AUDIT REPORT

Tennessee Local Development Authority

For the Year Ended
June 30, 2011

STATE OF TENNESSEE

COMPTROLLER OF THE TREASURY

Department of Audit

Division of State Audit

Tennessee Comptroller of the Treasury

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April 26, 2012

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

Ladies and Gentlemen:

Transmitted herewith is the financial and compliance audit of the Tennessee Local Development Authority for the year ended June 30, 2011. 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
11/093

State of Tennessee

Audit Highlights

Comptroller of the Treasury — Division of State Audit

Financial and Compliance Audit
Tennessee Local Development Authority
For the Year Ended June 30, 2011

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 Local Development Authority
For the Year Ended June 30, 2011

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Tennessee Local Development Authority
For the Year Ended June 30, 2011

INTRODUCTION

POST-AUDIT AUTHORITY

This is a report on the financial and compliance audit of the Tennessee Local Development 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 Local Development Authority was created April 2, 1978, by an act of the General Assembly, codified as Title 4, Chapter 31, *Tennessee Code Annotated*. The Authority is delegated the responsibility for issuing its debt obligations to provide funds to make loans to local governments for the State Loan Programs and for capital projects; certain small business concerns for pollution control facilities; farmers for certain capital improvements; counties for the acquisition of equipment for use by county or volunteer fire departments serving unincorporated areas of the counties; airport authorities and municipal airports; and mental health/retardation/alcohol and drug facilities (the Community Provider Pooled Loan Program). To date, the Authority has issued debt only to fund the State Loan Programs and the Community Provider Pooled Loan Program.

ORGANIZATION

The Tennessee Local Development Authority is composed of the Governor, the Secretary of State, the Comptroller of the Treasury, the State Treasurer, the Commissioner of Finance and Administration, and two other members—one appointed by the Speaker of the Senate from nominations by the Tennessee County Services Association and the other by the Speaker of the House from Nominations by the Tennessee Municipal League. The Governor serves as Chairman, and the Comptroller of the Treasury serves as Secretary.

An organization chart for the Tennessee Local Development Authority is on the following page.

AUDIT SCOPE

The audit was limited to the period July 1, 2010, through June 30, 2011, 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, 2011, and for comparative purposes, the year ended June 30, 2010. The Tennessee Local Development 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);

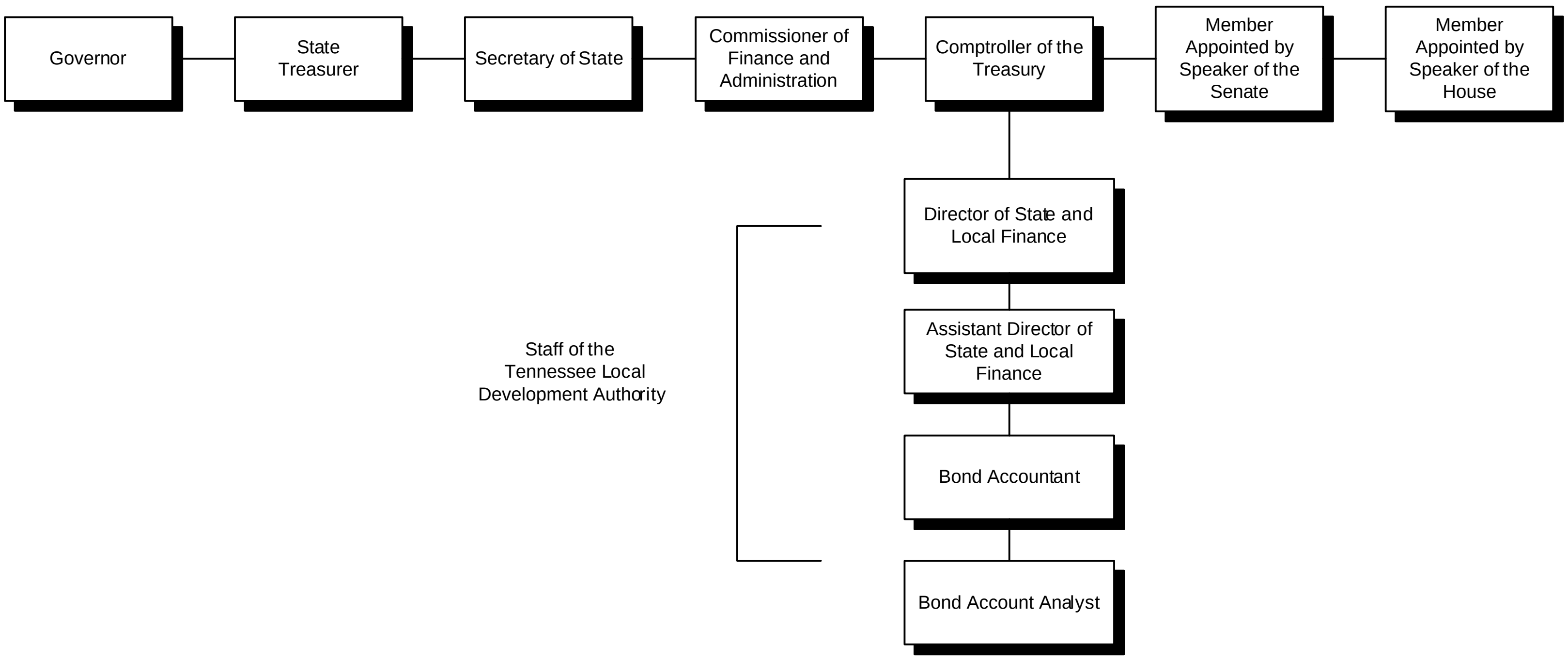
3. to determine the fairness of the presentation of the financial statements; and

4. to recommend appropriate actions to correct any deficiencies.

PRIOR AUDIT FINDINGS

There were no findings in the prior audit report.

TENNESSEE LOCAL DEVELOPMENT AUTHORITY
ORGANIZATION CHART



OBSERVATIONS AND COMMENTS

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 Local Development Authority's financial statements for the year ended June 30, 2011, 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 Local Development 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*

December 16, 2011

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

Ladies and Gentlemen:

We have audited the financial statements of the Tennessee Local Development Authority, a component unit of the State of Tennessee, as of and for the year ended June 30, 2011, and have issued our report thereon dated December 16, 2011. 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

Management of the Tennessee Local Development Authority is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered the Authority's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the 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
COMPTROLLER OF THE TREASURY
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Independent Auditor's Report

December 16, 2011

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

Ladies and Gentlemen:

We have audited the accompanying statements of net assets of the Tennessee Local Development Authority, a component unit of the State of Tennessee, as of June 30, 2011, and June 30, 2010, 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 Local Development Authority. We do not believe that the Comptroller's service in this capacity affected our ability to conduct an independent audit of the Tennessee Local Development Authority.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Tennessee Local Development Authority as of June 30, 2011, and June 30, 2010, 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.

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 December 16, 2011, on our consideration of the 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., CPA
Director

AAH/ddm

As management of the Tennessee Local Development Authority, we offer readers of the Authority's financial statements this narrative overview and analysis of the financial activities of the Authority for the fiscal years ended June 30, 2011, and June 30, 2010, with comparative data for the year ended June 30, 2009. This discussion has been prepared by management along with the financial statements and related note disclosures and should be read in conjunction with the Independent Auditor's Report, the audited financial statements, and the accompanying notes. The financial statements, notes, and this discussion are the responsibility of management.

Program Activity Highlights

The Authority's purpose is to provide loans to Local Government Units under the State Loan Programs and State Infrastructure Program, and to qualified borrowers under the Community Provider Loan program. The table below summarizes this business activity.

Pursuant to Title 4, Chapter 31, *Tennessee Code Annotated*, the General Assembly of the state created the Tennessee Local Development Authority to issue bonds and notes to fund capital projects for a variety of purposes. Currently, the active programs of the Authority include:

1) the State Loan Programs providing assistance to Local Government Units in the construction of waterworks, sewage treatment, and energy and/or solid waste recovery facilities;

2) the Community Provider Program providing facility construction assistance to licensed, nonprofit, 501(c)(3) corporations under grant contracts with the state to deliver mental health, mental retardation, or alcohol and drug services; and

	Local Government Units			**Community Providers**		
	2011	2010	2009	2011	2010	2009
Number of borrowers with outstanding loans	28	36	37	6	6	6
Total number of outstanding loans	35	58	62	7	7	7
Total amount of outstanding loans (in thousands)	$7,527	$85,422	$93,799	$1,432	$1,839	$2,116
Number of loans approved in fiscal year	0	1	0	0	0	0
Amount of loans approved in fiscal year (in thousands)	$0	$1,194	$0	$0	$0	$0

3) the State Infrastructure Program providing assistance to Local Government Units in the construction of transportation infrastructure projects that provide public benefits by enhancing mobility or safety, promoting economic development, or increasing the quality of life and general welfare of the public. During the year ended June 30, 2011, one loan was approved in the amount of $1,725,000. No loans were approved or made for the years ended June 30, 2010, and June 30, 2009.

The financial statements and the analysis provided in the remainder of this report reflect the financial results of this activity. For more specific financial information on long-term debt activity, see Note 5, Debt Payable, in the Notes to the Financial Statements.

Debt Administration

A financial analysis of each loan in the State Loan Programs is undertaken before it is approved by the Authority. Each Local Government Unit must demonstrate that it has enacted rates and fees sufficient to repay the debt, as well as to fund operations, maintenance, and depreciation. The Authority is authorized to intercept the local community's state-shared taxes, should the government unit fail to repay timely its loan. Similarly, Community Providers must also charge fees sufficient to repay the debt and fund operations, maintenance, and depreciation. The Authority is also authorized by statute to intercept the state appropriation to the Community Provider should the borrower fail to make timely debt service payments to the Authority.

Under the financing program for the State Loan Programs, during the construction phase of a project, the project generally is funded through the issuance of Bond Anticipation Notes. When sufficient projects are completed to assure an appropriate economy of scale to sell bonds, the Authority fixes the interest rate for the term of the projects by issuing long-term debt. Interest rates on the State Loan Programs facilities long-term fixed-rate loans range from a low of 3.40% to a high of 5.00%. By pooling the financing of their capital needs, management believes that economic efficiencies of a single large borrowing administered by one agency are achieved. The creditworthiness of both large and small Local Government Units is homogenized into one credit resulting in a lower cost of borrowing to all participants.

The Authority's State Loan Programs are rated Aa3, AAA, and AA by Moody's Investors Service, Inc.; Standard & Poor's Rating Group; and Fitch Ratings, respectively. Fitch Ratings comments that the rating reflects the ongoing commitment to conservative practices of the program. Fitch also cites the structure of the Authority's board with its composition including the state's highest elected officials as an asset of the program. Standard & Poor's Rating Group notes that the ample debt service reserve fund and the underlying credit quality of the local governments receiving loans are strengths of the credit. Moody's Investors Service comments that the responsibility of the localities to repay loans, the sound legal provisions, and state oversight were factors in the rating process. All rating agencies commented that the fact that there had been no recourse to the state intercept of state-shared taxes nor to the statutory reserve fund was an additional strength of the credit.

The Community Provider program was originally authorized in 1990 by the General Assembly to provide construction financing for eligible borrowers at interest rates lower than would otherwise be obtainable in the capital market. The program was initially funded through the issuance of the 1992 and the 1994 Community Provider bonds. In 1999, the State Funding Board loaned $16,000,000 to the Authority to defease the 1992 and 1994 bonds. This loan was fully repaid during fiscal year 2009.

Overview of the Financial Statements

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 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 comprise 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; the Statement of Revenues, Expenses, and Changes in Net Assets; and the Statement of Cash Flows. The Statement of Net Assets depicts the Authority's overall financial position at June 30, the end of each fiscal year presented. The Statement of Revenues, Expenses, and Changes in Net Assets reports the results of operations for the year. The Statement of Cash Flows summarizes the inflows and outflows of cash throughout the fiscal year. These statements are supplemented by notes to the basic financial statements, which provide information essential to the reader's understanding of the financial statements. In addition to the basic financial statements and notes, this report also contains supplementary information containing 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 goal of the Authority is to provide timely access to the capital markets at the lowest possible cost and to make creditworthy loans. The Authority successfully achieved this goal. There were no incidents requiring the Authority to draw from the debt service reserve fund or refuse a loan to an applicant due to the inability to obtain capital funding.

No Revenue Bond Anticipation Notes were issued during the year ended June 30, 2011.

During the year ended June 30, 2010, the Authority issued $53,060,000 of State Loan Program Revenue Bond Anticipation Notes. Proceeds from this issue were used to retire 2009 Bond Anticipation Notes in the amount of $52,845,000. In addition, long-term principal in the amount of $3,720,000 was repaid during the year.

There are no unexpended note proceeds as of June 30, 2011. All notes have been defeased. In prior years, the cash balance in current assets included unexpended note proceeds available to fund loans to State Loan Programs' eligible borrowers of $4,395,496 at June 30, 2010, and $4,931,980 at June 30, 2009. The decrease in noncurrent assets as of June 30, 2010, is due to the declining frequency and the maturing of existing loans. Noncurrent assets will continue to decrease unless new loans are made. A decrease in interest receivable on investments, as a result of falling interest rates in the nation's financial markets, also impacted the current receivables number.

Statements of Net Assets Summary
(in thousands)

	2011	2010	2009
Current assets	$ 16,066	$ 24,019	$ 18,632
Restricted assets	1,611	5,580	5,910
Other assets	7,492	87,615	92,338
Total assets	25,169	117,214	116,880
Current liabilities	1,404	58,201	57,951
Noncurrent liabilities	7,361	44,712	48,168
Total liabilities	8,765	102,913	106,119
Net assets:			
Unrestricted net assets	16,404	14,301	10,761
Total net assets	$ 16,404	$ 14,301	$ 10,761

Note: The Authority owns no capital assets.

For the year ended June 30, 2011, the largest component of the total asset balance is the cash balance. For the years ended June 30, 2010, and June 30, 2009, the loans receivable balance, which represents the principal due from borrowers to the Authority, was the largest component of the total asset balance. Loans receivable (both current and noncurrent) totaled $8,958,662 at June 30, 2011, and $87,260,196 at June 30, 2010. The large decrease is due to the partial refunding that took place in December 2010. The partial refunding is also the reason for the significant decreases in cash, restricted assets, current liabilities, and noncurrent liabilities. Restricted assets represent the debt service reserve fund. The Authority's unrestricted net assets are available to fund operations and other expenses necessary to meet the goals of the Authority.

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

	2011	2010	2009
Operating Revenues			
Revenue from loans	$ 1,370	$ 2,311	$ 3,062
Interest income	48	93	404
Total operating revenue	1,418	2,404	3,466
Operating Expenses			
Interest expense	791	2,451	3,361
Subsidy to borrowers	29	21	173
Other expenses	174	216	295
Total operating expenses	994	2,688	3,829
Operating Income (Loss)	424	(284)	(363)
Nonoperating Revenue (Expense)	1,679	2,215	(375)
Increase (Decrease) in Net Assets	$ 2,103	$ 1,931	$ (738)

The Authority's operating expenses are supported by revenue received from the borrowers as a one-time cost of issuance expense not to exceed 2% at the time of permanent financing, interest on loans, and income on investments. Operating expenses include interest expense on outstanding debt, administrative expenses, and the amortization of bond costs of issuance. The Authority returns a portion of the investment earnings as a subsidy to its borrowers in the State Loan Programs.

While the Authority's operating expenses decreased from 2010 to 2011 and from 2009 to 2010, a decrease in operating revenues resulted in an overall operating loss for the year ended June 30, 2010. Falling market interest rates were responsible for a decrease in interest earned on the Authority's investments. Meanwhile, interest income from loans of the Authority experienced a decrease. This decrease is a result of a decline in the frequency of requests for new loans in recent years. All of the Authority's loans are structured such that the borrowers pay level debt service payments for the life of the loan. Therefore as the loans approach maturity, more of the payments received are applied toward principal, resulting in less interest income. Loan principal prepayments of loans in both the State Loan Program and the Community Provider Program were also partially responsible for the decrease in the interest revenue generated from the Authority's loans.

The increase in nonoperating revenue from 2010 to 2011 is due to a gain on the early termination of loans. The increase in nonoperating revenue from 2009 to 2010 was due to a transfer to the Authority in the amount of $2,190,000 from the Tennessee Department of Transportation (TDOT). The funds were transferred to the Authority after the creation of the Tennessee Transportation State Infrastructure Fund Act pursuant to Section 4-31-1201, *Tennessee Code Annotated*. The State Infrastructure Program provides assistance to Local Government Units in the construction of transportation infrastructure projects that provide public benefits by enhancing mobility or safety, promoting economic development, or increasing the quality of life and general welfare of the public.

The Authority has no plans to issue debt in the immediate future. Communities who had previously utilized the program have found other funding opportunities that better suit their needs.

Contacting the Authority's Financial Management Team

This discussion and analysis is designed to provide our citizens, local government units, community providers, 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 Office of State and Local Finance, State of Tennessee, Suite 1600, James K. Polk Building, Nashville, Tennessee 37243-0273, or visit our website at http://tn.gov/comptroller/sl/.

Exhibit A

TENNESSEE LOCAL DEVELOPMENT AUTHORITY
STATEMENTS OF NET ASSETS
JUNE 30, 2011, AND JUNE 30, 2010

(Expressed in Thousands)

	June 30, 2011	June 30, 2010
ASSETS		
Current assets:		
Cash (Note 2)	$ 14,478	$ 22,375
Receivables:		
Loans receivable (Notes 8 and 9)	1,588	1,643
Interest receivable on loans	-	1
Total current assets	16,066	24,019
Noncurrent assets:		
Restricted cash (Notes 2 and 3)	1,611	5,580
Loans receivable (Notes 8 and 9)	7,371	87,226
Deferred charges	121	389
Total noncurrent assets	9,103	93,195
Total assets	25,169	117,214
LIABILITIES		
Current liabilities:		
Accrued interest payable	127	730
Payable to borrowers (Note 4)	52	22
Notes payable (Note 5)	-	53,919
Revenue bonds payable (Note 5)	1,225	3,530
Total current liabilities	1,404	58,201
Noncurrent liabilities:		
Revenue bonds payable, net (Note 5)	7,361	44,712
Total noncurrent liabilities	7,361	44,712
Total liabilities	8,765	102,913
NET ASSETS		
Unrestricted (Note 6)	16,404	14,301
Total net assets	$ 16,404	$ 14,301

The Notes to the Financial Statements are an integral part of this statement.

Exhibit B

TENNESSEE LOCAL DEVELOPMENT AUTHORITY
STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS
FOR THE YEARS ENDED JUNE 30, 2011, AND JUNE 30, 2010

(Expressed in Thousands)

	Year Ended June 30, 2011	Year Ended June 30, 2010
OPERATING REVENUES		
Revenue from loans	$ 1,370	$ 2,311
Interest income	48	93
Total operating revenues	1,418	2,404
OPERATING EXPENSES		
Interest expense	791	2,451
Subsidy to borrowers	29	21
Note issuance cost	-	64
Administrative expense	174	152
Total operating expenses	994	2,688
Operating income (loss)	424	(284)
NONOPERATING REVENUES AND EXPENSES		
Gain on the early termination of loans (Note 8)	1,654	-
Transfer from the State of Tennessee (Note 7)	25	2,215
Total nonoperating revenue (expense)	1,679	2,215
Change in net assets	2,103	1,931
Net assets, July 1	14,301	10,761
Prior period adjustment for correction of error (Note 9)	-	1,609
Net assets, July 1, restated	14,301	12,370
Net assets, June 30	$ 16,404	$ 14,301

The Notes to the Financial Statements are an integral part of this statement.

Exhibit C

TENNESSEE LOCAL DEVELOPMENT AUTHORITY
STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED JUNE 30, 2011, AND JUNE 30, 2010

(Expressed in Thousands)

	Year Ended June 30, 2011	Year Ended June 30, 2010
CASH FLOWS FROM OPERATING ACTIVITIES		
Payments to service providers	$ (174)	$ (206)
Net cash used by operating activities	(174)	(206)
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES		
Proceeds from the issuance of notes	-	53,957
Principal payments	(1,520)	(56,565)
Interest paid	(1,735)	(2,843)
Subsidy to borrowers	-	(166)
Transfer from the State of Tennessee	25	2,215
Payment for defeasance of debt	(14,648)	-
Net cash used by noncapital financing activities	(17,878)	(3,402)
CASH FLOWS FROM INVESTING ACTIVITIES		
Loans issued	(612)	(1,000)
Collections of loan principal	5,379	9,627
Interest received on loans	1,371	2,311
Proceeds from sales and maturity of investments	-	188
Interest received on pooled investment fund	48	93
Net cash provided by investing activities	6,186	11,219
Net increase (decrease) in cash	(11,866)	7,611
Cash, July 1	27,955	20,344
Cash, June 30	$ 16,089	$ 27,955
Reconciliation of operating income (loss) to net cash used by operating activities:		
Operating income (loss)	$ 424	$ (284)
Adjustments to reconcile operating income (loss) to net cash used by operating activities:		
Amortization	-	36
Revenue from loans	(1,370)	(2,311)
Interest income	(48)	(93)
Interest expense	791	2,451
Administrative expense	-	(26)
Subsidy to borrowers	29	21
Total adjustments	(598)	78
Net cash used by operating activities	$ (174)	$ (206)

The Notes to the Financial Statements are an integral part of this statement.

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Reporting Entity

The Tennessee Local Development Authority was created to provide financial assistance to local governments through the issuance of revenue bonds or notes. The Authority has also issued bonds to assist nonprofit corporations in the construction of mental health, mental retardation, or alcohol and drug facilities.

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 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 Secretary of State, the Comptroller of the Treasury, the State Treasurer, the Commissioner of Finance and Administration, a State Senate appointee, and a State House appointee. The Governor serves as chairman and the Secretary of State serves as vice chairman. The Director of the Office of State and Local Finance serves as the assistant secretary; the office 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 (GASB). The Tennessee Local Development Authority follows all applicable GASB pronouncements as well as applicable private sector pronouncements issued on or before November 30, 1989. The Authority has chosen 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 Local Development Authority distinguishes operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with principal ongoing operations. The Authority's principal operation is to provide loans to local governments through the issuance of revenue bonds or notes. Therefore, the principal operating revenues of the Authority are from interest on loans made to borrowers. 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. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

Cash

This classification includes cash on hand and deposits in the pooled investment fund administered by the State Treasurer.

Investments

Investments are stated at fair value. Securities are recorded on trade-date basis.

Bond Discounts and Issuance Costs

Bond discounts and issuance costs are deferred and amortized over the life of the bonds using the straight-line method. Bonds payable are reported net of the applicable unamortized bond discount. Unamortized issuance costs are reported as deferred charges.

NOTE 2. DEPOSITS AND INVESTMENTS

Under the general bond resolution of the Tennessee Local Development Authority, the funds of the Authority are to be held and invested by the State Treasurer.

Deposits

The Authority does not utilize its own bank accounts but has cash on deposit for its operating cash purposes in the State Pooled Investment Fund administered by the State Treasurer. The Authority had $16,090,287 in the pooled investment fund at June 30, 2011, and $27,954,964 at June 30, 2010. The pooled investment fund is authorized by statute to invest funds in accordance with policy guidelines approved by the State Funding Board. The fund is not rated by a nationally recognized statistical rating organization. Its investment policy and required risk disclosures are presented in the *State of Tennessee's Treasurer's Report*. The report is posted on the state's website at www.treasury.tn.gov, or may be obtained by calling (615) 741-2956.

Investments

As of June 30, 2010, all of the Authority's investments had matured, and no investments were held at June 30, 2011.

NOTE 3. RESTRICTED ASSETS

The general bond resolution of the Authority requires that the principal of each bond issue include an amount equal to one year's debt service requirement and that such amount be placed in special trust accounts with the trustee. The required debt service reserve is $1,611,103 at June 30, 2011, and $5,580,454 at June 30, 2010.

The general bond resolution also requires that the debt service requirement in any year of the refunding bonds must not exceed the debt service requirement in any year of the refunded bonds. Two of the largest borrowers in the 2003 refunding issue chose to shorten the term of their loans by one year, causing the new debt service requirement in the year 2011 to exceed the prior debt service requirement by $26,148.75. The amount was yield restricted and placed in a special trust account with the trustee and held until March 1, 2011. The deposit, in effect, reduced the new debt service requirement not to exceed the prior debt service requirement.

NOTE 4. PAYABLE TO BORROWERS

This account represents interest earnings on restricted assets and loan principal overpayments that will be refunded to borrowers.

NOTE 5. DEBT PAYABLE

Notes. Revenue bond anticipation notes in the amount of $53,060,000 were issued in June 2010 to retire at maturity the $52,845,000 notes issued in 2009 and provide additional loan funds to local government units for water and sewer construction projects. No revenue bond anticipation notes were issued in fiscal year 2011.

Notes payable at June 30, 2010, were as follows (expressed in thousands):

	June 30, 2010
2010 Series A at an interest rate of 2.00% maturing June 24, 2011	$ 53,060
Total par amount of notes payable	53,060
Plus unamortized premium	859
Net notes payable	$ 53,919

Short-term debt activity for the year ended June 30, 2010, net of unamortized premium (expressed in thousands):

Beginning Balance	Additions	Reductions	Ending Balance
$53,288	$53,919	$53,288	$53,919

Revenue bonds. Bonds payable at June 30, 2011, and June 30, 2010, are as follows (expressed in thousands):

	June 30, 2011	June 30, 2010
2003 Refunding Series A at an interest rate of 4.00% maturing to 2015 (original par–$8,295)	$ 1,410	$ 2,060
2006 Refunding Series A at interest rates from 4.00% to 5.00% maturing to 2021 (original par–$20,070)	4,405	13,490
2006 Series B at interest rates from 3.4% to 4.375% maturing to 2029 (original par–$37,415)	3,030	33,390
Total par amount of bonds payable	8,845	48,940
Plus unamortized premium	256	714
Less unamortized discount	(16)	(172)
Bonds payable net of unamortized premium/discount	9,085	49,482
Less deferred amount on refunding	(499)	(1,240)
Net bonds payable	$ 8,586	$ 48,242

Debt service requirements to maturity of the revenue bonds payable at June 30, 2011, are as follows (expressed in thousands):

For the Year(s) Ending June 30	Principal	Interest	Total
2012	$ 1,253	$ 358	$ 1,611
2013	1,063	310	1,373
2014	1,093	264	1,357
2015	937	218	1,155
2016	809	179	988
2017-2021	2,686	442	3,128
2022-2026	1,191	194	1,385
2027-2029	53	22	75
Total	$ 9,085	$ 1,987	$ 11,072

The above for bonds does not reflect a $498,675 deduction from bonds payable for the deferred amount on refunding.

Changes in long-term debt payable for the year ended June 30, 2011, are as follows (expressed in thousands):

	Beginning Balance	Additions	Reductions	Ending Balance	Amounts Due Within One Year
Revenue bonds payable	$ 48,940	$ -	$ 40,095	$ 8,845	$ 1,225
Unamortized amounts:					
Premium	714	-	458	256	-
Discount	(172)	-	(156)	(16)	-
Deferred amount on refundings	(1,240)	-	(741)	(499)	-
Total bonds payable	$ 48,242	$ -	$ 39,656	$ 8,586	$ 1,225

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

	Beginning Balance	Additions	Reductions	Ending Balance	Amounts Due Within One Year
Revenue bonds payable	$ 52,660	$ -	$ 3,720	$ 48,940	$ 3,530
Unamortized amounts:					
Premium	783	-	69	714	-
Discount	(180)	-	(8)	(172)	-
Deferred amount on refundings	(1,375)	-	(135)	(1,240)	-
Total bonds payable	$ 51,888	$ -	$ 3,646	$ 48,242	$ 3,530

NOTE 6. STATUTORY RESERVE RESTATEMENT

In fiscal year 2011, the decision was made to restate amounts held in the Statutory Reserve Fund from restricted to unrestricted. The intention of the Fund was to ensure payment of the required annual debt service (principal and interest) for certain municipalities. As of June 30, 2011, Mount Carmel was the only borrower comprising the Fund. After review of the General Bond Resolution, it was determined that this amount should be classified as unrestricted. For comparative purposes, the Statutory Reserve Fund amount of $204,534 at June 30, 2010, was restated as unrestricted net assets on the June 30, 2010, Statement of Net Assets.

NOTE 7. STATE INFRASTRUCTURE FUND

In fiscal year 2010, the Tennessee Local Development Authority received funds in the amount of $2,190,000. The funds were transferred from the Department of Transportation to the Authority after the creation of the Tennessee Transportation State Infrastructure Fund Act pursuant to Section 4-31-1201, *Tennessee Code Annotated*. The State Infrastructure Program provides assistance to Local Government Units in the construction of transportation infrastructure projects that provide public benefits by enhancing mobility or safety, promoting economic development, or increasing the quality of life and general welfare of the public. As of June 30, 2011, one loan has been approved in the amount of $1,725,000.

NOTE 8. EARLY REPAYMENT OF LOANS AND DEFEASANCE OF RELATED DEBT

On December 2, 2010, Metropolitan Government of Nashville and Davidson County advised the Tennessee Local Development Authority (the "Authority") of its desire to prepay its program loans and defease its current TLDA debt outstanding that was issued by the Authority on its behalf. As of December 16, 2010, long-term debt in the amount of $38,575,000 and all of the bond anticipation notes, totaling $53,060,000, were defeased.

NOTE 9. PRIOR PERIOD ADJUSTMENT

During fiscal year 2010, the state converted accounting systems—moving from STARS (State of Tennessee Accounting and Reporting System) to Edison. Due to the bond refundings and issuances that occurred in 2003 and 2006, there were certain adjustments to the receivables balances that had never been entered in STARS. These adjustments which were not entered in STARS included a $954,015 adjustment to capitalize costs of issuance from the 2006 Series B bonds; a $254,896 adjustment to the project receivables for a change in the debt service reserve as a result of the 2003 Series A Refunding bond issue; and a $400,505 adjustment to the project receivables for a change in the debt service reserve as a result of the 2006 Series A Refunding bond issue, because the receivables balance in the accounting system is recorded net of the debt service reserve. Therefore, the Office of State and Local Finance found it necessary for proper record-keeping purposes to record these adjustments in Edison. This resulted in a $1,609,416 prior period adjustment, which is reflected on the Statement of Revenues, Expenses, and Changes in Net Assets for fiscal year 2010.

TENNESSEE LOCAL DEVELOPMENT AUTHORITY
SUPPLEMENTARY SCHEDULES OF NET ASSETS - PROGRAM LEVEL
JUNE 30, 2011, AND JUNE 30, 2010

(Expressed in Thousands)

	June 30, 2011				June 30, 2010			
	State Loan Programs	Community Providers	State Infrastructure Loan Program	Total	State Loan Programs	Community Providers	State Infrastructure Loan Program	Total
ASSETS								
Current assets:								
Cash	$ 11,065	$ 1,211	$ 2,202	$ 14,478	$ 19,476	$ 701	$ 2,198	$ 22,375
Receivables:								
Loans receivable	1,235	353	-	1,588	1,312	331	-	1,643
Interest receivable on loans	-	-	-	-	1	-	-	1
Total current assets	12,300	1,564	2,202	16,066	20,789	1,032	2,198	24,019
Noncurrent assets:								
Restricted cash	1,611	-	-	1,611	5,580	-	-	5,580
Loans receivable	6,292	1,079	-	7,371	85,718	1,508	-	87,226
Deferred charges	121	-	-	121	389	-	-	389
Total noncurrent assets	8,024	1,079	-	9,103	91,687	1,508	-	93,195
Total assets	20,324	2,643	2,202	25,169	112,476	2,540	2,198	117,214
LIABILITIES								
Current liabilities:								
Accrued interest payable	127	-	-	127	730	-	-	730
Payable to borrowers	52	-	-	52	22	-	-	22
Notes payable	-	-	-	-	53,919	-	-	53,919
Revenue bonds payable	1,225	-	-	1,225	3,530	-	-	3,530
Total current liabilities	1,404	-	-	1,404	58,201	-	-	58,201
Noncurrent liabilities:								
Revenue bonds payable, net	7,361	-	-	7,361	44,712	-	-	44,712
Total noncurrent liabilities	7,361	-	-	7,361	44,712	-	-	44,712
Total liabilities	8,765	-	-	8,765	102,913	-	-	102,913
NET ASSETS								
Unrestricted	11,559	2,643	2,202	16,404	9,563	2,540	2,198	14,301
Total net assets	$ 11,559	$ 2,643	$ 2,202	$ 16,404	$ 9,563	$ 2,540	$ 2,198	$ 14,301

TENNESSEE LOCAL DEVELOPMENT AUTHORITY
SUPPLEMENTARY SCHEDULES OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS - PROGRAM LEVEL
FOR THE YEARS ENDED JUNE 30, 2011, AND JUNE 30, 2010

(Expressed in Thousands)

	Year Ended June 30, 2011				Year Ended June 30, 2010			
	State Loan Programs	Community Providers	State Infrastructure Loan Program	Total	State Loan Programs	Community Providers	State Infrastructure Loan Program	Total
OPERATING REVENUES								
Revenue from loans	$ 1,269	$ 101	$ -	$ 1,370	$ 2,192	$ 119	$ -	$ 2,311
Interest income	42	2	4	48	84	1	8	93
Total operating revenues	1,311	103	4	1,418	2,276	120	8	2,404
OPERATING EXPENSES								
Interest expense	791	-	-	791	2,451	-	-	2,451
Subsidy to borrowers	29	-	-	29	21	-	-	21
Note issuance cost	-	-	-	-	64	-	-	64
Administrative expense	174	-	-	174	152	-	-	152
Total operating expenses	994	-	-	994	2,688	-	-	2,688
Operating income (loss)	317	103	4	424	(412)	120	8	(284)
NONOPERATING REVENUES AND EXPENSES								
Gain on the early termination of loans	1,654	-	-	1,654	25	-	2,190	2,215
Transfer from the State of Tennessee	25	-	-	25	-	-	-	-
Total nonoperating revenue (expense)	1,679	-	-	1,679	25	-	2,190	2,215
Change in net assets	1,996	103	4	2,103	(387)	120	2,198	1,931
Net assets, July 1	9,563	2,540	2,198	14,301	8,341	2,420	-	10,761
Prior period adjustment for correction of error	-	-	-	-	1,609	-	-	1,609
Net assets, July 1, restated	9,563	2,540	2,198	14,301	9,950	2,420	-	12,370
Net assets, June 30	$ 11,559	$ 2,643	$ 2,202	$ 16,404	$ 9,563	$ 2,540	$ 2,198	$ 14,301

TENNESSEE LOCAL DEVELOPMENT AUTHORITY
SUPPLEMENTARY SCHEDULES OF CASH FLOWS - PROGRAM LEVEL
FOR THE YEARS ENDED JUNE 30, 2011, AND JUNE 30, 2010

(Expressed in Thousands)

	Year Ended June 30, 2011				Year Ended June 30, 2010			
	State Loan Programs	Community Providers	State Infrastructure Loan Program	Total	State Loan Programs	Community Providers	State Infrastructure Loan Program	Total
CASH FLOWS FROM OPERATING ACTIVITIES								
Payments to service providers	$ (174)	$ -	$ -	$ (174)	$ (206)	$ -	$ -	$ (206)
Net cash used by operating activities	(174)	-	-	(174)	(206)	-	-	(206)
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES								
Proceeds from the issuance of notes	-	-	-	-	53,957	-	-	53,957
Principal payments	(1,520)	-	-	(1,520)	(56,565)	-	-	(56,565)
Interest paid	(1,735)	-	-	(1,735)	(2,843)	-	-	(2,843)
Subsidy to borrowers	-	-	-	-	(164)	(2)	-	(166)
Transfer from the State of Tennessee	25	-	-	25	25	-	2,190	2,215
Payment for defeasance of debt	(14,648)	-	-	(14,648)	-	-	-	-
Net cash used by noncapital financing activities	(17,878)	-	-	(17,878)	(5,590)	(2)	2,190	(3,402)
CASH FLOWS FROM INVESTING ACTIVITIES								
Loans issued	(612)	-	-	(612)	(1,000)	-	-	(1,000)
Collections of loan principal	4,972	407	-	5,379	9,349	278	-	9,627
Interest received on loans	1,270	101	-	1,371	2,192	119	-	2,311
Proceeds from sales and maturity of investments	-	-	-	-	188	-	-	188
Interest received on pooled investment fund	42	2	4	48	84	1	8	93
Net cash provided by investing activities	5,672	510	4	6,186	10,813	398	8	11,219
Net increase (decrease) in cash	(12,380)	510	4	(11,866)	5,017	396	2,198	7,611
Cash, July 1	25,056	701	2,198	27,955	20,039	305	-	20,344
Cash, June 30	$ 12,676	$ 1,211	$ 2,202	$ 16,089	$ 25,056	$ 701	$ 2,198	$ 27,955
Reconciliation of operating income (loss) to net cash used by operating activities:								
Operating income (loss)	$ 317	$ 103	$ 4	$ 424	$ (412)	$ 120	$ 8	$ (284)
Adjustments to reconcile operating income (loss) to net cash used by operating activities:								
Amortization	-	-	-	-	36	-	-	36
Revenue from loans	(1,269)	(101)	-	(1,370)	(2,192)	(119)	-	(2,311)
Interest income	(42)	(2)	(4)	(48)	(84)	(1)	(8)	(93)
Interest expense	791	-	-	791	2,451	-	-	2,451
Administrative expense	-	-	-	-	(26)	-	-	(26)
Subsidy to borrowers	29	-	-	29	21	-	-	21
Total adjustments	(491)	(103)	(4)	(598)	206	(120)	(8)	78
Net cash used by operating activities	$ (174)	$ -	$ -	$ (174)	$ (206)	$ -	$ -	$ (206)