NASHVILLE & EASTERN RAILROAD AUTHORITY
FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2015

NASHVILLE & EASTERN RAILROAD AUTHORITY

JUNE 30, 2015

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INDEPENDENT AUDITORS' REPORT

To the Board of Directors
Nashville & Eastern Railroad Authority

Report on the Financial Statements

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, 2015, and the related notes to the financial statements, which collectively comprise the Nashville & Eastern Railroad 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, 2015, 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 Schedule of State & Federal Contract Expenditures and Schedule of Fidelity Bonds of Principal Officials are presented for purposes of additional analysis and are not a required part of the basic financial statements.

The Schedule of State & 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 & 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.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated March 24, 2016, 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 internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Nashville & Eastern Railroad Authority's internal control over financial reporting and compliance.

Dempsey Vantrease & Follis PLLC

Lebanon, TN
March 24, 2016

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, 2015. Please read it in conjunction with the financial statements, which follow this section.

Financial Highlights

The Organization's net position decreased $1,844,350 over the course of this year's operations caused by the Class 1 railroad industry filing a discrimination lawsuit against the State of Tennessee. TDOT subsequently put a freeze on The Transportation Equity Fund that is annually allocated to shortlines based on a needs study to maintain the shortline system to a safe and efficient level of operation.

The Tennessee Shortline system of 800 plus miles serves 35 out of 95 Counties plus small to medium size urban areas. The 800 miles generates a wide economic footprint developing the industrial landscape that brings jobs to Tennessee.

The change in net position is a 4.69% decrease from the fiscal year ended June 30, 2014.

The total cost of the Organization's expenditures in 2015 decreased 2.29% from the fiscal year ended June 30, 2014. Operating Revenue dropped 76.44% during the fiscal year ended June 30, 2015.

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 fund 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 decreased $1,844,350 between fiscal years 2014 and 2015. In comparison, net position for the fiscal year ended June 30, 2014 decreased $1,049,110 from the fiscal year ended June 30, 2013. Income from ongoing operations decreased $844,567 during the fiscal year ended June 30, 2015 from the fiscal year ended June 30, 2014.

Nashville & Eastern Railroad Authority
Net Position
June 30, 2015 and 2014

	2015	2014	% Change
Current and Other Assets	$ 296,879	$ 489,150	-39.31%
Capital Assets	46,198,610	47,851,889	-3.45%
Total Assets	46,495,489	48,341,039	-3.82%
Current and Other Liabilities	8,219,954	8,798,715	-6.58%
Long Term Liabilities	827,561	250,000	231.02%
Total Liabilities	9,047,515	9,048,715	
Net Position			
Net Investment in Capital Assets	38,501,678	39,870,495	-3.43%
Unrestricted	(1,053,704)	(578,171)	-82.25%
Total Net Position	$ 37,447,974	$ 39,292,324	-4.69%

Changes In Net Position. The Authority's total revenues decreased $844,567 during the fiscal year. The Authority's primary sources of revenue are sequestered 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 decreased $876,687. The total cost of all programs decreased by $49,327.

Nashville & Eastern Railroad Authority
Changes in Net Position
June 30, 2015 and 2014

	2015	2014	% Change
Total Operating Revenues	$ 260,239	$ 1,104,806	-76.44%
Total Operating Expenses	2,104,589	2,153,916	-2.29%
Operating Income/(Deficit)	(1,844,350)	(1,049,110)	-75.80%
Increase/(Decrease) in Net Position	$ (1,844,350)	$ (1,049,110)	-75.80%

Capital Assets. As of June 30, 2015, the Organization had invested $38,501,678 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 Organization's fiscal year 2015 capital budget was cut. 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, 2015

	Governmental Activities
ASSETS	
Cash and Cash Equivalents	$ 183,625
Accounts Receivable	113,254
Total Current Assets	296,879
Property & Equipment (Net of Accumulated Depreciation)	46,198,610
Total Assets	46,495,489
LIABILITIES	
Accounts Payable	63,398
Accrued Interest	696,894
State Contract Revenues for Future Projects	340,291
Current Portion of Long-Term Debt	7,119,371
Total Current Liabilities	8,219,954
Notes Payable	827,561
Total Liabilities	9,047,515
NET POSITION	
Unrestricted (deficit)	(1,053,704)
Net Investment in Capital Assets	38,501,678
Total Net Position	$ 37,447,974

See Accompanying Notes To Financial Statements.

NASHVILLE & EASTERN RAILROAD AUTHORITY
STATEMENT OF ACTIVITIES
FOR THE FISCAL YEAR ENDED JUNE 30, 2015

Functions/Programs	Expenses	Program Revenues: Charges For Services	Program Revenues: Grants and Contributions	Net (Expense) Revenue and Changes in Net Position
Governmental Activities				
Infrastructure Development	$ 1,715,682	$ 252,739	$ -	$ (1,462,943)
General & Administrative	93,343	7,500	-	(85,843)
Interest on Long-Term Debt	295,564	-	-	(295,564)
	2,104,589	260,239	-	(1,844,350)
General Revenues				
Interest Income				-
Total General Revenues, Special Items, & Transfers				-
Change In Net Position				(1,844,350)
Net Position - Beginning of Year				39,292,324
Net Position - End of Year				$ 37,447,974

See Accompanying Notes To Financial Statements

FUND STATEMENTS

NASHVILLE & EASTERN RAILROAD AUTHORITY
BALANCE SHEET
JUNE 30, 2015

ASSETS

Current Assets		
Cash and Cash Equivalents	$	183,625
Accounts Receivable - Other		113,254
Total Current Assets	$	296,879

LIABILITIES AND FUND BALANCE

Current Liabilities		
Accounts Payable	$	63,398
State Contract Revenues to be used for future projects		340,291
Fund Balances		
Unassigned		(106,810)
Total Liabilities, Deferred Inflows & Fund Balance	$	296,879
Total Fund Balance Per Fund Financial Statements	$	(106,810)
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.		46,198,610
Accrued interest on bonds are not included in the fund financial statements prepared on the modified accrual basis of accounting.		(696,894)
Long term debt is not included in the fund financial statements prepared on the modified accrual basis of accounting		(7,946,932)
Net Position	$	37,447,974

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, 2015

Revenues		
Nashville & Eastern Rail Corp.	$	252,739
Rent		7,500
Total Revenues		260,239
Expenditures		
Rail Rehabilitation		62,404
Audit		6,000
Directors' Fees		5,550
Legal Services		4,462
Administration		32,331
Principal Payments on Loans		284,461
Interest Expense		58,850
Managing Director Fees		45,000
Total Expenditures		499,058
Excess of Revenues over Expenditures		(238,819)
Fund Balance - Beginning of Year		132,009
Fund Balance - End of Year	$	(106,810)
Reconciliation to Statement of Activities:		
Net Change in Fund Balances - Total Governmental Funds	$	(238,819)
Purchases of fixed assets are an expenditure in the governmental funds, but are increases in property and equipment on the statement of net position in the government-wide statements.		62,404
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.		284,461
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.		(236,714)
Depreciation is not recorded in the fund financial statements but is reported in the government-wide financial statements.		(1,715,682)
Change in net position	$	(1,844,350)

See Accompanying Notes to Financial Statements

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.

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.

NOTE 2 – CASH AND CASH EQUIVALENTS

At June 30, 2015 the bank balance of cash and cash equivalents is $187,659. This account was not designated as a governmental fund.

Various restrictions on deposits and investments are imposed by state statutes. These restrictions are summarized as follows: All deposits with financial institutions other than savings and loan associations must be collateralized in an amount equal to 105% of the value of the deposit secured thereby. The collateral must be placed by the depository bank in an escrow account in a second bank for the benefit of the authority.

Deposits with savings and loan associations must be collateralized by one of the following methods: 1) By an amount equal to 105% of the face amount of uninsured deposits if the collateral is of the same character as that required for other financial institutions; 2) By an irrevocable letter of credit issued by the Federal Home Loan Bank; or, 3) By a surety bond issued by an insurance company licensed under the laws of the State of Tennessee whose claims paying ability is rated in the highest category by at least two nationally recognized statistical rating services.

The promissory notes must be in an amount equal to 150% of the amount of uninsured deposits. Nashville & Eastern Railroad Authority had no deposits with savings and loan associations during the period under audit.

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 one pending lawsuit according to the Authority's legal counsel. See Note 10 – Uncertainties. 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. The operator will provide appropriate maintenance of the line. Currently, quarterly lease payments of 4% of the gross freight revenues on the first $3,695,267.06; 5% between $3,695,267.07 and $4,927,022.73; and 6% of operating revenues over $4,927,022.74 are due. For commuter rail service, the Authority receives 10% of

NOTE 4 – LEASES, CONTINUED

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 $252,739 for the year ended June 30, 2015.

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 $7,500 for the year ended June 30, 2015.

At June 30, 2015, the Authority had a receivable related to these leases in the amount of 113,254.

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, 2015.

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.

Unearned grant revenues at June 30, 2015 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 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. The contract expired April 2015.

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,

NOTE 6 – FIXED ASSETS, CONTINUED

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, 2015 is presented below:

	Balance July 1, 2014	Additions (Deductions)	Balance June 30, 2015
Nondepreciable Assets			
Land	$ 499,666	$ -	$ 499,666
Total Nondepreciable Assets	499,666	-	499,666
Depreciable Assets			
Buildings	1,001,808		1,001,808
Branchline and Right of Way	2,168,227	-	2,168,227
Rail Rehabilitation	65,457,061	62,404	65,519,465
	69,126,762	62,404	69,189,166
Accumulated Depreciation			
Buildings	326,595	25,045	351,640
Branchline and Right of Way	1,628,510	54,206	1,682,716
Rail Rehabilitation	19,319,769	1,636,431	20,956,200
	21,274,874	1,715,682	22,990,556
Capital Assets, Net	$ 47,851,888	$ (1,653,278)	$ 46,198,610

Depreciation expense for the fiscal year ended June 30, 2015 was $1,715,682.

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

NOTE 7 – COMMUTER RAIL, CONTINUED

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.

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, 2015, the Authority had an outstanding balance of $645,521 on that line which was used to fund the commuter rail costs. The loan was in default, so in September 2014 there was a forbearance agreement signed by both parties. The forbearance agreement states "the Lender hereby agrees to forbear from exercising its remedies under the Loan Documents until the earlier of (i) July 15, 2015, or (ii) the occurrence of a Termination Event, as defined in Section 3 of this Agreement". On January 30, 2015, the Authority entered into an Amended and Restated Promissory Note ("Note") with First Tennessee Bank National Association. The Note was to pay back the funds still owed to First Tennessee on the line of credit dated December 3, 2004. In the Note, the amount the Authority owed to First Tennessee was $929,591.93. The Authority had a principal pay down of $250,000 for the Lender to accept the Note. The Note shall mature on the earlier of: (a) July 15, 2017 or (b) the date on which the unpaid amount of this Note has been declared or automatically has become due and payable, whether by acceleration or otherwise (the "Maturity Date"). The Note defines that all principal outstanding hereunder shall earn interest at a fixed rate of interest equal to 4.81% per annum. This Note shall be repaid as follows: (a) commencing March 31, 2015, and on the last day of each quarter thereafter through June 30, 2017, the Authority shall pay to First Tennessee a principal payment of $16,990, plus accrued interest outstanding as of quarter-end.

NOTE 9 – NOTES PAYABLE, CONTINUED

Principal maturities over the life of the loan are scheduled as follows:

	Principal	Interest
2016	$67,960	$30,330
2017	67,960	26,934
2018	509,692	1,022
	$645,612	$58,286

The Nashville & Eastern Railroad Authority made the principal pay down of $250,000, three interest only payments under the forbearance agreement, and two payments under the Note during the fiscal year ended June 30, 2015.

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, 2015 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. The loan is currently in default. According to the loan document, "upon default in the payments of any principal and accrued interest on the bonds or in the performance of any covenant or agreement contained herein or in the instruments incident to making or insuring the loan, the USDA at its option may (a) declare the entire principal amount then outstanding and accrued interest immediately due and payable, (b) for the account of the Association (payable from the source of funds pledged to pay the bonds or any other legally permissible source), incur and pay reasonable expenses for repair, maintenance, and operation of the facility and such other reasonable expenses as may be necessary to cure the cause of default, and/or (c) take possession of the facility, repair, maintain, and operate or rent it. Default under the provisions of this resolution or any instrument incident to the making or insuring of the loan may be construed by the USDA to constitute default under any other instrument held by the USDA and executed or assumed by the Association, and default under any such instrument may be construed by the USDA to constitute default hereunder." See Note 10 – Uncertainties. The Nashville & Eastern Railroad Authority signed a work-out agreement in the June 30, 2015 fiscal year. The work-out agreement states that the "borrower will complete the following actions to resolve the defaults". The following actions are required: "1. Provide quarterly financial statements including Balance Sheet, Income Statement, and Cash Flow Statement. To be completed one month following each quarter. Provide NERA Audit annually. 2. Notify this office of all court hearing dates and provide the results of those hearings that affect his case. To be completed as information becomes available. 3. After the final ruling is determined for this case, Nashville & Eastern Railroad Authority financial information will be evaluated and this account will be paid current if feasible. 4. After the final ruling, if the account cannot be paid current additional servicing actions may be considered by the agency upon Nashville & Eastern Railroad Authority financial statement

NOTE 9 – NOTES PAYABLE, CONTINUED

review." As of June 30, 2015, this case (see Note 10) is still pending. The amount currently due on the loan is as follows:

	Principal	Interest
2015	$7,051,411	$696,894

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, 2015 was as follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Amounts Due Within 1 Year
State of Tennessee	$250,000	$-	$-	$250,000	$-
First Tennessee Bank	929,982	-	284,461	645,521	67,960
USDA	7,051,411	-	-	7,051,411	7,051,411
	$8,231,393	$-	$284,461	$7,946,932	$7,119,371

NOTE 10 – UNCERTAINTIES

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.

Suit has been filed against Nashville and Eastern Railroad Authority in the Davidson County Chancery Court by Binkley Family Investments for damages associated with alleged trespass on properties owned/controlled by Binkley Family Investments. Suit has not been fully resolved as of the date of the audit report. Nashville & Eastern Railroad Authority categorically denies any wrong-doing and will take the matter to trial and as far as necessary to defend the cause of action. The likelihood of success is extremely high and no judgment against Nashville & Eastern Railroad Authority is expected.

INTERNAL CONTROL AND COMPLIANCE SECTION

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

To the Board of 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, 2015, 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 March 24, 2016.

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, we did identify certain deficiencies in internal control, described below 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 the following instance of noncompliance or other matters that are required to be reported under *Government Auditing Standards*

> Tennessee Code Annotated Section 9-1-118(c) states "any funds invested, deposited or placed for deposit which are not covered by federal deposit insurance shall be collateralized in the same manner as

state deposits or in the collateral pool". Nashville & Eastern Railroad Authority had a bank account with First Tennessee Bank that was not designated as a governmental account. First Tennessee Bank is a member of the state collateral pool, but the funds were not collateralized in accordance with state statutes because the account was not designated as a governmental account. The Authority should make sure the account has been designated as a governmental account.

Nashville & Eastern Railroad Authority's Response to Findings

Nashville & Eastern Railroad Authority's response to the findings identified in our audit is described 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 to material weakness: 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.

Response to noncompliance or other matters: The bank account has since been designated as a governmental account.

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 Vantrease & Follis PLLC

Lebanon, TN
March 24, 2016

SUPPLEMENTARY SCHEDULES

Nashville Eastern Railroad Authority
Schedule of State and Federal Contract Expenditures
June 30, 2015

Number	Grantor Agency	Balance July 01, 2014	Receipts	Expenditures	Balance June 30, 2015
GG-10-33918-00	TN Department of Transportation	$ (340,291)	$ -	$ -	$ (340,291)
	Total State Contracts	(340,291)	-	-	(340,291)
	Total Federal Contracts	-	-	-	-
	Total Federal and State Contracts	$ (340,291)	$ -	$ -	$ (340,291)

Reconciliation to Statement of Net Position:
Unearned Revenue - State Contracts - see Note 5 $ (340,291)

See Accompanying Notes to Financial Statements

NASHVILLE & EASTERN RAILROAD AUTHORITY
SCHEDULE OF SALARIES AND FIDELITY BONDS
OF PRINCIPAL OFFICIALS (UNAUDITED)
JUNE 30, 2015

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