AUDIT REPORT

Tennessee State School Bond Authority

For the Year Ended
June 30, 2010

STATE OF TENNESSEE

COMPTROLLER OF THE TREASURY

Department of Audit

Division of State Audit

Tennessee Comptroller of the Treasury

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June 23, 2011

The Honorable Bill Haslam, Governor
and
Members of the General Assembly
State Capitol
Nashville, Tennessee 37243
and
Members of the Tennessee State School Bond Authority
State Capitol
Nashville, Tennessee 37243

Ladies and Gentlemen:

Transmitted herewith is the financial and compliance audit of the Tennessee State School Bond Authority for the year ended June 30, 2010. You will note from the independent auditor's report that an unqualified opinion was given on the fairness of the presentation of the financial statements.

Consideration of internal control over financial reporting and tests of compliance resulted in no audit findings.

Sincerely,

Arthur A. Hayes, Jr., CPA
Director

AAH/ddm
11/015

State of Tennessee

Audit Highlights

Comptroller of the Treasury — Division of State Audit

Financial and Compliance Audit

Tennessee State School Bond Authority

For the Year Ended June 30, 2010

AUDIT OBJECTIVES

The objectives of the audit were to consider the Authority's internal control over financial reporting; to determine compliance with certain provisions of laws, regulations, and contracts (including the bond resolutions); to determine the fairness of the presentation of the financial statements; and to recommend appropriate actions to correct any deficiencies.

AUDIT FINDINGS

The audit report contains no findings.

OPINION ON THE FINANCIAL STATEMENTS

The opinion on the financial statements is unqualified.

Audit Report
Tennessee State School Bond Authority
For the Year Ended June 30, 2010

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Tennessee State School Bond Authority
For the Year Ended June 30, 2010

INTRODUCTION

POST-AUDIT AUTHORITY

This is a report on the financial and compliance audit of the Tennessee State School Bond Authority. The audit was conducted pursuant to Section 4-3-304, *Tennessee Code Annotated*, which authorizes the Department of Audit to "perform currently a post-audit of all accounts and other financial records of the state government, and of any department, institution, office, or agency thereof in accordance with generally accepted auditing standards and in accordance with such procedures as may be established by the comptroller."

Section 8-4-109, *Tennessee Code Annotated*, authorizes the Comptroller of the Treasury to audit any books and records of any governmental entity that handles public funds when the Comptroller considers an audit to be necessary or appropriate.

BACKGROUND

The Tennessee State School Bond Authority was established by the Tennessee State School Bond Authority Act, Chapter 256 of the Public Acts of 1965. As provided in this act and in Chapter 429 of the Public Acts of 1999, the Authority is to act as a corporate governmental agency of the State of Tennessee for financing projects of the state's higher education institutions and qualified zone academy projects for primary and secondary schools of local government. The Authority is empowered to issue negotiable bonds and notes as a means of providing funds for financing approved projects. These projects include buildings, equipment, structures, and improvements. In 1980, the legislature amended the original act to include, as a project, a program for student loans. To date, the Authority has not issued debt to fund a student loan program. The amount of funds provided should be sufficient to cover the actual project costs, as well as the Authority's administrative expenses, including the cost of conducting the bond and note sales.

In 2009, the Authority was designated by the General Assembly as the Education Agency for the Qualified School Construction Bonds (QSCBs). The QSCBs are tax credit bonds that were authorized in the American Recovery and Reinvestment Act of 2009 and Section 49-3-12, *Tennessee Code Annotated*, as amended. Through the designation, the Authority is authorized to issue QSCBs to make loans to local governments to fund K-12 school construction and renovations.

ORGANIZATION

The Tennessee State School Bond Authority consists of seven members: the Governor, the State Treasurer, the Secretary of State, the Commissioner of Finance and Administration, the Comptroller of the Treasury, the Chancellor of the Tennessee Board of Regents, and the President of the University of Tennessee. The Governor serves as chairman, and the Comptroller of the Treasury serves as secretary. The Director of the Division of State and Local Finance serves as the assistant secretary; the division provides administrative and financial services to the Tennessee State School Bond Authority.

An organization chart for the Tennessee State School Bond Authority is on the following page.

AUDIT SCOPE

The audit was limited to the period July 1, 2009, through June 30, 2010, and was conducted in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in generally accepted government auditing standards. Financial statements are presented for the year ended June 30, 2010, and for comparative purposes, the year ended June 30, 2009. The Tennessee State School Bond Authority has been included as a component unit in the *Tennessee Comprehensive Annual Financial Report*.

OBJECTIVES OF THE AUDIT

The objectives of the audit were

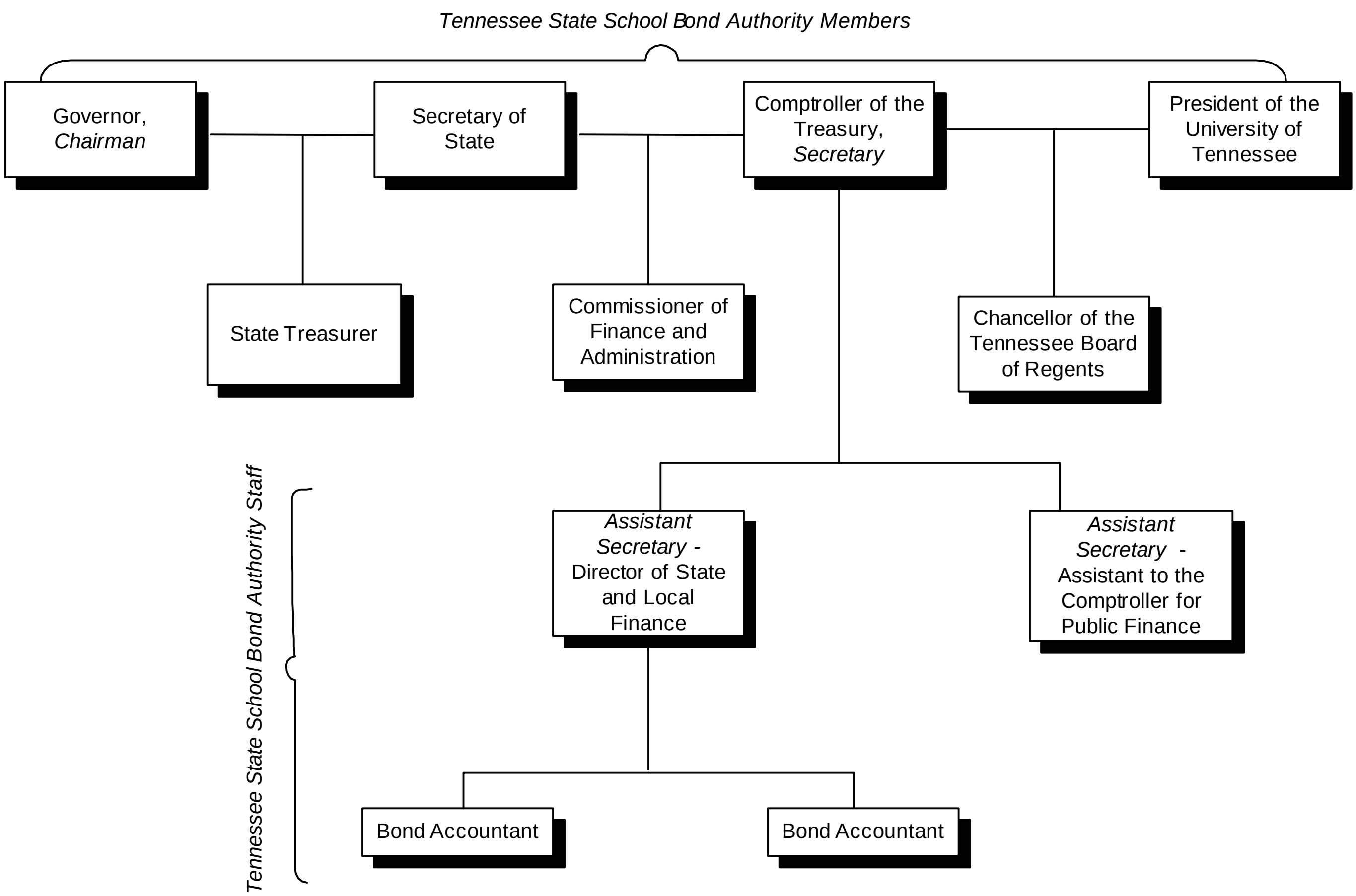
1. to consider the Authority's internal control over financial reporting as a basis for designing auditing procedures for the purpose of expressing an opinion on the financial statements;

2. to determine compliance with certain provisions of laws, regulations, and contracts (including the bond resolutions);

3. to determine the fairness of the presentation of the financial statements; and

4. to recommend appropriate actions to correct any deficiencies.

Tennessee State School Bond Authority
Organization Chart



PRIOR AUDIT FINDINGS

There were no findings in the prior audit report.

OBSERVATIONS AND COMMENTS

CERTIFICATE OF ACHIEVEMENT FOR EXCELLENCE IN FINANCIAL REPORTING

The Government Finance Officers Association of the United States and Canada (GFOA) awarded a Certificate of Achievement for Excellence in Financial Reporting to the Tennessee State School Bond Authority for its *Comprehensive Annual Financial Report (CAFR)* for the year ended June 30, 2009. This is the eighth year that the Authority has prepared a comprehensive annual financial report and received this prestigious award. In order to be awarded a Certificate of Achievement, a government must publish an easily readable and efficiently organized comprehensive annual financial report. This report must satisfy both generally accepted accounting principles and applicable legal requirements. A Certificate of Achievement is valid for a period of one year only. The Authority has submitted its *Comprehensive Annual Financial Report* for the fiscal year ended June 30, 2010, to the GFOA Certificate of Achievement Program.

MANAGEMENT'S RESPONSIBILITY FOR RISK ASSESSMENT

Auditors and management are required to assess the risk of fraud in the operations of the entity. The risk assessment is based on a critical review of operations considering what frauds could be perpetrated in the absence of adequate controls. The auditors' risk assessment is limited to the period during which the audit is conducted and is limited to the transactions that the auditors are able to test during that period. The risk assessment by management is the primary method by which the entity is protected from fraud, waste, and abuse. Since new programs may be established at any time by management or older programs may be discontinued, that assessment is ongoing as part of the daily operations of the entity.

Risks of fraud, waste, and abuse are mitigated by effective internal controls. It is management's responsibility to design, implement, and monitor effective controls in the entity. Although internal and external auditors may include testing of controls as part of their audit procedures, these procedures are not a substitute for the ongoing monitoring required of management. After all, the auditor testing is limited and is usually targeted to test the effectiveness of particular controls. Even if controls appear to be operating effectively during the time of the auditor testing, they may be rendered ineffective the next day by management override or by other circumventions that, if left up to the auditor to detect, will not be noted until the next audit engagement and then only if the auditor tests the same transactions and controls. Furthermore, since staff may be seeking to avoid auditor criticisms, they may comply with the controls during the period that the auditors are on site and revert to ignoring or disregarding the control after the auditors have left the field.

The risk assessments and the actions of management in designing, implementing, and monitoring the controls should be adequately documented to provide an audit trail both for auditors and for management, in the event that there is a change in management or staff, and to maintain a record of areas that are particularly problematic. The assessment and the controls should be reviewed and approved by the head of the entity.

FRAUD CONSIDERATIONS

Statement on Auditing Standards No. 99, *Consideration of Fraud in a Financial Statement Audit,* promulgated by the American Institute of Certified Public Accountants requires auditors to specifically assess the risk of material misstatement of an audited entity's financial statements due to fraud. The standard also restates the obvious premise that management, not the auditors, is primarily responsible for preventing and detecting fraud in its own entity. Management's responsibility is fulfilled in part when it takes appropriate steps to assess the risk of fraud within the entity and to implement adequate internal controls to address the results of those risk assessments.

During our audit, we discussed these responsibilities with management and how management might approach meeting them. We also increased the breadth and depth of our inquiries of management and others in the entity as we deemed appropriate. We obtained formal assurances from top management that management had reviewed the entity's policies and procedures to ensure that they are properly designed to prevent and detect fraud and that management had made changes to the policies and procedures where appropriate. Top management further assured us that all staff had been advised to promptly alert management of all allegations of fraud, suspected fraud, or detected fraud and to be totally candid in all communications with the auditors. All levels of management assured us there were no known instances or allegations of fraud that were not disclosed to us.

RESULTS OF THE AUDIT

AUDIT CONCLUSIONS

Internal Control

As part of the audit of the Tennessee State School Bond Authority's financial statements for the year ended June 30, 2010, we considered internal control over financial reporting as a basis for designing auditing procedures for the purpose of expressing an opinion on the financial statements, as required by auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in generally accepted government auditing standards. Consideration of internal control over financial reporting disclosed no material weaknesses.

Compliance and Other Matters

The results of our audit tests disclosed no instances of noncompliance or other matters that are required to be reported under generally accepted government auditing standards.

Fairness of Financial Statement Presentation

The Division of State Audit has rendered an unqualified opinion on the Tennessee State School Bond Authority's financial statements.

STATE OF TENNESSEE
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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*

January 28, 2011

The Honorable Bill Haslam, Governor
and
Members of the General Assembly
State Capitol
Nashville, Tennessee 37243
and
Members of the Tennessee State School Bond Authority
State Capitol
Nashville, Tennessee 37243

Ladies and Gentlemen:

We have audited the financial statements of the Tennessee State School Bond Authority, a component unit of the State of Tennessee, as of and for the year ended June 30, 2010, and have issued our report thereon dated January 28, 2011. As discussed in Note 1, the Authority implemented GASB Statement 53, "Accounting and Financial Reporting for Derivative Instruments." 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 generally accepted government auditing standards.

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 Authority's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the 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 deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the 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 was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

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, and contracts (including the bond resolutions), 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 generally accepted government auditing standards.

This report is intended solely for the information and use of the General Assembly of the State of Tennessee, the board of directors, management, and others within the entity and is not intended to be and should not be used by anyone other than these specified parties. However, this report is a matter of public record.

Sincerely,

Arthur A. Hayes, Jr., CPA
Director

AAH/ddm

STATE OF TENNESSEE
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Independent Auditor's Report

January 28, 2011

The Honorable Bill Haslam, Governor
and
Members of the General Assembly
State Capitol
Nashville, Tennessee 37243
and
Members of the Tennessee State School Bond Authority
State Capitol
Nashville, Tennessee 37243

Ladies and Gentlemen:

We have audited the accompanying statements of net assets of the Tennessee State School Bond Authority, a component unit of the State of Tennessee, as of June 30, 2010, and June 30, 2009, and the related statements of revenues, expenses, and changes in net assets and cash flows for the years then ended. These financial statements are the responsibility of the Authority's management. Our responsibility is to express an opinion on these financial statements, based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in generally accepted government auditing standards. 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 audits provide a reasonable basis for our opinion. Tennessee statutes, in addition to audit responsibilities, entrust certain other responsibilities to the Comptroller of the Treasury. Those responsibilities include serving as a member of the board of directors of the Tennessee State School Bond Authority. We do not believe that the Comptroller's service in this capacity affected our ability to conduct an independent audit of the Tennessee State School Bond Authority.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Tennessee State School Bond Authority as of June 30, 2010, and June 30, 2009, and the changes in its financial position and cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 1, the Authority implemented GASB Statement 53, “Accounting and Financial Reporting for Derivative Instruments.”

The management’s discussion and analysis, as listed in the table of contents, is not a required part of the basic financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audits were conducted for the purpose of forming an opinion on the basic financial statements. The accompanying financial information listed as supplementary schedules in the table of contents is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audits of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

In accordance with generally accepted government auditing standards, we have also issued our report dated January 28, 2011, on our consideration of the Tennessee State School Bond Authority’s internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, and contracts (including the bond resolutions) 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 generally accepted government auditing standards and should be considered in assessing the results of our audit.

Sincerely,

Arthur A. Hayes, Jr.

Arthur A. Hayes, Jr., CPA
Director

AAH/ddm

Management's Discussion and Analysis

As management of the Tennessee State School Bond Authority (the "Authority"), we offer readers of the Authority's financial statements this narrative overview and analysis of the financial activities as presented in the financial statements and notes to the financial statements of the Authority for the fiscal year ended June 30, 2010. These activities are compared to the results of the fiscal years ended June 30, 2009, and June 30, 2008. This section should be read in conjunction with the Independent Auditor's Report and the audited financial statements and accompanying notes.

Program Activity Highlights

The Authority's purpose is to provide loans to the State's higher education institutions by issuing bonds and notes of the Authority and to local governments on behalf of local education agencies ("LEAs") through Qualified Zone Academy Bonds ("QZABs") and Qualified School Construction Bonds ("QSCBs"). The tables below summarize this business activity.

	Higher Education Facilities Programs		
	2010	**2009**	**2008**
Number of institutions with outstanding loans	20	23	23
Total number of outstanding loans	266	305	302
Balance of outstanding loans	$1,071,728,642	$999,366,228	$859,656,775
Number of loans approved in fiscal year	16	13	28
Dollar value of loans approved in fiscal year	$ 137,587,000	$ 100,194,540	$ 404,899,000
Dollar value of loans approved in fiscal year - unfunded	$ 126,040,774	$ 74,207,486	$ 337,845,001
Dollar value of loans financed in fiscal year	$ 114,860,132	$ 177,063,069	$ 143,962,380
Bonds issued in fiscal year	$ -	$ 276,895,000	$ 118,530,000
Commercial paper issued in fiscal year	$ 110,000,000	$ 163,000,000	$ 147,376,000

	Qualified Zone Academy Bond Program		
	2010	**2009**	**2008**
Number of LEAs with outstanding loans	14	14	14
Total number of outstanding loans	23	23	23
Balance of outstanding loans	$ 28,011,400	$ 31,020,448	$ 33,613,648
Number of loans approved in fiscal year	-	-	-
Dollar value of loans approved in fiscal year	$ -	$ -	$ -
Dollar value of loans approved in fiscal year - unfunded	$ -	$ -	$ -
Dollar value of loans financed in fiscal year	$ 88,899	$ 201,522	$ 7,744,414
Bonds issued in fiscal year	$ -	$ -	$ -

	Qualified School Construction Bond Program		
	2010	2009	2008
Number of LEAs with outstanding loans	13	-	-
Total number of outstanding loans	13	-	-
Balance of outstanding loans	$ 23,191,666	$ -	$ -
Number of loans approved in fiscal year	13	-	-
Dollar value of loans approved in fiscal year	$ 177,000,000	$ -	$ -
Dollar value of loans approved in fiscal year - unfunded	$ 164,654,954	$ -	$ -
Dollar value of loans financed in fiscal year	$ 12,345,046	$ -	$ -
Bonds issued in fiscal year	$ 177,000,000	$ -	$ -

The financial statements and the analysis provided in the remainder of this report reflect the financial results of this activity.

Debt Administration

Pursuant to Section 49-3-1201 et seq., *Tennessee Code Annotated*, the General Assembly of the State created the Tennessee State School Bond Authority to issue revenue bonds and notes to fund capital projects for the higher education institutions including both four-year institutions and two-year community colleges. Such loans are payable from user fees or savings generated from the projects in the case of energy conservation projects. The statute was amended in 1999 to authorize the Authority to issue QZABs and again in 2009 to authorize the Authority to issue QSCBs on behalf of local education agencies throughout the State. For more specific financial information on long-term debt activity, see Note 5, Debt Payable, in the Notes to the Financial Statements.

The State is not liable on the bonds, and the bonds are not a debt of the State of Tennessee.

Higher Education Facilities Programs. When an institution applies for project funding through the Authority, an analysis of the financial feasibility of each loan application is undertaken before it is approved by the Authority. Each higher education system (the University of Tennessee and the Tennessee Board of Regents) must include in its annual budget sufficient funds to repay total debt service. This pledge is a gross revenue pledge of the institution and its system. The Authority is also authorized by statute to intercept the state appropriation to that institution and system if the institution fails to make timely debt service payments to the Authority.

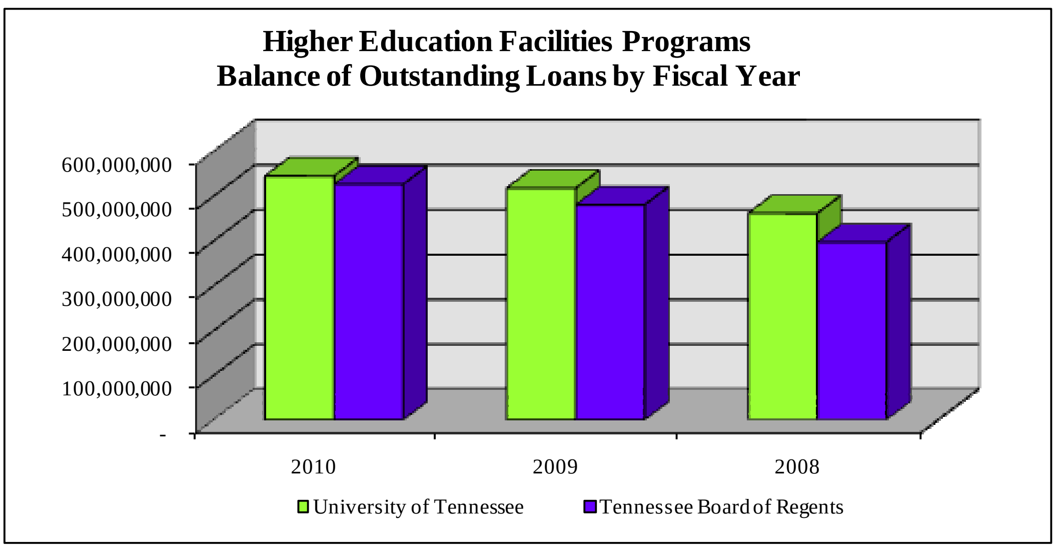
Generally under the financing program for higher education institutions, a project is funded through the Authority's commercial paper program during its construction phase. When projects totaling $50 million or greater are completed or near completion, the Authority fixes the interest rate for the term of the projects by issuing long-term debt. The range of the commercial paper interest rates are shown below for the fiscal year ended June 30, 2010, as compared to the fiscal years 2009 and 2008. The range of the commercial paper interest rates were a function of the term of the commercial paper and a volatile capital market.

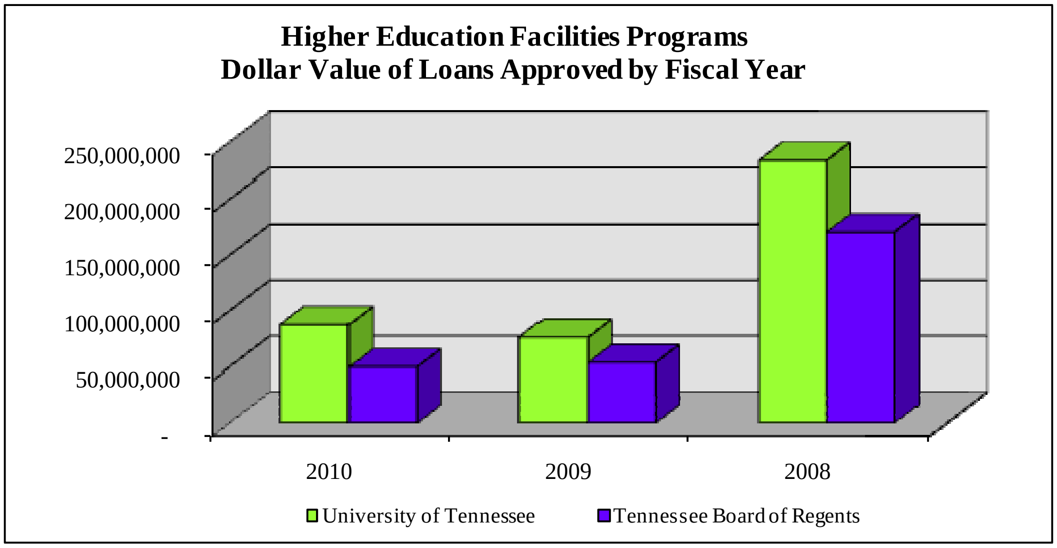
Higher Education Facilities Programs Commercial Paper Interest Rates Range				
	Tax-Exempt		Taxable	
Fiscal Year	Low	High	Low	High
2010	0.17%	0.55%	0.15%	0.50%
2009	0.35%	5.00%	0.35%	6.25%
2008	0.70%	3.90%	2.45%	5.40%

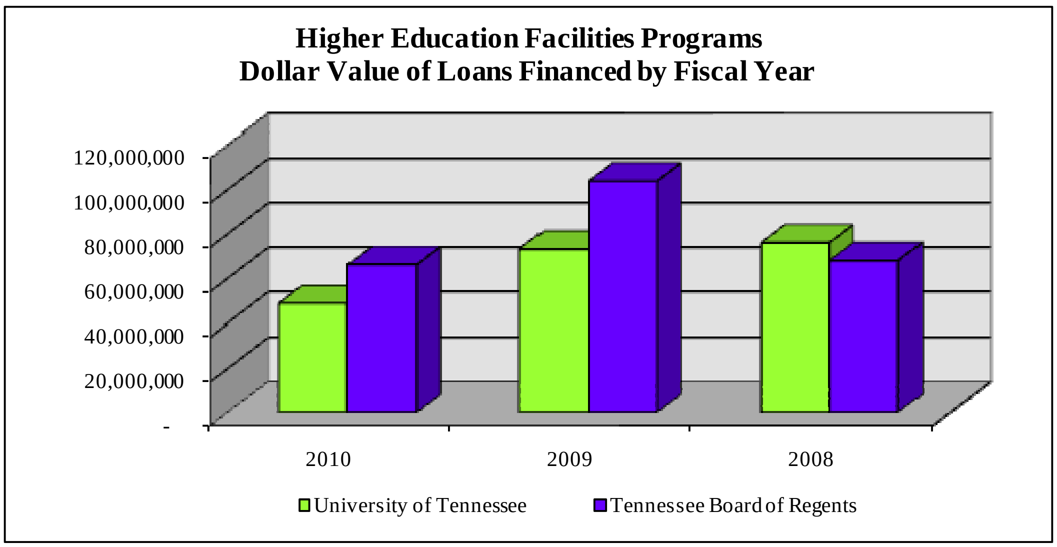
The Authority currently has a Credit Agreement with State Street Bank allowing for a total amount of $300,000,000 of commercial paper to be outstanding. The Credit Agreement with State Street Bank has an expiration date of March 30, 2014, and a commitment fee of .105% paid quarterly in arrears. If the liquidity facility is called upon, the Authority must repay the advance on the earlier of (i) the date of such Advance or (ii) the Termination Date. Should the Authority fail to repay the advance by the Term Loan Closing Date, the principal amount will convert to a term loan with six equal semi-annual payments. As of the fiscal year ended June 30, 2010, the Authority did not have to call upon the liquidity facility.

For the fiscal year ended June 30, 2010, interest rates on the higher education facilities long-term fixed-rate tax-exempt bonds ranged from a low of 2.00% to a high of 5.50%, and the interest rates on the higher education facilities long-term fixed-rate taxable bonds ranged from a low of 4.00% to a high of 5.66%. By pooling the financing of the capital needs for all public higher education facilities, management believes that economic efficiency is achieved through a single large borrowing administered by one agency. The creditworthiness of both large and small institutions is homogenized into one credit resulting in a lower cost of borrowing and providing a more equitable cost to students and other users who repay the debt through various user fees and charges and student debt service fees.

Higher Education Facilities Programs Debt Ratings. As of the fiscal year ended June 30, 2010, the Authority's higher education facilities program is rated AA, Aa2, and AA by Fitch, Moody's Investors Service and Standard & Poor's Rating Group, respectively.



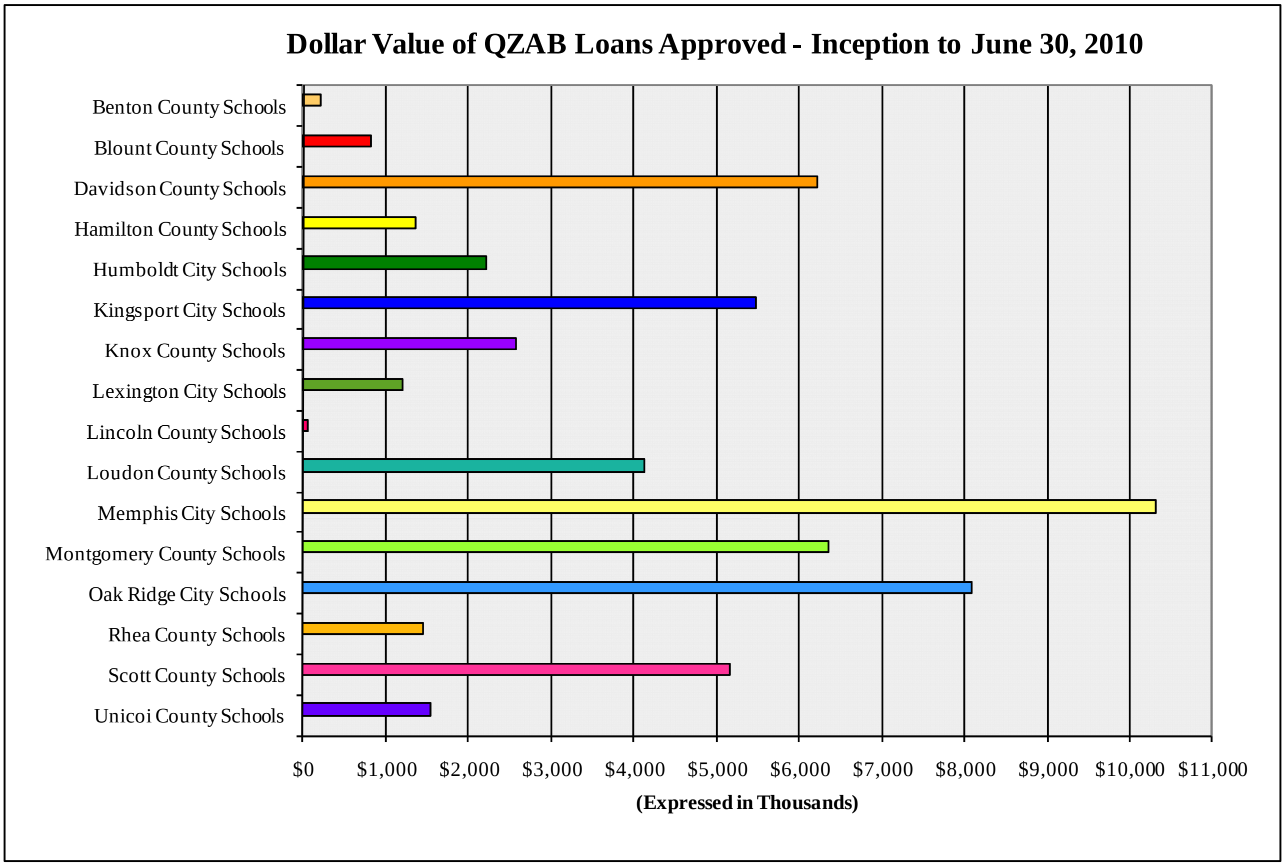




Qualified Zone Academy Bond Program. The QZAB program is a capital financing program authorized by the federal government under the Taxpayer Relief Act of 1997, Section 227(a). A QZAB is a taxable bond issued by the State, the proceeds of which are used to finance certain eligible public schools' renovation projects and equipment purchases. During the time the bond is outstanding, an eligible holder of a QZAB is generally allowed annual federal income tax credits in lieu of receiving periodic interest payments from the issuer. These credits compensate the holder for lending money to the borrower and function as payments of interest on the bonds. The Tennessee Department of Education distributes the application for a QZAB allocation to all local education agencies in the State. The Department recommends those projects that best meet the requirements of the program to the Authority for funding.

The local education agencies and the city or county supporting the agency must provide a general obligation pledge to the Authority for the repayment of its loans. The Authority is authorized to intercept the local community's state-shared taxes, should the local education agency/local government fail to repay its loan timely.

As of June 30, 2010, the QZAB program has unused allocations totaling $75,028,000. Of this amount, $9,547,000 of the 2008 allocation expired on December 31, 2010. The State has up to two years after the yearly allocations are made by the federal government to issue bonds or the allocations will be forfeited.



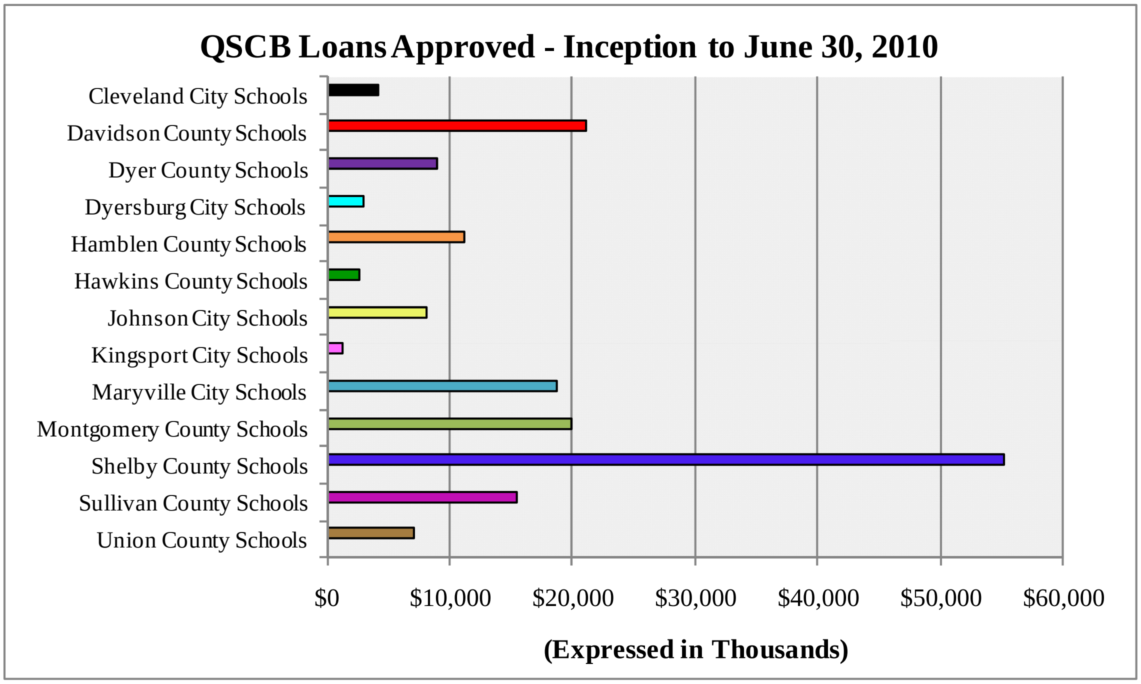
Qualified Zone Academy Bond Program Debt Ratings. All of the QZAB's have been placed with private investors. The QZAB's are not rated.

Qualified School Construction Bond Program. The QSCB program is a capital financing program originally authorized by the federal government under the American Recovery and Reinvestment Act of 2009 and Section 49-3-12, *Tennessee Code Annotated*, as amended. A QSCB is a tax credit bond issued by the State, the proceeds of which are used to finance certain eligible public schools' renovation and rehabilitation projects, equipment purchases, new building construction and land acquisition. An eligible holder of a QSCB is generally allowed quarterly federal income tax credits in addition to quarterly supplemental interest payments from the issuer during the time the bond is outstanding. These credits compensate the holder for lending money to the borrower and function as partial payments of interest on the bonds.

In the fiscal year ended June 30, 2010, the United States Secretary of the Treasury allocated $184.606 million of QSCBs for issuance in the State. Of that allocation, the Authority issued QSCBs totaling $177 million (2010 QSCBs), the proceeds of which were loaned to 13 local government units.

The Authority distributes the applications for a QSCB allocation to all the local education agencies of the State. The Tennessee Advisory Committee on Intergovernmental Relations ("TACIR") recommends those projects that best meet the requirements of the program to the Authority for funding. The city or county supporting the LEA must provide a general obligation pledge to the Authority for the repayment of its loans. The Authority is authorized to intercept the local community's state-shared taxes, should the local government fail to repay its loan timely.

As of June 30, 2010, the QSCB program has unused allocations from the 2009 allocation totaling $7,606,000 and has not yet used the 2010 allocation of $204,836,000. The Authority staff along with the staff of the TACIR encouraged local education authorities, cities and counties to take advantage of these low interest loans.



Qualified School Construction Bonds Program Debt Ratings. As of the fiscal year ended June 30, 2010, the Authority's QSCB program is rated Aa3 and AA by Moody's Investors Service and Standard & Poor's Rating Group, respectively.

<u>Overview of the Financial Statements</u>

The Authority is a discretely presented component unit of the State of Tennessee and uses proprietary fund accounting. The financial statements are prepared in conformity with accounting principles generally accepted in the United States of America using the accrual basis of accounting and the flow of economic resources measurement focus. This basis recognizes revenues when earned and expenses at the time liabilities are incurred. Using the economic resources measurement focus, a reader is presented information that allows him/her to determine the transactions and events that have increased or decreased the total economic resources for the period.

This discussion and analysis is intended to serve as an introduction to the Authority's basic financial statements. The Authority's basic financial statements are comprised of two components: 1) the basic financial statements and 2) notes to the financial statements. The basic financial statements consist of the Statement of Net Assets; Statement of Revenues, Expenses and Changes in Net Assets; and the Statement of Cash Flows.

The Statements of Net Assets depict the Authority's financial position at June 30, 2010, and June 30, 2009. The Statements of Revenues, Expenses and Changes in Net Assets portray the results of operations and the change in net assets for the years presented. The Statements of Cash Flows summarize the sources and uses of cash for the fiscal years presented. These statements are accompanied by notes to the financial statements that provide information that is essential to the reader's understanding of the financial statements. The Authority's basic financial statements are followed by supplementary information containing the financial statement information at the program level.

Financial Analysis of the Authority

Standard indicators of financial success are not applicable to the Authority. The financial goals of the Authority are to provide timely access to the capital markets for qualified educational institutions and local governments on behalf of local education agencies at the lowest possible cost, to repay debt timely and to achieve the highest possible rating for its debt. The Authority achieved these goals under volatile market conditions. During the fiscal year ended June 30, 2010, the Authority frequently entered the short-term market. The Authority was also able to enter the long-term capital market on a timely basis. At no time did the Authority deny approval of a loan application due to its inability to access the capital market. There were no incidents requiring the Authority to withdraw funds from the debt service reserve fund or the commercial paper credit agreement to pay debt service timely. The Authority maintained both its long and short-term credit ratings with all rating agencies.

Statements of Net Assets Summary

(in thousands)

	2010	2009	2008
Current assets	$ 102,776	$ 108,126	$ 74,269
Noncurrent assets	1,298,421	1,042,164	889,627
Total assets	1,401,197	1,150,290	963,896
Current liabilities	74,555	67,672	42,900
Noncurrent liabilities	1,318,598	1,074,527	913,145
Total liabilites	1,393,153	1,142,199	956,045
Net assets (unrestricted)	$ 8,044	$ 8,091	$ 7,851

Note: The Authority owns no capital assets.

At June 30, 2010, current assets include $19,196,131 of unexpended bond proceeds and commercial paper that will fund approved loans as compared to $37,566,295 at June 30, 2009 and $17,800,606 at June 30, 2008. During the fiscal year ended June 30, 2010, the Authority issued $177,000,000 in QSCBs. During the fiscal year ended June 30, 2009, the Authority issued $276,895,000 in Higher Education Facilities Second Program Bonds which were used to retire $225,808,000 of commercial paper proceeds with the remainder to be used to fund various costs of the projects involved. During the fiscal year ended June 30, 2008, the Authority issued $118,530,000 in Higher Education Facilities Second Program Bonds which were used to retire $64,927,000 of commercial paper proceeds with the remainder to fund various costs for the projects involved. Principal payments were made on the outstanding long-term bonds in the amounts of $47,352,000 in 2010; $35,147,000 in 2009; and $30,067,000 in 2008. No QZAB bonds were issued or retired during fiscal year 2010, 2009 or 2008.

Net assets are available to fund ongoing operations and other expenses necessary to meet the goals of the Authority. Assets and liabilities increase in correlation due to the increase in debt issuance and resulting loans and decrease in correlation due to the repayment of debt and loans. Due to the issuance of the 2009 Higher Education Facilities Second Program Bonds, the 2010 QSCBs and the repayment of debt in both years, there was not a significant change in net assets for the years ending June 30, 2010 and June 30, 2009. With interest earned by the Authority on funds placed with the Treasurer in the State Pooled Investment Fund, the Authority continues to absorb certain administrative costs associated with bonded indebtedness of the higher education facilities program rather than passing those costs to the borrowers of the higher education facilities program.

The Authority's operating revenues include revenue from loans in the form of administrative fees, interest on loans, and investment income earned on cash. Operating expenses include interest expense on outstanding bonds and commercial paper, administrative expenses, and the amortization of bond costs of issuance. For the fiscal year ending June 30, 2010, the change in net assets did not significantly vary from that of fiscal year 2009. The total increase in operating revenue for the fiscal year ending 2010 is primarily due to the addition of the QSCB program which increased loans to the borrowers which brought in increased interest revenue; however, it is offset by the increase in total operating expenses which also mainly pertained to the QSCB Program and the increased interest expense. For the fiscal year ending June 30, 2009, the change in net assets did not significantly vary from that of fiscal year 2008. The total increase in operating revenue for the fiscal year ending 2009 was primarily due to the increase in loans to borrowers; however, it was offset by the increase in total operating expenses which mainly pertained to the increase in interest expense which was caused by the interest rate spike for short-term debt during the fall of 2009.

Statements of Revenues, Expenses, and Changes in Net Assets Summary (in thousands)

	2010	2009	2008
Operating Revenues			
Revenue from loans	$ 43,377	$ 38,979	$ 34,991
Investment earnings	386	742	1,356
Total operating revenue	43,763	39,721	36,347
Operating Expenses			
Interest expense	42,114	37,456	33,629
Subsidy to borrowers	291	511	1,183
Other expenses	1,405	1,513	1,242
Total operating expenses	43,810	39,480	36,054
Operating income (loss) and change in net assets	$ (47)	$ 241	$ 293

Note: The Authority has no non-operating revenues or expenses.

For the fiscal year ended June 30, 2010, the Authority elected to return the investment income that it earned on funds held by the Trustee and interest earned on unspent bond proceeds as a subsidy in the form of a credit on debt service to its borrowers in the higher education facilities program.

Pursuant to the bond resolution for the QZABs, Sinking Fund payments are invested in the State Pooled Investment Fund ("SPIF"). SPIF rates for 2010 ranged from 0.21% to 0.57%. Investment earnings related to the QZAB program are held by the Authority for the benefit of the local education agencies participating in the program and credited to their individual debt service sinking fund payment annually. Pursuant to the supplemental bond resolutions for the 2004 and 2005 Series QZABs, sinking fund payments are invested in Forward Delivery Agreements which guarantee a fixed rate of interest of 3.00% and 3.64%, respectively, on investments. The investments are held by the State Treasurer in the Authority's name.

Investment earnings related to the QSCB program are held by the Authority for the benefit of the local governments participating in the program and credited to their individual debt service interest payments monthly. The QSCB program had not received any principal payments as of June 30, 2010.

Future Financing Activities

Higher Education Facilities Programs. As Tennessee enters an economic era that emphasizes the human capital potential of its citizens rather than physical capital and natural resources, the higher education system must be positioned to serve the broader-based need for access to post-secondary education. A host of policy and environmental factors influence both demands for access and the means through which this demand will be met. These factors include:

- Economic conditions of 2008 through 2010 have produced a surge in enrollments in Tennessee. University enrollment increased seven percent from 2008 to 2010, while community college enrollment increased 22 percent in the same time period, the largest increase in more than two decades.
- The demographic composition of the state is changing dramatically and the higher education system must position itself to serve the needs of an increasingly diverse population.
- The advent of the Tennessee Education Lottery Scholarship program allowed more Tennesseans to attend college. In 2009-10, the Tennessee Lottery provided an estimated $284 million in scholarships to more than 98,000 students.

In January 2010, Tennessee passed the Complete College Tennessee Act (CCTA), a comprehensive reform agenda that seeks to transform public higher education through changes in academic, fiscal and administrative policies at the state and institutional level. The primary goal of these reforms is for more Tennesseans to be better educated and trained. At the heart of the CCTA is a new Public Agenda for higher education which establishes the direct link between the state's economic development and its educational system. The overarching goal of the Public agenda is to have Tennessee meet the projected national average in educational attainment by 2025. The primary state policy levers for addressing the state's educational needs are a new funding formula, which incorporates outcomes in lieu of enrollment, a new Performance Funding program, which focuses on quality assurance, and the establishment of institutional mission statements or profiles, which distinguish each institution by degree level, program offerings and student characteristics. Other major components of the reform agenda include more efficient student transfer, a more integrated community college system, reforms to the delivery of student remediation programs and an enhanced research focus for the University of Tennessee Knoxville and the University of Memphis, the state's two public Carnegie Research institutions.

In the Knowledge Economy, the importance of receiving training beyond high school is significant. In 2008, 24.5 percent of Tennessee's working-age adults held a college degree, compared to the national average of 29.5 percent. To reach the national average educational attainment levels, Tennessee would need an additional 170,000 citizens with a bachelor's degree or higher, more than double the current annual degree production of the state's public and private institutions. Furthermore, the percentage of adults in the state with an associate's degree or some college in 2008 was 31.3 percent, in comparison with the national average of 37.9 percent. To reach the national average, Tennessee would need an additional 220,000 citizens with an associate's degree or higher. The availability of new and/or improved learning facilities near work and home will have a major impact on the State's success in achieving these goals.

The increased enrollment and continued demand for advanced education and training will put stress on the capital facilities at all campuses. As a result, the State anticipates an increased need for funding of various facilities through the Authority.

Qualified School Construction Bond Program. QSCBs are tax credit bonds that were authorized in the American Recovery and Reinvestment Act of 2009 and Section 49-3-12, *Tennessee Code Annotated*, as amended. The Authority was allocated by the Federal Government $119.131 million in the 2010 allocations. Three local education agencies which included Nashville-Davidson County School District, Knox County School District, and Memphis City School District received a direct allocation for a combined total of $85.705 million. The local education agencies reallocated to the Authority their direct allocations to be issued on their behalf by the Authority. With the combination of the State allocation, the local education agencies' direct allocations and the $7.606 million remaining from the 2009 allocation, the Authority issued QSCBs in October 2010 in the amount of $212.44 million to provide loans to fifteen borrowers. The QSCB program is a limited program and was only intended to provide funding for fiscal years 2009 and 2010. The QSCB program was not extended beyond December 31, 2010.

Contacting the Authority's Management Team

This discussion and analysis is designed to provide our citizens, education agencies, investors and creditors with a general overview of the Authority's finances and to demonstrate its accountability for the monies it receives. If you have questions about this report or need additional financial information, contact the Director of State and Local Finance, State of Tennessee, Suite 1600, James K. Polk Center, 505 Deaderick St., Nashville, Tennessee 37243-1402, or visit our website at http://tn.gov/comptroller/sl/.

Exhibit A

TENNESSEE STATE SCHOOL BOND AUTHORITY
STATEMENTS OF NET ASSETS
JUNE 30, 2010, AND JUNE 30, 2009

(Expressed in Thousands)

	June 30, 2010	June 30, 2009
ASSETS		
Current assets:		
Cash (Note 2)	$ 39,325	$ 46,437
Cash with fiscal agent (Note 2)	357	957
Investments with fiscal agent (Note 2)	14	14
Deferred outflow - derivatives (Notes 1 and 2)	1,613	2,686
Prepaid interest expense	-	24
Loans receivable (Note 3)	54,475	50,807
Interest receivable (Note 3)	6,527	6,621
Receivables for administrative fees (Note 3)	465	580
Total current assets	102,776	108,126
Noncurrent assets:		
Restricted cash (Notes 2 and 4)	183,061	15,391
Restricted investments (Notes 2 and 4)	36,897	38,167
Loans receivable (Note 3)	1,068,456	979,585
Deferred charges	10,007	9,021
Total noncurrent assets	1,298,421	1,042,164
Total assets	1,401,197	1,150,290
LIABILITIES		
Current liabilities:		
Accounts payable	11,603	9,324
Accrued liabilities	10,847	-
Fair Value of derivatives (Notes 1 and 2)	1,613	2,686
Due to primary government	7	-
Accrued interest payable	6,607	6,768
Unearned revenue (Note 6)	1,955	1,693
Bonds payable (Note 5)	41,923	47,201
Total current liabilities	74,555	67,672
Noncurrent liabilities:		
Unearned revenue (Note 6)	3,735	1,965
Commercial paper payable (Note 5)	281,782	174,300
Bonds payable (Note 5)	1,033,081	898,262
Total noncurrent liabilities	1,318,598	1,074,527
Total liabilities	1,393,153	1,142,199
NET ASSETS		
Unrestricted	$ 8,044	$ 8,091

The notes to the financial statements are an integral part of this statement.

Exhibit B

TENNESSEE STATE SCHOOL BOND AUTHORITY
STATEMENTS OF REVENUES, EXPENSES, AND
CHANGES IN NET ASSETS
FOR THE YEARS ENDED JUNE 30, 2010, AND JUNE 30, 2009

(Expressed in Thousands)

	Year Ended June 30, 2010	Year Ended June 30, 2009
OPERATING REVENUES		
Revenue from loans	$ 43,377	$ 38,979
Investment earnings	386	742
Total operating revenues	43,763	39,721
OPERATING EXPENSES		
Interest expense-commercial paper	757	3,457
Interest expense-bonds	41,357	33,999
Subsidy to borrowers	291	511
Administrative expense	773	970
Amortization of bond issuance costs	632	543
Total operating expenses	43,810	39,480
Operating income (loss) and change in net assets	(47)	241
Net assets, July 1	8,091	7,850
Net assets, June 30	$ 8,044	$ 8,091

The notes to the financial statements are an integral part of this statement.

Exhibit C

TENNESSEE STATE SCHOOL BOND AUTHORITY
STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED JUNE 30, 2010, AND JUNE 30, 2009

(Expressed in Thousands)

	Year Ended June 30, 2010	Year Ended June 30, 2009
CASH FLOWS FROM OPERATING ACTIVITIES		
Receipts from borrowers for administrative fees	$ 629	$ 373
Payment to suppliers	(762)	(832)
Receipts from borrowers to the interest rate reserve fund	573	757
Payments to borrowers from the interest rate reserve fund	(394)	(616)
Net cash provided by (used in) operating activities	46	(318)
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES		
Proceeds from sale of bonds	177,000	282,737
Proceeds from sale of commercial paper	110,000	163,000
Bond issuance costs paid	(1,614)	(498)
Principal paid - bonds and commercial paper	(49,870)	(267,076)
Interest paid - bonds and commercial paper	(42,533)	(36,090)
Subsidy to borrowers	(438)	(511)
Net cash provided by noncapital financing activities	192,545	141,562
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchases of investments	(17,593)	(46,246)
Proceeds from sales and maturities of investments	18,720	19,256
Interest received on investments	1,159	923
Loans issued	(125,633)	(177,264)
Loan escrow paid	(130)	2,306
Collections of loan principal	47,924	43,455
Interest received on loans	43,113	35,719
Refund to borrowers	(193)	-
Net cash used in investing activities	(32,633)	(121,851)
Net increase (decrease) in cash	159,958	19,393
Cash, July 1	62,785	43,392
Cash, June 30	$ 222,743	$ 62,785

(Continued on next page)

TENNESSEE STATE SCHOOL BOND AUTHORITY
STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED JUNE 30, 2010, AND JUNE 30, 2009

(Expressed in Thousands)

	2010	2009
Reconciliation of cash to the Statement of Net Assets:		
Cash	$ 39,325	$ 46,437
Cash with fiscal agent	357	957
Restricted cash	183,061	15,391
Cash, June 30	$ 222,743	$ 62,785
Reconciliation of operating income (loss) to net cash provided by (used in) operating activities:		
Operating income (loss)	$ (47)	$ 241
Adjustments to reconcile operating income (loss) to net cash provided by (used in) operating activities:		
Amortization of bond issuance costs	631	543
Investment earnings	(386)	(733)
Interest expense	42,114	37,456
Subsidy to borrowers	291	511
Interest income (loss) from loans	(42,459)	(38,555)
Changes in assets and liabilities:		
(Increase) decrease in receivables for administrative fees	(114)	213
(Increase) decrease in payables for administrative fees	(4)	(24)
Increase (decrease) in due to primary government	7	-
Increase (decrease) in unearned revenue	13	30
Total adjustments	93	(559)
Net cash provided by (used in) operating activities	$ 46	$ (318)
Noncash financing activities:		
Accretion of capital appreciation bonds	$ 151	$ 322
Bond issuance costs	1,614	(5,481)
Total noncash financing activities	$ 1,765	$ (5,159)
Noncash investing activities:		
Increase (decrease) in fair value of investments	$ (217)	$ (52)

The notes to the financial statements are an integral part of this statement.

Tennessee State School Bond Authority
Notes to the Financial Statements
June 30, 2010, and June 30, 2009

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Reporting Entity

The Tennessee State School Bond Authority (the Authority) was created to provide a mechanism for financing capital projects for the state's higher education institutions. During 1999, the General Assembly empowered the Authority to issue Qualified Zone Academy Bonds (QZABs) for local governments to borrow for financing improvement projects on behalf of local education agencies pursuant to the federal program authorized in the Taxpayer Relief Act of 1997. In addition, under the American Recovery and Reinvestment Act of 2009, the Authority was authorized to issue Qualified School Construction Bonds (QSCBs) for local governments to borrow on behalf of local education agencies at nominal or zero percent interest for financing renovation and rehabilitation projects, equipment purchases, new building construction and land acquisition.

The Authority is a component unit of the State of Tennessee (the State) and a separate legal entity. In accordance with the Governmental Accounting Standards Board's (GASB) Statement No. 14, *The Financial Reporting Entity*, the Authority is discretely presented in the *Tennessee Comprehensive Annual Financial Report* because the Authority's board consists of state officials which include the Governor, the State Treasurer, the Secretary of State, the Commissioner of Finance and Administration, the Comptroller of the Treasury, the Chancellor of the Tennessee Board of Regents, and the President of the University of Tennessee. The Governor serves as chairman, and the Comptroller of the Treasury serves as secretary. The Director of the Division of State and Local Finance serves as the assistant secretary; the division provides administrative and financial services to the Authority. Therefore, the State has the ability to affect the day-to-day operations of the Authority.

Basis of Presentation

The accompanying financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America as prescribed by the Governmental Accounting Standards Board. Private-sector standards of accounting and financial reporting issued prior to December 1, 1989, generally are followed in the financial statements to the extent that those standards do not conflict with or contradict guidance of the Governmental Accounting Standards Board. The Authority has the option of following subsequent private-sector guidance subject to this same limitation. The Authority has elected not to follow subsequent private-sector guidance.

Measurement Focus and Basis of Accounting

The accompanying financial statements have been prepared using the accrual basis of accounting and the flow of economic resources measurement focus. Under this basis, revenues are recorded when earned and expenses are recorded at the time liabilities are incurred.

The Tennessee State School Bond Authority distinguishes operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and producing and delivering services in connection with principal ongoing operations. The Authority's principal ongoing operation is to provide loans for constructing capital projects, renovating and rehabilitating facilities, acquiring land and acquiring equipment to higher educational facilities and to local government units pursuant to the criteria set by the federal government for the QZAB and QSCB programs. Therefore, the Authority also recognizes income on investments as operating revenue. The Authority's operating expenses include interest paid on borrowings, subsidies to borrowers, bond issuance costs, arbitrage, and administrative expenses. Any revenues and expenses not meeting this definition would be reported as nonoperating revenues and expenses.

Investments

Investments are stated at fair value.

Amortized Amounts

A. Bond Issuance Costs. The Authority amortizes bond issuance costs using the straight-line method over the life of the bonds. Unamortized bond issuance costs are reported as deferred charges.

B. Bond Discounts, Premiums, and Deferred Amount on Refundings. The Authority amortizes bond discounts and premiums using the straight-line method over the life of the bonds. The deferred amount on refundings is amortized using the straight-line method over the remaining life of the old debt or the life of the new debt, whichever is shorter. Bonds payable are reported net of the applicable unamortized bond discount or premium and the unamortized deferred amount on refundings.

   Amortization of bond discount, premium, and deferred amount on refundings is reported with bond interest expense in the financial statements.

C. Accretion. The difference between the face amount of College Saver Bonds (capital appreciation bonds) and the public offering price is not treated as bond discount. Capital appreciation bonds are subject to redemption at prices which increase from the initial public offering price to the face amount. The carrying amount of these bonds is adjusted semi-annually and at June 30 to reflect the increased liability, with a corresponding charge to interest expense.

D. Unearned Revenue. When the Authority issues bonds to finance capital projects, the par amount of the bonds is adjusted by certain amounts (such as bond discount/premium, underwriters' fees, and other costs of issuance) in order to arrive at the amount of bond proceeds available for capital expenditures. These amounts, discussed above, are capitalized and amortized pursuant to accounting principles generally accepted in the United States of America. A similar situation arises when accounting for the loans to the higher education institutions and local governments. Because of the adjustments mentioned above (discount, costs of issuance, etc.), the principal amount of the loan differs from the actual amount of funds available for capital expenditures. Because the higher education institutions and the local governments bear the cost of this difference, it is carried on the statement of net assets as unearned revenue and amortized on a straight-line basis over the life of the related bond.

   The Authority requires the higher education institutions to contribute funds to the Interest Rate Reserve Fund based on the amount of outstanding commercial paper. The principal of the Interest Rate Reserve Fund is credited back to the institution as commercial paper is redeemed. The Interest Rate Reserve Fund is reported on the statement of net assets as unearned revenue and is not amortized.

Change in Accounting Principle

Effective July 1, 2009, the Authority adopted Statement Number 53 of the Governmental Accounting Standards Board, *Accounting and Financial Reporting for Derivative Instruments*. GASB Statement Number 53 requires that derivative instruments be reported at fair value on the statement of net assets. The classification of derivative instruments depends on whether they represent assets or liabilities. Totals on the statement of net assets for June 30, 2009, have been restated for comparative purposes. There is no effect on net assets or on investment earnings resulting from the restatement.

NOTE 2. DEPOSITS AND INVESTMENTS

The investments under the Higher Education First Program General Bond Resolution of the Tennessee State School Bond Authority can be invested in direct obligations of the United States, or obligations of which the principal and interest are guaranteed by the United States. Moneys pertaining to the Higher Education Second Program General Bond Resolution, the Qualified Zone Academy Bonds First Program Resolution and the Qualified School Construction Bonds General Bond Resolution of the Tennessee State School Bond Authority, pursuant to *Tennessee Code Annotated*, Section 49-3-1205, can be invested, pursuant to each Bond Resolution listed above, in obligations of the United States or its agencies under flexible repurchase agreements which are fully collateralized by obligations of the United States or obligations the timely payment of the principal of and interest on which are guaranteed by the United States, the State's pooled investment fund as provided in *Tennessee Code Annotated*, Section 9-4-603, and any other investment authorized by the state investment policy adopted by the State Funding Board pursuant to *Tennessee Code Annotated*, Section 9-4-602.

Deposits

The Tennessee State School Bond Authority has cash on deposit in the State Pooled Investment Fund and Local Government Investment Pool administered by the State Treasurer. The funds' investment policy and required risk disclosures are presented in the *State of Tennessee's Treasurer's Report.* That report is available on the State's website at http://www.tn.gov/treasury or by calling (615) 741-2956.

The Authority's deposits are held in a financial institution, which participates in the bank collateral pool administered by the State Treasurer. The securities pledged to protect these accounts are pledged in the aggregate rather than against each individual account. The members of the pool may be required by agreement to pay an assessment to cover any deficiency. Under this additional assessment agreement, public fund accounts covered by the pool are considered to be insured for purposes of credit risk disclosure.

Investments

As of June 30, 2010, the Authority has the following investments:

Investment	Maturity	Fair Value
U.S. Treasury Bills	October 28, 2010	$24,544,925
	November 18, 2010	3,411,542
	December 2, 2010	3,920,939
U.S. Treasury Securities:		
State and Local Government Series		5,033,477
Total Investments		$36,910,883

As of June 30, 2010, the Tennessee State School Bond Authority holds two separate State and Local Government Series U.S. Treasury Securities. One security covers the debt of the QZAB borrower's remaining loan balance of $4,419,476, and the other security covers the remaining loan balance of $614,001 of the Higher Education borrower's debt.

As of June 30, 2009, the Authority had the following investments:

Investment	Maturity	Fair Value
U.S. Treasury Bills	October 29, 2009	$27,469,941
	November 19, 2009	2,687,310
	December 3, 2009	2,886,619
U.S. Treasury Securities:		
State and Local Government Series		5,137,888
Total Investments		$38,181,758

As of June 30, 2009, the Tennessee State School Bond Authority held two separate State and Local Government Series U.S. Treasury Securities. One security covered the debt of the QZAB borrower's remaining loan balance of $4,419,476, and the other security covered the remaining loan balance of $718,412 of the Higher Education borrower's debt.

Interest Rate Risk

Interest rate risk is the risk that future changes in prevailing market rates of interest will have an adverse effect on the fair value of debt investments. The Authority does not have a formal investment policy that limits investment maturities as a means of managing its exposure to interest rate risk.

Credit Risk

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. At June 30, 2010, and June 30, 2009, the Authority's investments were in U.S. Government obligations which are not considered to have credit risk.

Custodial Credit Risk

For an investment, custodial credit risk is the risk that, in the event of the failure of a counterparty, the Authority will not be able to recover the value of investment or collateral securities that are in the possession of an outside party. The Authority's investment securities are exposed to custodial credit risk if they are uninsured, are not registered in the name of the Authority and are held by either the counterparty or the counterparty's trust department or agent but not in the Authority's name. At June 30, 2010, and June 30, 2009, the Authority's investments were registered in the name of the Authority.

Concentration of Credit Risk

A concentration of investments in any one single issuer of debt securities presents a greater risk for loss in the event that the issuer fails on its obligations. At June 30, 2010, and June 30, 2009, the Authority's investments were in U.S. Treasury securities.

Forward Delivery Agreements

On November 24, 2004, the Authority entered into a Forward Delivery Agreement (the "Agreement") with Bank of America, N.A. related to the series 2004 QZAB Bonds. The Agreement guarantees to the Authority a fixed rate of interest of 3%. Cash from borrowers' loan repayments will be used to purchase securities from Bank of America, N.A. in accordance with the Agreement. The accumulated funds will be used to redeem the $12,600,000 series 2004 QZAB Bonds at maturity. As a result of the Agreement, borrowers will repay only $9,984,800 of the $12,600,000 principal. The investments will be held by the State Treasurer in the Authority's name. As of June 30, 2010, there is $3,411,542 invested through the Agreement. As of June 30, 2009, there was $2,687,310 invested through the Agreement. The Authority negotiated a "one way" termination provision in the event of counterparty default on the Agreement. The Authority also has the right to optionally terminate the Agreement at any time.

On December 28, 2005, the Authority entered into a Forward Delivery Agreement (the "Agreement") with J.P. Morgan Chase Bank, N.A. related to the series 2005 QZAB Bonds. The Agreement guarantees to the Authority a fixed rate of interest of 3.64%. Cash from borrowers' loan repayments will be used to purchase securities from J.P. Morgan Chase Bank, N.A. in accordance with the Agreement. The accumulated funds will be used to redeem the $17,545,000 series 2005 QZAB Bonds at maturity. As a result of the Agreement, borrowers will repay only $13,438,510 of the $17,545,000 principal. The investments will be held by the State Treasurer in the Authority's name. As of June 30, 2010, there is $3,920,939 invested through the Agreement. As of June 30, 2009, there was $2,886,619 invested through the Agreement. The Authority negotiated a "one way" termination provision in the event of counterparty default on the Agreement. The Authority also has the right to optionally terminate the Agreement at any time.

Terms of the Forward Delivery Agreements

	QZAB Series 2004	QZAB Series 2005
Trade Date	11/24/2004	12/28/2005
Provider	Bank of America, N.A	J.P Morgan Chase Bank, N.A.
Notional Amount	$12,600,000	$17,545,000
Guaranteed Interest Rate	3.00%	3.64%
Amount Invested in Agreement at 6/30/10 at fair value	$3,411,542	$3,920,939
Amount Invested in Agreement at 6/30/09 at fair value	$2,687,310	$2,886,619
Date of Deposits	Nov. 24, 2005 through 2020	Dec. 8, 2006 through 2020

For the fiscal year ended June 30, 2010, the Forward Delivery Agreement for the 2004 QZAB bonds has a negative fair value of ($715,213) and the Forward Delivery Agreement for the 2005 QZAB bonds has a negative fair value of ($897,463). For the fiscal year ended June 30, 2009, the Forward Delivery Agreement for the 2004 QZAB bonds had a negative fair value of ($1,356,562) and the Forward Delivery Agreement for the 2005 QZAB bonds had a negative fair value of ($1,329,638). The Authority did not enter into these agreements as interest rate hedges. These negative fair values are reported as liabilities on the statement of net assets. The agreements were valued by an independent investment advisor using the parameters contained in the Forward Delivery Agreements and prevailing market conditions and benchmark yields on June 30, 2010, upon which the fair values depend. Borrowers pay no interest on these bonds. The interest rate credit is established by the federal government. The Forward Delivery Agreements are agreed to as one of the terms of purchase to induce the investor to purchase the bond. The Authority has a scheduled amount of Qualified Securities required to be on deposit on specified delivery dates. These Forward Delivery Agreements are forward contracts, or commitments to deliver the same Qualified Securities on the scheduled dates at a pre-determined rate. Therefore, these are hedging derivative instruments employed as a fair value hedge of the Qualified Securities for the required deposits. These forward contracts meet all criteria under GASB 53 Paragraph 39 that addresses the consistent critical terms method for forward contracts. All terms of the required deposits and the Forward Delivery Agreements are consistent, therefore hedge accounting is applied.

Termination Risk

Termination risk is the risk that a counterparty will terminate a Forward Delivery Agreement at a time when the State owes it a termination payment. The State has mitigated this risk by specifying that the counterparty has the right to terminate only as a result of the following events: the failure by the State, for any reason, to purchase Qualified Securities in accordance with the Agreement; the amount to purchase Qualified Securities on the Delivery date is less than the Scheduled Fund Amount; the State is not in compliance with any covenant or obligation, incorporated by reference in, this Agreement; any representation or warranty of the State contained in the Agreement proves to have been incorrect, false or misleading; insolvency of the State; or the principal amount under the Bonds becomes due and payable for any reason prior to the maturity date.

If the current market interest rate is higher than the fixed interest rate agreed to in the Forward Delivery Agreement, the Forward Delivery Agreement has a negative fair value. In the event of termination under this circumstance, the State owes a termination payment to the counterparty. If the fair value is positive, the State is due a termination payment from the counterparty. As of June 30, 2010, the fair value of the State's Forward Delivery Agreements is a total negative value of ($1,612,676). As of June 30, 2009, the fair value of the State's Forward Delivery Agreements was a total negative value of ($2,686,200). Therefore, if the Agreement was terminated, for any reason, the State would owe a termination payment of this amount.

NOTE 3. LOANS RECEIVABLE

Higher Education Facilities Programs

The Authority has entered into financing agreements with both the Board of Trustees of the University of Tennessee (the Board of Trustees) and the Tennessee Board of Regents of the State University and Community College System of the State of Tennessee (the Tennessee Board of Regents). The First Financing Agreement and the Second Financing Agreement (the "Agreements"), are dated May 1, 1967, and November 1, 1997, respectively, as amended. Under the Agreements, the Authority agrees to finance construction projects for the Board of Trustees or the Tennessee Board of Regents. Annual financing charges payable under the Agreements must be sufficient to pay the debt obligations of the Authority and the costs of administering the programs.

Qualified Zone Academy Bonds Program

The Authority has entered into loan agreements with the local governments on behalf of local education agencies for the 1999 QZABs, dated November 30, 1999; the 2001 QZABs dated December 18, 2001; the 2003 QZABs dated December 23, 2003; the 2004 QZABs dated November 24, 2004; and the 2005 QZABs dated December 28, 2005. Under the agreements, the Authority agrees to finance renovation projects and equipment for the local education agencies. On the date designated in the agreements, annual financing charges must be paid by the borrower sufficient to pay the annual principal payment, which is deposited into a bond sinking fund held by the State Treasurer that will pay the bonds at maturity, and the costs of administering the program.

Qualified School Construction Bonds Program

The Authority has entered into loan agreements with the local governments on behalf of local education agencies for the 2009 QSCBs, dated December 1, 2009. Under the agreements, the Authority agrees to finance renovation and rehabilitation projects, equipment purchases, new building construction and land acquisition for the local education agencies. On the date designated in the agreements, monthly financing charges must be paid by the borrower sufficient to pay the monthly principal payment, which is deposited into a bond sinking fund held by the State Treasurer that will pay the bonds at maturity, and the costs of administering the program.

NOTE 4. RESTRICTED ASSETS

Cash and Investments

The General Higher Education Facilities Bond Resolution (the First Program) requires that an amount equal to the maximum annual debt service requirement be placed in a debt service reserve account with the trustee. The first general bond resolution is effective for all bonds issued prior to 1998.

The Higher Education Facilities Second Program General Bond Resolution, effective for all bonds issued in 1998 and thereafter, permits the Authority to satisfy the debt service reserve requirement by either placing an amount equal to the maximum semiannual debt service requirement in a debt service reserve account or by maintaining a Reserve Fund Credit Facility. The Authority obtained a surety bond, constituting a Reserve Fund Credit Facility under the Resolution, in lieu of maintaining a debt service reserve fund for the 1998 Series A, B, C, and D; 2000 Series A and B; 2002 Series A; 2004 Series A, B, and C; 2005 Series A and B; 2006 Series A and B; 2007 Series A, B and C; and 2008 Series A Bonds. Due to market conditions at the time of issuance of the 2008 Series B and 2009 Series A Bonds, the Authority deposited funds into a debt service reserve account equal to the maximum semiannual debt service for those bonds.

The first program bond resolution of the QZABs requires the establishment of a special trust fund, the bond sinking fund account. This account represents the funds set aside to redeem the QZABs at maturity.

The first program bond resolution of the QSCBs requires the establishment of a special trust fund, the bond sinking fund account. This account represents the funds set aside to redeem the QSCBs at maturity.

NOTE 5. DEBT PAYABLE

The State of Tennessee shall not be liable on the bonds issued by the Authority and the bonds shall not be a debt of the State of Tennessee.

Higher Education Facilities Programs

A. Bonds. The bonds issued under the First and Second Program Higher Education Facilities Bond Resolutions constitute special obligations of the Authority. The First Program, which commenced in 1967, is no longer utilized, but any payments by the Boards thereunder will be superior to the Boards' payments under the Second Program Higher Education Facilities Bond Resolution. The principal, Sinking Fund Installments, if any, and Redemption Price of and interest on the bonds are payable solely from the Annual Financing Charges, Legislative Appropriations, and other moneys and securities held or set aside under the Resolutions.

B. Commercial Paper. Commercial paper constitutes a special obligation of the Authority. Principal of and interest on the commercial paper is payable from the following sources: (i) as to principal only, the proceeds of the sale of commercial paper issued to pay the principal of other outstanding commercial paper, (ii) the proceeds of draws on the Liquidity Facility, (iii) available revenues, (iv) the moneys and securities (if any) on deposit in the Reimbursement Fund and in the Debt Service Fund, (v) the moneys and securities (if any) on deposit in the Project Construction Account for such projects, and (vi) the proceeds of bonds or notes issued to make such payments.

Qualified Zone Academy Bonds Program

On September 9, 1999, the Authority adopted a Qualified Zone Academy Bond Resolution authorizing the issuance of Qualified Zone Academy Bonds to make loans to local governments on behalf of local education agencies for the purpose of financing eligible costs of certain projects. The State Department of Education recommends the projects to the Authority that should be funded under the QZAB program. The Taxpayer Relief Act of 1997 provided this financial tool whereby interest on QZABs is paid by the federal government in the form of an annual tax credit to the financial institutions that hold the QZABs. The bonds are secured solely by the payments made by the borrowers under the Loan Agreements, including amounts collected from unobligated state-shared taxes in the event of non-payment by the local governments and by certain funds held under the Qualified Zone Academy Bond Resolution.

Qualified School Construction Bonds Program

On November 5, 2009, the Authority adopted a Qualified School Construction Bond Resolution authorizing the issuance of Qualified School Construction Bonds to make loans to local governments on behalf of local education agencies for the purpose of financing eligible costs of certain projects. The Tennessee Advisory Commission on Intergovernmental Relations (TACIR) recommends the projects to be funded by the Authority under the QSCB program. The American Recovery and Reinvestment Act of 2009 provided this financial tool whereby interest on QSCBs is paid by the federal government in the form of a quarterly tax credit to the financial institutions that hold the QSCBs. Market conditions at the time of issuance demanded the borrowers pay an additional quarterly interest payment to supplement the tax credit to the investors. The bonds are secured solely by the payments made by the borrowers under the Loan Agreements, including amounts collected from unobligated state-shared taxes in the event of non-payment by the local governments and by certain funds held under the Qualified School Construction Bond Resolution.

Changes in debt payable for the year ended June 30, 2010, and 2009 are as follows (expressed in thousands):

	Balance July 1, 2009	Additions	Deletions	Balance June 30, 2010	Amounts Due Within One Year
Commercial paper	$ 174,300	$ 110,000	$ 2,518	$ 281,782	$ -
Bonds payable	$ 938,948	$ 177,152	$ 47,352	$ 1,068,748	$ 41,923
Less: unamortized bond discount	(426)	-	(63)	(363)	-
Add: unamortized bond premium	26,343	-	1,358	24,985	-
Less: unamortized deferred amount on refundings	(19,403)	-	(1,037)	(18,366)	-
Total bonds payable	$ 945,462	$ 177,152	$ 47,610	$ 1,075,004	$ 41,923

	Balance July 1, 2008	Additions	Deletions	Balance June 30, 2009	Amounts Due Within One Year
Commercial paper	$ 243,229	$ 163,000	$ 231,929	$ 174,300	$ -
Bonds payable	$ 696,878	$ 277,217	$ 35,147	$ 938,948	$ 47,201
Less: unamortized bond discount	(491)	-	(65)	(426)	-
Add: unamortized bond premium	20,393	7,156	1,206	26,343	-
Less: unamortized deferred amount on refundings	(20,440)	-	(1,037)	(19,403)	-
Total bonds payable	$ 696,340	$ 284,373	$ 35,251	$ 945,462	$ 47,201

Additions to bonds payable include accretion of interest in the amount of $151,368 in 2010 and $322,432 in 2009.

Bonds and commercial paper payable at June 30, 2010, and June 30, 2009, are as follows (expressed in thousands):

	June 30, 2010	June 30, 2009
Bonds Payable:		
1976 Series B at an interest rate of 3.0% maturing to 2011 (original par - $6,037)	$ 183	$ 360
1989 College Saver Bonds with a yield of 6.9% maturing to 2010 (at accreted value); (original principal - $21,935)	0	2,608
1998 Refunding Series D at interest rates from 4.45% to 4.85% maturing to 2021 (original par - $33,540)	15,695	16,940
2000 Series A at interest rates from 4.700% to 5.125% maturing to 2010 (original par - $70,680)	0	2,250

2000 Series B (Federally Taxable) at an interest rate of 7.15% maturing to 2010 (original par - $33,730)	0	2,820
2002 Series A at an interest rate of 5.00% maturing to 2012 (original par - $119,135); see additional disclosures regarding the 2007 advance refunding	9,220	13,490
2004 Series A at interest rates from 4.00% to 4.50% maturing to 2026 (original par - $67,965)	54,305	57,615
2004 Series B at interest rates from 4.00% to 4.50% maturing to 2034 (original par - $60,575)	48,995	51,085
2004 Series C (Federally Taxable) at interest rates from 4.00% to 5.50% maturing to 2034 (original par - $37,230)	31,630	32,800
2005 Series A at interest rates from 3.375% to 5.00% maturing to 2030 (original par - $100,540)	93,570	97,115
2005 Series B (Federally Taxable) at interest rates from 4.19% to 4.88% maturing to 2028 (original par - $30,960)	30,410	30,960
2006 Series A at interest rates from 4.00% to 4.60% maturing to 2036 (original par - $53,820)	46,455	48,310
2006 Series B at an interest rate of 4.00% maturing to 2011 (original par - $12,485)	580	3,640
2007 Series A at interest rates from 4.00% to 5.00% maturing to 2036 (original par - $33,730)	29,965	31,040

2007 Series B (Federally Taxable) at interest rates from 5.243% to 5.666% maturing to 2036 (original par - $14,040)	12,155	12,700
2007 Series C at interest rates from 4.00% to 5.00% maturing to 2032 (original par - $89,940)	85,740	87,195
2008 Series A at interest rates from 3.25% to 5.00% maturing to 2037 (original par - $118,530)	112,130	115,185
2008 Series B at interest rates from 3.50% to 5.50% maturing to 2038 (original par - $166,990)	161,225	165,720
2009 Series A at interest rates from 2.00% to 5.00% maturing to 2039 (original par - $109,905)	102,280	109,905
1999 Qualified Zone Academy Bonds non-interest bearing maturing in 2011 (original par - $13,290)	13,290	13,290
2001 Qualified Zone Academy Bonds non-interest bearing maturing in 2015 (original par - $11,330)	11,330	11,330
2003 Qualified Zone Academy Bonds non-interest bearing maturing in 2018 (original par - $2,445)	2,445	2,445
2004 Qualified Zone Academy Bonds non-interest bearing maturing in 2020 (original par - $12,600)	12,600	12,600

2005 Qualified Zone Academy Bonds non-interest bearing maturing in 2020 (original par - $17,545)	17,545	17,545
2009 Qualified School Construction Bonds at an interest rate of 1.515% and a federal tax credit rate of 5.86% maturing in 2026 (original par - $177,000)	177,000	0
Total Par Amount of Bonds Payable	1,068,748	938,948
Plus Unamortized Premium/Less Unamortized Discount	24,622	25,917
Bonds Payable Net of Unamortized Premium/ Discount	1,093,370	964,865
Less: Deferred Amount on Refundings	(18,366)	(19,403)
Net Bonds Payable	$ 1,075,004	$ 945,462
Commercial paper, at interest rates from 0.15% to 0.55%	$ 281,782	$ 174,300

Debt service requirements to maturity of the bonds payable at June 30, 2010, are as follows (expressed in thousands):

For the Year(s) Ending June 30	Principal	Interest	Total
2011	$ 56,518	$ 37,074	$ 93,592
2012	42,578	35,488	78,066
2013	42,253	33,929	76,182
2014	43,538	32,069	75,607
2015	50,353	30,331	80,684
2016-2020	235,588	125,944	361,532
2021-2025	199,426	79,836	279,262
2026-2030	322,646	38,793	361,439
2031-2035	73,750	14,460	88,210
2036-2039	26,720	1,948	28,668
	$ 1,093,370	$ 429,872	$ 1,523,242

The above principal for bonds is more than that presented on the accompanying financial statements by $18.366 million, representing the deferred amount on bond refundings. This amount is deducted from bonds payable in the accompanying financial statements but is included in the debt service schedule above.

The Authority may issue taxable and/or tax-exempt bonds. Proceeds for the tax-exempt bonds issued after September 1, 1986, are subject to the 1986 Tax Reform Act. The Authority invests, records, and reports these proceeds in the manner set forth by the U.S. Treasury and Internal Revenue Service to maintain the tax-exempt status of the bonds. Arbitrage liabilities, when applicable, are reported as a current accrued liability. For the year ended June 30, 2010 and June 30, 2009, the Authority did not have a liability for arbitrage.

On December 17, 2009, the Authority issued the 2009 Qualified School Construction Bonds (“2009 QSCB”). The 2009 QSCB proceeds in the amount of $177,000,000 were issued for the purposes of financing various qualifying QSCB projects and to pay the costs of issuance of the 2009 QSCBs.

On April 15, 2009, the Authority issued the 2009 Series A Bonds. The 2009 Series A tax-exempt bond proceeds in the amount of $109,905,000 were issued to redeem $82,035,000 of the Authority’s tax-exempt commercial paper and $4,595,000 of the Authority’s taxable commercial paper. The balance of the proceeds of the 2009 Series A was used to pay for new construction projects, various costs of issuance and to fund the debt service reserve fund.

On December 17, 2008 the Authority issued the 2008 Series B Bonds. The 2008 Series B tax-exempt bond proceeds in the amount of $166,990,000 were issued to redeem $139,178,000 of the Authority’s tax-exempt commercial paper. The balance of the proceeds of the 2008 Series B was used to pay for new construction projects, various costs of issuance and to fund the debt service reserve fund.

Prior-Year Defeasance of Debt

In prior years, certain Authority bonds were defeased by placing the proceeds of new bonds in irrevocable trusts to provide for all future debt service on the old bonds. Accordingly, the trust account assets and the liability for the defeased bonds are not included in the Authority’s financial statements. On June 30, 2010, $210,010,000 of bonds outstanding is considered defeased.

Commercial Paper Program

The Tennessee State School Bond Authority issues short-term debt to finance certain capital projects for the State of Tennessee's higher education institutions. The maximum principal to be issued by the Authority is $300,000,000. Commercial paper may be issued as tax-exempt or as taxable. At the program's inception, commercial paper refinanced certain outstanding bond anticipation note indebtedness that the Authority had previously issued to finance capital projects. The commercial paper dealer is J.P. Morgan Chase. At June 30, 2010, $139,552,000 of tax-exempt commercial paper and $142,230,000 of taxable commercial paper is outstanding. At June 30, 2009, $72,070,000 of tax-exempt commercial paper and $102,230,000 of taxable commercial paper was outstanding

The maturity of the paper may not exceed 270 days, and the maximum interest rate may not exceed 12%. Upon maturity, the paper is remarketed by the commercial paper dealer, redeemed, or extinguished with long-term debt. Interest rates on commercial paper ranged from 0.15% to 0.55% during the fiscal year. Interest is payable upon maturity.

The Authority currently has State Street Bank and Trust Company as their liquidity provider under a Credit Agreement with an expiry date of March 30, 2014, subject to extension and earlier termination. The total available commitment is $304,593,750. The obligation of State Street Bank and Trust Company is to purchase unremarketed commercial paper. In the event the liquidity facility is called upon, the Authority must repay the advance on the earlier of (i) the date of such Advance or (ii) the Termination Date. Unless the Authority repays the advance by the Term Loan Closing Date, the principal amount will convert to a term loan with six equal semi-annual payments. In accordance with Financial Accounting Standards Board Statement No. 6, *Classification of Short-Term Obligations Expected to Be Refinanced*, this agreement meets the criteria of a financing agreement; thus, the commercial paper payable is classified as a long-term liability.

NOTE 6. UNEARNED REVENUE

Changes in unearned revenue for the year ended June 30, 2010, and 2009, are as follows (expressed in thousands):

	Balance July 1, 2009	Additions	Deletions	Balance June 30, 2010
Interest rate reserve fund	$ 1,195	$ 574	$ 394	$ 1,375
Other unearned revenue	2,463	2,758	905	4,316
Total unearned revenue	$ 3,658	$ 3,332	$ 1,299	$ 5,691

	Balance July 1, 2008	Additions	Deletions	Balance June 30, 2009
Interest rate reserve fund	$ 1,054	$ 757	$ 616	$ 1,195
Other unearned revenue	7,941	249	5,727	2,463
Total unearned revenue	$ 8,995	$ 1,006	$ 6,343	$ 3,658

Unearned revenue at June 30, 2010, and June 30, 2009, is as follows (expressed in thousands):

	June 30, 2010	June 30, 2009
Interest Rate Reserve Fund	$ 1,375	$ 1,195
Difference in bond proceeds available for capital expenditure and the par value of bonds to be repaid-adjustments for discount/premium, underwriters' fees, and other costs of issuance:		
1998 Series D bonds, which was an advance refunding of the 1992 Series A bonds; amortized through 2021	1,518	1,658
1999 Qualified Zone Academy Bonds; amortized through 2012	46	84
2000 Series A bonds; amortized through 2010	0	25

2000 Series B bonds; amortized through 2010	0	16
2001 Qualified Zone Academy Bonds; amortized through 2016	114	136
2002 Series A bonds; amortized through 2012	73	109
2003 Qualified Zone Academy Bonds; amortized through 2019	68	76
2004 Series A bonds; amortized through 2026	3,478	3,699
2004 Series B bonds; amortized through 2034	(1,210)	(1,261)
2004 Series C bonds; amortized through 2034	384	400
2004 Qualified Zone Academy Bonds; amortized through 2020	55	61
2005 Series A bonds; amortized through 2030	72	75
2005 Series B bonds; amortized through 2028	3,470	3,664
2005 Qualified Zone Academy Bonds; amortized through 2021	386	423
2006 Series A bonds; amortized through 2021	533	581
2006 Series B bonds; amortized through 2011	10	20

2007 Series A bonds; amortized through 2026	(332)	(354)
2007 Series B bonds; amortized through 2036	127	132
2007 Series C bonds; amortized through 2032	(928)	(971)
2008 Series A bonds; amortized through 2027	(1,225)	(1,299)
2008 Series B bonds; amortized through 2038	(2,006)	(2,079)
2009 Series A bonds; amortized through 2039	(2,665)	(2,757)
2009 QSCB bonds; amortized through 2026	2,327	-
Other unearned revenue	21	25
Total	$ 5,691	$ 3,658

NOTE 7. SUBSEQUENT EVENTS

On January 28, 2011, the Authority has outstanding $95,717,000 in tax-exempt commercial paper and $10,595,000 in taxable commercial paper. Between June 30, 2010, and January 28, 2011, the Authority has issued $50,218,000 in commercial paper to pay construction expenditures.

On September 15, 2010, the Authority issued the 2010 Series A Bonds and the 2010 B Bonds (Federally Taxable). The 2010 Series A tax-exempt bond proceeds in the amount of $213,920,000 were issued to redeem $94,036,000 of the Authority's tax-exempt commercial paper and $110,498,000 of the Authority's taxable commercial paper. A portion of the projects funded under the 2010 Series A Bonds were being funded with taxable commercial paper awaiting a private letter ruling from the Internal Revenue Service. Once the private letter ruling had been received with the notion that those projects could be financed with tax-exempt bonds, the Authority included them in the 2010 Series A Bond issuance. The 2010 Series B taxable bond proceeds in the amount of $18,015,000 were issued to redeem $15,833,000 taxable commercial paper. The balance of the proceeds of the 2010 Series A and 2010 Series B were used to pay for new construction projects, various costs of issuance and to fund the debt service reserve fund.

On October 7, 2010, the Authority issued Qualified School Construction Bonds, Series 2010 (2010 QSCB) in the amount of $212,440,000. The 2010 QSCB proceeds were issued for the purposes of financing various qualifying QSCB projects and to pay the costs of issuance of the 2010 QSCBs.

On December 31, 2010, $9,547,000 of the 2008 QZAB allocation expired.

TENNESSEE STATE SCHOOL BOND AUTHORITY
SUPPLEMENTARY SCHEDULES OF NET ASSETS - PROGRAM LEVEL
JUNE 30, 2010, AND JUNE 30, 2009

(Expressed in Thousands)

	June 30, 2010				June 30, 2009		
	Higher Education Facilities Programs	Qualified Zone Academy Bonds Program	Qualified School Construction Bonds Program	Total	Higher Education Facilities Programs	Qualified Zone Academy Bonds Program	Total
ASSETS							
Current assets:							
Cash	$ 39,192	$ 130	$ 3	$ 39,325	$ 45,396	$ 1,041	$ 46,437
Cash with fiscal agent	357	-	-	357	957	-	957
Investments with fiscal agent	-	14	-	14	-	14	14
Deferred outflow - derivatives	-	1,613	-	1,613	-	2,686	2,686
Prepaid interest expense	-	-	-	-	24	-	24
Loans receivable	41,818	3,453	9,204	54,475	47,100	3,707	50,807
Interest receivable	6,478	16	33	6,527	6,605	16	6,621
Receivables for administrative fees	455	10	-	465	570	10	580
Total current assets	88,300	5,236	9,240	102,776	100,652	7,474	108,126
Noncurrent assets:							
Restricted cash	9	17,576	165,476	183,061	8	15,383	15,391
Restricted investments	25,159	11,738	-	36,897	28,188	9,979	38,167
Loans receivable	1,029,910	24,558	13,988	1,068,456	952,271	27,314	979,585
Deferred charges	7,836	601	1,570	10,007	8,331	690	9,021
Total noncurrent assets	1,062,914	54,473	181,034	1,298,421	988,798	53,366	1,042,164
Total assets	1,151,214	59,709	190,274	1,401,197	1,089,450	60,840	1,150,290
LIABILITIES							
Current liabilities:							
Accounts payable	11,600	-	3	11,603	9,324	-	9,324
Accrued liabilities	-	-	10,847	10,847	-	-	-
Fair value of derivatives	-	1,613	-	1,613	-	2,686	2,686
Due to primary government	-	-	7	7	-	-	-
Accrued interest payable	6,488	-	119	6,607	6,768	-	6,768
Unearned revenue	1,735	109	111	1,955	1,584	109	1,693
Bonds payable	41,923	-	-	41,923	47,201	-	47,201
Total current liabilities	61,746	1,722	11,087	74,555	64,877	2,795	67,672
Noncurrent liabilities:							
Unearned revenue	958	561	2,216	3,735	1,293	672	1,965
Commercial paper payable	281,782	-	-	281,782	174,300	-	174,300
Bonds payable	798,901	57,180	177,000	1,033,081	841,094	57,168	898,262
Total noncurrent liabilities	1,081,641	57,741	179,216	1,318,598	1,016,687	57,840	1,074,527
Total liabilities	1,143,387	59,463	190,303	1,393,153	1,081,564	60,635	1,142,199
NET ASSETS							
Unrestricted	$ 7,827	$ 246	$ (29)	$ 8,044	$ 7,886	$ 205	$ 8,091

TENNESSEE STATE SCHOOL BOND AUTHORITY
SUPPLEMENTARY SCHEDULES OF REVENUES,
EXPENSES AND CHANGES IN NET ASSETS - PROGRAM LEVEL
FOR THE YEARS ENDED JUNE 30, 2010, AND JUNE 30, 2009

(Expressed in Thousands)

	Year ended June 30, 2010				Year ended June 30, 2009		
	Higher Education Facilities Programs	Qualified Zone Academy Bonds Program	Qualified School Construction Bonds Program	Total	Higher Education Facilities Programs	Qualified Zone Academy Bonds Program	Total
OPERATING REVENUES							
Revenue from loans	$ 41,749	$ 128	$ 1,500	$ 43,377	$ 38,851	$ 128	$ 38,979
Investment earnings	354	30	2	386	678	64	742
Total operating revenues	42,103	158	1,502	43,763	39,529	192	39,721
OPERATING EXPENSES							
Interest expense-commercial paper	757	-	-	757	3,457	-	3,457
Interest expense-bonds	39,899	13	1,445	41,357	33,986	13	33,999
Subsidy to borrowers	291	-	-	291	511	-	511
Administrative expense	719	15	39	773	949	21	970
Amortization of bond issuance costs	496	89	47	632	454	89	543
Total operating expenses	42,162	117	1,531	43,810	39,357	123	39,480
Operating income (loss) and change in net assets	(59)	41	(29)	(47)	172	69	241
Net assets, July 1	7,886	205	-	8,091	7,714	136	7,850
Net assets, June 30	$ 7,827	$ 246	$ (29)	$ 8,044	$ 7,886	$ 205	$ 8,091

TENNESSEE STATE SCHOOL BOND AUTHORITY
SUPPLEMENTARY SCHEDULES OF CASH FLOWS - PROGRAM LEVEL
FOR THE YEARS ENDED JUNE 30, 2010, AND JUNE 30, 2009

(Expressed in Thousands)

	Year ended June 30, 2010					Year ended June 30, 2009		
	Higher Education Facilities Programs	Qualified Zone Academy Bonds Program	Qualified School Construction Bonds Program	Total		Higher Education Facilities Programs	Qualified Zone Academy Bonds Program	Total
CASH FLOWS FROM OPERATING ACTIVITIES								
Receipts from borrowers for administrative fees	$ 613	$ 16	$ -	$ 629		$ 357	$ 16	$ 373
Payment to suppliers	(715)	(15)	(32)	(762)		(811)	(21)	(832)
Receipts from borrowers to the interest rate reserve fund	573	-	-	573		757	-	757
Payments to borrowers from the interest rate reserve fund	(394)	-	-	(394)		(616)	-	(616)
Net cash provided by (used in) operating activities	77	1	(32)	46		(313)	(5)	(318)
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES								
Proceeds from sale of bonds	-	-	177,000	177,000		282,737	-	282,737
Proceeds from sale of commercial paper	110,000	-	-	110,000		163,000	-	163,000
Bond issuance costs paid	-	-	(1,614)	(1,614)		(498)	-	(498)
Principal paid - bonds and commercial paper	(49,870)	-	-	(49,870)		(267,076)	-	(267,076)
Interest paid - bonds and commercial paper	(41,207)	-	(1,326)	(42,533)		(36,090)	-	(36,090)
Subsidy to borrowers	(438)	-	-	(438)		(511)	-	(511)
Net cash provided by noncapital financing activities	18,485	-	174,060	192,545		141,562	-	141,562
CASH FLOWS FROM INVESTING ACTIVITIES								
Purchases of investments	(3,276)	(14,317)	-	(17,593)		(32,715)	(13,531)	(46,246)
Proceeds from sales and maturities of investments	6,132	12,588	-	18,720		7,399	11,857	19,256
Interest received on investments	520	448	191	1,159		593	330	923
Loans issued	(114,860)	(89)	(10,684)	(125,633)		(177,062)	(202)	(177,264)
Loan escrow paid	(130)	-	-	(130)		(130)	2,436	2,306
Collections of loan principal	45,080	2,844	-	47,924		43,199	256	43,455
Interest received on loans	41,169	-	1,944	43,113		35,936	(217)	35,719
Refund to borrower	-	(193)	-	(193)		-	-	-
Net cash provided by (used in) investing activities	(25,365)	1,281	(8,549)	(32,633)		(122,780)	929	(121,851)
Net increase (decrease) in cash	(6,803)	1,282	165,479	159,958		18,469	924	19,393
Cash, July 1	46,361	16,424	-	62,785		27,892	15,500	43,392
Cash, June 30	$ 39,558	$ 17,706	$ 165,479	$ 222,743		$ 46,361	$ 16,424	$ 62,785
Reconciliation of cash to the Statement of Net Assets:								
Cash	$ 39,192	$ 130	$ 3	$ 39,325		$ 45,396	$ 1,041	$ 46,437
Cash with fiscal agent	357	-	-	357		957	-	957
Restricted cash	9	17,576	165,476	183,061		8	15,383	15,391
Cash, June 30	$ 39,558	$ 17,706	$ 165,479	$ 222,743		$ 46,361	$ 16,424	$ 62,785
Reconciliation of operating income (loss) to net cash provided by (used in) operating activities:								
Operating income (loss)	$ (59)	$ 41	$ (29)	$ (47)		$ 172	$ 69	$ 241
Adjustments to reconcile operating income (loss) to net cash provided by (used in) operating activities:								
Amortization of bond issuance costs	495	89	47	631		454	89	543
Investment earnings	(354)	(30)	(2)	(386)		(678)	(55)	(733)
Interest expense	40,656	13	1,445	42,114		37,443	13	37,456
Subsidy to borrowers	291	-	-	291		511	-	511
Interest income (loss) from loans	(41,014)	-	(1,445)	(42,459)		(38,546)	(9)	(38,555)
Changes in assets and liabilities:								
(Increase) in receivables for administrative fees	(114)	-	-	(114)		213	-	213
(Increase) decrease in payables for administrative fees	(4)	-	-	(4)		(24)	-	(24)
Increase (decrease) in due to primary government	-	-	7	7		-	-	-
Increase (decrease) in unearned revenue	180	(112)	(55)	13		142	(112)	30
Total adjustments	136	(40)	(3)	93		(485)	(74)	(559)
Net cash provided by (used in) operating activities	$ 77	$ 1	$ (32)	$ 46		$ (313)	$ (5)	$ (318)
Noncash financing activities:								
Accretion of capital appreciation bonds	$ 151	$ -	$ -	$ 151		$ 322	$ -	$ 322
Bond issuance costs	-	-	1,614	1,614		(5,481)	-	(5,481)
Total noncash financing activities	$ 151	$ -	$ 1,614	$ 1,765		$ (5,159)	$ -	$ (5,159)
Noncash investing activities:								
Increase (decrease) in fair value of investments	$ (217)	$ -	$ -	$ (217)		$ (52)	$ -	$ (52)