

NASHVILLE & EASTERN RAILROAD AUTHORITY
FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2011

NASHVILLE & EASTERN RAILROAD AUTHORITY

JUNE 30, 2011

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INDEPENDENT AUDITORS' REPORT

To the Board of Directors
Nashville & Eastern Railroad Authority

We have audited the accompanying financial statements of the governmental activities and the major fund, of the Nashville & Eastern Railroad Authority as of and for the year ended June 30, 2011, which collectively comprise the Nashville & Eastern Railroad Authority's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the Nashville & Eastern Railroad Authority's management. Our responsibility is to express opinions on these financial statements based on our audit.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, and the major fund as of June 30, 2011, and the respective changes in financial position for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated March 22, 2012, on our consideration of the Nashville & Eastern Railroad Authority'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.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 5 – 8 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing 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 because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Nashville & Eastern Railroad Authority's basic financial statements. The schedule of salaries and fidelity bonds is presented for purposes of additional analysis and is not a required part of the basic financial statements. The accompanying schedule of state contract expenditures is presented for purposes of additional analysis as required by the *Comptroller of the Treasury of the State of Tennessee Audit Manual* but is not a required part of the basic financial statements of the Nashville & Eastern Railroad Authority. The schedule of state contract expenditures 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 financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the basic financial statements taken as a whole. The schedule of salaries and fidelity bonds of principal officials on page 28 has not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we express no opinion on it.

Dempsey Vantrase + Folles, PLLC

Lebanon, Tennessee

March 22, 2012

Management's Discussion And Analysis

This section of the Nashville & Eastern Railroad Authority's (the Authority) audited financial statements presents our discussion and analysis of the Organization's financial performance during the fiscal year that ended on June 30, 2011. Please read it in conjunction with the financial statements, which follow this section.

Financial Highlights

- The Organization's net assets decreased \$6,754 over the course of this year's operations. The change in net assets is a 0.02% decrease from the fiscal year ended June 30, 2010.
- During the year, the Organization's operating revenues exceeded operating expenses by \$13,494 due to a decrease in operating expenses, mainly in legal fees.
- The total cost of the Organization's expenditures decreased 7.69% in the fiscal year ended June 30, 2011. The decrease was mainly due to a decrease in legal fees, which in the prior year included fees related to a lawsuit that was settled.
- Balances of cash increased \$141,263 during the fiscal year ended June 30, 2011. The increase is primarily due to being more up to date on routine maintenance and increased shipping and receiving revenue from rail customers due to upturn in the economy as well as funds received in the current fiscal year that will be used on future projects.
- The Authority's liabilities decreased \$391,103 during the year ending June 30 2011 due to accrued flood damages paid in current year and principal payments on loans.

Overview Of The Financial Statements

This annual report consists of three parts – management's discussion and analysis, the basic financial statements, and required supplementary information. The basic financial statements include two kinds of statements that present different views of the Nashville & Eastern Railroad Authority:

- The first two statements are government-wide financial statements that provide both long-term and short-term information about the Board's overall financial status.
- The remaining statements are fund financial statements that focus on individual parts of the government, reporting the Board's operations in more detail than the government-wide statements.

- The governmental funds statements tell how general government services were financed in the short term as well as what remains for future spending.

The financial statements also include notes that explain some of the information in the financial statements and provide more detailed data. The statements are followed by a section of required supplementary information that further explains and supports the information in the financial statements.

Government-wide Statements

The government wide statements report information about the Nashville & Eastern Railroad Authority as a whole using accounting methods similar to those used by private-sector companies. The statement of net assets includes all of the government's assets and liabilities. All of the current year's revenues and expenses are accounted for in the statement of activities regardless of when cash is received or paid. The two government-wide statements report the Board's net assets and how they have changed. Net assets – the difference between the Board's assets and liabilities – is one way to measure the Nashville & Eastern Railroad's financial health, or position.

- Over time, increases or decreases in the Authority's net assets are an indicator of whether its financial health is improving or deteriorating, respectively.
- To assess the overall health of the Authority you need to consider additional non-financial factors.

Fund Financial Statements

The fund financial statements provide more detailed information about the Authority's most significant funds – not the Authority as a whole. Funds are accounting devices that the Authority uses to keep track of specific sources of funding and spending for particular purposes.

- Some funds are required by State law and bond covenants.
- Other funds are established to control and manage money for particular purposes or to show that the government is properly using taxes.

The Nashville & Eastern Railroad Authority has only one kind of fund:

- Governmental funds – Most basic services are included in governmental funds, which focus on (1) how cash and other financial assets that can readily be converted to cash flow in and out and (2) the balances left at year-end that are available for spending. Consequently, the governmental funds statements provide a detailed short-term view that helps you determine whether there are more or fewer financial resources that can be spent in the near future to finance programs. Since the government-wide focus includes the long-term view, comparisons between these two perspectives may provide insight into the long-term impact of

short-term financing decisions. Both the governmental fund balance sheet and the governmental fund statement of revenues, expenditures, and changes in fund balances provide a reconciliation to the government wide statements to assist in understanding the differences between these two perspectives.

Financial Analysis Of The Organization As A Whole

Net Assets. The Organization's net assets decreased \$6,754 between fiscal years 2010 and 2011. In comparison, net assets for the fiscal year ended June 30, 2010 decreased \$1,357,075 from the fiscal year ended June 30, 2009. Income from ongoing operations increased \$942,619 during the fiscal year ended June 30, 2011 from the fiscal year ended June 30, 2010.

Nashville & Eastern Railroad Authority
Net Assets
June 30, 2011 and June 30, 2010

	<u>2011</u>	<u>2010</u>	<u>% Change</u>
Current and Other Assets	\$ 387,864	\$ 200,007	93.93%
Capital Assets	\$ 49,337,517	\$ 49,923,221	(1.17)%
Total Assets	<u>\$ 49,725,381</u>	<u>\$ 50,123,228</u>	(0.79)%
 Current and Other Liabilities	 \$ 9,129,881	 \$ 9,520,984	 (4.11)%
 Net Assets			
Invested In Capital Assets			
Net of Related Debt	\$ 40,752,658	\$ 41,061,852	(0.75)%
Unrestricted	\$ (157,158)	\$ (459,598)	(65.81)%
Total Net Assets	<u>\$ 40,595,500</u>	<u>\$ 40,602,254</u>	(0.02)%
 Total Liabilities and Net Assets	 <u>\$ 49,725,381</u>	 <u>\$ 50,123,238</u>	 (0.79)%

Changes In Net Assets. The Authority's total revenues increased \$942,619 during the fiscal year. The Authority's primary sources of revenue are appropriations from the Tennessee Department of Transportation for railroad improvements and a lease agreement between the Authority and railroad operator which requires the operator to pay 4% - 6% of gross revenues from freight hauled on the railroad back to the Authority as a lease fee. Revenues from the Department of Transportation increased \$940,679. Revenues from the lease of the railroad increased \$1,940. The total cost of all programs decreased by \$177,985 due mainly to a decrease in legal fees, which in the prior year included fees related to a lawsuit that was settled.

Nashville & Eastern Railroad Authority
 Changes In Net Assets
 June 30, 2011 and June 30, 2010

	<u>2011</u>	<u>2010</u>	<u>% Change</u>
Total Operating Revenues	\$ 2,149,373	\$ 1,206,754	78.11%
Total Operating Expenses	<u>2,135,879</u>	<u>2,313,864</u>	-7.69%
Operating Income/(Deficit)	13,494	(1,107,110)	-101.22%
Non-Operating Income	-	35	-100.00%
Extraordinary Item	<u>(20,248)</u>	<u>(250,000)</u>	-91.90%
Increase/(Decrease) In Net Assets	<u>\$ (6,754)</u>	<u>(1,357,075)</u>	-99.50%

Capital Assets. As of June 30, 2011, the Organization had invested \$40,752,658 in capital assets net of related debt and accumulated depreciation. The principal capital asset of the Authority is the railroad itself which has been in the process of being upgraded since it was purchased by the Authority in 1986. The railroad continued to receive substantial improvements through TDOT during the fiscal year ended June 30, 2011 including a supplemental apportionment for all program eligible shortline railroads. More detail about the Organization's capital assets is available in Notes to the financial statements.

The Organizations fiscal year 2012 capital budget projects approximately \$2,000,000 in capital expenditures funded by grants from the Transportation Equity Fund of the Tennessee Department of Transportation.

Contacting The Organization's Financial Management

This financial report is designed to provide the citizens, taxpayers, and customers of the Nashville & Eastern Railroad Authority information about the Organization's finances and to demonstrate the Organization's accountability for the money it receives. If you have questions about this report or need additional information, contact the Nashville & Eastern Railroad Authority at 206 South Maple Street, Lebanon, TN 37087.

GOVERNMENT-WIDE STATEMENTS

NASHVILLE & EASTERN RAILROAD AUTHORITY
STATEMENT OF NET ASSETS
JUNE 30, 2011

ASSETS	<u>Governmental Activities</u>
Cash and Cash Equivalents	\$ 251,433
Accounts Receivable	136,431
Total Current Assets	<u>387,864</u>
Property & Equipment (Net of Accumulated Depreciation)	<u>49,337,517</u>
Total Assets	<u>\$ 49,725,381</u>
LIABILITIES AND NET ASSETS	
Accounts Payable	\$ 58,491
Accrued Interest	181,470
Deferred Revenue - FEMA	55,061
Current Portion of Long-Term Debt	288,948
Total Current Liabilities	<u>583,970</u>
Notes Payable	<u>8,545,911</u>
Total Liabilities	9,129,881
Net Assets	
Unrestricted	(157,158)
Invested In Capital Assets, Net of Related Debt and Depreciation	<u>40,752,658</u>
Total Net Assets	<u>40,595,500</u>
Total Liabilities and Net Assets	<u>\$ 49,725,381</u>

See Accompanying Notes To Financial Statements.

NASHVILLE & EASTERN RAILROAD AUTHORITY
STATEMENT OF ACTIVITIES
FOR THE FISCAL YEAR ENDED JUNE 30, 2011

Functions/Programs	Expenses	Program Revenues		Net (Expense) Revenue and Changes in Net Assets
		Charges For Services	Grants and Contributions	
Governmental Activities				
Infrastructure Development	\$ 2,043,091	\$ 2,149,373	\$ -	\$ 106,282
General & Administrative	92,788	-	-	(92,788)
	2,135,879	2,149,373	-	13,494
General Revenues				
Interest Income				-
Total General Revenues, Special Items, & Transfers				-
Flood Damage				(20,248)
Change In Net Assets				(6,754)
Net Assets - Beginning of Year				40,602,254
Net Assets - End of Year				\$ 40,595,500

See Accompanying Notes To Financial Statements

FUND STATEMENTS

NASHVILLE & EASTERN RAILROAD AUTHORITY
BALANCE SHEET
JUNE 30, 2011

ASSETS

Current Assets	
Cash and Cash Equivalents	\$ 251,433
Accounts Receivable - Other	<u>136,431</u>
 Total Current Assets	 <u><u>\$ 387,864</u></u>

LIABILITIES AND FUND BALANCE

Current Liabilities	
Accounts Payable	\$ 58,491
Deferred Revenue - FEMA	<u>55,061</u>
Total Current Liabilities	113,552

Fund Balances	
Unassigned	<u>274,312</u>

Total Liabilities & Fund Balance	<u><u>\$ 387,864</u></u>
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Total Fund Balance Per Fund Financial Statements	\$ 274,312
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Reconciliation to the Statement of Net Assets:

Fixed assets are not included in the fund financial statements prepared on the modified accrual basis of accounting.	49,337,517
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Accrued interest on bonds are not reported in the current period and therefore are not reported in the fund financial statements.	(181,470)
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Long term debt is not included in the fund financial statements prepared on the modified accrual basis of accounting	<u>(8,834,859)</u>
Net Assets	<u><u>\$ 40,595,500</u></u>

See Accompanying Notes to Financial Statements

NASHVILLE & EASTERN RAILROAD AUTHORITY
STATEMENT OF REVENUES, EXPENDITURES,
AND CHANGES IN FUND BALANCE
FOR THE YEAR ENDED JUNE 30, 2011

Revenues	
State of Tennessee	\$ 2,020,634
Nashville & Eastern Rail Corp.	<u>128,738</u>
Total Revenues	2,149,372
Expenditures	
Rail Rehabilitation	1,046,482
Audit	6,000
Legal Services	15,981
Administration	28,805
Principal Payments On Loans	276,520
Interest Expense	378,375
Managing Director Fees	<u>42,000</u>
Total Expenditures	<u>1,794,163</u>
Excess of Revenues Over Expenditures Before Extraordinary Items	355,209
Extraordinary Items Flood Damage	<u>(20,248)</u>
Excess of Expenditures Over Revenues After Extraordinary Items	334,961
Fund Balance - Beginning of Year	<u>(60,649)</u>
Fund Balance - End of Year	<u><u>\$ 274,312</u></u>

See Accompanying Notes to Financial Statements

NASHVILLE & EASTERN RAILROAD AUTHORITY
STATEMENT OF REVENUES, EXPENDITURES,
AND CHANGES IN FUND BALANCE
FOR THE YEAR ENDED JUNE 30, 2011

Reconciliation to Statement of Activities:	
Net Change in Fund Balances - Total Governmental Funds	\$ 334,961
Purchases of fixed assets are an expenditure in the governmental funds, but are increases in property and equipment on the statement of net assets in the government-wide statements.	1,046,482
Principal payments on long term debt are included as an expense in the governmental funds, but are reductions of long term debt in the statement of net assets in the government-wide statements.	276,520
Change in accrued interest in the statement of activities does not require use of current financial resources and is not reported as an expenditure in governmental funds.	(32,521)
Depreciation is not recorded in the fund financial statements but is reported in the government-wide financial statements.	(1,632,196)
Change in net assets	<u>\$ (6,754)</u>

NASHVILLE & EASTERN RAILROAD AUTHORITY
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2011

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. Reporting Entity

The financial statements present the accounts and operations of the Nashville & Eastern Railroad Authority. The Nashville and Eastern Railroad Authority was created according to an act of the Tennessee Legislature in 1983 to purchase from Seaboard System Railroad, Inc., the property, track, and roadbed along approximately 130 miles in Davidson, Wilson, Smith and Putnam Counties. The business of the Nashville and Eastern Railroad Authority is conducted by a board of directors whose members are appointed by the governing bodies of the cities and counties of service. The Authority's primary revenue source is rehabilitation contracts with the Tennessee Department of Transportation.

B. Government-Wide and Fund Financial Statements

The government-wide financial statements include the statement of net assets and the statement of activities. These statements report financial information for the Nashville & Eastern Railroad Authority as a whole. Individual funds are not displayed in the government-wide financial statements and the Organization has only governmental activities supported by government allocations.

The statement of activities reports the expenses of a given function offset by program revenues directly connected with the functional program. A function is an assembly of similar activities and may include portions of a fund or summarize more than one fund to capture the expenses and program revenues associated with a distinct functional activity. Program revenues include: (1) charges for services which report fees, fines and forfeitures, and other charges to users of the Board's services; (2) operating grants and contributions which finance annual operating activities including restricted investment income; (3) capital grants and contributions which fund the acquisition, construction, or rehabilitation of capital assets and include fees to developers. Other revenue sources not properly included with program revenues are reported as general revenues.

Fund Financial Statements

Fund financial statements are provided for the governmental fund.

NASHVILLE & EASTERN RAILROAD AUTHORITY
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2011

C. Measurement Focus, Basis of Accounting, and Financial Statement Presentation

The financial statements of the Nashville & Eastern Railroad Authority are prepared in accordance with generally accepted accounting principles (GAAP).

The government-wide statements report using the economic resources measurement focus and the accrual basis of accounting generally including the reclassification or elimination of internal activity (between or within funds). Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows.

Governmental fund financial statements report using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized when they are both measurable and available. Available means collectible within the current period or soon enough thereafter to pay current liabilities. The Nashville & Eastern Railroad Authority considers revenues to be available if they are collected within 60 days of the end of the fiscal year. Expenditures are recorded when the related fund liability is incurred.

The Board's general spending prioritization policy is to consider restricted resources to have been used first, followed by committed, assigned, and unassigned amounts when expenditures have been incurred for which resources in more than one classification could be used.

D. Fund Types and Major Funds

The Nashville & Eastern Railroad Authority reports the following major governmental fund:

General Fund – The General Fund is the general operating fund of the Organization. It is used to account for all financial resources except those required to be accounted for in another fund.

E. Other Significant Policies

Bad Debt - The Nashville & Eastern Railroad Authority has recorded no provision for bad debts as all accounts receivable are considered fully collectible.

NOTE 2 – CASH AND CASH EQUIVALENTS

At June 30, 2011 the bank balance of cash and cash equivalents is \$260,882. The bank balances were entirely secured by FDIC insurance or collateralized through the State of Tennessee Bank Collateral Pool.

NASHVILLE & EASTERN RAILROAD AUTHORITY
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2011

NOTE 3 – RISK MANAGEMENT

The Authority is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; and natural disasters. The Authority has secured fidelity bonds on the officers as disclosed in the accompanying schedule. The lease agreement with Nashville and Eastern Railroad Corporation specified that the Corporation "...shall maintain insurance...in such amounts and covering such risks as is customarily carried by companies engaged in similar...businesses... and cause the Authority to be protected as an additional named insured." At year-end, there was no pending or threatened litigation according to the Authority's legal counsel. There have been no significant reductions in insurance coverage by the Authority. Settlement amounts have not exceeded insurance coverage for the current year or the three prior years.

NOTE 4 – LEASES

The Authority originally entered into a ten-year lease, dated August 28, 1986, with Nashville and Eastern Railroad Corporation to operate the line. Under the terms of the lease, the Authority is required to rehabilitate the line. After this rehabilitation, the operator will provide appropriate maintenance of the line. Currently, quarterly lease payments of 4% of the gross freight revenues on the first \$3,000,000; 5% between \$3,000,000 and \$4,000,000; and 6% of operating revenues over 4,000,000 are due. For commuter rail service, the Authority receives 10% of the gross commuter rail track usage or other passenger mileage fees. Finally, the Nashville and Eastern Railroad Corporation pays \$1,250 per month for the use of its maintenance facility in Lebanon to the Authority beginning in January 2005. This lease agreement has been renewed through the year 2053 in order to comply with the need to provide the long-term capabilities involved in the proposed commuter rail program between Lebanon and Nashville, Tennessee. Revenues from the lease totaled \$128,738 for the year ended June 30, 2011.

NOTE 5 – CONTRACTS & GRANTS

FEDERAL RAILROAD ADMINISTRATION (F.R.A.) – The FRA grant is an agreement between the State of Tennessee, acting through its Department of Transportation and the Authority. Funds provided from FRA grants are to be used for further rehabilitation work along the branchline. The payments create a contingent interest in the branchline for the State of Tennessee. If the Authority sells, abandons, or disposes of the branchline, they shall repay to the State the federal share as determined in accordance with attachment N to OMB Circular No. A102. The Authority received no federal funds for the year ended June 30, 2011.

TENNESSEE DEPARTMENT OF TRANSPORTATION - The Tennessee Department of Transportation (T.D.O.T.) has contracted with the Authority to provide funds to purchase, rehabilitate, and maintain the line. In the event of disposition of the branchline the Authority shall return to the State a portion of the sales price or the appraised value, whichever is applicable, which is in proportion to the State's prorata share of the total purchase price plus the total rehabilitation expenditures prior to the date of the sales.

NASHVILLE & EASTERN RAILROAD AUTHORITY
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2011

NOTE 6 – FIXED ASSETS

In the government wide financial statements, fixed assets are recorded at cost and depreciated over their estimated useful lives. Office equipment is generally depreciated over 5 years, furniture and fixtures over 7 years, leasehold improvements over 30 years, and improvements to the railroad over 40 years using the straight line method.

A summary of fixed assets for the fiscal year ended June 30, 2011 is presented below:

	<u>Balance</u> <u>July 1, 2010</u>	<u>Additions</u> <u>(Deductions)</u>	<u>Balance</u> <u>June 30, 2011</u>
<u>Nondepreciable Assets</u>			
Land	\$ 477,306	\$ -	\$ 477,306
Total Nondepreciable Assets	<u>477,306</u>	<u>-</u>	<u>477,306</u>
<u>Depreciable Assets</u>			
Buildings	670,323	-	670,323
Branchline and Right of Way	2,168,227	-	2,168,227
Rail Rehabilitation	61,234,655	1,046,482	62,281,138
	<u>\$ 64,550,511</u>	<u>\$ 1,046,482</u>	<u>\$ 65,596,994</u>
<u>Accumulated Depreciation by Major Asset Class</u>			
Buildings	\$ 244,339	\$ 17,141	\$ 261,480
Branchline and Right of Way	1,436,688	54,206	1,490,894
Rail Rehabilitation	12,946,254	1,560,849	14,507,103
	<u>\$ 14,627,281</u>	<u>\$ 1,632,196</u>	<u>\$ 16,259,477</u>
Property & Equipment Net of Accumulated Depreciation			<u>\$ 49,337,517</u>

Depreciation expense for the fiscal year ended June 30, 2011 was \$1,632,196.

NASHVILLE & EASTERN RAILROAD AUTHORITY
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2011

NOTE 7 – COMMUTER RAIL

The Regional Transportation Authority was approved by the U.S. House of Representatives for a grant from the Federal Transit Administration to cover 80% of the cost of construction of the first leg of a commuter rail system which would link the cities of Nashville, Mt. Juliet, Lebanon, Gallatin, Hendersonville, Lavergne, Smyrna, Murfreesboro, Franklin, and Kingston Springs. Construction on the commuter rail project to bring the railroad up to FRA Class III Safety Standards and link the cities of Lebanon, Mt. Juliet and Nashville began during the fiscal year ended June 30, 2005. The Authority has agreed to fund up to 2.5 million (10%) of the cost of this upgrade and established a line of credit with First Tennessee Bank in that amount in order to assist with the commuter rail project. Nashville and other local governments will share in the remaining 10% of the cost of the project.

Construction on the commuter rail project was completed during the fiscal year ended June 30, 2007. Those improvements have been capitalized in the government wide financial statements of the Nashville & Eastern Railroad Authority and are being depreciated over an estimated useful life of 40 years.

The commuter rail system comes as an improvement to the Authority's already existing railroad assets. Commuter rail could significantly increase the amount of funds received by NERA from their share of operating revenues of the railroad under the lease described in Note 4.

NOTE 8 - BUDGET TO ACTUAL

Only general budget information is available. Each year the rehabilitation, maintenance, and expansion of the branchline is contracted between the Tennessee Department of Transportation, the Nashville and Eastern Railroad Authority, and the Nashville and Eastern Railroad Corporation. However, there is a three-year window in which the work specified in the contract must be completed or the funding for that project will lapse. The Authority uses the contract amounts to monitor actual results with the amounts budgeted for the individual contracts. However, there is no budget prepared for each individual fiscal year.

NASHVILLE & EASTERN RAILROAD AUTHORITY
 NOTES TO FINANCIAL STATEMENTS
 JUNE 30, 2011

NOTE 9 – NOTES PAYABLE

As mentioned in note 7, the Nashville & Eastern Railroad Authority established a line of credit with First Tennessee Bank in the amount of \$2.5 million to fund 10% of the cost of the first stage of the commuter rail program. At June 30, 2011, the Authority had an outstanding balance of \$1,316,163 on that line which was used to fund the commuter rail costs. The outstanding balance will be amortized on a 16 year schedule at a variable interest rate, currently 4.56%, with annual payments of \$250,000 being due beginning June 1, 2006 through June 1, 2018. Principal maturities over the life of the loan are scheduled as follows:

	Principal		Interest
2012	\$ 188,697	\$	61,303
2013	197,483		52,517
2014	206,679		43,321
2015	216,303		33,697
2016	226,375		23,625
2017-2018	280,626		15,135
	<u>\$ 1,316,163</u>	<u>\$</u>	<u>229,597</u>

The Nashville & Eastern Railroad Authority made one payment during the fiscal year ended June 30, 2011.

In September of 2006, the Nashville & Eastern Railroad Authority was approved for a \$7,202,000 loan from the United States Department of Agriculture to make the necessary improvements to the branch line between the cities of Algood and Monterey. At June 30, 2011 the outstanding balance on the loan is \$7,268,696. The loan accrues interest at 4.125% per annum and is secured by the improvements being made to the railroad. Annual payments of principal and interest in the amount of \$404,895 will be due through March of 2045. A schedule of principal and interest payments to maturity on this loan is as follows:

NASHVILLE & EASTERN RAILROAD AUTHORITY
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2011

NOTE 9 – NOTES PAYABLE (CONTINUED)

	Principal		Interest
2012	\$ 100,252	\$	304,643
2013	104,453		300,442
2014	108,831		296,064
2015	113,392		291,503
2016	118,145		286,750
2017-2021	669,283		1,355,192
2022-2026	821,796		1,202,679
2027-2031	1,009,064		1,015,411
2032-2036	1,239,006		785,469
2037-2041	1,521,345		503,130
2042-2045	1,463,128		156,451
	<u>\$ 7,268,696</u>	<u>\$</u>	<u>6,497,734</u>

In November, 2009, the Tennessee Department of Transportation loaned the Nashville and Eastern Railroad Authority \$250,000 to settle a lawsuit involving the moving of gas pipeline during commuter rail construction. The loan will be deducted from future allocations from TDOT by taking \$50,000 from the Nashville & Eastern Railroad Authority each year until the balance is paid in full. The Tennessee Department of Transportation is not charging interest on this loan. Repayment was originally scheduled to begin in the fiscal year ended June 30, 2011, but the State did not reduce funding in the current year.

NOTE 10 – FLOOD DAMAGE

In May 2010, Middle Tennessee experienced a severe flood that caused significant property damage. At June 30, 2010, the Authority had accrued \$250,000 in flood damages, reported in accounts payable and accrued flood damages on the statement of net assets and as an extraordinary item on the statement of activities. During the current fiscal year, the authority spent \$270,248 on flood repairs. Therefore, at June 30, 2011, the Authority reported an extraordinary item of \$20,248 on the statement of net assets. The Authority received some FEMA assistance to defray the cost of the flood repairs. Since these repairs were already funded by a State contract, these funds will be used for future projects. Therefore, at June 30, 2011, the Authority reported deferred revenues of \$55,061 on the statement of net assets.

INTERNAL CONTROL AND COMPLIANCE SECTION



Independent Auditors' Report on Internal Control Over
Financial Reporting and on Compliance and Other Matters
Required By *Government Auditing Standards*

To the Board of Directors
Nashville & Eastern Railroad Authority
Lebanon, Tennessee

We have audited the financial statements of the governmental activities and major fund of the Nashville & Eastern Railroad Authority, as of and for the year ended June 30, 2011, which collectively comprise the Nashville & Eastern Railroad Authority's basic financial statements and have issued our report thereon dated March 22, 2012. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

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

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 control 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.

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 or material weaknesses. We did identify the following deficiency in internal control over financial reporting that we consider to be a material weakness, as defined above.

The Nashville & Eastern Railroad Authority does not have personnel with the training and experience to prepare financial statements in accordance with generally accepted accounting principles.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Authority's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, grant agreements and other matters, 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.

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

Dempsey Vantrase & Follis, PLLC
Lebanon, Tennessee
March 22, 2012

SUPPLEMENTARY SCHEDULES

Nashville Eastern Railroad Authority
Schedule of State and Federal Contract Expenditures
June 30, 2011

Number	Grantor Agency	Balance July 01, 2010	Receipts	Expenditures	Balance June 30, 2011
GG-10-30906-00	TN Department of Transportation	-	54,233	54,233	-
GG-10-31055-00	TN Department of Transportation	-	431,567	431,568	1
GG-10-33918-00	TN Department of Transportation	-	273,110	273,110	-
GG-11-32097-00	TN Department of Transportation	-	289,055	291,746	2,691
Z-10-220816-00	TN Department of Transportation	-	15,851	15,851	-
Z-11-RE2016-00	TN Department of Transportation	-	566	2,685	2,119
Z-11-RE2034-00	TN Department of Transportation	-	4,455	13,414	8,959
Z-11-RR1006-00A	TN Department of Transportation	-	185,506	217,882	32,376
Z-11-RR1012-00	TN Department of Transportation	-	41,062	57,046	15,984
Z-11-RR1015-00	TN Department of Transportation	-	413,100	413,100	-
Z-11-RR1016-00	TN Department of Transportation	-	250,000	250,000	-
	FEMA	-	55,061	-	(55,061)
		-	-	-	-
		\$ -	\$ 2,013,565	\$ 1,966,402	\$ (47,163)
Reconciliation to Fund Financial Statements					
Deferred FEMA Grant			(55,061)		
Prior Year Accounts Receivable			-		
Current Year Accounts Receivable			62,130		
Revenues Per Fund Financial Statements			<u>\$ 2,020,634</u>		

See Accompanying Notes to Financial Statements

NASHVILLE & EASTERN RAILROAD AUTHORITY
SCHEDULE OF SALARIES AND FIDELITY BONDS
OF PRINCIPAL OFFICIALS (UNAUDITED)
JUNE 30, 2011

Official	Title	Annual Salary	Bond
Mike Jennings	Chairman	0	200,000
Eldon Leslie	Vice-Chairman	0	200,000
Henry Schumpf	Treasurer	0	200,000
Michael Nesbitt	Secretary	0	200,000
Val Kelley	Managing Director	0	200,000

See Accompanying Notes To Financial Statements