271,433</u>	<u>\$ 9,027,770</u>	<u>\$ 43,299,204</u>

The above schedule does not include future payments towards the KIA-Lower Howards Creek financing, as this is interim financing, and payments will not be scheduled until after completion.

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).

CITY OF WINCHESTER, KENTUCKY
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2012

NOTE 10 - LONG-TERM DEBT (CONTINUED)

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.

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 estimated to be June 1, 2010 with full principal and interest payments to commence within one year of initiation of operation estimated to be 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.

**CITY OF WINCHESTER, KENTUCKY
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2012**

NOTE 10 - 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 estimated to be June 1, 2010 with full principal and interest payments to commence within one year of initiation of operation estimated to be 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.

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. As of June 30, 2012, \$26,706,654 of the total 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. 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.

Capital Lease

On May 14, 2008, the Utility entered into a capital lease agreement with Oce’ Financial Services, Inc. for a copier in the amount of \$18,169. Payments are for \$561 per month for 36 months at an interest rate of 7.00%. The capital lease was paid in full on May 28, 2011. 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 amortization of \$2,790 as of June 30, 2012.

The following presents future minimum lease payments at June 30, 2012 as follows:

	<u>06/30/13</u>	<u>06/30/14</u>	<u>Total</u>
	\$7,776	\$7,776	\$15,552
Less: Interest			1,602
Present value of Minimum Lease Payments			<u>\$13,950</u>

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

**CITY OF WINCHESTER, KENTUCKY
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2012**

NOTE 10 - LONG-TERM DEBT (CONTINUED)

Long-Term Debt consists of bonds and other indebtedness for which the changes in the years ended June 30, 2012 are as follows:

Description	Beginning	Borrowings Additions	Repayments Reductions	2012 Ending	Current
Compensated Absences	\$ 398,425	\$ 36,715	\$ 33,838	\$ 401,302	\$ 52,399
Bonds	16,206,826	7,435,931	7,771,356	15,871,401	589,980
KIA Loan	18,987,705	0	1,170,433	17,817,272	1,180,235
Capital Lease	0	20,923	6,973	13,950	6,974
KIA-Lower Howards	6,399,475	20,307,179	0	26,706,654	0
KIA-Storage Tank	333,364	0	14,133	319,231	14,417
KIA-Vaught Court	275,583	0	12,054	263,529	12,296
Total Long-Term Debt	<u>\$ 42,601,378</u>	<u>\$ 27,800,748</u>	<u>\$ 9,008,787</u>	<u>\$ 61,393,339</u>	<u>\$ 1,856,301</u>

NOTE 11 – COMPLIANCE WITH BOND ORDINANCE – COMPONENT UNIT (WMU)

The bonds and KIA loan requires 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, 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

As of June 30, 2011, Winchester Municipal Utilities was required to maintain an interest coverage ratio of 1.4 times – annual debt service requirements for bonds and 1.0 times – annual debt service requirements for bonds and KIA loans. On April 3, 2012, a new general bond ordinance was adopted and Winchester Municipal Utilities is now required 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, 2012

**NOTE 11 – COMPLIANCE WITH BOND ORDINANCE – COMPONENT UNIT (WMU)
(CONTINUED)**

	2012
Bonds:	
Income Available for Debt Service	\$ 2,801,066
Add: Depreciation	3,467,372
Subtract: Interest & Principal Payments on Bonds	0
Cash Available for Bond Debt Service	\$ 6,268,438
Maximum Debt Service on Bonds	0
Annual Debt Service on Bonds	1,407,396
Coverage Ratio	4.45
KIA:	2012
Income Available for Debt Service	\$ 2,801,066
Add: Depreciation	3,467,372
Cash Available for Debt Service	\$ 6,268,438
Annual Debt Service on all Debt	2,803,022
Coverage Ratio	2.24

The Winchester Municipal Utilities are in compliance with all of the covenants of the bond ordinance and KIA loan agreement as of June 30, 2012.

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

WMU has pledged future revenues from water, wastewater and solid waste to repay the 2002 and 2012 bonds and KIA outstanding debt referenced in Note 5. 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.

NOTE 13 – PENSION PLANS

The City participates in two separate defined benefit plans for full-time employees. The Police and Firemen'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 - POLICE AND FIREMEN'S PENSION FUND

Plan Description. The City of Winchester Police and Firemen's Pension Plan is a single-Employer defined benefit pension plan administered by the City of Winchester Police and Firemen'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 covers 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 phases out the Police and Firemen'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.

CITY OF WINCHESTER, KENTUCKY
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2012

NOTE 13 – PENSION PLANS (CONTINUED)

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 Plan's actuarial valuation was performed on July 1, 2011, 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 Firemen's Pension Board.

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

	6/30/2012	6/30/2011	6/30/2010
Annual required contribution	\$ 105,609	\$ 114,664	\$ 110,036
Interest on net pension obligation	20,754	18,645	16,353
Adjustment to annual required contribution	<u>(95,873)</u>	<u>(86,131)</u>	<u>(75,542)</u>
Annual Pension Cost	<u>30,490</u>	<u>47,178</u>	<u>50,847</u>
Contributions Made	<u>(5,000)</u>	<u>(5,000)</u>	<u>(5,000)</u>
Increase (decrease) in net pension obligation	<u>25,490</u>	<u>42,178</u>	<u>45,847</u>
Net pension obligation beginning of year	415,082	372,904	327,057
Net pension obligation end of year	<u>\$ 440,572</u>	<u>\$ 415,082</u>	<u>\$ 372,904</u>

As of June 30, 2012, the total actuarial unfunded liability was \$557,147 if retirees are granted a 3% annual cost of living adjustment. If this COLA is not implemented, assets available for benefits (\$1,689,894) exceed the actuarial liability (\$1,552,190) by \$137,704.

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, 2012 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, 2012, the plan's funded ratio was 75.2% (actuarial value of assets compared to actuarial accrued liability).

Membership Data.

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

CITY OF WINCHESTER, KENTUCKY
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2012

NOTE 13 – PENSION PLANS (CONTINUED)

The schedule of funding progress, presented as required supplementary information following the notes to the financial statements, present multi-year information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liability.

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, 2012.

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 18.96% of gross pay for regular employees and 35.76% 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, 2012, 2011 and 2010, under the current plan amounted to \$1,864,646, \$1,725,644 and \$1,633,577, respectively.

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 is developing the revised plan description documents to outline these changes. More information is available on the KRS website at <http://www.kyret.gov/>.

CITY OF WINCHESTER, KENTUCKY
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2012

NOTE 13 – PENSION PLANS (CONTINUED)

D - 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 2012, and the Retirement Systems' Board of Trustees sets the employer contribution rates, currently 18.96% for fiscal year ending 2012. 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, 2012, 2011 and 2010, under the current plan amounted to \$505,126, \$432,605 and \$407,933, respectively, which represents 100% of the required contributions.

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 for the year ended June 30, 2012.

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.

**CITY OF WINCHESTER, KENTUCKY
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2012**

NOTE 13 – PENSION PLANS (CONTINUED)

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

NOTE 14 – CONTINGENCIES

A – INDUSTRIAL DEVELOPMENT BONDS
INDUSTRIAL BUILDING REVENUE BONDS

<u>Description</u>	<u>Origination Date</u>	<u>Maturity Date</u>	<u>Outstanding Balance</u>
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 in direct negotiations with counsel for the firefighters in the Clark Circuit case. 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, 2012. It is recorded in the government-wide financial statements as part of accrued payroll and related liabilities.

NOTE 15 – WMU – LANDFILL POST-CLOSURE COSTS

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.

**CITY OF WINCHESTER, KENTUCKY
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2012**

NOTE 15 – WMU – LANDFILL POST-CLOSURE COSTS (CONTINUED)

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. WMU expects that permit limits will be relaxed in the coming months allowing monthly costs to return to what would be considered normal for this operation.

NOTE 16 – WMU – ECONOMIC DEPENDENCY

WMU is economically dependent for revenues from the following four entities:

Name	2012
Sekisui	\$ 727,684
Alltech	556,451
The Kroger Company	492,413
East Clark County WD	270,307
	\$ 2,046,855

NOTE 17 – COMMITMENTS

As of June 30, 2012, WMU had several uncompleted construction contracts. The remaining commitment on these construction contracts was approximately \$10,005,918 financed with KIA loans.

NOTE 18 – RISK MANAGEMENT

The City and its component unit (WMU) is 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 and its component unit (WMU) 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.

**CITY OF WINCHESTER, KENTUCKY
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2012**

NOTE 18 – RISK MANAGEMENT (CONTINUED)

Fiscal Year Ended June 30,	Claims Payable July 1,	Claims and Changes in Estimates	Claims Paid	Claims Payable June 30,
2012	\$ 221,300	\$ 1,093,578	\$ 1,216,878	\$ 98,000
2011	\$ 178,000	\$ 1,216,214	\$ 1,172,914	\$ 221,300

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 (\$12,647) and shared revenues (\$620,503) from the Commonwealth of Kentucky. Committed fund balance includes amounts set aside by the City Commission for special projects (\$270,636) and capital acquisitions (\$2,008,769). The City Commission is the highest level of decision-making authority of the City. Assigned fund balance includes balances (\$49,703) 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 \$26,857 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 2012, the City spent \$28,500.

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 2012.

Winchester/Clark County Planning & Zoning	\$ 9,568
Winchester/Clark County Parks & Recreation	250,000
Clark County/Winchester Heritage Commission	12,000
Winchester/Clark County Recreation	55,000
Winchester/Clark County Industrial Development Authority	94,500
Winchester/Clark County Board of Adjustment	1,500
Clark County GIS	70,029
 Total Contributions	 <u>\$ 492,596</u>

REQUIRED SUPPLEMENTARY INFORMATION

**CITY OF WINCHESTER, KENTUCKY
POLICE AND FIREFIGHTERS PENSION FUND
REQUIRED SUPPLEMENTARY INFORMATION
FOR THE YEAR ENDED JUNE 30, 2012**

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

1. SCHEDULES OF FUNDING PROGRESS

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial 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

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%

3. NOTES TO REQUIRED SUPPLEMENTARY INFORMATION

Valuation Date	7/1/2010
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, 2012

	MUNICIPAL AID FUND	LOCAL GOVERNMENT ECONOMIC ASSISTANCE FUND	ROOM TAX FUND	ADMINISTRATION SPECIAL PROJECTS FUND	MAINSTREETS 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	\$ 574,447	\$ 55,259	\$ 2	\$ 38,595	\$ 68,505	\$ 57,486	\$ 67,834	\$ 10,905	\$ 12,617	\$ 12,647	\$ 898,297
Accounts Receivable	24,417	0	0	0	0	0	0	0	0	797	25,214
Due from Other Funds	0	0	0	0	0	0	0	0	15,324	0	15,324
TOTAL ASSETS	\$ 598,864	\$ 55,259	\$ 2	\$ 38,595	\$ 68,505	\$ 57,486	\$ 67,834	\$ 10,905	\$ 27,940	\$ 13,445	\$ 938,835
LIABILITIES:											
Accounts Payable	\$ 33,623	\$ 0	\$ 0	\$ 39	\$ 25	\$ 0	\$ 0	\$ 0	\$ 564	\$ 0	\$ 34,252
Due to Other Funds	0	0	0	0	0	0	0	0	0	797	797
TOTAL LIABILITIES	33,623	0	0	39	25	0	0	0	564	797	35,049
FUND BALANCES:											
Restricted Fund Balance	565,241	55,259	2	0	0	0	0	0	0	12,647	633,150
Committed Fund Balance	0	0	0	38,556	68,480	57,486	67,834	10,905	27,376	0	270,636
TOTAL FUND BALANCES	565,241	55,259	2	38,556	68,480	57,486	67,834	10,905	27,376	12,647	903,786
TOTAL LIABILITIES AND FUND BALANCES	\$ 598,864	\$ 55,259	\$ 2	\$ 38,595	\$ 68,505	\$ 57,486	\$ 67,834	\$ 10,905	\$ 27,940	\$ 13,445	\$ 938,835

CITY OF WINCHESTER, KENTUCKY
 COMBINING STATEMENT OF REVENUES, EXPENDITURES
 AND CHANGES IN FUND BALANCES
 NONMAJOR GOVERNMENTAL FUNDS
 FOR THE YEAR ENDED JUNE 30, 2012

	MUNICIPAL AID FUND	LOCAL GOVERNMENT ECONOMIC ASSISTANCE FUND	ROOM TAX FUND	ADMINISTRATION SPECIAL PROJECTS FUND	MAINSTREETS 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	\$ 109,894	\$ 176	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0	\$ 110,071
Intergovernmental	606,910	26,857	0	5,200	0	13,662	11,783	0	15,400	5,747	685,558
Investment Income	3,711	435	67	282	358	425	453	66	155	184	6,137
Other	0	0	820	1,378	32,337	9,077		8,413	3,883	0	55,907
TOTAL REVENUES	<u>610,621</u>	<u>27,292</u>	<u>110,782</u>	<u>7,036</u>	<u>32,695</u>	<u>23,164</u>	<u>12,236</u>	<u>8,480</u>	<u>19,438</u>	<u>5,931</u>	<u>857,673</u>
EXPENDITURES:											
Main Street Department	0	0	0	1,225	11,135	0	0	0	0	5,747	18,107
Planning	0	0	0	5,400	0	0	0	0	0	0	5,400
Police Department	0	0	0	0	0	17,201	3,480	0	9,784	0	30,465
Fire Department	0	0	0	0	0	0	0	6,381	0	0	6,381
Public Works	291,500	28,500	0	0	0	0	0	0	0	0	320,000
Intergovernmental	0	0	110,782	0	0	0	0	0	0	0	110,782
Capital	249,725	0	0	0	0	0	0	0	0	36,525	286,250
TOTAL EXPENDITURES	<u>541,224</u>	<u>28,500</u>	<u>110,782</u>	<u>6,625</u>	<u>11,135</u>	<u>17,201</u>	<u>3,480</u>	<u>6,381</u>	<u>9,784</u>	<u>42,272</u>	<u>777,385</u>
Excess (Deficit) of Revenues over Expenditures	69,396	(1,208)	0	410	21,560	5,963	8,756	2,099	9,653	(36,341)	80,288
OTHER FINANCING SOURCES (USES):											
Operating Transfers In	0	0	0	0	0	0	0	0	0	0	0
Operating Transfers Out	0	0	0	0	0	0	0	0	0	0	0
TOTAL OTHER FINANCING SOURCES (USES):	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>
Excess (Deficit) of Revenues and Other Financing Sources over Expenditures and Other Financing Uses	69,396	(1,208)	0	410	21,560	5,963	8,756	2,099	9,653	(36,341)	80,288
Fund Balance June 30, 2011	495,844	56,468	2	38,146	46,919	51,523	59,078	8,806	17,723	48,989	823,498
Fund Balance June 30, 2012	<u>\$ 565,241</u>	<u>\$ 55,259</u>	<u>\$ 2</u>	<u>\$ 38,556</u>	<u>\$ 68,480</u>	<u>\$ 57,486</u>	<u>\$ 67,834</u>	<u>\$ 10,905</u>	<u>\$ 27,376</u>	<u>\$ 12,647</u>	<u>\$ 903,786</u>

**CITY OF WINCHESTER, KENTUCKY
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED JUNE 30, 2012**

<u>Federal Grantor/Pass-Through Grantor/ Program Title</u>	<u>Federal CFDA Number</u>	<u>Grant Number</u>	<u>Federal Expenditures</u>
<u>HOUSING & URBAN DEVELOPMENT</u>			
Passed Through Commonwealth of Kentucky:			
Community Development Block Grant	14.228	09-066	\$ 555,714
Community Development Block Grant	14.228	10-126	600,000
TOTAL HOUSING & URBAN DEVELOPMENT			<u>1,155,714</u>
<u>U.S. DEPT. OF TRANSPORTATION</u>			
Passed Through Commonwealth of Kentucky :			
Traffic Safety Program	20.600	OP-11-28	1,772
Depot Street- ARRA	20.205	PO2-628-1000004390	11,964
TOTAL U.S. DEPT. OF TRANSPORTATION			<u>13,736</u>
<u>U.S. DEPT. OF JUSTICE</u>			
Enforce Underage Drinking Laws	16.727	2010-AH-FX-0093-CC	40,258
TOTAL U.S. DEPT. OF JUSTICE			<u>40,258</u>
<u>EPA</u>			
Passed Through Commonwealth of Kentucky:			
Pollution Control	66.460	C9994861-04	74,431
Wastewater Revolving Loan Program	66.458	A10-03	3,227,241
TOTAL EPA			<u>3,301,672</u>
<u>FEDERAL EMERGENCY MANAGEMENT AGENCY</u>			
FEMA Equipment Grant	97.039	HMGP DR-1818-0049	60,727
TOTAL FEMA			<u>60,727</u>
<u>HOMELAND SECURITY</u>			
Passed Through Commonwealth of Kentucky:			
Homeland Security Grant	97.067	BERT 10-219	239,689
Homeland Security Grant	97.067	KOHS Project 11-257	40,959
TOTAL HOMELAND SECURITY			<u>280,648</u>
TOTAL FEDERAL FINANCIAL ASSISTANCE			<u>\$ 4,852,755</u>

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 federal awards to subrecipients as follows:

#66.458	Wastewater Revolving Loan Program	\$3,227,241
#14.228	Community Development Block Grant	\$1,155,714

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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1961-1992

**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 the financial statements of the governmental 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, 2012, which collectively comprise the City of Winchester, Kentucky's basic financial statements and have issued our report thereon dated January 25, 2013. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

Management of City of Winchester, Kentucky, is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered City of Winchester, Kentucky's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of City of Winchester, Kentucky's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the City of Winchester, Kentucky's internal control over financial reporting.

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

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. We consider the deficiency described in the accompanying schedule of findings and questioned costs to be a material weakness. (2012-02)

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. We consider the deficiency described in the accompanying schedule of findings and questioned costs to be a significant deficiency. (2012-01)

Compliance and Other Matters

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

We noted a certain matter that we reported to management of City of Winchester, Kentucky, in a separate letter dated January 25, 2013.

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

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

Summers, McCrary & Sparks, PSC

Lexington, KY

January 25, 2013

SUMMERS, MCCRARY & SPARKS, P.S.C.
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INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE WITH REQUIREMENTS
THAT COULD HAVE A DIRECT AND MATERIAL EFFECT ON EACH MAJOR PROGRAM AND
ON INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-
133

To the City Commissioners
City of Winchester, Kentucky

Compliance

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, 2012. 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. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs is the responsibility of City of Winchester, Kentucky's management. Our responsibility is to express an opinion on City of Winchester, Kentucky's compliance based on our audit.

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

In our opinion, City of Winchester, Kentucky, complied, in all material respects, with the 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, 2012.

Management of City of Winchester, Kentucky, is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered City of Winchester Kentucky's internal control over compliance with the requirements that could have a direct and material effect on a major federal program to determine the auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133, 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, KY'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.

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 deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses, as defined above.

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

Summers, McCrary & Sparks, PSC

Lexington, Kentucky

January 25, 2013

CITY OF WINCHESTER, KENTUCKY

SCHEDULE OF FINDINGS AND QUESTIONED COSTS For the Year Ended June 30, 2012

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 and one material weakness disclosed during the audit of the financial statements are reported in the "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*."
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 with Requirements that could have a Direct and Material Effect on each Major Program and on Internal Control over Compliance in accordance with OMB Circular A-133". No material weaknesses were 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 program tested as a major program includes: CFDA #14.228 Community Development Block Grants/State's program and Non-Entitlement Grants; 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:

2012-01: Purchase Orders

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

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

Cause: The City's purchasing employees are overriding this internal control.

Effect: Potential exists for a department to exceed budget.

Recommendation: We recommend management review purchase order procedures with each purchasing employees and their importance as an internal control.

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.

MATERIAL WEAKNESS:

2012-02: Budget

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

Criteria: Cities are required under KRS 91.030 to adopt a budget which is sufficient to cover current year expenditures.

Cause: The City did not obtain the federal grant budget from its component unit who is the subrecipient of the pass through federal grant.

Effect: The City's budget was not sufficient to cover actual expenditures.

Recommendation: The City should communicate with its subrecipient for the current year budget of federal grants and adopt this amount in its federal grant budget. The City should contact the subrecipient throughout the year for any budget amendments.

Management Response and Corrective Action: The City will contact subrecipient and include in this year's budget and going forward.

FINDINGS AND QUESTIONS COSTS – MAJOR FEDERAL AWARD PROGRAMS

NONE