

NASHVILLE & EASTERN RAILROAD AUTHORITY
FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2013

NASHVILLE & EASTERN RAILROAD AUTHORITY

JUNE 30, 2013

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INDEPENDENT AUDITOR'S 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 Nashville & Eastern Railroad Authority, as of and for the year ended June 30, 2013, and the related notes to the financial statements, which collectively comprise the Authority's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express 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 from material misstatement.

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

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

Opinions

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 of the Nashville & Eastern Railroad Authority, as of June 30, 2013, and the respective changes in financial position thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis 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 the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Nashville & Eastern Railroad Authority's basic financial statements. The supplementary schedules are presented for purposes of additional analysis and are not a required part of the basic financial statements.

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

The schedule of fidelity bonds of principal officials has not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we do not express an opinion or provide any assurance on it.

Dempsey Kintrese - Trolis ACC

Lebanon, TN 37087

February 21, 2014

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, 2013. Please read it in conjunction with the financial statements, which follow this section.

Financial Highlights

The Organization's net position increased \$250,139 over the course of this year's operations. The change in net position is a .62% increase for the fiscal year ended June 30, 2013. During the year, the Organization's revenues exceeded expenses by \$250,139

The total cost of the Organization's expenditures in 2013 decreased 2.06% from the fiscal year ended June 30, 2012. Balances of cash increased \$119,435 during the fiscal year ended June 30, 2013.

The Authority's liabilities decreased \$845,704 over the fiscal year ended June 30, 2013 primarily a result of principal paid on loans.

Overview of the Financial Statements

This annual report consists of three parts – management's discussion and analysis (this section), 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 Authority's overall financial status.

The remaining statements are fund financial statements that focus on individual parts of the government, reporting the Authority'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 position 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 Authority's net position and how they have changed. Net position – 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 position 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:

1. 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 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 Position. The Organization's net position increased \$250,139 between fiscal years 2012 and 2013. In comparison, net position for the fiscal year ended June 30, 2012 decreased \$504,206 from the fiscal year ended June 30, 2011. Income from ongoing operations increased \$710,163 during the fiscal year ended June 30, 2013 from the fiscal year ended June 30, 2012.

Nashville & Eastern Railroad Authority

Net Position

June 30, 2013 and 2012

	2013	Restated 2012	% Change
Current and Other Assets	\$ 511,647	\$ 655,941	-22.00%
Capital Assets	48,635,093	49,086,364	-0.92%
Total Assets	<u>49,146,740</u>	<u>49,742,305</u>	-1.20%
Current and Other Liabilities	1,612,726	1,307,036	23.39%
Long Term Liabilities	7,192,581	8,343,974	-13.80%
Total Liabilities	<u>8,805,307</u>	<u>9,651,010</u>	
Net Position			
Net Investment in Capital Assets	40,653,698	40,690,453	-0.09%
Unrestricted	<u>(312,264)</u>	<u>(599,158)</u>	-47.88%
Total Net Position	<u>\$ 40,341,434</u>	<u>\$ 40,091,295</u>	0.62%

Changes In Net Position. The Authority's total revenues increased \$710,153 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 \$450,091. Revenues from the lease of the railroad decreased \$39,926. The total cost of all programs decreased by \$44,162.

Nashville & Eastern Railroad Authority
 Changes in Net Position
 June 30, 2013 and 2012

	2013	Restated 2012	% Change
Total Operating Revenues	\$ 2,347,610	\$ 1,637,457	43.37%
Total Operating Expenses	2,097,471	2,141,663	-2.06%
Operating Income/(Deficit)	250,139	(504,206)	-149.61%
 Increase/(Decrease) in Net Position	 <u>\$ 250,139</u>	 <u>\$ (504,206)</u>	 -149.61%

Capital Assets. As of June 30, 2013, the Organization had invested \$40,653,699 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 received substantial improvements during the fiscal year ended June 30, 2013 from construction to upgrade the railroad from Algood to Monterey and normal improvements to the railroad, performed with funding from the Tennessee Department Of Transportation.

The Organizations fiscal year 2014 capital budget is uncertain. All funds once available from The General Assembly through TDOT have been sequestered as a result of a federal lawsuit regarding discrimination between modes 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 POSITION
JUNE 30, 2013

	Governmental Activities
ASSETS	
Cash and Cash Equivalents	\$ 271,265
Accounts Receivable	240,382
Total Current Assets	511,647
Property & Equipment (Net of Accumulated Depreciation)	48,635,093
Total Assets	49,146,740
LIABILITIES	
Accounts Payable	79,963
Accrued Interest	153,658
State Contract Revenues for Future Projects	340,291
Current Portion of Long-Term Debt	1,038,814
Total Current Liabilities	1,612,726
Notes Payable	7,192,581
Total Liabilities	8,805,307
NET POSITION	
Unrestricted	(312,264)
Net Investment in Capital Assets	40,653,698
Total Net Position	\$ 40,341,434

See Accompanying Notes To Financial Statements.

NASHVILLE & EASTERN RAILROAD AUTHORITY
STATEMENT OF ACTIVITIES
FOR THE FISCAL YEAR ENDED JUNE 30, 2013

Functions/Programs	Expenses	Program Revenues Charges For Services	Grants and Contributions	Net (Expense) Revenue and Changes in Net Assets
Governmental Activities				
Infrastructure Development	\$ 1,662,929	\$ 2,346,110	\$ -	\$ 683,181
General & Administrative	112,606	1,500	-	(111,106)
Interest on Long-Term Debt	321,936	-	-	(321,936)
	2,097,471	2,347,610	-	250,139
General Revenues				
Interest Income				-
Total General Revenues, Special Items, & Transfers				-
				250,139
Change In Net Position				250,139
Net Position - Beginning of Year, Restated				40,091,295
Net Position - End of Year				\$ 40,341,434

See Accompanying Notes To Financial Statements

FUND STATEMENTS

NASHVILLE & EASTERN RAILROAD AUTHORITY
BALANCE SHEET
JUNE 30, 2013

ASSETS

Current Assets	
Cash and Cash Equivalents	\$ 271,264
Accounts Receivable - Other	240,382
	240,382
Total Current Assets	\$ 511,646

LIABILITIES AND FUND BALANCE

Current Liabilities	
Accounts Payable	\$ 79,963
State Contract Revenues to be used for future projects	340,291
Fund Balances	
Unassigned	91,392
	91,392
Total Liabilities, Deferred Inflows & Fund Balance	\$ 511,646

Total Fund Balance Per Fund Financial Statements	\$ 91,392
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Reconciliation to the Statement of Net Position:

Fixed assets are not included in the fund financial statements prepared on the modified accrual basis of accounting.	48,635,093
Accrued interest on bonds are not reported in the current period and therefore are not reported in the fund financial statements.	(153,658)
Long term debt is not included in the fund financial statements prepared on the modified accrual basis of accounting	(8,231,393)
Net Position	\$ 40,341,434

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, 2013

Revenues	
State of Tennessee	\$ 1,860,433
Nashville & Eastern Rail Corp.	186,589
Federal Emergency Management Agency	299,088
Rent	<u>1,500</u>
 Total Revenues	 2,347,610
 Expenditures	
Rail Rehabilitation	1,175,658
Audit	6,115
Directors' Fees	2,800
Legal Services	16,498
Administration	78,991
Miscellaneous	(798)
Principal Payments On Loans	414,517
Interest Expense	343,307
Managing Director Fees	<u>45,000</u>
 Total Expenditures	 <u>2,082,088</u>
 Excess of Revenues over Expenditures	 265,522
 Fund Balance - Beginning of Year, Restated	 <u>(174,130)</u>
Fund Balance - End of Year	<u><u>\$ 91,392</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, 2013

Reconciliation to Statement of Activities:	
Net Change in Fund Balances - Total Governmental Funds	\$ 265,522
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.	1,211,659
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.	414,517
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.	21,370
Depreciation is not recorded in the fund financial statements but is reported in the government-wide financial statements.	<u>(1,662,929)</u>
Change in net position	<u>\$ 250,139</u>

See Accompanying Notes to Financial Statements

NASHVILLE & EASTERN RAILROAD AUTHORITY
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2013

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 position 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, 2013

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, CONTINUED

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.

NASHVILLE & EASTERN RAILROAD AUTHORITY
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2013

NOTE 2 – CASH AND CASH EQUIVALENTS

At June 30, 2013 the bank balance of cash and cash equivalents is \$281,879. The bank balances were entirely secured by FDIC insurance or collateralized through the State of Tennessee Bank Collateral Pool.

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 to the Authority \$1,250 per month for the use of its maintenance facility in Lebanon beginning in January 2005 and \$700 per month for the use of its storage facility beginning July 2012. This lease agreement has been renewed through the year 2063 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 leases totaled \$186,589 for the year ended June 30, 2013.

The Authority leases a piece of property purchased in the prior fiscal year under a month to month lease. Revenues from this lease amounted to \$1,500 for the year ended June 30, 2013.

NASHVILLE & EASTERN RAILROAD AUTHORITY
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2013

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, 2013.

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.

Accounts Receivable at June 30, 2013 consists of the following :

State Contracts	\$ 72,200
FEMA Contracts	90,637
Other	77,545
	<u>\$ 240,382</u>

Deferred grant revenues at June 30, 2013 are \$340,291. This represents amounts received in prior years under State grant GG-10-33918-00 that were used to fund the flood repairs until the FEMA grant money was received. Since the majority of the FEMA money has been received, the State funding received in prior years will now be used to fund future rail rehabilitation projects as directed by the State. This is reported in the financial statements as a current liability.

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, 2013 is presented below:

NASHVILLE & EASTERN RAILROAD AUTHORITY
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2013

NOTE 6 – FIXED ASSETS, CONTINUED

	Balance July 1, 2012	Additions (Deductions)	Balance June 30, 2013
<u>Nondepreciable Assets</u>			
Land	\$ 499,666	\$ -	\$ 499,666
Total Nondepreciable Assets	499,666	-	499,666
<u>Depreciable Assets</u>			
Buildings	965,808	36,000	1,001,808
Branchline and Right of Way	2,168,227	-	2,168,227
Rail Rehabilitation	63,371,612	1,175,659	64,547,271
	67,005,313	1,211,659	68,216,972
<u>Accumulated Depreciation</u>			
Buildings	277,198	24,352	301,550
Branchline and Right of Way	1,520,098	54,206	1,574,304
Rail Rehabilitation	16,121,654	1,584,371	17,706,025
	17,918,950	1,662,929	19,581,879
Capital Assets, Net	\$ 49,586,029	\$ (451,270)	\$ 48,635,093

Depreciation expense for the fiscal year ended June 30, 2013 was \$1,662,929.

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.

NASHVILLE & EASTERN RAILROAD AUTHORITY
 NOTES TO FINANCIAL STATEMENTS
 JUNE 30, 2013

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.

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, 2013, the Authority had an outstanding balance of \$929,983 on that line which was used to fund the commuter rail costs. The note bears interest at a variable interest rate, with annual payments of \$250,000 being due beginning June 1, 2006. The loan matures January 15, 2014. Subsequent to the date of these financial statements, the bank extended the maturity date through April 15, 2014.

	<u>Principal</u>	<u>Interest</u>
2014	\$ 929,983	\$ 38,110

The Nashville & Eastern Railroad Authority made one payment during the fiscal year ended June 30, 2013.

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, 2013 the outstanding balance on the loan is \$7,051,411. 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, 2013

NOTES PAYABLE - CONTINUED

	Principal	Interest
2014	\$ 108,831	\$ 296,064
2015	113,392	291,503
2016	118,145	286,750
2017	123,097	281,798
2018	128,256	276,639
2019-2023	726,560	1,297,915
2024-2028	892,126	1,132,349
2029-2033	1,095,420	929,055
2034-2038	1,345,040	679,435
2039-2043	1,651,542	372,933
2044-2045	749,003	48,206
	<u>\$ 7,051,411</u>	<u>\$ 5,892,648</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 a prior year, but the State has not reduced funding yet.

Long-term liability activity for the year ended June 30, 2013 was as follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Amounts Due Within 1 Year
State of Tennessee	\$ 250,000	\$ -	\$ -	\$ 250,000	\$ -
First Tennessee Bank	1,127,466	-	(197,483)	929,983	929,983
First Tennessee Line of Credit	100,000	-	(100,000)	-	-
USDA	7,168,445	-	(117,034)	7,051,411	108,831
	<u>\$ 8,645,911</u>	<u>\$ -</u>	<u>\$ (414,517)</u>	<u>\$ 8,231,394</u>	<u>\$ 1,038,814</u>

NOTE 10 – RESTATEMENT OF NET POSITION AND FUND BALANCE

See note 5 above for information regarding deferred grant revenue. As this is funding that was previously reported as earned revenue in prior years, opening net position – unrestricted and opening fund balance – unassigned were reduced by \$340,291.

NASHVILLE & EASTERN RAILROAD AUTHORITY
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2013

NOTE 11 – SUBSEQUENT EVENTS

Subsequent to the fiscal year end, the Authority was issued a Stop Work Notice by the State of Tennessee Department of Transportation involving all active grant contracts. The Stop Work Notice was in response to a ruling against the Tennessee Department of Revenue involving sales tax charged on diesel fuel sales to railroads. As this is the main source of funding for the grant contracts awarded to the Authority, and the length of time that the Stop Work Notice will be in effect is unknown, the effect on the future operations of the Authority are uncertain.

INTERNAL CONTROL AND COMPLIANCE SECTION

**INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER FINANCIAL
REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF
FINANCIAL STATEMENTS PERFORMED
IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS***

To the Board of Directors
Nashville & Eastern Railroad Authority

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the governmental activities and the major fund of Nashville & Eastern Railroad Authority, as of and for the year ended June 30, 2013, and the related notes to the financial statements, which collectively comprise Nashville & Eastern Railroad Authority's basic financial statements and have issued our report thereon dated February 21, 2014.

Internal Control Over Financial Reporting

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

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. However, as described below we identified certain deficiencies in internal control that we consider to be material weaknesses.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiencies described below to be material weaknesses:

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.

A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Compliance and Other Matters

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

Nashville & Eastern Railroad Authority's Response to Findings

Nashville & Eastern Railroad Authority's response to the findings identified in our audit is presented below. Nashville & Eastern Railroad Authority's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

Response: We do simple accounting utilizing Quickbooks and one general fund which is basically checkbook accounting with the ability to categorize all areas of receipts and expenditures as necessary. We feel the expense to add additional expertise is unnecessary, due to the low volume of accounting transactions. A cost/benefit ratio would never rise to a positive level and we have never experienced any major accounting deficiencies in our adopted procedures.

Purpose of this Report

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

Dempsey Vantrouse & Foltz PLLC

Lebanon, TN
February 21, 2014

SUPPLEMENTARY SCHEDULES

Nashville Eastern Railroad Authority
Schedule of State and Federal Contract Expenditures
June 30, 2013

Number	Grantor Agency	Balance July 01, 2012	Receipts	Expenditures	Balance June 30, 2013
Z-10-220816A-00	TN Department of Transportation	\$ -	\$ 927	\$ 927	\$ -
GG-10-30906A-00	TN Department of Transportation	-	442	442	-
GG-10-33918-00	TN Department of Transportation	-	340,291	-	(340,291)
Z-11-RE2053-00	TN Department of Transportation	-	5,750	5,750	-
Z-11-RR1006-00A	TN Department of Transportation	42,633	204,087	161,455	-
Z-12-RE1013-00	TN Department of Transportation	3,662	25,010	21,348	-
Z-12-RE1031-00	TN Department of Transportation	11,068	58,502	47,434	-
Z-12-RR1021-00	TN Department of Transportation	18,278	121,155	102,877	-
Z-12-RR1024-00	TN Department of Transportation	295,210	865,382	570,173	-
Z-12-RE1049-00	TN Department of Transportation	-	47,000	47,000	-
Z-13-RR1014-00	TN Department of Transportation	-	255,000	255,000	-
Z-13-RR1015-00	TN Department of Transportation	-	413,100	413,100	-
Z-13-RE2011-00	TN Department of Transportation	-	7,783	8,233	450
Z-13-RR2029-00	TN Department of Transportation	-	9,047	10,771	1,724
Z-13-RR1021-00	TN Department of Transportation	-	145,898	215,925	70,027
	Total State Contracts	<u>370,851</u>	<u>2,498,448</u>	<u>1,859,507</u>	<u>(268,091)</u>
FEMA-1909-DR-TN	TN Emergency Management Agency	-	135,177	138,467	3,290
FEMA-1937-DR-TN	TN Emergency Management Agency	-	78,819	160,621	81,803
	Total Federal Contracts	<u>-</u>	<u>213,995</u>	<u>299,088</u>	<u>85,093</u>
	Total Federal and State Contracts	<u>\$ 370,851</u>	<u>\$ 2,712,443</u>	<u>\$ 2,158,595</u>	<u>\$ (182,998)</u>

Reconciliation to Statement of Net Position:

Accounts Receivable - State Contracts - see Note 5	\$ 72,200
Deferred Revenue - State Contracts - see Note 5	(340,291)
	<u>\$ (268,091)</u>
Accounts Receivable - FEMA Contracts - see Note 5	\$ 90,637
Accounts Payable - FEMA - included in Accounts Payable	(5,544)
	<u>\$ 85,093</u>

See Accompanying Notes to Financial Statements

NASHVILLE & EASTERN RAILROAD AUTHORITY
SCHEDULE OF SALARIES AND FIDELITY BONDS
OF PRINCIPAL OFFICIALS (UNAUDITED)
JUNE 30, 2013

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

See Accompanying Notes To Financial Statements