REPORT OF THE AUDIT OF THE LEE COUNTY FISCAL COURT

For The Fiscal Year Ended June 30, 2007

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CERTIFICATION OF COMPLIANCE - LOCAL GOVERNMENT ECONOMIC ASSISTANCE PROGRAM 42

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To the People of Kentucky
Honorable Steven L. Beshear, Governor
Johnathan Miller, Secretary
Finance and Administration Cabinet
Honorable Steve Mays, Lee County Judge/Executive
Members of the Lee County Fiscal Court

Independent Auditors' Report

We have audited the accompanying financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of Lee County, Kentucky, as of and for the year ended June 30, 2007, which collectively comprise the County's basic financial statements, as listed in the table of contents. These financial statements are the responsibility of the Lee County Fiscal Court. Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, and the *Audit Guide For Fiscal Court Audits* issued by the Auditor of Public Accounts, Commonwealth of Kentucky. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

As described in Note 1, Lee County, Kentucky, prepares its financial statements on a prescribed basis of accounting that demonstrates compliance with the modified cash basis, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, each major fund, and the aggregate remaining fund information of Lee County, Kentucky, as of June 30, 2007, and the respective changes in financial position, thereof for the year then ended in conformity with the modified cash basis of accounting.

In accordance with *Government Auditing Standards*, we have also issued our report dated December 3, 2007, on our consideration of Lee County, 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 the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

To the People of Kentucky
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Members of the Lee County Fiscal Court

The county has not presented the management's discussion and analysis that the Governmental Accounting Standards Board (GASB) has determined is necessary to supplement, although not required to be part of, the basic financial statements. The budgetary comparison information is not a required part of the basic financial statements but is supplementary information required by GASB. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the budgetary comparison information. However, we did not audit it and express no opinion on it.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the primary government of Lee County, Kentucky's basic financial statements. The accompanying supplementary information and combining fund financial statements, are presented for purposes of additional analysis and are not a required part of the basic financial statements. The combining fund financial statements have been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, are fairly stated in all material respects in relation of the basic financial statements taken as a whole.

Based on the results of our audit, we present the comment and recommendation, included herein, which discusses the following report comment:

2007-1 The County Should Implement Better Internal Control Procedures Over Solid Waste Collections And Billings

Respectfully submitted,

Morgan - Franklin, LLC

Morgan-Franklin, LLC

December 3, 2007

LEE COUNTY OFFICIALS

For The Year Ended June 30, 2007

Fiscal Court Members:

Steve Mays	County Judge/Executive
Ronnie Paul Begley	Magistrate
Lenard Carl Ross	Magistrate
Bennie Todd	Magistrate
Billy Joe Coomer	Magistrate

Other Elected Officials:

Thomas Hollon	County Attorney
Corbett Dunaway	Jailer
Russell Stamper	County Clerk
Emma Adams	Circuit Court Clerk
Donnie Hogan	Sheriff
Elizabeth Roach	Property Valuation Administrator
Ray Shuler	Coroner

Appointed Personnel:

Pearl Spencer	County Treasurer

LEE COUNTY
STATEMENT OF NET ASSETS - MODIFIED CASH BASIS

June 30, 2007

LEE COUNTY
STATEMENT OF NET ASSETS - MODIFIED CASH BASIS

June 30, 2007

	Primary Governmental Governmental Activities
ASSETS	
Current Assets:	
Cash and Cash Equivalents	$ 709,109
Capital Asset Held For Resale	296,172
Total Current Assets	1,005,281
Noncurrent Assets:	
Capital Assets - Net of Accumulated Depreciation	
Land	280,094
Construction In Progress	116,316
Buildings	1,595,263
Other Equipment	221,700
Vehicles	474,477
Equipment	245,382
Infrastructure Assets - Net of Depreciation	1,464,396
Total Noncurrent Assets	4,397,628
Total Assets	5,402,909
LIABILITIES	
Current Liabilities:	
Financing Obligations	358,059
Noncurrent Liabilities:	
Financing Obligations	269,584
Total Liabilities	627,643
NET ASSETS	
Invested in Capital Assets, Net of Related Debt	4,066,157
Unrestricted	709,109
Total Net Assets	$ 4,775,266

The accompanying notes are an integral part of the financial statements.

LEE COUNTY
STATEMENT OF ACTIVITIES - MODIFIED CASH BASIS

For The Year Ended June 30, 2007

LEE COUNTY
STATEMENT OF ACTIVITIES - MODIFIED CASH BASIS

For The Year Ended June 30, 2007

Functions/Programs Reporting Entity	Expenses	Program Revenues Received: Charges for Services	Program Revenues Received: Operating Grants and Contributions	Program Revenues Received: Capital Grants and Contributions
Primary Government:				
Governmental Activities:				
General Government	$ 1,186,805	$	$ 192,734	$ 46,269
Protection to Persons and Property	1,181,435	832,882	64,290	
General Health and Sanitation	437,898	352,336	82,451	
Social Services	61,589			
Recreation and Culture	27,104	58		
Roads	830,639		1,717,631	
Interest On L/T & S/T Debt	37,716			
Capital Projects	97,588			
Total Governmental Activities	$ 3,860,774	$ 1,185,276	$ 2,057,106	$ 46,269

The accompanying notes are an integral part of the financial statements.

LEE COUNTY
STATEMENT OF ACTIVITIES - MODIFIED CASH BASIS
For The Year Ended June 30, 2007
(Continued)

	Net (Expenses) Revenues and Changes in Net Assets Primary Government
	Governmental Activities
	$ (947,802)
	(284,263)
	(3,111)
	(61,589)
	(27,046)
	886,992
	(37,716)
	(97,588)
	(572,123)
General Revenues:	
Taxes:	
Real Property Taxes	735,142
Personal Property Taxes	69,093
Motor Vehicle Taxes	86,006
Other Taxes	26,609
Coal Severance Projects	351,671
In Lieu Payments	21,800
Excess Fees	1,067
E-911 Fees	35,380
Licenses and Permits	20,742
Unrestricted Investment Earnings	6,185
General Revenue	40,040
Miscellaneous Revenues	242,687
Total General Revenues	1,636,422
Change in Net Assets	1,064,299
Net Asset - Beginning	3,710,967
Net Asset - Ending	$ 4,775,266

The accompanying notes are an integral part of the financial statements.

LEE COUNTY
BALANCE SHEET - GOVERNMENTAL FUNDS - MODIFIED CASH BASIS

June 30, 2007

LEE COUNTY
BALANCE SHEET - GOVERNMENTAL FUNDS - MODIFIED CASH BASIS

June 30, 2007

	General Fund	Road Fund	Ambulance Fund	Non Major Funds	Total Governmental Funds
ASSETS					
Cash and Cash Equivalents	$ 410,453	$ 128,289	$ 26,509	$ 143,858	$ 709,109
Total Assets	$ 410,453	$ 128,289	$ 26,509	$ 143,858	$ 709,109
FUND BALANCES					
Reserved for:					
Encumbrances	$ 6,673	$ 17,065	$ 4,931	$ 11,633	$ 40,302
Unreserved:					
General Fund	403,780				403,780
Special Revenue Funds		111,224	21,578	132,225	265,027
Total Fund Balances	$ 410,453	$ 128,289	$ 26,509	$ 143,858	$ 709,109

Reconciliation of Balance Sheet - Governmental Funds to Statement of Net Assets:

Total Fund Balances	$ 709,109
Amounts Reported for Governmental Activities in the Statement of Net Assets are Different Because:	
Capital Assets of $5,896,611 Net of Accumulated Depreciation of $1,498,983 Used in Governmental Activities are not Financial Resources and Therefore are not Reported in the Funds.	4,397,628
Capital Assets Held For Resale	296,172
Short-term and Long-term Debt is not Due and Payable in the Current Period and, Therefore, is not Reported in the Funds.	
Financing Obligations	(627,643)
Net Assets of Governmental Activities	$ 4,775,266

The accompanying notes are an integral part of the financial statements.

LEE COUNTY
STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES
IN FUND BALANCES - GOVERNMENTAL FUNDS - MODIFIED CASH BASIS

For The Year Ended June 30, 2007

LEE COUNTY
STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES
IN FUND BALANCES - GOVERNMENTAL FUNDS - MODIFIED CASH BASIS

For The Year Ended June 30, 2007

	General Fund	Road Fund	Ambulance Fund	Non-Major Funds	Total Governmental Funds
REVENUES					
Taxes	$ 1,303,901	$	$	$	$ 1,303,901
In Lieu	9,733	12,068			21,801
Excess Fees	1,067				1,067
Licenses and Permits	20,742				20,742
Intergovernmental	239,043	1,383,337	10,684	511,352	2,144,416
Charges for Services	5,348		826,496	352,430	1,184,274
Miscellaneous	154,821	298,615	17,234	15,875	486,545
Interest	3,343	1,759	280	803	6,185
Total Revenues	1,737,998	1,695,779	854,694	880,460	5,168,931
EXPENDITURES					
General Government	611,328				611,328
Protection to Persons and Property	167,155		713,428	241,029	1,121,612
General Health and Sanitation				408,656	408,656
Social Services	61,717				61,717
Recreation and Culture	179,022				179,022
Roads	62,750	1,503,571		60,624	1,626,945
Debt Service	6,534	331,283		43,605	381,422
Capital Projects	163,077	7,105			170,182
Administration	213,185	88,489	219,592	68,880	590,146
Total Expenditures	1,464,768	1,930,448	933,020	822,794	5,151,030
Excess (Deficiency) of Revenues Over Expenditures Before Other Financing Sources (Uses)	273,230	(234,669)	(78,326)	57,666	17,901
Other Financing Sources (Uses)					
Financing Obligation Proceeds		299,835			299,835
Transfers from Other Funds			90,000	204,169	294,169
Transfers to Other Funds	(90,169)			(204,000)	(294,169)
Total Other Financing Sources (Uses)	(90,169)	299,835	90,000	169	299,835
Net Change in Fund Balances	183,061	65,166	11,674	57,835	317,736
Fund Balances - Beginning	227,392	63,123	14,835	86,023	391,373
Fund Balances - Ending	$ 410,453	$ 128,289	$ 26,509	$ 143,858	$ 709,109

The accompanying notes are an integral part of the financial statements.

LEE COUNTY
RECONCILIATION OF THE STATEMENT OF REVENUES,
EXPENDITURES, AND CHANGES IN FUND BALANCES OF
GOVERNMENTAL FUNDS TO THE STATEMENT OF ACTIVITIES - MODIFIED CASH BASIS

For The Year Ended June 30, 2007

LEE COUNTY
RECONCILIATION OF THE STATEMENT OF REVENUES,
EXPENDITURES, AND CHANGES IN FUND BALANCES OF
GOVERNMENTAL FUNDS TO THE STATEMENT OF ACTIVITIES - MODIFIED CASH BASIS

For The Year Ended June 30, 2007

Net Change in Fund Balances - Total Governmental Funds	$ 317,736
Governmental Funds Report Capital Outlays as Expenditures. However, in the Statement of Activities the Cost of Those Assets are Allocated Over Their Estimated Useful Lives and Reported as Depreciation Expense.	
Capital Outlay	1,020,454
Depreciation Expense	(304,859)
Net Book Value of Disposed Assets	(40,275)
Asset Held For Resale Purchase	296,172
Assets Held For Resale Disposal	(268,800)
Financing Obligation and Bond Principal Payments are Expensed in the Governmental Funds as a Use of Current Financial Resources. However, These Transactions Have no Effect on Net Assets.	
Financing Obligation Principal Payments	343,706
The Issuance of Long-Term and Short-Term Debt Provides Current Finanacial Resources to Governmental Funds. These Transactions, However; Have no Effect on Net Assets:	
Lease Proceeds	(299,835)
Change in Net Assets of Governmental Activities	$ 1,064,299

The accompanying notes are an integral part of the financial statements.

Note 1. Summary of Significant Accounting Policies

A. Basis of Presentation

The county presents its government-wide and fund financial statements in accordance with a modified cash basis of accounting, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America. Under this basis of accounting, assets, liabilities, and related revenues and expenditures are recorded when they result from cash transactions, with a few exceptions. This modified cash basis recognizes revenues when received and expenditures when paid. Notes receivable are recognized on the Statement of Net Assets, but notes receivable are not included and recognized on Balance Sheet - Governmental Funds. Property tax receivables, accounts payable, compensated absences, and donated assets are not reflected in the financial statements.

Encumbrances lapse at year-end and are not reflected on the Statement of Net Assets and Statement of Activities; however encumbrances are reflected on the Balance Sheet - Governmental Funds as part of the fund balance (Reserved for Encumbrances).

The State Local Finance Officer does not require the county to report capital assets and infrastructure; however the value of these assets is included in the Statement of Net Assets and the corresponding depreciation expense is included on the Statement of Activities.

B. Reporting Entity

The financial statements of Lee County should include the funds, agencies, boards, and entities for which the fiscal court is financially accountable. Financial accountability, as defined by Section 2100 of the Governmental Accounting Standards Board (GASB) *Codification of Governmental Accounting and Financial Reporting Standards*, as amended by GASB 14 and GASB 39, was determined on the basis of the government's ability to significantly influence operations, select the governing authority, participate in fiscal management and the scope of public service. Consequently, the reporting entity includes organizations that are legally separate from the primary government. Legally separate organizations are reported as component units if either the county is financially accountable or whose exclusion would cause the county's financial statements to be misleading or incomplete. Component units may be blended or discretely presented. Blended component units either provide their services exclusively or almost entirely to the primary government, or their governing bodies are substantively the same as the primary government. All other component units are discretely presented. The County has no discretely presented component units.

Blended Component Unit

The following legally separate organization provides its services exclusively to the primary government, and the fiscal court is able to impose its will on this organization. This organization's balances and transactions are reported as though they are part of the county's primary government using the blending method.

Note 1. Summary of Significant Accounting Policies (Continued)

B. Reporting Entity (Continued)

Blended Component Unit (Continued)

Public Service Corporation

The Public Service Corporation is a legally separate entity established to provide debt service for the purchase of real estate property from the Kentucky Mountains Farm Cooperative. The Public Service Corporation's governing body consists entirely of Fiscal Court members. Therefore, management should include the Public Service Corporation as a component unit, and its financial activity should be blended with the Fiscal Court. However, the Public Service Corporation had no financial activity during the year and had no financial information to blend with that of the fiscal court.

C. Lee County Elected Officials

Kentucky law provides for election of the officials below from the geographic area constituting Lee County. Pursuant to state statute, these officials perform various services for the Commonwealth of Kentucky, its judicial courts, the fiscal court, various cities and special districts within the county, and the board of education. In exercising these responsibilities, however, they are required to comply with state laws. Audits of their financial statements are issued separately and individually and can be obtained from their respective administrative offices. These financial statements are not required to be included in the financial statements of Lee County, Kentucky.

- Circuit Court Clerk
- County Attorney
- Property Valuation Administrator
- County Clerk
- County Sheriff

D. Government-wide and Fund Financial Statements

The government-wide financial statements (i.e., the statement of net assets and the statement of activities) report information on all of the non-fiduciary activities of the primary government and its non-fiduciary component units. For the most part, the effect of interfund activities has been removed from these statements. Governmental activities are normally supported by taxes and intergovernmental revenues.

The statement of net assets presents the reporting entity's non-fiduciary assets and liabilities, the difference between the two being reported as net assets. Net assets are reported in three categories: 1) invested in capital assets, net of related debt - consisting of capital assets, net of accumulated depreciation and reduced by outstanding balances for debt related to the acquisition, construction, or improvement of those assets; 2) restricted net assets - resulting from constraints placed on net assets by creditors, grantors, contributors, and other external parties, including those constraints imposed by law through constitutional provisions or enabling legislation; and 3) unrestricted net assets - those assets that do not meet the definition of restricted net assets or invested in capital assets.

Note 1. Summary of Significant Accounting Policies (Continued)

D. Government-wide and Fund Financial Statements (Continued)

The statement of activities demonstrates the degree to which the direct expenses of a given function are offset by program revenues. Direct expenses are those that are clearly identifiable with a specific function. Program revenues include: 1) charges to customers or applicants who purchase, use, or directly benefit from goods, services, or privileges provided by a given function; 2) operating grants and contributions; and 3) capital grants and contributions that are restricted to meeting the operational or capital requirements of a particular function. Internally dedicated resources such as taxes and unrestricted state funds are reported as general revenues.

Funds are characterized as either major or non-major. Major funds are those whose assets, liabilities, revenues, or expenditures/expenses are at least ten percent of the corresponding total (assets, liabilities, etc.) for all funds or type (governmental or proprietary) and whose total assets, liabilities, revenues, or expenditures/expenses are at least five percent of the corresponding total for all governmental and enterprise funds combined. The fiscal court may also designate any fund as major. Major individual governmental funds are reported as separate columns in the financial statements.

Governmental Funds

The primary government reports the following major governmental funds:

General Fund - This is the primary operating fund of the fiscal court. It accounts for all financial resources of the general government, except where the Governor's Office for Local Development requires a separate fund or where management requires that a separate fund be used for some function.

Road Fund - This fund is for road and bridge construction and repair. The primary source of revenue for this fund is state payments for truck licenses distribution, municipal road aid, and transportation grants. The Governor's Office for Local Development requires the fiscal court to maintain these receipts and expenditures separately from the General Fund.

Ambulance Fund – This fund accounts for all revenues from uses of the Ambulance Service along with some state contributions.

The primary government also has the following non-major funds: Jail, Local Government Economic Assistance, Solid Waste, and Handicap Van Funds.

Note 1. Summary of Significant Accounting Policies (Continued)

D. Government-wide and Fund Financial Statements (Continued)

Special Revenue Funds:

The Road Fund, Ambulance Fund, Jail Fund, Local Government Economic Assistance Fund, Solid Waste Fund, and Handicap Van Fund are presented as special revenue funds. Special revenue funds are used to account for the proceeds of specific revenue sources and expenditures that are legally restricted for specific purposes.

E. Property Tax Calendar

Generally and except as otherwise provided by law, property taxes are assessed as of January 1, levied (mailed) November 1, due at discount November 30, due at face value December 31, delinquent January 31 following the assessment, and subject to lien and sale April 30 following the delinquency date.

F. Deposits and Investments

The government's cash and cash equivalents are considered to be cash on hand, demand deposits, certificates of deposit, and short-term investments with original maturities of three months or less from the date of acquisition.

KRS 66.480 authorizes the county to invest in the following, including but not limited to, obligations of the United States and of 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, obligations of any corporation of the United States government, bonds or certificates of indebtedness of this state, and certificates of deposit issued by or other interest-bearing accounts of any bank or savings and loan institution which are insured by the Federal Deposit Insurance Corporation (FDIC) or which are collateralized, to the extent uninsured, by any obligation permitted by KRS 41.240(4).

G. Capital Assets

Capital assets, which include land, land improvements, buildings, furniture and office equipment, building improvements, machinery, equipment, and infrastructure assets (roads and bridges) that have a useful life of more than one reporting period based on the government's capitalization policy, are reported in the applicable governmental or business-type activities of the government-wide financial statements. Such assets are recorded at historical cost or estimated historical cost when purchased or constructed. However, the county has elected not to report major general infrastructure assets retroactively.

Note 1. Summary of Significant Accounting Policies (Continued)

G. Capital Assets (Continued)

Cost of normal maintenance and repairs that do not add to the value of the asset or materially extend the asset's life are not capitalized. Land and Construction In Progress are not depreciated. Interest incurred during construction is not capitalized. Capital assets and infrastructure are depreciated using the straight-line method of depreciation over the estimated useful life of the asset.

	Capitalization Threshold	Useful Life (Years)
Land Improvements	$ 12,500	10-60
Buildings and Building Improvements	$ 25,000	10-75
Machinery and Equipment	$ 2,500	3-25
Vehicles	$ 2,500	3-25
Infrastructure	$ 20,000	10-50

H. Long-term Obligations

In the government-wide financial statements and proprietary fund types in the fund financial statements, long term debt and other long-term obligations are reported as liabilities in the applicable financial statements. The principal amount of bonds, notes and financing obligations are reported.

In the fund financial statements, governmental fund types recognize bond interest, as well as bond issuance costs when received or when paid, during the current period. The principal amount of the debt and interest are reported as expenditures. Issuance costs, whether or not withheld from the actual debt proceeds received, are reported as expenditures. Debt proceeds are reported as other financing sources.

I. Fund Equity

In the fund financial statements, the difference between the assets and liabilities of governmental funds is reported as fund balance. Fund balance is divided into reserved and unreserved components, with unreserved considered available for new spending. Unreserved fund balances may be divided into designated and undesignated portions. Designations represent fiscal court's intended use of the resources and should reflect actual plans approved by the fiscal court.

Governmental funds report reservations of fund balance for amounts that are legally restricted by outside parties for use for a specific purpose, long-term receivables, and encumbrances.

"Reserved for Encumbrances" are purchase orders that will be fulfilled in a subsequent fiscal period. Although the purchase order or contract creates a legal commitment, the fiscal court incurs no liability until performance has occurred on the part of the party with whom the fiscal court has entered into the arrangement. When a government intends to honor outstanding commitments in subsequent periods, such amounts are encumbered. Encumbrances lapse at year-end and are not reflected on the Statement of Net Assets and Statement of Activities; however, encumbrances are reflected on the Balance Sheet - Governmental Funds as part of the fund balance.

Note 1. Summary of Significant Accounting Policies (Continued)

J. Budgetary Information

Annual budgets are adopted on a cash basis of accounting and according to the laws of Kentucky as required by the State Local Finance Officer.

The County Judge/Executive is required to submit estimated receipts and proposed expenditures to the fiscal court by May 1 of each year. The budget is prepared by fund, function, and activity and is required to be adopted by the fiscal court by July 1.

The fiscal court may change the original budget by transferring appropriations at the activity level; however, the fiscal court may not increase the total budget without approval by the State Local Finance Officer. Expenditures may not exceed budgeted appropriations at the activity level.

K. Joint Venture

A legal entity or other organization that results from a contractual agreement and that is owned, operated, or governed by two or more participants as a separate activity subject to joint control, in which the participants retain (a) an ongoing financial interest or (b) an ongoing financial responsibility is a joint venture. Based upon these criteria, the following is considered a joint venture of the Lee County Fiscal Court:

Three Forks Regional Jail

On October 6, 2000, the Counties of Lee, Owsley, and Wolfe (the participating counties) entered into an Interlocal Cooperation Agreement in order to provide for joint and cooperative action in the acquisition, construction, installation, maintenance and financing of the Three Forks Regional Jail. Pursuant to this interlocal agreement, Lee County (the lead county) established the Three Forks Public Properties Corporation, a legally separate organization, to act as an agency and instrumentality of the participating counties in financing the acquisition and construction of the Three Forks Regional Jail. On December 1, 2000, the corporation issued $6,295,000 of mortgage revenue bonds.

The only source of funds expected by the Three Forks Public Properties Corporation to meet the debt service requirements on the bonds are the rental payment from the participating counties, as stipulated in the lease and sublease agreements dated October 1, 2000. Pursuant to the lease and sublease, each participating county covenants to met its proportionate share of the debt service requirements on the bonds as follows (the "proportionate share" or "use allowance"): 40% for Lee County, 22% for Owsley County and 38% for Wolfe County.

On December 1, 2000, the three participating counties established the Three Forks Regional Jail Authority pursuant to the provisions of KRS 441.800 and KRS 441.810 to act as the constituted authority of the participating counties in the acquisition, construction, equipping and operation of the Three Forks Regional Jail.

The Three Forks Regional Jail Authority and the Three Fork's Public Properties Corporation are comprised on an eight (8) member board of directors. Lee County appoints three of the eight members. Wolfe and Owsley counties appoint two members each. In addition, the Lee County Jailer is a required member of the board.

A copy of the Three Forks Regional Jail Authority's audit report may be obtained by writing the Three Forks Regional Jail, 2475 Center Street, Beattyville, Kentucky 41311.

Note 2. Deposits

The primary government maintained deposits of public funds with depository institutions insured by the Federal Deposit Insurance Corporation (FDIC). According to KRS 66.480(1)(d) and KRS 41.240(4), the depository institution should pledge or provide sufficient collateral which, together with FDIC insurance, equals or exceeds the amount of public funds on deposit at all times. In order to be valid against the FDIC in the event of failure or insolvency of the depository institution, this pledge or provision of collateral should be evidenced by an agreement between the county and the depository institution, signed by both parties, that is (a) in writing, (b) approved by the board of directors of the depository institution or its loan committee, which approval must be reflected in the minutes of the board or committee, and (c) an official record of the depository institution. These requirements were met.

Custodial Credit Risk – Deposits

Custodial credit risk is the risk that in the event of a depository institution failure, the County's deposits may not be returned to it. The County does not have a deposit policy for custodial credit risk but rather follows the requirements of KRS 41.240(4). As of August 31, 2006, $166,818 of the County's bank balance of $1,066,818 was exposed to custodial credit risk at People's Bank as follows:

Uninsured and unsecured	$ 166,818

Note 3. Capital Assets

Capital asset activity for the year ended June 30, 2006 was as follows:

	Reporting Entity			
Primary Government:	Beginning Balance	Increases	Decreases	Ending Balance
Governmental Activities:				
Capital Assets Not Being Depreciated:				
Land	$ 240,094	$ 40,000	$	$ 280,094
Construction In Progress	58,200	70,316	(12,200)	116,316
Total Capital Assets Not Being Depreciated	298,294	110,316	(12,200)	396,410
Capital Assets, Being Depreciated:				
Buildings	2,027,975	126,697		2,154,672
Other Equipment	287,607	83,080		370,687
Vehicles	893,564	12,000	(66,752)	838,812
Equipment	442,502	70,050	(56,727)	455,825
Infrastructure	1,049,694	630,511		1,680,205
Total Capital Assets Being Depreciated	4,701,342	922,338	(123,479)	5,500,201
Less Accumulated Depreciation For:				
Buildings	(526,130)	(33,279)		(559,409)
Other Equipment	(108,210)	(40,777)		(148,987)
Vehicles	(345,830)	(78,057)	59,552	(364,335)
Equipment	(202,684)	(31,411)	23,652	(210,443)
Infrastructure	(94,474)	(121,335)		(215,809)
Total Accumulated Depreciation	(1,277,328)	(304,859)	83,204	(1,498,983)
Total Capital Assets, Being Depreciated, Net	3,424,014	617,479	(40,275)	4,001,218
Governmental Activities Capital Assets, Net	$ 3,722,308	$ 727,795	$ (52,475)	$ 4,397,628

Depreciation expense was charged to functions of the primary government as follows:

Governmental Activities:	
General Government	$ 31,008
Protection to Persons and Property	75,889
General Health and Sanitation	25,742
Social Services	4,672
Recreation and Culture	20,340
Roads, Including Depreciation of General Infrastructure Assets	147,208
Total Depreciation Expense - Governmental Activities	$ 304,859

Note 4. Short-term Debt

A. Kentucky Advance Revenue Program

In July 2006, Lee County participated in the Kentucky Association of Counties Kentucky Advance Revenue Program by issuing notes in the amount of $289,700, with principal being due in January 2007 with an interest rate of 4.65 percent. However, the county withdrew $200,000 for operating expenses, leaving $89,700 to earn interest. The county received net interest earnings from the Kentucky Association of Counties Kentucky Advance Revenue Program of $746.

B. Mack Truck

On February 23, 2007, the Lee County Fiscal Court entered into a lease agreement in the amount of $296,172 with the Kentucky Association of Counties Leasing Trust for Mack truck purchases. The County purchased heavy trucks to use for one year; then the trucks will be sold at an auction. It is intended that the auction will generate funds sufficient to pay off most, if not the entire outstanding principal. The agreement requires one payment due March 20, 2008, with an interest rate of 5.180 percent. The principal balance of the agreement was $296,172 as June 30, 2007.

C. Mack Truck

In January 2006, the county entered into a lease agreement for $272,463 with Kentucky Association of Counties Leasing Trust Program for the purchase of three Mack trucks. The County purchased heavy trucks for $268,800 to use for one year; then the trucks were sold at an auction. It was intended that the auction would generate funds sufficient to pay off most, if not the entire outstanding principal. Terms of the agreement stipulate a one-year repayment schedule, with variable monthly interest payment and a fixed yearly principal payment with an interest rate of 4.637 percent. The principal balance of the agreement was paid in full as of June 30, 2007.

D. Changes In Short-term Liabilities

Governmental Activities	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Kentucky Advance Revenue Program	$	$ 289,700	$ 289,700	$	$
Financing Obligations	268,800	299,835	272,463	296,172	296,172
Governmental Activities Short-term Liabilities	268,800	589,535	562,163	296,172	296,172
Less: KARP Activity Not Recorded on Books See Note 4 (A)		89,700	89,700		
Net Governmental Activities Short-term Liabilities	$ 268,800	$ 499,835	$ 472,463	$ 296,172	$ 296,172

Note 5. Financing Obligations

A. Truck/Backhoe

In July 1997, the county entered into a financing obligation agreement for $71,000 with Kentucky Association of Counties Leasing Trust Program for a truck and a backhoe. Terms of the agreement stipulate a ten-year repayment schedule, with variable monthly interest payments and variable annual principal payments with an interest rate of 4.6 percent. The principal amount is due January 20 of each year to end on January 20, 2007. As of June 30, 2007, the principal balance was $0.

B. Road Paving

In May 2002, the county entered into a financing obligation agreement for $300,000 with Kentucky Association of Counties Leasing Trust Program for road paving. Terms of the agreement stipulate a ten-year repayment schedule, with variable monthly interest payments and variable annual principal payments. The principal amount is due on January 20 of each year to end on January 20, 2012 with an interest rate of 2.75 percent. As of June 30, 2007, the principal balance was $165,000. Obligations for the remaining years are:

Fiscal Year Ended June 30	Principal	Interest & Fees
2008	$ 30,000	$ 7,429
2009	30,000	5,968
2010	35,000	4,405
2011	35,000	2,700
2012	35,000	995
Totals	$ 165,000	$ 21,497

C. Solid Waste Equipment

In July 2003, the county entered into a financing obligation agreement for $325,000 with Kentucky Association of Counties for a multi-purpose agreement for the purchase of solid waste equipment. However the county only used $250,241 of the proceeds. During December 2003, the County Judge/Executive requested that the balance of the agreement be applied towards the principal thereby reducing monthly payments. Terms of the agreement stipulate a ten-year repayment schedule, with variable monthly interest payments and variable monthly principal payments to end on June 20, 2013 with an interest rate of 2.175 percent. As of June 30, 2007, the principal balance was $158,736. Payments for the remaining years are:

Fiscal Year Ended June 30	Principal	Interest & Fees
2008	$ 24,151	$ 7,496
2009	24,885	6,286
2010	25,642	5,044
2011	26,421	3,696
2012	28,826	2,369
2013	28,811	1,037
Totals	$ 158,736	$ 25,928

Note 5. Financing Obligations (Continued)

D. Jail Library Renovation

In February 2006, the county entered into a financing obligation agreement for $20,000 with Kentucky Association of Counties Leasing Trust Program for funds to perform a renovation of the jail library. Terms of the agreement stipulate a two-year repayment schedule, with variable monthly interest payments and variable monthly principal payments. The principal amount is due on the 20th day of each month to end on March 20, 2008 with an interest rate of 4.25 percent. As of June 30, 2007, the principal balance was $7,736. Lease payments for the remaining years are:

Fiscal Year Ended June 30	Principal	Interest & Fees
2008	$ 7,736	$ 246
Totals	$ 7,736	$ 246

E. Changes In Long-term Liabilities

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Primary Government:					
Governmental Activities:					
Financing Obligations	$ 402,714		$ 71,243	$ 331,471	$ 61,887
Governmental Activities Long-term Liabilities	$ 402,714	$	$ 71,243	$ 331,471	$ 61,887

Note 6. Employee Retirement System

The fiscal court has elected to participate in the County Employees Retirement System (CERS), pursuant to KRS 78.530 administered by the Board of Trustees of the Kentucky Retirement Systems. This is a cost-sharing multiple-employer defined benefit pension plan, which covers all eligible full-time employees and provides for retirement, disability and death benefits to plan members. Benefit contributions and provisions are established by statute. Nonhazardous covered employees are required to contribute 5 percent of their salary to the plan. The county's contribution rate for nonhazardous employees was 13.19 percent. Hazardous covered employees are required to contribute 8 percent of their salary to the plan. The county's contribution rate for hazardous employees was 28.21 percent.

Note 6. Employee Retirement System (Continued)

Benefits fully vest on reaching five years of service for nonhazardous employees. Aspects of benefits for nonhazardous employees include retirement after 27 years of service or age 65. Aspects of benefits for hazardous employees include retirement after 20 years of service or age 55.

Historical trend information showing the CERS' progress in accumulating sufficient assets to pay benefits when due is presented in the Kentucky Retirement Systems' annual financial report. This report may be obtained by writing the Kentucky Retirement System, 1260 Louisville Road, Frankfort, KY 40601-6124, or by telephone at (502) 564-4646.

Note 7. Insurance

For the fiscal year ended June 30, 2007, Lee County was a member of the Kentucky Association of Counties' All Lines Fund (KALF). KALF is a self-insurance fund and was organized to obtain lower cost coverage for general liability, property damage, public officials' errors and omissions, public liability, and other damages. The basic nature of a self-insurance program is that of a collectively shared risk by its members. If losses incurred for covered claims exceed the resources contributed by the members, the members are responsible for payment of the excess losses.

Note 8. Subsequent Review

On August 13, 2007 the County entered into a Memorandum of Agreement for a coal severance project awarding the City of Beattyville $250,000 towards the construction of a water plant.

Note 9. Construction In Progress

Construction In Progress consisted of the following project as of June 30, 2007:

	Balance at June 30, 2006	Additions	Deletions	Balance at June 30, 2007
Happy Top Park Construction	$ 58,200	$ 70,316	$ (12,200)	$ 116,316

LEE COUNTY
BUDGETARY COMPARISON SCHEDULES
Required Supplementary Information - Modified Cash Basis

For The Year Ended June 30, 2007

	GENERAL FUND			
	Budgeted Amounts		Actual Amounts, (Budgetary Basis)	Variance with Final Budget Positive (Negative)
	Original	Final		
REVENUES				
Taxes	$ 1,047,460	$ 1,067,460	$ 1,303,901	$ 236,441
In Lieu	8,000	8,000	9,733	1,733
Excess Fees	317	317	1,067	750
Licenses and Permits	13,993	13,993	20,742	6,749
Intergovernmental	151,500	219,432	239,043	19,611
Charges for Services	8,375	8,375	5,348	(3,027)
Miscellaneous	78,660	98,660	154,821	56,161
Interest	6,150	6,150	3,343	(2,807)
Total Revenues	1,314,455	1,422,387	1,737,998	315,611
EXPENDITURES				
General Government	491,794	631,284	611,328	19,956
Protection to Persons and Property	235,620	180,550	167,155	13,395
Social Services	71,090	67,889	61,717	6,172
Recreation and Culture	94,409	186,841	179,022	7,819
Roads		63,000	62,750	250
Debt Service	266,250	206,536	206,534	2
Capital Projects	258,000	174,059	163,077	10,982
Administration	202,459	217,395	213,185	4,210
Total Expenditures	1,619,622	1,727,554	1,664,768	62,786
Excess (Deficiency) of Revenues Over Expenditures Before Other Financing Sources (Uses)	(305,167)	(305,167)	73,230	378,397
OTHER FINANCING SOURCES (USES)				
Kentucky Advanced Revenue Program Proceeds	233,631	233,631	200,000	(33,631)
Transfers To Other Funds	(188,664)	(188,664)	(90,169)	98,495
Total Other Financing Sources (Uses)	44,967	44,967	109,831	64,864
Net Changes in Fund Balance	(260,200)	(260,200)	183,061	443,261
Fund Balance - Beginning	260,200	260,200	227,392	(32,808)
Fund Balance - Ending	$	$	$ 410,453	$ 410,453

LEE COUNTY
BUDGETARY COMPARISON SCHEDULES
Required Supplementary Information - Modified Cash Basis
For The Year Ended June 30, 2007
(Continued)

	ROAD FUND			
	Budgeted Amounts		Actual Amounts, (Budgetary Basis)	Variance with Final Budget Positive (Negative)
	Original	Final		
REVENUES				
In Lieu	$ 8,294	$ 8,294	$ 12,068	3,774
Intergovernmental	716,600	1,304,600	1,383,337	78,737
Miscellaneous	245,208	281,208	302,278	21,070
Interest	1,232	1,232	1,759	527
Total Revenues	971,334	1,595,334	1,699,442	104,108
EXPENDITURES				
Roads	556,107	1,219,463	1,207,399	12,064
Debt Service	353,629	335,503	331,283	4,220
Miscellaneous	4,647	7,106	7,105	1
Administration	116,551	93,262	88,489	4,773
Total Expenditures	1,030,934	1,655,334	1,634,276	21,058
Excess (Deficiency) of Revenues Over Expenditures Before Other Financing Sources (Uses)	(59,600)	(60,000)	65,166	125,166
OTHER FINANCING SOURCES (USES)				
Kentucky Advanced Revenue Program Proceeds	29,600			
Net Changes in Fund Balance	(30,000)	(60,000)	65,166	125,166
Fund Balance - Beginning	30,000	60,000	63,123	3,123
Fund Balance - Ending	$	$	$ 128,289	$ 128,289

LEE COUNTY
BUDGETARY COMPARISON SCHEDULES
Required Supplementary Information - Modified Cash Basis
For The Year Ended June 30, 2007
(Continued)

	AMBULANCE FUND			
	Budgeted Amounts		Actual Amounts, (Budgetary Basis)	Variance with Final Budget Positive (Negative)
	Original	Final		
REVENUES				
Intergovernmental	$ 11,000	$ 11,000	$ 10,684	$ (316)
Charges For Services	750,000	750,000	826,496	76,496
Miscellaneous	8,000	8,000	17,234	9,234
Interest	100	100	280	180
Total Revenues	769,100	769,100	854,694	85,594
EXPENDITURES				
Protection to Persons and Property	736,846	758,782	713,428	45,354
Administration	250,918	228,982	219,592	9,390
Total Expenditures	987,764	987,764	933,020	54,744
Excess (Deficiency) of Revenues Over Expenditures Before Other Financing Sources (Uses)	(218,664)	(218,664)	(78,326)	140,338
OTHER FINANCING SOURCES (USES)				
Transfers From Other Funds	188,664	188,664	90,000	(98,664)
Net Changes in Fund Balance	(30,000)	(30,000)	11,674	41,674
Fund Balance - Beginning	30,000	30,000	14,835	(15,165)
Fund Balance - Ending	$	$	$ 26,509	$ 26,509

LEE COUNTY
NOTES TO REQUIRED SUPPLEMENTARY INFORMATION

June 30, 2007

1. Budgetary Information

Annual budgets are adopted on a cash basis of accounting and according to the laws of Kentucky as required by the State Local Finance Officer.

The County Judge/Executive is required to submit estimated receipts and proposed expenditures to the fiscal court by May 1 of each year. The budget is prepared by fund, function, and activity and is required to be adopted by the fiscal court by July 1.

The fiscal court may change the original budget by transferring appropriations at the activity level; however, the fiscal court may not increase the total budget without approval by the State Local Finance Officer. Expenditures may not exceed budgeted appropriations at the activity level.

2. Reconciliation of Required Supplementary Information to Statement of Revenues, Expenditures, and Changes in Fund Balances

	Revenues	Expenditures	Other Financing Sources (Uses)
Road Fund			
Budgetary Comparison Schedule	$ 1,699,442	$ 1,634,276	$ 0
Record Purchase of Mack Trucks		296,172	296,172
Reclassify Lease Proceeds	(3,663)		3,663
Statement of Revenues, Expenditures, and Changes in Fund Balance - Governmental Funds - Modified Cash Basis	$ 1,695,779	$ 1,930,448	$ 299,835

	Expenditures	Other Financing Sources (Uses)
General Fund		
Budgetary Comparison Schedule	$ 1,664,768	109,831
Kentucky Advanced Revenue Program Proceeds and Payoff	(200,000)	(200,000)
Statement of Revenues, Expenditures, and Changes in Fund Balance - Governmental Funds - Modified Cash Basis	$ 1,464,768	$ (90,169)

2. Reconciliation of Required Supplementary Information to Statement of Revenues, Expenditures, and Changes in Fund Balances (Continued)

	Miscellaneous Revenues	Financing Obligation Proceeds
Road Fund		
Budgetary Comparison Schedule	$ 302,278	$
Reclassification of Lease Proceeds	(3,663)	3,663
Record Purchase of Mack Trucks		296,172
Statement of Revenues, Expenditures, and Changes in Fund Balance - Governmental Funds - Modified Cash Basis	$ 298,615	$ 299,835

	Roads
Road Fund	
Budgetary Comparison Schedule	$ 1,207,399
Record Purchase of Mack Trucks	296,172
Statement of Revenues, Expenditures, and Changes in Fund Balance - Governmental Funds - Modified Cash Basis	$ 1,503,571

	Debt Service	Financing Obligation Proceeds
General Fund		
Budgetary Comparison Schedule	$ 206,534	200,000
Kentucky Advanced Revenue Program Proceeds and Payoff	(200,000)	(200,000)
Statement of Revenues, Expenditures, and Changes in Fund Balance - Governmental Funds - Modified Cash Basis	$ 6,534	$ 0

LEE COUNTY
COMBINING BALANCE SHEET -
NON-MAJOR GOVERNMENTAL FUNDS - MODIFIED CASH BASIS
Other Supplementary Information

June 30, 2007

LEE COUNTY
COMBINING BALANCE SHEET -
NON-MAJOR GOVERNMENTAL FUNDS - MODIFIED CASH BASIS
Other Supplementary Information

June 30, 2007

	Jail Fund	LGEA Fund	Solid Waste Fund	Handicap Van Fund	Total Non-Major Governmental Funds
ASSETS					
Cash and Cash Equivalents	$ 16,903	$ 60,160	$ 21,340	$ 45,455	$ 143,858
Total Assets	$ 16,903	$ 60,160	$ 21,340	$ 45,455	$ 143,858
FUND BALANCES					
Reserved for:					
Encumbrances	$ 0	$ 0	$ 11,633	$ 0	$ 11,633
Unreserved:					
Special Revenue Funds	16,903	60,160	9,707	45,455	132,225
Total Fund Balances	$ 16,903	$ 60,160	$ 21,340	$ 45,455	$ 143,858

The accompanying notes are an integral part of the financial statements.

LEE COUNTY
COMBINING STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES
IN FUND BALANCES - NON-MAJOR GOVERNMENTAL FUNDS - MODIFIED CASH BASIS
Other Supplementary Information

For The Year Ended June 30, 2007

LEE COUNTY
COMBINING STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES
IN FUND BALANCES - NON-MAJOR GOVERNMENTAL FUNDS - MODIFIED CASH BASIS
Other Supplementary Information

For The Year Ended June 30, 2007

	Jail Fund	LGEA Fund	Solid Waste Fund	Handicap Van Fund	Total Non-Major Governmental Funds
REVENUES					
Intergovernmental	$ 54,607	$ 386,340	$ 30,405	$ 40,000	$ 511,352
Charges For Services			352,336	94	352,430
Miscellaneous	1,425	1,000	7,590	5,860	15,875
Interest	116	428	209	50	803
Total Revenues	56,148	387,768	390,540	46,004	880,460
EXPENDITURES					
General Health and Sanitation		95,693	312,439	524	408,656
Protection to Persons and Property	241,029				241,029
Roads		60,624			60,624
Debt Service	8,762		34,843		43,605
Administration	6,599	5,274	56,982	25	68,880
Total Expenditures	256,390	161,591	404,264	549	822,794
Excess (Deficiency) of Revenues Over Expenditures Before Other Sources (Uses)	(200,242)	226,177	(13,724)	45,455	57,666
Other Financing Sources (Uses)					
Transfers To Other Funds		(204,000)			(204,000)
Transfers From Other Funds	204,000		169		204,169
Total Other Financing Sources (Uses)	204,000	(204,000)	169		169
Net Change in Fund Balances	3,758	22,177	(13,555)	45,455	57,835
Fund Balances - Beginning	13,145	37,983	34,895		86,023
Fund Balances - Ending	$ 16,903	$ 60,160	$ 21,340	$ 45,455	$ 143,858

The accompanying notes are an integral part of the financial statements.

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

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The Honorable Steve Mays, Lee County Judge/Executive
Members of the Lee County Fiscal Court

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

We have audited the financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of the Lee County Fiscal Court, as of and for the year ended June 30, 2007, which collectively comprise the County's basic financial statements and have issued our report thereon dated December 3, 2007. Lee County presents its financial statements on the modified cash basis of accounting, which is a comprehensive basis of accounting other than generally accepted accounting principles. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the County's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the County's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the County's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed below, we identified certain deficiencies in internal control over financial reporting that we consider to be a significant deficiency.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the County's ability to initiate, authorize, record, process, or report financial data reliably in accordance with the modified cash basis of accounting such that there is more than a remote likelihood that a misstatement of the County's financial statements that is more than inconsequential will not be prevented or detected by the County's internal control over financial reporting.

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
(Continued)

Internal Control Over Financial Reporting (Continued)

We consider the deficiencies described in the accompanying comment and recommendation to be a significant deficiency in internal control over financial reporting as item:

2007-1 The County Should Implement Better Internal Control Procedures Over Solid Waste Collections And Billings

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the County's internal control. Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies and accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, we consider the significant deficiency described above to be a material weakness.

Compliance And Other Matters

As part of obtaining reasonable assurance about whether the Lee County Fiscal Court's financial statements for the year ended June, 30, 2007 are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards.*

The Lee County Judge/Executive's responses to the findings identified in our audit are included in the accompanying comments and recommendations. We did not audit the County Judge/Executive's responses and, accordingly, we express no opinion on them.

This report is intended solely for the information and use of management and the Kentucky Governor's Office for Local Development and is not intended to be and should not be used by anyone other than these specified parties.

Respectfully submitted,

Morgan - Franklin, LLC

Morgan-Franklin, LLC

December 3, 2007

LEE COUNTY
COMMENT AND RECOMMENDATION

Fiscal Year Ended June 30, 2007

LEE COUNTY
COMMENT AND RECOMMENDATION

Fiscal Year Ended June 30, 2007

MATERIAL WEAKNESS

2007-1 The County Should Implement Better Internal Control Procedures Over Solid Waste Collections And Billings

The County's controls over solid waste receipts and billing should be improved. During our testing, we noted the following:

a) The Solid Waste employee receives cash and also handles complaints from customers.
b) An independent person does not reconcile the computer print out of receipts to the bank deposits on a regular basis.
c) It appears that the fiscal court is not looking into large accounts receivable balances in a timely and diligent manner.
d) It appears that some residential and commercial users are not billed at all and some are billed the incorrect rates.

We recommend the county implement the following:

a) Someone independent of cash collections should handle complaints. This could be implemented by indicating on the bills a number and name/position to contact if you have any complaints.
b) An independent person should compare the deposit prepared by the Solid Waste Coordinator to the daily receipt register and investigate any differences.
c) The Fiscal Court should send past due notices to customers monthly. After a specified number of months of nonpayment delinquent bills should be turned over to the county attorney for collection.
d) The Fiscal Court should create and maintain a complete and accurate list of all residential and commercial customers to insure that bills are sent out to all customers. All customers should be billed at the rates approved by the fiscal court.

Lee County Fiscal Court Judge Executive Steve Mays's Response: Have implemented new rates and will implement the recommendation of the auditors.

CERTIFICATION OF COMPLIANCE -
LOCAL GOVERNMENT ECONOMIC ASSISTANCE PROGRAM

LEE COUNTY FISCAL COURT

For The Year Ended
June 30, 2007

CERTIFICATION OF COMPLIANCE

LOCAL GOVERNMENT ECONOMIC ASSISTANCE PROGRAM

LEE COUNTY FISCAL COURT

For The Year Ended June 30, 2007

The Lee County Fiscal Court hereby certifies that assistance received from the Local Government Economic Assistance Program was expended for the purpose intended as dictated by the applicable Kentucky Revised Statutes.

Steve Mays
County Judge/Executive

Pearl Spencer
County Treasurer