HOPKINSVILLE ELECTRIC SYSTEM

OF THE

CITY OF HOPKINSVILLE, KENTUCKY

FINANCIAL STATEMENTS

FOR THE YEARS ENDED

JUNE 30, 2013 AND 2012

HOPKINSVILLE ELECTRIC SYSTEM
OF THE
CITY OF HOPKINSVILLE, KENTUCKY

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INDEPENDENT AUDITORS' REPORT

The Board of the
Hopkinsville Electric System of the
City of Hopkinsville, Kentucky
Hopkinsville, Kentucky

Report on the Financial Statements

We have audited the accompanying financial statements of the Hopkinsville Electric System of the City of Hopkinsville, Kentucky as of and for the years ended June 30, 2013 and 2012, and the related notes to the financial statements, which collectively comprise the System's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

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

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

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

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Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Hopkinsville Electric System of the City of Hopkinsville, Kentucky as of June 30, 2013 and 2012, and the respective changes in financial position, and cash flows thereof for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 4–14 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information

Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise the Hopkinsville Electric System of the City of Hopkinsville, Kentucky's basic financial statements. The introductory section and the accompanying financial information listed as supplementary information is presented for purposes of additional analysis and is not a required part of the basic financial statements.

The accompanying financial information listed as supplementary information is the responsibility of management and is derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the accompanying financial information listed as supplementary information is fairly stated in all material respects in relation to the basic 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.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated November 20, 2013, on our consideration of the Hopkinsville Electric System of the City of Hopkinsville, Kentucky's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Hopkinsville Electric System of the City of Hopkinsville, Kentucky's internal control over financial reporting and compliance.

Kem, Duguid & Associates, P.S.C.
Kem, Duguid & Associates, P.S.C.
Certified Public Accountants
Hopkinsville, Kentucky

November 20, 2013

MANAGEMENT'S DISCUSSION AND ANALYSIS

HOPKINSVILLE ELECTRIC SYSTEM
OF THE
CITY OF HOPKINSVILLE, KENTUCKY
MANAGEMENT'S DISCUSSION AND ANALYSIS
JUNE 30, 2013

The management of Hopkinsville Electric System of the City of Hopkinsville (HES, the "System") offers Management's Discussion and Analysis to provide an overview and analysis of the System's financial activities for the year ended June 30, 2013. To fully understand the entire scope of the System's financial activities, this information should be read in conjunction with the financial statements provided in this document.

FINANCIAL HIGHLIGHTS

- The assets of HES exceeded its liabilities at the close of the 2013 fiscal year by $21,105,879 (*net position*). Of this amount, $1,353,828 (*unrestricted net position*) may be used to meet the System's ongoing obligations to citizens and creditors.

- The System's total net position increased by $623,607 during the period. This increase was primarily due to a mild winter coupled with a full year of seasonal demand and energy wholesale costs.

- Total operating revenues for the 2013 fiscal year increased by $515,296 or about 1.38% compared to the previous period.

- FY 2013 operating expenses totaled $36,541,681 which was $41,881 or about .11% more than the previous year's amount.

OVERVIEW OF THE FINANCIAL STATEMENTS

The discussion and analysis is intended to serve as an introduction to the Electric System's basic financial statements. The System's basic financial statements are comprised of two components: (1) basic financial statements and (2) notes to basic financial statements. The basic financial statements and notes to these statements reflect the combined accounts and activities of both the electric and broadband divisions. The report also contains other supplementary information in addition to the basic financial statements. The supplementary information section contains statements that show the results of operations for the separate divisions.

REQUIRED FINANCIAL STATEMENTS

The financial statements of the System report information utilizing the full accrual basis of accounting. This method of accounting recognizes revenues when earned instead of when received and recognizes expenses when incurred rather than when paid. The financial statements conform to accounting principles which are generally accepted in the United States of America.

Statement of Net Position

The Statement of Net Position includes information on the System's assets and liabilities, with the difference between the two reported as net position. Over time, increases and decreases in net position may serve as a useful indicator of whether the financial position of the System is improving or deteriorating.

Statement of Revenues, Expenses and Changes in Net Position

While the Statement of Net Position provides information about the nature and amount of resources and obligations at year-end, the Statement of Revenues, Expenses and Changes in Net Position presents the results of the System's operations over the course of the operating cycle. This statement can be used to determine whether the System has successfully recovered all of its actual costs including depreciation through user fees and other charges. All changes in net position are reported during the period in which the underlying event giving rise to the change occurs, regardless of the timing of the related cash flows. Thus, revenues and expenses are reported in this statement for some items that will result in cash flows in future fiscal periods, such as delayed collection of operating revenues and delayed payment of current year expenses.

Statement of Cash Flows

The Statement of Cash Flows provides information on the System's cash receipts, cash payments, and net changes in cash resulting from operations, investing, and financing activities. From the Statement of Cash Flows, the reader can obtain information on the source and use of cash and the change in the cash balance for the operating cycle.

Financial Analysis of the Fiscal Year Ended June 30, 2013

Over the past year, total assets of the System increased by $651,190 while total liabilities increased by $27,583. And for the current period, the operating income of the System totaled $623,607. Operating revenues include $639,275 from Electric and ($15,668) from Telecommunications.

Condensed Statements of Net Position

The Statement of Net Position, shown in tabular format below, represents information on all of the System's assets and liabilities with the difference between the two reported as net position. The System's total net position increased from the prior year by $623,607 or about 3.04% for the period.

Our analysis that follows focuses on the System's net position (shown in Table 1) and the changes in net position (shown in Table 2) during the year.

TABLE 1
Condensed Statements of Net Position

	Fiscal Year		Change in FY 2012 to FY 2013	
	2013	2012	Amount	Percent
Current and other assets	$ 11,052,512	$ 10,692,314	$ 360,198	3.37%
Capital assets	31,996,189	31,705,197	290,992	0.92%
Total assets	43,048,701	42,397,511	651,190	1.54%
Current liabilities	8,586,809	8,540,045	46,764	0.55%
Long-term liabilities	13,356,013	13,375,194	(19,181)	-0.14%
Total liabilities	21,942,822	21,915,239	27,583	0.13%
Invested in utility plant, net of related debt	18,752,048	18,396,264	355,784	1.93%
Restricted for capital projects	1,000,003	-	1,000,003	100.00%
Restricted for debt service	-	268,841	(268,841)	-100.00%
Unrestricted	1,353,828	1,817,167	(463,339)	-25.50%
Total net position	$ 21,105,879	$ 20,482,272	$ 623,607	3.04%

Analysis of Net Position

To better understand the System's actual financial positions and its ability to deliver services in future periods, the reader will need to review the various components of the net position category and obtain an understanding of how each relate specifically to the business activities that we perform. For example, the vast majority of net position ($18,752,048 or 88.84% of total net assets) represents investment in plant assets, which is the lifeblood to the provision of electric and telecommunication services.

	Fiscal Year		Change FY 2012 to FY 2013	
	2013	2012	Amount	Percent
Invested in capital assets, net of related debt	$ 18,752,048	$ 18,396,264	$ 355,784	1.93%
Restricted for capital projects	1,000,003	-	1,000,003	100.00%
Restricted for debt service	-	268,841	(268,841)	-100.00%
Unrestricted	1,353,828	1,817,167	(463,339)	-25.50%
	$ 21,105,879	$ 20,482,272	$ 623,606	3.04%

For the 2013 fiscal year, *Net Position Invested in Capital Assets, Net of Related Debt* increased by $355,785 or 1.93% compared to the previous year. The amount shown in this category is calculated by taking the depreciated value of our capital assets and subtracting the associated bond debt. The significance of this increase on future operations is that it represents additional equity that the System has accumulated in its plant, equipment and infrastructure.

In comparing the total amount of *Restricted Net Position* with the previous fiscal year, there was a decrease of $268,841 or 100%. The components of this category consists of the 1998A Sinking Fund and other Debt Service Funds. The 1998A bond was paid in full during FY 2013. Restricted for capital projects increased by $1,000,003 as a result of the 2013 bond issue.

Compared to the prior year's balance, there was a decrease in the *Unrestricted Net Position* category of $463,339 or 25.50%.

Unrestricted net position consists of net position that does not meet the definition of "restricted" or "invested in capital assets, net of related debt".

Analysis of Current Assets

The textbook definition of "current assets" is balance sheet items which equal the sum of cash and cash equivalents, accounts receivable, inventory, marketable securities, prepaid expenses, and other assets that could be converted to cash in less than one year. Current assets are important in any financial analysis because it is from current assets that a business funds its ongoing, day-to-day operations. A comparison of the June 30, 2013 and 2012 balances by asset classification is shown in the table below.

TABLE 3
Comparison of Current Assets

	Fiscal Year		Change from FY 2012 to FY 2013	
	2013	2012	Amount	Percent
Cash and cash equivalents	$ 2,679,750	$ 2,800,789	$ (121,039)	-4.32%
Accounts receivable (net)	2,972,282	2,763,415	208,867	7.56%
Unbilled revenue	1,081,499	1,062,236	19,263	1.81%
Inventories	774,032	785,277	(11,245)	-1.43%
Prepaid expenses	78,454	95,365	(16,911)	-17.73%
Other	70,527	135,913	(65,386)	-48.11%
	$ 7,656,544	$ 7,642,995	$ 13,549	0.18%

Analysis of Noncurrent Assets

Noncurrent assets represent assets that are not reasonably expected to be realized in cash or sold or consumed during the next fiscal year. When making the distinction between whether an asset should be considered current or noncurrent, liquidity or nearness to cash is not the proper basis for determining the classification. In making this determination, any encumbrances on the use of the asset must be considered. Thus, cash investments intended for liquidation or liabilities due beyond the one-year period are noncurrent assets, as would assets segregated or restricted for the liquidation of long-term debts (including amounts due within the next operating cycle). Assets designated to be used to acquire, construct, or improve capital assets would also be noncurrent.

In the following table, the Noncurrent Assets of the System at June 30, 2013 and 2012 are compared to major classification. As indicated by the tabular information, total noncurrent assets increased by $637,641 or 1.83% during the 2013 fiscal year.

TABLE 4
Comparison on Noncurrent Assets

	Fiscal Year		Change from FY 2012 to FY 2013	
	2013	2012	Amount	Percent
Restricted:				
Investments - special funds	$ 2,035,250	$ 1,721,020	$ 314,230	18.26%
Investment in affiliated organization	75,423	10,116	65,307	86.59%
Nonutility property	33,958	33,958	-	0.00%
Deferred charges	1,251,337	1,284,225	(32,888)	-2.56%
Capital assets (net)	31,996,189	31,705,197	290,992	0.92%
	$ 35,392,157	$ 34,754,516	$ 637,641	1.83%

The table above demonstrates the relatively large investment that the System has made in capital assets. At the end of the 2013 fiscal year, capital assets represented about 90.40% of the noncurrent assets.

In examining the balance for the Restricted Noncurrent Assets category at June 30, 2013, it shows a increase of $314,230 or 18.26% compared to the previous fiscal year.

Analysis of Liabilities

In financial accounting, the term "liability" is defined as an obligation of an entity arising from past transactions or events, the settlement of which may result in the transfer or use of assets, provision of services or other yielding of economic benefits in the future. To put it in more simplistic terms, this section analyzes the various claims that creditors have against the System's assets.

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TABLE 5
Comparison of Current Liabilities from Unrestricted Net Position

	Fiscal Year		Change From FY 2012 to FY 2013	
	2013	2012	Amount	Percent
Accounts payable - purchased power	$ 2,650,358	$ 5,060,594	$ (2,410,236)	-47.63%
Accounts payable - other	2,314,435	128,543	2,185,892	1700.51%
Customer deposits	1,558,029	1,432,786	125,243	8.74%
Accrued taxes	372,706	380,447	(7,741)	-2.03%
Accrued interest	-	12,640	(12,640)	-100.00%
Unearned pole rental	(79,214)	66,613	(145,827)	-218.92%
Deferred revenue - MuniNet	135,405	-	135,405	100.00%
Line of credit	200,000	-	200,000	100.00%
Other current and accrued liabilities	477,487	383,165	94,322	24.62%
	$ 7,629,206	$ 7,464,788	$ 164,418	2.20%

Current Liabilities Payable from Unrestricted Assets had a net increase in its various components of $164,418 or about 2.20% compared to the previous fiscal year's balance. Of that amount, $200,000 line of credit was outstanding and $135,405 deferred revenue – MuniNet was present (Note 17).

As the reader of the financial statements might surmise from the preceding discussion, an argument can certainly be made that the System's financial position has indeed improved over that of the previous year. Management feels that each of the positive indicators discussed above speak to the continued financial viability of the System's operations.

As indicated in Table 6, the change in net position for the fiscal year ended June 30, 2013 was $623,607.

TABLE 6
Condensed Statements of Revenues, Expenses and Changes in Net Position

	Fiscal Year		Change From FYE 2012 To FYE 2013	
	2013	2012	Amount	Percent
Operating revenues:				
Electric revenues	$ 35,728,517	$ 35,460,165	$ 268,352	0.76%
Telecom revenues	2,251,514	2,004,570	246,944	12.32%
Total operating revenues	37,980,031	37,464,735	515,296	1.38%
Operating expenses:				
Purchased power	27,797,919	28,145,277	(347,358)	-1.23%
Other expenses	8,743,762	8,354,523	389,239	4.66%
Total operating expenses	36,541,681	36,499,800	41,881	0.11%
Net operating income	1,438,350	964,935	473,415	49.06%
Non-operating income, net	(814,743)	(356,632)	(458,111)	128.45%
Change in net position	623,607	608,303	15,304	2.52%
Net position, beginning of year	20,482,272	19,873,969	608,303	3.06%
Net position, end of year	$ 21,105,879	$ 20,482,272	$ 623,607	3.04%

Analysis of Revenue

For the 2013 fiscal year, the *Operating Revenues* of the System totaled $37,980,031. This amount represented an increase of 1.38% more than the previous year's total of $37,464,735. The increase was due to a mild winter coupled with a full year of seasonal demand and energy wholesale costs.

Included in the *Non-Operating Revenues (net)* is interest income of $30,083, interest expense of $321,654, amortization expense of $9,981and other expense of $513,191. The implementation of a full-system change out to electric meters caused the disposal of all existing meters resulting in an offset of revenue of $595,811 which is included in other expense of $513,191.

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JUNE 30, 2013

Analysis of Expenses

The *Total Operating Expenses* for FY 2013 were $36,541,681. That amount represents an increase of $41,881 or about .11% more than the prior fiscal year total of $36,499,800. The eight major categories of Operating Expenses are shown in the chart below.

TABLE 7
Comparison of Operating Expenses

	Fiscal Year		Change from FY 2012 to FY 2013	
	2013	2012	Amount	Percent
Cost of power	$ 27,797,919	$ 28,145,277	$ (347,358)	-1.23%
Cost of sales - telecom	194,383	198,317	(3,934)	-1.98%
Distribution:				
operation	1,541,649	1,379,986	161,663	11.71%
maintenance	953,281	855,061	98,220	11.49%
Transmission - maintenance	1,975	777	1,198	100.00%
Customer accounts	680,099	709,529	(29,430)	-4.15%
Sales	128,827	112,067	16,760	14.96%
Administrative and general	2,144,140	2,066,362	77,778	3.76%
Depreciation	1,580,561	1,497,886	82,675	5.52%
Taxes	1,518,847	1,534,538	(15,691)	-1.02%
	$ 36,541,681	$ 36,499,800	$ 41,881	0.11%

As indicated by the comparative information presented above, *Cost of Power* decreased by $347,358 or 1.23% compared to the prior year.

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets

Hopkinsville Electric System's investment in capital assets as of June 30, 2013 was $31,996,189 (net of accumulated depreciation), as shown in the following table.

TABLE 8
Schedule of Capital Assets (Net of Depreciation)

	Fiscal Year 2013	Fiscal Year 2012	Increase (Decrease)
Land	$ 425,717	$ 425,715	$ -
Construction in progress-			
Electric	5,026,629	4,319,609	707,020
Telecommunications	250,779	729,761	(478,982)
Transmission plant	382,215	383,143	(928)
Distribution plant	12,920,975	13,581,362	(660,387)
General plant	1,472,447	1,601,530	(129,083)
Telecommunications plant	11,517,427	10,664,077	853,350
Total capital assets	$ 31,996,189	$ 31,705,197	$ 290,990

Additional detailed information concerning the System's capital assets can be found in Note 2 in the notes to the financial statements.

Long-term Debt

At June 30, 2013, the System had roughly $13.2 million in debt outstanding, a decrease of $64,792 or approximately .49% less than the previous fiscal year. The System's debt is comprised of various bonds and notes. A comparative schedule at June 30, 2013 and 2012 is shown in the tabular information provided below.

TABLE 9

	Fiscal Year 2013	Fiscal Year 2012	Increase (Decrease)
Revenue bond	$ -	$ 510,000	$ (510,000)
KY League of Cities leases	10,244,141	10,047,125	197,016
KIA loan	3,000,000	2,751,808	248,192
	$ 13,244,141	$ 13,308,933	$ (64,792)

Additional detailed information concerning the System's liabilities can be found in the notes to the financial statements, Note 8.

Economic Factors

Although the System had a healthy income margin this year, the future financial condition of the System will be affected by two factors in the future: weather conditions and the length of the current recession. Weather is a tremendous driver in kWh sales – extreme hot conditions and extreme cold conditions will drive up kWh sales and mild temperatures drive down usage.

Also affecting the System's financial condition is the recent change to Seasonal Demand and Energy rates put in place by TVA. These rates were implemented April 1, 2011. TVA is trending toward all utilities being billed under Time-of-Use (TOU) rates. When this will be mandatory is still a huge question. HES moved forward with installing new electronic metering system to accommodate TOU rates, eliminate manual meter reading, connection/disconnect of service and provide better information to customers on energy volume.

HES EnergyNet continues to gain high speed broadband customers. Because of expenditures for expanding this year, annual net income was negative $15,668 for the year but should be positive in the long run.

As we demonstrate financial responsibility, we continue to strive to deliver the highest quality of services to our community at the lowest feasible cost.

REQUESTS FOR INFORMATION

This financial report is designed to provide a general overview of the Hopkinsville Electric System's finances for all those with an interest in the System's finances. Questions or requests for additional information may be addressed to Austin Carroll, Manager, Hopkinsville Electric System, 1820 East Ninth Street, Hopkinsville, KY 42240.

FINANCIAL STATEMENTS

HOPKINSVILLE ELECTRIC SYSTEM
OF THE
CITY OF HOPKINSVILLE, KENTUCKY
STATEMENTS OF NET POSITION
JUNE 30, 2013 AND 2012

ASSETS

	2013	2012
Utility plant	$ 48,264,566	$ 47,054,779
Less accumulated depreciation	16,268,377	15,349,582
Net utility plant	31,996,189	31,705,197
Restricted assets		
Investments - special funds	2,035,250	1,721,020
Other assets		
Investment in affiliated organizations	75,423	10,116
Nonutility property	33,958	33,958
	109,381	44,074
Current assets		
Cash - general funds	2,679,750	2,800,789
Accounts receivable (less accumulated provision for uncollectible accounts of $28,995 in 2013 and $28,289 in 2012)	2,972,282	2,763,415
Unbilled revenue	1,081,499	1,062,236
Inventories (at weighted-average cost)	774,032	785,277
Prepaid expenses	78,454	95,365
Other current assets	70,527	135,913
Total current assets	7,656,544	7,642,995
Deferred charges	1,251,337	1,284,225
Total assets	43,048,701	42,397,511

See accompanying notes to financial statements

HOPKINSVILLE ELECTRIC SYSTEM
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STATEMENTS OF NET POSITION, continued
JUNE 30, 2013 AND 2012

LIABILITIES

	2013	2012
Current liabilities		
Current maturities of long-term debt	957,603	1,075,257
Accounts payable - purchased power	2,650,358	5,060,594
Accounts payable - other	2,314,435	128,543
Customer deposits	1,558,029	1,432,786
Accrued taxes	372,706	380,447
Accrued interest	-	12,640
Unearned pole rental	(79,214)	66,613
Deferred revenue - MuniNet	135,405	-
Line of credit	200,000	-
Other current & accrued liabilities	477,487	383,165
Total current liabilities	8,586,809	8,540,045
Noncurrent liabilities		
Long-term debt	12,286,538	12,233,676
Advances from others:		
Conservation advances - TVA	1,069,475	1,141,518
Total noncurrent liabilities	13,356,013	13,375,194
Total liabilities	21,942,822	21,915,239
NET POSITION		
Invested in capital assets, net of related debt	18,752,048	18,396,264
Restricted for capital projects	1,000,003	-
Restricted for debt service	-	268,841
Unrestricted	1,353,828	1,817,167
Total net position	$ 21,105,879	$ 20,482,272

See accompanying notes to financial statements

HOPKINSVILLE ELECTRIC SYSTEM
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CITY OF HOPKINSVILLE, KENTUCKY
STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET POSITION
FOR THE YEARS ENDED JUNE 30, 2013 AND 2012

	2013	2012
OPERATING REVENUES	$ 37,980,031	$ 37,464,735
OPERATING EXPENSES		
Cost of power	27,797,919	28,145,277
Cost of sales - telecommunications	194,383	198,317
Distribution - operation	1,541,649	1,379,986
- maintenance	953,281	855,061
Transmission - maintenance	1,975	777
Customer accounts	680,099	709,529
Sales	128,827	112,067
Administrative and general	2,144,140	2,066,362
Depreciation	1,580,561	1,497,886
Taxes	1,518,847	1,534,538
Total operating expenses	36,541,681	36,499,800
Net operating revenues	1,438,350	964,935
NONOPERATING REVENUES (EXPENSES)		
Interest on long-term debt	(297,020)	(333,543)
Other interest	(24,634)	(46,118)
Amortization of debt expense	(9,981)	(9,980)
Interest income	30,083	32,255
Other revenue (expenses)	(513,191)	754
Net nonoperating revenues (expenses)	(814,743)	(356,632)
CHANGE IN NET POSITION	623,607	608,303
NET POSITION, BEGINNING OF YEAR	20,482,272	19,873,969
NET POSITION, END OF YEAR	$ 21,105,879	$ 20,482,272

See accompanying notes to financial statements

HOPKINSVILLE ELECTRIC SYSTEM
OF THE
CITY OF HOPKINSVILLE, KENTUCKY
STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED JUNE 30, 2013 AND 2012

	2013	2012
Cash flows from operating activities		
Receipts from customers and users	$ 37,817,287	$ 37,948,965
Payments to suppliers	(30,728,034)	(31,472,771)
Payments to employees	(2,678,151)	(2,125,847)
Payments of taxes	(1,526,588)	(1,542,528)
Net cash provided (used) by operating activities	2,884,514	2,807,819
Cash flows from capital financing activities		
Expenditures for utility plant	(2,737,847)	(2,303,540)
Net cost of retiring plant	843,163	(74,755)
Principal payments on long-term debt	(1,367,984)	(1,029,602)
Conservation advances from TVA	(72,043)	2,950
Proceeds from debt issuance	1,303,192	513,961
Bond issue cost from issuance of costs	(55,000)	-
Proceeds from line of credit	200,000	-
Interest paid	(322,303)	(376,747)
Net cash provided (used) by capital financing activities	(2,208,823)	(3,267,733)
Cash flows from investing activities		
Conservation loan receivable	65,919	(2,170)
Investment in affiliated companies	(65,307)	(10,116)
Purchases/maturities of investments	(314,230)	1,054,525
Interest and other revenues	(483,112)	33,009
Net cash provided (used) by investing activities	(796,730)	1,075,248
Net increase (decrease) in cash	(121,039)	615,334
Cash, beginning of year	2,800,789	2,185,455
Cash, end of year	$ 2,679,750	$ 2,800,789

See accompanying notes to financial statements

HOPKINSVILLE ELECTRIC SYSTEM
OF THE
CITY OF HOPKINSVILLE, KENTUCKY
STATEMENTS OF CASH FLOWS, continued
FOR THE YEARS ENDED JUNE 30, 2013 AND 2012

	2013	2012
Reconciliation of operating income to net cash provided by operating activities:		
Net operating revenues	$ 1,438,350	$ 964,935
Adjustments to reconcile net operating revenues to net cash provided by operating activities:		
Depreciation	1,603,692	1,530,924
Changes in assets and liabilities:		
Receivables	(208,867)	399,403
Unbilled revenues	(19,263)	155,484
Materials and supplies	11,245	(20,850)
Prepaid expenses and other current assets	82,297	(81,174)
Accounts payable	(224,344)	(464,408)
Accrued taxes	(7,741)	(7,990)
Other current and accrued liabilities	94,322	11,947
Unearned pole rental	(145,827)	66,613
Customer deposits	125,245	252,935
Deferred revenue - MuniNet	135,405	-
Total adjustments	1,446,164	1,842,884
	$ 2,884,514	$ 2,807,819

See accompanying notes to financial statements

NOTES TO FINANCIAL STATEMENTS

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Financial Reporting Entity

The Electric Plant Board of the City of Hopkinsville (d.b.a. Hopkinsville Electric System) was created by Ordinance No. 382, passed June 2, 1942, pursuant to authority conferred upon the City by Chapter 119 of the General Assembly of Kentucky, 1932, amended.

The Board was established for the purpose of owning and operating all properties, real, personal, and mixed tangible or intangible, acquired or used or held for use, in connection with the electric plant acquired by purchase from Kentucky – Tennessee Light and Power Company.

The Board consists of four appointed members, the term of one expiring each year, and a fifth member from the City's governing body, presently represented by Wesley Grimes, a member of the Common Council. The Hopkinsville Electric System elects its own officers and management.

Basis of Presentation and Accounting

The records of the Board are maintained in accordance with provisions of the power contract with the Tennessee Valley Authority, and are consistent with requirements of the Federal Energy Regulatory Commission's system of accounts. Revenues and expenses are recognized on the accrual basis.

Proprietary Fund Type

The Board is intended to be self-supporting through user charges. All of its revenues, expenses, assets, and liabilities, including fixed assets and long-term debt associated with the specific activity, are accounted for within its financial statements.

Proprietary funds are used to account for activities similar to those found in the private sector, where the determination of net income is necessary or useful to sound financial administration. Proprietary funds distinguish operating revenues and expenses from nonoperating items. Operating revenues and expenses result from providing services and delivering goods in connection with the fund's principle ongoing operations such as charges to customers for sales and services and expenses such as salaries, product costs, administrative expenses, and depreciation. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

Use of Estimates

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

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, continued

Cash and Cash Equivalents

For the purposes of the statements of cash flows, the System considers all highly liquid debt instruments purchased with a maturity of three months or less to be cash equivalents.

Material and Supplies Inventory

Material and supplies inventory (which consists of wire, poles, and other supplies) is valued at cost determined by the weighted-average method.

Utility Plant

Utility plant is stated at original cost, which includes payroll related costs such as taxes, fringe benefits, and administrative and general costs. Interest expense incurred during a construction period is capitalized. Construction work in progress has been included in the rate base for determining retail customer rates. The System has not recorded any significant allowance for funds used during construction.

When property subject to depreciation is retired or otherwise disposed of in the normal course of business, its original cost, together with its cost of removal less salvage, is charged to the accumulated provision for depreciation. The System charges maintenance and repairs, including the cost of renewals of minor items of property, to maintenance expense accounts or applicable clearing accounts. Placements of property (exclusive of minor items of property) are capitalized to utility plant accounts.

Depreciation

Property and equipment in plant accounts are recorded at cost with depreciation being computed at rates recommended by the Tennessee Valley Authority. The rates used throughout the current year were consistent with those in use in the prior year.

Compensated Absences

Full-time employees are allowed to carryover a maximum of forty (40) hours accumulated annual leave. Upon retirement from Hopkinsville Electric System, the employee is entitled to payment for unused accumulated annual leave time. Accrued vacation leave was $386,896 and $283,959 for the years ended June 30, 2013 and 2012, respectively.

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, continued

Impairment of Capital Assets

In accordance with GASB Statement No. 42, *Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries*, management evaluates prominent events or changes in circumstances affecting capital assets to determine whether impairment of a capital asset has occurred. A capital asset is generally considered impaired if both (a) the decline in service utility of the capital asset is large in magnitude, and (b) the event or change in circumstance is outside the normal life cycle of the capital asset. No impairment losses were recognized in the years ended June 30, 2013 and 2012.

Revenues and Expenses

Revenues and expenses are distinguished between operating and non-operating items. Operating revenues generally result from providing services, producing, and delivering goods in connection with the System's principal ongoing operations. The principal operating revenues of the System 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.

Net Position

Net position is categorized as invested in capital assets (net of related debt), restricted, and unrestricted and further described as follows.

- *Invested in Capital Assets, Net of Related Debt* - This category groups all capital assets including infrastructure into one component of net position. Accumulated depreciation and the outstanding balances of debt that are attributed to the acquisition, construction or improvement of these assets reduce the balance in this category.

- *Restricted* - This category represents those assets which have constraints placed on the expenditures either externally imposed or imposed by law or enabled by legislature.

- *Unrestricted* - This category presents the net position of the Board not included elsewhere.

When both restricted and unrestricted resources are available for use, it is the System's policy to use restricted resources first, then unrestricted resources as they are needed.

Income Tax Status

The System is exempt from federal and state income taxes. Accordingly, the financial statements include no provision for such taxes.

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, continued

Subsequent Events

Subsequent events have been evaluated through November 20, 2013, which is the date the financial statements were available to be issued.

Implementation of Accounting Policies

In 2013, the Board adopted GASB Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources and Net Position (GASB 63)* and GASB Statement No. 65, *Items Previously Reported as Assets and Liabilities (GASB 65).* The objective of these Statements is to provide guidance for reporting deferred outflows of resources, deferred inflows of resources, and net position in a statement of financial position (net assets/balance sheet). Amounts that are required to be reported as deferred outflows should be reported in a statement of net position in a separate section following assets. Similarly, amounts required to be reported as deferred inflows of resources should be reported in a separated section following liabilities. The statement of net position should report the residual amount as net position, rather than net assets or equity. GASB 63 and 65 were implemented retroactively. The adoption of these statements resulted in a change in the presentation of the Statement of Net Assets to net position.

In March 2012, the GASB issued Statement 66, *Technical Corrections – 2012 – an amendment of GASB Statements No. 10 and No. 62*. GASB 66 improves accounting and financial reporting for a governmental financial reporting entity by resolving conflicting guidance that resulted from the issuance of two pronouncements, Statements No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions, and No. 62, Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*. This Statement is effective for periods beginning after December 15, 2012 although the District elected to early implement Statement 62 in fiscal year 2013. The adoption of GASB 66 does not have any impact on the System's financial statements.

In June 2012, the GASB issued Statement 67, *Financial Reporting for Pension Plans – an amendment of GASB Statement 25.* GASB 67 improves financial reporting by state and local governmental pension plans. The requirements of this Statement will improve financial reporting primarily through enhanced note disclosures and schedules of required supplementary information that will be presented by the pension plans that are within its scope. This Statement is effective for financial statements for fiscal years beginning after June 15, 2013. Management is currently evaluating the impact of the adoption of this statement on the System's financial statements.

In June 2012, the GASB issued Statement 68, *Accounting and Financial Reporting for Pensions – an amendment of GASB Statement 27.* GASB 68 improves accounting and financial reporting by state and local governments for pensions. It also improves information provided by state and local governmental employers about financial support for pensions that is provided by other entities. This Statement results from a comprehensive review of the effectiveness of existing standards of accounting and financial reporting for pensions with regard to providing decision-useful information, supporting assessments of accountability and inter-period equity, and creating additional transparency. This Statement is effective for fiscal years beginning after June 15, 2014. Management is currently evaluating the impact of the adoption of this statement on the System's financial statements.

NOTE 2 – UTILITY PLANT AND DEPRECIATION PROCEDURES

A summary of changes in major classifications of the utility plant in service is as follows:

	Balance June 30, 2012	Additions	Reclassifications/ Retirements	Balance June 30, 2013
Utility plant not depreciated:				
Land	$ 425,715	$ -	$ -	$ 425,715
Construction in progress - electric	4,319,609	707,020	-	5,026,629
Construction in progress - telecommunications	729,761	-	478,964	250,797
Total utility plant not depreciated	5,475,085	707,020	478,964	5,703,141
Utility plant depreciated:				
Transmission plant	640,884	14,565	4,819	650,630
Distribution plant	22,146,832	502,606	1,054,414	21,595,024
General plant	5,067,253	109,264	29,871	5,146,646
Telecommunications plant	13,724,725	1,883,356	438,956	15,169,125
Total utility plant depreciated	41,579,694	2,509,791	1,528,060	42,561,425
Accumulated depreciation	(15,349,582)	(1,603,692)	684,897	(16,268,377)
Total utility plant depreciated, net	26,230,112	906,099	843,163	26,293,048
Total utility plant	$ 31,705,197	$ 1,613,119	$ 1,322,127	$ 31,996,189

Transmission Plant depreciation rates have been applied on a straight-line basis and are as follows:

Towers and fixtures	2.00%
Poles and fixtures	3.00

NOTE 2 – UTILITY PLANT AND DEPRECIATION PROCEDURES, continued

Provision has been made for depreciation of Distribution Plant on a straight-line basis and rates are as follows:

Station equipment	4.00%
Poles, towers, and fixtures	4.00
Overhead conductors and devices	1.75
Underground equipment	4.00
Line transformers	2.00
Services	5.25
Meters	2.00
Security lighting	6.00
Street lighting and signal systems	3.75

General Plant depreciation rates have been applied on a straight-line basis and are as follows:

Structures and improvements	3.00%
Office furniture	VAR
Transportation equipment	25.00
Laboratory equipment	8.00

Transactions through the Accumulated Provision for Depreciation account for the years ended June 30, 2013 and 2012 are summarized as follows:

	2013	2012
Accumulated provision for depreciation, July 1	$ 15,349,582	$ 14,166,804
Add:		
Depreciation charged directly to expense	1,509,040	1,426,364
Depreciation charged to transportation - clearing	94,652	104,560
Subtotal	16,953,274	15,697,728
Deduct:		
Original cost of plant retired	1,222,536	273,391
Cost of removal less salvage	(537,639)	74,755
Total charges against provision	684,897	348,146
Accumulated provision for depreciation, June 30	$ 16,268,377	$ 15,349,582

NOTE 3 – INVESTMENTS – SPECIAL FUNDS

Investments - Special Funds at June 30 consisted of:

	2013	2012
Operation and maintenance fund	$ 700,000	$ 700,000
Revenue bond sinking fund	-	148,833
Debt service reserve fund	-	120,008
Depreciation reserve fund	-	356,020
2007 Telecom bond issue fund	244,505	244,480
Savings account - BB&T	90,742	90,595
Construction fund	-	61,084
Construction fund - Series 2013	1,000,003	-
Total investments - special funds	$ 2,035,250	$ 1,721,020

Excess monies in the above funds have been invested in certificates of deposit at local banks and in trust for short-term U.S. Government securities.

The operation and maintenance fund, established by the bond ordinance, is a reserve for extraordinary costs of operating and maintaining the plant over and above ordinary operation and maintenance.

In order to provide for the payment of the Debt Service on the Series 1998-A bonds, the Revenue Bond Sinking Fund was established. The total amount required in the Sinking Fund was $113,890 for the 1998-A bonds at June 30, 2012. The 1998-A bond was paid in full as of June 30, 2013.

The Debt Service Fund was established for security in the event monies on deposit in the sinking fund are insufficient to pay principal and interest when due on the Series 1998-A bonds. The bond ordinance required the reserve fund to accumulate “an amount equal to not less than the maximum amount of principal and interest requirements falling due in any twelve-month period on all of the outstanding bonds or such lesser amount equal to 10% of the principal amount issued of all bonds.” At June 30, 2012, the required reserve balance was $51,000. The actual reserve balance was $120,008 resulting in an overfunding of $69,008 in the reserve fund. The 1998-A bond was paid in full FY 2013.

The existence of the Depreciation Reserve Fund is in accordance with the 1998-A bond ordinance, which established a fund “to provide monies which will be available for necessary and anticipated renewals, replacements, extensions, improvements, acquisitions and additions to the Plant”. The ordinances call for $71,200 to be set aside each fiscal year until the sum of $356,000 is reached. At June 30, 2012, this requirement was met and no additional deposits were needed. The 1998-A bond was paid in full FY 2013.

At year end, the amount of total investments held in banks was $2,035,250, all of which was covered by collateral held in safekeeping by agents of the respective banks or by government backed securities.

NOTE 3 – INVESTMENTS - SPECIAL FUNDS, continued

The System has invested Other Special Funds in repurchase agreements with local banks. Securities investments that the company has the positive intent and the ability to hold to maturity are classified as held-to-maturity securities and are recorded in investments and other assets at amortized cost, which approximates fair value.

Included in total investments of $2,035,250 are the following held-to-maturity investments. The remaining funds of $1,335,250 are invested in cash equivalents.

	Cost	Fair Value	Unrealized Gain	Unrealized Loss
Held-to-maturity securities repurchase agreements	$ 700,000	$ 700,000	$ -	$ -

Investment income included in the Statement of Revenues and Expenditures is summarized as follows:

	2013	2012
Listed	$ 29,980	$ 31,872
Deposits	103	383
	$ 30,083	$ 32,255

Interest Rate Risk

The System does not have a formal investment policy that limits its investment maturities as a means of managing its exposure to losses arising from changes in interest rates. In general, certificates of deposit are not subject to interest rate risk.

Custodial Credit Risk

Under Kentucky Revised Statutes Section 66.480, the System is authorized to invest in obligations of the United States and its agencies and instrumentalities, obligations and contracts for future delivery or purchase of obligations backed by the full faith and credit of the United States or of its agencies, obligations of any corporation of the United States government, certificates of deposit, commercial paper rated in one of the three highest categories by nationally recognized rating agencies and shares in mutual funds. For an investment, custodial credit risk is the risk that, in the event of the failure of the counterparty, the System will not be able to recover the value of its investments held in possession of an outside party. The System does not have an investment policy that would further limit its investment choices. In general, certificates of deposit are not subject to investment credit risk.

NOTE 4 – CASH - GENERAL FUND

The carrying amounts are reflected in the financial statements as follows:

	2013	2012
Change funds	$ 1,750	$ 1,750
Checking accounts	2,676,750	2,797,711
TVA power bill early payment	-	78
Other	1,250	1,250
Total	$ 2,679,750	$ 2,800,789

<u>Custodial Credit Risk</u>

Custodial credit risk is the risk that, in the event of a depository institution failure, the System's deposits may not be returned to it. The System does not have a policy regarding custodial credit risk for deposits.

State law requires collateralization of all deposits with federal depository insurance; bonds and other obligations of the U.S. Treasury, U.S. agencies or instrumentalities of the State of Kentucky; bonds of any city, county, school district or special road district of the State of Kentucky; bonds of any state; or a surety bond having an aggregate value at least equal to the amount of deposits.

At June 30, 2013, the Board's deposits in depository institutions had a carrying amount of $2,676,750 and bank balances of $2,692,280. At June 30, 2013, the deposits were covered entirely by FDIC insurance or a properly executed collateral security agreement. At June 30, 2012, the System's deposits in depository institutions had a carrying amount of $2,797,711 and bank balances of $2,849,141. At June 30, 2012, the deposits were covered entirely by FDIC insurance or a properly executed collateral security agreement.

NOTE 5 – RECEIVABLES

Net receivables include the following at June 30:

	2013	2012
Accounts Receivable		
Electric	$ 2,856,276	$ 2,733,249
	2,856,276	2,733,249
Other Receivables		
Employee appliance/computer loans	9,660	21,393
FEMA receivable	-	25,597
Other miscellaneous	135,341	11,465
	145,001	58,455
Total Receivables	3,001,277	2,791,704
Less: Reserve for Uncollectible Accounts	(28,995)	(28,289)
Total	$ 2,972,282	$ 2,763,415

Electric accounts and miscellaneous accounts together with the current billing for home insulation, heat pump, and wood burning stove loans, were aged as follows:

	June 30, 2013		June 30, 2012	
	Amount	Percent	Amount	Percent
Accounts Having Discount Dates After June 30	$ 2,795,612	93.15	$ 2,572,470	92.15
Accounts With Credit Balances	-	-	-	-
Accounts Less Than One Month Past Due	-	-	-	-
Accounts 31 to 60 Days Past Due	106,578	3.55	92,308	3.31
Accounts 61 to 90 Days Past Due	25,515	1.10	17,570	0.63
Accounts Over 90 Days Past Due	73,572	9.86	109,356	3.92
	$ 3,001,277	107.66	$ 2,791,704	100.00

NOTE 5 – RECEIVABLES, continued

A reserve for uncollectible electric accounts is maintained by means of monthly charges to operations. Lists of accounts considered to be worthless are charged to the reserve account annually, with the last such list having been prepared as of June 30, 2013. Accounts charged off are turned over to various agencies for collection as authorized by HES.

A summary of the reserve's transactions for each year is as follows:

	2013	2012
Beginning balance	$ 28,289	$ 25,915
Monthly additions and adjustments	85,770	96,749
Charge-off of bad accounts	(93,700)	(96,788)
Recoveries	8,636	2,413
Balance, June 30	$ 28,995	$ 28,289

NOTE 6 – MATERIAL AND SUPPLIES

The values of electric materials at balance sheet dates were ascertained by reference to perpetual inventory records. Hopkinsville Electric System personnel make physical counts of stock at the end of each year and adjust the perpetual inventory records to actual count. The adjustment to the general ledger control is made to bring it into conformity with perpetual stock records. This amount is charged against stores expense (clearing) in January of each year. The positive (negative) adjustments required were ($6,665) and ($4,940) as of June 30, 2013 and 2012, respectively.

NOTE 7 – DEFERRED CHARGES

Deferred Charges at June 30 consisted of:

	2013	2012
Deferred costs on bond issue-2004	$ 19,009	$ 22,385
Deferred costs on bond issue-2007	100,632	110,611
Deferred costs on bond issue - 2013 KLC	53,167	-
Unamortized debt discount-1998	-	4,116
Unamortized debt discount-2007	26,880	29,545
Customers energy conservation loans-TVA	1,051,649	1,117,568
Total	$ 1,251,337	$ 1,284,225

NOTE 8 – BONDED INDEBTEDNESS

On August 1, 1999, the System issued Series 1998-A revenue bonds in the amount of $2,945,000 for the purpose of refunding certain outstanding obligations and improving its electric plant distribution system. Payments of interest are paid semi-annually and payments of principal are paid annually with the last principal payment scheduled for February 1, 2014. The debt is secured by revenues of the electric system. The bond was paid in full during FY 2013.

On January 27, 2004, the System entered into a lease with Kentucky League of Cities Funding Trust to fund an electric substation/transformer. Payments of principal and interest are paid monthly with the last principal payment scheduled for February 15, 2019. The interest rate is 3.45 percent. This debt is secured by the property.

On August 1, 2008, the System entered into a lease with Kentucky League of Cities Funding Trust in the amount of $10,189,560 for refunding of the $4,000,000 Electric Revenue Bond Anticipation Notes, Series 2007A and $6,000,000 Electric Revenue Bond Anticipation Notes, Series 2007B. The proceeds of the notes were used to acquire improvements to the electric plant and distribution system, including broadband and telecommunications improvements and to pay issuance costs of the obligations. Payments of principal and interest are paid monthly with the last principal payment schedule for August 1, 2023. The lease is to bear interest at a rate of 3.62% per annum. The debt is secured by revenues of the electric system. Interest paid on the 2007 bonds is capitalized during the construction phase. Capitalized interest for each year is $183,161 and $195,999 for June 30, 2013 and 2012, respectively.

On February 1, 2008, the System entered into a loan agreement with Kentucky Infrastructure Authority in the amount of $3,000,000 to assist in funding the construction of a fiber optic communication line from Hopkinsville, Kentucky to Bowling Green, Kentucky. The loan is to bear interest at 0.7% semi-annually. Interest payment dates for the loan are December 1 or June 1 succeeding the first draw which is at least three months, but no more than nine months, after the first draw. Principal payments will commence on June 1 or December 1 immediately succeeding the date of the last draw of funds. The loan is for ten years. The debt is secured by revenues of the telecommunications system. As of June 30, 2013, the System has received $3,000,000 in loan draws. The project was completed in the fiscal year 2013. Upon completion of the project, the loan will be converted to a permanent loan.

On February 14, 2013, the System entered into a lease agreement with Kentucky Bond Corporation in the amount of $1,055,000 for system upgrades and enhancements for various projects. Monthly payments are made into the Debt Service Fund for principal retirement, interest payment and fees. The interest rate is 2 percent. Debt is secured with the pledge of net revenues set forth in existing bond resolutions.

NOTE 8 – BONDED INDEBTEDNESS, continued

The changes in outstanding debt are as follows:

	Balance July 1, 2012	New Issues	Debt Payments and Refunds	Balance June 30, 2013
Series 1998-A	$ 510,000	$ -	$ 510,000	$ -
KY League of Cities-Series 2004	1,836,294	-	248,724	1,587,570
Kentucky Infrastructure Authority	2,751,808	248,192	-	3,000,000
KY League of Cities - Series 2007	8,210,831	-	576,533	7,634,298
Revenue Bond, Series 2013A	-	1,055,000	32,727	1,022,273
	$ 13,308,933	$ 1,303,192	$ 1,367,984	$ 13,244,141

Accrued interest on the 1998-A bonded indebtedness represents the liability for the periods from February 1, the last payment date, to June 30. The accrued interest for year end June 30, 2012 was $12,640. The 1998-A bond was paid in full FY 2013.

In accordance with the bond ordinance for Series 1998-A, the net revenues, as adjusted, of the System for any fiscal year are to equal at least 1.10 times the maximum annual debt service due in any fiscal year on the outstanding bonds; and that rates will be adjusted so as to produce the necessary revenues. The 1998-A bond was paid in full FY 2013.

The discount associated with the issuance of the revenue bonds payable is being amortized on the straight-line method over the term of the bonds. The amount charged to interest expense for the year ending June 30 follows:

	2013	2012
Series 1998-A	$ 4,117	$ 2,816
Series 2004	3,120	3,120
Series 2007	2,666	2,666
	$ 9,903	$ 8,602

NOTE 8 – BONDED INDEBTEDNESS, continued

The cost of issuance associated with the issuance of the revenue bonds payable is being amortized on the straight-line method over the term of the bonds. Amortization charged to expense for the year ending June 30 follows:

	2013	2012
Series 2004	$ 256	$ 256
Series 2007	9,980	9,980
Series 2013	1,833	-
	$ 12,069	$ 10,236

The following represents principal and interest payments on outstanding debt (excluding the $3,000,000 KIA loan. The entire $3,000,000 has been received as of June 30, 2013. The repayment schedule is expected to be finalized during FY 2014.):

	Series 2004 Principal	Series 2004 Interest	Series 2004 Total	Series 2007 Principal	Series 2007 Interest	Series 2007 Total
2014	$ 257,698	$ 66,402	$ 324,100	$ 603,048	$ 336,896	$ 939,944
2015	266,997	55,201	322,198	631,409	308,986	940,395
2016	253,031	67,280	320,311	660,575	279,872	940,447
2017	310,214	8,069	318,283	692,427	249,294	941,721
2018	296,955	19,247	316,202	724,559	217,300	941,859
2019	202,675	5,716	208,391	758,608	183,789	942,397
2020	-	-	-	793,985	148,760	942,745
2021-2024	-	-	-	2,769,687	220,528	2,990,215
	$ 1,587,570	$ 221,915	$ 1,809,485	$ 7,634,298	$ 1,945,425	$ 9,579,723

	Series 2013A Principal	Series 2013A Interest	Series 2013A Total	All Series Combined Principal	All Series Combined Interest	All Series Combined Total
2014	$ 96,857	$ 22,603	$ 119,460	$ 957,603	$ 425,901	$ 1,383,504
2015	95,000	20,543	115,543	993,406	384,730	1,378,136
2016	97,084	18,643	115,727	1,010,690	365,795	1,376,485
2017	100,000	16,702	116,702	1,102,641	274,065	1,376,706
2018	102,084	14,702	116,786	1,123,598	251,249	1,374,847
2019	105,000	12,660	117,660	1,066,283	202,165	1,268,448
2020	107,084	10,473	117,557	901,069	159,233	1,060,302
2021-2024	319,164	16,067	335,231	3,088,851	236,595	3,325,446
	$ 1,022,273	$ 132,393	$ 1,154,666	$ 10,244,141	$ 2,299,733	$ 12,543,874

NOTE 9 – ADVANCES FROM OTHERS

Advances have been received from Tennessee Valley Authority for the purpose of making long-term loans to electric customers under various energy conservation programs. The balances due Tennessee Valley Authority were $1,069,475 and $1,141,518 as of June 30, 2013 and 2012, respectively.

NOTE 10 – SHORT TERM DEBT

At June 30, 2013, the System had a $200,000 line of credit balance. The line of credit bears a variable rate of the bank's prime rate plus .250%. Accrued interest is paid monthly with one final payment of all remaining principal and accrued interest due March 4, 2015.

NOTE 11 – PENSION PLANS

<u>County Employee Retirement System</u>

Plan Description: Effective August 1, 1988, the Board and the employees elected to discontinue participation in the "Electric Plant Board of the City of Hopkinsville Retirement Plan" and participate in the statewide County Employees' Retirement System (CERS) as provided under Section 78.530 of the Kentucky Revised Statutes. The County Employees' Retirement System, a component unit of the Commonwealth of Kentucky (CERS), is a cost-sharing multiple-employer defined benefit plan. The CERS provides retirement and disability benefits, annual cost-of-living adjustments, medical insurance, and death benefits to Plan members and beneficiaries. Under the provisions of the Kentucky Revised Statutes Section 61.645, the Board of Trustees of Kentucky Retirement Systems administers the CERS and has the ability to establish and amend benefit provisions. The CERS issues a publicly available financial report that includes financial statements and required supplementary information. CERS' report may be obtained by writing to Kentucky Retirement Systems, Perimeter Park West, 1260 Louisville Road, Frankfort, KY 40601-6124 or by calling (502) 564-5656.

Funding Policy: CERS plan members who began participating before September 1, 2008 are required to contribute 5% of their covered salary. Members who began participating on or after September 1, 2008 are required to contribute 6% of their covered salary. The System is required to contribute to the CERS at an actuarially determined rate. The current rate is 19.55% of annual covered payroll. For those employees hired before June 1, 1994, the Hopkinsville Electric System Board elected to pay the entire contribution up to 12.68%. The System's contributions to CERS for the years ending June 30, 2013, 2012 and 2011 were $548,201, $543,433 and $425,951, respectively, equal to the required contributions for the year.

<u>Medical Insurance Plan</u>

Plan Description – In addition to the pension benefits described above, Kentucky Revised Statute 61.702 requires the CERS to provide post-retirement healthcare benefits to eligible members and dependents. The CERS medical insurance benefit is a cost-sharing multiple employer defined benefit plan. Changes made to the medical plan may be made by the Board of Trustees of Kentucky Retirement Systems, the Kentucky Department of Employee Insurance and the General Assembly.

NOTE 11 – PENSION PLANS, continued

Funding Policy – The post-retirement healthcare provided by CERS is financed on a pay-as-you-go basis. In order to fund the post-retirement healthcare benefit, one and five tenths percent (1.5%) of the gross annual payroll of all active members is contributed. One-half (1/2) of this amount is derived from member contributions and one-half (1/2) from state appropriation. Also, the premiums collected from retirees as described in the plan description and investment interest help with the medical expenses of the plan.

<u>System's Thrift Plan</u>

Plan Description – The System's employees hired after September 1, 1969 have the option to participate in the System's Thrift Plan, which consists of a 401K plan and a 401M plan.

Funding Policy – Employees who participate in the Plan may contribute up to 100% (in multiples of 1%) of their base annual compensation. Employees who elect to also participate in the 401M plan are limited to 14% in their contributions. All such amounts were deposited with the trustee, Manulife, Clarksville, Tennessee, to be held or invested in accordance with provisions in the Thrift Plan Trust Agreement executed November 24, 1969. Employer contributions, which totaled $91,907 and $95,667 in the years ended June 30, 2013 and 2012, respectively, are charged monthly to plant and expense in the same ratio as payroll.

NOTE 12 – OTHER CURRENT AND ACCRUED LIABILITIES

Following is a summary of the amounts recorded as other current and accrued liabilities as of June 30, 2013 and 2012:

	2013	2012
Accrued pole rentals	$ 31,080	$ 42,563
Accrued payroll	59,511	56,643
Compensated absences	386,896	283,959
	$ 477,487	$ 383,165

NOTE 13 – COMMITMENTS

Under its wholesale power agreement, dated April 20, 1982, the System is committed to purchase its electric power and energy requirements from the Tennessee Valley Authority (TVA). As provided by amendment dated October 1, 1997, the contract may be terminated by either party at any time upon not less than five years prior written notice. Neither party shall exercise its right to give notice of termination before the date occurring five years after the date of the agreement. The rates paid for such purchases are subject to change periodically by the supplier. As provided by amendment effective October 1, 1999, the System has a decreasing term contract beginning on that date. The term decreases one year each year until the term levels off at five years.

NOTE 14 – RISK MANAGEMENT AND LITIGATION

The System is exposed to various risks of loss related torts; theft of, damage to and destruction of assets; errors and omissions; injuries to employees and natural disasters. The System carries commercial insurance for the risks of loss, including worker's compensation, and property and casualty loss insurance. Settled claims resulting from these risks have not exceeded commercial insurance coverage in any of the past three fiscal years. Limits of insurance coverage remain unchanged in the past three years.

From time to time, the System is party to various pending claims and legal proceedings. Although the outcome of such matters cannot be forecast with certainty, it is the opinion of management and legal counsel that the likelihood is remote that any such claims or proceedings will have a material adverse effect on the System's financial statements.

NOTE 15 – CONSTRUCTION WORK IN PROGRESS

The balances of construction work in progress – electric were $5,026,629 and $4,319,609 as of June 30, 2013 and 2012, respectively. Included in the June 30, 2013 balance is $4,637,305 for the automated meter infrastructure project.

The balances of construction work in progress – telecommunications were $250,797 and $729,761 as of June 30, 2013 and 2012, respectively.

NOTE 16 – RATE INCREASE

Wholesale Base Rates: In April 2011, the Tennessee Valley Authority changed its wholesale rate calculation from one based on actual Retail Customer Usage to one based on Demand and Energy metered at the wholesale delivery point. This resulted in decreased costs during FY 2012. However, the full effect of demand and energy rates is uncertain for the future.

Fuel Cost Adjustment: In October 2009, TVA changed from a quarterly FCA to monthly FCA. In April 2011, TVA separated its fuel cost, which had been included in its Base Rates prior to the implementation of the quarterly FCA in October 2007, and started to include it in its monthly FCA.

Environmental Charge: In October 2003, TVA added a charge to its wholesale rates to recover its cost to add equipment to its generation facilities to meet government environmental standards. The charge is a fixed amount and is $0.00186 per kWh under the new Demand and Energy rate structure. The charge will automatically expire in September 2013.

Retail Adder: The System's margin is provided by a Retail Adder. The System's adder has not been changed since July 2010.

The System implemented a rate increase effective May 1, 2013.

NOTE 17 – MUNINET

MuniNet Fiber Agency ("MuniNet") was formed to undertake the financing, acquisition, construction, management, operation, utilization and ownership of fiber network projects and any and all facilities, including all equipment, structures, machinery, and tangible and intangible property, real or personal, useful for such projects, either within or without the Commonwealth of Kentucky. Projects are approved by the MuniNet Board on a project-specific basis. After a project is approved, MuniNet and the individual MuniNet members who desire to participate in the project enter into a Project Participation Agreement which sets forth the terms and conditions of the project's development and operation and establishes each participant's rights and obligations with respect to the project.

MuniNet Project 2 ("Project 2") consists of the development of a fiber optic cable system and a contractual arrangement for a connection to an Internet Access Provider (IAP) located in Nashville, Tennessee that will provide each project participant with high speed access to the internet. The estimated cost of Project 2 is $3,173,049.

On April 30, 2013, the Board signed a Resolution approving the Project 2 Participation Agreement among the Board, MuniNet and the other Project 2 participants. Hopkinsville Electric System is one of seven (7) Kentucky public utility companies who are participants in Project 2. Each participant in Project 2 ("Participant") has a one-seventh (1/7) interest in the project ("Project Share").

MuniNet obtained a loan from the Kentucky Infrastructure Authority in the amount of $3,200,000 to finance the development, construction and equipping of Project 2.

The Superintendent/General Manager of each participant appoints one representative to the Project Management Committee and one alternate, either or both of whom, may be employees of the Participant The Superintendent/General Manager of the participant may appoint himself as the representative or alternate to the Project Management Committee.

Costs and expenses associated with financing, development, equipping, maintenance and operation of Project 2, including debt service, will be paid from the revenue generated from the project. In the event the revenue generated from Project 2 is insufficient to pay the full amount of the costs and expenses associated with the project as they come due, each participant will be responsible for its Project Share of the deficit.

Hopkinsville Electric System has provided MuniNet with an indefeasible right of use (IRU) for fibers on the System's existing fiber system. MuniNet has agreed to pay Hopkinsville Electric System for its provision of an IRU in such fibers in the amount of $270,809. The amount is to be amortized over a 20 year term with no interest. During fiscal year June 30, 2013, $135,404 is recorded as a receivable. Amortization expense for the current fiscal year was $-0-.

MuniNet bills each participant monthly indicating the amount payable for its project share of payment obligations due under the Project Participation Agreement. In addition, MuniNet bills each participant administrative and operating costs which will be expensed. The Board paid $3,145 for administrative and operating costs during fiscal year June 30, 2013.

NOTE 17 – MUNINET, continued

The following are costs incurred for the initial investment in MuniNet and Project 2 costs:

Initial investment	$ 5,000
Project 2 Investment in Muninet	
Beginning balance July 1, 2012	5,115
Program revenue	
Costs incurred	94,365
Less MuniNet reimbursements	(29,057)
	70,423
Ending balance June 30, 2013	$ 75,423

SUPPLEMENTARY INFORMATION

HOPKINSVILLE ELECTRIC SYSTEM
OF THE
CITY OF HOPKINSVILLE, KENTUCKY
COMBINED SCHEDULE OF REVENUES, EXPENSES AND CHANGES IN NET POSITION
FOR THE YEAR ENDED JUNE 30, 2013

	ELECTRIC	TELECOM	TOTAL
OPERATING REVENUES	$ 35,728,517	$ 2,251,514	$ 37,980,031
OPERATING EXPENSES			
Cost of power	27,797,919	-	27,797,919
Cost of sales - telecom	-	194,383	194,383
Distribution - operation	849,894	691,755	1,541,649
- maintenance	930,993	22,288	953,281
Transmission - maintenance	1,975	-	1,975
Customer accounts	650,691	29,408	680,099
Sales	94,200	34,627	128,827
Administrative and general	1,680,626	463,514	2,144,140
Depreciation and amortization	1,033,107	547,454	1,580,561
Taxes	1,378,951	139,896	1,518,847
Total operating expenses	34,418,356	2,123,325	36,541,681
Net operating revenues	1,310,161	128,189	1,438,350
NONOPERATING REVENUES (EXPENSES)			
Interest on long-term debt	(156,791)	(140,229)	(297,020)
Other interest	(24,634)	-	(24,634)
Amortization of debt expense	(6,288)	(3,693)	(9,981)
Interest income	30,018	65	30,083
Other income (expenses)	(513,191)	-	(513,191)
Total nonoperating revenues (expenses)	(670,886)	(143,857)	(814,743)
CHANGE IN NET POSITION	639,275	(15,668)	623,607
NET POSITION - BEGINNING OF YEAR	21,652,051	(1,169,779)	20,482,272
NET POSITION - END OF YEAR	$ 22,291,326	$ (1,185,447)	$ 21,105,879

HOPKINSVILLE ELECTRIC SYSTEM
OF THE
CITY OF HOPKINSVILLE, KENTUCKY
COMPARATIVE SCHEDULE OF REVENUES AND EXPENSES - ELECTRIC
FOR THE YEARS ENDED JUNE 30, 2013 AND 2012

	ELECTRIC 2013	ELECTRIC 2012	VARIANCE FAVORABLE (UNFAVORABLE)
OPERATING REVENUES	$ 35,728,517	$ 35,460,165	$ 268,352
OPERATING EXPENSES			
Cost of power	27,797,919	28,145,277	347,358
Distribution - operation	849,894	758,717	(91,177)
- maintenance	930,993	833,647	(97,346)
Transmission - maintenance	1,975	777	(1,198)
Customer accounts	650,691	683,054	32,363
Sales	94,200	72,554	(21,646)
Administrative and general	1,680,626	1,644,481	(36,145)
Depreciation	1,033,107	1,026,766	(6,341)
Taxes	1,378,951	1,370,565	(8,386)
Total operating expenses	34,418,356	34,535,838	117,482
Net operating revenues	1,310,161	924,327	385,834
NONOPERATING REVENUES (EXPENSES)			
Interest on long-term debt	(156,791)	(157,160)	369
Other interest	(24,634)	(46,118)	21,484
Amortization of debt expense	(6,288)	(6,287)	(1)
Interest income	30,018	31,993	(1,975)
Other revenues (expenses)	(513,191)	754	(513,945)
Total nonoperating revenues (expenses)	(670,886)	(176,818)	(494,068)
CHANGE IN NET POSITION	$ 639,275	$ 747,509	$ (108,234)

HOPKINSVILLE ELECTRIC SYSTEM
OF THE
CITY OF HOPKINSVILLE, KENTUCKY
COMPARATIVE STATEMENT OF REVENUES AND EXPENSES - TELECOMMUNICATIONS
FOR THE YEARS ENDED JUNE 30, 2013 AND 2012

	TELECOM 2013	TELECOM 2012	VARIANCE FAVORABLE (UNFAVORABLE)
OPERATING REVENUES	$ 2,251,514	$ 2,004,570	$ 246,944
OPERATING EXPENSES			
Cost of sales - telecom	194,383	198,317	3,934
Distribution - operation	691,755	621,269	(70,486)
- maintenance	22,288	21,414	(874)
Customer accounts	29,408	26,475	(2,933)
Sales	34,627	39,513	4,886
Administrative and general	463,514	421,881	(41,633)
Depreciation and amortization	547,454	471,120	(76,334)
Taxes	139,896	163,973	24,077
Total operating expenses	2,123,325	1,963,962	(159,363)
Net operating revenues	128,189	40,608	87,581
NONOPERATING REVENUES (EXPENSES)			
Interest on long-term debt	(140,229)	(176,383)	36,154
Amortization of debt expense	(3,693)	(3,693)	-
Interest income	65	262	(197)
Total nonoperating revenues (expenses)	(143,857)	(179,814)	35,957
CHANGE IN NET POSITION	$ (15,668)	$ (139,206)	$ 123,539

HOPKINSVILLE ELECTRIC SYSTEM
OF THE
CITY OF HOPKINSVILLE, KENTUCKY
COMPARATIVE ANALYSIS OF OPERATING EXPENSES - ELECTRIC

	For the Year Ended June 30, 2013 Amount	Percent		For the Year Ended June 30, 2012 Amount	Percent		Increase (Decrease)
Distribution							
Supervision & engineering	$ 104,524	0.29	%	$ 99,360	0.28	%	$ 5,164
Station expense	153,919	0.43		109,411	0.31		44,508
Overhead lines expense	234,067	0.66		335,418	0.95		(101,351)
Underground line expense	-	0.00		-	0.00		-
Street light & signal system expense	35,235	0.10		26,940	0.08		8,295
Meter expense	30,325	0.08		73,257	0.21		(42,932)
Customer installation expense	31,439	0.09		37,352	0.11		(5,913)
Miscellaneous distribution expense	22,331	0.06		21,651	0.06		680
Rents	238,054	0.67		55,328	0.16		182,726
Total distribution	$ 849,894	2.38	%	$ 758,717	2.16	%	$ 91,177
Maintenance expense							
Distribution:							
Supervision & engineering	$ 19,557	0.05	%	$ 18,708	0.05	%	$ 849
Substations	38,353	0.11		6,002	0.02		32,351
Overhead lines	798,649	2.24		742,062	2.09		56,587
Underground services	12,072	0.03		8,042	0.02		4,030
Transformers	38,181	0.11		38,391	0.11		(210)
Street light & signal system	24,181	0.07		20,442	0.06		3,739
Meters	-	0.00		-	0.00		-
Total distribution maintenance	$ 930,993	2.61	%	$ 833,647	2.35	%	$ 97,346
Transmission:							
Maintenance of overhead lines	$ 1,975	0.00	%	$ 777	0.00	%	$ 1,198
Total transmission maintenance	$ 1,975	0.00	%	$ 777	0.00	%	$ 1,198
Customer accounts							
Supervision	$ 310	0.00	%	$ 1,036	0.00	%	$ -
Meter reading	44,627	0.12		66,339	0.19		(21,712)
Customer records & collection expense	421,021	1.18		417,781	1.18		3,240
Uncollectible accounts	82,913	0.23		92,365	0.26		(9,452)
Miscellaneous customer accounting expense	3,659	0.01		3,649	0.01		10
Customer assistance expense	48,387	0.14		50,029	0.14		(1,642)
Information & instructional advertising	49,774	0.14		51,855	0.15		(2,081)
Total customer accounts	$ 650,691	1.82	%	$ 683,054	1.93	%	$ (31,637)

HOPKINSVILLE ELECTRIC SYSTEM
OF THE
CITY OF HOPKINSVILLE, KENTUCKY
COMPARATIVE ANALYSIS OF OPERATING EXPENSES - ELECTRIC, continued

	For the Year Ended June 30, 2013		For the Year Ended June 30, 2012		Increase
	Amount	Percent	Amount	Percent	(Decrease)
Sales expense					
Demonstrating and selling expense	$ 70,542	0.20 %	$ 50,373	0.14 %	$ 20,169
Advertising expense	22,743	0.06	21,269	0.06	1,474
Miscellaneous	915	0.00	912	0.00	3
Total sales	$ 94,200	0.26 %	$ 72,554	0.20 %	$ 21,646
Administrative and general					
Administrative & office salaries	$ 366,701	1.03 %	$ 348,315	0.98 %	$ 18,386
Office supplies & expense	142,349	0.40	133,044	0.38	9,305
Outside services employed	59,473	0.17	78,649	0.22	(19,176)
Property insurance	125,398	0.35	126,985	0.36	(1,587)
Injuries & damages	48,977	0.14	33,080	0.09	15,897
Employees pension & other benefits	830,430	2.32	794,202	2.24	36,228
Duplicate charges (credit)	(117,669)	(0.33)	(110,685)	(0.31)	(6,984)
Miscellaneous general expense	71,068	0.20	100,034	0.28	(28,966)
Maintenance	153,899	0.43	140,857	0.40	13,042
Total administrative and general	$ 1,680,626	4.71 %	$ 1,644,481	4.64 %	$ 36,145

HOPKINSVILLE ELECTRIC SYSTEM
OF THE
CITY OF HOPKINSVILLE, KENTUCKY
COMPARATIVE ANALYSIS OF OPERATING EXPENSES - TELECOMMUNICATIONS

	For the Year Ended June 30, 2013 Amount	Percent		For the Year Ended June 30, 2012 Amount	Percent		Increase (Decrease)
Distribution							
Supervision & engineering	$ 90,682	4.03	%	$ 88,123	4.40	%	$ 2,558
Hub expenses	65,997	2.93		29,558	1.47		36,439
Overhead cable expense	314,885	13.99		257,932	12.87		56,953
Meter expense	-	0.00		-	0.00		1
Customer installation expense	211,716	9.40		196,275	9.79		15,441
Miscellaneous distribution expense	9,976	0.44		9,718	0.48		258
Rents	(1,501)	(0.07)		39,663	1.98		(41,164)
Total distribution	$ 691,755	30.72	%	$ 621,269	30.99	%	$ 70,486
Maintenance expense							
Distribution:							
Supervision & engineering	$ 12,172	0.54	%	$ 11,887	0.59	%	$ 285
Hub expenses	638	0.03		3,264	0.16		(2,626)
General maintenance	9,478	0.42		6,192	0.31		3,286
Maintenance underground services	-	0.00		71	0.00		(71)
Total distribution maintenance	$ 22,288	0.99	%	$ 21,414	1.06	%	$ 874
Customer accounts							
Billing expense	$ 6,167	0.27	%	$ 2,235	0.11	%	$ 3,932
Customer records & collection expense	2,577	0.11		2,402	0.12		175
Uncollectible accounts	13,331	0.59		14,202	0.71		(871)
Customer assistance expense	7,333	0.33		7,636	0.38		(303)
Total customer accounts	$ 29,408	1.30	%	$ 26,475	1.32	%	$ 2,933

HOPKINSVILLE ELECTRIC SYSTEM
OF THE
CITY OF HOPKINSVILLE, KENTUCKY
COMPARATIVE ANALYSIS OF OPERATING EXPENSES -
TELECOMMUNICATIONS, continued

	For the Year Ended June 30, 2013		For the Year Ended June 30, 2012	
	Amount	Percent	Amount	Percent
Sales expense				
Demonstrating and selling expense	$ 14,428	0.64 %	$ 13,668	0.68 %
Advertising expense	20,199	0.90	25,845	1.29
Total sales	$ 34,627	1.54 %	$ 39,513	1.97 %
Administrative and general				
Administrative & office salaries	$ 61,639	2.74 %	$ 62,742	3.13 %
Office supplies & expense	22,680	1.01	21,538	1.07
Meeting expenses	17,074	0.76	6,890	0.34
Outside services employed	16,872	0.75	16,875	0.84
Property insurance	21,059	0.94	14,099	0.70
Injuries & damages	10,946	0.49	19,663	0.98
Employees pension & other benefits	199,250	8.85	174,354	8.70
General advertising	19	0.00	-	0.00
Miscellaneous general expense	1,208	0.05	1,207	0.06
Maintenance	112,767	5.01	104,513	5.21
Total administrative and general	$ 463,514	20.60 %	$ 421,881	21.03 %

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INDEPENDENT AUDITORS' 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 Board of the
Hopkinsville Electric System of the
City of Hopkinsville, Kentucky
Hopkinsville, Kentucky

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the Hopkinsville Electric System of the City of Hopkinsville, Kentucky, as of and for the years ended June 30, 2013 and 2012, and the related notes to the financial statements, which collectively comprise the Hopkinsville Electric System of the City of Hopkinsville, Kentucky's basic financial statements and have issued our report thereon dated November 20, 2013.

Internal Control Over Financial Reporting

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

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

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

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Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Hopkinsville Electric System of the City of Hopkinsville, Kentucky's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion.

Hopkinsville Electric System of the City of Hopkinsville, Kentucky's Response to Findings

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

Purpose of this Report

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

Kem, Duguid & Associates, P.S.C.

Kem, Duguid & Associates, P.S.C.

Certified Public Accountants
Hopkinsville, Kentucky

November 20, 2013

HOPKINSVILLE ELECTRIC SYSTEM
OF THE
CITY OF HOPKINSVILLE, KENTUCKY
SUMMARY SCHEDULE OF FINDINGS AND RESPONSES
JUNE 30, 2013

2013-01 Internal Controls

Condition: The System does not have control over the preparation of the financial statements footnote disclosures in order to prevent or detect a misstatement in the disclosures. The independent auditor cannot be a compensating control for the client.

Criteria: Statement on Auditing Standards (SAS 115) states that a control deficiency exists when an entity does not have controls in place which would prevent or detect a misstatement in the financial statements and related footnote disclosures.

Effect: Lack of accountability and possible misstatement of financial statement footnote disclosures.

Recommendation: The System should designate an individual who possesses suitable skill, knowledge, and/or experience to review the financial statements footnote disclosures, and take responsibility for these disclosures.

Response: It is not feasible for the System to invest the resources for a member of the financial accounting staff to obtain the training necessary to obtain knowledge related to Financial Accounting Standards Board (FASB) and Government Accounting Standards Board (GASB) pronouncements and to remain current with this knowledge. Management does not consider the deficiency to be imperative to the daily internal control operations of the System.