AUDIT REPORT

Tennessee State School Bond Authority

For the Year Ended
June 30, 2013

STATE OF TENNESSEE
COMPTROLLER OF THE TREASURY

Department of Audit

Division of State Audit

Tennessee Comptroller of the Treasury

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March 11, 2014

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

Ladies and Gentlemen:

Transmitted herewith is the financial and compliance audit of the Tennessee State School Bond Authority for the year ended June 30, 2013. You will note from the independent auditor's report that an unmodified 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,

Deborah V. Loveless

Deborah V. Loveless, CPA
Director

14/009

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Tennessee State School Bond Authority
For the Year Ended June 30, 2013

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Opinion on the Financial Statements

The opinion on the financial statements is unmodified.

Audit Findings

The audit report contains no findings.

STATE OF TENNESSEE
COMPTROLLER OF THE TREASURY
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Independent Auditor's Report

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

Report on the Financial Statements

We have audited the accompanying financial statements of the Tennessee State School Bond Authority, a component unit of the State of Tennessee, as of and for the years ended June 30, 2013, and June 30, 2012, and the related notes to the financial statements, which collectively comprise the Authority's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express 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 *Government Auditing Standards* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

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

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

Opinion

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, 2013, and June 30, 2012, and the changes in financial position and cash flows thereof for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As discussed in Note 1 to the financial statements, the Authority adopted Statement Number 65 of the Governmental Accounting Standards Board, *Items Previously Reported as Assets and Liabilities*, during the year ended June 30, 2013. The statement requires that deferred amounts on refunding should be recognized as a deferred outflow/inflow on the statements of net position. Previously, bonds payable were reported net of the deferred amount on refunding. The statement also requires that cost of issuance be expensed instead of being amortized over the life of the bonds. The cumulative effect on net position has been reported on the statement of revenues, expenses, and changes in net position. Amounts on the statement of net position and statement of revenues, expenses, and changes in net position have been restated for comparative purposes for the year ended June 30, 2012. Our opinion is not modified with respect to this matter.

Other Matters

Required Supplementary Information

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

Supplementary Information

Our audits were conducted for the purpose of forming an opinion on the financial statements that collectively comprise the Tennessee State School Bond Authority's 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 is the responsibility of management and was derived from, and relates directly to, the underlying accounting and other records used to prepare the basic financial statements. The information has been subjected to the auditing procedures applied in the audits of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated, in all material respects, in relation to the basic financial statements as a whole.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated December 13, 2013, 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, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Tennessee State School Bond Authority's internal control over financial reporting and compliance.

Deborah V. Loveless

Deborah V. Loveless, CPA
Director
December 13, 2013

TENNESSEE STATE SCHOOL BOND AUTHORITY
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, 2013. These activities are compared to the results of the fiscal years ended June 30, 2012, and 2011. We encourage readers to consider the information presented here in conjunction with the Independent Auditor's Report, the audited financial statements and accompanying notes of this report.

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		
	2013	**2012**	**2011**
Number of higher education facilities with outstanding loans	20	20	20
Total number of outstanding loans	257	232	252
Balance of outstanding loans	$1,245,179,920	$1,165,180,547	$1,107,639,831
Number of loans approved in fiscal year	12	10	9
Dollar amount of loans approved in fiscal year	$ 55,688,000	$ 242,662,000	$ 85,608,000
Dollar amount of loans approved in fiscal year - unspent	$ 42,692,636	$ 237,839,410	$ 84,423,304
Dollar amount of loans financed in fiscal year	$ 170,967,267	$ 114,983,407	$ 111,260,649
Bonds issued in fiscal year	$ 437,720,000	$ -	$ 231,935,000
Commercial paper issued in fiscal year	$ 123,000,000	$ 97,000,000	$ 107,218,000

	Qualified Zone Academy Bond Program		
	2013	**2012**	**2011**
Number of LEAs with outstanding loans	12	12	14
Total number of outstanding loans	16	16	23
Balance of outstanding loans	$ 18,963,617	$ 21,926,992	$ 24,729,304
Balance held in Sinking Fund	$ 24,958,453	$ 21,994,043	$ 32,480,696
Balance of principal outstanding	$ 43,920,000	$ 43,920,000	$ 57,210,000
Dollar amount of loans approved in fiscal year	$ -	$ -	$ -
Dollar amount of loans approved in fiscal year - not disbursed	$ -	$ -	$ -
Dollar amount of loan proceeds disbursed in fiscal year	$ -	$ -	$ -
Bonds issued in fiscal year	$ -	$ -	$ -

	Qualified School Construction Bond Program		
	2013	2012	2011
Number of LEAs with outstanding loans	23	23	23
Total number of outstanding loans	28	28	28
Balance of outstanding loans	$ 330,122,385	$ 290,801,492	$ 145,281,252
Balance held in Sinking Fund	$ 56,297,778	$ 32,838,679	$ 9,764,134
Balance of outstanding debt	$ 389,440,000	$ 389,440,000	$ 389,440,000
Number of loans approved in fiscal year	-	-	15
Dollar amount of loans approved in fiscal year	$ -	$ -	$ 212,440,000
Dollar amount of loans approved in fiscal year - not disbursed	$ -	$ -	$ 182,197,555
Dollar amount of loan proceeds disbursed in fiscal year	$ 70,165,187	$ 172,830,188	$ 124,797,041
Bonds issued in fiscal year	$ -	$ -	$ 212,440,000

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 LEAs 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 a higher education facility applies for project funding through the Authority, an analysis of the financial feasibility of each loan application is undertaken by comparing the projected debt service to the pledged revenue before it is approved by the Authority. Once approved by the Authority, the project will be included in the Financing Agreement between the Authority and the respective higher education system (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 “Board of Regents”), referred to collectively as the “Boards”). The Boards covenant and agree in the Financing Agreements to establish and collect Fees and Charges at each institution at a level sufficient to produce in each fiscal year no less than two times the amount required for the payment of total debt service. Fees and Charges include all revenues, fees, rental and other charges received by or on behalf of an institution which are available to pay debt service. In addition, the Boards agree in the Financing Agreements that the Commissioner of Finance and Administration, after notice from the Authority that the Board has failed to pay its Annual Financing Charges or Administrative Fees, shall deduct from the institution’s appropriations the amount required to make it current with respect to the unpaid Annual Financing Charges and Administrative Fees.

Generally, under the financing program for higher education facilities, a project is funded through the Authority's commercial paper program during its construction phase. When commercial paper totaling $50 million or greater is outstanding for projects that are completed or near completion, the Authority may fix 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, 2013, as compared to the fiscal years 2012 and 2011.

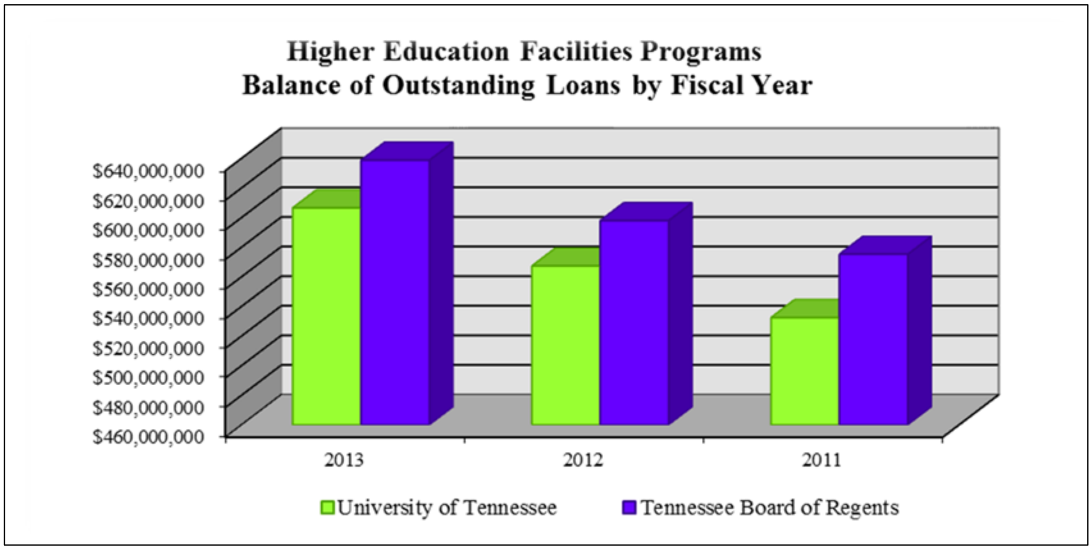
Higher Education Facilities Programs
Commercial Paper Interest Rates Range

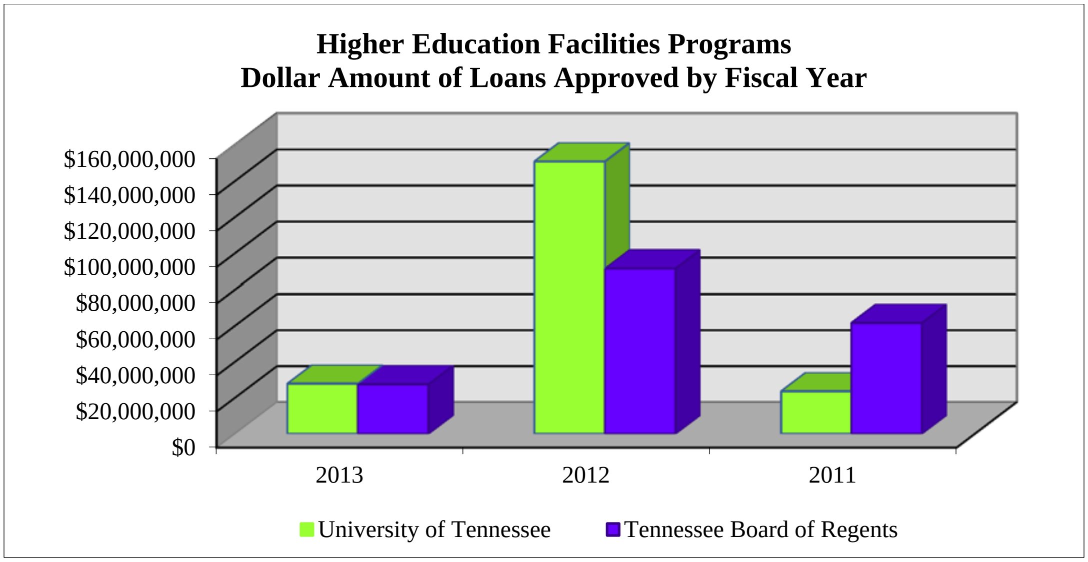
	Tax-Exempt		Federally Taxable	
Fiscal Year	**Low**	**High**	**Low**	**High**
2013	0.10%	0.22%	0.12%	0.22%
2012	0.10%	0.33%	0.10%	0.25%
2011	0.14%	0.34%	0.20%	0.40%

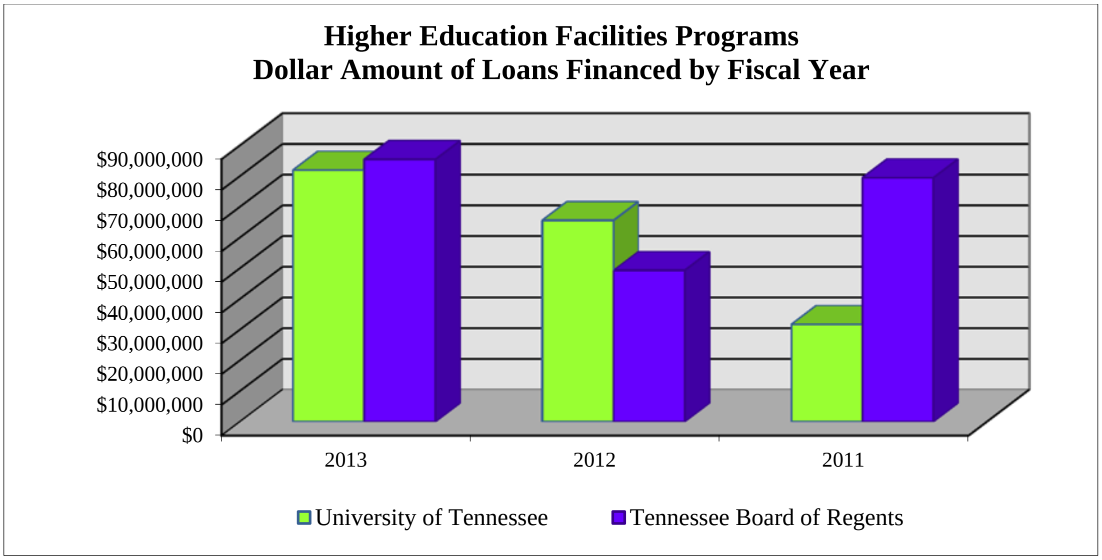
The Authority currently has a Credit Agreement with State Street Bank that provides for a total amount of $300,000,000 of commercial paper principal and 45 days of accrued interest in the amount of $4,593,750, which is calculated at the rate of 12.25% per annum on the basis of a 360-day year. The Credit Agreement with State Street Bank has an expiration date of March 30, 2014, and a commitment fee of .105% which is charged quarterly in arrears. If the liquidity facility is called upon, pursuant to the Advance Agreement, the Authority is obligated to reimburse the Bank for all amounts drawn and paid under the Liquidity Facility, together with interest thereon if not reimbursed on the same day. If not reimbursed on the same day of the advance, the principal amount will convert to a term loan with six equal semi-annual payments. As of the fiscal year June 30, 2013, the Authority had not called upon the liquidity facility.

For the fiscal year ended June 30, 2013, interest rates on the higher education facilities long-term fixed-rate tax-exempt bonds ranged from a low of 0.35% to a high of 5.50%, and the interest rates on the higher education facilities long-term fixed-rate federally taxable bonds ranged from a low of 0.50% to a high of 5.67%. 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 blended 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, 2013, the Authority's higher education facilities program is rated AA+ and AA by Fitch and Standard & Poor's Rating Group, respectively. Moody's Investors Service has assigned the Authority's bonds an enhanced rating of Aa1 and a programmatic rating of Aa1.


Higher Education Facilities Programs
Balance of Outstanding Loans by Fiscal Year
$640,000,000
$620,000,000
$600,000,000
$580,000,000
$560,000,000
$540,000,000
$520,000,000
$500,000,000
$480,000,000
$460,000,000
2013
2012
2011
University of Tennessee
Tennessee Board of Regents

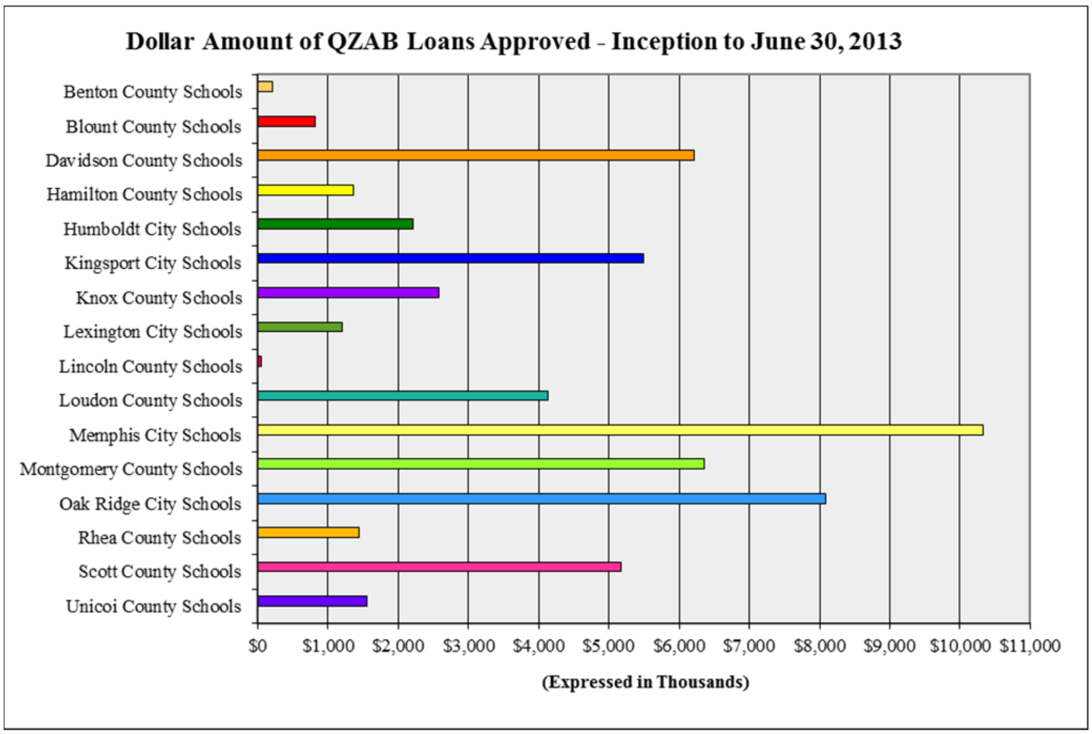

Higher Education Facilities Programs
Dollar Amount of Loans Approved by Fiscal Year
$160,000,000
$140,000,000
$120,000,000
$100,000,000
$80,000,000
$60,000,000
$40,000,000
$20,000,000
$0
2013
2012
2011
University of Tennessee
Tennessee Board of Regents


Higher Education Facilities Programs
Dollar Amount of Loans Financed by Fiscal Year
$90,000,000
$80,000,000
$70,000,000
$60,000,000
$50,000,000
$40,000,000
$30,000,000
$20,000,000
$10,000,000
$0
2013
2012
2011
University of Tennessee
Tennessee Board of Regents

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 Authority, 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 LEAs in the State. The Department recommends those projects that best meet the requirements of the program to the Authority for funding.

The LEA 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 LEA/local government fail to repay its loan timely.

As of June 30, 2013, the QZAB program has unused allocations totaling $27,705,000. Of this amount, $9,431,000 of the 2011 allocation will expire on December 31, 2013. 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.

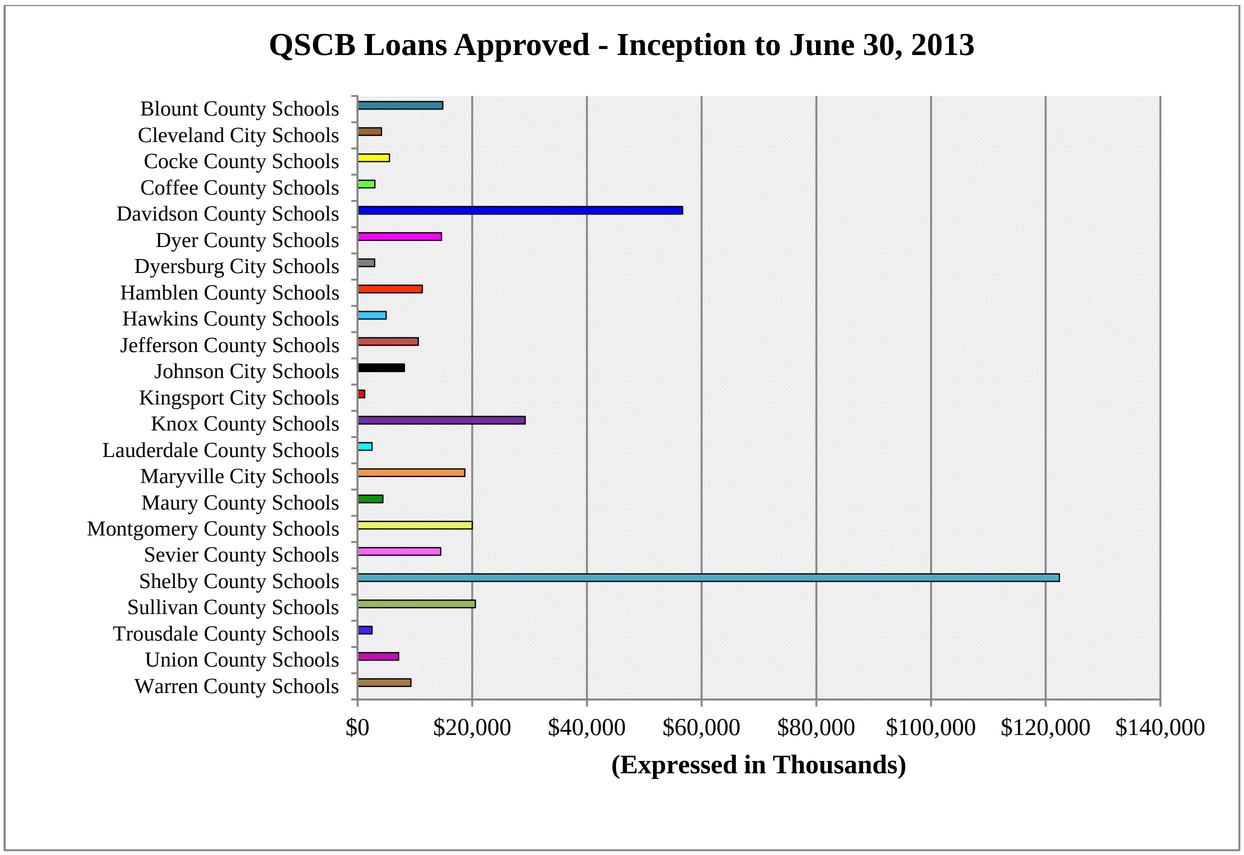


Qualified Zone Academy Bond Program Debt Ratings. All of the QZABs have been placed with private investors. The QZABs are not rated.

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. The

QSCBs are bonds issued by the Authority, the proceeds of which are used to finance certain eligible public schools' renovation and rehabilitation projects, equipment purchases, new building construction, and land acquisition. The Series 2009 QSCB is structured as a tax credit bond under which 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 period the bond is outstanding. These credits compensate the bondholder for lending money to the Authority and function as partial payments of interest on the bonds. The Series 2010 QSCB is structured as a direct subsidy payment bond under which the holder of the bond is compensated with a semi-annual cash interest payment that is subsidized by the Federal Government. The Authority elects to receive the direct interest subsidy payments from the United States Treasury, and the loan agreements provide that the subsidy payments received by the Authority will then be transferred to the borrowers.

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.



Qualified School Construction Bonds Program Debt Ratings. As of the fiscal year ended June 30, 2013, the Authority's QSCB program is rated Aa2, AA, and AA by Moody's Investors Service, Inc., Standard & Poor's Ratings Service, and Fitch Ratings, respectively.

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/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 financial statements and 2) the notes to the financial statements. The basic financial statements consist of the Statement of Net Position; the Statement of Revenues, Expenses, and Changes in Net Position; and the Statement of Cash Flows.

The Statements of Net Position present the Authority's financial position at June 30, 2013, and June 30, 2012. The Statements of Revenues, Expenses, and Changes in Net Position portray the results of operations and the change in net position 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 public higher educational institutions and local governments on behalf of LEAs at the lowest possible cost, to repay debt timely, and to achieve the highest possible rating for its debt. During the fiscal year ended June 30, 2013, the Authority frequently entered the short-term market. 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 Position Summary (in thousands)			
	2013	2012	2011
Current assets	$ 195,192	$ 117,832	$ 129,786
Noncurrent assets	1,704,025	1,600,727	1,576,698
Total assets	1,899,217	1,718,559	1,706,484
Deferred outflows of resources	19,145	16,291	1,316
Current liabilities	78,461	79,296	100,783
Noncurrent liabilities	1,830,374	1,643,123	1,599,186
Total liabilities	1,908,835	1,722,419	1,699,969
Deferred inflows of resources	357	2,128	-
Net position (unrestricted)	$ 9,170	$ 10,303	$ 7,831

Note: The Authority owns no capital assets.

At June 30, 2013, current assets include $87,850,086 of unexpended bond proceeds and commercial paper that will fund approved higher education loans as compared to $15,242,698 at June 30, 2012, and $31,917,018 at June 30, 2011. During the fiscal year ended June 30, 2013, the Authority issued $437,720,000 in Higher Education Facilities Second Program bonds which were used to retire $163,345,386 of commercial paper proceeds with the remainder to be used to fund various project costs and costs of issuance. During the fiscal year ended June 30, 2012, the Authority did not issue any long-term debt. During the fiscal year ended June 30, 2011, the Authority issued $231,935,000 in Higher Education Facilities Second Program Bonds which were used to retire $220,366,027 of commercial paper proceeds with the remainder to be used to fund various project costs and costs of issuance. During the fiscal year June 30, 2011, the Authority issued $212,440,000 in QSCBs which were used to fund various project costs and costs of issuance.

Principal payments were made on the higher education outstanding long-term bonds in the amounts of $53,870,000 in 2013; $50,659,000 in 2012; and $47,493,000 in 2011. Deposits to the sinking fund for the QZABs were made in the amounts of $3,402,835 in 2013; $3,403,891 in 2012; and $3,463,796 in 2011. During the fiscal year ended June 30, 2012, the 1999 Series QZAB bonds were retired in the amount of $13,290,000, decreasing both the QZAB sinking fund balance and the balance of outstanding bonds. No QZAB bonds were retired during fiscal years 2013 or 2011. Deposits to the sinking fund for the QSCBs were made in the amounts of $23,459,099 in 2013; $23,074,545 in 2012; and $9,764,134 in 2011. No QSCB bonds were retired during the fiscal years 2013, 2012, or 2011.

Net position is available to fund ongoing operations and other expenses necessary to meet the goals of the Authority. Assets and liabilities increase and decrease together in correlation to the issuance and repayment of debt and the resulting loans.

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

	2013	2012	2011
Operating Revenues			
Revenue from loans	$62,496	$59,242	$57,310
Investment earnings	1,725	1,100	512
Total operating revenues	64,221	60,342	57,822
Operating Expenses			
Interest expense	61,005	58,011	55,355
Subsidy to borrowers	12,314	11,314	8,061
Other expenses	2,334	1,143	2,143
Total operating expenses	75,653	70,468	65,559
Operating loss	(11,432)	(10,126)	(7,737)
Nonoperating Revenues			
Federal subsidy on bonds	10,299	10,299	7,524
Total nonoperating revenues	10,299	10,299	7,524
Increase (decrease) in net position	$ (1,133)	$ 173	$ (213)

The Authority's operating revenues include revenue from loans in the form of administrative fees, interest on loans, and income earned on investments. Operating expenses include interest expense on outstanding bonds and commercial paper and administrative expenses. With the issuance of the 2012 Series Bonds, Revenue from Loans and Interest Expense both increased at approximately the same rate while Federal subsidy on bonds remained unchanged. The increase in the operating expenses, which was mainly from the issuance of the 2012 Series Bonds that caused other expenses to increase from the expensing of the related costs of issuance and the increased interest expense, was the major contributor to the decrease in operating income and change in net position.

For the fiscal years ended June 30, 2013, June 30, 2012, and June 30, 2011, the Authority elected to return the investment income that it earned on funds held by the Trustee and interest earned on unspent bond proceeds to its borrowers in the higher education facilities program as a subsidy in the form of a credit to amounts due on debt service from the borrowers.

Pursuant to the bond resolution for the QZABs, Sinking Fund payments are invested in the State Pooled Investment Fund ("SPIF"). SPIF rates for fiscal year ended June 30, 2013, ranged from 0.10% to 0.15%. Investment earnings related to the QZAB program are held by the Authority for the benefit of the LEAs participating in the program and credited to their individual debt service sinking fund payment on an annual basis. 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 are credited on a monthly basis to the amounts due on their individual debt service principal and interest payments.

Future Financing Activities

Higher Education Facilities Programs. As Tennessee continues into 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 and to produce degree and certificate holding work-ready citizens. A host of policy and environmental factors influence the demands for access and completion, and the means through which this demand will be met.

These factors include:

- Economic conditions in 2008 led to an enrollment bulge in Tennessee colleges and universities that rippled through 2010. University enrollment increased 7% from 2008 to 2010, while community college enrollment increased 22% in the same time period, the largest increase in more than two decades. These enrollment increases began to wane in 2011. Total enrollments declined 2.4% from 2011 to 2012, but they remain well above the levels before the economic downturn. Since 2007, enrollments have increased 8% at universities and 19% at community colleges.
- 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 2012-13, the Tennessee Lottery provided an estimated $312 million in scholarships to more than 102,000 students.

In January 2010, the Tennessee General Assembly enacted 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 that 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 include (1) a new funding formula that incorporates outcomes in lieu of enrollment; (2) a new Performance Funding program that focuses on quality assurance; and (3) the establishment of institutional mission statements or profiles that 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.

With the creation of CCTA, the importance of receiving training beyond high school became more significant. In 2008, 24.5% of Tennessee's working-age adults held a college degree, compared to the national average of 29.5%. To reach the national average educational attainment levels of 2008, Tennessee would have needed an additional 170,000 citizens with a bachelor's degree or higher, more than double the annual degree production of the state's public and private institutions at that time. Furthermore, the percentage of adults in the state with an associate's degree or some college in 2008 was 31.3%, in comparison with the national average of 37.9%. To reach the 2008 national average, Tennessee would have needed an additional 220,000 citizens with an associate's degree or higher. As of 2011, the percentage of adults in the state with a bachelor's degree or higher was 25.3% compared to the national rate of 30.1%. Those with an associate's degree or higher increased to 32.1%, while the national rate was 38.7%.

While Tennessee continues to trail the national rate, the gap has narrowed for adults with an associate's or bachelor's degree. The increased enrollment during the economic downturn years and the demand for advanced education and training put stress on the capital facilities at all campuses. As the State continues to promote educational attainment to its citizens, we anticipate an increased need for funding of various facilities through the Authority.

Higher Education Facilities Programs Change in Legislation. The definition of "Institution" was amended by Chapter 174, Public Laws of 2013. "Institution" means, as appropriate, (i) the University of Tennessee system, including all of its branches and divisions wherever located, and the services, programs and activities provided therein, and the Board of Trustees, in the aggregate, and (ii) the state university and community college system, including all of its constituent institutions wherever located (whether or not conferring degrees), and the services, programs and activities provided therein, and the Board of Regents, in the aggregate.

Qualified Zone Academy Bonds and Qualified School Construction Bonds Programs. The issuance of bonds within the QZAB and QSCB programs is limited to the amounts allocated by the federal government. At this time, the Authority does not anticipate further issuance of debt for the QZAB program due to economic and financial conditions and constraints. The QSCB program expired 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 Building, 505 Deaderick St., Nashville, Tennessee 37243-1402, visit our website at www.comptroller.tn.gov/TSSBA, or call (615) 747-5370.

TENNESSEE STATE SCHOOL BOND AUTHORITY
Statements of Net Position
June 30, 2013, and June 30, 2012

(Expressed in Thousands)

	June 30, 2013	June 30, 2012
ASSETS		
Current assets:		
Cash (Note 2)	$ 96,308	$ 22,715
Cash with fiscal agent (Note 2)	788	1,055
Fair value of derivatives (Notes 1 and 2)	357	2,128
Loans receivable (Notes 3 and 7)	84,492	79,843
Interest receivable (Note 3)	8,871	7,626
Federal subsidy receivable	3,004	3,004
Receivables for administrative fees (Note 3)	1,372	1,461
Total current assets	195,192	117,832
Noncurrent assets:		
Restricted cash (Notes 2 and 4)	26,421	96,238
Restricted investments (Notes 2 and 4)	111,696	82,585
Loans receivable (Notes 3 and 7)	1,565,908	1,421,904
Total noncurrent assets	1,704,025	1,600,727
Total assets	1,899,217	1,718,559
DEFERRED OUTFLOWS OF RESOURCES		
Derivatives - Forward Delivery Agreement (Notes 1 and 2)	66	-
Deferred amount on refunding	19,079	16,291
Total deferred outflows of resources	19,145	16,291
LIABILITIES		
Current liabilities:		
Accounts payable	315	21
Accrued liabilities	8,154	15,118
Fair value of derivatives (Notes 1 and 2)	66	-
Accrued interest payable	11,672	10,533
Unearned revenue (Note 6)	3,114	3,589
Bonds payable (Note 5)	55,140	50,035
Total current liabilities	78,461	79,296
Noncurrent liabilities:		
Unearned revenue (Note 6)	22	24
Commercial paper payable (Note 5)	209,429	253,676
Bonds payable (Note 5)	1,620,923	1,389,423
Total noncurrent liabilities	1,830,374	1,643,123
Total liabilities	1,908,835	1,722,419
DEFERRED INFLOWS OF RESOURCES		
Deferred inflow - derivatives (Notes 1 and 2)	357	2,128
Total deferred inflows of resources	357	2,128
NET POSITION		
Unrestricted	$ 9,170	$ 10,303

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

TENNESSEE STATE SCHOOL BOND AUTHORITY
Statements of Revenues, Expenses, and Changes in Net Position
For the Years Ended June 30, 2013, and June 30, 2012

(Expressed in Thousands)

	Year Ended June 30, 2013	Year Ended June 30, 2012
OPERATING REVENUES		
Revenue from loans	$62,496	$59,242
Investment earnings	1,725	1,100
Total operating revenues	64,221	60,342
OPERATING EXPENSES		
Interest expense-commercial paper	244	323
Interest expense-bonds	60,761	57,684
Loss on retirement of bonds	-	4
Subsidy to borrowers	12,314	11,314
Administrative expense	2,334	1,143
Total operating expenses	75,653	70,468
Operating loss	(11,432)	(10,126)
NONOPERATING REVENUES		
Federal subsidy on bonds	10,299	10,299
Total nonoperating revenues	10,299	10,299
Increase (decrease) in net position	(1,133)	173
NET POSITION		
Net position, July 1	10,303	7,831
Cumulative effect of a change in accounting principle (Note 1)	-	2,299
Net position, July 1, as restated	10,303	10,130
Net position, June 30	$ 9,170	$10,303

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

TENNESSEE STATE SCHOOL BOND AUTHORITY
Statements of Cash Flows
For the Years Ended June 30, 2013, and June 30, 2012

(Expressed in Thousands)

	Year Ended June 30, 2013	Year Ended June 30, 2012
CASH FLOWS FROM OPERATING ACTIVITIES		
Receipts from borrowers for administrative fees	$ 1,809	$ 367
Payment to suppliers	(947)	(1,147)
Receipts from borrowers to the interest rate reserve fund	613	502
Payments to borrowers from the interest rate reserve fund	(874)	(3)
Net cash provided by (used in) operating activities	601	(281)
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES		
Proceeds from sale of bonds	284,910	-
Proceeds from sale of refunding bonds	195,258	-
Proceeds from sale of commercial paper	123,000	97,000
Bond interest subsidy from federal government	10,299	10,299
Call premium paid	-	(4)
Bond issuance costs paid	(1,387)	-
Refunding bond proceeds placed in escrow	(194,700)	-
Principal paid - bonds and commercial paper	(221,117)	(69,922)
Interest paid - bonds and commercial paper	(61,722)	(59,191)
Subsidy to borrowers	(10,662)	(10,551)
Net cash provided by (used in) noncapital financing activities	123,879	(32,369)
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchases of investments	(68,666)	(38,531)
Proceeds from sales and maturities of investments	43,000	20,328
Interest received on investments	1,599	1,131
Loans issued	(241,132)	(287,814)
Loan escrow paid	-	(520)
Collections of loan principal	82,737	82,038
Interest received on loans	61,491	58,810
Collections of call premium	-	4
Refund to borrower	-	(601)
Net cash used in investing activities	(120,971)	(165,155)
Net increase (decrease) in cash	3,509	(197,805)
Cash, July 1	120,008	317,813
Cash, June 30	$123,517	$120,008

TENNESSEE STATE SCHOOL BOND AUTHORITY
Statements of Cash Flows (Continued)
For the Years Ended June 30, 2013, and June 30, 2012

(Expressed in Thousands)

	Year Ended June 30, 2013	Year Ended June 30, 2012
Reconciliation of cash to the Statement of Net Position:		
Cash	$ 96,308	$ 22,715
Cash with fiscal agent	788	1,055
Restricted cash	26,421	96,238
Cash, June 30	$123,517	$120,008
Reconciliation of operating income (loss) to net cash provided by (used in) operating activities:		
Operating income (loss)	$ (11,432)	$ (10,126)
Adjustments to reconcile operating income (loss) to net cash provided by (used in) operating activities:		
Investment earnings	(1,725)	(1,215)
Interest expense	61,005	58,007
Subsidy to borrowers	12,314	11,314
Interest income (loss) from loans	(69,857)	(58,162)
Changes in assets and liabilities:		
(Increase) decrease in receivables for administrative fees	89	(595)
Increase (decrease) in unearned revenue	10,207	496
Total adjustments	12,033	9,845
Net cash provided by (used in) operating activities	$ 601	$ (281)
Noncash investing activities:		
Increase in fair value of investments	$ 699	$ 264

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

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 of Tennessee'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 a majority of 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 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.

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 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 for the Higher Education and QZAB Programs are stated at fair value. Investments for the QSCB program will be held to maturity and are stated at amortized value.

Amortized Amounts

A. 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.

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

B. Unearned Revenue. 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 position as unearned revenue and is not amortized.

   The Authority requires the QSCB borrowers to prepay bondholder interest to the Debt Service Fund as outlined in the loan agreements. The interest of the Debt Service Fund is credited back to the borrower as bondholder interest payments are made. The prepaid interest is reported on the statement of net position as unearned revenue and is not amortized.

Change in Accounting Principle

The Authority implemented the Governmental Accounting Standards Board's Statement 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*, during the year ended June 30, 2013. As a result, the residual of all other elements in the statement of financial position was named as net position, rather than net assets.

Also, effective for periods beginning after December 15, 2012, the Authority adopted Statement Number 65 of the Governmental Accounting Standards Board, *Items Previously Reported as Assets and Liabilities*. It dictates that for periods beginning after December 15, 2012, deferred amounts on refunding should be recognized as deferred outflow/inflow on the statements of net position. Previously, bonds payable were reported net of the applicable unamortized bond discount or premium and the deferred amount if refunding. Beginning with the statements dated as of June 30, 2013, the unamortized deferred amount on refunding is shown on the statement of net position as a deferred outflow/inflow. The statement also required that cost of issuance be expensed instead of being amortized over the life of the bonds. Therefore, all unamortized costs were expensed. Since all unamortized costs of issuance were expensed, an adjusting entry to unearned revenue was also made to write off costs of issuance from that balance as well. The cumulative effect on net position, which includes the netting of the expensing of the unamortized cost of issuance and the writing off of the costs of issuance from unearned revenues, has been reported on the statement of revenues, expenses, and changes in net position for the period ending June 30, 2012. Amounts on the statement of net position and statement of revenues, expenses, and changes in net position have been restated for comparative purposes for the period ending June 30, 2012.

Note 2. Deposits and Investments

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, may 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 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 Treasurer's Report.* That report is available on the State's website at www.treasury.tn.gov.

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, 2013, the Authority has the following Higher Education and QZAB investments:

Investment	Maturity	Fair Value
U.S. Treasury Bills	July 11, 2013	$ 5,657,943
	October 31, 2013	3,438,347
U.S. Treasury Notes	August 15, 2014	3,945,479
	September 15, 2013	8,511,645
	October 15, 2013	23,736,792
	November 30, 2013	7,258,280
	November 30, 2014	4,075,602
Total Investments		$56,624,088

As of June 30, 2013, the Authority has the following QSCB investments:

Investment	Maturity	Amortized Value
U.S. Treasury Bonds	August 15, 2026	$12,877,203
	August 15, 2027	9,315,622
U.S. Treasury Securities:		
Agency Zeroes & Strips	August 15, 2026	18,073,367
Agency Zeroes & Strips	August 15, 2027	14,805,830
Total Investments		$55,072,022

As of June 30, 2012, the Authority had the following Higher Education and QZAB investments:

Investment	Maturity	Fair Value
U.S. Treasury Bill	December 6, 2012	$ 6,106,273
U.S. Treasury Notes	July 31, 2012	4,790,135
	September 15, 2013	8,548,110
	October 15, 2013	23,774,728
U.S. Government Supported Corporate Debt	September 28, 2012	4,111,789
	December 28, 2012	4,165,764
Total Investments		$51,496,799

As of June 30, 2012, the Authority had the following QSCB investments:

Investment	Maturity	Amortized Value
U.S. Treasury Bonds	August 15, 2026	$ 9,471,995
	August 15, 2027	4,567,242
U.S. Treasury Securities:		
Agency Zeroes & Strips	August 15, 2026	10,618,118
Agency Zeroes & Strips	August 15, 2027	6,431,216
Total Investments		$31,088,571

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 State's Investment Policy does not formally address interest rate risk. As a matter of practice, higher education investments are invested no longer than five years to reduce the interest rate risk. QZAB investments follow the guidelines in the Forward Delivery Agreements which are limited to six-month maturities so that interest rate risk is contained. The Authority's investments are specifically identified above.

Credit Risk

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. At June 30, 2013, and June 30, 2012, the Authority only invested in U.S. Government obligations, or obligations of which the principal and interest are guaranteed by the United States.

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, 2013, and June 30, 2012, 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, 2013, and June 30, 2012, the Authority only invested in U.S. Treasury securities, or obligations of which the principal and interest are guaranteed by the United States.

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 QZABs. 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 QZABs 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, 2013, $5,657,943 is invested through the Agreement. As of June 30, 2012, $4,790,135 was 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 QZABs. 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 QZABs 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, 2013, $7,258,280 is invested through the Agreement. As of June 30, 2012, $6,106,273 was 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 6/30/13 at fair value	$5,657,943	$7,258,280
Amount Invested in Agreement at 6/30/12 at fair value	$4,790,135	$6,106,273
Date of Deposits	Nov. 24, 2005 through 2020	Dec. 8, 2006 through 2020

For the fiscal year ended June 30, 2013, the Agreement for the 2004 QZABs has a negative fair value of $66,149, and the Agreement for the 2005 QZABs has a positive fair value of $357,449. The positive fair value is reported as a deferred inflow on the statement of net position, and the negative fair value is reported as a deferred outflow on the statement of net position. For the fiscal year ended June 30, 2012, the Agreement for the 2004 QZABs had a positive fair value of $422,423, and the Agreement for the 2005 QZABs had a positive fair value of $1,705,408. The Authority did not enter into these agreements as interest rate hedges. These positive fair values are reported as deferred inflows on the statement of net position. The Agreements were valued by an independent investment advisor using the parameters contained in the Agreements and prevailing market conditions and benchmark yields on June 30, 2013, upon which the fair values depend. Borrowers pay no interest on these bonds. The interest rate credit is established by the federal government. The 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 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, which addresses the consistent critical terms method for forward contracts. All terms of the required deposits and the 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 Agreement, the 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, 2013, the fair value of the State’s Agreements is a total positive value of $291,300. As of June 30, 2012, the fair value of the State’s Agreements was a total positive value of $2,127,831.

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 Second Financing Agreement (the “Agreement”) is dated November 1, 1997, and was amended and restated on May 9, 2013. Under the Agreement, the Authority agrees to finance construction projects for the Board of Trustees or the Tennessee Board of Regents. Annual financing charges payable under the Agreement 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, and the 2010 QSCBs, dated October 1, 2010. 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 dates 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; interest payment; and the costs of administering the program.

Note 4. Restricted Assets

Cash and Investments

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; 2009 Series A; and 2010 Series A and B Bonds, the Authority deposited funds into a debt service reserve account equal to the maximum semiannual debt service for those bonds. The Authority elected to establish a separate debt service reserve fund solely for the 2012 Series A, B, and C bonds with no current funding requirement.

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.

Higher Education Facilities Programs

A. Bonds. 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 QZABs 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 QSCBs 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) recommended 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, Series 2009, 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 2010 QSCBs were issued as direct subsidy payment bonds, a financial tool whereby the interest on the QSCBs is intended to be fully subsidized by the federal government. 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.

Notes to the Financial Statements (Continued)

Changes in debt payable for the years ended June 30, 2013, and 2012 are as follows (expressed in thousands):

	Balance July 1, 2012	Additions	Deletions	Balance June 30, 2013	Amounts Due Within One Year
Commercial paper	$ 253,676	$123,000	$167,247	$ 209,429	$ -
Bonds payable	$1,401,681	$437,724	$237,925	$1,601,480	$55,140
Less: unamortized bond discount	(268)	-	(238)	(30)	-
Add: unamortized bond premium	38,040	42,448	5,875	74,613	-
Add: call premium	4	-	4	-	-
Total bonds payable	$1,439,457	$480,172	$243,566	$1,676,063	$55,140

	Balance July 1, 2011	Additions	Deletions	Balance June 30, 2012	Amounts Due Within One Year
Commercial paper	$ 162,653	$ 97,000	$ 5,977	$ 253,676	$ -
Bonds payable	$1,465,630	$ -	$ 63,949	$1,401,681	$50,035
Less: unamortized bond discount	(312)	-	(44)	(268)	-
Add: unamortized bond premium	39,955	-	1,915	38,040	-
Add: call premium	-	4	-	4	-
Total bonds payable	$1,505,273	$ 4	$ 65,820	$1,439,457	$50,035

Bonds and commercial paper payable at June 30, 2013, and June 30, 2012, are as follows (expressed in thousands):

	June 30, 2013	June 30, 2012
Bonds Payable:		
1998 Refunding Series D at interest rates from 4.60% to 4.85% maturing to 2021 (original par - $33,540)	$ 0	$ 13,245
2004 Series A at interest rates from 4.00% to 4.50% maturing to 2026 (original par - $67,965)	0	46,586
2004 Series B at interest rates from 4.00% to 4.50% maturing to 2034 (original par - $60,575)	0	44,545

	June 30, 2013	June 30, 2012
2004 Series C (Federally Taxable) at interest rates from 4.25% to 5.50% maturing to 2034 (original par - $37,230)	1,375	29,150
2005 Series A at interest rates from 3.625% to 5.00% maturing to 2030 (original par - $100,540)	74,410	83,205
2005 Series B (Federally Taxable) at interest rates from 4.31% to 4.88% maturing to 2028 (original par - $30,960)	4,610	26,365
2006 Series A at interest rates from 4.00% to 4.60% maturing to 2036 (original par - $53,820)	6,780	42,505
2007 Series A at interest rates from 4.00% to 5.00% maturing to 2036 (original par - $33,730)	26,465	27,680
2007 Series B (Federally Taxable) at interest rates from 5.243% to 5.666% maturing to 2036 (original par - $14,040)	10,335	10,975
2007 Series C at interest rates from 4.00% to 5.00% maturing to 2032 (original par - $89,940)	83,730	84,080
2008 Series A at interest rates from 3.50% to 5.00% maturing to 2037 (original par - $118,530)	102,205	105,635
2008 Series B at interest rates from 4.00% to 5.50% maturing to 2038 (original par - $166,990)	144,445	150,270
2009 Series A at interest rates from 3.00% to 5.00% maturing to 2039 (original par - $109,905)	78,860	86,695
2010 Series A at interest rates from 3.00% to 5.00% maturing to 2040 (original par - $213,920)	191,415	200,110
2010 Series B at interest rates from 2.00% to 5.20% maturing to 2040 (original par - $18,015)	16,810	17,275
2012 Series A at interest rates from 0.18% to 5.00% maturing to 2042 (original par - $208,295)	206,055	0
2012 Series B (Federally Taxable) at interest rates from 0.40% to 3.845% maturing to 2042 (original par - $103,790)	102,650	0
2012 Refunding Series C at interest rates from 0.18% to 5.000% maturing to 2034 (original par - $125,635)	117,975	0
2001 Qualified Zone Academy Bonds non-interest bearing maturing in 2015 (original par - $11,330)	11,330	11,330

	June 30, 2013	June 30, 2012
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	177,000
2010 Qualified School Construction Bonds at an interest rate of 4.848% maturing in 2027 (original par - $212,440)	212,440	212,440
Total Par Amount of Bonds Payable	$1,601,480	$1,401,681
Plus: Unamortized Premium/Less Unamortized Discount	74,583	37,772
Call Premium	0	4
Net Bonds Payable	$1,676,063	$1,439,457
Commercial paper, at interest rates from 0.10% to 0.22%	$ 209,429	$ 253,676

Debt service requirements to maturity of the bonds payable at June 30, 2013, are as follows (expressed in thousands):

For the Year(s) Ending June 30	Principal	Interest	Total
2014	$ 55,140	$ 50,889	$ 106,029
2015	64,000	48,892	112,892
2016	53,500	46,662	100,162
2017	54,545	44,361	98,906
2018	58,510	42,097	100,607
2019-2023	314,270	172,732	487,002
2024-2028	650,825	111,837	762,662
2029-2033	175,760	59,381	235,141
2034-2038	114,385	27,161	141,546
2039-2042	60,545	5,156	65,701
Total	$1,601,480	$609,168	$2,210,648

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, 2013, and June 30, 2012, the Authority did not have a liability for arbitrage.

On August 1, 2012, the Authority issued three new series of bonds, 2012 Series A, B, and C. The 2012 Series A tax-exempt bond proceeds in the amount of $208,295,000 were issued to redeem $129,859,517 of the Authority's tax-exempt commercial paper and $13,659,450 of the Authority's taxable commercial paper. The 2012 Series B taxable bond proceeds in the amount of $103,790,000 were issued to redeem $19,826,419 of the Authority's taxable commercial paper and to advance refund $26,455,000 of the 2004 Series C bonds and $19,595,000 of the 2005 Series B bonds. The balance of the proceeds of the 2012 Series A and B was used to pay for new construction projects and various costs of issuance. The 2012 Series C tax-exempt bond proceeds in the amount of $125,635,000 were issued to current refund $13,245,000 of the 1998 Series D bonds, $46,590,000 of the 2004 Series A bonds, and $44,545,000 of the 2004 Series B bonds and to advance refund $33,625,000 of the 2006 Series A bonds. The 2012 Series B refunding resulted in a difference between the reacquisition price and the net carrying amount of the old debt of $5,240,767. This amount is reported as a deferred outflow from resources and is being charged to operations through the year 2028. The 2012 Series B refunding resulted in a reduction of total debt service payments of $5,505,925 over the next 16 years and an economic gain (difference between the present values of the old and new debt service payments) of $4,447,734.57. The 2012 Series C refunding resulted in a difference between the reacquisition price and the net carrying amount of the old debt of $6,233,558. This amount is reported as a deferred outflow from resources and is being charged to operations through the year 2034. The 2012 Series C refunding resulted in a reduction of total debt service payments of $22,076,213 over the next 22 years and an economic gain (difference between the present values of the old and new debt service payments) of $18,956,994.54. The funds provided for the advance refundings were placed in irrevocable refunding trust funds to pay the interest on the refunded bonds on each interest payment date to and including the respective redemption date and on the respective redemption, the redemption price then due on the refunded bonds.

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, 2013, the Authority did not have any bonds outstanding that were considered defeased.

Commercial Paper Program

The Authority issues short-term debt to finance certain capital projects for the State'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, 2013, $180,668,000 of tax-exempt commercial paper and $28,761,000 of taxable commercial paper are outstanding. At June 30, 2012, $214,328,000 of tax-exempt commercial paper and $39,348,000 of taxable commercial paper were 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 0.10% to 0.22% during the fiscal year. Interest is payable upon maturity.

The Authority currently has State Street Bank and Trust Company as its liquidity provider under a Credit Agreement with an expiry date of March 30, 2014, subject to extension and earlier termination. The total available commitment, including 45 days of accrued interest in the amount of $4,593,750, 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 the Financial Accounting Standards Board's *Accounting Standards Codification* (ASC) 275, *Risks and Uncertainties*, 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 years ended June 30, 2013, and 2012, are as follows (expressed in thousands):

	Balance July 1, 2012	Additions	Deletions	Balance June 30, 2013
Interest rate reserve fund	$1,166	$ 613	$ 873	$ 906
Other unearned revenue	2,447	2,206	2,423	2,230
Total unearned revenue	$3,613	$2,819	$3,296	$3,136

	Balance July 1, 2011	Additions	Deletions	Balance June 30, 2012
Interest rate reserve fund	$ 667	$ 502	$ 3	$1,166
Other unearned revenue	2,768	2,436	2,757	2,447
Total unearned revenue	$3,435	$2,938	$2,760	$3,613

Note 7. Loans Receivable Restatement

In fiscal year 2013, the decision was made to restate loans receivable for the fiscal year ended June 30, 2012, to include amounts previously reported as deferred charges and unearned revenue. When the Authority issues bonds to finance capital projects for the higher education institution and local governments, the principal amount of the loan differs from the actual amount of funds available for capital expenditures because the par amount of the bonds is adjusted by certain amounts (such as bond discount/premium and underwriters' fees) in order to arrive at the amount of bond proceeds available for capital expenditures. These discounts and premiums are amortized on a straight-line basis over the life of the related bond because the higher education institutions and the local governments either receive the benefit or bear the cost of this difference. These differences were previously reported as deferred charges of $33,562,000 and unearned revenue of $12,632,000. These differences are now included in loans receivable on the statement of net position.

Note 8. Subsequent Events

As of December 12, 2013, the Authority has $82,101,000 outstanding in tax-exempt commercial paper and $35,961,000 in taxable commercial paper. Between June 30, 2013, and December 12, 2013, the Authority has issued $45,000,000 in commercial paper to pay construction expenditures.

On November 6, 2013, the Authority issued the 2013 Series A bonds. The 2013 Series A tax-exempt bond proceeds in the amount of $149,130,000 were sold with an original issue premium of $14,036,286.39. The bond proceeds redeemed $132,991,992 of the Authority's tax-exempt commercial paper and $2,763,930 of the Authority's taxable commercial paper. A portion of a project funded under the 2013 Series Bonds was being funded with taxable commercial paper. With a change in scope and a review from bond counsel, it was decided that this project could be financed with tax-exempt bonds and was included in the 2013 Series A Bond issuance. The balance of the proceeds will be used to pay for construction costs of certain projects and various costs of issuance.

The September 15, 2013, federal interest subsidy payment for the 2010 QSCBs was reduced by 8.7%, or $448,010.47, as a part of the Budget Control Act of 2011. The sequestration reduction rate was applicable until the end of the federal fiscal year, September 30, 2013. On October 1, 2013, the Internal Revenue Service announced that federal subsidy payments will be cut by 7.2% during the 2014 federal fiscal year.

TENNESSEE STATE SCHOOL BOND AUTHORITY
Supplementary Schedules of Net Position - Program Level
June 30, 2013, and June 30, 2012

(Expressed in Thousands)

	June 30, 2013				June 30, 2012			
	Higher Education Facilities Programs	Qualified Zone Academy Bonds Program	Qualified School Construction Bonds Program	Total	Higher Education Facilities Programs	Qualified Zone Academy Bonds Program	Qualified School Construction Bonds Program	Total
ASSETS								
Current assets:								
Cash	$ 95,212	$ 124	$ 972	$ 96,308	$ 21,837	$ 138	$ 740	$ 22,715
Cash with fiscal agent	777	-	11	788	1,040	-	15	1,055
Fair value of derivatives	-	357	-	357	-	2,128	-	2,128
Loans receivable	57,262	2,930	24,300	84,492	52,612	2,930	24,301	79,843
Interest receivable	8,488	-	383	8,871	7,379	-	247	7,626
Federal subsidy receivable	-	-	3,004	3,004	-	-	3,004	3,004
Receivables for administrative fees	1,365	7	-	1,372	1,454	7	-	1,461
Total current assets	163,104	3,418	28,670	195,192	84,322	5,203	28,307	117,832
Noncurrent assets:								
Restricted cash	-	12,189	14,232	26,421	-	11,206	85,032	96,238
Restricted investments	43,708	12,916	55,072	111,696	40,600	10,896	31,089	82,585
Loans receivable	1,244,052	16,034	305,822	1,565,908	1,136,405	18,998	266,501	1,421,904
Total noncurrent assets	1,287,760	41,139	375,126	1,704,025	1,177,005	41,100	382,622	1,600,727
Total assets	1,450,864	44,557	403,796	1,899,217	1,261,327	46,303	410,929	1,718,559
DEFERRED OUTFLOWS OF RESOURCES								
Derivatives - Forward Delivery Agreement	-	66	-	66	-	-	-	-
Deferred amount on refunding	19,079	-	-	19,079	16,291	-	-	16,291
Total deferred outflows of resources	19,079	66	-	19,145	16,291	-	-	16,291
LIABILITIES								
Current liabilities:								
Accounts payable	315	-	-	315	21	-	-	21
Accrued liabilities	-	-	8,154	8,154	-	-	15,118	15,118
Fair value of derivatives	-	66	-	66	-	-	-	-
Accrued interest payable	8,520	-	3,152	11,672	7,381	-	3,152	10,533
Unearned revenue	906	1	2,207	3,114	1,166	2	2,421	3,589
Bonds payable	55,140	-	-	55,140	50,035	-	-	50,035
Total current liabilities	64,881	67	13,513	78,461	58,603	2	20,691	79,296
Noncurrent liabilities:								
Unearned revenue	15	7	-	22	15	9	-	24
Commercial paper payable	209,429	-	-	209,429	253,676	-	-	253,676
Bonds payable	1,187,572	43,911	389,440	1,620,923	956,073	43,910	389,440	1,389,423
Total noncurrent liabilities	1,397,016	43,918	389,440	1,830,374	1,209,764	43,919	389,440	1,643,123
Total liabilities	1,461,897	43,985	402,953	1,908,835	1,268,367	43,921	410,131	1,722,419
DEFERRED INFLOWS OF RESOURCES								
Deferred inflow - derivatives	-	357	-	357	-	2,128	-	2,128
Total deferred inflows of resources	-	357	-	357	-	2,128	-	2,128
NET POSITION								
Unrestricted	$ 8,046	$ 281	$ 843	$ 9,170	$ 9,251	$ 254	$ 798	$ 10,303

TENNESSEE STATE SCHOOL BOND AUTHORITY
Supplementary Schedules of Revenues, Expenses, and Changes in Net Position - Program Level
For the Years Ended June 30, 2013, and June 30, 2012

(Expressed in Thousands)

	Year Ended June 30, 2013				Year Ended June 30, 2012			
	Higher Education Facilities Programs	Qualified Zone Academy Bonds Program	Qualified School Construction Bonds Program	Total	Higher Education Facilities Programs	Qualified Zone Academy Bonds Program	Qualified School Construction Bonds Program	Total
OPERATING REVENUES								
Revenue from loans	$49,153	$ 15	$13,328	$62,496	$45,894	$ 20	$13,328	$59,242
Investment earnings (loss)	247	39	1,439	1,725	398	(67)	769	1,100
Total operating revenues	49,400	54	14,767	64,221	46,292	(47)	14,097	60,342
OPERATING EXPENSES								
Interest expense-commercial paper	244	-	-	244	323	-	-	323
Interest expense-bonds	47,779	1	12,981	60,761	44,697	6	12,981	57,684
Loss on retirement of bonds	-	-	-	-	4	-	-	4
Subsidy to borrowers	392	-	11,922	12,314	253	-	11,061	11,314
Administrative expense	2,190	27	117	2,334	944	7	192	1,143
Total operating expenses	50,605	28	25,020	75,653	46,221	13	24,234	70,468
Operating income (loss)	(1,205)	26	(10,253)	(11,432)	71	(60)	(10,137)	(10,126)
NONOPERATING REVENUES								
Federal subsidy on bonds	-	-	10,299	10,299	-	-	10,299	10,299
Total nonoperating revenues	-	-	10,299	10,299	-	-	10,299	10,299
Increase (decrease) in net position	(1,205)	26	46	(1,133)	71	(60)	162	173
NET POSITION								
Net position, July 1	9,251	255	797	10,303	7,435	284	112	7,831
Cumulative effect of a change in accounting principle	-	-	-	-	1,745	30	524	2,299
Net position, July 1, as restated	9,251	255	797	10,303	9,180	314	636	10,130
Net position, June 30	$ 8,046	$281	$ 843	$ 9,170	$ 9,251	$254	$ 798	$10,303

TENNESSEE STATE SCHOOL BOND AUTHORITY
Supplementary Schedules of Cash Flows - Program Level
For the Years Ended June 30, 2013, and June 30, 2012

(Expressed in Thousands)

	Year Ended June 30, 2013				Year Ended June 30, 2012			
	Higher Education Facilities Programs	Qualified Zone Academy Bonds Program	Qualified School Construction Bonds Program	Total	Higher Education Facilities Programs	Qualified Zone Academy Bonds Program	Qualified School Construction Bonds Program	Total
CASH FLOWS FROM OPERATING ACTIVITIES								
Receipts from borrowers for administrative fees	$ 1,454	$ 14	$ 341	$ 1,809	$ -	$ 16	$ 351	$ 367
Payment to suppliers	(802)	(28)	(117)	(947)	(948)	(7)	(192)	(1,147)
Receipts from borrowers to the interest rate reserve fund	613	-	-	613	502	-	-	502
Payments to borrowers from the interest rate reserve fund	(874)	-	-	(874)	(3)	-	-	(3)
Net cash provided by (used in) operating activities	391	(14)	224	601	(449)	9	159	(281)
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES								
Proceeds from sale of bonds	284,910	-	-	284,910	-	-	-	-
Proceeds from the sale of refunding bonds	195,258	-	-	195,258	-	-	-	-
Proceeds from sale of commercial paper	123,000	-	-	123,000	97,000	-	-	97,000
Bond interest subsidy from federal government	-	-	10,299	10,299	-	-	10,299	10,299
Call premium paid	-	-	-	-	(4)	-	-	(4)
Bond issuance costs paid	(1,387)	-	-	(1,387)	-	-	-	-
Refunding bond proceeds placed in escrow	(194,700)	-	-	(194,700)	-	-	-	-
Principal paid - bonds and commercial paper	(221,117)	-	-	(221,117)	(56,632)	(13,290)	-	(69,922)
Interest paid - bonds and commercial paper	(48,742)	-	(12,980)	(61,722)	(46,210)	-	(12,981)	(59,191)
Subsidy to borrowers	(363)	-	(10,299)	(10,662)	(252)	-	(10,299)	(10,551)
Net cash provided by (used in) noncapital financing activities	136,859	-	(12,980)	123,879	(6,098)	(13,290)	(12,981)	(32,369)
CASH FLOWS FROM INVESTING ACTIVITIES								
Purchases of investments	(19,713)	(25,465)	(23,488)	(68,666)	-	(16,714)	(21,817)	(38,531)
Proceeds from sales and maturities of investments	19,516	23,484	-	43,000	976	19,352	-	20,328
Interest received on investments	313	478	808	1,599	349	368	414	1,131
Loans issued	(170,967)	-	(70,165)	(241,132)	(114,984)	-	(172,830)	(287,814)
Loan escrow paid	-	-	-	-	(520)	-	-	(520)
Collections of loan principal	57,989	2,485	22,263	82,737	56,629	3,021	22,388	82,038
Interest received on loans	48,725	-	12,766	61,491	46,156	-	12,654	58,810
Collections of call premium	-	-	-	-	4	-	-	4
Refund to borrower	-	-	-	-	-	(601)	-	(601)
Net cash provided by (used in) investing activities	(64,137)	982	(57,816)	(120,971)	(11,390)	5,426	(159,191)	(165,155)
Net increase (decrease) in cash	73,113	968	(70,572)	3,509	(17,937)	(7,855)	(172,013)	(197,805)
Cash, July 1	22,877	11,344	85,787	120,008	40,814	19,199	257,800	317,813
Cash, June 30	$ 95,990	$12,312	$15,215	$123,517	$ 22,877	$11,344	$ 85,787	$120,008
Reconciliation of cash to the Statement of Net Position:								
Cash	$ 95,213	$ 123	$ 972	$ 96,308	$ 21,837	$ 138	$ 740	$ 22,715
Cash with fiscal agent	777	-	11	788	1,040	-	15	1,055
Restricted cash	-	12,189	14,232	26,421	-	11,206	85,032	96,238
Cash, June 30	$ 95,990	$12,312	$15,215	$123,517	$ 22,877	$11,344	$ 85,787	$120,008
Reconciliation of operating income (loss) to net cash provided by (used in) operating activities:								
Operating income (loss)	$ (1,205)	$ 25	$(10,252)	$ (11,432)	$ 71	$ (60)	$ (10,137)	$ (10,126)
Adjustments to reconcile operating income (loss) to net cash provided by (used in) operating activities:								
Investment earnings	(246)	(39)	(1,440)	(1,725)	(398)	(48)	(769)	(1,215)
Interest expense	48,023	1	12,981	61,005	45,020	6	12,981	58,007
Subsidy to borrowers	392	-	11,922	12,314	253	-	11,061	11,314
Interest income (loss) from loans	(56,876)	-	(12,981)	(69,857)	(45,298)	117	(12,981)	(58,162)
Changes in assets and liabilities:								
(Increase) decrease in receivables for administrative fees	89	-	-	89	(595)	-	-	(595)
Increase (decrease) in unearned revenue	10,214	(1)	(6)	10,207	498	(6)	4	496
Total adjustments	1,596	(39)	10,476	12,033	(520)	69	10,296	9,845
Net cash provided by (used in) operating activities	$ 391	$ (14)	$ 224	$ 601	$ (449)	$ 9	$ 159	$ (281)
Noncash investing activities:								
Increase (decrease) in fair value of investments	$ 107	$ -	$ 592	$ 699	$ (41)	$ -	$ 305	$ 264

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Independent Auditor's Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance With *Government Auditing Standards*

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

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, 2013, and the related notes to the financial statements, which collectively comprise the Authority's basic financial statements, and have issued our report thereon dated December 13, 2013. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

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

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Authority's financial statements are free from 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 *Government Auditing Standards*.

Purpose of this Report

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

Deborah V. Loveless

Deborah V. Loveless, CPA
Director
December 13, 2013