

**KENTUCKY MUNICIPAL
POWER AGENCY**

**FINANCIAL STATEMENTS
YEARS ENDED JUNE 30, 2014 AND 2013**

TABLE OF CONTENTS

	<u>Page</u>
Independent Auditor's Report	1- 2
Required Supplementary Information: Management's Discussion and Analysis	3- 8
Basic Financial Statements:	
Statements of Net Assets (Deficit)	9
Statements of Revenues, Expenses, and Changes in Net Assets (Deficit)	10
Statements of Cash Flows	11-12
Notes to Financial Statements	13-26
Supplementary Information: Operating Expenses	27
Report On Internal Control Over Financial Reporting And On Compliance And Other Matters Based On An Audit Of Financial Statements Performed In Accordance With <i>Government Auditing Standards</i>	28-29

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Independent Auditor's Report

To the Board of Directors of the
Kentucky Municipal Power Agency
Paducah, Kentucky

We have audited the accompanying financial statements of the Kentucky Municipal Power Agency, as of and for the years ended June 30, 2014 and 2013 and the related notes to the financial statements which comprise the Agency's basic financial statements, as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards general 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 upon 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 principles used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statement.

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of Kentucky Municipal Power Agency, as of June 30, 2014 and 2013, 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 3 through 8 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Government 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

The schedule of operating expenses presented on page 27 is the responsibility of management and was 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 schedule of operating expenses presented on page 27 is fairly stated in all material respects in relation to the basic financial statements as a whole.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated February 9, 2015 on our consideration of Kentucky Municipal Power Agency'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 Kentucky Municipal Power Agency's internal control over financial reporting and compliance.



Paducah, Kentucky
February 9, 2015

REQUIRED SUPPLEMENTARY INFORMATION

KENTUCKY MUNICIPAL POWER AGENCY MANAGEMENT'S DISCUSSION AND ANALYSIS

The Kentucky Municipal Power Agency (Agency) is presenting the following discussion and analysis in order to provide an overall review of the Agency's financial activities for the fiscal years ending June 30, 2014 and 2013. We encourage readers to consider the information presented here in conjunction with the Agency's financial statements and notes to the basic financial statements to enhance their understanding of the Agency's financial performance.

Financial Highlights

- The Agency's total assets decreased \$7.853 million from fiscal year 2013 to fiscal year 2014, which primarily was a result of capital asset depreciation. Total liabilities decreased by \$8.043 million from payment of maturing revenue bond principal. These events resulted in total net assets increasing \$0.190 million over the course of the year's operations compared to fiscal year 2013.
- The Agency had an operating gain in fiscal year 2014 and fiscal year 2013 due to debt service charges being billed to members.

Non-operating net revenues, including investment income, decreased \$8 million from fiscal year 2013 to fiscal year 2014. This decrease is primarily related to the elimination of interest charged to construction as the Prairie State Generation Plant was placed into service and the fact that no investment contracts were terminated such as occurred in November 2012 when Morgan Stanley paid the Agency \$4.8 million to terminate an investment contract for the Series 2007A Debt Service Reserve.

Overview of the Financial Highlights

This annual report includes the management's discussion and analysis report, the independent auditor's report and the basic financial statements of the Agency. The financial statements also include notes that explain in more detail some of the information in the financial statements.

Required Financial Highlights

The financial statements of the Agency report information of the Agency using accounting methods similar to those used by private sector companies. These statements offer short- and long-term financial information about its activities. The Statements of Net Assets (Deficit) include all the Agency's assets and liabilities and provide information about the nature and amounts of investments and resources (assets) and the obligations to the Agency's creditors (liabilities). They also provide the basis for evaluating the capital structure of the Agency and assessing the liquidity and financial flexibility of the Agency.

All of the current year's revenues and expenses are accounted for in the Statements of Revenues, Expenses, and Changes in Net Assets (Deficit). These statements measure the success of the Agency's operations over the past year and can be used to determine whether the Agency has successfully recovered all its costs through its fees and other charges, and also assess the profitability and creditworthiness of the Agency.

The final required financial statements are the Statements of Cash Flows. The statements report cash receipts, cash payments, and net changes in cash resulting from operations, investing, and financing activities and provide answers to such questions as where did cash come from, what was cash used for, and what was the change in the cash balance during the reporting period. Cash for fiscal year 2014 and fiscal year 2013 was provided by revenue bonds issued in May 2010 (\$183.7 million), Bond Anticipation Notes drawn during the 2013 and 2012 fiscal years (\$35 million) and the sale of electricity to Agency members.

The notes to the financial statements provide additional information that is essential to a full understanding of the data provided in the basic financial statements. The notes to the financial statements follow the Statements of Cash Flows in this report.

(Continued)

**KENTUCKY MUNICIPAL POWER AGENCY
MANAGEMENT'S DISCUSSION AND ANALYSIS**

Financial Analysis of the Agency

The most common financial question posed to the Agency is “How did we do financially from fiscal year 2013 to fiscal year 2014?” The Statements of Net Assets (Deficit) and the Statements of Revenues, Expenses, and Changes in Net Assets report information about the Agency’s activities in a way that will help answer this question. These two statements report the net assets of the Agency and the changes in them. One can think of the Agency’s net assets (deficit) – the difference between assets and liabilities – as one way to measure financial health or financial position. Over time, increases or decreases in the Agency’s net assets are one indicator of whether the financial health is improving or deteriorating. However, one will need to consider other non-financial factors such as changes in economic conditions and new or changed governmental legislation. As the Agency was a developmental stage entity, it is expected and reasonable that net assets continued to decrease until sales of electricity from the Prairie State Project began in June 2012 and the Agency began to bill its members for power supply and costs.

To begin our analysis, a summary of the Agency’s Statements of Net Assets (Deficit) is presented to Table A-1.

**Table A-1
Condensed Statements of Net Assets (Deficit)
(000’s)**

	<u>2014</u>	<u>2013</u>	<u>2012</u>	2013-2014 Dollar Change	2012-2013 Dollar Change
Current and other assets	\$ 83,210	\$ 82,493	\$ 73,589	\$ 717	\$ 8,904
Capital assets	<u>435,030</u>	<u>443,600</u>	<u>442,996</u>	<u>(8,570)</u>	<u>(2,396)</u>
Total assets	<u>518,240</u>	<u>526,093</u>	<u>519,585</u>	<u>(7,853)</u>	<u>6,508</u>
Revenue bonds	510,851	520,121	514,060	(9,270)	6,061
Other liabilities	<u>23,163</u>	<u>21,936</u>	<u>13,833</u>	<u>1,227</u>	<u>8,103</u>
Total liabilities	<u>534,014</u>	<u>542,057</u>	<u>527,893</u>	<u>(8,043)</u>	<u>14,164</u>
Invested in capital assets, net of related debt	(40,536)	(35,170)	(12,944)	(5,366)	(22,226)
Restricted	10,323	9,460	-	863	9,460
Unrestricted	<u>14,439</u>	<u>9,746</u>	<u>4,636</u>	<u>4,693</u>	<u>5,110</u>
Total Net Assets (Deficit)	<u>\$(15,774)</u>	<u>\$(15,964)</u>	<u>\$(8,308)</u>	<u>\$ 190</u>	<u>\$ (7,656)</u>

(Continued)

**KENTUCKY MUNICIPAL POWER AGENCY
MANAGEMENT'S DISCUSSION AND ANALYSIS**

Financial Analysis of the Agency

**Table A-2
Condensed Statements of Revenues, Expenses, and
Changes in Net Assets
(000's)**

	<u>2014</u>	<u>2013</u>	<u>2012</u>	<u>2013-2014 Dollar Change</u>	<u>2012-2013 Dollar Change</u>
Operating revenue	\$ 68,224	\$ 57,381	\$ 52,048	\$10,843	\$ 5,333
Non-operating revenue	3,306	11,373	26,406	(8,067)	(15,033)
Total revenue	<u>71,530</u>	<u>68,754</u>	<u>78,454</u>	<u>2,776</u>	<u>(9,700)</u>
Other operating expense	44,915	49,786	51,266	(4,871)	(1,480)
Non-operating expense	<u>26,425</u>	<u>26,624</u>	<u>26,175</u>	<u>(199)</u>	<u>449</u>
Total expenses	<u>71,340</u>	<u>76,410</u>	<u>77,441</u>	<u>(5,070)</u>	<u>(1,031)</u>
Changes in net assets	190	(7,656)	1,013	7,846	(8,669)
Beginning net assets (deficit)	<u>(15,964)</u>	<u>(8,308)</u>	<u>(9,321)</u>	<u>(7,656)</u>	<u>(1,013)</u>
Ending net assets (deficit)	<u>\$ (15,774)</u>	<u>\$ (15,964)</u>	<u>\$ (8,308)</u>	<u>\$ 190</u>	<u>\$ (7,656)</u>

While the Statements of Net Assets (Deficit) show net assets (deficit) of the Agency, the Statements of Revenues, Expenses, and Changes in Net Assets (Deficit) provide answers as to the nature and source of these changes. As illustrated in Table A-2, there was a positive change in net assets for fiscal year 2014 and fiscal year 2012 and a negative change in net assets for fiscal year 2013.

Prior to June 2012, electrical power sold to members was obtained by the Agency through contracts with power suppliers. At that time, Unit 1 of the Prairie State Project came online and the Agency sold power produced by that unit for the benefit of its members. The Agency continued as a developmental stage entity until the Prairie State Generation Project completed the construction phase with the completion of Unit 2 in November 2012. At that time, the Agency began billing its members for power sales. The amount billed to the members was based upon the Agency's operating costs, the Agency's cost of power purchased on behalf of the members, and the Agency's debt service costs related to the Prairie State Generation Plant. In fiscal year 2013, the Agency utilized \$8.1 million from its Rate Stabilization Fund to avoid billing members for transmission congestion and Prairie State operating costs that were significantly higher than budgeted.

Non-operating revenues represent investment income from the 2007 and 2010 revenue bond funds and interest charged to construction resulting from the 2007 and 2010 bond issues as well as income relating to the Federal Build America Bond (BABS) subsidy. The Agency is entitled to a payment of 32.48% of interest expense relating to the BABS portion of the 2010 bond issue from the United States Government. Income related to the BABS subsidy was \$2.5 million in fiscal year 2014, \$2.6 million in fiscal year 2013 and 2.7 million in fiscal year 2012. Interest charged to construction decreased \$17.4 million from fiscal year 2012 to fiscal year 2013 due to the completion of construction of the Prairie State Generating Plant. No interest charged to construction occurred in fiscal year 2014.

Other operating expenses decreased in fiscal year 2014 due to increased purchase of electricity from the Prairie State Generation Plant. 2014 was the first full fiscal year of operations for the plant.

(Continued)

**KENTUCKY MUNICIPAL POWER AGENCY
MANAGEMENT'S DISCUSSION AND ANALYSIS**

Non-Operating Expenses are comprised mainly of interest paid on indebtedness related to the 2007 and 2010 bond issues.

Capital Assets

At the end of fiscal year 2014, the Agency had \$435 million invested in capital assets. There was a decrease in capital assets from fiscal year 2013 to fiscal year 2014 of \$8.5 million due to \$4.5 million in capital asset additions and \$12 million in additional depreciation. There was a small decrease in capital assets from fiscal year 2012 to fiscal year 2013 of \$2 million, thus a grand total decrease of \$11 million was seen from fiscal year 2012 to fiscal year 2014. Capital assets are entirely comprised of assets related to completed construction at the Prairie State Energy Campus Plant.

The Capital Assets comparison between fiscal years 2014, 2013, and 2012, is shown in Table A-3.

**Table A-3
Capital Assets
(000's)**

	<u>2014</u>	<u>2013</u>	<u>2012</u>	<u>2013-2014 Dollar Change</u>	<u>2012-2013 Dollar Change</u>
Construction in progress	\$ 5,080	\$ 575	\$ 165,084	\$ 4,505	\$(164,509)
Property, plant, and equipment	453,159	454,227	281,557	(1,068)	172,670
Less accumulated depreciation	(23,209)	(11,202)	(645)	(12,007)	(10,557)
Total capital assets	\$ 435,030	\$ 443,600	\$ 445,996	\$ (8,570)	\$ (2,396)

Administration

The revenue bonds outstanding increased from \$514 million in fiscal year 2012 to \$520 million in fiscal year 2013 as a result of a draw from the Bond Anticipation Notes in the amount of \$15 million related to the Prairie State Energy Campus Plant. The bonds are payable from the sale of electric power to Paducah Power System and Princeton Electric Plant Board. The power sales to Paducah Power System and Princeton Electric Plant Board are made pursuant to "take or pay" Power Sales Agreements with those entities. The Agency recognized \$9.1 million in revenue bonds outstanding as a current liability as it will pay bond holders this amount in principal on 9/1/14.

Economic Factors and Other Information

The Agency Formation

The Agency is a public agency organized under provisions of Chapter 65 of the Kentucky Revised Statutes, pursuant to an Interlocal Corporation Agreement dated February 7, 2005, and approved by the Attorney General of the Commonwealth of Kentucky on February 11, 2005. The Agency was organized for the purpose of providing municipal electric systems in the Commonwealth with an on-going source and supply of electric power to meet the demands for growth of power consumption.

The Agency Organization

The Agency currently is comprised of two municipal utility members, Paducah Power System and Princeton Electric Plant Board. Additional members may be added if approved by the Agency Board and its members. The Board of Directors is currently comprised of four individuals: an appointee made by the Board of Directors of Paducah Power System, an appointee made by the Board of Directors of Princeton Electric Plant Board, and the general manager of each member electric system.

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**KENTUCKY MUNICIPAL POWER AGENCY
MANAGEMENT'S DISCUSSION AND ANALYSIS**

Economic Factors and Other Information

Members Wholesale Power Contracts

Both Paducah Power System and Princeton Electric Plant Board were full requirements wholesale distribution customers of the Tennessee Valley Authority (TVA) for more than four decades. In December 2004 and January 2005, Paducah Power System and Princeton Electric Plant Board, respectively, provided TVA with a five-year written notice of their decision to terminate their Wholesale Power Contracts. Subsequent to providing TVA with said notice, Paducah Power System and Princeton Electric Plant Board determined that they would meet their baseload wholesale power requirements through respective power sales agreements with the Agency. The Agency obtains the power necessary to meet those needs primarily through its participation and ownership in the Prairie State Energy Campus.

Prairie State Project

February 5, 2005, the Agency executed a Project Development Agreement with the Prairie State Generating Company (PSGC), at the time a subsidiary of Peabody Energy. The Prairie State Project is a 1600 MW supercritical mine mouth coal generating facility and newly developed adjacent coal mine located in Southern Illinois, forty miles southeast of St. Louis, Missouri. After financial closing, the plant and coal mine became owned as tenants in common by all participants. The coal mine is estimated to contain sufficient reserves to fuel the generating plant for approximately 30 years. The Project also includes transmission upgrades and interconnection to the Ameren system which is a member of the Midcontinent Independent-Transmission System Operator, Inc. (MISO) transmission grid.

The Agency's current entitlement in the Project is 124 MW, of which Paducah Power System is entitled to 104 MW and Princeton Electric Plant Board is entitled to 20 MW. Other participants in the Project are American Municipal Power, Inc., Illinois Municipal Electric Agency, Indiana Municipal Power Agency, Missouri Joint Municipal Electric Utility Commission, Northern Illinois Municipal Power Agency, Prairie Power, Inc., Southern Illinois Power Cooperative, and Lively Grove Energy Partners, LLC, a wholly-owned subsidiary of Peabody Energy Corporation.

Bechtel was issued Full Notice to Proceed with construction of the Plant on October 1, 2007. As of the end of December 2014, PSGC reported that, for activities related solely to Bechtel's Amended Engineering, Procurement and Construction (EPC) Contract, engineering efforts are 100 percent complete, construction activities are 100 percent complete, and overall efforts are 100 percent complete. Unit 1 of the Prairie State Project achieved provisional completion on June 6, 2012 at which time PSGC took care, custody and control. Unit 2 of the Prairie State Project achieved provisional completion on November 1, 2012 at which time PSGC took care, custody and control.

Equipment and construction specifications for the Mine were issued, and construction activities on the Mine portal began in early May of 2008. As of the end of December 2014, 100 percent of construction activities on the Mine had been completed. 100 percent of the expected total equipment and contract costs of the Mine had been committed to in the form of either actual purchases or signed commitments for equipment, materials and supplies, and construction services with fixed prices.

The Agency's anticipates no additional costs to complete the construction and equipping of the Project as of the end of December 2014.

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**KENTUCKY MUNICIPAL POWER AGENCY
MANAGEMENT'S DISCUSSION AND ANALYSIS**

Agency Contact Information

The financial report is designed to provide creditors with a general overview of Kentucky Municipal Power Agency's finances. Anyone having questions regarding this report, or desiring additional information may contact John A. Humphries, General Manager, Kentucky Municipal Power Agency, P.O. Box 0180, Paducah, KY 42002-0180 or by telephone at 270.365.2031 or by email at jahumphries@pepb.org.

BASIC FINANCIAL STATEMENTS

KENTUCKY MUNICIPAL POWER AGENCY
STATEMENTS OF NET ASSETS (DEFICIT)
JUNE 30

ASSETS

	2014	2013
Current Assets:		
Cash and temporary cash investments	\$ 5,075,047	\$ 3,318,403
Accounts receivable	1,391,765	1,377,678
Working capital Prairie State	2,180,327	3,256,526
Other receivables	8,135,345	5,692,281
Inventory	3,024,159	2,390,214
Prepaid expenses	3,020	2,997
	<hr/>	<hr/>
Total current assets	19,809,663	16,038,099
Restricted assets:		
Project fund	-	5,941,419
Principal and interest sinking fund	15,349,619	14,999,222
Reserve fund	37,089,284	36,486,841
Pledged collateral	4,739,382	3,106,625
Interest receivable	259,054	197,425
	<hr/>	<hr/>
Total restricted assets	57,437,339	60,731,532
Capital assets:		
Construction work in progress	5,080,105	575,244
Property, plant, and equipment	453,158,404	454,226,543
Less accumulated depreciation	(23,208,840)	(11,201,999)
	<hr/>	<hr/>
Total capital assets	435,029,669	443,599,788
Deferred debits and other assets:		
Prairie State reserve funds	540,315	54,812
Unamortized debt issuance costs	5,423,217	5,668,826
	<hr/>	<hr/>
Total deferred debits and other assets	5,963,532	5,723,638
	<hr/>	<hr/>
Total noncurrent assets	498,430,540	510,054,958
	<hr/>	<hr/>
Total assets	<u>\$ 518,240,203</u>	<u>\$ 526,093,057</u>

See notes to financial statements.

LIABILITIES

Current Liabilities:	<u>2014</u>	<u>2013</u>
Accounts payable	\$ 4,280,425	\$ 3,090,376
Bonds held by public current portion	9,135,000	8,805,000
Other payables	1,015,403	1,198,128
Current liabilities payable from restricted assets:		
Accrued interest	<u>8,732,421</u>	<u>8,842,905</u>
Total current liabilities	<u>23,163,249</u>	<u>21,936,409</u>
Noncurrent Liabilities:		
Long-term debts:		
Bonds held by public	473,500,000	482,635,000
Bond anticipation notes	35,000,000	35,000,000
Unamortized debt discounts	(2,155,059)	(2,262,181)
Unamortized debt premium	<u>4,506,384</u>	<u>4,747,887</u>
Total noncurrent liabilities	<u>510,851,325</u>	<u>520,120,706</u>
Total liabilities	<u>534,014,574</u>	<u>542,057,115</u>

NET ASSETS (DEFICIT)

Invested in capital assets, net of related debt	(40,535,902)	(35,170,435)
Restricted for debt service	10,322,876	9,460,367
Unrestricted - net (deficit)	<u>14,438,655</u>	<u>9,746,010</u>
TOTAL NET ASSETS (DEFICIT)	<u>\$ (15,774,371)</u>	<u>\$ (15,964,058)</u>

KENTUCKY MUNICIPAL POWER AGENCY
STATEMENTS OF REVENUES, EXPENSES, AND
CHANGES IN NET ASSETS (DEFICIT)
YEARS ENDED JUNE 30

	<u>2014</u>	<u>2013</u>
Operating Revenues:		
Service revenue	\$ 68,224,379	\$ 57,380,576
Total operating revenues	<u>68,224,379</u>	<u>57,380,576</u>
Purchased Power and Operating Expenses:		
Purchased power cost	28,895,642	36,948,908
General operating expense	<u>16,019,202</u>	<u>12,837,142</u>
Total purchased power and operating expenses	<u>44,914,844</u>	<u>49,786,050</u>
Operating income	<u>23,309,535</u>	<u>7,594,526</u>
Nonoperating Revenues (Expenses):		
Interest paid on indebtedness	(26,254,365)	(26,472,695)
Investment income	791,182	5,747,730
Federal Build America Bond's subsidy	2,514,469	2,638,087
Interest charged to construction	-	2,987,748
Net amortization discount and premium on debt	<u>(171,134)</u>	<u>(151,174)</u>
Total nonoperating revenues (expenses)	<u>(23,119,848)</u>	<u>(15,250,304)</u>
Change in net assets	189,687	(7,655,778)
Net assets (deficit), beginning of year	<u>(15,964,058)</u>	<u>(8,308,280)</u>
NET ASSETS (DEFICIT), END OF YEAR	<u><u>\$(15,774,371)</u></u>	<u><u>\$(15,964,058)</u></u>

See notes to financial statements.

KENTUCKY MUNICIPAL POWER AGENCY
STATEMENTS OF CASH FLOWS
YEARS ENDED JUNE 30

	<u>2014</u>	<u>2013</u>
Cash Flows from Operating Activities:		
Receipts from customers	\$ 65,767,228	\$ 56,518,588
Payments to suppliers	(31,662,159)	(38,515,192)
Payments to employees	(872,489)	(959,370)
	<u>33,232,580</u>	<u>17,044,026</u>
Cash Flows from Capital and Related Financing Activities:		
Capital expenditures	(5,144,236)	(5,101,105)
Proceeds from issuance of long-term debt	-	15,000,000
Principal payments made on bonds	(8,805,000)	-
Interest payments on long-term debt	(26,254,365)	(26,215,027)
Federal Build America Bond's subsidy	2,514,469	2,638,087
	<u>(37,689,132)</u>	<u>(13,678,045)</u>
Net cash used by capital and related financing activities		
Cash Flows from Investing Activities:		
Purchases of investments	(12,637,339)	(39,158,730)
Proceeds from sale of investments	28,045,934	-
Investment income	729,553	2,581,959
	<u>16,138,148</u>	<u>(36,576,771)</u>
Net cash provided by investing activities		
Net increase in cash and cash equivalents	11,681,596	(33,210,790)
Cash and cash equivalents, beginning of year	<u>11,418,039</u>	<u>44,628,829</u>
CASH AND CASH EQUIVALENTS, END OF YEAR	<u><u>\$ 23,099,635</u></u>	<u><u>\$ 11,418,039</u></u>

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KENTUCKY MUNICIPAL POWER AGENCY
STATEMENTS OF CASH FLOWS
YEARS ENDED JUNE 30

Reconciliation of Operating Income to Net	<u>2014</u>	<u>2013</u>
Cash Used by Operating Activities:		
Operating income	\$ 23,309,535	\$ 7,594,526
Depreciation expense	12,006,840	10,560,650
Adjustments to reconcile operating income to net cash used by operating activities:		
Changes in operating assets and liabilities:		
Accounts receivable	(14,087)	88,108
Other accounts receivable	(2,443,064)	(950,096)
Prepaid expenses	(23)	(32)
Other assets	(633,945)	558,816
Accounts payable	1,190,048	(1,206,453)
Other current and accrued liabilities	(182,725)	398,507
NET CASH USED BY OPERATING ACTIVITIES	<u>\$ 33,232,579</u>	<u>\$ 17,044,026</u>
Schedule of Noncash Financing Activities:		
Amortization of bond issue and discount costs	\$ (171,134)	\$ (151,174)
Interest charged to construction	-	2,987,748

See notes to financial statements.

KENTUCKY MUNICIPAL POWER AGENCY
NOTES TO FINANCIAL STATEMENTS

Note 1 - Summary of Significant Accounting Policies:

Entity

The Agency is a joint public agency formed by municipal utilities and is organized under provisions of Chapter 65 of the Kentucky Revised Statutes, pursuant to an Inter local Cooperation Agreement dated February 7, 2005. The two members of the Agency are Paducah Electric Plant Board (Paducah Power System), a municipal utility of Paducah, Kentucky, and Princeton Electric Plant Board (Princeton Electric), a municipal utility of Princeton, Kentucky. The Agency was created to supply municipal electric systems in the Commonwealth of Kentucky with an ongoing source and supply of electric power to meet their current requirements and demands for future growth in electric power. Additional members may be added if approved by the Agency's Board of Directors and members. The Agency is governed by a four-person Board of Directors consisting of the General Manager of Paducah Power System, an appointee of the Board of Paducah Power System, the General Manager of Princeton Electric, and an appointee of the Board of Princeton Electric.

The Agency acquired an undivided interest in a "mine mouth", pulverized coal-fueled power generating facility on a site in Washington, Randolph, and St. Clair Counties, Illinois, (Prairie State Energy Campus) for the purpose of providing wholesale base load power to its members, Paducah Power System and Princeton Electric. The Agency is not regulated. The rates to be charged to Paducah Power System and Princeton Electric will be set by the Board through operating and power agreements.

Measurement Focus, Basis of Accounting and Basis of Presentation

The financial statements of the Agency are prepared in accordance with generally accepted accounting principles (GAAP) as applied to governmental units. This requires the accrual basis of accounting for proprietary entities. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles.

The financial statements are reported using the economic resources measurement focus and 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.

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

(Continued)

KENTUCKY MUNICIPAL POWER AGENCY
NOTES TO FINANCIAL STATEMENTS

Note 1 - Summary of Significant Accounting Policies:

Deposits and Investments

For purposes of the statement of cash flows, cash and cash equivalents have original maturities of three months or less from the date of acquisition.

Investment of Agency funds is restricted by bond indentures. Investments are limited to:

- a. Obligations of the United States and of its agencies and instrumentalities, including obligations subject to repurchase agreements, if delivery of these obligations subject to repurchase agreements is taken either directly or through an authorized custodian. These investments may be accomplished through repurchase agreements reached with sources including, but not limited to, national or state banks chartered in Kentucky.
- b. Obligations and contracts for future delivery or purchase of obligations backed by the full faith and credit of the United States or a United States government agency, including, but not limited to:
 1. United States Treasury,
 2. Export-Import Bank of the United States,
 3. Farmers Home Administration,
 4. Government National Mortgage Corporation, and
 5. Merchant Marine bonds.
- c. Obligations of any corporation of the United States government, including but not limited to:
 1. Federal Home Loan Mortgage Corporation,
 2. Federal Farm Credit Banks,
 3. Bank for Cooperatives,
 4. Federal Intermediate Credit Banks,
 5. Federal Land Banks,
 6. Federal Home Loan Banks,
 7. Federal National Mortgage Association, and
 8. Tennessee Valley Authority.
- d. Certificates of deposit or other interest bearing accounts issued by any bank or savings and loan institution which are insured by the Federal Deposit Insurance Corporation or similar entity, or which are collateralized, to the extent uninsured, by any obligations, including surety bonds, permitted by KRS 41.240(4).
- e. Uncollateralized certificates of deposit issued by any bank or savings and loan institution rated in one (1) of the three (3) highest categories by a nationally recognized rating agency.
- f. Bankers' acceptances for banks rated in one (1) of the three (3) highest categories by a nationally recognized rating agency.
- g. Commercial paper rated in the highest category by a nationally recognized rating agency.
- h. Bonds or certificates of indebtedness of the State and of its agencies and instrumentalities.
- i. Securities issued by a state or local government, or any instrumentality or agency thereof, in the United States, and rate in one (1) of the three (3) highest categories by a nationally recognized rating agency.

(Continued)

KENTUCKY MUNICIPAL POWER AGENCY
NOTES TO FINANCIAL STATEMENTS

Note 1 - Summary of Significant Accounting Policies:

Deposits and Investments

- j. Shares of mutual funds, each of which have the following characteristics:
 - 1. The mutual fund shall be an open-end diversified investment company registered under the Federal Investment Company Act of 1940, as amended;
 - 2. The management company of the investment company shall have been in operation for at least five (5) years; and
 - 3. All of the securities in the mutual fund shall be investments in any one or more of the investments described above.

Investments are stated at fair value, which is the amount at which an investment could be exchanged in a current transaction between willing parties. Fair values are based on quoted market prices. No investments are reported at amortized cost. Adjustments necessary to record investments at fair value are recorded in the operating statement as increases or decreases in investment income. Market values of investments may have changed significantly since year end.

Receivables

Receivables consist of all revenues earned at year-end and not yet received.

Inventories

Inventories are valued at cost. Inventory consists of the Agency's portion of materials and supplies held for use by Prairie State Generating Company, LLC.

Prepayments

This balance represents a prepayment of insurance which will benefit future operations of the Agency.

Restricted Assets

Mandatory segregations of assets are presented as restricted assets. Such segregations are required by bond agreements and other external parties. Current liabilities payable from these restricted assets are so classified.

Capital Assets

Capital assets are generally defined by the Agency as assets with an initial, individual cost of more than \$1,000 and an estimated useful life in excess of one year.

Capital assets of the Agency are recorded at cost or the fair market value at the time of contribution to the Agency. Major outlays for utility plants are capitalized as projects are constructed. Interest incurred during the construction phase is reflected in the capitalized value of the capital assets constructed, net of interest earned on invested proceeds over the same period. Capital assets in service are depreciated over their estimated useful lives using the straight-line method of depreciation.

Long-Term Obligations

Long-term debt and other obligations are reported as liabilities. Bond premiums and discounts, as well as issuance costs, are deferred and amortized over the life of the bonds using the straight-line method. Gains or losses on prior refundings are amortized over the remaining life of the old debt or the life of the new debt, whichever is shorter.

(Continued)

**KENTUCKY MUNICIPAL POWER AGENCY
NOTES TO FINANCIAL STATEMENTS**

Note 1 - Summary of Significant Accounting Policies:

Revenues and Expenses

The Agency distinguishes operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with the Agency's principal ongoing operations. The operating revenues of the Agency are the charges to members for sales and services. The Agency began the supply of electricity to Paducah and Princeton on commercial operations of the Prairie State Energy Campus in June 2012.

Operating expenses 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 nonoperating revenues and expenses.

Reclassification

Certain reclassifications have been made to the 2013 financial statements to make them conform to the 2014 presentation.

Note 2 - Deposits and Investments:

The investment policies of the Agency are governed by the State statute. In general, this requires that all deposits and investments, not covered by FDIC insurance, are to be collateralized. For the years ended June 30, 2014 and 2013, the Agency's operating and investment accounts were fully collateralized as required by State statute.

The fair value of cash and investments as of June 30 is disclosed as follows:

	<u>2014</u>	<u>2013</u>
Checking and savings	\$ 5,615,362	\$ 3,373,216
MISO collateral funds	3,446,625	3,106,626
Mutual funds-money market	1,100,766	6,435,935
Commercial paper	16,923,823	1,663,701
Guaranteed investment security	22,874,482	37,788,013
Repurchase agreement	<u>11,539,832</u>	<u>11,539,832</u>
TOTAL CASH AND INVESTMENTS	<u>\$61,500,890</u>	<u>\$63,907,323</u>

Deposits

The financial institution balances of the Agency's deposits were \$61,500,890 for the year ended June 30, 2014. The book balance was \$61,500,890. Of the various financial institution balances at June 30, 2014, \$250,000 was insured by federal depository insurance, and the remaining balance of \$61,250,890 was subject to custodial credit risk. Custodial credit risk is the risk that in the event of a bank failure, the Agency's deposits may not be returned to it. The remaining balance of \$61,250,890 was uninsured and collateralized by U.S. Treasury pooled investments not held in the Agency's name.

The financial institution balances of the Agency's deposits were \$63,907,323 for the year ended June 30, 2013. The book balance was \$63,907,323. Of the various financial institution balances at June 30, 2013, \$250,000 was insured by federal depository insurance, and the remaining balance of \$63,657,323 was subject to custodial credit risk. Custodial credit risk is the risk that in the event of a bank failure, the Agency's deposits may not be returned to it. The remaining balance of \$63,657,323 was uninsured and collateralized by U.S. Treasury pooled investments not held in the Agency's name.

As of June 30, 2014 and 2013, \$0 and \$0 of the Agency's bank balances were known to be individually exposed to custodial credit risk at Citibank, N.A.

(Continued)

**KENTUCKY MUNICIPAL POWER AGENCY
NOTES TO FINANCIAL STATEMENTS**

Note 2 - Deposits and Investments:

Credit Risk

Credit risk is the risk an issuer or other counterparty to an investment will not fulfill its obligations.

As of June 30, 2014 and 2013, the Agency's investments were rated as follows:

<u>Investment Type</u>	<u>Standard & Poors</u>
Mutual funds-money market	Not Rated
Guaranteed investment certificates	Not Rated
Commercial paper	A
Repurchase agreement	A

Concentration of Credit Risk

Concentration of credit risk is the risk of loss attributed to the magnitude of a government's investment in a single issuer.

As of June 30, 2014, the Agency's investment portfolio was concentrated as follows:

<u>Issuer</u>	<u>Investment Type</u>	<u>Percentage of Portfolio</u>
Regions collateralized sweep account	Money market	2%
Bayerische Landesbank	Repurchase agreement	22%
BB&T Reserve Investment	Guaranteed investment certificate	44%
Visionary Funding, LLC	Commercial paper	3%
Barclay's Capital Bond	Commercial paper	29%

As of June 30, 2013, the Agency's investment portfolio was concentrated as follows:

<u>Issuer</u>	<u>Investment Type</u>	<u>Percentage of Portfolio</u>
Regions collateralized sweep account	Money market	11%
Bayerische Landesbank	Repurchase agreement	20%
BB&T Reserve Investment	Guaranteed investment certificate	66%
Visionary Funding, LLC	Commercial paper	3%

Interest Rate Risk

Interest rate risk is the risk changes in interest rates will adversely affect the fair value of an investment.

KENTUCKY MUNICIPAL POWER AGENCY
NOTES TO FINANCIAL STATEMENTS

Note 2 - Deposits and Investments:

Interest Rate Risk

As of June 30, 2014, the Agency's investments were as follows:

<u>Investment Type</u>	<u>Fair Value</u>	<u>Maturity (In Years)</u>		
		<u>Less than 1 Year</u>	<u>1 - 5 Years</u>	<u>6 - 10 Years</u>
Mutual funds-money market	\$ 1,100,706	\$ 1,100,706	\$ -	\$ -
Commercial paper				
Guaranteed investment certificates	16,923,883	16,923,883	-	-
Investment Certificates	22,881,402	-	22,881,402	-
Repurchase agreement	<u>11,539,832</u>	-	<u>11,539,832</u>	-
TOTALS	<u>\$52,445,823</u>	<u>\$18,024,589</u>	<u>\$34,421,234</u>	<u>\$ -</u>

As of June 30, 2013, the Agency's investments were as follows:

<u>Investment Type</u>	<u>Fair Value</u>	<u>Maturity (In Years)</u>		
		<u>Less than 1 Year</u>	<u>1 - 5 Years</u>	<u>6 - 10 Years</u>
Mutual funds-money market	\$ 6,435,935	\$ 6,435,935	\$ -	\$ -
Commercial paper	1,663,701	1,663,701	-	-
Guaranteed investment certificates	37,788,013	-	37,788,013	-
Repurchase agreement	<u>11,539,832</u>	-	<u>11,539,832</u>	-
TOTALS	<u>\$57,427,481</u>	<u>\$ 8,099,636</u>	<u>\$49,327,845</u>	<u>\$ -</u>

Note 3 - Restricted Assets:

Certain proceeds of the Agency's debt, as well as certain resources set aside for their repayment, are classified as restricted assets on the statements of net assets because their use is limited by applicable bond covenants and energy trading contracts. The following accounts are reported as restricted assets:

- Project Fund - Used to report revenue bond proceeds restricted for use in construction and working capital.
- Reserve Fund - Used to report resources set aside to make up potential future deficiencies in the future redemption amount.
- Pledged Collateral - Used to report collateral called to make up potential future deficiencies in energy trading contracts.

Restricted assets represent mandatory segregations of assets required by the long-term debt agreements and energy trading contracts.

KENTUCKY MUNICIPAL POWER AGENCY
NOTES TO FINANCIAL STATEMENTS

Note 3 - Restricted Assets:

The following calculation supports the amount of restricted net assets:

	2014	2013
Restricted assets:		
Project fund	\$ -	\$ 5,941,419
Sinking and reserve funds	52,438,903	51,486,063
Pledged collateral	3,446,625	3,106,625
Accrued interest receivable	259,054	197,425
Less: restricted assets not funded by revenues:		
Project fund	-	(5,941,419)
Reserve fund	(37,089,284)	(36,486,841)
Current liabilities payable from restricted assets	(8,732,421)	(8,842,905)
TOTAL RESTRICTED NET ASSETS AS CALCULATED	<u>\$ 10,322,877</u>	<u>\$ 9,460,367</u>

GASB does not allow the presentation of negative restricted net assets. The deficiency in restricted net assets is netted against unrestricted net assets in 2014 and 2013.

Note 4 - Capital Assets:

Capital asset activity for the year ended June 30, 2014, was as follows:

	Beginning Balance	Increases	Decreases	Ending Balance
Capital Assets Not Being Depreciated:				
Land	\$ 1,003,935	\$ -	\$ -	\$ 1,003,935
Construction in progress	575,245	4,504,860	-	5,080,105
TOTAL CAPITAL ASSETS NOT BEING DEPRECIATED	<u>\$ 1,579,180</u>	<u>\$ 4,504,860</u>	<u>\$ -</u>	<u>\$ 6,084,040</u>
Capital Assets Being Depreciated or Deleted:				
Land rights	\$ 4,216,025	\$ -	\$ -	\$ 4,216,025
Coal reserves	6,601,965	20,821	135,766	6,487,020
Non-utility property	16,494,161	281,514	-	16,775,675
Structures and improvements	38,596,301	30,241	-	38,626,542
Equipment	387,314,156	306,798	1,571,747	386,049,207
Total capital assets being depreciated				
Less accumulated depreciation	453,222,608	639,374	1,707,513	452,154,469
Total capital assets being depreciated, net	11,202,000	12,006,840	-	23,208,840
TOTAL CAPITAL ASSETS, NET	<u>\$443,599,788</u>	<u>\$(6,862,606)</u>	<u>\$1,707,513</u>	<u>\$435,029,669</u>

(Continued)

KENTUCKY MUNICIPAL POWER AGENCY
NOTES TO FINANCIAL STATEMENTS

Note 4 - Capital Assets:

Capital assets activity for the year ended June 30, 2013, was as follows:

	<u>Beginning Balance</u>	<u>Increases</u>	<u>Decreases</u>	<u>Ending Balance</u>
Capital Assets Not Being Depreciated:				
Land	\$ 891,745	\$ 112,190	\$ -	\$ 1,003,935
Construction in progress	<u>165,083,923</u>	<u>267,985</u>	<u>164,776,663</u>	<u>575,245</u>
TOTAL CAPITAL ASSETS NOT BEING DEPRECIATED	<u>\$165,975,668</u>	<u>\$ 380,175</u>	<u>\$164,776,663</u>	<u>\$ 1,579,180</u>
Capital Assets Being Depreciated:				
Land rights	\$ 3,324,280	\$ 891,745	\$ -	\$ 4,216,025
Coal reserves	6,736,123	-	134,158	6,601,965
Non-utility property	15,604,277	889,884	-	16,494,161
Structures and improvements	30,693,601	7,902,700	-	38,596,301
Equipment	<u>224,306,902</u>	<u>163,007,254</u>	<u>-</u>	<u>387,314,156</u>
Total capital assets being depreciated	280,665,183	172,691,583	134,158	453,222,608
Less accumulated depreciation	<u>644,667</u>	<u>10,557,333</u>	<u>-</u>	<u>11,202,000</u>
Total capital assets being depreciated, net	<u>280,020,516</u>	<u>162,134,250</u>	<u>134,158</u>	<u>442,020,608</u>
TOTAL CAPITAL ASSETS, NET	<u>\$445,996,184</u>	<u>\$162,514,425</u>	<u>\$164,910,821</u>	<u>\$443,599,788</u>

Note 5 - Accounts Payable:

The elements comprising accounts payable are as follows:

	<u>2014</u>	<u>2013</u>
Due for purchased power	\$1,740,118	\$ 774,394
Accounts payable, general	<u>2,540,307</u>	<u>2,315,983</u>
TOTAL ACCOUNTS PAYABLE	<u>\$4,280,425</u>	<u>\$3,090,377</u>

Note 6 - Long-Term Indebtedness:

Notes Payable

The following revenue bond anticipation notes have been issued:

<u>Date</u>	<u>Purpose</u>	<u>Final Maturity</u>	<u>Interest Rate</u>	<u>Original Amount</u>	<u>Outstanding Amount 6/30/14</u>
3/20/12	Finance Prairie State and working capital needs	9/1/17	Floating	\$35,000,000	\$35,000,000

The Kentucky Municipal Power Agency Power System Revenue Bond Anticipation Notes (Prairie State Project) Series 2012 were issued on March 20, 2012 with a floating interest rate, to be adjusted monthly at 65% of then current one-month LIBOR, plus 136.8 basis points. The interest rate at June 30, 2014 was 1.524 %.

These notes are secured on a parity basis with the Agency's 2007 and 2010 bond issues. All revenues received by the Agency through Power Sales Agreements are pledged as collateral.

(Continued)

KENTUCKY MUNICIPAL POWER AGENCY
NOTES TO FINANCIAL STATEMENTS

Note 6 - Long-Term Indebtedness:

Bonds

The following revenue bonds have been issued:

<u>Date</u>	<u>Purpose</u>	<u>Final Maturity</u>	<u>Interest Rate</u>	<u>Original Amount</u>	<u>Outstanding Amount 6/30/14</u>
9/20/07	Finance Prairie State and working capital needs	9/1/42	4.00-5.25%	\$291,065,000	\$290,440,000
9/20/07	Finance Prairie State and working capital needs	9/1/16	5.34-5.46%	16,645,000	12,820,000
5/27/10	Finance Prairie State and working capital needs	9/1/24	2.00-4.00%	53,600,000	50,235,000
5/27/10	Finance Prairie State and working capital needs	9/1/37	5.56-6.39%	122,405,000	122,405,000
5/27/10	Finance Prairie State and working capital needs	9/1/19	2.47-5.06%	<u>7,725,000</u>	<u>6,735,000</u>
TOTALS				<u>\$491,440,000</u>	<u>\$482,635,000</u>

For the years ended June 30, 2014 and 2013, bonds payable totaling \$484,986,325 and \$493,925,706, are recorded net of \$(2,155,059) and \$(2,262,181) of unamortized bond discount and \$4,506,384 and \$4,747,887 of unamortized bond premium, respectively.

In May 2010, the Agency issued \$122,405,000 in Taxable (Build America Bonds – Direct Pay) Power System Revenue Bonds. The Agency will receive a subsidy payment from the federal government equal to thirty-five percent of each interest payment on the Build America Bonds.

All revenues received by the Agency through Power Sales Agreements net of specified monthly project costs, in addition to all funds held by the Trustee under the terms of the bond agreement, are pledged as security of the above revenue bonds until the bonds are defeased. Total pledged funds for the years ended June 30, 2014 and 2013, as defined are \$53,731,661 and \$57,427,832, respectively. The term of the commitment is 35 years or until the bonds are defeased. Annual principal and interest payments are expected to require 100% of net revenues over the term of the commitment. During fiscal year 2010, the Agency began providing its members purchased power through power sales agreements with various vendors. During fiscal year 2012, the Agency began supplying power through operations of Prairie State as the first of two units came online in June 2012. The second unit came on line during the fiscal year ended June 30, 2013. Interest paid for the years ended June 30, 2014 and 2013, was \$26,254,364 and \$26,472,695, respectively.

(Continued)

KENTUCKY MUNICIPAL POWER AGENCY
NOTES TO FINANCIAL STATEMENTS

Note 6 - Long-Term Indebtedness:

Changes in Long-term Debt and Maturities

Long-term obligation activity for the year ended June 30, 2014, is as follows:

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending Balance</u>	<u>Due Within One Year</u>
Revenue bonds	\$491,440,000	\$ -	\$ 8,805,000	\$482,635,000	\$ 9,135,000
Bond anticipation notes	35,000,000	-	-	35,000,000	-
Unamortized debt discount	(2,262,181)	-	(107,122)	(2,155,059)	-
Unamortized debt premium	4,747,887	-	241,503	4,506,384	-
TOTALS	<u>\$528,925,706</u>	<u>\$ -</u>	<u>\$ 8,939,381</u>	<u>\$519,986,325</u>	<u>\$ 9,135,000</u>

Long-term obligation activity for the year ended June 30, 2013, is as follows:

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending Balance</u>	<u>Due Within One Year</u>
Revenue bonds	\$491,440,000	\$ -	\$ -	\$491,440,000	\$ 8,805,000
Bond anticipation notes	20,000,000	15,000,000	-	35,000,000	-
Unamortized debt discount	(2,369,303)	-	(107,121)	(2,262,181)	-
Unamortized debt premium	4,989,390	-	241,503	4,747,887	-
TOTALS	<u>\$514,060,087</u>	<u>\$ 15,000,000</u>	<u>\$ 134,382</u>	<u>\$528,925,706</u>	<u>\$ 8,805,000</u>

Total debt service to maturity:

<u>Maturities</u>	<u>Principal</u>	<u>Interest</u>	<u>Subsidized Interest</u>	<u>Total</u>
2015	\$ 9,135,000	\$ 25,510,689	\$ 2,716,877	\$ 31,928,812
2016	9,525,000	25,122,170	2,716,877	31,930,293
2017	11,615,000	24,658,912	2,716,877	33,557,035
2018	45,380,000	24,540,575	2,716,877	67,203,698
2019	10,845,000	23,715,737	2,716,877	31,843,860
2020-2024	62,870,000	109,942,785	13,584,384	159,228,401
2025-2029	80,025,000	91,127,682	13,349,604	157,803,078
2030-2034	100,800,000	65,942,179	10,319,407	156,422,772
2035-2039	114,935,000	34,267,643	5,393,620	143,809,023
2040-2044	72,505,000	7,862,794	508,759	79,859,035
TOTALS	<u>\$ 517,635,000</u>	<u>\$ 432,691,166</u>	<u>\$ 56,740,159</u>	<u>\$ 893,586,007</u>

(Continued)

**KENTUCKY MUNICIPAL POWER AGENCY
NOTES TO FINANCIAL STATEMENTS**

Note 6 - Long-Term Indebtedness:

Bond Covenant Disclosures

The following information is provided in compliance with the resolution creating the 2007 A and B revenue bonds and the 2010 A, B, and C revenue bonds:

Insurance

The Agency is exposed to various risks of loss related to torts, theft of, damage to, or destructions of assets, errors and omissions, workers compensation, and health care of its employees. These risks are covered through the purchase of commercial insurance, with minimal deductibles. Settled claims have not exceeded coverage in any of the last three years.

The Agency is covered under the following insurance policies at June 30, 2014:

Type	Coverage	Expiration
General & Public Officials Liability	\$10,000,000	January 17, 2015

Note 7 - Net Assets:

GASB No. 34 requires the classification of net assets into three components - invested in capital assets, net of related debt; restricted; and unrestricted. These classifications are defined as follows:

Invested in capital assets, net of related debt - This component of net 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. If there are significant unspent related debt proceeds at year-end, the portion of the debt attributable to the unspent proceeds is not included in the calculation of invested in capital assets, net of related debt. Rather, that portion of the debt is included in the same net assets component as the unspent proceeds.

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

Unrestricted net assets - This component of net assets consists of net assets that do not meet the definitions of "restricted" or "invested in capital assets, net of related debt".

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

The following calculation supports the Agency's net assets invested in capital assets, net of related debt:

(Continued)

KENTUCKY MUNICIPAL POWER AGENCY
NOTES TO FINANCIAL STATEMENTS

Note 7 - Net Assets:

	<u>2014</u>	<u>2013</u>
Property, plant, and equipment	\$ 453,158,404	\$ 454,226,543
Less accumulated depreciation	(23,208,840)	(11,201,999)
Working capital and collateral Prairie State	3,473,085	3,256,526
Construction work in progress	<u>5,080,105</u>	<u>575,244</u>
Sub-totals	<u>438,502,754</u>	<u>446,856,314</u>
Less: Capital related debt		
Bonds held by public	(482,635,000)	(491,440,000)
Bond anticipation notes	(35,000,000)	(35,000,000)
Unamortized bond issuance cost	5,423,217	5,668,826
Asset retirement obligation	(1,564,832)	(1,198,128)
Unamortized debt discount	2,155,059	2,262,181
Unamortized debt premium	<u>(4,506,384)</u>	<u>(4,747,887)</u>
Sub-totals	<u>(516,127,940)</u>	<u>(524,455,008)</u>
Add: Unspent debt proceeds		
Project fund	-	5,941,419
Reserve fund	37,089,284	36,486,841
Pledged collateral	<u>-</u>	<u>-</u>
Sub-totals	<u>37,089,284</u>	<u>42,428,260</u>
TOTAL NET ASSETS INVESTED IN CAPITAL ASSETS, NET OF RELATED DEBT	<u>\$ (40,535,902)</u>	<u>\$ (35,170,434)</u>

Note 8 - Commitments and Contingencies:

Prairie State Energy Campus

In February 2005, the Agency joined several other entities in the development of the Prairie State Energy Campus, a 1600 MW twin unit, coal-fired electric generating facility to be located in Washington, St. Claire, and Randolph counties, Illinois (the "Prairie State Project"). In addition to the generation station, the Prairie State Project includes coal reserves, a coal mine, a coal combustion waste disposal facility, and other ancillary support equipment. The Prairie State Project is being developed by the Prairie State Generating Company, LLC ("PSGC"), initially a wholly-owned subsidiary of Peabody Energy Corporation and now controlled by the nine owners.

Since entering the project, the Agency has increased its participation from an initial 80 MW level to its present 124 MW share. After financial closing of the transaction, the Agency's share translated into a 7.82% undivided ownership interest as a tenant-in-common with the other project participants. The other joint owners in the Prairie State Project are the American Municipal Power, Illinois Municipal Electric Agency, the Indiana Municipal Power Agency, the Missouri Public Utility Alliance, The Northern Illinois Municipal Power Agency, Prairie Power, Inc. (formerly known as Soyland Power Cooperative, Inc.), Lively Grove Energy Partners, LLC, a wholly-owned indirect subsidiary of Peabody Energy Corporations ("Peabody Energy"), and Southern Illinois Power Cooperative.

Pursuant to the terms of the Project Development Agreement dated February 5, 2005, the Fee Agreement of the same date, and the AI Fee Agreement dated August 31, 2006, the Agency paid certain fees for the right to participate in the Prairie State Project and ultimately own its share of the coal reserves and other project assets at financial close. On June 19, 2007, the Agency executed, amended, and restated versions of the Project Development Agreement, the Fee Agreement, and the AI Fee Agreement. The amended

(Continued)

**KENTUCKY MUNICIPAL POWER AGENCY
NOTES TO FINANCIAL STATEMENTS**

Note 8 - Commitments and Contingencies:

Prairie State Energy Campus

agreements memorialized certain changes in the various percentage ownership interests of the participants in the Project and certain changes regarding the manner in which the Project will be developed. The Agency is also obligated under the agreements to pay its proportionate share of all ongoing costs and expenses associated with the Prairie State Project. The Agency's cost for participation in the project total \$17.2 million.

In July 2010, the owners entered into an agreement with Bechtel Corporation ("Bechtel") to convert the original, cost reimbursable EPC Agreement for the Prairie State Project to a lump sum turn-key EPC Agreement. This agreement provides the owners with a cap on future cost increases, and transfers cost and schedule risk from the owners to Bechtel. Provisional completion of Unit 1 was achieved on June 6, 2012, at which time Prairie State Generating Company took care custody and control of the unit. Provisional completion of Unit 2 was achieved on November 1, 2012, at which time Prairie State Generating Company took care custody and control of the unit.

The Agency has entered in Power Sales Agreements described below in order to provide additional power to its members.

Power Sales Agreement

The Boards of Paducah Power System and Princeton Electric authorized a Power Sales Agreement with the Agency on July 23, 2007. The Power Sales Agreement is a take or pay agreement that stipulates that Paducah Power System and Princeton Electric will take all power from the Agency which the Agency receives from the Prairie State Project. Paducah Power System's share of the energy is 83.7% and Princeton Electric's is 16.3%.

Each party to the Power Sales Agreement agrees to a step up of 20% additional power in the case that the other party to the agreement defaults on its commitment. This effectively means that Paducah Power System agrees, if necessary, to commit to take all power from the Agency since Princeton Electric's share of power is less than 20% of the project.

The Agency has entered into transactions for the purchase of blocks or strips of electric capacity and energy of varying sizes with a number of electric power suppliers. These strips of purchased power cover periods of varying lengths. Each of the transactions was entered into within the framework of an EEI Master Power Purchase & Sale Agreement ("Master Agreement") between the Agency and the power supplier. The Agency purchased 5 x 16 strips of power from NextEra Energy Power Marketing, LLC on November 14, 2011. The price of the power purchased in these transactions was \$49.50/MWh for delivery to the Cinergy Hub of the Midwest Independent Transmission System Operator ("MISO"). The price does not include the cost of transmitting the power to the Agency's members, the Electric Plant Boards of the Cities of Paducah and Princeton, Kentucky (the "Members") from the Cinergy Hub.

All of the Agency's power purchase transactions are considered "firm" obligations in that they are backed by provisions requiring the payment of liquidated damages in the event of non-delivery, as is standard in the EEI Master Power Purchase & Sale Agreement; however, seller's failure to deliver is not considered an event of default.

Under the Master Agreements for each of the above-referenced purchases, either party may call for collateral to be posted by the other when the calling party is "in the money" based on a mark-to-market calculation. The effect is that the Agency can be required to post collateral whenever the market value of

(Continued)

**KENTUCKY MUNICIPAL POWER AGENCY
NOTES TO FINANCIAL STATEMENTS**

Note 8 - Commitments and Contingencies:

Power Sales Agreement

the transactions entered into pursuant to a particular Master Agreement drops far enough below the contract price. Each Master Agreement establishes a collateral threshold for the Agency against which the cumulative mark-to-market value of the transactions entered to is measured on each day of the life of the contract. On days when the collateral threshold is exceeded, a party that is in the money may require the other to provide some acceptable form of performance assurance such as cash collateral, appropriate guaranties, and/or a letter of credit. The Agency's Members have executed guaranty agreements that can be called upon to satisfy all or a portion of the performance assurance requirements in certain instances. A party that is "in the money" may make a collateral call even if its counter-party is not in default and there is no substantial concern about the counter-party's creditworthiness. The collateral thresholds applicable to the Agency under the Master Agreements have been termed "very generous" by the Agency's power supply consultant, Fellon-McCord & Associates, and are expected to permit the Agency to operate without having to provide unduly burdensome performance assurances.

The Agency has also procured from Macquarie Energy, LLC, formerly Integrys Energy Services, Inc., ("Macquarie") options to purchase certain 5 x 16 strips of power for the period December 2009 through December 2014. The options may be exercised on a day ahead basis at a price that is a certain dollar amount above a MISO index price. These options were acquired on June 9, 2008 and November 25, 2008. Due to power supply needs, the Agency exercised these options during fiscal year 2010. The Agency did not exercise these options during the fiscal years 2013 or 2014.

Claims and Judgments

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

Note 9 - Disclosures Regarding the Statement of Cash Flows:

Accounting Policy

For purposes of the Statement of Cash Flows, cash and cash investments include all highly liquid debt instruments with maturities of three months or less.

The composition of cash and cash investments at June 30, 2014 and 2013, is as follows:

	<u>2014</u>	<u>2013</u>
Cash and temporary cash investments	\$ 5,075,047	\$ 3,318,403
Restricted cash and short-term investments:		
Project and reserve funds and pledged collateral	<u>18,024,589</u>	<u>8,099,636</u>
TOTAL CASH AND CASH INVESTMENTS	<u>\$23,099,636</u>	<u>\$11,418,039</u>

Note 10 - Subsequent Events:

The Agency did not have any subsequent events through February 9, 2015, which is the date the financial statements were available to be issued for events requiring recording or disclosure in the financial statements for the year ended June 30, 2014.

SUPPLEMENTARY INFORMATION

KENTUCKY MUNICIPAL POWER AGENCY
OPERATING EXPENSES
YEARS ENDED JUNE 30

General Operating Expenses:	<u>2014</u>	<u>2013</u>
Administrative and general:		
Payroll	\$ 872,489	\$ 959,370
Office supplies and expense	848,836	350,757
Outside services employment	1,535,355	528,585
Depreciation	12,006,840	10,560,650
Depletion	142,911	-
Insurance	378,845	268,866
Injuries and damages	115,383	116,609
General plant maintenance	<u>118,543</u>	<u>52,305</u>
 Total administrative and general	 <u>16,019,202</u>	 <u>12,837,142</u>
 TOTAL GENERAL OPERATING EXPENSES	 <u><u>\$16,019,202</u></u>	 <u><u>\$12,837,142</u></u>

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Independent Auditor's Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards*

To the Board of Directors
Kentucky Municipal Power Agency
Paducah, Kentucky

We have audited, in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, the financial statements of Kentucky Municipal Power Agency as of and for the year ended June 30, 2014, and the related notes to the financial statements, which collectively comprise the Kentucky Municipal Power Agency's basic financial statements, and have issued our report thereon dated February 9, 2015.

Internal Control Over Financial Reporting

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

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Kentucky Municipal Power Agency's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance

with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

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.

A handwritten signature in cursive script that reads "Williams, Williams & Fenty LLP".

Paducah, Kentucky
February 9, 2015