CITY OF FRANKLIN, TENNESSEE
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2011

NOTE 3 - DETAILED NOTES ON ALL FUNDS (Cont.)

A. Deposits and Investments (Cont.)

Investments:
Interest Rate Risk: Investments held for longer periods are subject to increased risk for adverse interest rate changes. City policy provides that to the extent practicable, investments are matched with anticipated cash flows. Typically certificates of deposit are issued for periods less than one year and investments in the Local Government Investment Pool are available daily. At June 30, 2011, investments of the City had average weighted maturities as noted below.

Credit Risk: The City's general investment policy is derived from the model investment policy created by the Government Finance Officers Association. Its general objectives are safety, liquidity, and yield and its standard of care to be used by investment officials is formulated around the prudent-person rule: investments are made as a prudent person should be expected to make, with discretion and intelligence, to produce reasonable income, preserve capital and, in general, avoid speculative investments.

As of June 30, 2011, the City, exclusive of the Pension Fund, had the following investments with the noted weighted average maturities:

Investment Type	Fair Value	Weighted Average Maturity (Years)
Certificates of Deposit	$ 14,067,259	0.54
Money Market Accounts	8,797,432	-
Treasury Securities	1,411,612	1.75
Municipal Bonds	596,647	2.16
Federal Farm Credit	200,910	3.38
Federal Home Loan Bank	682,393	3.28
Federal National Mortgage Assn	361,669	3.69
Total Investments at Fair Value	$ 26,117,922	
Portfolio Weighted Avg. Maturity		0.60

All investments are rated Aaa by Moody's and the certificates of deposit are in banks covered by the State collateral pool or under FDIC.

As of June 30, 2011, the investments that constituted a concentration risk due to the investments exceeding 5% of the portfolio balance were the CD's, the money market accounts, and treasury securities.

As of December 31, 2010 the City of Franklin's Pension Fund had the following investments:

Investment Type	Fair Value	Weighted Average Maturity (Years)
Investments Available for Sale	$ 52,489,083	
Total Investments at Fair Value	$ 52,489,083	
Portfolio Weighted Avg. Maturity		n/a

Investments available for sale include short term investments, domestic corporate stock, mutual funds, and other investments.

CITY OF FRANKLIN, TENNESSEE
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2011

NOTE 3 - DETAILED NOTES ON ALL FUNDS (Cont.)

B. Receivables

Receivables as of June 30, 2011, including the applicable allowances for uncollectible accounts, are as follows:

	General Fund	Multi-Purpose Capital Project Fund	Debt Service Fund	Water & Sewer Fund	Other Governmental Funds	Total
Receivables:						
Accounts	$ 985,450	$ -	$ -	$ 4,168,464	$ 791,210	$ 5,945,124
Property taxes	7,554,788	-	4,946,729	-	-	12,501,517
Grants	501,882	1,150,819	-	293,385	534,105	2,480,191
Special assessments	53,762	-	-	-	-	53,762
Intergovernmental	2,409,544	-	-	-	491,737	2,901,281
Fines	643,548	-	-	-	-	643,548
Local option sales tax	3,931,939	-	-	-	-	3,931,939
Other	3,019,746	40,239	-	-	521,460	3,581,445
Gross receivables	19,100,659	1,191,058	4,946,729	4,461,849	2,338,512	32,038,807
Less: Allowance for uncollectibles	(519,945)	-	-	(9,000)	-	(528,945)
Net total receivables	$ 18,580,714	$ 1,191,058	$ 4,946,729	$ 4,452,849	$ 2,338,512	$ 31,509,862

Governmental funds report deferred revenue in connection with receivables for revenues that are available to liquidate liabilities of the current period. Governmental funds also defer revenue recognition in connection with resources that have been received, but not yet earned. At the end of the current fiscal year, various components of deferred revenue and unearned revenue reported in the governmental funds were as follows:

	Unavailable	Unearned
Delinquent property taxes receivable	$ 266,345	$ -
Property tax penalties and interest receviable	110,385	-
2010 property tax assessment	-	11,232,926
Special assessments	-	210,678
Confiscated funds	-	24,111
Franchise fees	431,745	-
Court fines receivable	225,242	-
Unrequested grant proceeds	1,303,359	-
Total deferred revenue for fund financial statements	$ 2,337,076	$ 11,467,715

CITY OF FRANKLIN, TENNESSEE
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2011

NOTE 3 - DETAILED NOTES ON ALL FUNDS (Cont.)

C. Capital Assets

Capital asset activity for the year ended June 30, 2011 was as follows:

Governmental activities:	Balance June 30, 2010	Reclassifications	Additions	Disposals	Balance June 30, 2011
Capital assets, not being depreciated:					
Land	$ 47,241,564	$ -	$ 846,917	$ -	$ 48,088,481
Construction in process	14,639,918	(4,459,509)	17,288,545	-	27,468,954
Total capital assets, not being depreciated	61,881,482	(4,459,509)	18,135,462	-	75,557,435
Capital assets, being depreciated:					
Buildings and improvements	63,316,410	-	31,143	-	63,347,553
Improvements other than buildings	21,028,982	-	-	-	21,028,982
Equipment	50,005,424	-	1,437,283	1,916,183	49,526,524
Infrastructure	429,876,014	4,459,509	10,203,336	1,068,181	443,470,678
Total capital assets, being depreciated	564,226,830	4,459,509	11,671,762	2,984,364	577,373,737
Accumulated depreciation					
Buildings and improvements	6,487,458	-	1,313,016	-	7,800,474
Improvements other than buildings	3,197,738	-	1,036,525	-	4,234,263
Equipment	26,368,562	-	4,461,251	1,612,945	29,216,868
Infrastructure	87,501,630	-	8,916,659	22,112	96,396,177
Total accumulated depreciation	123,555,388	-	15,727,451	1,635,057	137,647,782
Total capital assets being depreciated, net	440,671,442	4,459,509	(4,055,689)	1,349,307	439,725,955
Total governmental activities capital assets, net	502,552,924	-	14,079,773	1,349,307	515,283,390
Business-type activities:					
Capital assets, not being depreciated:					
Land	5,216,746	-	22,199	-	5,238,945
Construction in process	8,455,983	(3,586,899)	5,898,824	-	10,767,908
Total capital assets, not being depreciated	13,672,729	(3,586,899)	5,921,023	-	16,006,853
Capital assets, being depreciated:					
Buildings and improvements	11,291,016	-	-	-	11,291,016
Utility plant in service	175,725,779	3,586,899	173,591	-	179,486,269
Machinery and equipment	4,771,367	-	561,541	165,596	5,167,312
Total capital assets, being depreciated	191,788,162	3,586,899	735,132	165,596	195,944,597
Accumulated depreciation					
Buildings and improvements	7,725,427	-	309,769	-	8,035,196
Utility plant in service	39,176,378	-	4,296,607	-	43,472,985
Machinery and equipment	3,685,823	-	289,229	122,637	3,852,415
Total accumulated depreciation	50,587,628	-	4,895,605	122,637	55,360,596
Total capital assets being depreciated, net	141,200,534	3,586,899	(4,160,473)	42,959	140,584,001
Business-type activities capital assets, net	154,873,263	-	1,760,550	42,959	156,590,854
Total capital assets, net	$ 657,426,187	$ -	$ 15,840,323	$ 1,392,266	$ 671,874,244

CITY OF FRANKLIN, TENNESSEE
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2011

NOTE 3 - DETAILED NOTES ON ALL FUNDS (Cont.)

C. **Capital Assets** (Cont.)

Depreciation expense was charged to functions/programs of the primary government as follows:

Governmental activities:		
General government	$	297,229
Administration		2,570
Capital improvement planning		6,205
Police department		1,366,372
Fire department		792,311
Highways and streets		9,239,764
Engineering		66,307
Stormwater		82,730
Sanitation		912,021
Transit		185,276
Parks		1,159,442
Maintenance		3,155
Planning		6,210
Building and neighborhood services		28,253
Human resources		7,412
Communications		4,634
Finance		26,078
Municipal information and technology		1,541,482
Total depreciation expense – governmental activities	$	15,727,451
Business-type activities:		
Water and sewer	$	4,895,605
Total depreciation expense – business-type activities	$	4,895,605

D. **Interfund Receivables, Payables and Transfers**

The following is a summary of transfers during the year ended June 30, 2011:

Transfer from	Transfer to		Amount
General	Street Aid	$	578,450
General	Sanitation		1,508,605
General	Transit Authority		292,414
General	Capital Project		481,504
Sanitation	Debt Service		532,022
Road Impact Fee	Debt Service		2,730,648
Hotel/Motel Tax	Debt Service		1,708,248
Total		$	7,831,891

NOTE 3 - DETAILED NOTES ON ALL FUNDS (Cont.)

D. Interfund Receivables, Payables and Transfers (Cont.)

The purposes of the transfers are noted below:

- The transfers from the General Fund to the Sanitation, Transit Authority, and State Street Aid funds are for the purpose of providing the annual operating subsidy.
- The transfers from the Sanitation, Road Impact, and Hotel/Motel funds to the Debt Service Fund are for the purpose of transferring funds to cover annual debt service requirements.

Interfund balances below are expected to be repaid within the next fiscal year and are considered ordinary in nature. The composition of interfund balances as of June 30, 2011, are as follows:

Due from	Due to	Amount
Sanitation	General	$ 417,322
Street Aid	General	49,269
Transit Authority	Storm Water	1,563,445
Road Impact Fee	General	792,527
Facilities Tax	General	291,165
Drug Fund	General	137,997
CDBG	General	69,100
Total		$ 3,320,825

The purposes of the interfund balances are:

- The balance between the General Fund and the Sanitation Fund is due to a negative cash balance in the Sanitation Fund at year end due to outstanding receivables.
- The balance between the General Fund and the Street Aid Fund is due to a negative cash balance in the Street Aid Fund at year end due to outstanding receivables.
- The balance between the Storm Water Fund and the Transit Authority Fund is due to a negative cash balance in the Transit Fund at year end because of outstanding grants receivable.
- The balance between the General Fund and the Road Impact Fee Fund is due to a negative cash balance in the Road Impact Fee Fund at year end because of a deficit fund balance.
- The balance between the General Fund and the Facilities Tax Fund is due to a negative cash balance in the Facilities Tax Fund at year end because of a deficit fund balance.
- The balance between the General Fund and the CDBG Fund is due to a negative cash balance in the CDBG Fund at year end because of outstanding grants receivable.

NOTE 3 - DETAILED NOTES ON ALL FUNDS (Cont.)

E. Capital Leases

The City has entered into three (3) lease agreements as lessee for financing the acquisition of equipment:

1. SunTrust Leasing for $2,500,000,
2. DeLage Leasing for $360,791, and
3. PNC Leasing for $341,691.

These lease agreements qualify as capital leases for accounting purposes and, therefore, have been recorded at the present value of their future minimum lease payments as of the inception date. The assets acquired through capital leases are as follows:

Assets:	
911 Dispatch Equipment	$ 1,202,017
3 Recycling Trucks	230,400
Compost Screener	112,550
Disaster Recovery Equipment	360,791
Utility billing software	341,691
	2,247,449
Less: Accumulated Depreciation	(364,731)
Total	$ 1,882,718

The future minimum lease obligations and the net present value of these minimum lease payments as of June 30, 2011 were as follows:

Year Ending June 30,	
2012	$ 811,281
2013	778,726
2014	551,980
2015	551,980
Total minimum lease payments	2,693,967 *
Less: Amount representing interest	(191,967)*
Present value of minimum lease payments	$ 2,502,000

* The minimum lease payments and interest schedule assumes the entire SunTrust lease is used. Of the $2,500,000 original amount, $1,544,967 has been used with $955,033 remaining. (Both the DeLage lease of $360,791 and PNC lease of $341,691 have been used).

CITY OF FRANKLIN, TENNESSEE
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2011

NOTE 3 - DETAILED NOTES ON ALL FUNDS (Cont.)

F. Long-term Debt

Long-term debt at June 30, 2011, is comprised of the following:

Governmental Activities:	
General obligation bonds:	
City of Clarksville, Pooled Loan Program - 2001 variable rate of interest; final maturity May 25, 2017	$ 2,429,000
Tennessee Municipal Variable Rate Pooled Loan Program - 2001; variable rate of interest, final maturity May 25, 2018	1,108,000
Series 2002 - General Obligation Refunding Bonds, 3.00% to 4.50% interest, final maturity November 1, 2012.	1,055,000
Series 2004 - General Obligation Refunding Bonds, 2.00% to 3.625% interest, final maturity, October 1, 2014	3,175,000
Series 2004 - General Obligation Public Improvement Bonds, 2.00% to 4.50% interest, final maturity March 1, 2024	355,000
City of Clarksville, Pooled Loan Program - 2004 variable rate of interest, final maturity May 25, 2017	2,900,000
City of Lawrenceburg, TN Loan Agreement 2005 variable rate of interest, final maturity July 1, 2020	3,275,000
Series 2009B - General Obligation Build America Bonds (BAB) 4.45% to 5.70% interest, final maturity, March 1, 2029	30,625,000
Series 2009A - General Oligation Public Improvement Bonds 2.50% interest, final maturity, March 1, 2017	11,800,000
Series 2007 - General Obligation Public Improvement Bonds - 101-A-1, variable rate of interest, final maturity June 1, 2037	20,000,000
Montgomery County, Pooled Loan Program - 2009 variable rate of interest, final maturity May 25, 2029	23,370,000
Series 2010 - General Obligation Recovery Zone Economic Development Bonds (RZEDB), 4.625% to 5.375% interest, final maturity March 1, 2030	15,725,000
Series 2010 - General Obligation Refunding Bonds, 2.00% to 3.00% interest, final maturity March 1, 2024	16,000,000
Total Governmental Activities Long-Term Debt	$ 131,817,000

The aforementioned bonds are secured by the full faith and credit of the City. During 2011, debt service for the aforementioned debt was provided by the Debt Service Fund through property tax collections as well as transfers from the Sanitation Fund, Road Impact Fund and the Hotel/Motel Tax Fund.

CITY OF FRANKLIN, TENNESSEE
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2011

NOTE 3 - DETAILED NOTES ON ALL FUNDS (Cont.)

F. Long-term Debt (Cont.)

Business - Type Activities:	
Revenue and tax bonds:	
Series 2002B - Sewer and Water Revenue and Tax Bonds: 3.00% to 5.00% interest; final maturity April 1, 2025	$ 2,600,000
Series 2002A - Sewer and Water Revenue and Tax Refunding Bonds 3% to 4% interest; final maturity June 30, 2013	1,540,000
Series 2005 - Sewer and Water Revenue and Tax Refunding Bonds: 3% to 5% interest; final maturity April 1, 2025	24,390,000
Series 2008 - Tennessee Municipal Bond Fund Variable Rate Pooled Loan Program, variable rate of interest; final maturity May 25, 2030	19,362,000
Notes payable:	
Drinking Water SRF Loan provided through ARRA funding, 2.82% interest; final maturity December 20, 2030	1,471,395
Clean Water SRF Loan provided through ARRA funding, 2.69% interest; final maturity estimated to be December 2031	1,065,839
Total Business-Type Activities Long-Term Debt	$ 50,429,234

The aforementioned bonds are secured by the full faith and credit of the City and backed by the revenues of the Water and Sewer Fund. During 2011, debt service for the aforementioned debt was provided solely by the Water and Sewer Fund.

The annual requirements, by type of issue, to amortize all long-term debt outstanding, except compensated absences, at June 30, 2011, are as follows:

Year Ending	Revenue and Tax Bonds		General Obligation Bonds		Total	
June 30,	Principal	Interest	Principal	Interest	Principal	Interest
2012	3,038,801	1,481,277	6,361,000	4,274,969	9,399,801	5,756,246
2013	3,226,344	1,383,881	6,588,000	4,137,305	9,814,344	5,521,186
2014	2,841,143	1,292,428	6,265,000	4,008,793	9,106,143	5,301,221
2015	2,896,017	1,187,087	5,927,000	3,899,872	8,823,017	5,086,959
2016	2,952,974	1,080,579	5,691,000	3,790,988	8,643,974	4,871,567
2017 - 2021	16,114,181	3,729,413	26,503,000	17,085,501	42,617,181	20,814,914
2022 - 2026	13,075,487	1,013,638	33,379,000	12,578,110	46,454,487	13,591,748
2027 - 2031	6,244,794	96,630	30,528,000	5,274,195	36,772,794	5,370,825
2032 - 2036	39,493	465	8,625,000	1,451,363	8,664,493	1,451,828
2037	-	-	1,950,000	77,805	1,950,000	77,805
Totals	$ 50,429,234	$ 11,265,398	$ 131,817,000	$ 56,578,901	$ 182,246,234	$ 67,844,299

CITY OF FRANKLIN, TENNESSEE
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2011

NOTE 3 - DETAILED NOTES ON ALL FUNDS (Cont.)

F. Long-term Debt (Cont.,)

Debt expense associated with the bond issues was recorded as other assets and is being amortized on a straight-line basis over the life of the issue.

All significant debt covenants and restrictions as set forth in the bond agreements were complied with.

Long-term liability activity for the year ended June 30, 2011, was as follows:

	Beginning Balance	Additions	Reductions/ Amortization	Ending Balance	Due Within One Year
Governmental activities:					
General obligation bonds	$ 122,295,000	$ 32,315,000	$ 22,793,000	$ 131,817,000	$ 6,361,000
Unamortized bond premiums	499,047	891,236	(23,558)	1,413,841	122,609
Deferred amounts from refunding	(196,774)	(470,277)	(68,578)	(598,473)	(80,262)
Total bonds payable	122,597,273	32,735,959	22,700,864	132,632,368	6,403,347
Capital lease obligations	1,881,353	92,743	608,062	1,366,034	629,463
Compensated absences	5,507,375	2,669,120	2,538,207	5,638,288	2,538,207
Total long-term liabilities	$ 129,986,001	$ 35,497,822	$ 25,847,133	$ 139,636,690	$ 9,571,017
Business-type activities:					
Bonds and notes payable	$ 52,299,516	$ 1,066,323	$ 2,936,605	$ 50,429,234	$ 3,038,801
Deferred amounts from refunding	(1,615,495)	-	(145,453)	(1,470,042)	(144,610)
Unamortized bond premiums	1,670,356	-	126,988	1,543,368	113,420
Total bonds and notes payable	52,354,377	1,066,323	2,918,140	50,502,560	3,007,611
Capital lease obligations	-	273,353	95,813	177,540	100,225
Compensated absences	706,727	265,753	294,051	678,429	294,051
Total long-term liabilities	$ 53,061,104	$ 1,605,429	$ 3,308,004	$ 51,358,529	$ 3,401,887

Issuance of Bonds
On July 7, 2010, the City issued $15,725,000 General Obligation Public Improvement Bonds, Series 2010 (Federally Taxable - Recovery Zone Economic Development Bonds), maturing on March 1, 2030, with interest rates ranging from 4.625% to 5.375%. The bonds were issued to provide monies to make public improvements throughout the City.

On October 5, 2010, the City issued $16,590,000 General Obligation Refunding Bonds, Series 2010, maturing on March 1, 2024, with interest rates ranging from 1.75% to 4.00%. The bonds refunded outstanding General Obligation Public Improvement Refunding Bonds, Series 2004, and prepay the City's Series VI-B-1 Loan Agreement with the Public Building Authority of Sevier County, Tennessee. There was no significant economic gain.

Advance Refunding of Debt
During fiscal year 2011, and in prior years, the City defeased certain bonds by placing the proceeds of new bonds in irrevocable trusts to provide for all future debt service requirements on the retired bonds. Accordingly, the trust account assets and the liability for the defeased bonds are not included in the City's financial statements. As of June 30, 2011, outstanding bonds considered as defeased were as follows:

Sewer and Water Revenue and Tax Bonds - 2002B	$20,380,000
General Obligation Public Improvement Bonds - 2004	6,145,000
General Obligation VI-B-1 - 2004	10,225,000
Total	$36,750,000

During September 2011, the City refunded its Business-Type Activities Series 2008 - Tennessee Municipal Bond Fund Variable Rate debt, as described in Note 4-H.

NOTE 3 - DETAILED NOTES ON ALL FUNDS (Cont.)

F. Long-term Debt (Cont.)

Contingent Liability
The City of Franklin entered a standby loan agreement with the City of Franklin Industrial Development Board in December 2005, subsequent to an Industrial Development Board bond issue for $15 million. The bond issue provided funds to purchase land for the site of the Nissan North America Headquarters project, a 500,000 square feet building on a 50 – acre campus in the McEwen Economic Development District of Franklin. The Development District is a tax-increment financing district, created under Tennessee Law, which is designed to provide funds which will retire the bond issue from property taxes on future development.

At the inception of the project, the Industrial Development Board had approximately two years of debt service escrowed. As of January 2008, this escrow was fully spent and the City of Franklin began, as agreed, to make available short-term loans while the proceeds from the Development District were insufficient to cover the debt service. These loans apply only to project years three through seven (2009 through 2013), and cannot exceed $5 million at any time during that period. At present, expected development in the area is proceeding as projected in the debt repayment plan. Through June 30, 2011, the City has lent $2,833,900 to the Industrial Development Board under standby loan agreement. This amount will be repaid through future property taxes on the development.

Industrial Development Bonds
The City, through the Industrial Development Board, has in the past authorized issuance of various Industrial Revenue Bonds to provide financial assistance to private sector entities for the acquisition of industrial and commercial facilities deemed to be in the public interest. The bonds are secured by the property financed and payable solely from payments received on the underlying mortgage loans. Neither the City, State, nor any political subdivision thereof is obligated in any manner for repayment of bonds. Accordingly, the bonds are not reported as liabilities in the accompanying financial statements.

Swap Agreements
The City has two interest rate swap agreements which are considered to be derivative financial instruments under GASB Statement 53, "Accounting and Financial Reporting for Derivative Instruments." Accordingly, the derivatives are reported on the statement of net assets at fair value, and are tested for effectiveness to qualify for hedge accounting.

Both pay-fixed interest rate swap transactions are associated with variable debt. Combining a pay-fixed receive-variable rate swap with variable debt results in "synthetic" fixed rate debt: The economics are similar to fixed rate debt, but another instrument is involved unlike regular fixed rate debt. Each time the City created synthetic fixed rate debt, a comparison and determination was made that the fixed rate on regular debt would have been higher than the fixed rate on the swap.

For both swaps, there are two main strategies the City pursued with respect to each transaction. Each swap can achieve one or more of these strategies. Then as a result of execution of the derivative, its value will change with respect to how prevailing rates on each reporting period compare to when the derivative was put in place. The accumulated changes in fair value, or total fair value of the derivatives are a function of how prevailing interest rates and other market factors affect each transaction at each reporting period. Pursuant to GASB 53, each swap transaction is then evaluated to determine what type of accounting treatment to apply.

CITY OF FRANKLIN, TENNESSEE
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2011

NOTE 3 - DETAILED NOTES ON ALL FUNDS (Cont.)

F. Long-term Debt (Cont.)

(i) Mitigate the effect of fluctuations in variable interest rates. This is the primary function of both swaps where the City pays a fixed rate, and receives a variable rate. In an interest rate environment whose level is generally higher than the rate at which the City is fixed, the swap would result in a positive value to the City. Correspondingly, a lower rate environment than the fixed rate would result in a negative value to the City. The value primarily depends on the overall level of interest rates on the reporting date compared to what the City pays. The overall level of long term interest rates from period to period is the primary driver of changes in value recorded from the investment derivatives where the City pays fixed and receives a variable rate. Interest rates have trended lower since inception of the pay fixed swaps, therefore, the mark-to-market value is generally more negative to the City.

(ii) Reduce interest expense from expected benefit resulting from the difference between short and long term rates. This is the function of the swap where the City receives floating amounts based on a longer term index with the expectation of receiving an ongoing net benefit compared to short term rates paid on the variable bonds being hedged. Longer term interest rates, such as the 5 Year Constant Maturity Swap (CMS) Index, are generally higher than shorter term interest rates, such as a weekly rate, which the City pays on the variable bonds. Therefore, when shorter term interest rates came close to, or exceeded longer term rates, the City entered into a swap whose receipts on the receive floating leg are based on a longer term index that is expected to outperform the payments on the City's variable debt. Part of the fair value of this swap is determined by the prevailing level of short term versus long term rates, that is, the steepness of the yield curve. The higher the level of long term rates compared to shorter term rates, the higher the expected benefit to the City, therefore, the higher the mark-to-market value of the swap. The City pays a fixed rate on this swap transaction, therefore the other part of the value of this swap is determined by the prevailing level of interest rates compared to when the City entered into the swap transaction. Since interest rates have trended lower since inception, the mark-to-market value will be more negative to the City, even though the City may be receiving a net benefit from the receipts based on the 5 Year CMS Index.

2007 Swap Agreement
Effective March 1, 2007, the City entered into an interest rate swap agreement with Depfa Bank in connection with its $20,000,000 Local Government Public Improvement Bonds, Series 101-A-1 variable rate revenue bonds. Under the swap, the City pays a fixed rate of 3.59% and receives a variable payment of 63% of the 5-year London Interbank Offering Rate (LIBOR) (commonly referred to as a constant maturity swap). The swap has an original notional amount of $20,000,000 equal to the outstanding principal balance on the bonds issued. The notional value of the swap decreases on the same schedule as the bond principal payments until termination on June 1, 2037. As of June 30, 2011, none of the original notional amount has been retired.

2005 Swap Agreement
In 2005, the City entered into an interest rate swap agreement with SunTrust Bank in connection with its $4,500,000 variable rate loan from the City of Lawrenceburg Public Building Authority. Under the swap the City makes monthly payments based on a fixed rate of 3.65% and receives monthly payments based on 75% of the one-month LIBOR plus 18 basis points. The swap has a notional amount of $4,500,000 and expires on July 1, 2020. Of the original notional amount, $1,225,000 has been retired as of June 30, 2011. SunTrust may terminate the agreement at any time in the event of a default and the City may terminate the agreement at any time by paying a termination payment in an amount equal to the market value at the date of termination.

Pursuant to GASB 53, the swap transactions were evaluated for hedge effectiveness and the cumulative change in fair value of the transactions is offset by a corresponding deferred outflow on the statement of net assets.

NOTE 3 - DETAILED NOTES ON ALL FUNDS (Cont.)

F. Long-term Debt (Cont.)

Swap Agreement	2007 Swap Agreement with Depfa Bank	2005 Swap Agreement with SunTrust Bank
Original Notional Amount	$ 20,000,000	$ 4,500,000
Less Amount Retired	-	(1,225,000)
Current Notional Amount	$20,000,000	$ 3,275,000
Effective Date	3/1/2007	9/1/2005
Termination Date	6/1/2037	7/1/2020
Final Bond Maturity	6/1/2037	7/1/2020
City pays	3.59% Fixed	3.65% Fixed
Payments made by the City*	$ 718,000	$ 122,004
City Receives*	63% of 5 Year LIBOR CMS	LIBOR x 75% + 0.18%
Payments received by the City*	$ 254,331	$ 12,256
Net receipts/(disbursements)*	$ (463,669)	$ (109,748)
Fair Value of Swap Agreement	$ (1,492,155)	$ (271,688)

* Based on the period July 1, 2010 to June 30, 2011.

The valuations provided are derived from proprietary models based upon well-recognized principles and estimates about relevant future market conditions. The fair values take into consideration the prevailing interest rate environment and the specific terms and conditions of each swap. All fair values were estimated using the zero-coupon discounting method. This method calculates the future payments required by the swap, assuming that the current forward rates implied by the yield curve are the market's best estimate of future spot interest rates. These payments are then discounted using the spot rates implied by the current yield curve for a hypothetical zero-coupon rate bond due on the date of each future net settlement payment on the swaps.

Below is a list of risks inherent in the type of swaps the City entered into:

Tax Risk
The risk that changes or proposed changes in tax laws or events relating to the tax-exempt status of the City's obligations or of tax-exempt obligations generally will cause interest rates on the debt of the City to increase.

Basis Risk
The risk that the interest rate payable by the City on floating rate debt may not exactly coincide with payment made to the City pursuant to an interest rate swap based upon a floating rate index.

Termination Risk
The risk that the City may have to pay a substantial sum of money if either the City or the counterparty chooses to terminate a swap agreement prior to its otherwise stated termination date or if the agreement terminates for some other reason, including the occurrence of an event of default or a termination event in respect of either party to the Agreement.

Credit Risk
The City at June 30, 2011 had no credit risk since the swaps had negative values. If the value were a positive amount, then the City would be exposed to risk with Depfa Bank, with a rating by Moody's/, Standard & Poors/Fitch as of June 30, 2011 of A3/BBB/A-, or SunTrust, with ratings of A2/BBB+/BBB+.

NOTE 3 - DETAILED NOTES ON ALL FUNDS (Cont.)

G. Fund Balances

	General	Multi-Purpose Capital Project Fund	Debt Service Fund	State Street Aid Fund	Sanitation Fund	Road Impact Fee Fund	Facilities Tax Fund	Storm Water Fund	Drug Fund	Hotel / Motel Tax Fund	Transit Authority Fund	CDBG Fund	Totals
Fund balances:													
Non-Spendable	$ 522,733	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ 522,733
Restricted	-	-	-	-	-	-	-	-	269,691	-	-	19,266	288,957
Committed	17,180,294	12,058,809	1,099,568	-	-	-	-	6,095,953	-	1,944,996	-	-	38,379,620
Assigned	-	-	-	-	-	-	-	-	-	-	-	-	-
Unassigned	7,258,739	-	-	-	-	(796,990)	(291,165)	-	-	-	-	-	6,170,584
Total fund balances	$ 24,961,766	$ 12,058,809	$ 1,099,568	$ -	$ -	$ (796,990)	$ (291,165)	$ 6,095,953	$ 269,691	$ 1,944,996	$ -	$ 19,266	$ 45,361,894
Reason for Restriction/Commitment:													
Inventory	$ 522,733	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ 522,733
Stability funds	17,180,294	-	-	-	-	-	-	-	-	-	-	-	17,180,294
Board action limits use of funds	-	12,058,809	1,099,568	-	-	-	-	6,095,953	-	1,944,996	-	-	21,199,326
Restricted by State government	-	-	-	-	-	-	-	-	269,691	-	-	-	269,691
Restricted by Federal government	-	-	-	-	-	-	-	-	-	-	-	19,266	19,266
Unassigned	7,258,739	-	-	-	-	-	-	-	-	-	-	-	7,258,739
Unassigned - negative fund balance	-	-	-	-	-	(796,990)	(291,165)	-	-	-	-	-	(1,088,155)
Total fund balances	$ 24,961,766	$ 12,058,809	$ 1,099,568	$ -	$ -	$ (796,990)	$ (291,165)	$ 6,095,953	$ 269,691	$ 1,944,996	$ -	$ 19,266	$ 45,361,894

Fund Balance Policy – General Fund

The City has a "Fund Balance Policy Statement" specifying the following commitments of fund balance of the General Fund:

Financial Stabilization Reserve – an amount of unreserved fund balance equal to 33% of General Fund budgeted expenditures. The reserve is for covering contingencies, emergencies such as natural and man-made disaster expenditures, cash flow stabilization, debt service, property/casualty/health insurance loss reserves, and other post-employment benefits (OPEB).

Contingency Commitment	$ 2,603,075
Emergency Commitment	2,603,075
Cash Flow Commitment	7,288,609
Debt Service Commitment	1,561,845
Property/Casualty/Health Insurance Commitment	2,082,460
Health Benefits Commitment	1,041,230
	$17,180,294

NOTE 4 - OTHER INFORMATION

A. Risk Management

The City is exposed to various risks of losses related to torts, theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. The City decided it was more economically feasible to join a public entity risk pool as opposed to purchasing commercial insurance for certain general liability, auto liability, errors and omissions, worker's compensation, and physical damage coverage. The City joined the Tennessee Municipal League Risk Pool (TML), which is a public entity risk pool established in 1979 by the Tennessee Municipal League. The City pays an annual premium to the TML for its general liability and casualty insurance coverage. The City continues to carry commercial insurance for all other risks of loss, including employees' health and accident and environmental.

B. Commitments and Contingencies

Grants
Amounts received or receivable from grantor agencies are subject to audit and adjustment by grantor agencies, principally the Federal and State governments. Any disallowed claims, including amounts already collected, may constitute a liability of the applicable funds. The amount, if any, of expenditures which may be disallowed by the grantors cannot be determined at this time although the City's management expects such amounts, if any, to be immaterial.

Litigation
The City is a defendant in various lawsuits; however, the outcome of these lawsuits is not presently determinable. City Management, in consultation with legal counsel, does not expect any possible liability to materially exceed the City's limits of insurance.

Water Purchase Contract
The Water and Sewer Fund is committed under a long-term contract for the purchase of water. Minimum payments under the contract in future years are as follows:

Year Ending June 30,	Amount
2012	$ 46,325
2013	46,325
2014	46,325
2015	46,325
2016-2028	440,083
Total	$ 625,383

Construction Contracts
As of June 30, 2011, construction funds of $9,975,225 are restricted assets of the Water and Sewer Fund. These funds are restricted for future capital projects.

During 2011, various street, public works and park improvement projects were in process. At June 30, 2011, there was approximately $7,981,000 in uncompleted construction projects. These projects are being currently funded by the General, State Street Aid, Solid Waste, Road Impact, Facilities Tax, Storm Water, and Multi-Purpose Capital Project Funds.

NOTE 4 - OTHER INFORMATION (Cont.)

B. Commitments and Contingencies (Cont.)

Fuel-Hedging Program
The City participates in a fuel hedging program with the Metropolitan Government of Nashville and Davidson County. The City's objective is to hedge the changes in cash flows due to market price fluctuations related to a portion of expected purchases of fuel. Through its participation in the program, the City is committed to its portion of the fuel hedge contracts through June 30, 2012. Renewals of the contracts are expected in the normal course of operations. At June 30, 2011, the contracts are in an asset position. The City's portion of the contracts is approximately 6%, which is immaterial to the financial statements.

C. Employee Retirement Systems and Pension Plans

The City of Franklin administers the City of Franklin Employees' Pension Plan and Trust (the "Plan"), a single employer defined benefit pension plan. The assets of the Plan are held for investment and may be used only for the payment of benefits to members of the plan. The Plan's fiscal year ends on December 31. It was deemed impractical to report the financial activity of the Plan as of and for the year ended June 30, 2011. Accordingly, all financial statement information regarding the Plan is as of December 31, 2010 and the year then ended.

Plan Description
Membership of the Plan consisted of the following at January 1, 2011, the date of the latest actuarial valuation:

Retirees participants and beneficiaries	111
Disabled participants	3
Vested terminated participants	109
Active plan members	586
Total	809

The Plan is a single-employer defined benefit pension plan that covers the full time employees (who work 30 hours or more per week and are employed for 1 year) of the City including all departments, except for certain department heads who may opt out of the Plan. The Plan provides retirement, termination and death benefits to plan members and beneficiaries. Cost-of-living adjustments (COLA) to plan members and beneficiaries in receipt of monthly benefits are provided at the discretion of the Board of Mayor and Aldermen. Section 4-204(3)(p) of the City's Charter assigns the Human Resources Director the responsibility to administer the pension program under the direction of the City Administrator. All the benefits and provisions of the Plan are at the discretion of the Board of Mayor and Aldermen consistent with the laws of Tennessee and the Federal government.

The Plan uses the aggregate actuarial cost method to determine the required annual contributions. Because this method does not identify or separately amortize unfunded actuarial accrued liabilities, the information about unfunded status and funding progress is presented using the entry age actuarial cost method. The information presented is intended to serve as a surrogate for the funded status and funding progress of the plan.

Benefits and refunds of the defined benefit plan are recognized when due and payable in accordance with the terms of the plan. The financial statements of the Plan are presented solely in the Comprehensive Annual Financial Report of the City; there are no separate financial statements of the Plan issued. Administrative costs are paid from the pension fund as shown on page 32.

Contributions and Reserves (Funding Policy)
For employees hired before February 15, 2010, the City of Franklin Employees' Pension Plan is funded entirely by the City of Franklin; employees are not required to contribute to the Plan. Additionally, Plan members hired after July 1, 1995 through February 14, 2010 are required to contribute between 3% and 10% of their annual covered salary to a cash balance plan or 401(a) defined contribution plan. Any plan member may also voluntarily contribute between 1% and 10% of their annual covered salary. For these Plan employees, there is also an optional 457 plan available.

NOTE 4 - OTHER INFORMATION (Cont.)

C. Employee Retirement Systems and Pension Plans (Cont.)

Plan members hired on or after February 15, 2010 are required to contribute 5% of their compensation to participate in the Plan. (These employees hired on or after February 15, 2010, may select the City of Franklin 2010 Defined Contribution which also requires a 5% contribution but includes a 5% employer match. An additional 3% may be contributed that would be matched by the City). The Plan changes for employees hired on or after February 15, 2010 was due to a freeze on admittance to the prior non-contributory Pension Plan approved in January 2010. This approval was due to actuarial reports that showed the plan was underfunded and would require substantial increases in annual contributions for many years in order to bring the Plan to a fully-funded level.

The City has no regulatory amount to contribute but has established an informal policy to annually contribute an actuarial determined amount in four (4) quarterly installments on approximately the first day of each quarter during the fiscal year based on the previous January 1 actuarial valuation. The actuarial valuation at January 1, 2011 includes the following assumptions: (a) Interest: (Funding rates) Pre-retirement: 7.5% per year, compounded annually, net of expenses; Post-retirement: 7.5% per year, compounded annually, net of expenses, (b) Projected salary increases: Salaries are assumed to increase at 3.5% per year, (c) Cost of living increase: Post-retirement benefit is assumed to increase at 2.0% per year, (d) RP 2000 Mortality Table, and (e) Retirement dates ranging from 10% at age 55 to 10% at age 70. The Plan has no long-term contracts for contributions to the Plan and no legally required reserves.

Annual Pension Cost and Funded Status and Funding Progress
The City's annual pension cost and net pension obligation (asset) relating to the plan for the year ended June 30, 2011 were as follows:

Annual required contribution	$ 5,077,499
Interest on the net pension obligation (asset)	(145,600)
Adjustment to the annual required contributions	204,585
Annual pension cost	5,136,484
Contributions made	5,282,084
Increase in net pension obligation (asset)	(145,600)
Net pension obligation (asset)	
Beginning of year	(1,941,338)
End of year	$(2,086,938)

The following table presents three-year trend information for the pension plan:

Fiscal Year Ended	Annual Pension Cost	Percentage of Annual Pension Cost Contributed	Net Pension Obligation (Asset)
June 30, 2009	$4,497,443	131.7%	$(1,446,026)
June 30, 2010	$5,589,068	108.9%	$(1,941,338)
June 30, 2011	$5,136,484	102.8%	$(2,086,938)

NOTE 4 - OTHER INFORMATION (Cont.)

C. Employee Retirement Systems and Pension Plans (Cont.)

The funded status of the pension plan as of the valuation date January 1, 2010, the valuation used for June 30, 2011 reporting, is detailed below:

Actuarial accrued liability (a)	$51,465,753
Actuarial value of plan assets (b)	43,406,019
Unfunded actuarial accrued liability (a) - (b)	$ 8,059,734
Funded ratio (b) / (a)	84.34%
Covered payroll (c)	$29,389,625
Unfunded actuarial accrued liability as a percentage of covered payroll [(a) - (b)] / (c)	27.42%

Actuarial valuations of an ongoing plan involve 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 projected salary increases. 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 immediately following the notes to the financial statements, presents multiyear trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liabilities for benefits.

D. Self-Insured Employee Health Insurance

The City provides medical and dental insurance to its employees and retains the risk of loss to a limit of $105,000 per year, per employee. The City has obtained stop/loss commercial insurance policy to cover claims beyond this liability.

All full-time employees of the City are eligible to participate. Claim payments are paid by the Fund of the employee/ claimant. Liabilities are reported when it is probable that a loss has occurred and the amount of the loss can be reasonably estimated.

Claim liabilities are based on estimates of the ultimate cost of claims that have been reported but not settled, and of claims that have been incurred but not reported. The process used to compute claims liabilities does not necessarily result in an exact amount. Changes in the balance of claims liabilities during the past two fiscal years were as follows:

Year Ending	Liability, July 1	Claims and Changes in Estimates	Claims Paid	Liability, June 30
6/30/2011	$ 1,101,323	$ 6,468,654	$ (6,476,488)	$ 1,093,489
6/30/2010	$ 826,491	$ 6,364,356	$ (6,089,524)	$ 1,101,323

NOTE 4 - OTHER INFORMATION (Cont.)

F. Post Employment Benefits

Plan Description
The City of Franklin self-insures its employees for healthcare benefits. Benefits are established and amended by an insurance committee. The City provides health insurance from the date the employee retires up until the age of 65. No health insurance is available to retirees with less than 20 years of service. For retirees after 20 years of service and at least age 62, retirees pay only the employees' rate at the time of retirement. For retirees after 30 years and at least age 55, retirees pay Cobra rates less $705.04/month for family coverage or less $333.25/month for single coverage. (The City pays either the $705.04 or $333.25). Retirees age 61 and under with at least 25 years of service are eligible for insurance under Option II (high deductible plan) at the full rate less $125 per month for single coverage or $275 per month for family coverage.

Funding Policy
The premium requirements of plan members are established and may be amended by the insurance committee. Claims liabilities of the plan are periodically computed using the actuarial and statistical techniques to establish premiums.

Annual OPEB Cost and Funding Status and Funding Progress
The City's annual OPEB cost and net OPEB obligation (asset) for the year ended June 30, 2011 were as follows:

Annual required contribution	$ 328,500
Interest on the net OPEB obligation (asset)	(37,000)
Adjustment to the annual required contribution	-
Annual OPEB cost	291,500
Contributions made	259,300
Decrease in net pension obligation (asset)	32,200
Net OPEB obligation (asset)	
Beginning of year	(672,700)
End of year	$(640,500)

The Government's annual OPEB cost, the percentage of annual OPEB cost contributed to the plan, and the net OPEB obligation for 2011 and the two preceding years were as follows:

Fiscal Year Ended	Annual OPEB Cost	Percentage of Annual OPEB Cost Contributed	Net OPEB Obligation (Asset)
June 30, 2009	$273,800	74.8%	$(527,600)
June 30, 2010	277,600	152.3%	(672,700)
June 30, 2011	291,500	89.0%	(640,500)

NOTE 4 - OTHER INFORMATION (Cont.)

F. Post Employment Benefits

The funded status of the OPEB plans as of the valuation date June 30, 2011, was as follows:

Actuarial accrued liability (a)	$3,679,200
Actuarial value of plan assets (b)	1,027,000
Unfunded actuarial accrued liability (a) - (b)	$2,652,200
Funded ratio (b)/(a)	27.9%
Covered payroll (c)	27,958,552
Unfunded actuarial accrued liability as a percentage of covered payroll [(a)-(b)]/(c)	9.5%

Actuarial valuations involve estimates of the value of reported amounts and assumptions about the probability of events far into the future, and actuarially determined amounts are subject to continual revision as actual results are compared to past expectations and new estimates are made about the future. The schedule of funding progress, presented as required supplementary information immediately following the notes to the financial statements, presents multiyear trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liability for benefits.

Actuarial Methods and Assumptions
Calculations are based on the types of benefits provided under the terms of the substantive plan at the time of each valuation and on the pattern of sharing of costs between the employer and plan members to that point. Actuarial calculations reflect a long-term perspective. Consistent with that perspective, actuarial methods and assumptions used include techniques that are designed to reduce short-term volatility in actuarial accrued liabilities and the actuarial value of assets.

In the June 30, 2011, actuarial valuation, the entry age normal cost funding method was used. The information presented is intended to approximate the funded status and funding progress of the plan. The actuarial assumptions included a 3% investment rate of return (net of administrative costs) and an annual healthcare cost trend of 9.5% initially, reduced by decrements of .25% annually until 3% is reached. The unfunded actuarial accrued liability is being amortized as a level percentage of payroll on a closed basis over a 30 year period beginning with June 30, 2008.

G. Prior Period Adjustment

During fiscal year 2011, the following prior period adjustment was made to the financial statements:

In the statement of net assets, it was determined that the City had not recorded the net pension asset. The City's contributions in excess of the annual required contributions had previously been recorded in the statement of activities. An adjustment of $1,941,338 was made to record the net pension asset at June 30, 2010.

H. Subsequent Event

During September 2011, the City issued $19,430,000 Sewer and Water Revenue and Tax Refunding Bonds, Series 2011 (Series 2011 Bonds). The Series 2011 bonds were issued to provide the funds necessary to refund the aggregate outstanding principal of the City's Series 2008 Tennessee Municipal Bond Fund Variable Rate debt and pay for the costs of issuance. The refunding transaction was completed in order to reduce the City's variable rate exposure in the Water and Sewer Fund. The Series 2011 bonds bear interest at 2.480% and mature in various amounts through May, 2026.