CITY OF ELIZABETHTON ELECTRIC DEPARTMENT

AN ENTERPRISE FUND OF THE CITY OF ELIZABETHTON, TENNESSEE

FINANCIAL STATEMENTS AND SUPPLEMENTAL INFORMATION

WITH

INDEPENDENT AUDITORS' REPORT

For the Fiscal Year Ended June 30, 2010

CITY OF ELIZABETHTON ELECTRIC DEPARTMENT
AN ENTERPRISE FUND OF THE CITY OF ELIZABETHTON, TENNESSEE
TABLE OF CONTENTS
For the Fiscal Year Ended June 30, 2010

SECTION I

FINANCIAL SECTION

Blackburn, Childers & Steagall, PLC

CERTIFIED PUBLIC ACCOUNTANTS AND CONSULTANTS

REGIONAL EXPERTISE - LOCAL SERVICE

American Institute of Certified Public Accountants

INDEPENDENT AUDITORS' REPORT

Honorable Mayor, City Council Members and
City Manager
City of Elizabethton Electric Department
Elizabethton, Tennessee 37643

We have audited the accompanying financial statements of the City of Elizabethton Electric Department, an enterprise fund of the City of Elizabethton, Tennessee, as of and for the year ended June 30, 2010, as listed in the table of contents. These financial statements are the responsibility of the City of Elizabethton, Tennessee's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards,* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As discussed in Note 1, the basic financial statements present only the City of Elizabethton Electric Department and do not purport to, and do not, present fairly the financial position of the City of Elizabethton, Tennessee, as of June 30, 2010, and the changes in its financial position and cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the City of Elizabethton Electric Department, an enterprise fund of the City of Elizabethton, Tennessee, as of June 30, 2010, and the changes in financial position and cash flows for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated December 20, 2010 on our consideration of the City of Elizabethton Electric Department'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 the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Johnson City	801B Sunset Drive, P.O. Box 3745, Johnson City, TN 37602-3745	(423) 282-4511	Fax (423) 283-4532
Kingsport	440 E. Sullivan Street, P.O. Box 1504, Kingsport, TN 37662-1504	(423) 246-1725	Fax (423) 247-6800
Greeneville	550 Tusculum Boulevard, Greeneville, TN 37745-3939	(423) 638-8516	Fax (423) 638-3361

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Management has omitted the management's discussion and analysis that accounting principles generally accepted in the United States of America require to be presented to supplement the basic financial statements. Such missing information, although not a required part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. Our opinion the basic financial statements is not affected by this missing information. Accounting principles generally accepted in the United States of America require that the other required supplemental information on pages 26 and 27 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquires 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.

Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise the City of Elizabethton Electric Department, an enterprise fund of the City of Elizabethton, Tennessee's financial statements as a whole. The supplemental schedules are presented for purposes of additional analysis and are not a required part of the financial statements. The supplemental schedules, except for the Ratio of Outstanding Debt by Type, Number of Electric Customers by Type, and Electricity Rates are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the Untied States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole. The Ratio of Outstanding Debt by Type, Number of Electric Customers by Type, and Electricity Rates have not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we do not express an opinion or provide any assurance on them.

Blackburn, Childers + Steagall, PLC
BLACKBURN, CHILDERS & STEAGALL, PLC

December 20, 2010

CITY OF ELIZABETHTON ELECTRIC DEPARTMENT
AN ENTERPRISE FUND OF THE CITY OF ELIZABETHTON, TENNESSEE
STATEMENT OF NET ASSETS
June 30, 2010

ASSETS	
Current Assets	
Cash on Hand	$ 17,157
Certificates of Deposit	3,361,342
Investments	20,033,153
Accounts Receivable	
Customer Service	2,557,218
Interest, Rents and Other	1,936,955
Allowance for Uncollectible Amounts	(202,504)
Due from Other Funds	135,448
Inventories	1,038,795
Total Current Assets	28,877,564
Non-Current Assets	
Capital Assets	
Cost	77,938,462
Accumulated Depreciation	(21,739,564)
Net Capital Assets	56,198,898
Other Assets	
Accounts Receivable - Customers - Energy Right	1,495,979
Due from Other Funds	68,802
Unamortized Bond Issue Costs (Net)	901,076
CSA Stockholder Loan	27,343
Total Other Assets	2,493,200
Total Non-Current Assets	58,692,098
TOTAL ASSETS	$ 87,569,662

(Continued)

CITY OF ELIZABETHTON ELECTRIC DEPARTMENT
AN ENTERPRISE FUND OF THE CITY OF ELIZABETHTON, TENNESSEE
STATEMENT OF NET ASSETS
June 30, 2010

LIABILITIES	
Current Liabilities	
Cash Overdraft	$ 243,338
Accounts Payable	2,934,232
Accrued Wages	85,185
Accrued Interest	383,469
Accrued Taxes	137,052
Bonds Payable	735,000
Compensated Absences	390,291
Due to Other Funds	13,958
Customer Deposits Payable from Restricted Cash	2,173,162
Other Current and Accrued Liabilities	85,267
Total Current Liabilities	7,180,954
Non-Current Liabilities	
Compensated Absences	489,446
Bonds Payable (Net of Deferred Funding Cost and Bond Discount)	37,800,311
OPEB Liability	205,823
Advance from TVA	1,592,086
Total Non-Current Liabilities	40,087,666
TOTAL LIABILITIES	47,268,620
NET ASSETS	
Invested in Capital Assets, Net of Related Debt	18,154,567
Unrestricted	22,146,475
TOTAL NET ASSETS	$ 40,301,042

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

CITY OF ELIZABETHTON ELECTRIC DEPARTMENT
AN ENTERPRISE FUND OF THE CITY OF ELIZABETHTON, TENNESSEE
STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS
For the Fiscal Year Ended June 30, 2010

OPERATING REVENUES	
Sales of Electric Energy	
Residential	$ 29,833,411
Small Lighting and Power	4,412,045
Large Commercial and Industrial	12,261,591
Street and Outdoor Lighting	857,402
Other Operating Revenues	1,843,758
Total Operating Revenues	49,208,207
OPERATING EXPENSES	
Operation	
Power Purchased from Tennessee Valley Authority	37,956,861
Other Operation Expenses	4,288,329
Maintenance	3,374,706
Provision for Depreciation	1,653,467
Tax and Tax Equivalents	454,772
Total Operating Expenses	47,728,135
Operating Income (Loss)	1,480,072
NONOPERATING REVENUES (EXPENSES)	
Interest on Invested Funds	108,062
Interest Expense	(877,369)
Amortization Expense	(44,360)
Total Nonoperating Revenues (Expenses)	(813,667)
Income Before Transfer	666,405
Transfer Out	(605,496)
Change in Net Assets	60,909
NET ASSETS, JULY 1, 2010	40,240,133
NET ASSETS, JUNE 30, 2010	$ 40,301,042

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

CITY OF ELIZABETHTON ELECTRIC DEPARTMENT
AN ENTERPRISE FUND OF THE CITY OF ELIZABETHTON, TENNESSEE
STATEMENT OF CASH FLOWS
For the Fiscal Year Ended June 30, 2010

CASH FLOWS FROM OPERATING ACTIVITIES	
Cash Received from Electric Sales	$ 46,238,107
Cash Received from City of Elizabethton, TN	646,864
Cash Received from Rentals and Other Sales	1,543,311
Cash Payments to Suppliers for Goods and Services	(46,347,420)
Cash Payments for Employee Services and Benefits	(183,822)
Cash Payments for Tax Equivalents	(258,093)
Cash Paid to Lender On Behalf of Energy Right Customers	(316,263)
Cash Received on Loans by Energy Right Customers	377,702
Net Cash Provided by (Used for) Operating Activities	1,700,386
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES	
Transfer to Other Fund	(605,496)
Net Cash Provided by (Used For) Noncapital Financing Activities	(605,496)
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES	
Acquisition and Construction of Capital Assets	(8,976,794)
Bond Issue Proceeds	20,585,000
Principal Paid on Revenue Bonds	(705,000)
Bond Issue Costs	(279,756)
Interest Paid on Revenue Bonds	(753,611)
Net Cash Provided by (Used For) Capital and Related Financing Activities	9,869,839
CASH FLOWS FROM INVESTING ACTIVITIES	
Interest on Certificates of Deposit	1,419
Purchase of Certificates of Deposit and Investments	(19,845,075)
Sale of Certificates of Deposit and Investments	4,631,420
Net Cash Provided by (Used for) Investing Activities	(15,212,236)
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(4,247,507)
CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR	4,264,664
CASH AND CASH EQUIVALENTS, END OF YEAR	$ 17,157

(Continued)

CITY OF ELIZABETHTON ELECTRIC DEPARTMENT
AN ENTERPRISE FUND OF THE CITY OF ELIZABETHTON, TENNESSEE
STATEMENT OF CASH FLOWS
For the Fiscal Year Ended June 30, 2010

Reconciliation of Operating Income (Loss) to Net Cash Provided by (Used for) Operating Activities:	
Operating Income (Loss)	$ 1,480,072
Adjustments	
Depreciation	1,759,881
Provision for Uncollectible Accounts	(35,395)
(Increase) Decrease in Assets	
(Increase) Decrease in Accounts Receivable-Customer	(57,163)
(Increase) Decrease in Accounts Receivable-Other	(766,397)
(Increase) Decrease in Inventories	(229,976)
Increase (Decrease) in Liabilities	
Increase (Decrease) in Accounts Payable	(912,707)
Increase (Decrease) in Other Liabilities	(7,549)
Increase (Decrease) in Compensated Absences	12,857
Increase (Decrease) in Cash Overdraft	243,338
Increase (Decrease) in OPEB Liability	108,351
Increase (Decrease) in Customer Deposits	43,535
Increase (Decrease) in Energy Right Loans	61,539
Net Cash Provided by (Used for) Operating Activities	$ 1,700,386
Reconciliation of Cash and Cash Equivalents to Statement of Net Assets	
Cash on Hand	$ 17,157
Total Cash and Cash Equivalents	$ 17,157

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

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

City of Elizabethton Electric Department (the Department) is a utility furnishing electrical power to Carter County and portions of other Upper East Tennessee counties. The Department purchases its electrical power from the Tennessee Valley Authority (TVA).

The Department is a fund of the City of Elizabethton, Tennessee. These financial statements include only the statements of the Department and not the City of Elizabethton, Tennessee, as a whole.

The financial statements of the Department have been prepared in conformity with accounting principles generally accepted in the United States of America as prescribed by the Governmental Accounting Standards Board. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. GASB statement No. 20 gives governments the option of applying all Financial Accounting Standards Board (FASB) statements and interpretations issued after November 30, 1989, to its proprietary funds, unless they conflict with or contradict GASB pronouncements. The City of Elizabethton, Tennessee has elected not to implement FASB statements and interpretations issued thereafter, unless they are adopted by GASB.

The Department does not have any net assets restricted via constraints. Accordingly, the Department's net assets are categorized as invested in capital assets, net of related debt and unrestricted. The unrestricted category includes the sinking fund which was established by the Department to set aside funds for payment of bonds related to capital improvements and extensions of the Department.

Basis of Accounting

"Basis of Accounting" refers to the timing of recognizing revenues and expenses in the financial statements. The accompanying financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. With the exception, as in previous years, unbilled utility revenue and purchased power used between the June 2010 meter reading date and June 30, 2010, are not reflected in the financial statements. Under the accrual basis of accounting, revenues and related assets are recognized when earned, and expenses are recognized when obligations are incurred regardless of the timing of related cash flows.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Operating Revenues and Expenses

Proprietary funds distinguish operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing connection. The principal operating revenues of the Department are charges to customers for sales and services. Operating expenses for the Department include the cost of sales and services, administrative expenses, amortization and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

Restricted Assets

The Department's restricted assets consist of cash on deposit in the amount of $2,173,162, which are restricted for the payment of customer deposits.

Deposits and Investments

Cash on the statement of cash flows includes cash on hand and demand deposits in local banks.

Various restrictions on deposits and investments, including repurchase agreements, are imposed by state statutes. These restrictions are summarized as follows.

DEPOSITS - All deposits with financial institutions must be collateralized in an amount equal to 105% of the market value of uninsured deposits.

INVESTMENTS - The Department is authorized to make direct investments in bonds, notes or treasury bills of the U. S. Government and obligations guaranteed by the U. S. Government or any of its agencies. These investments may not have a maturity greater than two years. The Department may make investments with longer maturities if it follows various restrictions established by state law. The Department is also authorized to make investments in the State Pooled Investment Fund and in repurchase agreements. Repurchase agreements must be approved by the State Director of Local Finance and executed in accordance with procedures established by the State Funding Board. Investments are reported at fair value.

Securities purchased under a repurchase agreement must be obligations of the U. S. Government or obligations guaranteed by the U. S. Government or any of its agencies. When repurchase agreements are executed, the purchase of the securities must be priced at least 2% below the market value of the securities on the day of purchase. No repurchase agreements existed as of June 30, 2010.

The carrying amount of the Department's deposits with financial institutions was $(243,338) and the financial institution balance was $1,963,125. Carrying amounts differ from the financial institution balances primarily due to outstanding checks and deposits in transit.

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Deposits and Investments (Continued)

All deposits are insured with FDIC insurance. Amounts in excess of FDIC coverage are secured by the financial institution through the State Collateral Pool.

Certificates of deposit with original maturities greater than 90 days are recorded as Certificates of Deposit with a balance of $3,361,342. These certificates are stated at cost which approximates fair value and are not included as cash and cash equivalents because the original maturity exceeds 90 days. At June 30, 3010, these are insured with FDIC insurance and the excess is secured by the financial institution through the State Collateral Pool. The Department does not have a policy for interest rate risk or credit risk other than pledging securities for amounts in excess of the FDIC coverage.

Investments

The Department invests funds in the State of Tennessee's Local Government Investment Pool and bond proceeds with an investment advisor. The Department's interest in the Investment Pool is recorded at fair market value and at June 30, 2010, funds were $597,154. This is included as Investments on the Statement of Net Assets. The total investment with the investment firm is recorded at fair value and is $19,435,999 at June 30, 2010 and is included as Investments on the Statement of Net Assets.

Disclosures Relating to Interest Rate and Credit Risk

Interest rate risk is the risk that changes in market interest rates will adversely affect the fair value of an investment. Generally, the longer the maturity of an investment, the greater the sensitivity of its fair value to changes in market interest rates. One of the ways that the Department manages its exposure to interest rate risk is by purchasing a combination of shorter term and longer term investments and by timing cash flows from maturities so that a portion of the portfolio is maturing or coming close to maturity evenly over time as necessary to provide the cash flow and liquidity needed for operations.

Credit risk is the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment. This is the measure by the assignment of a rating by a nationally recognized statistical rating organization. Presented below is the minimum rating required for each investment type.

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Deposits and Investments (Continued)

As of June 30, 2010, the Department had the following investments.

	Carrying Amount	Market Value
Local Government Investment Pool	$ 597,154	597,154
Bond Fund Investments		
Fixed Rate Agency Securities	4,865,602	4,865,602
Municipal Securities	7,570,619	7,570,619
Treasury Securities	6,999,778	6,999,778
Total Bond Fund Investments	19,435,999	19,435,999
Total Investments	$ 20,033,153	20,033,153

The Department's bond fund investments had the following credit risk structure as of June 30, 2010:

Investment Type	Moody's Credit Rating	Fair Value	Percent of Total
Fixed Rate Agency Securities			
Federal Home Loan Bank	Aaa/AAA	$ 4,865,602	25%
Municipal Securities			
Taxable Municipals	AA2	624,612	3%
Taxable Municipals	A1	1,001,170	5%
Taxable Municipals	Unrated	1,086,723	6%
Tax-free Municipals	Aaa/AAA	400,000	2%
Tax-free Municipals	AA1	1,410,206	7%
Tax-free Municipals	AA2	2,489,120	13%
Tax-free Municipals	Unrated	558,788	3%
		7,570,619	
Treasury Securities			
U.S. Treasury Bill	Unrated	6,999,778	36%
Total Bond Fund Investments		$ 19,435,999	

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Deposits and Investments (Continued)

The Department's investment maturities by type are as follows:

		Investment Maturities (in Years)			
Investment Type	Fair Value	Less than 1	1 - 5	6 - 10	More Than 10
Fixed Rate Agency Securities	4,865,602	3,061,344	1,804,258	-	-
Municipal Securities	7,570,619	6,946,007	624,612	-	-
Treasury Securities	6,999,778	6,999,778	-	-	-
Total Bond Fund Investments	$ 19,435,999	17,007,129	2,428,870	0	0

Inventories

Materials and supplies inventories are stated at average cost on a per item basis.

Capital Assets

Land, buildings, machinery and equipment, and electrical distribution systems are stated at historical cost. Expenses for maintenance and repairs, which do not improve or extend the life of the asset, are charged to expense as incurred. Interest incurred during the construction of large projects is reflected in the capitalized value of the project. The assets are being depreciated on the straight-line method over the useful lives per guidelines of the TVA. When property is retired or otherwise disposed of, its average cost, together with its cost of removal less salvage, is charged to accumulated depreciation; no gain or loss is recognized as per federal energy regulations. The depreciation expense for the year ended June 30, 2010 was $1,759,881 of which $106,414 was charged to transportation expense.

The estimated useful lives of the utility plant of the City of Elizabethton Electric Department are as follows:

Class Description	Estimated Useful Life
Buildings	50.2 years
Office Equipment	20.0 years
Transportation Equipment	5.0 to 10.0 years
Other Machinery and Equipment	12.5 to 20.0 years
Power Distribution Department	12.5 to 44.44 years

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Compensated Absences

Accumulated Sick Leave:
Prior to May 12, 2005, the policy was as follows:
Sick leave accumulates at the rate of one day each month after an employee has been on the payroll for ninety days. Also, sick leave accumulates from year to year to a maximum of one hundred and eighty (180) days or 1,440 hours. For those employees with more than 180 days or 1,440 hours accumulated as of July 1, 1993, the amount accumulated will be the maximum. On date of termination or retirement, an employee will be paid one hundred percent (100%) of accumulated days of sick leave. In fiscal year 1996, the Board agreed that employees may transfer sick days to other employees that suffer catastrophic sickness and exhaust their accumulated sick days.

Accumulated Vacation:
Employees earn various days of vacation based on the number of years of service. Employees with more than twenty (20) years of service are entitled to a maximum of twenty-five (25) days of vacation per year. A maximum of thirty (30) days of accumulated vacation may be carried to the next calendar year. Vacation time accumulated prior to January 1, 1978 is exempt from the carry-forward limitation and capped at that balance. At the end of December 31 of each year, accumulated vacation leave in excess of thirty (30) days may be paid in cash. All accumulated vacation leave will be paid upon separation of service. Also, one additional day will be given each year for a year’s service without a lost-time accident or without taking a day of sick leave.

A liability for compensated absences and related fringe benefits is reflected on the statement of net assets at June 30, 2010, in the amount of $879,737. The portion of this liability expected to be paid within one (1) year is classified as a current liability and the remainder as a long-term liability.

After May 12, 2005, the policy of the City of Elizabethton, Tennessee became effective. The policy is to permit employees to accumulate earned but unused vacation and sick pay benefits. No liability is recorded for unpaid accumulated sick leave earned after May 12, 2005. The sick hours earned and unused after May 12, 2005 are added towards years of service when determining retirement eligibility. Vacation pay is accrued when earned.

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Power Contract

The Department has a power contract with the TVA whereby the Department purchases all its electric power from TVA and is subject to certain restrictions and conditions as provided in the contract. Either party may terminate this contract upon not less than five years prior written notice.

Budgets

The City of Elizabethton Electric Department is not required to demonstrate statutory compliance with budgets. Accordingly, budgetary data is not included in the financial statements. All budgets are prepared in accordance with bond covenants. Unexpended appropriations lapse at year end.

Transfer

The City of Elizabethton Electric Department transferred $605,496 to the City of Elizabethton's general fund for a payment in lieu of taxes.

NOTE 2 - LITIGATION

The Department has claims against it as of June 30, 2010 and discovery is on-going. Additional contingencies include worker compensation claims that are being handled by an attorney chosen by the Tennessee Municipal League. The Department was one of seven TVA Power Distributors to pursue resolution of a number of issues with a telephone utility company. The major disagreements concerned payment of net attachment fees for 2008 and application of the formula for setting attachment fees for 2009 and going forward. Subsequent to year-end, a settlement was reached. Amounts due to the Department through the 2nd Quarter 2010 totaled $601,457.

NOTE 3 - RISK COVERAGE

The Department has provided for coverage of the risks of loss through the purchase of commercial insurance. The coverage has been approximately the same for the past three years and there have been no settlements in excess of coverage during the past three years.

NOTE 4 - ACCOUNTS RECEIVABLE

Accounts Receivable at year end were as follows:

Customer Service	$ 2,557,218
Rent	850,965
Interest	125,960
TVA	252,852
TML Reimbursement	490,980
Miscellaneous Billing	216,198
	4,494,173
Less: Allowance for Uncollectible Amounts	(202,504)
	$ 4,291,669

The allowance for uncollectible amounts is an estimate established by a review of account history and knowledge of the industry. Accounts are directly written off once all methods of collection have been exhausted.

NOTE 5 - POST-RETIREMENT BENEFITS OTHER THAN PENSIONS

A Brief Description of the Retiree Medical and Life Insurance Plan:

Plan Types:

The City of Elizabethton, Tennessee will pay up to the level of the single premium paid for full time city employees until the retiree reaches age 65. The actuarial valuation assumes the City will pay 97.7% of the single premium, which is the current level paid by the City for full-time employees.

The City of Elizabethton, Tennessee offers post-employment health care benefits to certain eligible employees. Full service eligible retirees are those age 60 or older with a minimum of 5 years of creditable city service at retirement, or retiring at any age with at least 30 years of service. Early retirees are those age 55 or older with a minimum 10 years of creditable city service at retirement, or retiring at any age with at least 25 years of service. For the Electric Department, there are 19 employees covered by this arrangement. The co-insurance rate of reimbursement depends on the plan the employee is covered by. The base plan has a $1,500 deductible and out-of-pocket max of $3,000 with an 80% co-insurance rate. The buy up plan has a $750 deductible and out-of pocket max of $1,500 with an 80% co-insurance rate. During the fiscal year ending June 30, 2010, contributions received from employees was $87,924 and contributions received from retirees were $2,682.

NOTE 5 - POST-RETIREMENT BENEFITS OTHER THAN PENSIONS (CONTINUED)

Funding Policy:

The contribution requirements of plan members are based on pay-as-you go financing requirements.

Annual OPEB Cost and Net OPEB Obligation:

The Electric Department's other postemployment benefit (OPEB) cost (expense) is calculated based on the annual required contribution of the employer (ARC), an amount actuarially determined in accordance with the parameters of GASB Statement 45. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and amortize any unfunded actuarial liabilities (of funding excess) over a period not to exceed thirty years. The following table shows the components of the Electric Department's costs for the year, the amount actually contributed to the plan, and changes in the Electric Department's OPEB obligation.

Annual OPEB Cost and Net OPEB Obligation	
Annual Required Contribution (ARC)	$ 184,288
Interest on Net OPEB Obligation	-
Adjustment to ARC	-
Annual OPEB Cost (Expense)	184,288
Contribution Made (assumed end of year)	75,937
Increase in Net OPEB Obligation	108,351
Net OPEB Obligation - Beginning of Year	97,472
Net OPEB Obligation - End of Year	$ 205,823

The annual OPEB cost, the percentage of annual OPEB cost contributed to the plan, and the net OPEB obligation for fiscal years 2010 and 2009 are as follows:

Fiscal Year Ending	Annual OPEB Cost	Percentage Annual OPEB Cost Contributed	Net OPEB Obligation
6/30/2010	$ 184,288	41%	$ 205,823
6/30/2009	$ 184,288	48%	$ 97,472

NOTE 5 - POST-RETIREMENT BENEFITS OTHER THAN PENSIONS (CONTINUED)

Funded Status and Funding Progress:

As of June 30, 2009, the most recent actuarial valuation date, the plan was not funded. The actuarial accrued liability for benefits was $2,212,211. The covered payroll was $2,547,707 and the ratio of the unfunded actuarial accrued liability (UAAL) to the covered payroll was 87%. The funding ratio is 0%.

Actuarial valuations of an ongoing plan involved estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the healthcare cost trend. Amounts determined regarding the funded status of the plan and the annual required contributions of the employer are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future. The schedule of funding progress, presented as required supplementary information following the notes to the financial statements, presents trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liabilities for benefits.

Actuarial Methods and Assumptions:

Projects of benefits for financial reporting purposes are based on the substantive plan (the plan as understood by the employer and the plan members) and include the types of benefits provided at the time of each valuation and the historical pattern of sharing of benefit costs between the employer and plan members to that point. The actuarial methods and assumptions used include techniques that are designed to reduce the effects of short-term volatility in actuarial accrued liabilities and the actuarial value of assets, consistent with the long-term perspective of the calculations. The following methods and assumptions were used.

The valuation date is July 1, 2008 and year 1 represents the period of July 1, 2008 to June 30, 2009. A discount rate of 4.5% was used to discount expected liabilities to the valuation dates. This is the approximate rate of return available on A rated municipal bonds with maturities of 30 years as of December 27, 2007. Future salaries are expected to increase at an annual rate of 3.0%. Average health care trend costs rates are assumed to increase by 15% (year 1), 13% (year 2), 11% (year 33), 10% (year 4), 9% (year 5), 8% (year 6), 7% (year 7), 6% (year 8) and 5.5% for years 9 and subsequent. The ARC was calculated using the level dollar amortization method, amortizing costs over 30 years on a closed basis.

NOTE 6 - RETIREMENT COMMITMENTS

On October 1, 2005, the Department withdrew from the CSA Non Governmental Plan in a spin off whereby assets and liabilities were transferred into the Central Service Association Pension Plan for Governmental Employees. This is a new tax-qualified multiple employer defined benefit pension plan that is maintained as a governmental plan (as defined under section 414(d) of the Internal Revenue Code).

The plan covers all employees over 21 years of age with six months of service. The total contribution by both the Employer and Employees for the plan year ended September 30, 2009 and 2008 were $703,981 and $615,518. The recommended contribution was $818,112 and $798,324 for the plan years October 1, 2009 and 2008 respectively. Covered employees are required to contribute one and one-half (1 ½) percent of their monthly earnings to the plan. The Department is required to contribute the remaining amount necessary to fund pension cost accrued including amortization of unfunded prior service cost over a period not to exceed thirty (30) years. Any changes to the plan would need to be approved by the Board for the Department and CSA. The investment assumption is 7%, salary assumption is 4%, the actuarial method is the frozen entry age method and the amortization period is 21.

Monthly contributions are made based on an annual evaluation for the following plan year. The most recently completed Actuarial Report was for the plan year beginning October 1, 2009. The total plan liability for the 2009 plan year was $16,897,483 and the actuarial value of assets $9,180,054 leaving an unfunded liability of $7,717,429 and a funded ratio of 54.33%. The total plan liability for the 2008 year was $16,901,466 and the actuarial value of plan assets was $9,233,359, leaving an unfunded liability of $7,668,107 and a funded ratio of 54.64%. The total plan liability for the 2007 plan year was $15,840,429 and the actuarial value of plan assets was $9,515,599, leaving an unfunded liability of $6,324,830 and a funded ratio of 60.07%.

As of October 1, 2009, the pension benefit obligation is $16,897,483 and was $16,901,466 as of October 1, 2008.

The plan provides for a retirement date, which is the first day of the calendar month, which coincides with, or next follows the employee's 60th birthday, with a minimum of 30 years of service. Early retirement may be taken within ten years of the retirement date. Benefits are determined on credited service, earnings, marital status and choice of options.

The Central Service Association Defined Benefit Plan operates with assistance from Mass Mutual. Mass Mutual holds all of the assets in a wide range of diverse investment funds. Additional information may be obtained from Central Service Association, P.O. Box 3480, 93 South Coley Road, Tupelo, MS 38803-3480.

Effective January 12, 2007, the Department elected to discontinue enrolling new employees in the CSA Pension Plan Program as now, employees will be enrolled with the same retirement plan as the City of Elizabethton, Tennessee with the Tennessee Consolidated Retirement System.

NOTE 6 - RETIREMENT COMMITMENTS (CONTINUED)

The schedule of funding progress, presented as required supplementary information (RSI) following the notes to the financial statements, present multiyear trend information about whether the actuarial values of plan assets are increasing or decreasing over time relative to the actuarial accrued liability for benefits.

Actuarial Valuation Date	Actuarial Value of Assets	Actuarial Accrued Liability (AAL)	(UAAL) Unfunded AAL	Funded Ratio	Covered Payroll	UAAL as a Percentage of Covered Payroll
10/1/2009	$ 9,180,054	$ 16,897,483	$ 7,717,429	54.33%	$ 2,076,560	372%
10/1/2008	$ 9,233,359	$ 16,901,466	$ 7,668,107	54.64%	$ 2,303,866	283%
10/1/2007	$ 9,515,599	$ 15,840,429	$ 6,324,830	60.07%	$ 2,471,352	198%

The employees of the Department, along with employees of the City of Elizabethton, Tennessee are members of the Political Subdivision Pension Plan (PSPP), an agent multiple-employer defined benefit pension plan administered by the Tennessee Consolidated Retirement System (TCRS). TCRS provides retirement benefits as well as death and disability benefits. Benefits are determined by a formula using the member's high five-year average salary and years of service. Members become eligible to retire at the age of 60 with five years of service or at any age with 30 years of service. A reduced retirement benefit is available to vested members at the age of 55. Disability benefits are available to active members with five years of service who become disabled and cannot engage in gainful employment. There is no service requirement for disability that is the result of an accident or injury occurring while the member was in the performance of duty. Members joining the system after July 1, 1979 become vested after five years of service and members joining prior to July 1, 1979 were vested after four years of service. Benefit provisions are established in state statute found in Title 8, Chapter 34-37 of the Tennessee Code Annotated (TCA). State statutes are amended by the Tennessee General Assembly. Political subdivisions such as Elizabethton participate in the TCRS as individual entities and are liable for all costs associated with the operation and administration of their plan. Benefit improvements are not applicable to a political subdivision unless approved by the chief governing body.

The TCRS issues a publicly available financial report that includes financial statements and required supplementary information for the PSPP. That report may be obtained by writing to Tennessee Treasury Department, Consolidated Retirement System, 10th Floor Andrew Jackson Building, Nashville, TN 37243-0230 or can be accessed at http://treasury.state.tn.us/tcrs/PS/.

The Department is a fund of the City of Elizabethton, Tennessee and no specific pension benefit obligation can be isolated for the Department. Please refer to the City of Elizabethton, Tennessee as to aggregate funding status, progress, and net assets available for benefits.

NOTE 7 - CAPITAL ASSETS AND DEPRECIATION

	Beginning Balance	Increases	Decreases	Adjustments	Ending Balance
Capital assets, not being depreciated:					
Land	$ 595,994	-	-	(1,800)	594,194
Construction in Progress	13,176,637	5,124,667	-	-	18,301,304
Total capital assets, not being depreciated	13,772,631	5,124,667	-	(1,800)	18,895,498
Capital assets, being depreciated:					
Buildings	2,115,978	46,709	-	-	2,162,687
Office Equipment	589,532	25,773	(280)	-	615,025
Transportation Equipment	2,539,449	507,312	(147,239)	136,500	3,036,022
Other Machinery and Equipment	998,388	91,647	(11,591)	-	1,078,444
Transmission and Power Distribution System	50,229,550	2,691,479	(650,011)	(120,232)	52,150,786
Total capital assets, being depreciated	56,472,897	3,362,920	(809,121)	16,268	59,042,964
Less accumulated depreciation for:					
Buildings	(908,403)	(42,726)	-	-	(951,129)
Office Equipment	(249,646)	(30,187)	-	-	(279,833)
Transportation Equipment	(1,137,831)	(114,943)	159,108	-	(1,093,666)
Other Machinery and Equipment	(504,926)	(67,904)	-	-	(572,830)
Transmission and Power Distribution System	(18,462,847)	(1,504,121)	1,124,862	-	(18,842,106)
Total accumulated depreciation	(21,263,653)	(1,759,881)	1,283,970	-	(21,739,564)
Net Capital Assets being depreciated	35,209,244	1,603,039	474,849	16,268	37,303,400
Net Capital Assets	$ 48,981,875	6,727,706	474,849	14,468	56,198,898

NOTE 8 - LONG-TERM DEBT

The Electric Department issued $3,495,000 of Series 2005 Electric Department Revenue Refunding Bonds to provide resources that were placed in an irrevocable trust for the purpose of generating resources for the future debt service payments of $3,521,124 on the City's outstanding Series 1997 Department Revenue Bonds. As a result, the refunded bonds of $3,350,000 are considered to be defeased at June 30, 2006. The reacquisition price was more than the net carrying amount of the old debt by $145,000. This amount is being netted against the new debt and amortized over the remaining life of the refunded debt, which is the same as the life of the new debt issued in the basic financials. This advance refunding was undertaken to reduce the total debt service payments over the next seventeen years by $188,399 and resulted in an economic gain of $131,152.

During the June 30, 2008 year, there was a bond issue in the amount of $15,000,000 for improvements to the Department's electric distribution system. The bonds are secured by a pledge of the net revenues of the Department subject to the prior lien of the outstanding revenue refunding bonds (2005 issue). The Series 2007 Bonds were issued on December 27, 2007 for twenty years with an interest rate ranging from 4% to 5%. The bonds were issued at a premium, which along with the bond costs, are being amortized over the life of the bond on the straight line method.

During the June 30, 2010 year, there was another bond issue in the amount of $20,585,000 for additional improvements to the electric distribution and transmission system. The bonds, which are taxable Build America Bonds, mature September 2035 and carry an interest rate ranging from 1.75% to 6.25%. The full faith and credit of the City of Elizabethton, Tennessee is pledged. The bonds are also payable from and are secured by a pledge of the Net Revenues to be derived from the operation of the Electric Distribution System, subject to prior pledges of net revenues in favor of prior lien obligations. The bonds provide for a 35% federal subsidy on the total interest requirements which is paid semiannually corresponding with the interest payment dates to the bondholders. The interest requirements for this bond in the schedule of maturities are shown at the gross amount. The remaining federal subsidy totals $8,539,375 through the term of the bonds. The bonds were issued at a premium, which along with the bond costs, are being amortized over the life of the bond on the straight line method. Long-term liability activity for the year ended June 30, 2010 was as follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Revenue Bonds Payable - 2005	$ 3,280,000	-	(180,000)	3,100,000	185,000
Revenue Bonds Payable - 2007	15,000,000	-	(525,000)	14,475,000	550,000
Revenue Bonds Payable - 2010	-	20,585,000	-	20,585,000	-
Less Deferred Amount On Refunding	(76,284)	-	5,721	(70,563)	-
Add Deferred Amounts for Issuance Premium	181,477	556,213	(291,816)	445,874	-
Total Bonds Payable	18,385,193	21,141,213	(991,095)	38,535,311	735,000
OPEB Liability	97,472	184,288	(75,937)	205,823	
Compensated Absences	866,880	402,953	(390,096)	879,737	390,291
Total Long-term Liabilities	$19,349,545	21,728,454	(1,457,128)	39,620,871	1,125,291

NOTE 8 - LONG-TERM DEBT (CONTINUED)

Revenue bonds issued August 24, 2005 debt service requirements to maturity are as follows:

Fiscal Year Ending June 30	Principal	Interest	Total
2011	$ 185,000	119,764	304,764
2012	190,000	112,733	302,733
2013	200,000	105,170	305,170
2014	205,000	97,070	302,070
2015	215,000	88,670	303,670
2016-2020	1,230,000	305,508	1,535,508
2021-2023	875,000	54,938	929,938
	$ 3,100,000	883,853	3,983,853

Revenue bonds issued December 27, 2007 debt service requirements to maturity are as follows:

Fiscal Year Ending June 30	Principal	Interest	Total
2011	$ 550,000	617,600	1,167,600
2012	570,000	595,200	1,165,200
2013	595,000	571,900	1,166,900
2014	620,000	547,600	1,167,600
2015	645,000	519,075	1,164,075
2016-2020	3,695,000	2,102,425	5,797,425
2021-2025	4,545,000	1,248,375	5,793,375
2026-2028	3,255,000	224,213	3,479,213
	$14,475,000	6,426,388	20,901,388

NOTE 8 - LONG-TERM DEBT (CONTINUED)

Revenue bonds issued April 20, 2010 debt service requirements to maturity are as follows:

Fiscal Year Ending June 30	Principal	Interest	Total
2011	$ -	991,497	991,497
2012	-	1,185,844	1,185,844
2013	130,000	1,184,706	1,314,706
2014	135,000	1,181,965	1,316,965
2015	140,000	1,178,350	1,318,350
2016-2020	760,000	5,812,469	6,572,469
2021-2025	1,510,000	5,594,884	7,104,884
2026-2030	5,250,000	4,828,909	10,078,909
2031-2035	10,335,000	2,366,937	12,701,937
2036	2,325,000	72,656	2,397,656
	$20,585,000	24,398,217	44,983,217

Total debt service requirements to maturity for revenue bonds are as follows:

Fiscal Year Ending June 30	Principal	Interest	Total
2011	$ 735,000	1,728,861	2,463,861
2012	760,000	1,893,777	2,653,777
2013	925,000	1,861,776	2,786,776
2014	960,000	1,826,635	2,786,635
2015	1,000,000	1,786,095	2,786,095
2016-2020	5,685,000	8,220,402	13,905,402
2021-2025	6,930,000	6,898,197	13,828,197
2026-2030	8,505,000	5,053,122	13,558,122
2031-2035	10,335,000	2,366,937	12,701,937
2036	2,325,000	72,656	2,397,656
	$38,160,000	31,708,458	69,868,458

NOTE 9 - INTERFUND ACTIVITY

As described in Note 1, the Department is a self-supporting fund of the City of Elizabethton, Tennessee (City). In the normal course of operations, the Department provides electrical service to the City at standard electric rates which generated revenues of approximately $705,295 in 2010. As of June 30, 2010, $135,448 was receivable from the City for electrical services. Payment is due within approximately 30 days of the billing. These transactions were consummated on terms equivalent to those that prevail in arm's length transactions.

The Department made tax equivalent payments to the City of $605,496 in 2010. These payments are based on the Department's property, plant and equipment, along with average operating revenues less power costs.

In October 2004, the Department and the City of Elizabethton entered into an agreement where the Department would install a lighting system at the Twins baseball field. The terms of this agreement are for the City to pay the Department monthly payments of $1,337 which includes interest. The interest rate is a fixed interest rate of current prime rate plus 2% (as of July 1 of each year) and shall not exceed 7%. The period is for 120 months. The total amount at inception was $116,436. At June 30, 2010, the total amount due from the City of Elizabethton is $68,802.

NOTE 10 - OTHER MATTERS

The Department is a member of a cooperative, Central Service Association (CSA), consisting of several utilities in seven states. Normally, excess collections are allocated to the members and repaid in the form of credit memos in the following fiscal year.

Due to a settlement in fiscal year 2003, excess collections were higher than expected; however, the Board of Directors for CSA has projected deficits for future years due to the purchase of a Customer Information Department.

Therefore, special conditions have been adopted by CSA's Board as follows:

- The 2003 allocation will be accounted for separately and reduced as project expenses are recognized.
- Principal repayment of the 2003 allocation will not be required to begin repayment until all project expenses are fully recognized.
- Repayments of the 2003 allocation will be in the form of credit memos.

The Department's share is $15,919. This will be recognized by the Department as it is realized net of project costs.

NOTE 11 - COMMITTMENTS

The Department has active construction projects as of June 30, 2010 for substations and transmission lines. At year-end, the Department's commitments for the projects total approximately $9,700,000.

SECTION II

SUPPLEMENTAL INFORMATION

CITY OF ELIZABETHTON ELECTRIC DEPARTMENT
AN ENTERPRISE FUND OF THE CITY OF ELIZABETHTON, TENNESSEE
SCHEDULE OF FUNDING PROGRESS - UNAUDITED
For the Fiscal Year Ended June 30, 2010

Actuarial Valuation Date	Actuarial Value of Assets	Actuarial Accrued Liability (AAL)	(UAAL) Unfunded AAL	Funded Ratio	Covered Payroll	UAAL as a Percentage of Covered Payroll
10/1/2009	$ 9,180,054	$ 16,897,483	$ 7,717,429	54.33%	$ 2,076,560	372%
10/1/2008	$ 9,233,359	$ 16,901,466	$ 7,668,107	54.64%	$ 2,303,866	283%
10/1/2007	$ 9,515,599	$ 15,840,429	$ 6,324,830	60.07%	$ 2,471,352	198%

See independent auditors’ report.

CITY OF ELIZABETHTON ELECTRIC DEPARTMENT
AN ENTERPRISE FUND OF THE CITY OF ELIZABETHTON, TENNESSEE
SCHEDULE OF FUNDING PROGRESS OF POST RETIREMENT BENEFITS
OTHER THAN PENSIONS - UNAUDITED
For the Fiscal Year Ended June 30, 2010

Actuarial Valuation Date	Actuarial Value of Assets	Actuarial Accrued Liability (AAL)	(UAAL) Unfunded AAL	Funded Ratio	Covered Payroll	UAAL as a Percentage of Covered Payroll
7/1/2008	$ -	$ 2,212,211	$ 2,212,211	0.00%	$ 2,547,707	87%

Note: Data not available for the preceding two years.

See independent auditors' report.

CITY OF ELIZABETHTON ELECTRIC DEPARTMENT
AN ENTERPRISE FUND OF THE CITY OF ELIZABETHTON, TENNESSEE
SCHEDULE OF BOND PRINCIPAL AND INTEREST REQUIREMENTS
June 30, 2010

Schedule 1

Fiscal Year Ending	Principal	Interest	Total Requirements
6/30/2011	$ 735,000	1,728,861	2,463,861
6/30/2012	760,000	1,893,777	2,653,777
6/30/2013	925,000	1,861,776	2,786,776
6/30/2014	960,000	1,826,635	2,786,635
6/30/2015	1,000,000	1,786,095	2,786,095
6/30/2016	1,045,000	1,739,923	2,784,923
6/30/2017	1,090,000	1,691,262	2,781,262
6/30/2018	1,140,000	1,643,651	2,783,651
6/30/2019	1,180,000	1,597,180	2,777,180
6/30/2020	1,230,000	1,548,386	2,778,386
6/30/2021	1,275,000	1,497,416	2,772,416
6/30/2022	1,330,000	1,443,129	2,773,129
6/30/2023	1,385,000	1,385,056	2,770,056
6/30/2024	1,440,000	1,321,154	2,761,154
6/30/2025	1,500,000	1,251,442	2,751,442
6/30/2026	1,565,000	1,178,350	2,743,350
6/30/2027	1,630,000	1,101,419	2,731,419
6/30/2028	1,700,000	1,020,591	2,720,591
6/30/2029	1,770,000	928,275	2,698,275
6/30/2030	1,840,000	824,487	2,664,487
6/30/2031	1,910,000	716,675	2,626,675
6/30/2032	1,985,000	602,212	2,587,212
6/30/2033	2,060,000	480,862	2,540,862
6/30/2034	2,145,000	352,031	2,497,031
6/30/2035	2,235,000	215,157	2,450,157
6/30/2036	2,325,000	72,656	2,397,656
	$ 38,160,000	31,708,458	69,868,458

See independent auditors' report.

CITY OF ELIZABETHTON ELECTRIC DEPARTMENT
AN ENTERPRISE FUND OF THE CITY OF ELIZABETHTON, TENNESSEE
ADDITIONS AND RETIREMENTS TO UTILITY PLANT
June 30, 2010

Schedule 2

		Balance June 30, 2009	Additions	Retirements	Adjustments	Balance June 30, 2010
Land	$	595,994	-	-	(1,800)	594,194
Buildings		2,115,978	46,709	-	-	2,162,687
Office Equipment		589,532	25,773	(280)	-	615,025
Transportation Equipment		2,539,449	507,312	(147,239)	136,500	3,036,022
Other Machinery and Equipment		998,388	91,647	(11,591)	-	1,078,444
Transmission and Power Distribution System		50,229,550	2,691,479	(650,011)	(120,232)	52,150,786
Construction in Progress		13,176,637	5,124,667	-	-	18,301,304
Totals	$	70,245,528	8,487,587	(809,121)	14,468	77,938,462

See independent auditors’ report.

CITY OF ELIZABETHTON ELECTRIC DEPARTMENT
AN ENTERPRISE FUND OF THE CITY OF ELIZABETHTON, TENNESSEE
SCHEDULE OF INSURANCE
June 30, 2010

Schedule 3

Insurer	Policy Effective	Property Covered	Risk Covered	Limit of Coverage
Tennessee Municipal League	7/1/10	General Liability	Bodily & Personal Injury	
			- Per Person	300,000
			- Per Occurrence	700,000
			Property Damage	100,000
		Property	Building	44,828,500
			($2,500 Deductible)	
			Electronic Data Processing	89,300
			($250 Deductible)	
			Mobile Equipment	251,155
			($250 Deductible)	
			Equipment Breakdown	45,079,655
			($2,500 Deductible)	
	7/1/10	Employment Practices Liability	Employee Dishonesty	
			Per Loss	150,000
			Forgery or Alteration	150,000
			Theft	100,000
			Computer Fraud	100,000
			Errors or Omissions	1,000,000
		Fleet Auto	Bodily Injury	
			Per Person	300,000
			Per Occurrence	700,000
			Property Damage	100,000
			Each Other Loss	1,000,000
			Catastrophic Medical Expenses	1,000,000
			Per Person Medical Payments	1,000
			Per Accident Medical Payments	10,000
			Fire Damage	100,000
			Impounded Property	100,000
			Non-Monetary Defense Costs	100,000
TML Risk Management Pool	7/1/10	Workers' Compensation	Bodily Injury	
			- Each Accident	1,000,000
			- Disease (policy limit)	1,000,000
			- Disease (each employee)	1,000,000

See independent auditors’ report.

CITY OF ELIZABETHTON ELECTRIC DEPARTMENT
AN ENTERPRISE FUND OF THE CITY OF ELIZABETHTON, TENNESSEE
SCHEDULE OF CURRENT UTILITY RATES AND NUMBER OF CUSTOMERS
June 30, 2010

Schedule 4

Residential Rate Schedule	**RS**	
Customer Charge -		
per delivery point per month		
($9.58 less $1.71 hydro allocation credit)	$7.87	
Energy Charge - per kWh per month	$0.08329	
General Power Rate Schedule	**GSA** (Demand 0-5,000 kW)	**GSB** (Demand 5,000 to 12,000 kW)
Part 1.		
Customer Charge		
Per delivery point per month	$13.46	$1,500.00
Energy Charge - per kWh per month	$0.09494	
Per kWh up to 620 hours per month		$0.04132
Per kWh all additional per month		$0.03372
Demand Charge - per kW per month		$15.40
Excess of billing demand over contract demand - per kW per month		$14.89
Part 2.		
Customer Charge		
Per delivery point per month	$33.64	
Demand Charge - per kW per month		
First 50 kW	$0.00	
Excess over 50kW per month	$13.70	
Energy charge - per kWh per month		
First 15,000 kWh	$0.09464	
Additional kWh per month	$0.04975	
Part 3.		
Customer Charge		
Per delivery point per month	$89.63	
Demand Charge - per kW per month		
First 1,000 kW	$13.57	
Excess over 1,000 kW	$15.27	
Excess of higher of 2,500 kW or contract demand	$0.00	
Energy Charge - per kWh per month		
First 15,000 kWh	$0.08137	
Additional kWh	$0.04975	
Outdoor Lighting Rate Schedule	**LS**	
Customer Charges		
Per delivery point per month	$3.75	
Energy Charge - per kWh	$0.05889	
Number of Customers		
Residential	22,605	
General	3,263	
Street, Athletic and Outdoor Lighting	3,766	
Total Customers	29,634	

See independent auditors' report.

CITY OF ELIZABETHTON ELECTRIC DEPARTMENT
AN ENTERPRISE FUND OF THE CITY OF ELIZABETHTON, TENNESSEE
NET ASSETS BY COMPONENT
Last Eight Fiscal Years

Schedule 5

	Fiscal Year							
	2003	2004	2005	2006	2007	2008	2009	2010
Primary Government								
Invested in Capital Assets, Net of Related Debt	$28,498,564	28,760,803	29,598,525	30,384,839	31,119,505	22,226,537	30,596,682	18,154,567
Unrestricted	1,907,375	2,770,258	3,274,694	5,015,868	6,707,953	17,010,388	9,643,451	22,146,475
Total Primary Government Activities Net Assets	$30,405,939	31,531,061	32,873,219	35,400,707	37,827,458	39,236,925	40,240,133	40,301,042

NOTE: Comparable information was not available for prior years. The Electric Department implemented Governmental Accounting Standards Board Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – For State and Local Governments*, during the 2003 fiscal year.

See independent auditors' report.

CITY OF ELIZABETHTON ELECTRIC DEPARTMENT
AN ENTERPRISE FUND OF THE CITY OF ELIZABETHTON, TENNESSEE
CHANGES IN NET ASSETS
Last Eight Fiscal Years

Schedule 6

Fiscal Year	Operating Revenues	Operating Expenses	Operating Income	Total Nonoperating Revenues/ (Expenses)	Income/(Loss) before Transfers	Transfer Out	Change in Net Assets
2003	$ 35,616,463	34,372,515	1,243,948	(160,333)	1,083,615	-	1,083,615
2004	37,031,743	35,115,737	1,916,006	(156,550)	1,759,456	(634,334)	1,125,122
2005	37,603,457	35,463,423	2,140,034	(109,117)	2,030,917	(688,758)	1,342,159
2006	41,633,296	38,327,297	3,305,999	(88,519)	3,217,480	(689,992)	2,527,488
2007	43,901,756	40,976,797	2,924,959	190,965	3,115,924	(689,173)	2,426,751
2008	46,038,644	44,209,051	1,829,593	97,188	1,926,781	(517,314)	1,409,467
2009	52,304,639	50,351,085	1,953,554	(384,558)	1,568,996	(565,788)	1,003,208
2010	49,208,207	47,728,135	1,480,072	(813,667)	666,405	(605,496)	60,909

NOTE: Comparable information was not available for prior years. The Electric Department implemented Governmental Accounting Standards Board Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – For State and Local Governments*, during the 2003 fiscal year.

See independent auditors' report.

CITY OF ELIZABETHTON ELECTRIC DEPARTMENT
AN ENTERPRISE FUND OF THE CITY OF ELIZABETHTON, TENNESSEE
OPERATING REVENUE BY SOURCE
Last Eight Fiscal Years

Schedule 7

Fiscal Year	Residential	Large Commercial/ Industrial	Small Lighting/ Power	Street and Outdoor Lighting	Other Operating Revenues	Total
2003	$ 20,868,433	9,532,906	3,514,645	714,906	985,573	35,616,463
2004	21,702,385	9,830,428	3,708,461	731,145	1,059,324	37,031,743
2005	21,946,327	10,215,072	3,476,061	760,913	1,205,084	37,603,457
2006	24,678,822	11,351,765	3,627,682	809,565	1,165,462	41,633,296
2007	26,252,139	11,837,851	3,816,089	825,495	1,170,182	43,901,756
2008	27,653,761	12,366,936	4,123,824	854,016	1,040,107	46,038,644
2009	32,419,144	13,605,402	4,672,946	961,708	645,439	52,304,639
2010	29,833,411	12,261,591	4,412,045	857,402	1,843,758	49,208,207

NOTE: Comparable information was not available for prior years.

See independent auditors' report.

CITY OF ELIZABETHTON ELECTRIC DEPARTMENT
AN ENTERPRISE FUND OF THE CITY OF ELIZABETHTON, TENNESSEE
OPERATING EXPENSES
Last Eight Fiscal Years

Schedule 8

Fiscal Year	Power Purchased from TVA	Maintenance	Other Operating Expenses	Subtotal, Expenses before Tax and Depreciation	Tax and Tax Equivalents	Provision for Depreciation	Total Operating Expenses
2003	$ 27,092,252	1,462,119	3,459,074	32,013,445	1,048,004	1,311,066	34,372,515
2004	28,422,424	1,475,074	3,517,731	33,415,229	361,924	1,338,584	35,115,737
2005	28,532,987	1,508,146	3,662,089	33,703,222	387,119	1,373,082	35,463,423
2006	31,810,791	1,571,865	3,167,038	36,549,694	357,101	1,420,502	38,327,297
2007	34,022,346	1,657,904	3,461,806	39,142,056	355,702	1,479,039	40,976,797
2008	36,245,964	2,025,280	3,846,817	42,118,061	552,623	1,538,367	44,209,051
2009	42,343,783	2,121,113	3,915,170	48,380,066	389,379	1,581,640	50,351,085
2010	37,956,861	3,374,706	4,288,329	45,619,896	454,772	1,653,467	47,728,135

NOTE: Comparable information was not available for prior years.

See independent auditors' report.

CITY OF ELIZABETHTON ELECTRIC DEPARTMENT
AN ENTERPRISE FUND OF THE CITY OF ELIZABETHTON, TENNESSEE
NONOPERATING REVENUES AND EXPENSES
Last Eight Fiscal Years

Schedule 9

Fiscal Year	Interest on Invested Funds	Interest Expense	Amortization Expense	Total Nonoperating Revenues and Expenses
2003	$ 47,317	(203,280)	(4,370)	(160,333)
2004	43,109	(195,289)	(4,370)	(156,550)
2005	83,452	(188,199)	(4,370)	(109,117)
2006	146,711	(196,329)	(38,901)	(88,519)
2007	344,645	(148,838)	(4,842)	190,965
2008	472,415	(360,613)	(14,614)	97,188
2009	465,089	(831,566)	(18,081)	(384,558)
2010	108,062	(877,369)	(44,360)	(813,667)

Note: Comparable information was not available for prior years.

See independent auditors' report.

CITY OF ELIZABETHTON ELECTRIC DEPARTMENT
AN ENTERPRISE FUND OF THE CITY OF ELIZABETHTON, TENNESSEE
RATIO OF OUTSTANDING DEBT BY TYPE (UNAUDITED)
Last Eight Fiscal Years

Schedule 10

Fiscal Year	Revenue Bonds	Advance from TVA	Total Amount	Total Population	Total Per Capita
2003	$ 4,095,000	$ 1,804,568	$ 5,899,568	14,017	$ 421
2004	3,890,000	1,531,585	5,421,585	14,017	387
2005	3,765,000	1,315,704	5,080,704	14,017	362
2006	3,780,000	1,216,534	4,996,534	14,017	356
2007	3,620,000	1,253,795	4,873,795	14,017	348
2008	18,455,000	1,221,192	19,676,192	14,017	1,404
2009	18,280,000	1,429,484	19,709,484	14,017	1,406
2010	38,160,000	1,592,086	39,752,086	14,017	2,836

* Details regarding the Electric Department's outstanding debt can be found in the notes to the financial statements.

Source: The Population figure comes from the State ECD census of June 14, 2002.

NOTE: Comparable information was not available for prior years.

See independent auditors' report.

CITY OF ELIZABETHTON ELECTRIC DEPARTMENT
AN ENTERPRISE FUND OF THE CITY OF ELIZABETHTON, TENNESSEE
NUMBER OF ELECTRIC CUSTOMERS BY TYPE (UNAUDITED)
Last Eight Fiscal Years

Schedule 11

Fiscal Year	Residential	General *	Street and Outdoor Lighting	Total Customers
2003	21,174	4,044	109	25,327
2004	21,332	3,992	113	25,437
2005	22,157	3,300	117	25,574
2006	22,439	3,230	125	25,794
2007	22,484	3,271	160	25,915
2008	22,504	3,300	159	25,963
2009	22,552	3,290	154	25,996
2010	22,605	3,263	154	26,022

NOTE: Comparable information was not available for prior years.

* The General type of Electric Customer includes the Large Commercial and Industrial type and the Small Lighting and Power type. Furthur breakdown of this information was not available.

See independent auditors' report.

CITY OF ELIZABETHTON ELECTRIC DEPARTMENT
AN ENTERPRISE FUND OF THE CITY OF ELIZABETHTON, TENNESSEE
ELECTRICITY RATES (UNAUDITED)
Last Eight Fiscal Years

Schedule 12

	Fiscal Year							
	2003	2004	2005	2006	2007	2008	2009	2010
Residential Rate								
Customer Charge -								
per delivery point per month	$ 6.25	$ 7.25	$ 7.25	$ 7.25	$ 7.79	$ 7.87	$ 7.87	$ 7.87
Energy Charge - per kWh per month	0.05892	0.06231	0.06231	$0.07291	$0.07096	$0.08092	$0.07726	$0.08329
General Power Rate								
Part 1.								
Customer Charge								
Per delivery point per month								
(Demand 0-5,000 kW)	$ 12.00	$ 12.40	$ 12.40	$ 13.32	$ 13.32	$ 13.46	$ 13.46	$ 13.46
(Demand 5,000 to 12,000 kW)	1500	1500	1500	$1,500.00	$1,500.00	$1,500.00	$1,500.00	$1,500.00
Energy Charge - per kWh per month	0.06596	0.07088	0.07088	$0.08289	$0.08054	$0.09110	$0.08782	$0.09464
Per kWh up to 620 hours per month	0.02825	0.03035	0.03035	$0.03588	$0.03514	$0.04234	$0.04592	$0.04132
Per kWh all additional per month	0.02306	0.02477	0.02477	$0.02928	$0.02883	$0.03559	$0.00000	$0.03372
Demand Charge - per kW per month	10.85	11.58	11.58	$13.51	$12.95	$13.78	$13.46	$15.40
Excess of billing demand over								
contract demand - per kW per month	10.85	11.58	11.58	$13.51	$12.95	$13.78	$14.21	$14.89
Part 2.								
Customer Charge								
Per delivery point per month	30	31	31	$33.30	$33.30	$33.64	$33.64	$33.64
Demand Charge - per kW per month								
First 50 kW	0	0	0	0	0	0	0	0
Excess over 50kW per month	9.71	10.44	10.44	$12.08	$11.65	$12.43	$12.77	$13.70
Energy charge - per kWh per month								
First 15,000 kWh	0.06596	0.07088	0.07088	$0.08289	$0.08054	$0.09110	$0.08782	$0.09464
Additional kWh per month	0.03377	0.03649	0.03649	$0.04320	$0.04224	$0.05021	$0.04592	$0.04975
Part 3.								
Customer Charge								
Per delivery point per month	80	82.6	82.6	$88.73	$88.73	$89.63	$89.63	$89.63
Demand Charge - per kW per month								
First 1,000 kW	9.48	10.16	10.16	$11.87	$11.41	$12.23	$12.59	$13.57
Excess over 1,000 kW	10.2	11.25	11.25	$13.28	$12.74	$13.70	$14.12	$15.27
Excess of higher of 2,500 kW or								
contract demand	10.2	11.25	11.25	$0.00	$0.00	$0.00	$0.00	$0.00
Energy Charge - per kWh per month								
First 15,000 kWh	0.06434	0.06741	0.06741	$0.07450	$0.07354	$0.08183	$0.08592	$0.08137
Additional kWh	0.03377	0.03649	0.03649	$0.04320	$0.04224	$0.05021	$0.05430	$0.04975
Outdoor Lighting Rate Schedule								
Customer Charges								
Per delivery point per month	2.5	2.5	2.5	$2.50	$2.50	$3.75	$3.75	$3.75
Energy Charge - per kWh	0.04375	0.04616	0.04616	$0.05257	$0.05159	$0.05935	$0.05493	$0.05889

NOTE: Comparable information was not available for prior years.

See independent auditors' report.

SECTION III

INTERNAL CONTROL AND COMPLIANCE SECTION

Blackburn, Childers & Steagall, PLC

CERTIFIED PUBLIC ACCOUNTANTS AND CONSULTANTS

REGIONAL EXPERTISE - LOCAL SERVICE

American Institute of Certified Public Accountants

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

Honorable Mayor, City Council Members
and City Manager
City of Elizabethton Electric Department
Elizabethton, Tennessee 37643

We have audited the financial statements of the City of Elizabethton Electric Department (the "Department") (an enterprise fund of the City of Elizabethton, Tennessee) as of and for the year ended June 30, 2010, and have issued our report thereon dated December 20, 2010. The independent auditors' report contained an explanatory paragraph stating that the report of the Department does not purport to present the financial position and changes in financial position and cash flows of the City of Elizabethton, Tennessee. 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, we considered the Department's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Department's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Department's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses and therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. However, as described in the accompanying schedule of findings and responses, we identified certain deficiencies in internal control over financial reporting that we consider to be material weaknesses and other deficiencies that we consider to be significant deficiencies.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiencies described in the accompanying schedule of findings and responses to be material weakness: 2010-01, 2010-02 and 2010-03.

Johnson City	801B Sunset Drive, P.O. Box 3745, Johnson City, TN 37602-3745	(423) 282-4511	Fax (423) 283-4532
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website = http://www.BCScpa.com e-mail: BCS@BCScpa.com

A *significant deficiency* is a deficiency, or 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. We consider the deficiencies described in the accompanying schedule of findings and responses to be significant deficiencies. These include 2010-04, 2010-05, 2010-06, 2009-01 and 2007-03.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Department's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed an instance of noncompliance or other matters that is required to be reported under *Government Auditing Standards* and which is described in the accompanying schedule of findings and responses as item 2010-03.

We noted certain other matters that we reported to management of City of Elizabethton Electric Department in a separate letter dated December 20, 2010.

The Department's response to the findings identified in our audit is described in the accompanying schedule of findings and responses. We did not audit the Department's response and, accordingly, we express no opinion on it.

This report is intended solely for the information and use of management, the City Council and others within the organization and is not intended to be and should not be used by anyone other than these specified parties.

Blackburn, Childers & Steagall, PLC
BLACKBURN, CHILDERS & STEAGALL, PLC

December 20, 2010

CURRENT YEAR FINDINGS

2010-01: Material Weakness: Journal Entries

Condition: It appears that journal entries are lacking proper and timely approval before they are posted to the system. There also appears to be lack of supporting documentation for all posted journal entries.

Criteria: To enhance internal controls and to increase proper oversight and independent review, all adjustments and transfers should be appropriately documented and approved.

Effect: The effect of this weakness creates the possibility that misstatements may not be timely noted or corrected.

Recommendation: We recommend a procedure be in place for the timely review and approval of all journal entries. Someone other than the preparer should review these items. We suggest that a monthly listing of all entries posted be maintained.

Management's Response: Management will develop a spreadsheet noting all reoccurring entries and submitting it for approval at the beginning of the fiscal year. In addition, a signed weekly report will be required of the accountant stating that either there are no journal entries required for the preceding week or listing journal entries required for that week for signature approval and stating that those entries on the spreadsheet previously submitted for approval have been posted as journal entries. Said statement will be signed by the accountant.

2010-02: Material Weakness: Adjustments

Condition: Under current professional standards, the Electric Department is responsible for the internal control process which includes the preparation of year-end financial statements in accordance with generally accepted accounting principles and the modified accrual basis of accounting. Audit adjustments were necessary to properly state account balances including: investments, inventory stores expense and other post-employment benefit liability.

***Criteria*:** General ledger accounts should be timely reviewed, reconciled to the appropriate supporting documentation or subsidiary ledger reports and adjusted.

Effect: The effect of this deficiency creates the possibility that misstatements may not be timely noted or corrected.

Recommendation: We recommend a procedure be in place to prepare routine, monthly and year-end reconciliations for general ledger accounts to the supporting documentation and subsidiary ledgers and to make related adjustments. The procedure should require retention of supporting documentation for all entries and transfers, including indication of appropriate review and approval.

CURRENT YEAR FINDINGS (CONTINUED)

2010-02: Material Weakness: Adjustments (continued)

These routine reconciliations and adjustments will ensure meaningful and accurate financial statements. Reconciliation of Balance Sheet and other significant accounts quickly identify errors and needed corrections. If reconciliations are performed infrequently, errors and adjustments can occur, resulting in the need for significant corrections when the reconciliations are performed. Any reconciling differences should be corrected before the books are closed for the month end.

Management's Response: Management agrees with the finding and will develop procedures to implement for proper recording of bonds investments. The error has been corrected in 2010 financials. Management will develop an overhead rate to properly record Store Expenses. Also procedures will be developed to record amounts monthly. Said procedures will be proactive and require the accountant to submit a signed report monthly, stating that the month has been properly closed out and proper accounting procedures have been posted. If that statement cannot be signed by the accountant, the exceptions will be listed on the report along with a statement of what needs to be done to close the month properly, by whom, and what has been done to accomplish that work.

2010-03: Material Weakness: Supporting Documentation – Bond Funds

Condition: The Electric Department has numerous significant infrastructure construction projects on going. Bond funds were issued during the current year as well as in previous years for these projects. The bond proceeds are being invested with Morgan Keegan and periodic draws or requests for funds are prepared. Proper supporting documentation for some draws was not always present to properly match or indicate which vendor invoices, contractor statements, payroll runs or equipment items correlate to the request for bond funds.

Criteria**:** Request for bond funds should be properly documented to indicate the purpose of the draw/request of funds, and amount.

Effect: The effect of this deficiency creates a weakness in the internal control process regarding accounting for bond funds.

Recommendation: To provide a proper paper trail and supporting schedules, bond fund draws should be properly documented to indicate the purpose of the draw/request of funds, and amount. The Electric Department should properly maintain supporting schedules and/or documentation as an indication the reason for requesting the invested funds.

Management's Response: Management will development a request form to request and approve bond fund draws.

CURRENT YEAR FINDINGS (CONTINUED)

2010-04: Significant Deficiency: Cash Flow Concerns

***Condition*:** The Electric Department experienced a decrease in net income to approximately $61,000 for the year from approximately $1,003,000 in the prior year. In addition, the Electric Department experienced a significant decline in cash and cash equivalents. The Department maintains certificates of deposit and investment account which total $23,394,495 at June 30, 2010. However, cash and cash equivalents is an overdraft of $243,338 at year-end. As reflected on the Statement of Cash Flows, total cash and cash equivalents decreased by $4,247,507 to an ending cash of $17,157.

***Criteria*:** State statues require electric operations to have a rate structure sufficient to cover expenditures. Enterprise funds should be self-supporting. Cash balances should be adequate to properly cover expenditures.

Effect: The effect of this deficiency is a failure to comply with the state requirements as well as overall cash management.

Recommendation*:* Revenues and expenses should be reviewed to provide adequate income for the department. Monthly budgets and financial reports should be prepared and reviewed. Municipal officials should ensure cash reserves are in place in order to meet obligations.

Management's Response: Management is aware of cash flow requirements. However, last fiscal year had a number of extraordinary events which contributed to the finding. The destruction of assets from the winter storm of the decade in December cost the system approximately $900,000, not including cost associated with Winner Substation and lost revenue. Insurance reimbursement for Winner Substation ($490,979.95) did not arrive until late July. In addition, there were numerous wind and thunderstorms throughout the year with costs of $10,000 to $25,000 each for a total of about $80,000. This situation was compounded by a contract dispute with Embarq Telephone Company on line attachment fees, (over $1,000,000) which went unpaid for nearly two years and required legal intervention to get resolution. In addition, we had a commercial bankrupt account of $74,176.37, which is not normal based on our bad debt history. A rate increase was implemented in September 2010 along with reduction in capital improvements for the next fiscal year to begin increasing reserves.

CURRENT YEAR FINDINGS (CONTINUED)

2010-05: Significant Deficiency: Authorizations

Condition: Transfers of funds from the investment account, although traceable, were not always properly supported with a signed approval transfer form indicating the purpose of the transfer as well as approval.

***Criteria*:** Online or wire requests of funds should be properly authorized and supported with a traceable audit trail.

Effect: By ensuring that cash transactions are authorized by the appropriate level of Electric Department personnel, the risk of unauthorized disbursements can be reduced.

Recommendation: The procedures for wire transfers should be changed so that the authorization for the transfer is approved by an approved signer on the account. Proper supporting documentation of the request for funds, along with the corresponding financial institution confirmation, should be on file as support.

Management's Response: Management agrees and is developing a spreadsheet to tie the bond draws with capital expenses.

2010-06: Significant Deficiency: Disbursements

Condition: During audit procedures, some deficiencies with purchasing procedures were noted. For one disbursement tested, mileage was paid to a vendor for what appears to be an unsupported and unreasonable amount. We also noted that this payment was made without proper signed approval from an authorized employee.

***Criteria*:** The *Internal Control and Compliance Manual for Tennessee Municipalities,* issued by the State of Tennessee Comptroller's office, Title 5, Chapter 19 states in part that "expenditures for…mileage…generally will require additional notations to indicate the purpose, date and any other pertinent information regarding expenditures for such items." All disbursements should be approved by appropriate Electric Department personnel.

Effect: These issues create a deficiency in internal controls for the cash disbursement process.

Recommendation: To enhance the internal control for cash disbursements, we recommend the purchasing procedures adopted be followed. All invoices presented for payment should be clearly reviewed for accuracy, reasonableness of charges before processing and approving for payment. Appropriate approval should be clearly marked on the invoice previous to payment.

Management's Response: Management agrees with findings. The travel was discussed in the electric findings. Staff and Contractor were instructed on proper procedures on issuing purchase orders and invoices.

PRIOR YEAR FINDINGS NOT IMPLEMENTED

2009-01: Significant Deficiency: **Information Technology Controls** (Repeated from 6-30-09)

Condition: There was a lack of proper information technology controls, including restricting user access within the software. Exception and variance reports were not always ran and properly reviewed. There was also an instance of an account adjustment initiated by unauthorized personnel.

***Criteria*:** Proper IT controls are an essential component to the overall control environment.

Effect: The Electric Department risks access to its computer files by unauthorized personnel.

Recommendation: We recommend that the Electric Department institute a software package that has the ability to restrict user access within the system. System reports should be generated and reviewed in order to monitor employee access to customer information. Documentation should be on file and reviewed for rate adjustments and should be approved by the appropriate individual.

Management's Response: Management is in the process of addressing SAS 70 issues. We are in total agreement of the recommendation and have been trying to do so for the past two years. Most issues will be corrected with the changes in computer systems. However, it should be noted that computer conversion has taken an abnormal amount of time due to the present vendor, CSA, dragging out conversion data release for conversion. This issue has been through attorneys and has just now begun to have progress. Issues continue in getting data for conversion and abnormal fees charged by CSA, claiming they cannot give us a data dump because such dump may release proprietary information. Initial live conversion of some programs will start in April 2011. It appears final data conversion for 100% of the files will last until the fall of 2011.

2007-03: Significant Deficiency: **Work Orders** (Repeated from 6-30-07 Report, with additional current year items noted)

***Condition*:** Proper work order procedures and controls were not always followed. In some instances, materials and contracted labor were entered as both a purchase order and a payable. This required the reversal of those amounts that were entered twice. There is a general lack of understanding of the various reports printed from the WMS, especially those reports detailing open, active, and closed projects. It was noted that supporting documentation for several closed work orders had been lost. It appears that engineering did not always properly describe any aid to construction information on the work order. There were also instances were expense had been coded to the incorrect work order.

PRIOR YEAR FINDINGS NOT IMPLEMENTED (CONTINUED)

2007-03: Significant Deficiency: **Work Orders** (Repeated from 6-30-07 Report, with additional current year items noted) (continued)

***Criteria*:** Procedures for work orders should be followed to document all aspects of the work in order to enhance internal controls over the financial reporting process. These should be routinely reviewed for the status of the job and necessary adjustments should be documented and posted to close or transfer completed projects.

Effect: The effect of this deficiency results in a weakness in proper controls over financial reporting.

***Recommendation**:* We recommend, work orders be completed in full detail and work orders be reviewed and properly approved.

Management's Response: The Accounting Manager as well as Engineers and Warehouse Supervisor are being directed to run every report available in the Work Order System and forward them to the Director of Electric Services. The Director will review the report capability of the system, determine which reports are necessary to support the operation and conduct training classes with all involved. Weekly reports to the Director of Electric Services will then be developed to assure all know how the system works; work orders are being properly closed; properly posted to the general ledger; and time reports from payroll are properly posted to the work orders. Aid to Construction as well as detailed description of the aid will be listed on all work orders. If no aid to construction is required according to current line extension policy, a note to that effect will be listed on the work order and initialed by the originating engineer.

PRIOR YEAR FINDINGS IMPLEMENTED

2009-02 Account Reconciliations

2007-04 Adjustments and Reporting