creating a BRIGHT FUTURE

NASHVILLE ELECTRIC SERVICE

2012 annual report

NES

Nashville Electric Service, the nation's 10th-largest public utility, keeps Nashville bright. Here's a look at **NES** by the numbers:

Electric Service Area › 700 square miles

Number of Electric Accounts at Year End › 361,252

Number of Employees › 966

Miles of Distribution Line › 5,722

Project Help Donations › $147,000

Customers Paying Through NES E-bill › 72,000

from the PRESIDENT/CEO

Though the economy has sagged in many of our nation's cities in recent years, Metropolitan Nashville has seen an overall vibrant economy spurred partially by several significant construction projects under way downtown.

Nashville Electric Service is proud to report that some important infrastructure improvements that we made in recent years have positioned the city to take on the additional growth with the confidence that it will have reliable power for many years to come.

This report will provide you with accounts of NES' key role in enabling construction of facilities like our new Music City Center convention hall, a huge addition to the Country Music Hall of Fame and Museum, and a high-rise convention center hotel that will handle part of the expected increase in visitors to our city. In addition, new retail and residential complexes are keeping our core growing and Nashville's workforce employed.

A new state-of-the-art substation and underground wiring feed these places, and NES has used other innovations, such as leasing unused high-speed fiber to area businesses, to help energize our city.

While we have contributed to these many revenue-generating projects for our city, our utility has been judged for the second time in a row as one of the nation's best-run public utilities. Only NES and five other power companies, out of 2,000 nationally, were selected for this honor.

We are also proud of a long list of other achievements we made during the past year. They include restructuring some bonds to save millions of dollars, building on one of the nation's best power infrastructure systems, placing some stricter controls on spending and putting in place training programs for all of our employees. You will find a more detailed list of our past year's accomplishments on Page 13 of this report.

Our surveys and focus groups show that our customers overwhelmingly express satisfaction with our system and our work. I believe this report will show some of the reasons for that customer appreciation.

Decosta Jenkins

Decosta Jenkins
NES President and Chief Executive Officer

creating a BRIGHT FUTURE

The atmosphere in downtown Nashville these days is **electric**. The day-and-night musical excitement generated by honky-tonks along Broadway is supplemented by the sounds of construction work from three huge nearby projects that will total almost 2.5 million square feet when finished.

At the center of much of this activity is Nashville Electric Service, which has been busy in recent years putting in place the infrastructure needed to provide power to the giant projects when they open for visitors to Nashville.

While construction cranes fill the skyline of Nashville just south of Broadway, the NES pieces of this giant puzzle are mostly buried underground.

The much-anticipated Music City Center makes its mark on downtown.

A CITY on the rise
new additions to the skyline

On the rise are three structures that will help further develop Nashville's thriving convention and visitor business, the second-largest industry in the city next to health care:

› The **Music City Center**, which is slated to open early next year, will offer visitors a 1.2 million-square-foot facility in which to hold conventions, parties and meetings. It will have 90,000 square feet of meeting room space and a 57,000-square-foot ballroom, among other amenities. The annual electric bill for this $623 million project will be about $3 million per year, NES estimates.

› The accompanying **Omni Hotel** will feature 800 guest rooms and suites, and will offer visitors another 80,000 square feet of meeting and event space on top of the space available at the Music City Center. This $250 million project will eventually have an annual electric bill of about $2.7 million, estimates show.

› The large **addition to the Country Music Hall of Fame and Museum**, which will adjoin the Omni. This $75 million project will take the size of the facility to 350,000 square feet, including a new 800-seat theater and an education center.

There are other significant construction projects in the area, too, as apartment and condominium developments continue to spring up in the popular Gulch residential and retail area near the new convention center.

Gone from the area is an unslightly cluster of above-ground transformers, all part of a large substation that sat next to Demonbreun Street – right near the city's hockey and entertainment arena. In its place is a new gas-insulated substation which is one-fourth the size of the old one and completely hidden from public view.

The new substation is powered by six 69,000-volt transmission cables, which are fed into it via a 150-foot-deep and 3,000-foot-long tunnel. This helped eliminate some of the above-ground poles and wires on several streets in the downtown area.

Though you don't see them because they are underground, 98,000 feet of various types of cable were added to the Nashville system during the recent upgrades.

Before: *Transformers line Demonbreun Street. In their place now – the Music City Center.*

After: *The NES system downtown is now almost entirely below ground.*

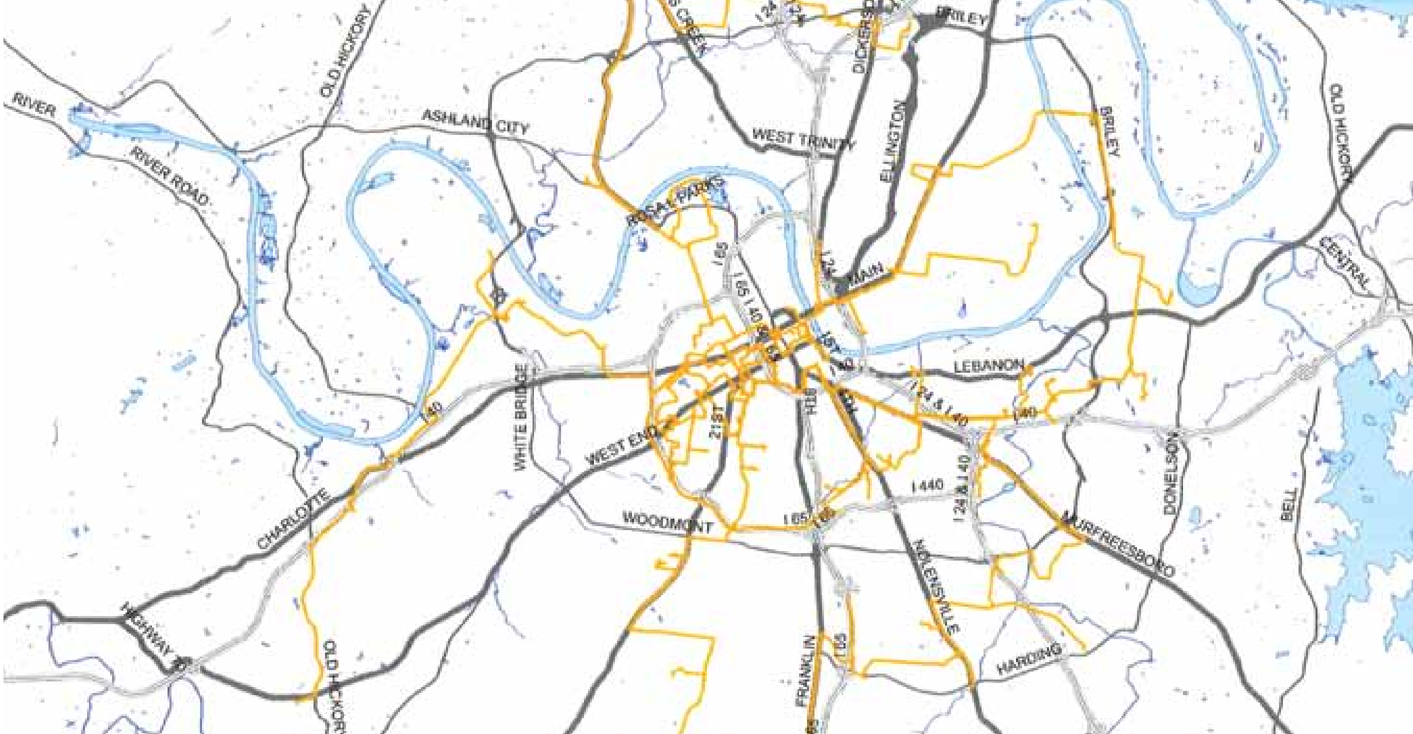
THE KEY
is what you don't see.

"Much of this was done through a cooperative effort between NES and the Music City Convention Center Authority," said NES President and CEO Decosta Jenkins.

"We are very proud of the fact that we have been able to contribute in a significant way to the growth of our convention and visitors industry while at the same time making improvements that help both the vitality and appearance of downtown Nashville."

*Miles of **power lines** wind beneath the streets of downtown, making the city's exciting expansion projects possible.*

Ric Eller and Mike Azevedo of Iris Networks collaborate with Chuck Reinitz and Todd Oney of NES. Iris has used ***NESnet*** *to share the music of Nashville with the world.*



NES net connects Nashville

The twangy guitar riffs that have filled downtown Nashville's famous **Tootsie's Orchid Lounge** for more than 50 years are now also swirling around the globe via the Internet, thanks in great part to fiber-optic lines provided by Nashville Electric Service's **NESnet program**.

In fact, organizations as varied as Nashville's Schermerhorn Symphony Center, a downtown hotel and a local TV station have been using NESnet to provide lightning-fast delivery in a world where speedy communication over the Web is a must.

NES uses its 170 miles of fiber lines to monitor its system across its service area. Each line has multiple fibers, but only a handful of them are used by the utility. The remaining "dark fiber" lines are being offered to organizations and businesses that need the speed, privacy and control that the NESnet system offers.

How fast are these lines? They are 1,000 times faster than the swiftest DSL or cable available. You could download the entire Library of Congress through one line in 35 minutes.

Some of the most innovative uses of the cable in Nashville have resulted when a third party leases the service from NES and helps a business make smart use of it. Such was the case when Ric Eller, now with Iris Networks, had just 13 days to stream live a Béla Fleck concert from the Schermerhorn Symphony Center to the Internet.

He began searching for a provider-partner, and only NES thought the task was possible. NESnet helped him accomplish the Nashville Symphony's goal, and the live Internet stream occurred just as the customer had hoped.

Not only does the NES network offer speed of service, but the network is also reliable. NES owns the lines and the other supporting elements for the network. The network is also efficient and uses only a small percentage of fibers that run through the cable line.

The rest of the fibers are "dark," meaning they aren't in use until someone puts them to use. This someone could be educational institutions, health care providers or organizations that need security and confidentiality. Customers are in control of what is done with their telecommunications equipment at all times, and NESnet will not impede on this.

Nashville Energy Works

raising awareness of the need for home energy upgrades

From May 2011 through July 2012, more than 2,800 in-home energy evaluations were conducted through the **Nashville Energy Works** (NEW) program – a partnership aimed at motivating residents to make home energy upgrades.

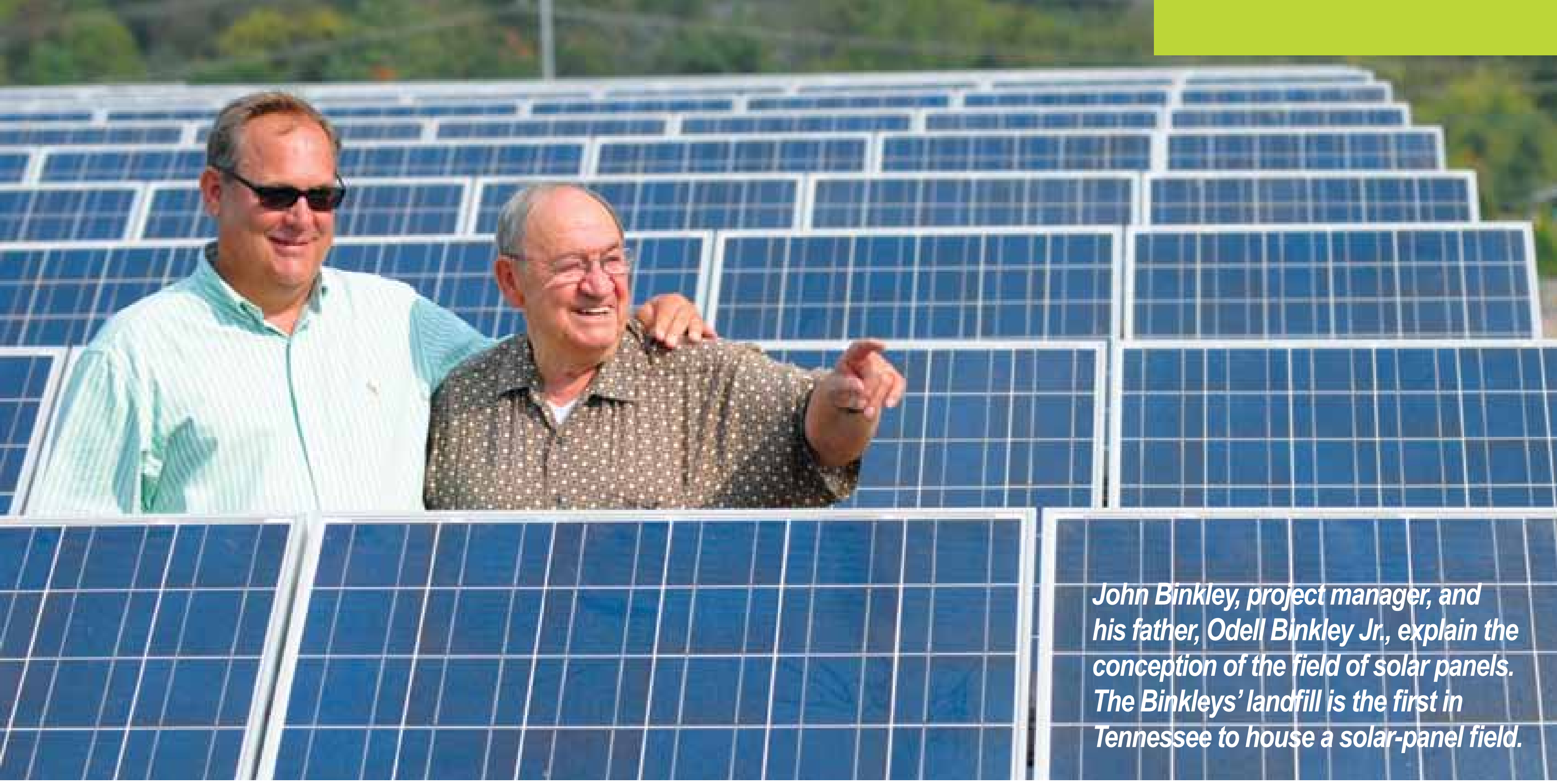
This program accounted for the highest number of energy evaluations ever in the entire seven-state TVA service territory in a 15-month period. Additionally, more than $677,000 in incentives were paid to Nashville homeowners who chose to implement energy-efficiency recommendations.

In the spring of 2011, Mayor Karl Dean's office launched the NEW green initiative. The program is a partnership among Metropolitan Nashville Government, the Tennessee Valley Authority and Nashville Electric Service that is designed to provide Davidson County homeowners with incentives to make home energy upgrades.

Specifically, NEW was launched to increase energy efficiency by raising awareness and making energy-saving improvements more affordable for Middle Tennesseans. Participating homeowners receive free in-home energy evaluations by certified energy advisers with Conservation Services Group, a leader in residential energy-efficiency services.

NEW is funded by a federal stimulus grant from the U.S. Department of Energy through the Southeast Energy Efficiency Alliance.

"The Nashville Energy Works (NEW) program would not be possible without the invaluable partnership of Nashville Electric Service. We are grateful for the utility's unwavering support in making NEW one of the leading energy-efficiency incentive programs in the Southeast," said Dean.



John Binkley, project manager, and his father, Odell Binkley Jr., explain the conception of the field of solar panels. The Binkleys' landfill is the first in Tennessee to house a solar-panel field.

Trash ... to power
Landfill becomes first in Tennessee with solar panels

For anyone who knows the Binkleys of Hermitage, Tenn., it should come as no surprise that family business protocol would not allow an at-capacity construction-debris landfill to sit and remain covered but unused.

And it's certainly not surprising that they did something that's both productive and environmentally friendly with the landfill, given their commitment to sustainability.

With the help of Nashville Electric Service and the federal American Recovery and Reinvestment Act of 2009, the Binkleys installed Tennessee's first solar-panel field at the site of a landfill, and since March 2012 they've been generating 1,000 kilowatt-hours of electricity each day, amounting to a source of energy that could power 150 homes for a year.

John Binkley, who served as the project manager, said doing something with the site that embraced green technology was an easy decision. "It's our responsibility as environmental stewards to do the right thing with our property," he said.

When the landfill reached capacity back in 1999, the Binkleys were unsure what they would do with the property. Regulations required that the landfill be compacted and covered for two years before anything could be done, and that gave them time to explore options. But it wasn't until the adoption of the renewable energy program as part of the federal stimulus package, combined with TVA's existing Green Power Provider Program, that the Binkleys decided it would be feasible to install a solar field and begin selling electricity back to NES. Making the decision easier was the fact that the Binkleys had worked with NES before – in 1981, as part of the Nashville District Corps of Engineers, they were awarded the grounds maintenance contract for NES substations.

After an extensive application process, the Binkleys broke ground on the project in late 2011, and the field of solar panels was completely installed within a few months. As part of the process, they even used the dirt and grass from Vanderbilt University's football field, which was removed for the installation of an artificial field as the landfill project was coming together, furthering their commitment to capitalizing on recycling. Not only are they selling electricity back to NES, but the Binkleys are also generating power for their construction recycling operation at the site. They expect to recoup their investment by 2018.

illuminating students' INNER CURIOSITY

Nashville Electric Service helps educate future scientists through Maplewood High School's Academy of Energy and Power

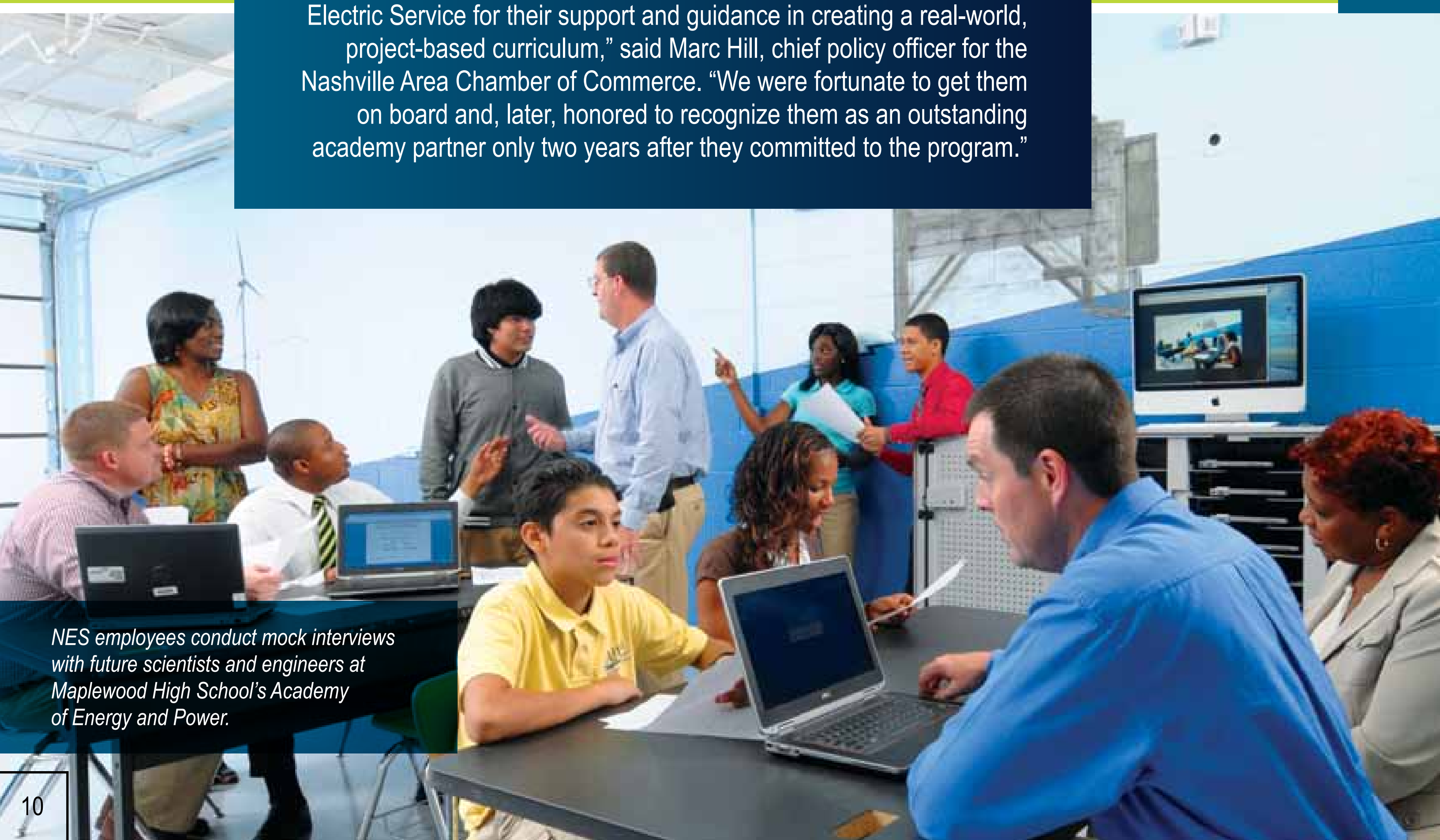
Nashville Electric Service is a proud partner with the Academy of Energy and Power at Maplewood High School. The partnership entails collaborating to create curriculum and course materials, recommending classroom and lab layouts, and mentoring teachers. The relationship allows students interested in the power distribution industry to experience job-shadow and internship opportunities. NES also assists the school with obtaining grants for the program.

The program is part of the Academies of Nashville initiative started by Metro Nashville Public Schools in 2006 and is designed to help students explore a career and choose a focus through which their core academic subjects are taught. Since the program's creation, more than 160 academy partnerships have been formed through the PENCIL Foundation, enabling students to apply their knowledge to real-world situations for deeper learning. PENCIL is a program that matches businesses with schools.

Jointly, Nashville Electric Service and the Academies of Nashville are fostering young engineers and technicians and encouraging students to pursue their passions while gaining a quality education. Forty-two students are enrolled in the program this year.

NES was honored by the Nashville Area Chamber of Commerce with the Academy Partnership of the Year Award in 2012, in the area of engineering, manufacturing and industrial technology.

"The Academies of Nashville depend upon companies like Nashville Electric Service for their support and guidance in creating a real-world, project-based curriculum," said Marc Hill, chief policy officer for the Nashville Area Chamber of Commerce. "We were fortunate to get them on board and, later, honored to recognize them as an outstanding academy partner only two years after they committed to the program."



NES employees conduct mock interviews with future scientists and engineers at Maplewood High School's Academy of Energy and Power.

Herb DeBerry, NES vice president of Human Resources, and PENCIL Foundation Executive Director Connie Williams visit the LP PENCIL Box store, which provides supplies to Metro teachers. NES continued its longtime support of Metro Nashville Public Schools and PENCIL by donating $3,000 to the store. Additionally, NES employees volunteer at Glenn Enhanced Option Elementary School through the PENCIL Foundation.

MAYOR'S WORKPLACE challenge on the rise

When Mayor Karl Dean announced his Workplace Challenge, aimed at making Nashville a "greener, healthier and more involved" working community, it was a no-brainer that Nashville Electric Service would sign up to participate since NES had made supporting the environment, promoting health and giving back priorities long ago.

NES is already a company to watch in the ongoing competition.

The utility was awarded gold seals of recognition in the Healthy and Involved categories and a silver seal of recognition in the Green category.

"To be identified by the mayor's office as a company that is excelling in the Challenge is a real honor and testament to the values that are inherent in our workplace," Communications Supervisor Tim Hill said. "We hope to continue the momentum and end up on the podium in March 2013."

As part of the Challenge, Nashville-based companies like NES will be awarded points based on their commitment to one or more of the following categories:

› **Green:** As a major utility company, it is essential that NES implement green initiatives to minimize its impact on the environment. NES has provided recycling receptacles throughout the office, has added water filters to the water fountains to cut down on the use of plastic bottles, has installed waterless urinals, and has placed timers on lights and copiers, forcing them to turn off when they haven't been used in a certain time period.

› **Healthy:** Aside from climbing up and down poles every day to ensure reliable and safe power, NES employees are healthy. Employees participate in the MTA Easy Ride Program, enjoy free health screenings through the company and are reimbursed by NES for YMCA memberships if they frequent the Y more than a certain number of times a year.

› **Involved:** NES and its employees are philanthropic and support a number of programs designed to help serve the community, including tutoring partnerships with the PENCIL Foundation and Maplewood High School's Academy of Energy and Power. The PENCIL Foundation matches businesses with schools, and it partners in ventures that help the schools. NES also supports the American Heart Association through a variety of employee-led fundraising events.

NES Wins Big

… For the second time in a row

And the Academy Award goes to … Nashville Electric Service!

No, NES didn't take home an Oscar, but it did receive the electric utility industry's equivalent: **The RP_3 Diamond Award**.

NES was selected from more than 2,000 public power utilities nationwide to receive the prestigious award.

With the support of its customers and the continued commitment of its staff, NES will undoubtedly continue to excel and add plenty more awards to its mantel.

In order to win, NES had to receive top marks in categories that are of the utmost importance for any electric company – reliability, sound management and safety.

The award, which only five other utilities across the country received, is a testament to the excellence of NES' staff, not to mention the positive and constructive feedback it receives from its customers.

During the 2011–2012 fiscal year, NES made significant steps within each department of the utility.

A few highlights are:

- *Having the lowest number of per-customer outages since that statistic began being compiled many years ago.*
- *Completing a major underground line tunnel project downtown that will serve the Music City Center and many other customers without above-ground lines.*
- *Conducting aerial inspections of lines to identify areas of strength and weakness and to increase reliability.*
- *Selling and restructuring various bond holdings to create an overall savings of $19.4 million.*
- *Deploying hardware and software across its system that will contribute greatly to the city's "smart grid," which will deliver a more reliable and accurately measured product with fewer interruptions.*
- *Instituting a program that will better manage peak demand hours, creating a savings of $1.3 million on its wholesale power bill.*
- *Receiving a 79 percent approval rating in its most recent written survey of customers. This was the best approval rating of any utility in the area.*
- *Building customer satisfaction through the work of NES' excellent call center. This year, the call center answered and addressed 1.9 million incoming calls overall, and 7,500 calls to the vegetation management hotline.*
- *Receiving the Academy Partnership of the Year Award for its sponsorship of Maplewood High School's Academy of Energy and Power.*
- *Supporting nine local chambers of commerce and remaining a primary sponsor of the Nashville Area Chamber of Commerce's Partnership 2020 economic development effort.*
- *Implementing a new five-year Strategic Plan for NES.*
- *Assisting the mayor's office with several "green" projects, including the Nashville Energy Works and Workplace Challenge initiatives, and obtaining a U.S. Department of Energy grant to reduce the cost of solar installations.*
- *Planning and coordinating multiple fundraisers which brought in nearly $96,000 and blood drives that collected 56 pints of blood. NES also supplied donations and/or volunteers for the Monroe Carell Jr. Children's Hospital at Vanderbilt, the Salvation Army Angel Tree and the Music City Marathon.*
- *Purchasing more than 16 percent of its goods and services through diversity vendors.*
- *Deploying additional companywide safety programs.*

NES HOSTS VISIT

USS Tennessee commander and officers tour new downtown substation

During Nashville Navy Week, NES hosted Commander Richard F. Dubnansky Jr. and officers from the USS Tennessee, an Ohio-class nuclear-powered submarine that has been in commission since 1988.

Naval officers who serve on nuclear submarines are used to being around high-tech equipment in cramped quarters, and NES made them feel right at home during Nashville Navy Week with a tour of the new Peabody Substation. During the substation tour, Navy officers were able to see firsthand how NES used gas-insulation technology to fit the substation into an area with space constraints. This technology is very similar to what the U.S. Navy uses on some of its larger ships.

Extreme home makeover

NES Crews Protect Local Ospreys, Equipment

NES line workers are accustomed to expecting the unexpected, but even seasoned veterans were surprised to discover that a pair of ospreys was calling one of NES' pole tops home. NES crews first noticed the nest in 2008.

Since then, the nest, built at the top of a pole behind the La Vergne Water Treatment Plant, has served as the summer home for the pair of birds every year until they migrate south for the winter.

"The birds, also known as fish hawks, built their nest in a particularly dangerous spot, as the power lines went right through it," said Darrell Mangrum, Overhead Distribution (Donelson). "It's surprising that the birds had not been killed since they were living so close to the wires."

Concerns about the safety of the birds and their young prompted NES crews to lower the existing lines and relocate a transformer that was directly below the nest in order to protect the ospreys from the high-voltage hazard.

Protecting the ospreys from the energized lines also reduces the risk of damage to NES' equipment and decreases the likelihood of an outage at the water treatment plant. The nest was built with fairly large sticks that were several feet long and several inches in diameter. If a stick or bird fell from the nest, a short circuit resulting in a loss of service would likely occur.

"Lowering the lines and relocating the transformer are beneficial to the ospreys as well as to our customers," Mangrum said. Because ospreys are extremely protective of their offspring, lowering the lines and transformer was not an easy task for NES. "It took one bucket crew to rework the lines and another bucket crew to protect the men working from the adult ospreys," Mangrum said. After the chicks hatched and left the nest, crews returned to the pole to further secure the lines and the nesting site.

The U.S. Fish and Wildlife Service was notified of the unusual situation, and continues to monitor the pair as they return each year at breeding time. The agency has been highly complimentary of the care and concern shown by NES and the employees who worked so hard to secure the safety of the ospreys and their young.

Sherry Deutschmann of Letter Logic manages the NES billing process with fellow employees Brian Rawlings, Amanda Flickinger, Carrie Arkle and Matt Brinkley.

Amping Up Local Business

NES supports minority- and women-owned businesses with Supplier Diversity Program

It has been 20 years since NES made a commitment to award 10 percent of its total contracts and purchases to local businesses owned by minorities and women through the NES Supplier Diversity Program.

This year, NES awarded 16 percent of its contracts to these businesses, exceeding its yearly goal of 14 percent for the second straight year, and is on track to award 20 percent of total contracts and purchases next year.

The Supplier Diversity Program isn't just an investment in the local economy, it allows NES to work with great businesses that offer topnotch services and products. A prime example of a locally owned small business providing outstanding service for NES and its customers is Letter Logic, a Nashville-based, woman-owned business that was awarded a bill printing and mailing contract with a potential value of $7.5 million.

Managing the billing process for more than 260,000 NES customers is no small feat, yet this vendor goes above and beyond by making sure to put a green touch on everything. The company's vehicles are energy-efficient. It's not uncommon for its employees to bike to work. And, along with NES, Letter Logic is participating in the Mayor's Workplace Challenge, which puts special emphasis on green efforts.

NES is constantly looking for opportunities to support and stimulate the growth of small businesses in and around Nashville in a sustainable and environmentally friendly way.

Speakers Bureau Sessions

Help Educate Customers About Energy Conservation

What do you think about when you hear the words "Nashville Electric Service"?

Ask the public that question, says Lamar Laws, a member of the NES Speakers Bureau, and you're guaranteed to get people talking – which is exactly why he always asks it first.

"That's a good icebreaker," he said, laughing.

Laws, a senior energy services specialist, has been part of the Speakers Bureau for about 20 years. The bureau was created to educate customers about energy conservation and address misconceptions about NES.

Laws has spoken more than 500 times to groups all over Nashville, and he spends much of his time addressing customers' questions about the little things they do that may contribute to the cost of their electric bills.

To illustrate his point, he tells people about a woman who attended one of his sessions. "She said, 'Mr. Laws, let me just tell you: I don't care if my bill is $1,000; my husband's going to pay it because I'm going to be warm in my house,'" he said. "Boy, everybody got a kick out of that."

Once he gets people talking about their lives, they loosen up. That's when Laws hears the best stories, like the couple whose teenage children took showers "so long that when they came out of the shower, they looked like prunes, just wasting all that water."

Little by little, the humorous stories help customers begin to understand where those costs are coming from, and they want to know how they can take responsibility for their electric bills.

Small things like repairing broken windows, making sure all doors are closed and changing filters go a long way, Laws says, and people are usually surprised how easy it is to save money.

"I tell them, 'You already know this stuff, but you've just got to put it into practice,'" he said.

By the time his sessions are over, Laws says, people see NES as an ally. "If we can help you in any kind of way to lower that bill and still have you real comfortable in your house, that's the ultimate goal. We're there to serve the people in any way we can."

And Laws says his service on the Speakers Bureau has been incredibly rewarding.

"I love just talking with the people," Laws said. "Actually changing their minds? That's the best part."




NASHVILLE ELECTRIC SERVICE

2012 annual report

FINANCIAL REPORT

ELECTRIC POWER BOARD OF THE
METROPOLITAN GOVERNMENT OF
NASHVILLE AND DAVIDSON COUNTY
FINANCIAL STATEMENTS FOR THE YEARS
ENDED JUNE 30, 2012 AND 2011

NES Board Chairman Richard Courtney and
NES President and CEO Decosta Jenkins

FINANCIAL REPORT

ELECTRIC POWER BOARD OF THE METROPOLITAN GOVERNMENT OF NASHVILLE AND DAVIDSON COUNTY

TABLE OF CONTENTS

	Page
SCHEDULE OF EXECUTIVE MANAGEMENT AND THE BOARD	20
INDEPENDENT AUDITORS' REPORT	21
MANAGEMENT'S DISCUSSION AND ANALYSIS	22 - 31
FINANCIAL STATEMENTS FOR THE YEARS ENDED JUNE 30, 2012 AND 2011:	
Statements of Net Assets	32 - 33
Statements of Revenues, Expenses and Changes in Net Assets	34
Statements of Cash Flows	35 - 36
Notes to Financial Statements	37 - 53

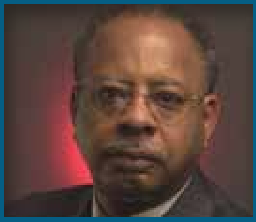
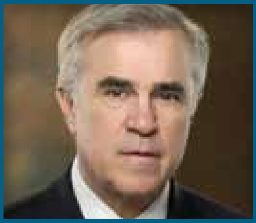
EXECUTIVE MANAGEMENT

Allen Bradley
Executive Vice President and
Chief Operating Officer

Decosta Jenkins
President and
Chief Executive Officer

Teresa Broyles-Aplin
Vice President of Finance and
Administration and
Chief Financial Officer

BOARD MEMBERS

Richard Courtney
NES Board Chairman
Partner
Christianson Patterson
Courtney and Associates

Sam Howard
Chairman
Phoenix Holdings, Inc.

Robert McCabe
Chairman
Pinnacle Financial Partners

Robert J. Mendes
Attorney
Frost Brown Todd, LLC

Yanika Smith-Bartley
Legal Counsel
Asurion

Deloitte & Touche LLP
424 Church Street
Suite 2400
Nashville, TN 37219
USA

Tel: +1 615 259 1800
www.deloitte.com

INDEPENDENT AUDITORS' REPORT

Electric Power Board of the Metropolitan
Government of Nashville and Davidson County
Nashville, Tennessee

We have audited the accompanying statements of net assets of the Electric Power Board of the Metropolitan Government of Nashville and Davidson County (the "Electric Power Board"), a component unit of the Metropolitan Government of Nashville and Davidson County, Tennessee, as of June 30, 2012 and 2011 and the related statements of revenues, expenses and changes in net assets and of cash flows for the years then ended. These financial statements are the responsibility of the Electric Power Board's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. 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 consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Electric Power Board's internal control over financial reporting. Accordingly, we express no such opinion. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and the significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to previously present fairly, in all material respects, the financial position of the Electric Power Board as of June 30, 2012 and 2011 and the changes in its net assets and its cash flows thereof for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 22-31 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 inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Deloitte & Touche LLP

October 31, 2012

As financial management of the Electric Power Board of the Metropolitan Government of Nashville and Davidson County (the "Board"), we offer readers of these financial statements this narrative overview and analysis of the financial activities of the Board for the fiscal years ended June 30, 2012 and 2011 as compared to fiscal years 2011 and 2010, respectively. In conducting the operations of the electrical distribution system, the Board does business as Nashville Electric Service ("NES"). NES is a component unit of the Metropolitan Government of Nashville and Davidson County, Tennessee. This discussion and analysis is designed to assist the reader in focusing on the significant financial issues and activities and to identify any significant changes in financial position. We encourage readers to consider the information presented here in conjunction with the financial statements taken as a whole.

Overview of the Financial Statements

This discussion and analysis is intended to serve as an introduction to NES' financial statements, which are comprised of the basic financial statements and the notes to the financial statements. Since NES is comprised of a single enterprise fund, no fund-level financial statements are shown.

Basic Financial Statements

The basic financial statements are designed to provide readers with a broad overview of NES' finances in a manner similar to that of a private-sector business.

The statements of net assets present information on all of NES' assets and liabilities, with the difference between the two reported as net assets. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of NES is improving or deteriorating. Net assets increase when revenues exceed expenses. Increases to assets without a corresponding increase to liabilities results in increased net assets, which indicates an improved financial position.

The statements of revenues, expenses and changes in net assets present information showing how NES' net assets changed during the fiscal year. All changes in net assets are reported as soon as the underlying event occurs, regardless of timing of related cash flows. Thus, revenues and expenses are reported for some items that will only result in cash flows in future fiscal periods (e.g., earned but unused vacation leave).

The statements of cash flows present changes in cash and cash equivalents resulting from operating, financing, and investing activities. These statements present cash receipts and cash disbursements information, without consideration as to the timing for the earnings event, when an obligation arises, or depreciation of capital assets.

Summary of Changes in Net Assets

Assets exceeded liabilities by $575.9 million at June 30, 2012, and $530.7 million at June 30, 2011. This represents an increase of $45.2 million in 2012 and $28.9 million in 2011.

The largest portion of the Board's net assets reflects its investment in capital assets less any related debt used to acquire those assets that is still outstanding. The Board uses these capital assets to provide service, and consequently, these assets are not available to liquidate liabilities or for other spending.

An additional portion of the Board's net assets represents resources that are subject to external restrictions on how they may be used. These restrictions include bond proceeds to be used for construction projects and reserve funds required by bond covenants.

STATEMENTS OF NET ASSETS ($000 omitted)

	June 30,		
	2012	**2011**	**2010**
ASSETS			
CURRENT ASSETS	$ 367,057	$ 329,741	$ 265,956
INVESTMENT OF RESTRICTED FUNDS	128,354	55,261	91,337
UTILITY PLANT, NET	865,013	842,384	819,335
ENERGY CONSERVATION PROGRAMS' NOTES RECEIVABLE	1,548	884	227
OTHER NON-CURRENT ASSETS	3,100	2,566	2,831
TOTAL ASSETS	1,365,072	1,230,836	1,179,686
LIABILITIES			
CURRENT LIABILITIES	208,789	198,213	168,554
CURRENT LIABILITIES PAYABLE FROM RESTRICTED ASSETS	26,852	22,113	18,350
LONG-TERM DEBT, LESS CURRENT PORTION	548,445	467,103	487,142
OTHER NON-CURRENT LIABILITIES			
Payable to TVA – energy conservation programs	1,493	785	227
Other	3,622	11,926	3,604
	5,115	12,711	3,831
COMMITMENTS AND CONTINGENCIES			
TOTAL LIABILITIES	789,201	700,140	677,877
NET ASSETS			
Invested in utility plant, net of related debt	364,249	358,152	355,501
Restricted	55,435	52,536	52,177
Unrestricted	156,187	120,008	94,131
TOTAL NET ASSETS	$ 575,871	$ 530,696	$ 501,809

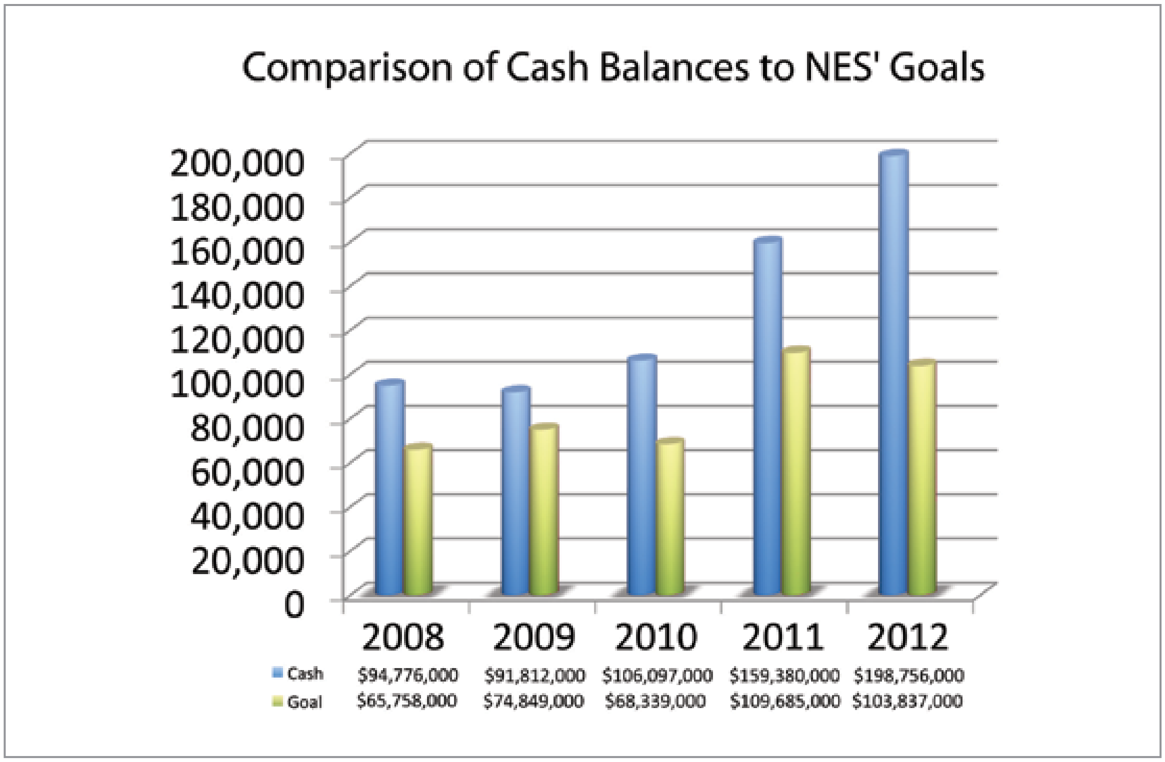
Liquidity and Capital Resources

The Board has sufficient debt capacity and a strong financial position. Therefore, the tax-exempt bond market is expected to be a future source of liquidity to supplement the cash flow from operations. On November 4, 2011, the Board closed on the sale of the Metropolitan Government of Nashville and Davidson County, Tennessee, Electric System Revenue Bonds, 2011 Series A and B. The purpose of the 2011 Series A Bonds was to reimburse NES for a portion of the 2011 capital expenditures and to fund approximately 50 percent of NES' projected $210.0 million Capital Budget for the fiscal years ending June 30, 2012, through June 30, 2014. The remainder will be funded with operating revenues. The par amount of the 2011 Series A Bonds, $100.9 million, plus original issue premium, less underwriter discount, cost of issuance, and a deposit to the debt service reserve fund netted proceeds in the amount of $110.6 million of which $105.0 million was deposited into the Special Construction Fund, $5.4 million in the Debt Service Reserve Fund and $246 thousand into the General Fund. During fiscal year 2012, NES drew down $35.0 million from these funds for capital expenditures. The remaining proceeds will be drawn down quarterly over the next two years. The 2011 Series B Bonds were being offered to refund $101.5 million aggregate principal amount of the 2001 Series A Bonds maturing on May 15, 2012 through 2026, and to refund $51.1 million aggregate principal amount of 2004 Series A Bonds maturing on May 15, 2018 through 2024.

In addition to operating cash flow and proceeds from tax-exempt bonds, the Board has a $25 million line of credit, which is renewed each year. The credit facility is not a source of liquidity for ongoing operations. It is available as an additional funding source in the event of a natural catastrophe.

The Board's financing cost may be impacted by short-term and long-term debt ratings assigned by independent rating agencies. During the fiscal year ended June 30, 2012, the Board's revenue bonds were rated at AA+ by both Standard & Poor's and Fitch. In issuing bond ratings, agencies typically evaluate financial operations, rate-setting practices, and debt ratios. Higher ratings aid in securing favorable borrowing rates, which results in lower interest costs.

Debt ratings are based, in significant part, on the Board's performance as measured by certain credit measures. In order to maintain its strong credit ratings, the Board has adopted certain financial goals. Such goals provide a signal to the Board as to the adequacy of rates for funding ongoing cash flows from operations. One such goal is a cash goal of 10 percent of in-lieu-of-tax payments, purchased power, and operating and maintenance expenses. That goal was met every month of the fiscal year 2012. That percentage was 19.1 percent as of June 30, 2012, and 14.5 percent as of June 30, 2011. The Board also has a goal of maintaining a debt coverage ratio of at least 2-to-1. The Board's debt coverage ratio for the 12 months ended June 30, 2012, was 3.9 to 1. The Board continues to exceed its goals. The outlook on all debt ratings is stable as of June 30, 2012.



Operations

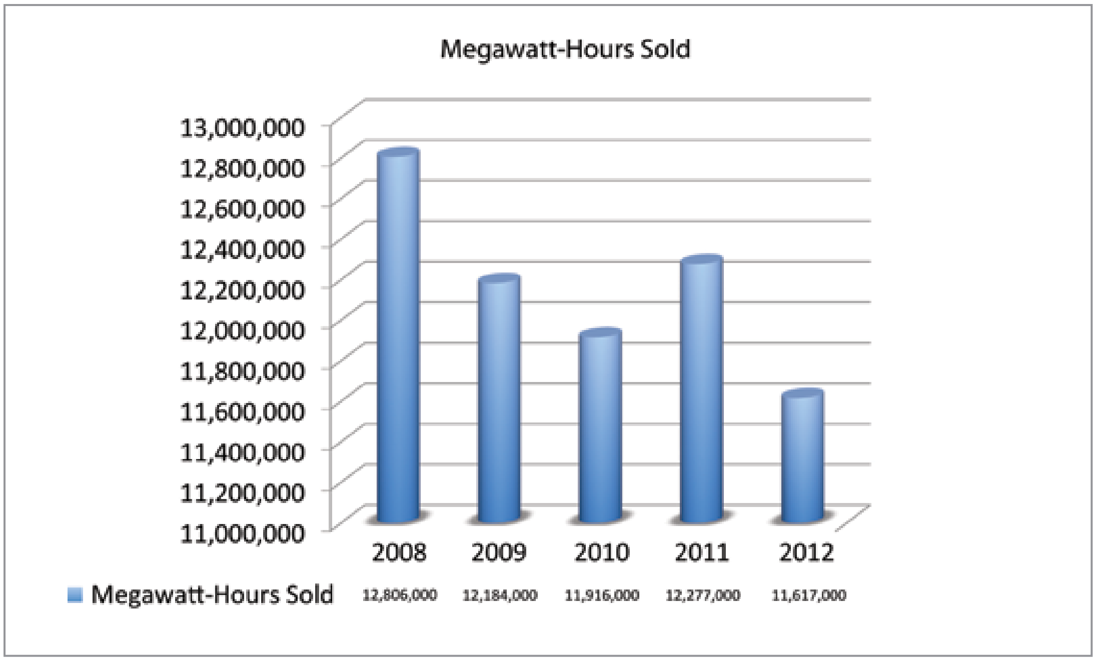
Summary Revenue & Expense Data
($000 omitted)

	Year Ended June 30, 2012	Year Ended June 30, 2011	Net Asset Effect	Year Ended June 30, 2010	Net Asset Effect
Operating Revenues	$1,154,512	$1,199,609	$ (45,097)	$1,063,155	$ 136,454
Purchased Power	868,453	927,065	58,612	816,152	(110,913)
Margin	286,059	272,544	13,515	247,003	25,541
Operating Expenses	141,289	142,189	900	133,314	(8,875)
Depreciation and Tax Equivalents	77,904	75,115	(2,789)	72,840	(2,275)
Interest Income	399	513	(114)	1,328	(815)
Interest Expense	24,100	24,451	351	26,362	1,911
Extraordinary Gain (Loss)	2,010	(2,415)	4,425	(2,110)	(305)
Increase in Net Assets	$ 45,175	$ 28,887	$ 16,288	$ 13,705	$ 15,182

2012 and 2011 Results of Operations

On April 1, 2011, the Tennessee Valley Authority ("TVA") implemented a new wholesale Time of Use rate structure. With the new structure, retail customers are billed under a seasonal rate structure. Retail and Wholesale billing units are misaligned due to timing of meter readings, which will impact retail revenue and wholesale power costs.

Operating Revenues. Operating revenues decreased by $45.1 million, or 3.8 percent, when compared to 2011. Total electric sales were $1.15 billion for the period versus $1.20 billion last year. The average realized rate on electric sales was $.0976 per kilowatt-hour in 2012 compared to $.0961 per kilowatt-hour in 2011. The increase in the average realized rate in 2012 is the result of the 2.20% rate increase passed-through from TVA in October 2011. Megawatt-hours sold in 2012 decreased by 5.4 percent when compared to 2011. Weather plays an important part in determining revenue for any year. The impact of weather is reflected in the comparison of degree-days from one period to the next. Degree-days represent the difference between the weather's average daily temperatures minus 65 degrees. Temperatures above 65 degrees are considered cooling degree-days; temperatures below 65 degrees are considered heating degree-days. Total cooling degree-days were 1,999 in 2012 compared to 2,069 in 2011. Total heating degree-days were 2,812 in 2012 compared to 3,665 in 2011. Total heating and cooling degree-days were 4,811 in 2012 compared to 5,734 in 2011 or a decrease of approximately 16.1 percent. Total average number of active year-to-date customers increased by 0.3 percent when compared to 2011. Revenue in Excess of Net Bills, (Late Charge) decreased by $0.5 million, and Rentals and Electric Property (primarily pole attachments) decreased by $0.2 million.



Non-operating Revenues. Interest income was $0.4 million in 2012 compared to $0.5 million in 2011. The average rate of return on the General Fund was 0.2 percent in 2012 and 2011. The average monthly balance of the General Fund was $148.3 million in 2012 compared to $126.3 million in 2011, an increase of 17.4 percent. Interest income was less than the previous year due to the maturity of a $22.0 million investment in June 2011 that carried an interest rate of 4.25%. The interest rate on the same funds in fiscal year 2012 was 0.23%.

Purchased Power and Operating Expenses. The Board purchases all of its power from TVA under an all-requirements contract that had an initial term of 20 years. Beginning on December 19, 1989, and on each subsequent anniversary thereafter, the contract is automatically extended for an additional one-year period. The contract is subject to earlier termination by either party on not less than 10 years' prior written notice. Purchased power was $868.5 million for the period compared to $927.1 million in 2011. The average realized rate on purchased power was $.072 per kilowatt-hour in 2012 compared to $.070 per kilowatt-hour in 2011. This decrease is due to the pass-through of the Fuel Cost Adjustment ("FCA") and the rate structure change in April 2011. In addition, TVA adjusted purchased power by $20.6 million in March 2012 due to an over-billing at the Old Hickory hydro substation. Megawatt-hours purchased were 12.1 million in 2012 compared to 13.2 million in 2011.

Distribution expenses for the period were $49.2 million compared to $55.7 million last year. This is a decrease of $6.5 million or 11.7 percent. The change is primarily attributable to a decrease in storms, $7.6 million; operation and maintenance miscellaneous expense, $2.4 million; operation and maintenance of overhead lines, $1.9 million; and emergency service, $0.9 million, offset by increases in tree-trimming, $4.3 million; operation and maintenance supervision and engineering, $0.6 million; operation and maintenance of street light and signal system, $0.5 million; operation and maintenance of meters, $0.5 million; operation and maintenance of station equipment, $0.2 million; operation and maintenance mapping, $0.1 million; and private lights, $0.1 million.

Customer Accounts expense and Customer Service and Information expenses combined were $25.1 million for the period compared to $23.7 million last year or an increase of $1.4 million or 5.9 percent. This is primarily the result of an increase in customer orders and service expenses, $0.5 million; customer records and collection, $0.4 million; data processing, $0.2 million; customer assistance costs, $0.2 million; supervision, $0.1 million; and meter reading, $0.1 million.

Administrative and General (A&G) expenses were $67.0 million for the period compared to $62.8 million last year. This was an increase of $4.2 million or 6.7 percent. The increase is primarily the result of increases in employee and retirement benefits, $4.0 million; employees' welfare, $0.7 million; maintenance of general plant, $0.4 million; data processing, $0.4 million; miscellaneous expense, $0.3 million; property insurance, $0.3 million, offset by decreases in injuries and damages, $1.2 million; office supplies and expenses, $0.4 million; and administrative and general salaries, $0.3 million.

Depreciation and Tax Equivalents were $49.3 million and $28.6 million compared to $47.5 million and $27.6 million for 2012 and 2011, respectively. The increase in depreciation was the result of increased investment in the utility plant. Tax equivalents consist primarily of payments in–lieu-of taxes to the Metropolitan Government and the surrounding counties. Such payments are calculated based on a prescribed formula that takes into consideration utility plant value and the average of the Board's last three years' operating margin. The increase in payments in-lieu-of taxes was the result of increases in tax rates coupled with increased investment in the utility plant.

Extraordinary Gain (Loss). In 2011, NES experienced an extraordinary loss due to extensive flooding that impacted the Nashville area in May of 2010. An event is deemed extraordinary if it is both unusual in nature and infrequent in occurrence. The extraordinary loss recognized in 2011 was $2.4 million. It was made up of $1.9 million in expenditures and a reduction to the prior year receivable of $0.5 million. NES received insurance recoveries in the current fiscal year in the amount of $2.0 million that resulted in an extraordinary gain from impairment loss on capital assets and other expenditures.

2011 and 2010 Results of Operations

Operating Revenues. Operating revenues increased by $136.4 million, or 12.8 percent, when compared to 2010. Total electric sales were $1.2 billion in 2011 versus $1.0 billion in 2010. The average realized rate on electric sales was $.0961 per kilowatt-hour in 2011 compared to $.0877 per kilowatt-hour in 2010. The increase in average realized rates in 2011 is the impact of TVA rate adjustments for fuel costs and the rate structure change. Megawatt-hours sold in 2011 increased by 3.0 percent when compared to 2010. In October 2009, TVA increased wholesale rates by 9.0 percent, which increased retail rates by 7.2 percent. The wholesale rate increase and monthly FCA were implemented as a pass-through to our retail customers. Since the increase in wholesale rates and fluctuations in the wholesale FCA were matched by corresponding adjustments in retail rates, there was no significant impact on NES net income. In addition, NES increased retail rates in October 2009 by 3.0 percent which had a direct impact on NES net income. Weather plays an important part in determining revenue for any year. The impact of weather is reflected in the comparison of degree-days from one period to the next. Degree-days represent the difference between the weather's average daily temperatures minus 65 degrees. Temperatures above 65 degrees are considered cooling degree-days; temperatures below 65 degrees are considered heating degree-days. Total cooling degree-days were 2,069 in 2011 compared to 1,730 in 2010. Total heating degree-days were 3,665 in 2011 compared to 3,942 in 2010. Total heating and cooling degree-days were 5,734 in 2011 compared to 5,672 in 2010 or an increase of approximately 1.1 percent. Total average number of active year-to-date customers increased by 0.2 percent when compared to 2010. Revenue in Excess of Net Bills, (Late Charge) increased by $1.0 million, and Rentals and Electric Property (primarily pole attachments) increased $0.7 million.

Non-operating Revenues. Interest income was $0.5 million in 2011 compared to $1.3 million in 2010. The average rate of return on the General Fund was 0.2 percent in 2011 compared to 0.2 percent in 2010. The average monthly balance of the General Fund was $126.3 million in 2011 compared to $102.8 million in 2010, an increase of 22.9 percent. Interest income was less in 2011 due to the additional draw-down of funds from the Construction Fund that were provided by the June 2008 bond issuance.

Purchased Power and Operating Expenses. The Board purchases all of its power from TVA under an all-requirements contract that had an initial term of 20 years. Beginning on December 19, 1989, and on each subsequent anniversary thereafter, the contract is automatically extended for an additional one-year period. The contract is subject to earlier termination by either party on not less than 10 years' prior written notice. Purchased power was $927.1 million in 2011 compared to $816.2 million in 2010. The average realized rate on purchased power was $.070 per kilowatt-hour in 2011 compared to $.065 per kilowatt-hour in 2010. This increase is due to the pass-through of the FCA and the rate structure change in April 2011. Megawatt-hours purchased were 13.2 million in 2011 compared to 12.5 million in 2010.

Distribution expenses for the period were $55.7 million compared to $43.6 million in 2010. This is an increase of $12.1 million or 27.8 percent. The change is primarily attributable to increases in miscellaneous expenses, $5.8 million; operation and maintenance of overhead lines, $2.4 million; storms, $2.1 million; supervision and engineering, $1.5 million; operation and maintenance of street lights, $0.9 million; and operation and maintenance of underground lines, $0.6 million, offset by a decrease in tree-trimming, $1.5 million.

Customer Accounts expense and Customer Service and Information expenses combined were $22.4 million in 2011 compared to $20.2 million in 2010 or an increase of $2.2 million or 10.9 percent. This was primarily the result of an increase in the uncollectible accounts accrual of $1.5

million; customer orders and service expenses of $0.7 million; data processing of $0.3 million, offset by a decrease in customer records and collection of $0.2 million.

Administrative and General (A&G) expenses were $62.8 million in 2011 compared to $68.3 million in 2010. This was a decrease of $5.5 million or 8.0 percent. The decrease is primarily the result of a decrease in employee health insurance, $4.2 million; employee pensions, $1.0 million; outside services employed, $0.6 million; and injuries and damages, $0.4 million, offset by an increase in data processing, $0.5 million; and administrative and general salaries, $0.1 million.

Depreciation and Tax Equivalents were $47.5 million and $27.6 million compared to $46.0 million and $26.8 million for 2011 and 2010, respectively. The increase in depreciation was the result of increased investment in the utility plant. Tax equivalents consist primarily of payments in–lieu-of taxes to the Metropolitan Government and the surrounding counties. Such payments are calculated based on a prescribed formula that takes into consideration utility plant value and the average of the Board's last three years' operating margin. The increase in payments in-lieu-of taxes was the result of increases in tax rates coupled with increased investment in the utility plant.

Extraordinary Loss. NES experienced an extraordinary loss due to extensive flooding that impacted the Nashville area in May of 2010. The extraordinary loss recognized in 2011 was $2.4 million. It was made up of $1.9 million in expenditures and a reduction to the prior year receivable of $0.5 million. The extraordinary loss recognized in 2010 of $2.1 million was made up of $1.0 million in expenditures in excess of the estimated $5.3 million receivable from Federal Emergency Management Agency ("FEMA") and a $1.1 million impairment loss on capital assets.

The following table shows the composition of the operating expenses of the Board by major classification of expense for the last three years:

Major Classifications of Expense ($000 omitted)

Description	Fiscal 2012	Fiscal 2011	Increase (Decrease)	Fiscal 2010	Increase (Decrease)
Labor	$ 56,244	$ 58,338	(3.6%)	$ 48,547	20.2%
Benefits	42,786	39,143	9.3%	46,761	(16.3%)
Tree-trimming	10,652	8,873	20.0%	8,393	5.7%
Outside Services	8,123	8,290	(2.0%)	8,579	3.4%
Materials	1,528	1,722	(11.3%)	3,240	(46.9%)
Transportation	4,184	4,412	(5.2%)	4,324	2.0%
Accrual for Uncollectible Accounts	5,180	5,234	(1.0%)	3,750	39.6%
Postage	1,317	1,323	(0.5%)	1,539	(14.0%)
Security/Police	1,168	1,186	(1.5%)	1,128	5.1%
Rentals	917	992	(7.6%)	738	(34.4%)
Professional Fees	1,162	1,132	2.7%	1,708	(33.7%)
Insurance Premiums	1,025	664	54.4%	688	3.5%
Other	7,003	10,880	(35.6%)	3,879	180.5%
	$141,289	$142,189	(0.6%)	$133,274	6.7%

The Board's total operating expenses decreased 0.6 percent from June 30, 2011 to June 30, 2012. Labor for fiscal year 2012 totaled $56.2 million, which represents a decrease from fiscal year 2011 due to less overtime from fewer storms offset by increases due to cost of living and merit adjustments, step increases, and changes in allocation between O&M and Capital. Benefits increased due to increases in Other Post-Employment Benefits, $4.3 million; and Vision, $0.2 million; offset by a decrease in Medical, $0.5 million. Tree-trimming increased due to additional circuit miles trimmed. Outside services decreased due to cost savings on various services. Materials were less in 2012 due to a FEMA reimbursement for the April 2011 storm damage. Transportation costs are less than in 2012 due to decreased storm restoration. Insurance Premiums increased due to implementation of property insurance program and an increase in Director and Officers coverage. The Other category contains a wide array of smaller accounts. In fiscal year 2012, decreases occurred in work order transfers, $3.7 million; clearing accounts (payroll, transportation, overhead, etc.), $3.1 million; injuries and damages, $0.9 million; transportation, $0.2 million, offset by increases in contract meter readings, $0.6 million; and insurance premiums, $0.4 million.

The Board's total operating expenses increased 6.7 percent from June 30, 2010, to June 30, 2011. Labor for fiscal year 2011 totaled $58.3 million, which represents an increase from fiscal year 2010 due to cost-of-living adjustment, step increases, and changes in allocation between O&M and Capital. This allocation change was a result of an assessment of labor in fiscal year 2010. The labor expense for fiscal 2010 was offset by $4.8 million of Federal Disaster assistance. Benefits decreased due to actuarial valuation results for Retirement and Survivors and Other Post-Employment Benefits. This was offset by an increase in Medical expenses. Tree-trimming increased because a full year of the four-year trim cycle was experienced. The Outside Services decreased due to additional contracts resulting from the May 2010 flood. Material costs were less than in 2010 due to salvageable material, related to the referenced flood, placed back into inventory. Transportation costs were more in 2011 due to increased storm restoration. The Accrual for Uncollectible Accounts increased due to escalated write-offs. Professional Fees decreased due to fewer litigation fees needed. The Other category contains a wide array of smaller accounts.

Capital Assets and Debt Administration

The Board's transmission and distribution facilities serve more than 700 square miles and include the Metropolitan Government of Nashville and Davidson County, Tennessee. The Board also serves portions of the adjacent counties of Cheatham, Rutherford, Robertson, Sumner, Wilson, and Williamson. Such facilities require significant annual capital and maintenance expenditures. The Board's target is to have the capital expenditures funded equally from cash flow from operations and proceeds from tax-exempt bonds. The Board's investment in utility plant at June 30, 2012, was $865.0 million compared to $842.4 million at June 30, 2011. Major projects during fiscal year 2012 included the Smart Grid Project, $11.7 million; completion of the 6th Avenue transmission tunnel and initial cable installation, $8.0 million; substation and feeder breaker replacements at Hermitage substation, $0.6 million; substation and feeder breaker replacements at Finn Street substation, $0.5 million; substation and feeder breaker replacements at Edgehill substation, $0.5 million; transformer installation at Brick Church and 10th Avenue substation, $0.3 million; and transformer installations at East substation, $0.1 million.

The Board has outstanding bonds payable of $569.8 million at June 30, 2012, compared to $482.1 million at June 30, 2011. This increase is due to the issuance of 2011 Series Revenue Bonds. More details about the Board's capital assets and debt can be found in the notes to the financial statements.

Respectfully submitted,

Teresa Broyles-Aplin
Vice President and Chief Financial Officer

Electric Power Board of the Metropolitan Government of Nashville and Davidson County

STATEMENTS OF NET ASSETS ($000 OMITTED)
JUNE 30, 2012 AND 2011

	2012	2011
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	$ 198,756	$ 159,380
Customer and other accounts receivable, less allowance for doubtful accounts of $2,608 and $1,170 respectively	144,702	148,276
Accrued interest receivable	407	11
Materials and supplies	21,041	19,884
Other current assets	2,151	2,190
TOTAL CURRENT ASSETS	367,057	329,741
INVESTMENT OF RESTRICTED FUNDS:		
Cash and cash equivalents	26,212	51,524
Other investments	102,142	3,737
TOTAL INVESTMENT OF RESTRICTED FUNDS	128,354	55,261
UTILITY PLANT:		
Electric plant, at cost	1,417,145	1,366,207
Less: Accumulated depreciation	(552,132)	(523,823)
TOTAL UTILITY PLANT, NET	865,013	842,384
ENERGY CONSERVATION PROGRAMS' NOTES RECEIVABLE	1,548	884
UNAMORTIZED BOND ISSUANCE COSTS	2,812	2,258
OTHER NON-CURRENT ASSETS	288	308
TOTAL ASSETS	1,365,072	1,230,836

See notes to financial statements.

STATEMENTS OF NET ASSETS ($000 OMITTED)
JUNE 30, 2012 AND 2011 (continued)

	2012	2011
LIABILITIES		
CURRENT LIABILITIES:		
Accounts payable for purchased power	163,828	155,802
Other accounts payable and accrued expenses	31,873	29,463
Customer deposits	13,088	12,948
TOTAL CURRENT LIABILITIES	208,789	198,213
CURRENT LIABILITIES PAYABLE FROM RESTRICTED ASSETS:		
Construction contracts payable	2,360	4,349
Accrued interest payable	3,125	2,726
Current portion of long-term debt	21,367	15,038
TOTAL CURRENT LIABILITIES PAYABLE FROM RESTRICTED ASSETS	26,852	22,113
LONG-TERM DEBT, LESS CURRENT PORTION	548,445	467,103
OTHER NON-CURRENT LIABILITIES:		
Payable to TVA—energy conservation programs	1,493	785
Other	3,622	11,926
TOTAL OTHER NON-CURRENT LIABILITIES	5,115	12,711
COMMITMENTS AND CONTINGENCIES		
TOTAL LIABILITIES	789,201	700,140
NET ASSETS		
Invested in utility plant, net of related debt	364,249	358,152
Restricted	55,435	52,536
Unrestricted	156,187	120,008
TOTAL NET ASSETS	$ 575,871	$ 530,696

See notes to financial statements.

STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS ($000 OMITTED)
YEARS ENDED JUNE 30, 2012 AND 2011

	2012	2011
OPERATING REVENUES:		
Residential	$ 470,306	$ 507,787
Commercial and industrial	648,961	656,448
Street and highway lighting	16,165	16,066
Other	19,080	19,308
Total operating revenues	1,154,512	1,199,609
PURCHASED POWER	868,453	927,065
MARGIN	286,059	272,544
OPERATING EXPENSES:		
Distribution	49,199	55,674
Customer accounts	23,570	22,446
Customer service and information	1,520	1,282
Administrative and general	67,000	62,787
Tax equivalents	28,628	27,592
Depreciation	49,276	47,523
Total operating expenses	219,193	217,304
Operating income	66,866	55,240
NON-OPERATING REVENUE (EXPENSE):		
Interest income	399	513
Interest expense	(24,100)	(24,451)
Total non-operating expense	(23,701)	(23,938)
EXTRAORDINARY GAIN (LOSS) – FLOOD	2,010	(2,415)
NET INCREASE IN NET ASSETS	45,175	28,887
NET ASSETS, beginning of year	530,696	501,809
NET ASSETS, end of year	$ 575,871	$ 530,696

See notes to financial statements.

Electric Power Board of the Metropolitan Government of Nashville and Davidson County

STATEMENTS OF CASH FLOWS ($000 OMITTED)
YEARS ENDED JUNE 30, 2012 AND 2011

	2012	2011
CASH FLOWS FROM OPERATING ACTIVITIES:		
Receipts from customers	$ 1,157,563	$ 1,188,306
Payments to suppliers for goods and services	(957,103)	(983,552)
Payments to employees	(47,909)	(48,972)
Payments for tax equivalents	(27,974)	(26,969)
Net cash provided by operating activities	124,577	128,813
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES:		
Acquisition and construction of utility plant	(67,829)	(59,204)
Utility plant removal costs	(8,802)	(10,641)
Salvage received from utility plant retirements	1,104	1,373
Principal payments on revenue bonds	(15,113)	(14,830)
Interest payments on revenue bonds	(32,139)	(29,266)
Proceeds from sale of revenue bonds	110,668	0
Net cash used in capital and related financing activities	(12,111)	(112,568)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of investment securities	(216,917)	(53,778)
Proceeds from sales and maturities of investment securities	118,512	138,023
Interest on investments	3	962
Net cash (used in) provided by investing activities	(98,402)	85,207
NET INCREASE IN CASH AND CASH EQUIVALENTS	14,064	101,452
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	210,904	109,452
CASH AND CASH EQUIVALENTS AT END OF YEAR	$ 224,968	$ 210,904

See notes to financial statements.

Electric Power Board of the Metropolitan Government
of Nashville and Davidson County

STATEMENTS OF CASH FLOWS ($000 OMITTED)
YEARS ENDED JUNE 30, 2012 AND 2011 (continued)

	2012	2011
Reconciliation of operating income to net cash provided		
by operating activities:		
Operating income	$ 66,866	$ 55,240
Adjustments to reconcile operating income		
to net cash provided by operating activities:		
Depreciation	50,909	49,030
Extraordinary gain (loss)–flood	2,010	(2,415)
Changes in assets and liabilities:		
Decrease (increase) in customer and other accounts receivable	3,574	(10,986)
(Increase) decrease in materials and supplies	(1,157)	131
Decrease (increase) in other current assets	39	(96)
Increase in energy conservation programs' notes receivable	(664)	(657)
Decrease in other non-current assets	20	27
Increase in accounts payable for purchased power	8,026	34,039
Increase (decrease) in other accounts payable and accrued expenses	2,410	(4,728)
Increase in customer deposits	140	348
Increase in payable to TVA–energy conservation programs	708	558
(Decrease) increase in other non-current liabilities	(8,304)	8,322
Net cash provided by operating activities	$ 124,577	$ 128,813

NON-CASH CAPITAL AND RELATED FINANCING ACTIVITIES:

Accounts payable associated with the acquisition and construction of utility plant was $2.0 million in 2012 and $3.6 million in 2011.

During 2012 and 2011, NES charged $14.9 million and $18.7 million, respectively, to accumulated depreciation representing the cost of retired utility plant.

During 2012 and 2011, $2.8 million and $0.6 million respectively, were charged to interest expense for amortization of bond premiums. Also, $1.3 million and $553 thousand were charged as amortization of the bond-issuance costs in 2012 and 2011, respectively.

During 2012, the 2011 Series B Bonds were offered to refund $101.455 million and $51.125 million aggregate principal amount of the Board's 2001 Series A and 2004 Series A Bonds, respectively.

See notes to financial statements.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Electric Power Board of the Metropolitan Government of Nashville and Davidson County (the "Board") was established in 1939 when the City of Nashville purchased certain properties of the Tennessee Electric Power Company for the purpose of exercising control and jurisdiction over the electric distribution system. In conducting the operations of the electric distribution system, the Board does business as Nashville Electric Service ("NES"). NES is a component unit of The Metropolitan Government of Nashville and Davidson County, Tennessee (the "Metropolitan Government"), and is operated by a five-member board appointed by the Mayor and confirmed by the Council of the Metropolitan Government. Members of NES serve five-year staggered terms without compensation. In accordance with the Charter of the Metropolitan Government, NES exercises exclusive control and management, except NES must obtain the approval of the Council before issuing revenue bonds. The Metropolitan Government does not assume liability for the financial obligations of NES. In addition, the assets of NES cannot be encumbered to satisfy obligations of the Metropolitan Government. NES appoints a chief executive officer, who is charged with the responsibility for the day-to-day operations, including the hiring of employees.

The financial statements of NES have been prepared in conformity with accounting principles generally accepted in the United States of America. NES maintains its accounts in accordance with the Uniform System of Accounts prescribed by the Federal Energy Regulatory Commission on the accrual basis of accounting. NES is not subject to the jurisdiction of federal or state energy regulatory commissions.

Under Governmental Accounting Standards Board ("GASB") Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*, NES has elected to apply Financial Accounting Standards Board ("FASB") Statements and Interpretations issued after November 30, 1989, except for those that conflict with or contradict GASB pronouncements.

The significant accounting policies followed by NES are outlined below.

Estimates used in the preparation of financial statements are based on management's best judgments. The most significant estimates relate to allowance for uncollectible accounts receivable, useful lives of capital assets, employee benefit plan obligations, and unreported medical claims. These estimates may be adjusted as more current information becomes available.

For purposes of the statements of cash flows, cash and cash equivalents include cash, commercial paper, U.S. Treasury Bills and certificates of deposit with an original maturity of three months or less.

Restricted Assets of NES represent bond proceeds designated for construction and other monies required to be restricted for debt service.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Utility Plant is stated at original cost. Such cost includes applicable general and administrative costs and payroll and related costs such as pensions, taxes and other fringe benefits related to plant construction. Interest cost incurred during the period of construction of certain plant is capitalized. Capitalized interest was $441 thousand in 2012 and $479 thousand in 2011.

When plant assets are disposed of at salvage value, NES charges the amount to accumulated depreciation. Costs of depreciable retired utility plant, plus removal costs, less salvage, are charged to accumulated depreciation.

Depreciation is provided at rates which are designed to amortize the cost of depreciable plant over the estimated useful lives ranging from 7 to 50 years. The composite straight-line rates expressed as a percentage of average depreciable plant were as follows for June 30, 2012 and 2011:

	2012	2011
Distribution plant, 18.2 to 40 years	3.5%	3.5%
Structure and improvements, 40 to 50 years	2.1%	2.1%
Office furniture and equipment, 7.1 to 16.7 years	13.6%	13.6%
Transportation equipment, 8 to 10 years	5.6%	5.9%
Other equipment, 8 to 33.3 years	5.7%	5.3%

Maintenance and repairs, including the cost of renewals of minor items of property, are charged to maintenance expense accounts. Replacements of property are charged to utility plant accounts.

Investments and Cash Equivalents (including restricted assets) consist primarily of short-term U.S. Government securities or mortgage-backed securities from agencies chartered by Congress, and certificates of deposit. In accordance with GASB Statement No. 31, *Accounting and Financial Reporting for Certain Investments and External Investment Pools*, investments are reflected at their fair value except those investments that have a remaining maturity at the time of purchase of one year or less and certificates of deposit, which are reflected at cost.

Materials and Supplies are stated at the moving weighted average cost which approximates actual cost.

Unamortized Bond Issuance costs incurred in connection with the issuance of bonds are being amortized over the respective lives of the bond issues using the effective interest method.

Compensated Absences represent the liability for employees' accumulated vacation days. The general policy of NES permits the accumulation, within certain limitations, of unused vacation days. This amount is included in other accounts payable and accrued expenses in the Statement of Net Assets.

Revenues are recognized from meters read on a monthly cycle basis. Service that has been rendered from the latest date of each meter-reading cycle to month end is estimated and accrued as unbilled revenue receivable.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

NES purchases electric power from the Tennessee Valley Authority ("TVA"). On April 1, 2011, TVA implemented a new wholesale Time of Use rate structure. With the new structure, retail customers are billed under a seasonal rate structure. In addition, wholesale rates are now billed based on energy use and demand charges. Prior to this, the cost of purchased power was calculated based upon retail billing units adjusted for estimated line losses.

Asset Retirement Obligations are periodically reviewed and management has concluded that, at present, NES does not have any such asset retirement obligations.

Operating and Non-operating Revenues and Expenses - Operating revenues include the sale of power and rental of electric property. Operating expenses include direct and indirect costs to operate and maintain the electric distribution system, including purchased power, fuel, depreciation, customer accounts, tax equivalents, and general and administrative costs. Non-operating revenues and expenses consist of interest income and expense.

Income Taxes - NES is not subject to federal or state income taxes. While NES is not subject to property tax, NES pays tax equivalents in-lieu-of taxes to the Metropolitan Government and surrounding counties. Such payments are calculated based on a prescribed formula that takes into consideration utility plant value and the average of the Board's last three years' operating margin.

Recent Accounting Pronouncements - In April 2012, GASB issued two Statements addressing important practice issues for state and local governments. Statement No. 65, *Items Previously Reported as Assets and Liabilities,* clarifies the appropriate reporting of deferred outflows of resources and deferred inflows of resources to ensure consistency in financial reporting. Statement No. 66, *Technical Corrections—2012,* enhances the usefulness of financial reports by resolving conflicting accounting and financial reporting guidance that could diminish the consistency of financial reporting. The provisions of both Statements are effective for periods beginning after December 15, 2012. NES does not expect adoption of these standards to have a material impact on its financial statements.

In June 2012, GASB issued two Statements addressing important practice issues for state and local governments. Statement No. 67, *Financial Reporting for Pension Plans*, improves financial reporting primarily through enhanced note disclosures and schedules of required supplementary information that will be presented by the pension plans that are within its scope. Statement No. 68, *Accounting and Financial Reporting for Pensions*, improves the decision-usefulness of information in employer and governmental nonemployer contributing entity financial reports and will enhance its value for assessing accountability and interperiod equity by requiring recognition of the entire net pension liability and a more comprehensive measure of pension expense. The provisions for the Statement No. 67 are No. 68 are effective for periods beginning after June 15, 2013, and June 15, 2014, respectively. NES has yet to determine the impact of the adoption of these standards on NES' financial position, results of operations, or cash flows.

Purchased Power Adjustments – The Tennessee Valley Authority adjusted purchased power in March 2012 in the amount of $20.6 million due to over-billings by TVA at the Old Hickory hydro substation.

2. UTILITY PLANT AND ACCUMULATED DEPRECIATION

Utility plant activity for the years ended June 30, 2012 and 2011, was as follows ($000 omitted):

	Balance June 30, 2011	Additions	Transfers & Retirements	Balance June 30, 2012
Distribution plant	$ 1,164,718	$ 56,152	$ (8,862)	$ 1,212,008
Land and land rights	1,139	-	-	1,139
Structures and improvements	46,610	1,667	-	48,277
Office furniture and equipment	40,743	3,112	(1,968)	41,887
Transportation equipment	7,198	839	(763)	7,274
Other equipment	38,513	4,325	(3,310)	39,528
Construction work-in-progress (a)	67,286	-	(254)	67,032
	$ 1,366,207	$ 66,095	$ (15,157)	$ 1,417,145

	Balance June 30, 2010	Additions	Transfers & Retirements	Balance June 30, 2011
Distribution plant	$ 1,124,772	$ 53,976	$ (14,030)	$ 1,164,718
Land and land rights	1,139	-	-	1,139
Structures and improvements	44,984	1,626	-	46,610
Office furniture and equipment	38,219	2,886	(362)	40,743
Transportation equipment	7,244	367	(413)	7,198
Other equipment	36,446	5,998	(3,931)	38,513
Construction work-in-progress (a)	69,326	-	(2,040)	67,286
	$ 1,322,130	$ 64,853	$ (20,776)	$ 1,366,207

(a) Represents the net activity to the construction work-in-progress account after transfers to plant accounts.

2. UTILITY PLANT AND ACCUMULATED DEPRECIATION (continued)

The related activity for accumulated depreciation for the years ended June 30, 2012 and 2011, was as follows ($000 omitted):

	Balance June 30, 2011	Provision	Original Cost	Cost of Removal	Salvage	Balance June 30, 2012
Distribution plant	$ 439,430	$ 41,651	$ (8,861)	$ (8,802)	$ 875	$ 464,293
Structures and improvements	16,885	988	-	-	-	17,873
Office furniture and equipment	39,977	5,642	(1,968)	-	-	43,651
Transportation equipment	2,765	407	(762)	-	136	2,546
Other equipment	24,766	2,221	(3,311)	-	93	23,769
	$ 523,823	$ 50,909	$ (14,902)	$ (8,802)	$ 1,104	$ 552,132

	Balance June 30, 2010	Provision	Original Cost	Cost of Removal	Salvage	Balance June 30, 2011
Distribution plant	$ 422,779	$ 40,297	$ (14,027)	$ (10,641)	$ 1,022	$ 439,430
Structures and improvements	15,946	939	-	-	-	16,885
Office furniture and equipment	34,967	5,371	(362)	-	1	39,977
Transportation equipment	2,383	426	(397)	-	353	2,765
Other equipment	26,720	1,997	(3,948)	-	(3)	24,766
	$ 502,795	$ 49,030	$ (18,734)	$ (10,641)	$ 1,373	$ 523,823

Depreciation is either capitalized as a cost of utility plant or reported as depreciation expense in the statements of revenues, expenses and changes in net assets.

3. CASH AND INVESTMENTS

Cash and investments consist of the following ($000 omitted):

2012

	Cash	Bond Funds	Special Construction	Total	Weighted Average Maturity (Years)
Cash and cash equivalents	$ 198,756	$ 25,014	$ 1,198	$ 224,968	-
U.S. Treasury Investments	-	4,172	-	4,172	0.38
Securities from Agencies Chartered by Congress	-	29,374	68,596	97,970	0.69
	$ 198,756	$ 58,560	$ 69,794	$ 327,110	0.21

2011

	Cash	Bond Funds	Special Construction	Total	Weighted Average Maturity (Years)
Cash and cash equivalents	$ 159,380	$ 51,524	$ -	$ 210,904	-
Securities from Agencies Chartered by Congress	-	3,737	-	3,737	-
	$ 159,380	$ 55,261	$ -	$ 214,641	-

Investments of $56.9 million in U.S. Treasury Investments and Securities from Agencies Chartered by Congress are reported at fair value as of June 30, 2012. There were no investments reported at fair value in U.S. Treasury Investments, Securities from Agencies Chartered by Congress, commercial paper and certificates of deposit held at June 30, 2011. Investments of $45.2 million and $3.7 million held in U.S. Treasury Investments and Securities from Agencies Chartered by Congress are reported at cost at June 30, 2012 and 2011, respectively.

The net decrease in the fair value of investments was $25.9 thousand and $1.2 million in fiscal years 2012 and 2011, respectively. The amounts take into account all changes in fair value (including purchases and sales) that occurred during the years.

3. CASH AND INVESTMENTS (CONTINUED)

Custodial Credit Risk – As of June 30, 2012 and 2011, NES' cash and cash equivalents held by financial institutions was $224.9 million and $210.9 million, respectively. Bank balances for such accounts totaled $150.6 million and $109.9 million, respectively. Deposits in financial institutions are required by State of Tennessee ("State") statute to be secured and collateralized by the institutions. The collateral must meet certain requirements and have a total minimum market value of 105 percent of the value of the deposits placed in the institutions less the amount protected by federal depository insurance. Collateral requirements are not applicable for financial institutions that participate in the State's collateral pool. As of June 30, 2012 and 2011, all of NES' deposits were held by financial institutions, which participate in the bank collateral pool administered by the State Treasurer. Participating banks determine the aggregated balance of their public-fund accounts for the Metropolitan Government. The amount of collateral required to secure these public deposits is a certain percentage set by the State, depending on the financial institution, and must be at least that percentage of the average daily balance of public deposits held. Collected securities required to be pledged by the participating banks to protect their public-fund accounts are pledged to the State Treasurer on behalf of the bank collateral pool. The securities pledged to protect these accounts are pledged in the aggregate rather than against each individual account. The members of the pool may be required by agreement to pay an assessment to cover any deficiency. Under this additional assessment agreement, public-fund accounts covered by the pool are considered to be insured for purposes of credit risk disclosure.

Credit Risk – NES is authorized to invest in obligations of the U.S. Treasury and U.S. governmental agencies, securities from agencies chartered by Congress, certificates of deposit, commercial paper rated A1 or equivalent and bonds of the State of Tennessee. Each of these investments is registered or held by NES or its agent in NES' name.

Concentration of Credit Risk – NES has a policy prohibiting investment of greater than $5 million or 20 percent of the total investment portfolio in any one issue, except for the U.S. Government or any of its agencies. In 2012, 96.0 percent of NES' investments are in Securities from Agencies Chartered by Congress. In 2011, 100 percent of NES' investments are in Securities from Agencies Chartered by Congress.

Interest Rate Risk – NES restricts its investments to maturities less than two years from the date of settlement as a means of managing exposure to fair value losses arising from changes in interest rates.

4. LONG-TERM DEBT

Long-term debt for the year ended June 30, 2012, is as follows ($000 omitted):

	Balance June 30, 2011	Deductions/ Repayments	Additions/ Amortization/ Accretion	Balance June 30, 2012
Electric System Revenue Bonds, 1996 Series A, bear interest at rates from 5.5% to 6%, maturing through May 15, 2013, interest paid semiannually.	$ 18,369	$ (5,158)	$ (6,967)	$ 6,244
Electric System Revenue Bonds, 1998 Series A, bear interest at rates from 5.125% to 5.40%, maturing through May 15, 2023, interest paid semiannually.	24,644	-	1,344	25,988
Electric System Revenue Bonds, 1998 Series B, bear interest at rates from 4.75% to 5.50%, maturing through May 15, 2017, interest paid semiannually.	33,342	(4,855)	33	28,520
Electric System Revenue Bonds, 2001 Series A, bear interest at rates from 4.50% to 5.125%, maturing through May 15, 2017, interest paid semiannually.	100,899	(101,455)	556	-
Electric System Revenue Bonds, 2001 Series B, bear interest at 5.50%, maturing through May 15, 2014, interest paid semiannually.	18,509	-	(39)	18,470
Electric System Revenue Bonds, 2004 Series A, bear interest at rates from 4.50% to 5.00%, maturing through May 15, 2029, interest paid semiannually.	109,383	(51,125)	(285)	57,973
Electric System Revenue Bonds, 2008 Series A, bear interest at rates from 3.25% to 5.00%, maturing through May 15, 2033, interest paid semiannually.	103,720	(2,860)	(195)	100,665
Electric System Revenue Bonds, 2008 Series B, bear interest at rates from 3.25% to 5.00%, maturing through May 15, 2023, interest paid semiannually.	73,275	-	(131)	73,144
Electric System Revenue Bonds, 2011 Series A, bear interest at rates from 1.50% to 5.00%, maturing through May 15, 2036, interest paid semiannually.	-	(2,110)	110,542	108,432
Electric System Revenue Bonds, 2011 Series B, bear interest at rates from 2.00% to 5.00%, maturing through May 15, 2026, interest paid semiannually.	-	(130)	150,506	150,376
	482,141	$ (167,693)	$ 255,364	569,812
Less current portion of long-term debt	(15,038)			(21,367)
	$ 467,103			$ 548,445

4. LONG-TERM DEBT (continued)

Long-term debt for the year ended June 30, 2011, is as follows ($000 omitted):

	Balance June 30, 2010	Deductions/ Repayments	Additions/ Amortization/ Accretion	Balance June 30, 2011
Electric System Revenue Bonds, 1996 Series A, bear interest at rates from 5.5% to 6%, maturing through May 15, 2013, interest paid semiannually.	$ 29,828	$ (5,510)	$ (5,949)	$ 18,369
Electric System Revenue Bonds, 1998 Series A, bear interest at rates from 5.125% to 5.40%, maturing through May 15, 2023, interest paid semiannually.	23,361	-	1,283	24,644
Electric System Revenue Bonds, 1998 Series B, bear interest at rates from 4.75% to 5.50%, maturing through May 15, 2017, interest paid semiannually.	33,281	-	61	33,342
Electric System Revenue Bonds, 2001 Series A, bear interest at rates from 4.50% to 5.125%, maturing through May 15, 2017, interest paid semiannually.	102,937	(2,060)	22	100,899
Electric System Revenue Bonds, 2001 Series B, bear interest at 5.50%, maturing through May 15, 2014, interest paid semiannually.	18,540	-	(31)	18,509
Electric System Revenue Bonds, 2004 Series A, bear interest at rates from 4.50% to 5.00%, maturing through May 15, 2029, interest paid semiannually.	109,379	-	4	109,383
Electric System Revenue Bonds, 2008 Series A, bear interest at rates from 3.25% to 5.00%, maturing through May 15, 2033, interest paid semiannually.	106,690	(2,770)	(200)	103,720
Electric System Revenue Bonds, 2008 Series B, bear interest at rates from 3.25% to 5.00%, maturing through May 15, 2023, interest paid semiannually.	77,956	(4,490)	(191)	73,275
	501,972	$ (14,830)	$ (5,001)	482,141
Less current portion of long-term debt	(14,830)			(15,038)
	$ 487,142			$ 467,103

4. LONG-TERM DEBT (continued)

NES issues Revenue Bonds to provide funds primarily for capital improvements and for refundings of other bonds. All bond issues are secured by a pledge and lien on the net revenues of NES on parity with the pledge established by all bonds issued. Annual maturities on all long-term debt and related interest are as follows for each of the next five fiscal years and in five-year increments thereafter ($000 omitted):

Year	Principal	Interest
2013	$ 21,367	$ 28,706
2014	26,270	23,673
2015	27,525	22,408
2016	28,735	21,195
2017	22,792	27,404
2018-2022	142,279	100,611
2023-2027	142,055	48,602
2028-2032	84,430	18,689
2033-2036	32,035	3,541
	527,488	$ 294,829
Unamortized premium	51,938	
Unamortized loss on reacquired debt	(9,614)	
Total long-term debt	$ 569,812	

On November 4, 2011, the Board closed on the sale of the Metropolitan Government of Nashville and Davidson County, Tennessee, Electric System Revenue Bonds, 2011 Series A and B. The purpose of the 2011 Series A Bonds was to reimburse NES for a portion of the 2011 capital expenditures and to fund approximately 50 percent of NES' projected $210.0 million Capital Budget for the fiscal years ending June 30, 2012, through June 30, 2014. The remainder will be funded with operating revenues. The par amount of the 2011 Series A Bonds, $100.9 million, plus original issue premium, less underwriter discount, cost of issuance, and a deposit to the debt service reserve fund netted proceeds in the amount of $110.6 million of which $105.0 million was deposited into the Special Construction Fund, $5.4 million in the Debt Service Reserve Fund and $246 thousand into the General Fund. During fiscal year 2012, the Board drew down $35.0 million from these funds for capital expenditures. The remaining funds will be drawn down quarterly over the next two years. The par amount of the 2011 Series B Bonds, $137.3 million, plus original issue premium and transfer from prior debt service funds, less underwriter discount and cost of issuance resulted in a deposit into an escrow fund of $159.1 million. The 2011 Series B Bonds were being offered to refund $101.5 million aggregate principal amount of the 2001 Series A Bonds maturing on May 15, 2012 through 2026, and to refund $51.1 million aggregate principal amount of 2004 Series A Bonds maturing on May 15, 2018 through 2024. The advance refunding resulted in a difference between the reacquisition price and the net carrying amount of the old debt of $7.3 million. This difference, reported in the accompanying financial statements as a deduction from long-term debt, is being charged to operations through the year 2026 using the effective-

4. LONG-TERM DEBT (continued)

interest method. The Board completed the advance refunding to reduce its total debt service payments over the next 14 years by $24.9 million and to obtain an economic gain of $1.8 million.

The following bond issues have been defeased through advanced refundings; therefore, the balances indicated, which are still outstanding at June 30, 2012, do not appear as liabilities on the Board's Statement of Net Assets:

1998 Series A Bonds	$ 74,430,000
2001 Series A Bonds	99,290,000
2004 Series A Bonds	51,125,000
	$ 224,845,000

NES had a $25 million unsecured line of credit through January 2012 and in 2011 to be used for purchased power in case of a natural disaster. Borrowings under this line of credit bore a negotiated interest rate. There were no borrowings under this line of credit at its expiration in January 2012 or at June 30, 2011. Furthermore, the Company renewed the line of credit effective July 1, 2012.

5. OTHER NON-CURRENT LIABILITIES

NES' other non-current liabilities consist primarily of TVA energy conservation program loans and customer contributions. The following table shows the activity for the year ($000 omitted):

June 30, 2011	Repayments	Additions	June 30, 2012
$ 12,711	$ (16,804)	$ 9,208	$ 5,115

June 30, 2010	Repayments	Additions	June 30, 2011
$ 3,831	$ (7,545)	$ 16,425	$ 12,711

NES is a fiscal intermediary for the TVA energy conservation programs whereby loans are made to NES' customers to be used in connection with TVA's Residential Energy Services Program. Pursuant to the terms of an agreement with TVA, the energy conservation loans made to NES' customers are funded and guaranteed by TVA. During 2011, NES received an advance payment of $10 million from TVA for the Smart Grid Pilot Program.

6. PENSION PLAN

The Nashville Electric Service Retirement Annuity and Survivors' Plan (the "Plan") is a single employer defined benefit pension plan administered by NES. The Plan provides retirement and survivors' benefits to members and beneficiaries. Cost-of-living adjustments are provided to members and beneficiaries annually. The Charter of the Metropolitan Government assigns the authority to establish and amend benefit provisions to NES. The Plan is not required to issue a separate financial report.

At June 30, 2012, all full-time regular employees under age 65 are eligible to participate in the Plan. Employees hired after June 30 are eligible to participate in the Nashville Electric Service Defined Contribution Plan. The vesting provision of the Plan provides for five-year cliff vesting. NES employees who retire at or after age 65 are entitled to annual retirement benefits payable monthly for life in an amount equal to 2 percent of final average compensation multiplied by years in the Plan not in excess of 35 years.

Final average compensation is the average compensation in the 36 consecutive months in which compensation is highest. Unused sick leave may be used to increase credited service and benefit percentage under certain circumstances. Early retirement is an option beginning at age 55 with 15 years of credited service or at age 50 with 30 years of credited service with an actuarially-reduced monthly benefit.

If the participant has attained age 55, and his/her age plus service is 85 or greater, then there is no reduction for early receipt of the benefit. However, a participant cannot use accumulated sick leave to increase effective age to meet the requirements for this unreduced benefit. For a participant with 25 or more years of service, the minimum pension benefit is $1,800 per month.

The contribution requirements of NES are established and may be amended by NES. The Plan is currently non-contributory. NES' practice is to typically fund at least the minimum contribution for a 30-year funding level. The current rate is 33.24 percent of annual covered payroll. NES contributed 100 percent of the required contribution for the Plan years 2012 and 2011.

The annual required contribution for the current year was determined as part of the April 1, 2011, actuarial valuation using the frozen initial liability method. The actuarial assumptions included (a) 8.0 percent investment rate of return and (b) projected salary increases of 4.5 percent. Both (a) and (b) included an inflation component. The assumptions include cost-of-living post-retirement benefit increases equal to 2 percent per year. The actuarial value of Plan assets is determined using techniques that smooth the effects of short-term volatility in the market value of investments over a three-year period. The unfunded actuarial accrued liability is being amortized over 30 years. The required schedule of funding progress below presents multi-year trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liability for benefits.

6. PENSION PLAN (continued)

A change was made in the plan funding method effective April 1, 2009, whereby the amortization period was reset to a 30-year period beginning April 1, 2009. The result of this funding method change was a decrease in the normal cost of the plan of $11.0 million and an increase in the Plan's actuarial accrued liability of $120.5 million.

Schedule of employer contributions for the past three years is shown below ($000 omitted):

Plan Year	Annual Required Contribution	Percentage Contributed
2012	$ 21,713	100%
2011	22,877	100%
2010	23,765	100%

Schedule of funding progress for the past three years is shown below ($000 omitted):

Actuarial Valuation Date	Actuarial Value of Assets	Actuarial Accrued Liability (AAL) Entry Age	Unfunded Actuarial Accrued Liability (UAAL)	Funded Ratio	Covered Payroll	Unfunded Actuarial Accrued Liability as a Percent of Covered Payroll
	(a)	(b)	(b-a)	(a/b)	(c)	(b-a)/c
4/1/2012	$ 318,502	$ 477,101	$ 158,599	66.80%	$ 69,419	228.47%
4/1/2011	291,658	441,801	150,143	66.00%	67,300	223.10%
4/1/2010	254,919	419,353	164,435	60.80%	66,879	245.87%

In 1994, NES established a non-qualified Supplemental Executive Retirement Plan (the "SERP"). The SERP was limited to certain employees of NES. Benefits accrued at the rate of 5 percent of salary for each year of credited service not to exceed 12 years and vests at the rate of 20 percent for each year of service, reduced by the percentage accrued and vested under NES' qualified plan. Effective April 1, 2005, the Board merged the SERP with the NES Retirement Annuity and Survivors' Benefit Plan. Adding the SERP benefits to the Plan increased the funding requirements for the Plan, but the amounts that had accumulated in the SERP Trust were transferred to the Plan in order to offset those increased costs. Future payments that would have been made into the SERP Trust will be directed into the Plan.

At the time of conversion, no benefits had been paid from the SERP. Any change in funding requirements is reflected in the above schedule.

Effective July 1, 2012, Nashville Electric Service established a Defined Contribution Retirement Plan for all new participants. This plan is intended to be a defined contribution money purchase pension plan. Its purpose is to provide retirement benefits to eligible employees. All full-time regular employees not vested in the Retirement Annuity and Survivors' Plan or hired after July 1, 2012, are eligible.

7. DEFERRED COMPENSATION PLAN

NES has a deferred compensation plan (the "457 Plan") created in accordance with Internal Revenue Code ("IRC") Section 457. The 457 Plan, which is available to all full-time employees, permits employees to defer a portion of their salary until future years. Employees may contribute up to the legal limit of their compensation to the 457 Plan with NES providing a matching contribution of up to 3 percent of compensation. The 457 Plan provides that assets or income of the 457 Plan shall be used for the exclusive purpose of providing benefits for participants and their beneficiaries or defraying reasonable expenses of administration of the 457 Plan. Since the assets of the 457 Plan are held in custodial and annuity accounts for the exclusive benefit of 457 Plan participants, the related assets of the 457 Plan are not reflected on the statements of net assets. Employees contributed $3.4 million during each of the years ended June 30, 2012 and 2011. NES contributed $1.9 million and $1.8 million to the 457 Plan for the years ended June 30, 2012 and 2011, respectively.

8. POST-EMPLOYMENT BENEFITS

In addition to the pension benefits described in Note 6 and the deferred compensation benefits described in Note 7, NES provides post-retirement medical, dental, and life insurance benefits to all employees who retire from NES under the provisions of the qualified plan and supplemental executive retirement plan. Medical and dental benefits are also provided to their spouses. As of June 30, 2012, approximately 571 retirees meet those eligibility requirements. Expenses for these post-retirement benefits have previously been recognized as retirees report claims. Those incurred claims totaled $10.0 million and $9.0 million for the years ended June 30, 2012 and 2011, respectively. During the year ended June 30, 2008, NES implemented the provisions of GASB Statement No. 45, *Accounting and Financial Reporting by Employers for Post-Employment Benefits Other Than Pensions.* These provisions were applied prospectively with respect to NES' Other Post-Employment Benefits (OPEB) Plan. GASB Statement No. 45 requires the accrual of OPEB obligations over the working careers of plan members rather than as claims are incurred. The total expenses that were recognized were $18.1 million during each of the years ended June 30, 2012 and 2011.

The NES OPEB Plan is a single-employer defined benefit plan funded through an irrevocable trust that was established during the year ended June 30, 2008. The OPEB Plan is not required to issue a separate financial report.

NES' annual OPEB cost (expense) is calculated based on the annual required contribution (ARC), an amount actuarially determined in accordance with the parameters of GASB Statement No. 45.

The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and to amortize any unfunded actuarial liabilities (or funding excess) over a 30-year period beginning April 1, 2009. The current rate is 25.68 percent of annual covered payroll. NES contributed 50 percent of the required contribution for the Plan year. The remaining 50 percent was funded by June 30, 2012.

Actuarial valuations involve estimates of the value of reported amounts and assumptions about the probability of events in the future. Amounts determined regarding the funded status of the plan and the annual required contributions of NES are subject to continual revision as actual results are compared to past expectations and new estimates are made about the future. The

8. POST-EMPLOYMENT BENEFITS (continued)

required schedule of funding progress presented below provides multiyear trend information that shows whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liability for benefits.

Projections of benefits are based on the substantive plan (the plan as understood by NES and plan members) and include the types of benefits in force at the valuation date and the pattern of sharing benefit costs between NES and the plan members to that point. Actuarial calculations reflect a long-term perspective and employ methods and assumptions that are designed to reduce short-term volatility in actuarial accrued liabilities and the actuarial value of assets. Significant methods and assumptions were as follows:

Actuarial valuation date: April 1, 2012

Actuarial cost method: Entry age, normal method

Amortization method: Level percentage of pay, open

Remaining amortization period: 30 years, closed

Asset valuation method: Adjust expected assets on the valuation date toward market value of assets by an amount equal to one-third of the difference between expected and market asset values.

The actuarial assumptions included (a) 8.0 percent investment rate of return and (b) projected salary increases of 4.5 percent. Both (a) and (b) included an inflation component. The assumptions include health care cost trend rate increases equal to 5 percent per year.

Schedule of employer contributions for the past three years is listed below:

Plan Year	Annual Required Contribution	Percentage Contributed
2012	$ 18,041,316	50%
2011	18,123,818	100%
2010	17,776,342	100%

Schedule of funding progress for the past three years is shown below ($000 omitted):

Actuarial Valuation Date	Actuarial Value of Assets	Actuarial Accrued Liability (AAL) Entry Age	Unfunded Actuarial Accrued Liability (UAAL)	Funded Percentage	Covered Payroll	Unfunded Actuarial Accrued Liability as a Percent of Covered Payroll
	(a)	(b)	(b-a)	(a/b)	(c)	(b-a)/c
4/1/2012	$ 36,894	$ 223,058	$ 186,164	16.54%	$ 74,623	249.5%
4/1/2011	34,650	249,243	214,593	13.90%	$ 70,245	305.5%
4/1/2010	22,532	248,269	225,737	9.10%	69,216	326.1%

9. LEASES

Total rental expense entering into the determination of net operating income amounted to approximately $1.0 million in both 2012 and 2011, respectively. Rental expense consists primarily of payments for facilities rental and leasing arrangements for software licensing. NES leases these facilities and software under various cancelable lease agreements. Rental income is received under pole-attachment leases, which are accounted for as operating leases. These leases are cancelable. Therefore, future minimum rentals under these leases are not significant. Rental income from this source totaled $2.1 million and $2.4 million for the years ended June 30, 2012 and 2011, respectively.

10. RISK MANAGEMENT AND LIABILITY

NES is exposed to various risks of loss related to torts; theft or damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. NES is an agency of the Metropolitan Government and is covered under the Tennessee Governmental Tort Liability Act, TCA 29-20-101, et al, (the "Act") and is self-insured under the act for tort liability. NES is immune from any award or judgment for death, bodily injury and/or property damage in excess of the limits as set forth in the Act. Therefore, NES has not secured insurance coverage in excess of such limits. As of June 30, 2011, NES was a participant in the Metropolitan Government Insurance Pool (the "Pool") for coverage of most property losses. The Pool is operated as a common risk management and insurance program for several public entities, including NES, the Metropolitan Nashville Airport Authority, the Metropolitan Transit Authority and the Department of Water and Sewerage Services. The Pool is self-sustaining through member premiums. NES subrogates for all losses paid out for the negligence of other parties.

At June 30, 2012, NES is no longer a participant of the Pool. With some of the sub-limits of the Pool coverage being reached as a result of the damage sustained by many participants of the Pool during the flood of 2010, NES deemed it prudent to withdraw from the Pool and obtain commercial property insurance that would no longer have shared sub-limits.

NES is self-insured for employee medical, dental and vision claims and self-insured up to $100,000 for employee medical claims. The changes in the insurance reserves for medical, dental and vision benefits for the years ended June 30, 2012 and 2011, are as follows ($000 omitted):

Balance—June 30, 2010	$ 1,764
Payments	(19,777)
Incurred claims	19,994
Balance—June 30, 2011	1,981
Payments	(19,417)
Incurred claims	19,987
Balance—June 30, 2012	$ 2,551

NES continues to carry commercial insurance for all other risks of loss, including a retention with excess workers' compensation coverage and employee health and accident insurance. Settled claims resulting from these risks have not exceeded commercial insurance coverage in any of the past three fiscal years.

10. RISK MANAGEMENT AND LIABILITY (continued)

NES is party to various lawsuits filed against it in the normal course of business. Management does not believe that damages, if any, arising from outstanding litigation, will have a material effect on the financial position of NES.

11. RELATED PARTY TRANSACTIONS

NES had related party balances and transactions as a result of providing electric power to the Metropolitan Government and entities of the Metropolitan Government, as well as making tax-equivalent payments to the Metropolitan Government and other payments to entities of the Metropolitan Government. These balances and transactions as of and for the years ended June 30, 2012 and 2011, are summarized as follows ($000 omitted):

	2012	2011
Balances:		
Accounts receivable	$ 2,479	$ 2,337
Accounts payable	-	-
Transactions:		
Commercial and industrial revenue—Metropolitan Government Entities	58,963	57,416
Street and highway lighting revenue—Metropolitan Government Entities	6,347	6,266
Tax equivalents operating expense—Metropolitan Government Entities	26,562	25,917

In addition to the receivables above, NES also has a receivable from the Nashville Convention Center Authority of $9.4 million and $7.3 million in 2012 and 2011, respectively.

12. FAIR VALUE OF FINANCIAL INSTRUMENTS

Fair Value of Financial Instruments has been determined by NES using available market information. However, judgment is required in interpreting market data to develop the estimates of fair value. Accordingly, the fair values are not necessarily indicative of the amounts that NES could realize in a current market exchange. The carrying amounts of cash and short-term investments, investments of special funds, accounts receivable and accounts payable are a reasonable estimate of their fair value. The fair value of NES' long-term debt is estimated to be $624.0 million and $514.1 million at June 30, 2012 and 2011, respectively.

13. EXTRAORDINARY GAIN (LOSS) – FLOOD

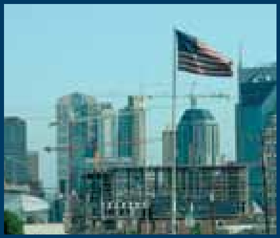
NES experienced significant damage and loss in connection with heavy rainfall and flooding in the Metro Nashville /Davidson County area in May 2010. The flooding resulted in the declaration of a Federal Disaster area by the Federal Emergency Management Agency. For the fiscal year ended June 30, 2012, NES received insurance recoveries in the amount of $2.0 million, which resulted in an extraordinary gain.

At June 30, 2011, NES recorded an extraordinary loss of $2.4 million in damages to reflect the unusual and infrequent nature of the damage and related loss to NES' assets and the associated costs of restoration, repair and replacement. The $2.4 million extraordinary loss was made up of $1.9 million in expenditures and a reduction to the prior year FEMA receivable of $0.5 million.

"Nashville Electric Service is proud to report that some important infrastructure improvements that we made in recent years have positioned the city to take on the additional growth with the confidence that it will have reliable power for many years to come."

Decosta Jenkins

2012 NES Annual Report photo credit: Dean Dixon, Dean Dixon Photography



NES

NASHVILLE ELECTRIC SERVICE

1214 CHURCH STREET • NASHVILLE, TN 37246

(615) 736-6900 • NESPOWER.COM