

**Comprehensive Annual
Financial Report**

Bristol Tennessee Essential Services

A Municipal Electric Utility
of the City of Bristol, Tennessee

Year ended June 30, 2007

Prepared by:

Accounting and Finance Department and CEO



Beth Ringley
Director of Management Services



R. Michael Browder
CEO

Bristol Tennessee Essential Services Comprehensive Annual Financial Report

Year ended June 30, 2007

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Bristol Tennessee Essential Services

Electric • Internet • Telephone • Cable

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December 11, 2007

To the Chairman and Members of
the Board of Directors of Bristol Tennessee
Essential Services

Letter of Transmittal

The Comprehensive Annual Financial Report (“CAFR”) of Bristol Tennessee Essential Services (“BTES”), a self-supporting governmental enterprise fund of the City of Bristol, Tennessee operated under the general supervision and control of a five-member Board of Directors as per Chapter 32 Public Acts of Tennessee 1935, for the fiscal year ended June 30, 2007, is submitted herewith.

The CAFR was compiled by the staff of the Accounting and Finance Department with the close cooperation of our independent auditor. It represents the official report of BTES' financial operations and conditions to the citizens, the Board of Directors, BTES management, rating agencies and other interested parties.

Responsibility for the accuracy of the presented data and the completeness and fairness of the presentation, including all disclosures, rests with BTES. We believe the data, as presented, are accurate in all material respects and are presented in a manner designed to fairly set forth the financial position and results of operations and cash flows of BTES.

All disclosures necessary for the reader to gain a thorough understanding of BTES' financial condition have been included.

In order to meet the needs of a broad spectrum of financial statement readers, the CAFR is presented in four sections:

- Introductory Section
- Financial Section
- Statistical Section
- Internal Control and Compliance Section

The **Introductory Section** includes the table of contents, this transmittal letter, an organizational chart of BTES, BTES' general philosophy, background of BTES and a brief recap of fiscal year 2007.

The **Financial Section** is composed of the report of independent auditors; Management Discussion and Analysis (“MD&A”), including a narrative introduction, financial overview and financial analysis; and the financial statements. This letter of transmittal is designed to complement the MD&A and should be read in conjunction with it. The notes to the financial statements are considered an integral and essential part of adequate disclosure and fair presentation of the financial statements.

Letter of Transmittal (continued)

The **Statistical Section** includes selected financial and demographic trend information. The tables within this section differ from certain information in the financial section in that they represent some non-accounting data covering ten fiscal years. These data were accumulated through BTES statistical collection.

The **Internal Control and Compliance Section** includes the Report of Independent Auditors on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards*.

The accompanying financial statements present the financial position, results of operations and cash flows of BTES, in accordance with the requirements of the Governmental Accounting Standards Board ("GASB").

This report does not include the financial activities of the City of Bristol, Tennessee. Financial reports are available directly from the City of Bristol, Tennessee.

Bristol, Tennessee is located in the northeastern portion of the state. It is one of three cities in Sullivan County, with the other two being Kingsport and Bluff City. The population of Sullivan County is 153,500. Its industrial base is primarily manufacturing, followed by the service sector and agriculture.

Because of its central location in the eastern United States, Bristol is within 600 miles of approximately 53% of the population of the United States. Interstate 81 passes through the city. Bristol is part of the consolidated metropolitan statistical area (CSA) of Bristol, Johnson City and Kingsport, commonly called the Tri-Cities CSA. With a population of 493,796 people, the Tri-Cities CSA is the 66th largest in the United States.

Bristol benefits from the state's high ranking in Alexander Grant and Company's GENERAL MANUFACTURING CLIMATES, which ranks Tennessee near the top in the nation as a place for manufacturing.

Bristol is a good place to work and live, with the following amenities:

- Excellent health care facilities
- Seven Tennessee Valley Authority lakes with 2,200 miles of shoreline
- Five national parks
- Bristol Motor Speedway (Two NASCAR dates per year with over 160,000 seats)
- Low crime rate
- Four distinct seasons
- Excellent schools
- Nine colleges and universities (Degrees ranging from Art to Medicine)
- Seven beautiful golf courses

Bristol and the surrounding areas continue to grow and prosper. Eastman Chemical Company is headquartered in Sullivan County. Exide's Super Battery Plant is in Bristol where they build and charge over 35,000 batteries per day. Several facilities have expanded this year. Touchstone Wireless moved most of their operation from their Blackley Road facility to a facility located on West State Street in 2006. They are continuing to grow and now employ 594 people. Royal Mouldings, the largest marketer and manufacturer of decorative polymer moldings in the United States, has completed a 250,000-square-foot expansion to their existing 150,000-square-foot building located in the Bristol Industrial Park.

Letter of Transmittal (continued)

FINANCIAL INFORMATION

BTES AS AN ENTERPRISE FUND

BTES operates under an independent Board of Directors as an enterprise fund of the City of Bristol, Tennessee. This being the case, BTES funds its expenditures through its rates and charges and receives no income from City taxes. BTES establishes rates annually to provide for anticipated cash outlays for operating expenses and capital improvement requirements.

ACCOUNTING SYSTEM AND BUDGETARY CONTROL

BTES' financial accounting system is based on accounting principles generally accepted in the United States of America. Internal accounting controls are an integral part of BTES' accounting process and are designed to provide reasonable, but not absolute, assurance that assets are safeguarded from unauthorized use or disposition and that records used for preparing financial statements and maintaining asset accountability are reliable.

BTES applies Financial Accounting Standards Board ("FASB") pronouncements issued on or before November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements, in which case, GASB prevails. Consistent with other public utility enterprise funds, BTES has elected not to adopt the FASB Statements and Interpretations issued after November 30, 1989, in accordance with GASB Statement No. 20, "Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting."

BTES' Board of Directors approves BTES' annual budget for its recommended rate, expenses and capital outlays. An analysis of revenue and operating expenses for the year ended June 30, 2007, is provided in the Financial Section of this report.

PLANT

Plant is stated at cost, which includes cost of contract work, labor, materials and allocated indirect charges. Major renewals and betterments are capitalized, while minor replacements and repairs are expensed as incurred. Property, plant and equipment are depreciated using the straight-line method at rates which will amortize costs over the estimated useful lives of the assets. The provision for depreciation does not include depreciation on transportation equipment per Federal Energy Regulatory Commission Guidelines. Those amounts are reported as operation expenses in the Statements of Revenues, Expenses and Changes in Net Assets. The cost of plant retired, together with removal costs less salvage, is charged to accumulated depreciation when property is removed from service.

CASH MANAGEMENT

BTES' moneys are deposited in banks insured by the FDIC. Investments permitted include obligations of the U.S. Treasury and U.S. agencies and certificates of deposit. Temporary investments, consisting entirely of certificates of deposit, are stated at cost which approximates fair value. The cash management performance for the year ended June 30, 2007, produced interest earnings of \$1,666,545.

Letter of Transmittal (continued)

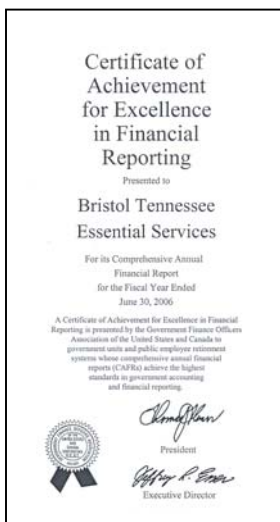
RISK MANAGEMENT

BTES' assets are protected through a third party insurance provider. Through this provider, coverage is provided for workers' compensation, comprehensive, general and automobile liability, auto physical damage, crime and fiduciary, errors and omissions, property, boiler and machinery and pollution. BTES has not experienced a loss in excess of insurance coverage in any of the past three fiscal years.

INDEPENDENT AUDIT

BTES has an annual audit performed by independent certified public accountants. The firm of Coulter & Justus, P. C., was selected by the Board of Directors. The auditor's report on the financial statements is included in the Financial Section of this report.

AWARDS



For the first time, the Government Finance Officers Association ("GFOA") awarded a Certificate of Achievement for Excellence in Financial Reporting to BTES for its CAFR for the fiscal year ended June 30, 1997. BTES was also awarded the certificate for its CAFR for the fiscal years ended June 30, 1998, 1999, 2000, 2001, 2002, 2003, 2004, 2005 and 2006. To qualify for this prestigious award, BTES issued an easily readable and efficiently organized CAFR. In addition, this report satisfied both accounting principles generally accepted in the United States of America and applicable legal requirements.

A Certificate of Achievement is valid for a period of one year only. We believe that our present report continues to meet the program's requirements, and we are submitting it to the GFOA to determine eligibility for another certificate.

ACKNOWLEDGMENTS

The preparation of this report could not have been accomplished without the staff of BTES. We express our sincere appreciation to those who assisted and contributed to its preparation.

Sincere appreciation is also expressed to Sam Coulter, CPA, Ricky Jackson, CPA, Adam Allen, CPA and the staff at Coulter & Justus, P.C., for assistance throughout the year pertaining to various financial matters and for their assistance in the preparation of this report.

In closing, we would like to thank the members of the Board of Directors of Bristol Tennessee Essential Services for their interest and support in planning and conducting the operations of BTES in a responsible and progressive manner.

Respectfully submitted,

Beth Ringley
Director of Management Services

R. Michael Browder
Chief Executive Officer

BACKGROUND INFORMATION

On June 30, 1945, the Tennessee Valley Authority (TVA) purchased the properties of East Tennessee Light and Power Company. Bristol Tennessee Electric System, now called Bristol Tennessee Essential Services (BTES), was started July 1, 1945 as a result of a referendum in which the citizens of Bristol, Tennessee voted to purchase from TVA a portion of these properties. A \$1.3 million issue of Electric Light and Power bonds was required to finance the transaction. BTES immediately agreed to terms of a 20-year power contract for TVA to supply power which BTES distributed to the public at substantially lower rates.

As per Chapter 32 Public Acts of Tennessee 1935 and the contract with TVA, a five-member board of directors was established by the city to have general supervision and control of the municipally-owned electric system with one member serving from City Council. Current board members include Chairman Patrick W. Hickie, Jr., CPA, Vice-Chairman Bryan K. Boyd, Pereda R. "Pete" Paty, J. Scott MacMorran and City Council Representative David K. Shumaker.

The International Brotherhood of Electrical Workers (IBEW) has represented the trades and crafts employees since prior to TVA purchasing the system from East Tennessee Light and Power.

Sixty BTES employees serve over 32,000 customers in Bristol and Sullivan County in Tennessee and a portion of Washington County, Virginia - approximately 280 square miles of service area.

BTES purchases electric power from TVA, the nation's largest public power generator of electricity. Our customers pay approximately 6.69 cents per kilowatt hour, while the national average is 8.9 cents per kilowatt hour. BTES has had seven rate reductions since June 1982 with the most recent in October 1997. This does not include changes in wholesale power costs from TVA. In October 2003, TVA added an environmental charge to their rate to cover the cost of certain air pollution equipment. This effectively raised the rates for all residential customers by 6% and small general power customers by 7%. TVA's rate increase in October 2005 raised rates for our customers by approximately 7%. TVA's rate increase in April 2006 raised rates for our customers by approximately 9%. Due to a TVA rate decrease in October 2006, BTES customers experienced approximately 4% in reduction of rates. Additionally, TVA implemented a Fuel Cost Adjustment at the same time, which is reviewed quarterly. The Fuel Cost Adjustment was zero in October 2006, .2% in January 2007, 1.3% in April 2007, .5% in July 2007 and 5.7% in October 2007.

The electricity we purchase from TVA is delivered at 161,000 volts to our two delivery points- Bluff City Primary and Blountville Primary Substations. We step it down to 69,000 volts for subtransmission to other substations and to 13,200/7620 volts for distribution. In some cases, small distribution substations provide additional voltage reduction to large general power loads. The voltage entering a customer's home is 120/240 volts which is utilized for lighting, heating and operating household appliances. Businesses and industries may be served at 208/120, 480/277, 4160/2400 and 13200/7620 volts or other standard voltages.

BACKGROUND INFORMATION (continued)

BTES provides high-speed Internet, telephone and cable television services over a fiber optic network. This same network provides numerous enhancements to BTES' electric system, including automatic meter reading, power outage detection and power outage reporting. In the future, this system will be used for pre-payment of electricity to offset the need for at risk customers to pay a deposit and for load management.

In 1994, BTES received the American Public Power Association's prestigious E. F. Scattergood System Achievement Award for outstanding achievement by a utility.

Also in 1994, BTES was one of three organizations to receive the Tennessee Quality Governor's Award, now called the Tennessee Center for Performance Excellence *Award of Excellence*, presented by Governor Ned McWherter. The other two recipients were Nissan and FedEx. Other organizations that have received this prestigious award include: Eastman Chemical Company, Philips Consumer Electronics Company, Bridgestone/Firestone Company, Eaton Corporation, Methodist Medical Center of Oak Ridge, Baptist Health Systems of Knoxville, Fleetguard, Caterpillar Financial Services, Memphis Light, Gas and Water, Eaton Aeroquip, Pal's Sudden Service, Tennessee Valley Authority Nuclear, John Deere Power Products and Mountain States Health Alliance.

In June 1996, BTES received the American Public Power Association's Golden Tree Award in recognition of BTES planting over one tree per customer.

In June 1997, BTES received the American Public Power Association's Community Service Award for outstanding civic and community involvement by our employees.

In October 1997, CEO R. Michael Browder received the 1997 Jim Spradley Award for individual accomplishments in the field of industrial and economic development in Tennessee that go above and beyond the requirements of the vocation for which they are compensated. The award was presented by Governor Don Sundquist at the Governor's Economic Summit in Nashville.

In May 2000, CEO R. Michael Browder received the Tennessee Valley Public Power Association's Distinguished Service Award for his exceptional performance and contributions toward the accomplishment of the organization's goals.

From July 2001 until June 2002, CEO R. Michael Browder served as Chairman of the Board of the American Public Power Association.

In October 2004, BTES received approval to offer cable television and Internet service.

On December 15, 2004, the BTES Board of Directors changed the name of the organization from *Bristol Tennessee Electric System* to *Bristol Tennessee Essential Services* to reflect the new services being offered.

In fall 2005, BTES began providing cable television and Internet service.

For fiscal year 2006, BTES received the Government Finance Officers Association *Certificate of Achievement for Excellence in Financial Reporting* for the ninth year in a row.

BACKGROUND INFORMATION (continued)

In March 2006, BTES received approval from the Tennessee Regulatory Authority to provide telephone service. In November 2006, BTES began providing telephone service.

In February 2007, BTES received the National Arbor Day Foundation Tree Line USA Award for the seventh year in recognition of quality tree care, annual worker training, tree planting and public education.

RECAP OF FISCAL YEAR 2007

During the past year, major engineering and construction projects included three-phase reconductor jobs on D. Droke Road and Brown Circle; three-phase relocation jobs on Highway 11E for Bristol Motor Speedway and in the Pennsylvania Avenue/Ash Street area for the new bridge; the relocation of a 69kV line with 13.2 underbuild along Highway 75 for two Tennessee state bridge projects; replacement of 750 MCM underground conductors serving from 294 Shelby Street Substation and a single-phase relocation on Barnett Road.

During routine maintenance, wooden cross arms were replaced on Holston Avenue, Jackson Street, Maryland Avenue, Florida Avenue and Beechwood Drive. Neutral and ground connections were reworked in all manholes in downtown Bristol. A new traffic signal was installed at Volunteer Parkway and Kennedy Road, and modifications were made to a traffic signal at Pennsylvania Avenue and State Street.

We installed over 29,000 feet of underground primary conductors to serve the following subdivisions and developments: Rogers Meadow, Carroll's Landing Condominium, Raceday Condominiums Building 2, River Bluff II, Lakeview RV Campground, Raceday Campground and Century Plaza.

We installed over 5,700 kVA of three-phase padmount transformers to serve the following general power customers: Bill Gatton Nissan, Royal Mouldings, Northeast State Technical Community College, Strongwell, AmSouth Bank, Raceday Condominiums, Sullivan County Jail and Kintronics Laboratories.

Approximately 3.75 miles of fiber optic cable were installed to provide another leg of redundancy to our fiber optic backbone system, which interconnects substations to the BTES Service Center. Heat pumps were installed at Airport and Pemberton Substations for the fiber optic equipment rooms.

Our outage time per customer was 58 minutes for calendar year 2006 which gives us a reliability index of 99.989%.

During the last five years, we have been able to maintain our goal of a five-year tree clearance cycle. We continue to monitor frequency of tree-caused outages by areas and make more frequent visits to these areas. In 2006-2007, we cleared trees along feeder lines at Shelby Substation circuits 284 and 294; Exide Substation circuits 214, 224, 254 and 274; Buffalo Substation circuits 214, 224 and 254; Bluff City Substation circuits 214, 224, 254, 264 and 274; Blountville Substation circuit 224; Ruthton Substation circuit 274; Industrial Substation circuit 214 and King College Substation circuits 214 and 224.

RECAP OF FISCAL YEAR 2007 (continued)

Our goal is to maintain the distribution transformer capacity ratio to 200 percent of peak demand or less. We continue to work to improve this number. We will continue our transformer loading program to help us predict new customer demand needs. The transformer loading program assists us in identifying transformers that we will investigate for being heavily loaded and change if necessary.

We checked 209 three-phase meter installations, finding all to be okay.

During our routine substation preventative maintenance program, we discovered potential problems and made repairs to regulators at Bluff City District, Buffalo and Blountville Substations. Also, we found and made repairs to mechanism problems on 15 kV distribution breakers at Bluff City District, Blountville and Piney Flats Substations and found two switch problems at Bluff City Primary.

Twenty-eight problems ranging from minor to critical were discovered and repaired during our annual infrared inspection.

Due to a TVA rate decrease, BTES customers experienced approximately 4% in reduction of rates beginning October 1, 2006. Additionally, TVA implemented a Fuel Adjustment Cost at the same time, which is reviewed quarterly. The Fuel Adjustment Cost was zero in October 2006, .2% in January 2007 and 1.3% in April 2007.

As the city's largest taxpayer, we paid the maximum in-lieu-of-tax payments as provided by Tennessee State Law and the TVA Contract to the City of Bristol in the amount of \$822,449 for fiscal year 2007. Combined with taxes paid to Sullivan County and Bluff City, Tennessee and Washington County, Virginia, a grand total of \$1,060,458 was paid by BTES in fiscal year 2007.

We planted 129 dogwoods during fiscal year 2007 through our Trade-A-Tree program. We also planted an Oak tree at each Bristol, Tennessee elementary school for a total of six new trees.

The initial installation of an electronic mapping system is complete. We are using Global Positioning System (GPS) data collected by Atlantic Engineering Group (AEG) to enter the geographic location of all power system features such as poles, transformers, meters and lines into the BTES mapping system. Through June 2007, AEG had collected 29,341 pole locations, which account for approximately 99% of all pole locations in the system. Approximately 25,000 of these pole locations have been mapped. The mapping platform operates as a Geographical Information System (GIS) that links BTES customer and facility data to the geographical symbols on the maps. A base map consisting of roads and property parcels is being used along with aerial photographs of the BTES service area. The field data is being collected on all of the power system facilities. The new electronic maps are replacing the existing paper mapping system. The maps include all of the fiber optic system.

In December 2002, we purchased \$8 million of Discounted Energy Units from TVA. Our participation in the program will assure a long-term supply of power at a low price and increase our return on investments. Our power bill is being discounted by the principle and interest earned.

RECAP OF FISCAL YEAR 2007 (continued)

Our electric bad debts, as a percentage of electric retail revenue, were 0.15 percent for fiscal year 2007, which is below our stated goal of 0.25 percent. The industry target is 0.4 percent. This has been accomplished in a variety of ways. We diligently work to prevent customers from falling too far behind in paying their BTES bill and thoroughly screen new applications to determine inclination to pay. In an effort to help those in need find necessary funding, we work with area churches, the Salvation Army, United Way, the Upper East Tennessee Human Development Agency and other customers via our *Help Your Neighbor* program. Our deposit procedure seems to be working well. Residential customers who demonstrate a history of paying their bills in a timely manner may have their deposit waived. A general power customer with a calculated standard deposit of \$10,000 or less, which has a principal owner who has lived in our service area five or more years with good pay and credit history and is willing to guarantee the account, may have the deposit reduced or waived. To date, no adverse effects have been detected.

Our *Help Your Neighbor* program was conducted successfully for the 15th year to assist residential electric customers in paying their winter electric bills during difficult times. This year \$10,797 was contributed by customers and BTES' match, providing assistance for over 64 families. As in the past, the need of the customer is identified by the Salvation Army and funds are administered by the United Way.

Efforts to increase sales of electricity continued. Efforts are ongoing to increase the use of electric heat pumps and electric water heaters, especially load-managed water heaters that can be switched off during peak-demand periods. During calendar year 2006, we inspected 342 heat pump installations and installed 587 water heaters. BTES has over 13,600 load-managed water heaters. During calendar year 2006, TVA paid us over \$810,000 for the ability to cycle these water heaters off during peak times. Sixteen loans were made through the Energy Savings Loan Program at a total of \$44,090.

During fiscal year 2007, we installed 265 miles of our fiber optic cable distribution system, bringing our total plant to 531 miles, serving a total of 4,160 homes and businesses with Internet, telephone and/or cable television service.

We continue to make subdivision development agreements available to developers. Instead of initially collecting the total cost for electric facilities installed to serve subdivisions, we offer to waive all or part of these costs for developers who agree to have all-electric homes with inspected energy-efficient heat pumps and load-managed water heaters built in their developments. Total costs are charged for any lots on which homes are built that are not all-electric. We presently have 850 lots in 27 subdivisions covered under this type agreement.

For the 16th consecutive year, in cooperation with the Bristol Chamber of Commerce, the City of Bristol Tennessee and NETWORKS - Sullivan Partnership, we maintained the Governor's Three-Star Community Economic Preparedness Program Award which signifies that Bristol has the organization, attitude, facilities and skills to attract and retain industry. A major component of this certification is having available property for industrial development. The Bristol Industrial Park purchased by BTES provides this component.

RECAP OF FISCAL YEAR 2006 (continued)

Each customer who purchases a BTES water heater, has an inspected electric heat pump installed or has fiber optic services installed is surveyed by mail. The surveys are used to monitor quality and customer satisfaction of each program and satisfaction with BTES employees and Quality Contractor Network employees.

In calendar year 2006, BTES personnel visited 75 existing industries to discuss electrical needs, expansion possibilities and their satisfaction with the service they are receiving. BTES worked with the City of Bristol, Tennessee; State of Tennessee; TVA and NETWORKS - Sullivan Partnership to identify and assist nine businesses with expansions or relocations to the Bristol area, resulting in the potential for 280 new jobs.

Sixty-nine percent of our employees had perfect attendance for calendar year 2006.

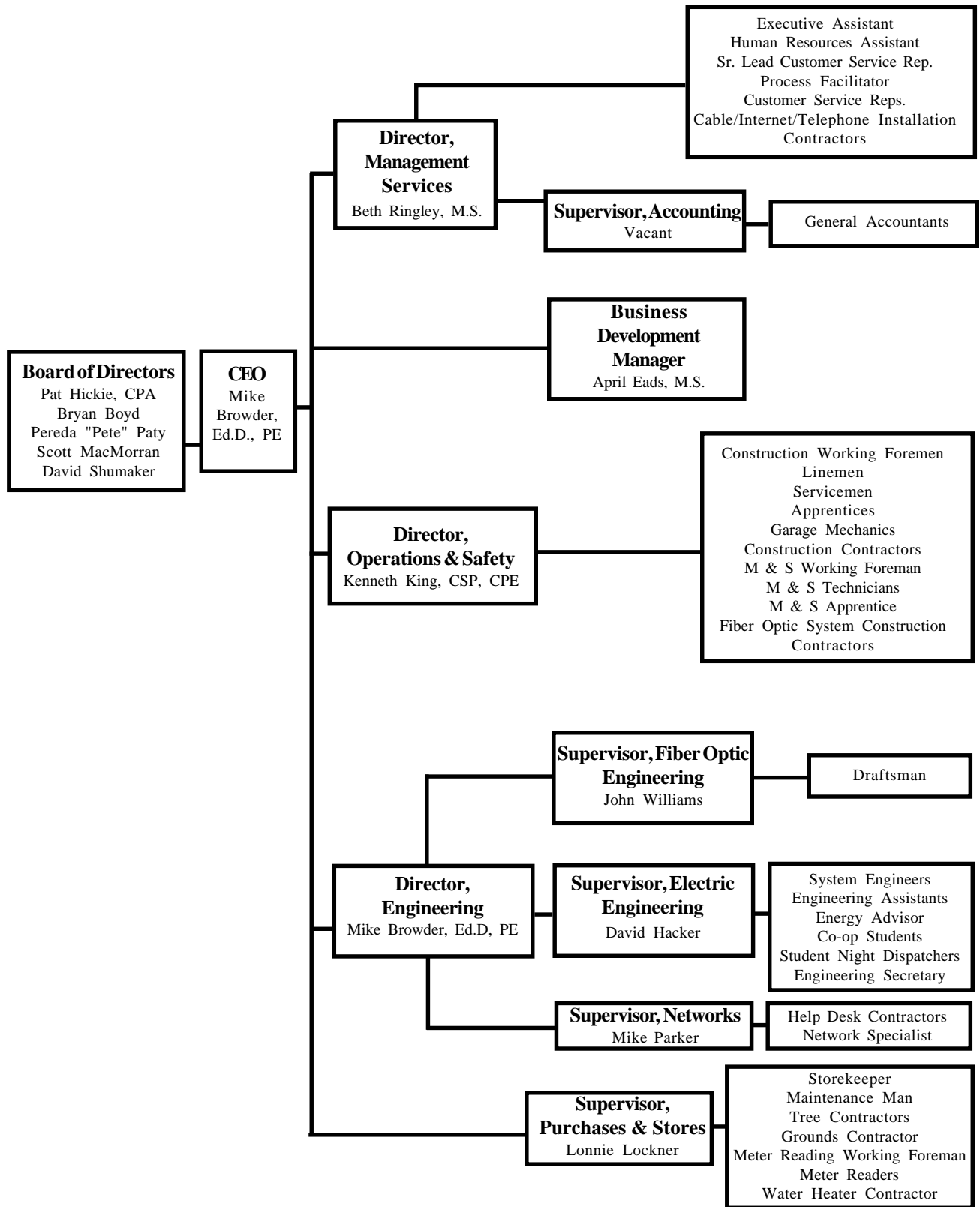
For the 24th consecutive year, we had no lost-time accidents for a total of over 3.2 million man-hours since the last lost-time accident in 1982.

During calendar year 2006, five full-time employees left BTES. This prompted organizational changes and the hiring of five new full-time employees. We continued a co-op program for electrical engineering students.

We presented 29 awards at our annual heat pump dinner for Quality Contractor Network members.

At the annual Service Awards Banquet, we presented awards representing 50 years of service including: one employee for 15 years of service, one employee for 10 years of service and five employees for five years of service to BTES and five recognition awards for new employees.

Organizational Chart



General Philosophy

■ ***Reliability For Our Customers Is Essential***

The customer is our reason for being and ultimately judges the quality of our service. We must provide safe, reliable, cost-effective service and properly allocate costs for BTES to survive, grow and meet the needs of our present and future customers.

■ ***BTES Employees Are Our Most Important Asset***

They provide the intelligence and determine the reputation of our organization. They are respected as valuable teamworkers striving to meet our goals of quality service. We are committed to providing a safe and healthy workplace for all BTES employees who are the driving force behind all we do.

■ ***Resources Must Be Wisely Allocated And Used***

Our resources (time, money, facilities and equipment) must be wisely allocated, utilized and invested to enable us to provide quality service at reasonable long-term rates.

■ ***Our Vendors And Suppliers Are Our Partners***

They provide goods and services that enable us to meet the needs of our customers. We will treat our vendors and suppliers with respect and create an environment which will ensure mutual success.

■ ***Increasing Sales Helps Keep Rates Down***

We are committed to increasing sales by developing additional load such as residential heat pumps, water heaters and industrial and commercial loads and by providing more customers with Internet, telephone and cable television services. This will help provide us a broader base to divide expenses which helps keep rates down.

■ ***Safety, Conservation And Efficient Use Of Electricity Are Essential***

We must provide a customer communication program through all area news media, school and civic programs, direct mail, in-house seminars and trade shows in order to educate and assist customers in the safety, conservation and efficient use of electricity.

■ ***Effective Use Of Fiber Optic System Enhances Quality of Life***

We must promote the use of the fiber optic system to customers in an effort to increase comfort, convenience, entertainment and productivity. The system will also enhance quality of life in our community as it is used as a tool for economic development.

■ ***Planning Is Vital To Achievement***

To achieve our objectives at BTES, it is necessary that we clearly understand our plans, objectives and strategies as we strive to maintain our excellence in service.

■ ***Continuous Improvement Is The Key To Long-Term Success***

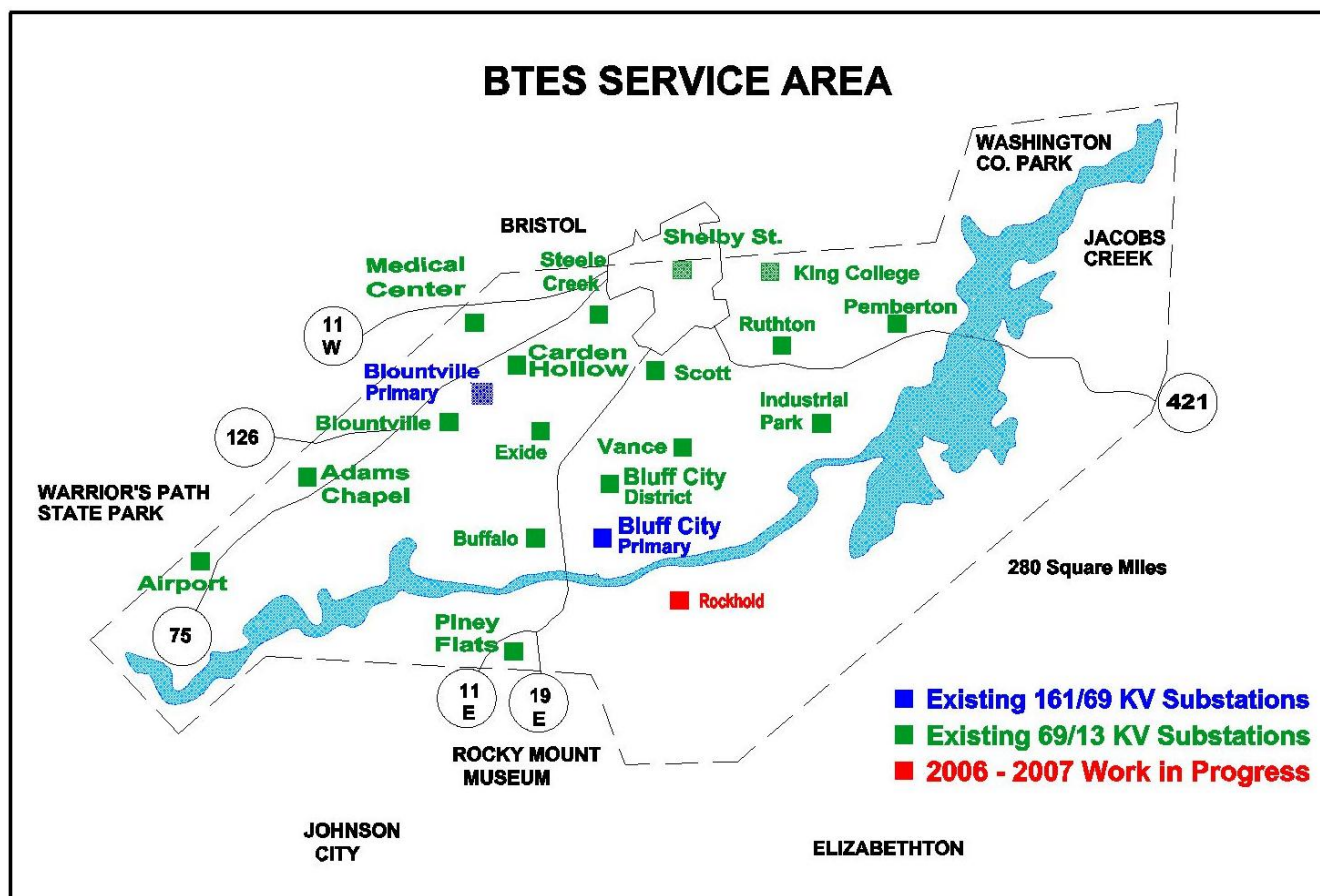
We must continually strive for excellence and quality in everything we do - in our workmanship and services, the appearance and safety of our workplace, human relations and our commitment to our community and ourselves.

■ ***We Want To Earn And Deserve The Trust And Respect Of Our Customers***

The customer entrusts his family's welfare to us to provide his electrical power, cable television, Internet and telephone needs. He must have complete confidence in the quality service we provide and the people who work for us.

■ ***A Positive Image Is A Valuable Asset***

We strongly believe in a professional image, and we will strive to maintain such an image in the eyes of our customers, vendors and business associates to improve the quality of life in our community.



Substations Owned and Operated by BTES

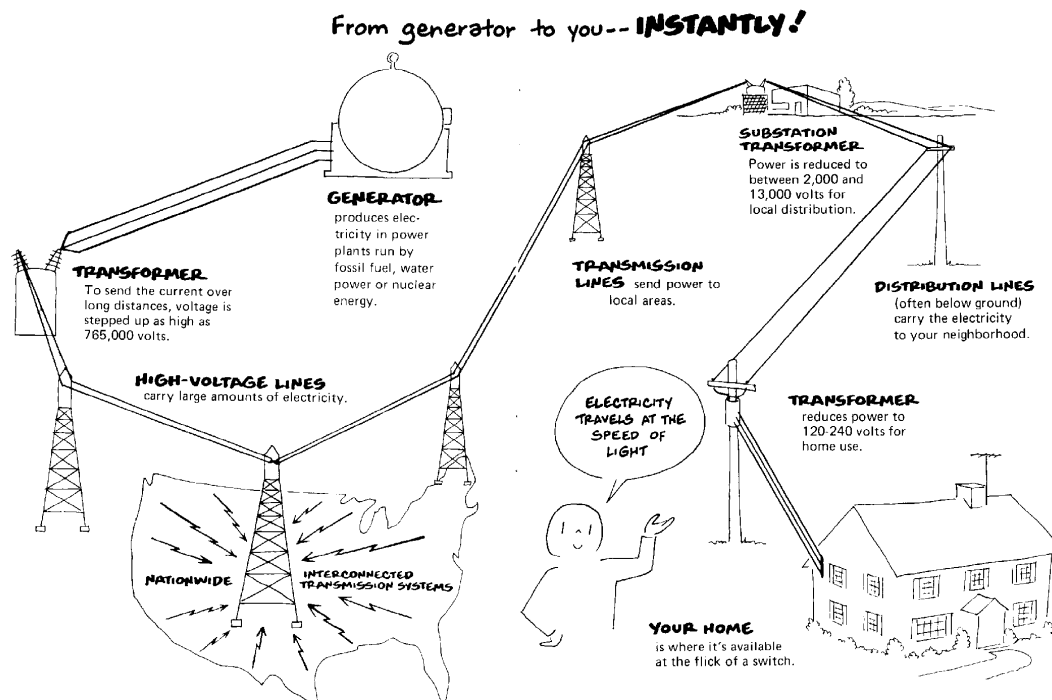
Bluff City Primary	*161/69 KV	200 MVA
Blountville Primary	*161/69 KV	200 MVA
Adams Chapel	69/13 KV	20 MVA
Airport	69/13 KV	20 MVA
Blountville	69/13 KV	25 MVA
Bluff City	69/13 KV	50 MVA
Buffalo	69/13 KV	20 MVA
Carden Hollow	69/13 KV	20 MVA
Exide	69/13 KV	40 MVA
Industrial Park	69/13 KV	20 MVA
King College	69/13 KV	20 MVA
Medical Center	69/13 KV	20 MVA
Pemberton	69/13 KV	20 MVA
Piney Flats	69/13 KV	20 MVA
Scott	69/13 KV	20 MVA
Shelby Street	69/13 KV	80 MVA
Steele Creek	69/13 KV	20 MVA
Ruthton	69/13 KV	10 MVA
Vance	69/13 KV	25 MVA

*Delivery Point from TVA

Substations in the 2007-2008 Work Plan

Rockhold	69/13 KV	20 MVA
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Electric Utility Terms



Air-Source Heat Pump - A system that can supply both space heating and cooling. In the heating cycle, the heat pump removes heat from the outside air and pumps it indoors. When cooling, the heat pump absorbs heat from the indoors and rejects it to the outside.

Ampere - Unit of measurement of electric current. It's proportional to the quantity of electrons flowing through a conductor past a given point in one second.

Base Load - The minimum load over a given period of time.

Blackout - A temporary loss of electricity in an area because of failure of generation or transmission equipment.

Brownout - A voltage reduction during an electrical shortage that causes conditions such as dim lights.

Bus - An electrical conductor which serves as a common connection for two or more electrical circuits.

Capacity - The load for which a generating unit, generating station or other electrical apparatus is rated by the user or the manufacturer.

Circuit Breaker - A switch that opens an electric circuit when a short occurs.

Conductor - Any substance, usually metallic, that will carry electricity.

Degree Day - A unit measuring the extent to which the average daily temperature varies from a standard reference temperature. Based on a reference temperature of 65 degrees Fahrenheit, if the average temperature (high plus low divided by 2) for a day is 70, then there are five cooling degree days for that day. Likewise, if the average temperature was 60, then there were five heating degree days. This historical information can be used for forecasting system load and planning unit maintenance outages, to name a few.

Electric Utility Terms (continued)

Delivery Point - The point, usually a substation, to which electricity is transmitted from its generating sources.

Demand - The rate at which electric energy is delivered to a system. The primary source of demand is the power consuming equipment of the customers.

Depreciation - Charges made against income to equitably distribute the cost of the decrease in plant value during the period when services are obtained from use of the facilities. The decrease in plant value is caused by wear, deterioration or obsolescence.

Deregulation - Movement of an industry from one of monopolistic entities or environments to one free market enterprise; in the electric industry this involves elimination of service area and rate restrictions and obligation to serve; results in distributor choice of supplier and eventually customer choice of supplier.

Dispatching - The control of an electric system involving switching substations, transmission/distribution lines and other equipment. Monitoring and operating the SCADA system. Dispatching crews for emergencies and maintaining a log of work locations and purpose for outside crews.

Distribution System - A system that enables delivering electric energy at 2.4 kV to 25 kV from convenient points (substations) on the transmission system to the customers.

Earth Coupled Heat Pump - An efficient electrical device that heats or cools by moving heat into or out of a building. It uses an antifreeze solution or refrigerant in a pipe buried in the ground to collect or disperse heat. Also called geothermal system, ground source heat pump or water source heat pump.

Easement - A right obtained from property owners that allows utility companies to construct, operate, maintain, and control facilities such as transmission lines on the property.

Eminent Domain - The right of government to take, or to authorize the taking of, private property for public use, just compensation usually being given to the owner.

Electric Current - The flow of electric charge in a conductor between two points having a difference in potential, generally expressed in amperes.

Electric and Magnetic Fields (EMF) - Radiation surrounding conductors that carry electricity - present wherever electric power is being used.

Fault - A point of defect in an electric circuit that prevents the current from following the intended course.

Insulator - A non conductor, usually of glass or porcelain, for insulating and supporting electric wires.

Kilowatt - The basic unit of electric demand, equal to 1,000 watts - average household demand is 10 to 20 kilowatts.

Kilowatt Hour - A unit of energy or work equal to 1,000 watt-hours. The basic measure of electric energy generation or use. A 100-watt light bulb burning for 10 hours uses one kilowatt hour.

Load - The amount of electric power delivered or required at any specified point on a system. Load originates at the power consuming equipment of the customers.

Electric Utility Terms (continued)

Load Factor - The ratio of the average load in kilowatts supplied during a designated period to the peak load in kilowatts occurring in that period.

Load Management - A program used by an electric utility to control its customers' use of electricity during times when their demand for electricity is high. Can involve reducing voltage or cutting off air conditioners or water heaters for short periods by remote control.

Losses - Power (kilowatts) and energy (kilowatt hours) lost during the operation of an electric system. Losses occur principally when energy is transformed into waste heat in conductors and other electrical apparatus.

Megawatt - 1,000 kilowatts or 1,000,000 watts.

Megawatt Hour - 1,000 kilowatt hours.

Peak Demand - The maximum rate at which electric energy is delivered to or by a system during a specific period of time.

Power Factor - The ratio of real power (kilowatts) to apparent power (kilovolt-amperes) for any given load and time.

Power Theft - Tampering with a meter to lower electric bills which is a dangerous and illegal act.

Ratchet - An electric rate charge based on the exceptional load of a seasonal peak in respect to the other seasons.

SCADA - Supervisory Control Data Acquisition System - Through a master station comprised of the equipment and computer software, SCADA provides instantaneous substation monitoring and control in addition to complete system status such as electric load, voltage levels and interruptions of service. Data also includes system kilowatt hours, amperage on each feeder phase, voltage on each phase, substation kilowatt hours and instantaneous kilowatt demand by substation or transformer bank. It includes data used for system planning, emergency switching and system maintenance.

Substation - An assemblage of equipment that enables switching and/or changing or regulating the voltage of electricity.

Transformer - A device to change the voltage of alternating current electricity.

Transmission System - The system that transports electric energy in bulk form - usually in high voltage - from a source of supply to the distribution systems or other major parts of the electric system.

Volt - The force when steadily applied to a circuit having a resistance of one ohm, will produce a current of one ampere.

Watt - The electrical unit of power or the rate of doing work. The rate of energy transfer equivalent to one ampere flowing under a pressure of one volt at unity power factor. One horsepower is equivalent to approximately 746 watts.

Deregulation Dictionary

The following are terms that you may encounter when reading about deregulation in the electric utilities industry.

Access Charge - a charge levied on a power supplier, or its customer, for access to a utility's transmission or distribution system. It is a charge for the right to send electricity over another's wires.

Aggregator - an entity that combines the needs of several smaller customers into a larger block of power in order to get a better price.

Capacity - the amount of electricity for which a generating plant or transmission system is rated.

Commercial Customer - non-manufacturing business customer.

Customer Choice - allows retail customers to select the power supplier or generator they buy electricity from.

Demand - the amount of power a customer takes at a given moment.

Direct Access - the ability of an electric end-user to connect directly with a power supplier, thus bypassing its local utility.

Distribution System - local delivery system of electricity to the retail customer's home or business through distribution lines. BTES is a distribution system.

Electric Cooperative - a member-owned electric utility company that distributes electricity on a nonprofit basis. Example: Mountain Electric Cooperative.

Federal Energy Regulatory Commission (FERC) - the agency that has jurisdiction over natural gas pricing, hydroelectric licensing, oil pipeline rates and gas pipeline certification.

Generation Company (genco) - an entity that operates electricity-generating plants. The genco may own the generation plants or interact with short-term marketers on behalf of plant owners.

Independent Power Producer (IPP) - a private entity that generates electricity and sells it to other businesses, including utilities.

Independent System Operator (ISO) - the independent operator of a transmission system, responsible for guaranteeing open access, scheduling, system reliability and accounting.

Industrial Customer - business customer engaged in manufacturing.

Investor-owned Utility (IOU) - a stockholder-owned power company that generates and distributes electric energy for profit. Example: American Electric Power.

Municipal - electric distribution system owned by a city to provide service for its residents. Example: BTES.

Non-power Services - includes such services as gas, home security and telecommunications.

Power Marketer - an entity that provides bulk wholesale power for use at a specific place and time. The marketer may or may not generate the power. Example: Cinergy.

Regional Transmission Organization (RTO) - FERC Order 2000 requires all investor-owned utilities to consider joining a RTO.

Deregulation Dictionary (continued)

Retail Wheeling - a system in which individual retail electric customers are allowed to choose their electric supplier. Also known as retail competition.

Service Area - the geographic region that a utility is required to serve, or has the exclusive right to serve, in supplying electricity to the ultimate consumer.

Stranded Costs - costs of a utility that have already been legitimately and prudently incurred that are not economically viable in a competitive market.

Tennessee Valley Authority - generation and transmission company supplying power to 158 electric utilities in a seven-state region including Tennessee.

Transmission System - all the lines, poles and other equipment used to move bulk electricity from a generating plant to a distribution system.

Unbundling - separating the costs of operations of generation, transmission and distribution of electricity. An unbundled electric bill would list all costs associated with providing electricity to the consumer.

Wheeling - transmitting bulk electricity from a generating plant to a distribution system across a third system's lines.

Wheeling Charge - an amount charged to an electric system by another for the transmission of energy to and from another system.

Wholesale Customer - a power purchaser that buys for resale to retail customers. Example: BTES.

Source: Tennessee Magazine

Glossary of Broadband Terms

3G – Third Generation: Intended to be the next great wireless technology, wideband mobile services and applications offering users faster access to the web.

ADSL - Asymmetric Digital Subscriber Line: DSL service with a larger portion of the capacity devoted to downstream communications, less to upstream. Typically thought of as a residential service.

ATM – Asynchronous Transfer Mode: A data service offering by ASI, that can be used for interconnection of customer's LAN. ATM provides service from 1 Mbps to 145 Mbps utilizing Cell Relay Packets.

Bandwidth – The amount of data transmitted in a given amount of time; usually measured in bits per second, kilobits per second, and megabits per second.

Bit – A single unit of data, either a one or a zero. In the world of broadband, bits are used to refer to the amount of transmitted data. A kilobit (Kb) is approximately 1,000 bits. A megabit (Mb) is approximately 1,000,000 bits.

BPL – Broadband Over Powerline: A theoretical technology that would provide broadband service over existing electrical power lines.

BPON – Broadband Passive Optical Network: BPON is a point-to-multipoint fiber-lean architecture network system which uses passive splitters to deliver signals to multiple users. Instead of running a separate strand of fiber from the CO to every customer, BPON uses a single strand of fiber to serve up to 32 subscribers.

Broadband – A descriptive term for evolving digital technologies that provide consumers with integrated access to voice, high-speed data service, video-demand services, and interactive delivery services (e.g. DSL, Cable Internet).

CAP – Competitive Access Provider: (or “Bypass Carrier”) A Company that provides network links between the customer and the Inter-Exchange Carrier or even directly to the Internet Service Provider. CAPs operate private networks independent of Local Exchange Carriers.

Cellular – A mobile communications system that uses a combination of radio transmission and conventional telephone switching to permit telephone communications to and from mobile users within a specified area.

CLEC – Competitive Local Exchange Carrier: Wireline service provider that is authorized under state and Federal rules to compete with ILECs to provide local telephone service. CLECs provide telephone services in one of three ways or a combination thereof: a) by building or rebuilding telecommunications facilities of their own, b) by leasing capacity from another local telephone company (typically an ILEC) and reselling it, and c) by leasing discrete parts of the ILEC network referred to as UNEs.

CO – Central Office: A circuit switch where the phone lines in a geographical area come together, usually housed in a small building.

Coaxial Cable – A type of cable that can carry large amounts of bandwidth over long distances. Cable TV and cable modem service both utilize this technology.

Glossary of Broadband Terms (continued)

CWDM – Coarse Wavelength Division Multiplexing (WDM): is generally held to be WDM with less than 8 active wavelengths per fiber.

Dial-Up – A technology that provides customers with access to the Internet over an existing telephone line.

DLEC – Data Local Exchange Carrier: DLECs deliver high-speed access to the Internet, not voice. DLECs include Covad, Northpoint and Rhythms.

Downstream – Data flowing from the Internet to a computer (Surfing the net, getting E-mail, downloading a file).

DSL – Digital Subscriber Line: The use of a copper telephone line to deliver “always on” broadband Internet service.

DSLAM – Digital Subscriber Line Access Multiplier: A piece of technology installed at a telephone company’s CO and connects the carrier to the subscriber loop (and ultimately the customer’s PC).

DWDM – Dense Wavelength Division Multiplexing (WDM): A SONNET term which is the means of increasing the capacity of Sonet fiber-optic transmission systems.

E-Rate – A Federal program that provides subsidy for voice and data lines to qualified schools, hospitals, CBOs, and other qualified institutions. The subsidy is based on a percentage designated by the FCC. CTF benefits are calculated net of the E-rate subsidy.

EON – Ethernet Optical Network: The use of Ethernet LAN packets running over a fiber network.

EvDO – Evolution Data Only: EvDO is a new wireless technology that provides data connections that are 10 times as fast as a regular modem.

FCC – Federal Communications Commission: A Federal regulatory agency that is responsible, among other things, of regulating VoIP.

FTTN – Fiber To The Neighborhood: A hybrid network architecture involving optical fiber from the carrier network, terminating in a neighborhood cabinet with converts the signal from optical to electrical.

FTTP – Fiber To The Premise (Or FTTB – Fiber To The Building): A fiber optic system that connects directly from the carrier network to the user premises.

GPON - Gigabyte-Capable Passive Optical Network: GPON uses a different, faster approach (up to 2.5 Gbit/s in current products) than BPON.

GPS – Global Positioning System: A system using satellite technology that allows an equipped user to know exactly where he is anywhere on earth.

GSM – Global System for Mobile Communications: This is the current radio/telephone standard in Europe and many other countries except Japan and the United States.

HFC – Hybrid Fiber Coaxial Network: An outside plant distribution cabling concept employing both fiber optic and coaxial cable.

IEEE - Institute of Electrical and Electronics Engineers

Glossary of Broadband Terms (continued)

ILEC – Incumbent Local Exchange Carrier: The traditional wireline telephone service providers within defined geographic areas. Prior to 1996, ILECs operated as monopolies having the exclusive right and responsibility for providing local and local toll telephone service within LATAs.

IP-VPN – Internet Protocol -Virtual Private Network: A software-defined network offering the appearance, functionality and usefulness of a dedicated private network

ISDN – Integrated Services Digital Network: An alternative method to simultaneously carry voice, data and other traffic, using the switched telephone network.

ISP – Internet Service Provider: A company providing Internet access to consumers and businesses, acting as a bridge between customer (end-user) and infrastructure owners for dial-up, cable modem and DSL services.

Kbps – Kilobits per second: 1,000 bits per second. A measure of how fast data can be transmitted.

LAN – Local Area Network: A geographically localized network consisting of both hardware and software. The network can link workstations within a building or multiple computers with a single wireless Internet connection.

LATA – Local Access and Transport Areas: A geographic area within which a divested Regional Bell Operating Company is permitted to offer exchange telecommunications and exchange access service. Calls between LATAs are often thought of as long distance service. Calls within a LATA (IntraLATA) typically include local and local toll services.

Local Loop – A generic term for the connection between the customer's premises (home, office, etc.) and the provider's serving central office. Historically, this has been a wire connection; however, wireless options are increasingly available for local loop capacity.

MAN – Metropolitan Area Network: A high-speed data intra-city network that links multiple locations with a campus, city or LATA. A MAN typically extends as far as 50 kilometers.

Mbps – Megabits per second: 1,000,000 bits per second. A measure of how fast data can be transmitted.

Overbuilders – Building excess capacity. In this context, it involves investment in additional infrastructure project to provide competition.

OVS – Open Video Systems: OVS is a new option for those looking to offer cable television service outside the current framework of traditional regulation. It would allow more flexibility in providing service by reducing the build out requirements of new carriers.

PON – Passive Optical Network: A Passive Optical Network consists of an optical line terminator located at the Central Office and a set of associated optical network terminals located at the customer's premise. Between them lies the optical distribution network comprised of fibers and passive splitters or couplers. In a PON network, a single piece of fiber can be run from the serving exchange out to a subdivision or office park, and then individual fiber strands to each building or serving equipment can be split from the main fiber using passive splitters / couplers. This allows for an expensive piece of fiber cable from the exchange to the customer to be shared amongst many customers thereby dramatically lowering the overall costs of deployment for fiber to the business (FTTB) or fiber to the home (FTTH) applications.

Glossary of Broadband Terms (continued)

Right-of-Way – A legal right of passage over land owned by another. Carriers and service providers must obtain right-of-way to dig trenches or plant poles for cable systems, and to place wireless antennae.

RPR – Resilient Packet Ring: RPR uses Ethernet switching and a dual counter-rotating ring topology to provide SONET-like network resiliency and optimized bandwidth usage, while delivering multi-point Ethernet/IP services.

RUS – Rural Utility Service: A division of the United States Department of Agriculture, it promotes universal service in unserved and underserved areas of the country with grants, loans, and financing.

SONNET – Synchronous Optical Network: A family of fiber-optic transmission rates.

Streaming – A Netscape innovation that downloads low bit text data first, then the higher bit graphics. This allows users to read the text of an Internet document first, rather than wait for the entire file to load.

Subscribership – Subscribership is how many customers have subscribed for a particular telecommunications service.

Switched Network – A domestic telecommunications network usually accessed by telephones, key telephone systems, private branch exchange trunks, and data arrangements.

T-1 – Trunk Level 1: A digital transmission link with a total signaling speed of 1.544 Mbps. It is a standard for digital transmission in North America.

T-3 – Trunk Level 3: 28 T1 lines or 44.736 Mbps.

UNE – Unbundled Network Elements: Leased portions of a carrier's (typically an ILEC's) network used by another carrier to provide service to customers.

Universal Service – The idea of providing every home in the United States with basic telephone service.

Upstream – Data flowing from your computer to the Internet (sending E-mail, uploading a file).

VDSL – Very High Data Rate Digital Subscriber Line: A developing technology that employs an asymmetric form of ADSL, with projected speeds of up to 155 Mbps.

Video On Demand – A service that allows users to remotely choose a movie from a digital library and be able to pause, fast-forward, or even rewind their selection.

VLAN – Virtual Local Area Network

VoIP – Voice Over Internet Protocol: A new technology that employs a data network (such as a broadband connection) to transmit voice conversations.

VPN – Virtual Private Network: VPN is a network that is constructed by using public wires to connect nodes. For example, there are a number of systems that enable you to create networks using the Internet as the medium for transporting data. These systems use encryption and other security mechanisms to ensure that only authorized users can access the network and that the data cannot be intercepted.

Glossary of Broadband Terms (continued)

WiMax - WiMax is a wireless technology that provides high-throughput broadband connections over long distances. WiMax can be used for a number of applications, including "last mile" broadband connections, hotspot and cellular backhaul, and highspeed enterprise connectivity for businesses.

Wireless – Telephone service transmitted via cellular, PCS, satellite, or other technologies that do not require the telephone to be connected to a land-based line.

Wireless Internet – 1) Internet applications and access using mobile devices such as cell phones and palm devices. 2) Broadband Internet service provided via wireless connection, such as satellite or tower transmitters.

Wireline – Service based on infrastructure on or near the ground, such as copper telephone wires or coaxial cable underground or on telephone poles.

Source: ConnectKentucky



Report of Independent Auditors

Board of Directors
Bristol Tennessee Essential Services

We have audited the accompanying balance sheets of Bristol Tennessee Essential Services ("BTES"), an enterprise fund of the City of Bristol, Tennessee, as of June 30, 2007 and 2006, and the related statements of revenues, expenses and changes in net assets and cash flows for the years then ended. These financial statements are the responsibility of BTES' management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

As discussed in Note 1, the financial statements present only BTES and do not purport to, and do not, present fairly the financial position of the City of Bristol, Tennessee, as of June 30, 2007 and 2006, and the changes in its financial position, or, where applicable its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Bristol Tennessee Essential Services at June 30, 2007 and 2006, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated November 7, 2007, on our consideration of BTES' internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.



Board of Directors
Bristol Tennessee Essential Services

The Management's Discussion and Analysis on pages 3 through 10 is not a required part of the financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurements and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audits were conducted for the purpose of forming an opinion on the financial statements taken as a whole. The other supplementary information listed in the introductory and statistical sections of the accompanying table of contents is presented for purposes of additional analysis and is not a required part of the financial statements of BTES. Such information has not been subjected to the auditing procedures applied in our audit of the financial statements and, accordingly, we express no opinion on it.

Coulter & Justus, P. C.

November 7, 2007

Bristol Tennessee Essential Services

Management's Discussion and Analysis

June 30, 2007

This discussion and analysis is intended to be an introduction to the financial statements and notes that follow this section and should be read in conjunction with them. This section will provide narrative discussion and analysis of the financial activities of BTES. The financial performance of BTES is discussed and analyzed within the context of the accompanying financial statements and disclosures following this section. The Introductory Section covers management's letter of transmittal and other BTES information.

Financial Statement Overview

The financial statements herein are comprised of the Balance Sheets, the Statements of Revenues, Expenses and Changes in Net Assets, the Statements of Cash Flows and the accompanying Notes to Financial Statements.

BTES is a self-supporting enterprise of the City of Bristol, Tennessee operated under the general supervision and control of a five-member Board of Directors as per Chapter 32 Public Acts of Tennessee 1935. BTES issues a comprehensive annual financial report which is incorporated in the City's comprehensive annual financial report.

Operating Highlights

Net Assets and Capital Assets

As indicated in Table 1, net assets were \$67,598,340 in 2007, compared to \$63,583,229 in 2006, and \$61,487,547 in 2005. Approximately 52% of the 2007 net assets are invested in capital assets, net of related debt. All remaining net assets are unrestricted and can be used for on-going operations of BTES, although the Board of Directors has established a renewal and replacement fund totaling \$8,000,000 for future construction, improvements and extensions of BTES.

Table 1

Bristol Tennessee Essential Services Condensed Balance Sheets June 30,			
	2007	2006	2005
Current and other assets	\$ 41,422,638	\$ 49,321,114	\$ 35,969,356
Capital assets	59,576,205	46,705,185	34,025,791
Total assets	100,998,843	96,026,299	69,995,147
Current liabilities	9,507,800	8,095,791	8,507,600
Bonds Payable	23,892,703	24,347,279	-
Total liabilities	33,400,503	32,443,070	8,507,600
Net assets:			
Invested in capital assets, net of related debt	35,243,502	33,531,067	34,025,791
Unrestricted	32,354,838	30,052,162	27,461,756
Total net assets	\$ 67,598,340	\$ 63,583,229	\$ 61,487,547

Management's Discussion and Analysis (continued)

As indicated in Table 2, during the year gross capital assets increased by \$15,074,223 or 17%. Note in Table 3 that the increase in plant in 2007 was 12% as compared to 5% in 2006. Construction work in progress increased from \$19,117,810 in 2006 to \$25,987,741 in 2007 with the additional installation of BTES' fiber to the home system. BTES served cable and/or Internet services to more than 2,500 homes and/or businesses resulting in an increase in Communications Plant. Refer to the notes of the audited financial statements for more information regarding capital assets.

Table 2

Bristol Tennessee Essential Services – Capital Assets				
	June 30 2007	Net of Accumulated Depreciation	June 30 2006	Net of Accumulated Depreciation
Transmission Plant				
Land and land rights	\$ 94,696	\$ 94,696	\$ 94,696	\$ 94,696
Station equipment	2,823,269	1,335,575	2,823,269	1,448,393
Total Transmission Plant	2,917,965	1,430,271	2,917,965	1,543,089
Distribution Plant				
Land & land rights	855,111	855,111	855,111	855,111
Structures & improvements	862,742	165,638	862,741	193,687
Station equipment	11,929,221	3,359,970	11,333,797	2,992,010
Poles, towers, and fixtures	12,066,247	3,557,515	12,006,819	3,947,248
Overhead conductors and devices	6,628,639	2,980,589	6,621,428	3,162,293
Underground conduit	1,097,457	340,605	1,085,280	348,191
Underground conductors and devices	3,325,267	517,106	3,371,319	690,303
Line transformers	11,964,661	5,940,059	11,455,911	5,708,617
Services	3,023,454	975,495	2,922,568	972,999
Meters	3,177,611	1,606,400	2,826,280	1,341,977
Installation on customers' premises	980,155	(127,372)	965,595	(66,972)
Street lighting and signal systems	2,907,369	187,915	2,896,974	358,930
Total Distribution Plant	58,817,932	20,379,031	57,203,823	20,504,394
General Plant				
Land and land rights	101,831	101,831	101,831	101,831
Structures and Improvements	1,158,943	586,102	1,158,943	593,679
Office Furniture and Equipment	445,965	200,939	421,372	182,827
Transportation Equipment	2,066,569	446,674	1,929,997	400,017
Stores Equipment	24,143	4,294	24,143	5,530
Tools, shop, and garage equipment	131,389	10,133	131,389	10,132
Laboratory equipment	104,035	5,965	104,035	5,965
Power operated equipment	104,946	10,203	104,946	10,204
Communication equipment	9,975,251	9,443,889	3,546,233	3,250,575
Miscellaneous equipment	43,407	3,653	43,407	3,652
Total General Plant	14,156,479	10,803,682	7,566,296	4,564,412
Total Plant in Service	75,892,376	32,612,984	67,688,084	26,611,895
Construction work in progress	25,987,741	25,987,741	19,117,810	19,117,810
Non-utility property	975,480	975,480	975,480	975,480
	\$			
Total Capital Assets All Sources	102,855,597	\$59,576,205	\$ 87,781,374	46,705,185

Management's Discussion and Analysis (continued)

Table 3

Bristol Tennessee Essential Services Changes to Plant in Service Years ended June 30,		
	2007	2006
Plant in service beginning	\$ 67,688,084	\$ 64,203,920
Increases	9,942,174	3,533,666
Decreases	1,737,882	49,502
Plant in service ending	<u>\$ 75,892,376</u>	<u>\$ 67,688,084</u>

Note: Plant in service does not include non-utility property or construction work in progress.

Results of Operations

As indicated in Table 4, net assets of BTES increased by \$4,015,111 from fiscal year 2006 to 2007 and increased by \$2,905,682 from fiscal year 2005 to 2006. Operating revenues were principally derived from retail sales of electricity. Operating revenues were \$72,560,080 in 2007 as compared to \$66,729,254 in 2006, and \$57,323,729 in 2005; resulting in a 9% increase from 2006 to 2007 and a 16% increase from 2005 to 2006. Temperature throughout the year has historically been a main driver of electric sales. Electric operating revenues are characterized in four major customer class types: residential, commercial, industrial and street and outdoor lighting, plus other revenue. In 2006 cable and Internet revenue was added as a form of operating revenue, and in 2007 telephone was added as a form of operating revenue. The percentage of total operating revenue by category has stayed consistent from 2005 to 2007 except for the addition of revenue from the Cable and Internet Business Unit in 2006 and the Telephone Business Unit in 2007. See Figures 1, 2 and 3. As shown in Table 4, the internal tax equivalent payments made to the City of Bristol, Tennessee are reported as transfers.

Table 4

Bristol Tennessee Essential Services Condensed Statement of Revenues, Expenses and Changes in Net Assets Years ended June 30,			
	2007	2006	2005
Revenues:			
Operating revenues	\$ 72,560,080	\$ 66,729,254	\$ 57,323,729
Non-operating revenues	1,666,545	997,881	892,961
Total Revenues	<u>74,226,625</u>	<u>67,727,135</u>	<u>58,216,690</u>
Expenses:			
Purchased power	59,088,380	56,367,935	47,006,165
Cable programming	801,066	70,545	-
Internet cost of sales	67,340	5,000	-
Telephone cost of sales	69,466	-	-
Operation expenses	3,362,770	2,825,591	2,829,462
Maintenance	3,029,132	2,750,187	2,559,977
Depreciation	2,376,640	2,024,190	1,937,812
Tax equivalents	324,992	238,009	214,494
Social security taxes	243,346	228,588	224,130
Interest exp on customer deposits	14,351	16,608	7,502
Amortization of bond issue costs	11,582	11,582	-
Total Expenses	<u>69,389,065</u>	<u>64,538,235</u>	<u>54,779,542</u>
Transfers out – tax equivalents to City of Bristol	<u>(822,449)</u>	<u>(1,093,218)</u>	<u>(361,146)</u>
Change in net assets	4,015,111	2,095,682	3,076,002
Beginning net assets	63,583,229	61,487,547	58,411,545
Ending net assets	<u>\$ 67,598,340</u>	<u>\$ 63,583,229</u>	<u>\$ 61,487,547</u>

Management's Discussion and Analysis (continued)

Figure 1

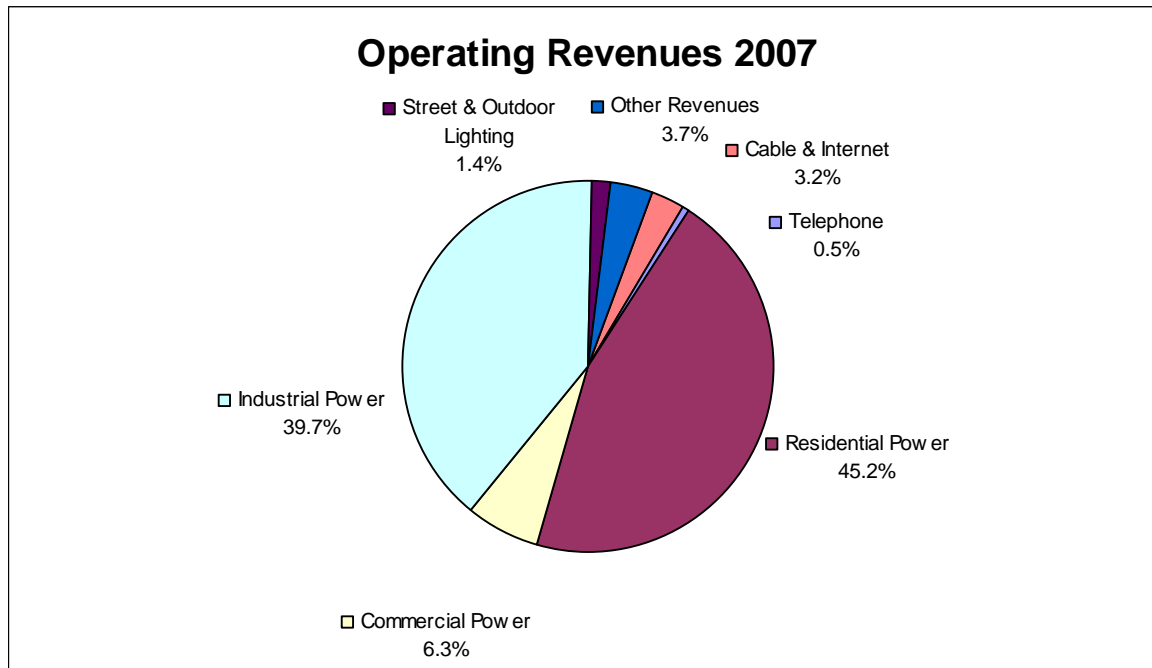
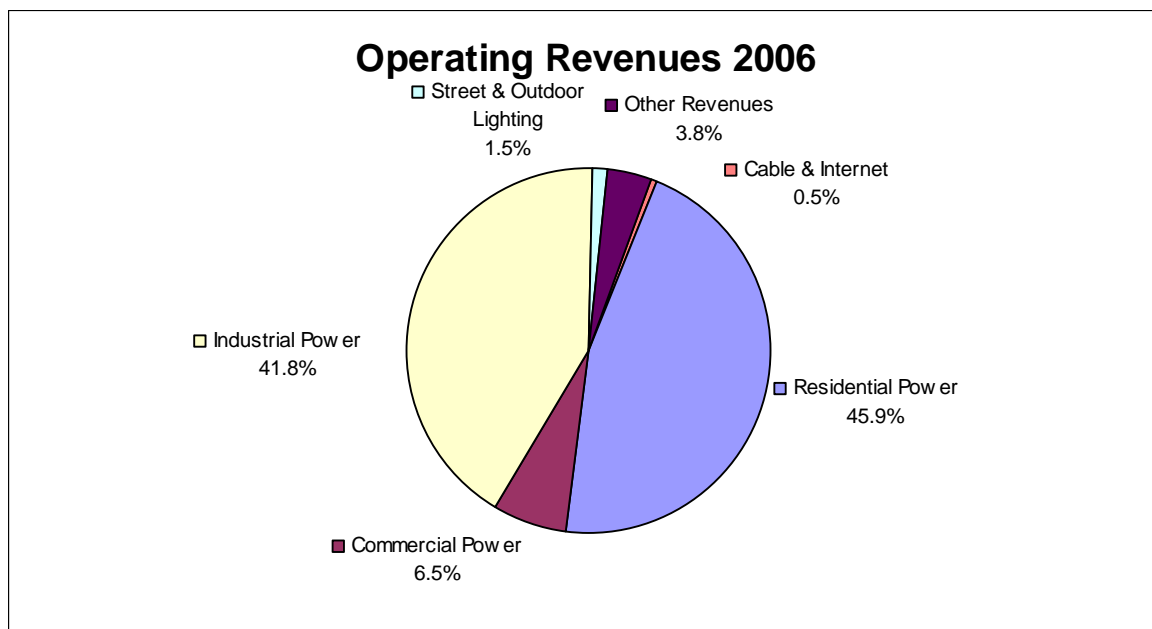
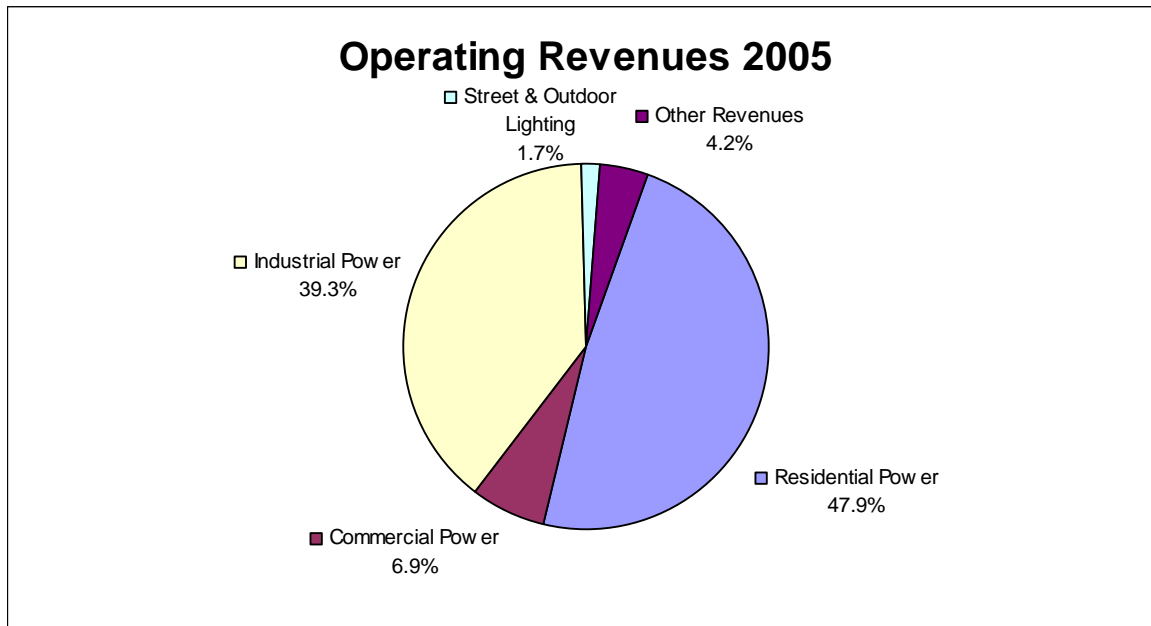


Figure 2



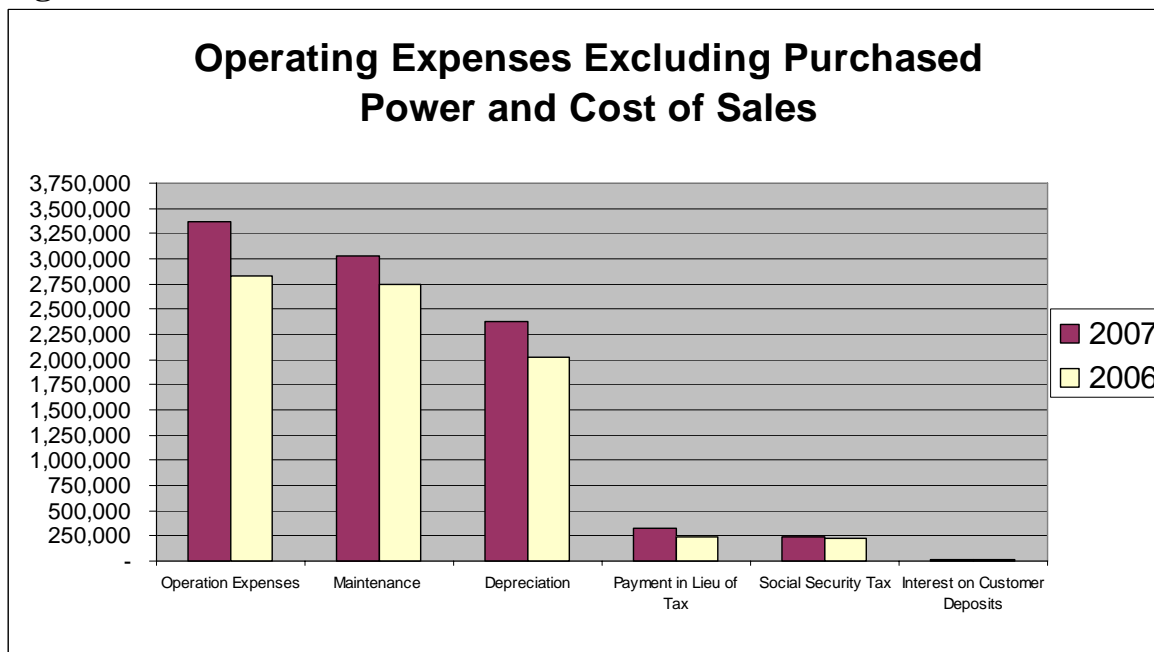
Management's Discussion and Analysis (continued)

Figure 3



Operating expenses, not including purchased power and cost of sales for cable, Internet and telephone, increased from 2006 to 2007, as indicated in Figure 4. The total was \$9,351,231 in 2007 compared to \$8,083,173 in 2006, resulting in a 16% increase.

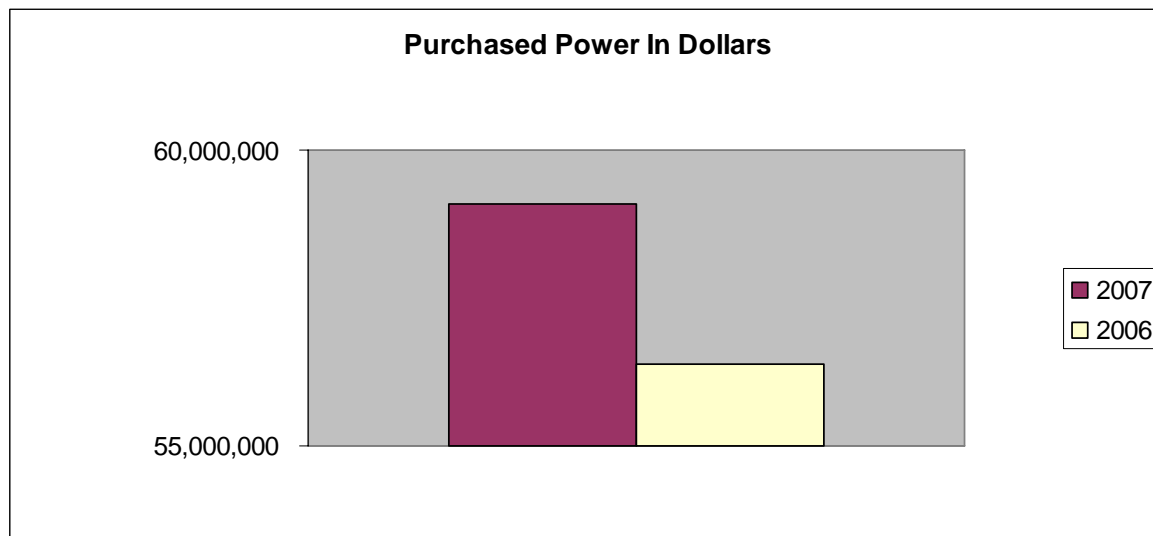
Figure 4



Management's Discussion and Analysis (continued)

As indicated in Figure 5, purchased power costs were \$59,088,380 in 2007 as compared to \$56,367,935 in 2006, resulting in a 5.0% increase. The correlation between electric sales and purchased power and weather is clearly shown as discussed on page 5. Temperature is a main driver; however recent rate increases passed by TVA have had a large affect on purchased power costs. TVA's rate increase in October 2005, increased purchase power rates by approximately 7.5%. TVA's rate increase in April 2006, increased purchase power rates by approximately 9.95%. Due to a TVA rate decrease in October 2006, BTES customers experienced approximately 4% in reduction of rates. Additionally, TVA implemented a Fuel Adjustment Cost at the same time, which is reviewed quarterly. The Fuel Adjustment Cost was zero in October 2006, 0.2% in January 2007 and 1.3% in April 2007.

Figure 5



Power Rates

BTES purchases its entire year power supply requirements from Tennessee Valley Authority ("TVA"). Rate options available to BTES' retail customers include firm, seasonal and interruptible service rates. The contract between TVA and BTES provides for TVA regulation over retail rates to customers. The interruptible rate programs provide large commercial and industrial customers with the potential for reduced rates along with the right for TVA to interrupt service as needed.

There are four customers participating in interruptible rate programs with a combined interruptible load of 31,692 kilowatts or about 14% of BTES' 2007 peak load. TVA's last curtailment of interruptible customers occurred in January 2004. Rate surveys show that BTES' rates are some of the most competitive in the U.S.

Management's Discussion and Analysis (continued)

Deregulation

Over the last few years, Congress has been debating legislation to restructure the electric utility industry. Because of TVA's unique situation, deregulation and competition at both national and state levels are moving more slowly to the Tennessee Valley. Under the existing law, TVA is the exclusive supplier of power within its statutorily defined service territory, an 80,000 square-mile area that includes virtually the entire state of Tennessee and parts of Kentucky, Mississippi, Alabama, Georgia, North Carolina and Virginia. BTES is shielded from competition until federal restructuring addresses the current law. BTES continues to be involved in the restructuring effort individually and also as a member of the Tennessee Valley Public Power Association, the American Public Power Association, Tennessee Municipal Electric Power Association and the State of Tennessee Legislature.

Debt

On July 27, 2005, BTES issued \$23,910,000 in Electric Revenue Bonds, Series 2005 for the purpose of financing improvements to BTES' system and pre-purchasing electrical power from TVA. The bonds are limited obligations of BTES payable solely from the net revenues of BTES.

The following is the bond activity for fiscal year 2007:

	Balance July 1, 2006	Decreases	Balance June 30, 2007
Electric System Revenue Bond	\$24,347,279	\$14,576	\$24,332,703

The following is the bond activity for fiscal year 2006:

	Balance July 1, 2005	Additions	Decreases	Balance June 30, 2006
Electric System Revenue Bond	\$ -	\$24,361,855	\$14,576	\$24,347,279

As the bonds are tax exempt and the bond proceeds are externally restricted for a specific purpose, GAAP requires interest income from the bond proceeds and interest expense on the outstanding bonds be netted for financial statement purposes; however, as all of the proceeds were used for improvements to the transmission and distribution system, BTES capitalized net interest cost of approximately \$805,000 during fiscal year 2007 and \$366,000 during fiscal year 2006.

Payment In Lieu of Taxes

BTES makes an in-lieu-of-tax payment to the municipalities and counties in which it sells power and has electric utility plant. For the City of Bristol, Tennessee, City of Bluff City, Tennessee and Sullivan County, Tennessee, the in-lieu-of-tax payment is based on the formula provided by the State of Tennessee Municipal Electric System Tax Equivalent Law of 1987. The formula includes a property tax equivalency calculation plus 4% of operating revenue less power costs (three-year average). For Washington County, Virginia the in-lieu-of-tax payment is based on the real property tax rate of the electric utility plant. The total in lieu of taxes paid during the years ended June 30, 2007 and 2006 were approximately \$1,060,000 and \$1,308,000, respectively. The differing amounts may be attributed to a payment to the City of Bristol, Tennessee in the amount of \$361,146 recorded in fiscal year 2006 related to fiscal year 2005.

Management's Discussion and Analysis (continued)

Non-Operating Revenue

Interest from investments increased from \$997,881 in 2006 to \$1,666,545 in 2007, resulting in an approximate 67% increase. As shown in Table 4, interest from investments is categorized as non-operating revenue. BTES continues to look for ways to maximize their earnings, such as the TVA's Discounted Energy Units Program discussed below.

Discounted Energy Units (DEU) Program

BTES invested \$8,000,000 in TVA's Discounted Energy Units ("DEU") Program in December 2003. The goal of the DEU Program is to create a financial partnership between TVA and its distributors, such as BTES, to help finance the re-start of the Browns Ferry Unit One power generator. This facility uses nuclear fuel to generate electricity. The potential benefits for BTES are to ensure a reliable, low-cost power supply and provide a vehicle to better use operating cash and improve working capital liquidity. This program provides BTES discounted monthly electric purchases that are equal to the monthly principle and interest payments. The discount rate is 5.5% and has a term of 10 years. BTES may borrow against part of the DEU investment in emergency situations, if needed. During 2007 and 2006, BTES recognized \$294,453 and \$334,468, respectively; in interest income from the amortization of the DEUs which is included in non-operating revenues discussed above.

Bristol Tennessee Essential Services

Balance Sheets

June 30, 2007 and 2006

	June 30	
	2007	2006
Assets		
Current assets:		
Cash and cash equivalents	\$ 15,848,584	\$ 12,176,520
Accounts receivable:		
Trade	3,592,348	3,281,473
Other	633,509	498,670
Allowance for bad debt	(327,017)	(77,968)
Net accounts receivable	3,898,840	3,702,175
Accrual for unbilled revenues	3,220,746	3,124,920
Interest receivable	118,485	4,238
Materials and supplies inventories	1,734,825	1,307,996
Current portion of customer notes receivable	370,000	406,000
Current portion of discounted energy units	791,820	749,547
Prepaid expenses and other current assets	132,652	210,020
Total current assets	26,115,952	21,681,416
Unrestricted noncurrent assets:		
Capital assets:		
Capital assets in service	75,892,376	67,688,084
Less accumulated depreciation	(43,279,392)	(41,076,189)
	32,612,984	26,611,895
Construction in progress	25,987,741	19,117,810
Non-utility property	975,480	975,480
Net capital assets	59,576,205	46,705,185
Other assets:		
Customer notes receivable, less current portion	2,024,289	2,065,991
Long-term investments	8,000,000	8,000,000
Prepaid pension cost	619,653	675,111
Discounted energy units, less current portion	4,153,471	4,945,292
Unamortized bond issue costs	335,922	347,505
Other	173,351	432,638
Total other assets	15,306,686	16,466,537
Total unrestricted noncurrent assets	74,882,891	63,171,722
Restricted cash and cash equivalents	-	11,173,161
Total noncurrent assets	74,882,891	74,344,883
Total assets	\$ 100,998,843	\$ 96,026,299

Bristol Tennessee Essential Services

Balance Sheets (continued)

June 30, 2007 and 2006

	June 30	
	2007	2006
Liabilities and net assets		
Current liabilities:		
Trade accounts payable	\$ 2,217,349	\$ 1,699,192
Accrual for unbilled power expense	2,819,524	2,781,509
Customer deposits and prepayments	2,212,556	2,088,295
Economic development funds passed through from Tennessee Valley Authority to City of Bristol, Tennessee	208,917	197,972
Interest payable	415,175	364,495
Other accrued liabilities	1,194,279	964,328
Current portion of bonds payable	440,000	-
Total current liabilities	9,507,800	8,095,791
Bonds payable, less current portion	23,892,703	24,347,279
Total liabilities	33,400,503	32,443,070
Net assets:		
Invested in capital assets, net of related debt	35,243,502	33,531,067
Unrestricted	32,354,838	30,052,162
Total net assets	67,598,340	63,583,229

Total liabilities and net assets

\$ 100,998,843 \$ 96,026,299

See accompanying Notes to Financial Statements.

Bristol Tennessee Essential Services

Statements of Revenues, Expenses and Changes in Net Assets

Years ended June 30, 2007 and 2006

	Year ended June 30	
	2007	2006
Operating revenues:		
Power revenues:		
Residential	\$ 32,770,537	\$ 30,666,486
Commercial (general power - under 50 kw)	4,585,336	4,363,430
Industrial (general power - 50 kw and over)	28,786,415	27,844,587
Street and outdoor lighting	1,033,334	983,468
Total power revenues	67,175,622	63,857,971
Cable revenues	1,604,935	247,943
Internet revenues	686,620	105,498
Telephone revenues	384,169	-
Other revenues	2,708,734	2,517,842
Total operating revenues	72,560,080	66,729,254
Cost of sales:		
Power purchased from Tennessee Valley Authority	59,088,380	56,367,935
Cable programming expense	801,066	70,545
Internet cost of sales	67,340	5,000
Telephone cost of sales	69,466	-
Total cost of sales	60,026,252	56,443,480
Gross profit	12,533,828	10,285,774
Operating expenses:		
Operations	3,362,770	2,825,591
Maintenance	3,029,132	2,750,187
Depreciation	2,376,640	2,024,190
Tax equivalents	324,992	238,009
Social security taxes	243,346	228,588
Interest expense on customer deposits	14,351	16,608
Total operating expenses	9,351,231	8,083,173
Operating income	3,182,597	2,202,601

Bristol Tennessee Essential Services

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

Years ended June 30, 2007 and 2006

	Year ended June 30	
	2007	2006
Nonoperating revenue (expense):		
Interest income (including \$294,453 in 2007 and \$334,468 in 2006 related to amortization of discounted energy units)	\$ 1,666,545	\$ 997,881
Amortization of bond issue costs	(11,582)	(11,582)
Income before transfers	4,837,560	3,188,900
Transfers out--tax equivalents to the City of Bristol, Tennessee	(822,449)	(1,093,218)
Change in net assets	4,015,111	2,095,682
Net assets at beginning of year	63,583,229	61,487,547
Net assets at end of year	<u>\$ 67,598,340</u>	<u>\$ 63,583,229</u>

See accompanying Notes to Financial Statements.

Bristol Tennessee Essential Services

Statements of Cash Flows

Years ended June 30, 2007 and 2006

	Year ended June 30	
	2007	2006
Cash flows from operating activities		
Cash received from customers	\$ 71,379,372	\$ 65,205,681
Cash received from City of Bristol, Tennessee	1,449,363	1,643,776
Cash paid to suppliers and vendors	(62,294,542)	(54,817,582)
Cash paid to employees for services	(3,250,534)	(3,178,298)
Cash paid to City of Bristol, Tennessee	-	(668,752)
Net cash provided by operating activities	<u>7,283,659</u>	<u>8,184,825</u>
Cash flows from noncapital financing activities		
Transfers to City of Bristol, Tennessee	(822,449)	(1,093,218)
Cash flows from investing activities		
Interest received on investments	1,532,749	1,376,507
Cash flows from capital and related financing activities		
Net proceeds from bonds payable	-	23,992,767
Interest payments on bonds payable	(1,055,100)	(705,114)
Net additions to capital assets	(14,439,956)	(15,799,668)
Net cash (used in) provided by capital and related financing activities	<u>(15,495,056)</u>	<u>7,487,985</u>
Decrease (increase) in cash and cash equivalents	(7,501,097)	15,956,099
Cash and cash equivalents at beginning of year	23,349,681	7,393,582
Cash and cash equivalents at end of year	<u><u>\$ 15,848,584</u></u>	<u><u>\$ 23,349,681</u></u>

Bristol Tennessee Essential Services
Statements of Cash Flows (continued)
Years ended June 30, 2007 and 2006

	Year ended June 30	
	2007	2006
Reconciliation of operating income to net cash provided by operating activities		
Operating income	\$ 3,182,597	\$ 2,202,601
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation	2,376,640	2,024,190
Provision for losses on accounts receivable	314,404	160,075
Redemption of discounted energy units	1,044,000	1,044,000
Changes in operating assets and liabilities:		
Accounts receivable	(511,069)	375,280
Accrual for unbilled revenues	(95,826)	(321,382)
Prepaid power purchased from Tennessee Valley Authority	-	3,093,653
Materials and supplies inventories	(426,829)	(426,791)
Customer notes receivable	77,702	7,930
Prepaid pension cost	55,458	55,458
Other assets	348,238	(381,759)
Trade accounts payable	515,172	33,119
Due to City of Bristol, Tennessee	10,945	(626,070)
Unbilled power expense	38,015	398,708
Customer deposits and prepayments	124,261	58,375
Other accrued liabilities	229,951	487,438
Net cash provided by operating activities	<u>\$ 7,283,659</u>	<u>\$ 8,184,825</u>

Supplemental disclosure of noncash activities

Accounts payable at June 30, 2007 and 2006 included \$423,671 and \$420,686 for construction in progress.

See accompanying Notes to Financial Statements.

Bristol Tennessee Essential Services

Notes to Financial Statements

June 30, 2007 and 2006

1. Significant Accounting Policies

General

Bristol Tennessee Essential Services ("BTES") is a self-supporting enterprise fund of the City of Bristol, Tennessee (the "City"). The City is the primary reporting entity. An enterprise fund is used to account for the financing of services to the general public on a continuing basis with costs recovered primarily through user charges. The Board of Directors of BTES is the level of responsibility that has oversight and control of BTES. The Board of Directors sets all policies, local rates and appoints the Chief Executive Officer. The Board of Directors is composed of five members, one of whom is also a member of the City Council, who are appointed by the mayor and confirmed by the City Council. They serve four-year staggered terms. BTES manages, operates and maintains the electric, cable, internet, and telephone utilities servicing the citizens of the City and surrounding areas. BTES issues a comprehensive annual financial report which is combined in the City's comprehensive annual financial report.

BTES has three business units within the enterprise fund, BTES accounts for the electric utility operations in the Electric Business Unit ("EBU"), the cable and internet operations in the Cable and Internet Business Unit ("CBU"), and telephone operations in the Telephone Business Unit ("TBU").

As required by Section 7-52-603 of the Tennessee Code Annotated ("TCA"), the EBU may not subsidize the operations of the CBU or the TBU with revenue from its power operations. In addition, the CBU and the TBU must maintain its own accounting records and any funds that are lent from the EBU must have a rate of interest, not less than the highest rate earned by the EBU on investment funds. See Note 16 for further discussion of these units.

BTES received approval in 2006 from the Tennessee Regulatory Authority for authorization to provide telecommunication services pursuant to Section 7-52-401 of the TCA.

The industries that CBU and TBU operate in are regulated by the Federal Communications Commission.

BTES utilizes the accrual basis of accounting whereby revenues are recorded in the period the related services are provided, and expenses are recorded in the period incurred. Accordingly, BTES has recorded an estimate of unbilled revenue and unbilled power expense. BTES considers all revenues and expenses to be operating, except for interest income and amortization of bond issue costs, which are classified as nonoperating.

Bristol Tennessee Essential Services
Notes to Financial Statements (continued)
June 30, 2007 and 2006

1. Significant Accounting Policies (continued)

General (continued)

BTES applies Financial Accounting Standards Board ("FASB") pronouncements issued on or before November 30, 1989, unless those pronouncements conflict with or contradict Governmental Accounting Standards Board ("GASB") pronouncements, in which case, GASB prevails. BTES has elected not to adopt the FASB Statements and Interpretations issued after November 30, 1989, in accordance with GASB Statement No. 20, "Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting."

BTES applies the provisions GASB No. 34, "Basic Financial Statements--and Management's Discussion and Analysis--for State and Local Governments" ("Statement 34"), as amended by GASB No. 37, "Basic Financial Statements--and Management's Discussion and Analysis--for State and Local Government: Omnibus" ("Statement 37"). Statements 34 and 37 established standards for external financial reporting and disclosure for all state and local governmental entities, which includes a balance sheet, a statement of revenues, expenses and changes in net assets and a statement of cash flows. Statement 34 requires the classification of net assets into three components – invested in capital assets, net of related debt; restricted; and unrestricted. These classifications are defined as follows:

- Invested in capital assets, net of related debt – This component of net assets consists of capital assets, including restricted capital assets, net of accumulated depreciation and reduced by the outstanding balances of any bonds, mortgages, notes, or other borrowings that are attributable to the acquisition, construction or improvement of those assets. If there are significant unspent related debt proceeds at year-end, the portion of the debt attributable to the unspent proceeds is not included in the calculation of invested in capital assets, net of related debt. Rather, that portion of the debt is included in the same net assets component as the unspent proceeds.
- Restricted – This component of net assets consists of constraints placed on net asset use through external constraints imposed by creditors (such as through debt covenants), grantors, contributors or laws or regulations of other governments or constraints imposed by law through constitutional provisions or enabling legislation.
- Unrestricted – This component of net assets consists of net assets that do not meet the definition of "restricted or "invested in capital assets, net of related debt."

The unrestricted category includes a renewal and replacement fund of \$8,000,000 which was established by the Board of Directors to set aside funds for future construction, improvements and extensions of BTES.

Bristol Tennessee Essential Services
Notes to Financial Statements (continued)
June 30, 2007 and 2006

1. Significant Accounting Policies (continued)

Measurement Focus

The accounting and financial reporting treatment applied to a fund is determined by its measurement focus. BTES operations are accounted for on a flow of economic resources measurement focus. With this measurement focus, all assets and all liabilities associated with the operation of the enterprise fund are included on the balance sheet. Operating statements present increases (e.g. revenues) and decreases (e.g. expenses) in net total assets.

Fiscal Year-End

BTES operates on a fiscal year ending June 30. All references in these notes refer to the fiscal year-end unless otherwise specified.

Cash and Cash Equivalents and Investments

Cash and cash equivalents include cash on hand and in demand deposits, and those investments which are generally a part of BTES short-term cash management activities. State statutes authorize BTES to invest in certificates of deposit, U.S. Treasury obligations, U.S. Agency issues and the State Local Government Investment Pool.

Temporary investments, consisting entirely of certificates of deposit, are stated at cost which approximates fair value.

Materials and Supplies Inventories

Materials and supplies are valued at the lower of cost or market, utilizing the moving average method of determining cost.

Capital Assets

Capital assets are carried at historical cost, including applicable general and administrative costs and payroll related costs such as pensions, taxes and other employee benefits. Substantially all renewals and betterments are capitalized in accordance with BTES' capitalization policy. When property is retired or otherwise disposed of, its average cost, together with its cost of removal less salvage, is charged to accumulated depreciation; no gain or loss is recognized.

Bristol Tennessee Essential Services
Notes to Financial Statements (continued)
June 30, 2007 and 2006

1. Significant Accounting Policies (continued)

Capital Assets (continued)

Capital assets other than land, construction in progress and non-utility property, are depreciated using the straight-line method at rates which will amortize costs over the estimated useful lives of the assets. The estimated useful lives of depreciable capital assets are as follows:

Transmission equipment, fixtures and devices	30 to 40 years
Distribution transformers, meters, fixtures and devices	15 to 50 years
Buildings and improvements	50 years
Electronic communication equipment	15 to 20 years
Furniture, fixtures and equipment	5 to 25 years

The provision for depreciation does not include depreciation on transportation equipment. Those amounts are reported as operating expenses in the Statements of Revenues, Expenses and Changes in Net Assets and totaled \$89,915 in 2007 and \$88,807 in 2006. The cost of maintenance and repairs is charged to expense as incurred.

Compensated Absences

BTES recognizes the cost of vacation pay as earned. In the event of termination or retirement, an employee is reimbursed for accumulated vacation days. In general, accumulated vacation days are limited to thirty days.

Reclassifications

Certain amounts in the prior year have been reclassified to conform with 2007 classifications.

Use of Estimates

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

2. Power Contract

BTES has a power contract with the Tennessee Valley Authority ("TVA") whereby BTES purchases all its electric power from TVA and is subject to certain restrictions and conditions as provided in the contract. Either party may terminate this contract at any time upon not less than five years prior written notice.

Bristol Tennessee Essential Services
Notes to Financial Statements (continued)
June 30, 2007 and 2006

3. Residential Energy Efficiency Program Loans

BTES provides loans to customers for heat pump and insulation costs under BTES Residential Energy Efficiency Program. The majority of these loans bears interest at rates ranging from 8% to 10.25% and has maturities of up to 10 years. Satisfactory credit reports are required prior to loan approval. Additionally, these loans are secured by a deed of trust on the property. BTES recorded interest income of approximately \$224,000 in 2007 and \$240,000 in 2006 related to these loans. These amounts offset operating expenses in the Statements of Revenues, Expenses and Changes in Net Assets, since management believes this is an operating activity and the income should offset the additional expenses associated with maintaining this loan program.

4. Concentration of Credit Risk

BTES provides electric, cable, internet, and voice services primarily to customers in northeastern Tennessee. Electric customers include residential, commercial and industrial service. Residential and commercial customers are required to have satisfactory credit reports or place deposits with BTES that approximate two months' highest expected bill. Industrial customers are generally required to either place deposits with BTES that approximate two months' highest expected bill or obtain a letter of credit or surety bond as security. Interest accrues on any deposits at the passbook interest rate of the bank where the funds are deposited and totaled \$10,083 in 2007 and \$16,608 in 2006. Cable, internet, and telephone customers are billed in advance of their service; however, any deferred revenue related to these services is not considered significant. BTES also makes and services loans to customers for heat pump and insulation costs. A subordinate deed of trust is obtained on the related property for these loans. Loss experience on accounts and notes receivable has historically not been significant to BTES operations.

5. Pension Plan

Plan Description

Certain employees of BTES are members of the Political Subdivision Pension Plan ("PSPP"), an agent multiple-employer defined benefit pension plan administered by the Tennessee Consolidated Retirement System ("TCRS"). TCRS provides retirement benefits as well as death and disability benefits. Benefits are determined by a formula using the member's high five-year average salary and years of service. Members become eligible to retire at the age of 60 with five years of service or at any age with 30 years of service. A reduced retirement benefit is available to vested members at the age of 55. Disability benefits are available to active members with five years of service who became disabled and cannot engage in gainful employment. There is no service requirement for disability that is the result of an accident or injury occurring while the member was in the performance of duty.

Bristol Tennessee Essential Services
Notes to Financial Statements (continued)
June 30, 2007 and 2006

5. Pension Plan (continued)

Funding Policy

Members joining BTES after July 1, 1979, become vested after five years of service and members joining prior to July 1, 1979, were vested after four years of service. Benefit provisions are established in state statute found in Title 8, Chapter 34-37 of the *Tennessee Code Annotated* ("TCA"). State statutes are amended by the Tennessee General Assembly. Political subdivisions such as BTES participate in the TCRS as individual entities and are liable for all costs associated with the operation and administration of their plan. Benefit improvements are not applicable to a political subdivision unless approved by the chief governing body.

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

BTES requires employees to contribute 5% of earnable compensation.

BTES is required to contribute at an actuarially determined rate using the frozen entry age actuarial cost method; the rate for 2007 and 2006 was 14.92% and 11.23%, respectively, of annual covered payroll. The 2006 required contributions were determined as part of the July 1, 2003 actuarial valuation. The 2007 required contributions were determined as part of the July 1, 2005 actuarial valuation. The contribution requirements for plan members are set by state statute. The contribution requirements for BTES are established and may be amended by the TCRS Board of Trustees.

Prepaid Pension Cost

GASB Statement No. 27, "Accounting for Pensions by State and Local Governmental Employers", requires employers to record contributions to a pension plan in excess of the annual pension cost as an asset. BTES has previously contributed amounts in excess of the annual pension cost to the PSPP and recorded these amounts as a prepaid pension cost. Activity in the prepaid pension cost is as follows for the years ended June 30:

	2007	2006
Balance at beginning of year	\$675,111	\$730,569
Annual pension cost:		
Annual required contribution	478,187	338,163
Interest on prepaid pension cost	(50,633)	(55,142)
Adjustment to the annual required contribution	106,091	110,600
Total annual pension cost	533,645	393,621
Contributions made	478,187	338,163
Decrease in prepaid pension cost	(55,458)	(55,458)
Balance at end of year	\$619,653	\$675,111

Bristol Tennessee Essential Services
Notes to Financial Statements (continued)
June 30, 2007 and 2006

5. Pension Plan (continued)

Actuarial Assumptions

Significant actuarial assumptions used in the July 1, 2005 and 2003, valuations include (a) rate of return on investment of present and future assets of 7.5% a year compounded annually, (b) projected salary increases of 4.75% (graded) annual rate (no explicit assumption is made regarding the portion attributable to the effects of inflation on salaries), (c) projected 3.5% annual increase in the Social Security wage base and (d) projected post-retirement increases of 3% annually. The actuarial value of assets was determined using techniques that smooth the effect of short-term volatility in the fair value of total investments over a five-year period. BTES' unfunded actuarial accrued liability is being amortized as a level dollar amount on a closed basis. The remaining amortization period at July 1, 2005, was 10 years.

Trend Information

Year ended June 30	Annual Pension Cost (APC)	Percentage of APC Contributed	Prepaid Pension Cost
2007	\$533,645	89.6%	\$619,653
2006	393,621	85.9%	675,111
2005	393,268	84.6%	730,569

Required Supplementary Information

Schedule of Funding Progress (Dollar amounts in thousands)

Actuarial Valuation Date	Actuarial Value of Assets	Actuarial Accrued Liability (AAL)	Unfunded AAL (UAAL)	Funded Ratio	Covered Payroll	UAAL as a Percentage of Covered Payroll
7/01/05	\$12,335	\$13,290	\$ 955	92.81%	\$2,890	33.06%
7/01/03	11,831	12,907	1,076	91.66%	2,584	41.64%
7/01/01	11,492	12,584	1,092	91.32%	2,465	44.30%

6. 401(k) Retirement Plan

BTES administers a defined contribution plan in the form of a 401(k) plan (Bristol Tennessee Electric System 401(k) Retirement Plan) available to all employees who have completed six months of employment. During 2007, the amount of payroll covered by the plan was \$2,960,288 of total payroll of \$3,291,513. During 2006, the amount of payroll covered by the plan was \$2,628,323 of total payroll of \$3,101,298. Under the plan terms, BTES will match participant contributions up to 6% of the participant's salary. Participants are not required but may contribute up to a total of 15% of their pre-tax earnings, subject to IRS limitations.

Bristol Tennessee Essential Services
Notes to Financial Statements (continued)
June 30, 2007 and 2006

6. 401(k) Retirement Plan (continued)

Additionally, participants may contribute up to 10% of their after-tax earnings. Participants are 100% vested in the employer contributions when they are made. During 2007 and 2006, BTES contributed \$162,953 and \$155,009, respectively, to the plan which represents 5.5% and 5.9%, respectively, of the covered payroll and 100% of the required contribution for each year. During 2007 and 2006, the participants contributed \$241,444 and \$218,023, respectively, which represents 8.2% and 8.3%, respectively, of the covered payroll.

7. Capital Assets

The following is a summary of capital assets for the year ended June 30, 2007:

	Balance July 1, 2006	Increases	Decreases	Balance June 30, 2007
Capital assets not being depreciated:				
Land	\$ 1,051,638	\$ —	\$ —	\$ 1,051,638
Non-utility property	975,480	—	—	975,480
Construction in progress	19,117,810	15,244,435	(8,374,504)	25,987,741
Total capital assets not being depreciated	21,144,928	15,244,435	(8,374,504)	28,014,859
Capital assets being depreciated:				
Transmission equipment, fixtures and devices	2,822,620	648	—	2,823,268
Distribution transformers, meters, fixtures and devices	55,486,617	1,783,675	(170,212)	57,100,080
Buildings and improvements	2,021,685	—	—	2,021,685
Furniture, fixtures and equipment	6,305,524	6,590,181	—	12,895,705
Total capital assets being depreciated	66,636,446	8,374,504	(170,212)	74,840,738
Less accumulated depreciation:				
Transmission equipment, fixtures and devices				
Distribution transformers, meters, fixtures and devices	(1,374,877)	(112,818)		(1,487,695)
Buildings and improvements	(36,263,262)	(1,789,240)	—	(38,052,502)
Furniture, fixtures and equipment	(1,001,430)	(18,577)	60,768	(959,239)
Total accumulated depreciation	(41,076,189)	(2,348,961)	145,758	(43,279,392)
Net capital assets being depreciated	25,560,257	6,025,543	(24,454)	31,561,346
Total net capital assets	\$46,705,185	\$21,269,978	\$(8,398,958)	\$59,576,205

During 2007, BTES capitalized approximately \$800,000 in interest expense, net of interest income from the tax-exempt borrowings of approximately \$250,000. During 2006, BTES capitalized approximately \$350,000 in interest expense, net of interest income from the tax-exempt borrowings of approximately \$700,000.

Bristol Tennessee Essential Services
Notes to Financial Statements (continued)
June 30, 2007 and 2006

8. Cash and Investments

Cash and investments consist of the following as of June 30, 2007:

	Amount	Interest Rate	Purchase Date	Maturity Date
Renewal and replacement fund:				
Certificate of deposit	\$ 324,582	5.26%	4/30/07	7/30/07
Certificate of deposit	2,169,512	5.20%	4/11/07	7/11/07
Certificate of deposit	2,177,478	5.26%	5/07/07	8/07/07
Certificate of deposit	3,328,428	5.20%	6/13/07	9/13/07
Total renewal and replacement fund	<u>8,000,000</u>			
Other funds:				
Certificate of deposit	1,587,301	5.26%	4/25/07	7/25/07
Certificate of deposit	2,289,416	5.26%	5/07/07	8/07/07
Certificate of deposit	2,430,102	5.20%	6/13/07	9/13/07
Certificate of deposit	2,606,846	5.26%	4/30/07	7/30/07
Business money market account	165,980	4.04%	—	—
Business money market account	1,898,506	4.25%	—	—
Cash on deposit	4,870,433	Various	—	—
Total other funds	<u>15,848,584</u>			
Total cash and investments	<u>\$23,848,584</u>			

Cash and investments consist of the following as of June 30, 2006:

	Amount	Interest Rate	Purchase Date	Maturity Date
Renewal and replacement fund:				
Certificate of deposit	\$ 1,500,000	4.74%	1/31/06	7/29/06
Certificate of deposit	2,000,000	4.98%	4/11/06	7/11/06
Certificate of deposit	2,000,000	4.65%	5/02/06	8/02/06
Certificate of deposit	2,500,000	4.75%	6/08/06	9/08/06
Total renewal and replacement fund	<u>8,000,000</u>			
Other funds:				
Certificate of deposit	520,432	4.15%	6/11/06	7/11/06
Certificate of deposit	2,123,811	4.65%	5/02/06	8/02/06
Certificate of deposit	2,325,712	5.16%	6/01/06	9/01/06
Certificate of deposit	2,501,126	4.74%	1/31/06	7/31/06
Business money market account	2,522,226	4.89%	—	—
Business money market account	11,173,161	4.87%	—	—
Cash on deposit	2,183,213	Various	—	—
Total other funds	<u>23,349,681</u>			
Total cash and investments	<u>\$31,349,681</u>			

Bristol Tennessee Essential Services
Notes to Financial Statements (continued)
June 30, 2007 and 2006

8. Cash and Investments (continued)

Custodial credit risk is the risk that in the event of a financial institution failure, BTES deposits may not be returned to it. As of June 30, 2007, the custodial credit risk of BTES deposits in financial institutions (including certificates of deposit) are summarized as follows:

	Financial Institution Balance
Insured	\$21,352,413
Uninsured and collateral held by the pledging financial institution's trust department not in BTES name	5,658,531
Total	<u>\$27,010,944</u>

The amount of deposits classified as "Uninsured and collateral held by the pledging financial institution's trust department not in BTES name" resulted from a financial institution inadvertently not reporting BTES accounts to the state as public accounts. This error was detected subsequent to year-end, and the accounts were insured at that time, resulting in no loss to BTES. Carrying amounts differ from financial institution balances primarily due to outstanding checks and deposits in transit.

Purchases of certificates of deposit in the renewal and replacement fund totaled \$34,241,990 in 2007 and \$20,524,000 in 2006. Sales of certificates of deposit in the renewal and replacement fund totaled \$35,276,351 in 2007 and \$37,827,000 in 2006.

9. Discounted Energy Units

During 2003, BTES purchased \$8,000,000 in discounted energy units from TVA which are redeemable on a straight-line basis over the next ten years. The units carry a discount of 5.5% and amounted to \$4,945,291 and \$5,694,839 as of June 30, 2007 and 2006, respectively.

10. Bonds Payable

Changes in bonds payable are summarized as follows:

	Balance July 1, 2006	Decreases	Balance June 30, 2007
Electric System Revenue Bonds, Series 2005	\$23,910,000	\$ —	\$23,910,000
Plus unamortized premium	437,279	(14,576)	422,703
Total bonds payable	\$24,347,279	\$(14,576)	<u>\$24,332,703</u>

Bristol Tennessee Essential Services
Notes to Financial Statements (continued)
June 30, 2007 and 2006

10. Bonds Payable (continued)

	Balance July 1, 2005	Additions	Decreases	Balance June 30, 2006
Electric System Revenue Bonds, Series 2005	\$ -	\$23,910,000	\$ -	\$23,910,000
Plus unamortized premium	-	451,855	(14,576)	437,279
Total bonds payable	<u>\$ -</u>	<u>\$24,361,855</u>	<u>\$(14,576)</u>	<u>\$24,347,279</u>

During 2006, the City issued \$23,910,000 in 2005 Electric System Revenue Bonds (the "Bonds") on behalf of BTES. The Bonds were issued for the purposes of providing funds to construct improvements and extensions of BTES' transmission and distribution system and to pre-purchase electric power from TVA. The Bonds are payable in annual installments ranging from \$440,000 in 2008 to \$1,450,000 in 2036. Bonds maturing on or after September 1, 2016 (\$18,765,000) are callable by the City at par at any time in any amount on or after September 1, 2015.

The interest rates on the Bonds are fixed and for each series, however, the interest rates for each series vary between 3.25% to 5% depending on the maturity. For 2007 and 2006, the effective annual interest rate on the Bonds was 4.413%.

The Bonds are secured by the net power revenues of BTES. As of June 30, 2007, BTES had expended all cash and cash equivalents from the proceeds of the debt issuance which were restricted for the purposes indicated above. In addition, BTES has obtained a surety bond in lieu of funding a debt service reserve fund as required by the bond agreement.

Maturities of the Bonds as of June 30, 2007, are as follows:

Fiscal Year	Principal	Interest	Total
2008	\$ 440,000	\$ 1,047,400	\$ 1,487,400
2009	455,000	1,031,738	1,486,738
2010	470,000	1,015,550	1,485,550
2011	485,000	998,838	1,483,838
2012	505,000	981,513	1,486,513
2013-2017	2,790,000	4,638,009	7,428,009
2018-2022	3,455,000	3,974,170	7,429,170
2023-2027	4,395,000	3,040,475	7,435,475
2028-2032	5,510,000	1,922,375	7,432,375
2033-2036	5,405,000	540,107	5,945,107
	<u>\$23,910,000</u>	<u>\$19,190,175</u>	<u>\$43,100,175</u>

Bristol Tennessee Essential Services
Notes to Financial Statements (continued)
June 30, 2007 and 2006

11. Self-Insurance Plan

BTES is self-insured for employee group health benefits. A liability is recorded, if necessary, for those claims incurred but not paid prior to year-end, both reported and unreported, based on prior experience and claims reported subsequent to year-end. Changes in estimates for claims incurred but not reported are recorded in the year the estimates are revised. BTES' risk is \$50,000 per covered employee up to an annual maximum of \$460,555. An insurance company has insured all claims exceeding \$460,555.

Activity in the estimated liability for claims incurred but not paid is as follows for the years ended June 30:

	2007	2006
Balance at beginning of year	\$ –	\$ –
Expense recorded related to:		
Current year	355,109	281,370
Prior year	46,021	27,000
Net expense recorded	401,130	308,370
Payments related to:		
Current year	225,071	281,242
Prior year	46,021	27,128
Total payments	271,092	308,370
Balance at end of year	\$130,038	\$ –

12. Risk Management

BTES is exposed to various risks of loss related to torts; theft of, damage to and destruction of assets; errors and omissions; natural disasters; and injuries of employees for which BTES carries commercial insurance purchased from independent third parties. BTES has not experienced a settlement in excess of insurance coverage in any of the past three fiscal years. BTES bears the risk of loss up to the deductible amounts which are disclosed in the accompanying Statistical Section.

13. Related Party Transactions

As described in Note 1, BTES is a self-supporting fund of the City. In the normal course of operations, BTES provides electrical service to the City at standard electric rates which generated revenues of \$1,492,028 in 2007 and \$1,662,054 in 2006. As of June 30, 2007 and 2006, \$140,515 and \$121,949, respectively, was recorded as a receivable from the City for these revenues. Payment is due within approximately 30 days of the billing.

Bristol Tennessee Essential Services
Notes to Financial Statements (continued)
June 30, 2006 and 2005

13. Related Party Transactions (continued)

During 1997, BTES received \$2,000,000 in purchased power credits from TVA for investments related to economic development of the City. At the City's request, BTES remits these funds to the City. Remaining activity related to these funds is as follows for the years ended June 30:

	<u>2007</u>	<u>2006</u>
Balance at beginning of year	\$197,972	\$824,042
Interest accruals	10,945	21,020
Payments remitted to City	—	(647,090)
Balance at end of year	<u>\$208,917</u>	<u>\$197,972</u>

Interest accruals are netted against interest income in the accompanying financial statements.

BTES made tax equivalent payments to the City of \$822,449 in 2007 and \$1,093,218 in 2006. These payments are based on BTES capital assets, along with average operating revenues less power costs.

14. Postemployment Benefits

As discussed in Note 11, BTES is self-insured for employee group health benefits. BTES also provides these benefits to certain retired employees, although not required by any statutory, contractual or other authority. As of June 30, 2007, there were 21 retirees eligible to receive these benefits. Benefits related to these retirees are expensed when paid and totaled approximately \$67,000 in 2007 and \$77,000 in 2006.

Additionally, BTES is self-insured for certain life insurance benefits for retirees. Employees who retire with 30 years of service or age 60 with a minimum of 20 years of service receive \$5,000 in life insurance for annual salaries less than \$10,000 plus \$1,000 in life insurance for each additional \$5,000 of annual salary or fraction thereof. As of June 30, 2007, there were 11 retirees eligible to receive these benefits and, accordingly, a liability for \$117,250 has been recorded for these benefits. BTES made no payments in 2007 and 2006 related to these benefits.

Bristol Tennessee Essential Services
Notes to Financial Statements (continued)
June 30, 2007 and 2006

15. Net Assets

Net assets consist of the following as of June 30:

	<u>2007</u>	<u>2006</u>
Invested in capital assets, net of related debt consists of the following:		
Capital assets	\$59,576,205	\$46,705,185
Restricted unspent bond funds	—	11,173,161
Less bond payable	24,332,703	24,347,279
Invested in capital assets, net of related debt	<u>\$35,243,502</u>	<u>\$33,531,067</u>

Unrestricted net assets consist of all other items in the balance sheet not reflected above.

16. Segment Information

As discussed in Note 1, BTES operates three different business units. BTES allocates direct costs to the specific business unit, common costs (costs that cannot be directly assigned to a business unit) are allocated based on a direct analysis of the origin of the costs, an indirect, cost-causative linkage to another category for which direct assignment or allocation is available, or based on a general allocator. For inter-unit loans, the business unit charges the highest rate of interest earned on invested funds. Depreciation, pole attachment fees, interest expense, and taxes are allocated based on a per service usage model.

Bristol Tennessee Essential Services
Notes to Financial Statements (continued)

June 30, 2007 and 2006

16. Segment Information (continued)

Summary financial statement information for each of the business units are as follows (does not include inter-unit eliminations):

Condensed Statement of Net Assets by Business Unit

	June 30, 2007		
	EBU	CBU	TBU
Assets:			
Current assets	\$ 25,894,438	\$ 167,813	\$ 53,701
Due from other business units	3,893,232	-	-
Net capital assets	55,624,867	2,899,155	1,052,183
Other noncurrent assets	15,306,686	-	-
Total assets	<u>\$ 100,719,223</u>	<u>\$ 3,066,968</u>	<u>\$ 1,105,884</u>
Liabilities and net assets:			
Current liabilities	\$ 9,489,984	\$ 11,785	\$ 6,031
Due to other business units	-	2,873,271	1,019,961
Bonds payable, long-term portion	23,892,703	-	-
Total liabilities	<u>33,382,687</u>	<u>2,885,056</u>	<u>1,025,992</u>
Invested in capital assets, net of related debt	35,185,396	25,884	32,222
Unrestricted	32,151,140	156,028	47,670
Total net assets	<u>67,336,536</u>	<u>181,912</u>	<u>79,892</u>
Total liabilities and net assets	<u>\$ 100,719,223</u>	<u>\$ 3,066,968</u>	<u>\$ 1,105,884</u>

Bristol Tennessee Essential Services
Notes to Financial Statements (continued)

June 30, 2007 and 2006

16. Segment Information (continued)

Condensed Statement of Revenues, Expenses and Changes in Net Assets

	Year ended June 30, 2007		
	EBU	CBU	TBU
Operating revenues	\$ 69,850,039	\$ 2,322,091	\$ 387,950
Cost of sales	59,088,380	868,406	69,466
Gross profit	10,761,659	1,453,685	318,484
Operating expenses	8,015,158	1,137,634	198,439
Operating income	2,746,501	316,051	120,045
Nonoperating revenue (expense)	1,894,911	(199,795)	(40,153)
Income before transfers	4,641,412	116,256	79,892
Transfers out	(822,449)	-	-
Change in net assets	3,818,963	116,256	79,892
Net assets at beginning of year	63,517,573	65,656	-
Net assets at end of year	\$ 67,336,536	\$ 181,912	\$ 79,892

Condensed Statement of Cash Flows by Business Unit

	Year ended June 30, 2007		
	EBU	CBU	TBU
Net cash provided by (used in):			
Operating activities	\$ 7,283,659	\$ -	\$ -
Noncapital financing activities	(822,449)	-	-
Investing activities	1,532,749	-	-
Capital and related financing activities	(15,495,056)	-	-
Decrease in cash and cash equivalents	(7,501,097)	-	-
Cash and cash equivalents at beginning	23,349,681	-	-
Cash and cash equivalents at end of year	\$ 15,848,584	\$ -	\$ -

Bristol Tennessee Essential Services

Notes to Financial Statements (continued)

June 30, 2007 and 2006

16. Segment Information (continued)

Condensed Statement of Net Assets by Business Unit

	June 30, 2006		
	EBU	CBU	TBU
Assets:			
Current assets	\$ 21,606,767	\$ 74,649	\$ -
Due from other business units	4,088,719	-	-
Net capital assets	43,284,440	3,096,846	323,899
Other noncurrent assets	26,968,013	366,576	305,109
Total assets	<u>\$ 95,947,939</u>	<u>\$ 3,538,071</u>	<u>\$ 629,008</u>
Liabilities and net assets:			
Current liabilities	\$ 8,083,087	\$ 12,704	\$ -
Due to other business units	-	3,459,711	629,008
Bonds payable	24,347,279	-	-
Total liabilities	<u>32,430,366</u>	<u>3,472,415</u>	<u>629,008</u>
Invested in capital assets, net of related debt	33,947,111	(68,539)	-
Unrestricted	29,570,462	134,195	-
Total net assets	<u>63,517,573</u>	<u>65,656</u>	<u>-</u>
Total liabilities and net assets	<u>\$ 95,947,939</u>	<u>\$ 3,538,071</u>	<u>\$ 629,008</u>

Bristol Tennessee Essential Services

Notes to Financial Statements (continued)

June 30, 2007 and 2006

16. Segment Information (continued)

Condensed Statement of Revenues, Expenses and Changes in Net Assets

	Year ended June 30, 2006		
	EBU	CBU	TBU
Operating revenues	\$ 66,375,813	\$ 353,441	\$ -
Cost of sales	56,367,935	75,545	-
Gross profit	10,007,878	277,896	-
Operating expenses	7,870,933	212,240	-
Operating income	2,136,945	65,656	-
Nonoperating revenue	986,299	-	-
Income before transfers	3,123,244	65,656	-
Transfers out	(1,093,218)	-	-
Change in net assets	2,030,026	65,656	-
Net assets at beginning of year	61,487,547	-	-
Net assets at end of year	\$ 63,517,573	\$ 65,656	\$ -

Condensed Statement of Cash Flows by Business Unit

	Year ended June 30, 2006		
	EBU	CBU	TBU
Net cash provided by (used in):			
Operating activities	\$ 8,184,825	\$ -	\$ -
Noncapital financing activities	(1,093,218)	-	-
Investing activities	1,376,507	-	-
Capital and related financing activities	7,487,985	-	-
Increase in cash and cash equivalents	15,956,099	-	-
Cash and cash equivalents at beginning of year	7,393,582	-	-
Cash and cash equivalents at end of year	\$ 23,349,681	\$ -	\$ -

Bristol Tennessee Essential Services

Schedule of Net Assets (Last Ten Years)

Fiscal Years 2007 - 1998 (in thousands)

	2007	2006	2005	2004	2003	2002	2001	2000	1999	1998
Invested in capital assets, net of related debt	\$ 35,243	\$ 33,531	\$ 34,026	\$ 31,895	\$ 31,568	\$ 29,297	\$ 27,744	\$ 27,753	\$ 28,273	\$ 27,902
Unrestricted	32,355	30,052	27,462	26,516	24,485	26,346	26,658	24,408	21,255	19,831
Total net assets	\$ 67,598	\$ 63,583	\$ 61,488	\$ 58,411	\$ 56,053	\$ 55,643	\$ 54,402	\$ 52,161	\$ 49,528	\$ 47,733

Note 1: Information is summarized from audited financial statements for the year indicated.

Bristol Tennessee Essential Services

Statement of Revenues and Expenses (Last Ten Years)

Fiscal Years 2007-1998 (in thousands)

	2007	2006	2005	2004	2003	2002	2001	2000	1999	1998
Operating revenues:										
Residential	\$ 32,770	\$ 30,666	\$ 27,475	\$ 28,368	\$ 26,699	\$ 24,746	\$ 25,877	\$ 24,212	\$ 23,575	\$ 23,408
Commercial	4,585	4,363	3,936	3,888	3,621	3,373	3,562	3,442	3,408	3,280
Industrial	28,786	27,845	22,524	22,143	20,072	19,006	19,650	18,953	19,224	17,814
Street and outdoor lighting	1,033	984	965	911	855	852	919	844	832	815
Cable	1,605	248	-	-	-	-	-	-	-	-
Internet	687	105	-	-	-	-	-	-	-	-
Telephone	385	-	-	-	-	-	-	-	-	-
Other revenues	2,709	2,518	2,424	2,448	2,100	2,018	2,023	1,919	1,844	1,807
Total operating revenues	72,560	66,729	57,324	57,758	53,347	49,995	52,031	49,370	48,883	47,124
Cost of sales:										
Power purchased from TVA	59,088	56,368	47,006	48,328	44,701	41,631	43,630	41,265	40,913	39,373
Cable programming expense	801	71	-	-	-	-	-	-	-	-
Internet cost of sales	67	5	-	-	-	-	-	-	-	-
Telephone cost of sales	70	-	-	-	-	-	-	-	-	-
Total cost of sales	60,026	56,444	47,006	48,328	44,701	41,631	43,630	41,265	40,913	39,373
Gross profit	12,534	10,285	10,318	9,430	8,646	8,364	8,401	8,105	7,970	7,751
Operating expenses:										
Operations	3,363	2,826	2,829	2,743	2,599	2,412	2,339	2,213	2,128	1,975
Maintenance	3,029	2,750	2,560	2,635	2,533	2,319	2,275	2,212	2,137	2,267
Depreciation	2,377	2,024	1,938	1,898	1,960	1,918	1,863	1,814	1,765	1,655
Tax equivalents	325	238	214	212	206	195	857	868	913	888
Social security taxes	243	228	224	206	213	193	162	158	156	156
Interest on customer deposits	14	17	8	6	6	11	19	19	17	17
Total operating expenses	9,351	8,083	7,773	7,700	7,517	7,048	7,515	7,284	7,116	6,958
Operating income	3,183	2,202	2,545	1,730	1,129	1,316	886	821	854	793
Net non-operating revenue	1,655	986	892	628	587	591	1,355	1,071	918	816
Income before transfers	4,838	3,188	3,437	2,358	1,716	1,907	2,241	1,892	1,772	1,609
Transfers out--tax equivalents to the										
City of Bristol, Tennessee	(822)	(1,093)	(361)	(700)	(606)	(666)	-	-	-	-
Change in net assets	\$ 4,016	\$ 2,095	\$ 3,076	\$ 1,658	\$ 1,110	\$ 1,241	\$ 2,241	\$ 1,892	\$ 1,772	\$ 1,609

Note 1: Cable and internet services commenced in 2006.

Note 2: Telephone services commenced in 2007.

Bristol Tennessee Essential Services

Purchased Power, Consumption and Active Service Statistics (Last Ten Years)

Fiscal Years 2007-1998

	2007	2006	2005	2004	2003	2002	2001	2000	1999	1998
Purchased power from Tennessee										
Valley Authority (megawatt hours)	1,047,479	1,039,435	1,003,918	1,014,411	997,525	935,485	961,853	918,151	919,696	913,322
Consumption (megawatt hours):										
Residential	479,605	472,002	454,880	468,611	469,302	432,282	456,277	425,639	416,726	419,346
Commercial	55,411	55,620	53,642	53,344	54,335	49,880	52,200	51,351	51,337	50,391
Industrial	457,434	456,250	451,031	437,853	412,832	398,728	396,534	388,268	399,571	393,905
Street and athletic	5,719	5,638	6,455	5,164	5,255	5,209	5,086	4,973	4,936	4,908
Outdoor lighting	3,625	4,150	4,105	4,139	4,211	4,221	4,297	4,359	4,346	4,340
Internal use	-	-	-	-	-	-	-	-	843	901
Total consumption	1,001,794	993,660	970,113	969,111	945,935	890,320	914,394	874,590	877,759	873,791
Line losses and megawatt hours										
accounted for	45,685	45,775	33,805	45,300	51,590	45,165	47,459	43,561	41,937	39,531
Percentage of line losses and megawatt										
hours unaccounted for to purchased										
power	4.36%	4.40%	3.37%	4.47%	5.17%	4.83%	4.93%	4.74%	4.56%	4.33%
Active service (number of power customers):										
Residential	28,166	28,070	27,760	27,650	27,458	27,360	27,234	26,951	26,603	26,315
Commercial	3500	3,500	3,425	3,332	3,291	3,304	3,229	3,241	3,144	3,130
Industrial	636	622	609	614	591	588	584	551	543	536
Street and athletic	40	40	41	41	41	38	38	38	29	28
Outdoor lighting	161	159	160	161	160	158	161	161	155	157
	32,503	32,391	31,995	31,798	31,541	31,448	31,246	30,942	30,474	30,166

Note: Information is compiled from internally generated statistical reports.

Bristol Tennessee Essential Services

Schedule of Bonds Payable by Type

December 31, 2007 and 2006

	December 31	
	2007	2006
Revenue bonds (in thousands)	\$ 24,333	\$ 24,347
Number of customers	32,503	32,391
Outstanding debt per customer	\$ 749	\$ 752

Note: No outstanding debt existed prior to fiscal year 2006.

Bristol Tennessee Essential Services

Schedule of Power System Revenue Bond Coverage

Fiscal Year 2007 and 2006 (in thousands)

	Power Operating Revenues	Power Operating Expenses	Net Revenue for Debt Service	Debt Service Requirements			
				Principal	Interest	Total	Coverage
2007	69,850	64,934	4,916	-	1,055	1,055	4.66
2006	66,376	62,283	4,093	-	627	627	6.53

Note 1: Power operating expenses do not include depreciation.

Note 2: No outstanding debt existed prior to fiscal year 2006.

Bristol Tennessee Essential Services

Schedule of Property, Casualty and Other Insurance (Unaudited)

June 30, 2007

Type of Coverage	Limits	Deductible	Period of Coverage	Company
Theft, disappearance and destruction	\$ 250,000	\$ -	12/04/05 to 12/04/08	Cincinnati Ins. Co.
Workers' compensation	500,000	-	12/04/06 to 12/04/07	Cincinnati Ins. Co.
General liability:		0 to 1,000	12/04/05 to 12/04/08	Cincinnati Ins. Co.
Products-completed operations aggregate	2,000,000			
Personal and advertising injury	1,000,000			
Each occurrence	1,000,000			
Fire damage (any one fire)	100,000			
Medical expense (any one person)	10,000			
Employee benefits:				
Each claim	1,000,000			
Aggregate	3,000,000			
Automobile policy:		100 to 1,000	12/04/06 to 12/04/07	Cincinnati Ins. Co.
Liability	1,000,000			
Comprehensive	Actual Cash Value			
Uninsured motorist	1,000,000			
Collision	Actual Cash Value			
Medical payments	5,000 per person			
Commercial umbrella liability	20,000,000	-	12/04/05 to 12/04/08	Cincinnati Ins. Co.
Fire, extended coverage & vandalism and malicious mischief:		10,000	12/04/05 to 12/04/08	Cincinnati Ins. Co.
On premise property	23,281,918			
Off premise property	250,000			

Bristol Tennessee Essential Services

Schedule of Property, Casualty and Other Insurance (Unaudited) (continued)

June 30, 2007

Type of Coverage	Limits	Deductible	Period of Coverage	Company
Scheduled property floater:				
Flood	\$ 2,000,000	\$ 25,000	12/05/05 to	Cincinnati Ins. Co.
Earthquake	10,000,000	500,000	12/04/08	
Directors & officers liability	10,000,000	0 to 10,000	04/28/07 to 04/28/08	Cincinnati Ins. Co.
Boiler & machinery policy	500,000	5,000 to 50,000	12/04/06 to 12/04/09	Cincinnati Ins. Co.
Employee dishonesty	500,000	1,000	12/04/05 to 12/04/08	Cincinnati Ins. Co.
Electronic data processing equipment and media	4,118,134	1,000	12/04/05 to 12/04/08	Cincinnati Ins. Co.
Mobile property - machinery	1,027,228	250	12/04/05 to 12/04/08	Cincinnati Ins. Co.
Employment related practices liability:		2,500	12/04/05 to 12/04/08	Cincinnati Ins. Co.
Each insured event limit	1,000,000			
Total limit	1,000,000			

Note 1: Information is compiled from internal records.

Bristol Tennessee Essential Services

Schedule of Electric Rates (Last Ten Years) (Unaudited)

Fiscal Years 2007 - 1998

	2007	2006	2005	2004	2003	2002	2001	2000	1999	1998
Residential										
Monthly customer charge	\$ 6.29	\$ 6.29	\$ 6.29	\$ 6.29	\$ 5.52	\$ 5.52	\$ 5.52	\$ 5.52	\$ 5.52	\$ 5.52
Energy charge:										
First 1,000 kWh per month	0.06157	0.06352	0.05374	0.05374	0.05018	0.05018	0.05018	0.05018	0.05018	0.05018
Additional kWh per month	0.06701	0.06896	0.05918	0.05918	0.05615	0.05615	0.05615	0.05615	0.05615	0.05615
Commercial, Industrial, Governmental and Institutional										
Plan A-1 (demand up to 50 kW and usage up to 15,000 kWh):										
Customer charge per month	14.00	14.00	14.00	14.00	10.00	10.00	10.00	10.00	10.00	10.00
Energy charge	0.07112	0.07346	0.06240	0.06240	0.05820	0.05820	0.05820	0.05820	0.05820	0.05820
Plan A-2 (demand of 50 kW to 1,000 kW or demand less than 50 kW but usage in excess of 15,000 kWh):										
Customer charge per month	25.00	25.00	25.00	25.00	10.00	10.00	10.00	10.00	10.00	10.00
Demand charge:										
First 50 kW	-	-	-	-	-	-	-	-	-	-
Excess of 50 kW	9.63	10.06	8.56	8.56	7.86	7.86	7.86	7.86	7.86	7.86
Energy charge:										
First 15,000 kWh per month	0.07066	0.07300	0.06194	0.06194	0.05774	0.05774	0.05774	0.05774	0.05774	0.05774
Additional kWh per month	0.03947	0.04042	0.03420	0.03420	0.03184	0.03184	0.03184	0.03184	0.03184	0.03184
Plan A-3 (demand of 1,001 kW to 5,000 kW):										
Customer charge per month	25.00	25.00	25.00	25.00	10.00	10.00	10.00	10.00	10.00	10.00
Demand charge:										
First 1,000 kW	9.67	10.14	8.56	8.56	7.89	7.89	7.89	7.89	7.89	7.89
Excess of 1,000 kW	11.39	11.94	10.06	10.06	9.09	9.09	9.09	9.09	9.09	9.09
Energy charge	0.03947	0.04042	0.03420	0.03420	0.03184	0.03184	0.03184	0.03184	0.03184	0.03184

Bristol Tennessee Essential Services

Schedule of Electric Rates (Last Ten Years) (Unaudited) (continued)

Fiscal Years 2007 - 1998

	2007	2006	2005	2004	2003	2002	2001	2000	1999	1998
Commercial, Industrial, Governmental and Institutional (continued)										
Plan B (demand of 5,001 kW to 15,000 kW)										
Customer charge per month	1,500.00	1,500.00	1,500.00	1,500.00	1,500.00	1,500.00	1,500.00	1,500.00	1,500.00	1,500.00
Demand charge	12.33	12.89	10.96	10.96	10.23	10.23	10.23	10.23	10.23	10.23
Energy charge:										
First 620 kWh per month	0.03514	0.03588	0.03050	0.03050	0.02825	0.02825	0.02825	0.02825	0.02825	0.02825
Additional kWh per month	0.02883	0.02928	0.02477	0.02477	0.02306	0.02306	0.02306	0.02306	0.02306	0.02306
Plan C (demand of 15,001 kW to 25,000 kW)										
Customer charge per month	1,500.00	1,500.00	1,500.00	1,500.00	1,500.00	1,500.00	1,500.00	1,500.00	1,500.00	1,500.00
Demand charge	12.44	13.00	11.07	11.07	10.34	10.34	10.34	10.34	10.34	10.34
Energy charge:										
First 620 kWh per month	0.03514	0.03588	0.03035	0.03035	0.02825	0.02825	0.02825	0.02825	0.02825	0.02825
Additional kWh per month	0.02883	0.02928	0.02477	0.02477	0.02306	0.02306	0.02306	0.02306	0.02306	0.02306
Plan D (demand in excess of 25,000 kW)										
Customer charge per month		-	-	-	1,500.00	1,500.00	1,500.00	1,500.00	1,500.00	1,500.00
Demand charge		-	-	-	12.60	12.60	12.60	12.60	12.60	12.60
Energy charge		-	-	-	0.02265	0.02265	0.02265	0.02265	0.02265	0.02265

Note1: Summarized from internal records.

Bristol Tennessee Essential Services

Schedule of Telephone, Cable and Internet Rates (Unaudited)

June 30, 2007 and 2006

Telephone	2007	2006
Basic Telephone Service	\$ 22.90	\$ -
<i>Includes: Caller ID w/ Name and Number, Call Waiting/Cancel Call Waiting, Unconditional Call Forwarding, Remote Access to Call Forwarding, Three-Way Calling, Speed Calling (One Digit), Caller ID for Call Waiting</i>		
Enhanced Telephone Service	28.90	-
<i>Includes: Above list of features plus Voicemail, *67 Caller ID Blocking,</i>		
100 Minutes Long Distance	6.95	-
200 Minutes Long Distance	12.95	-
500 Minutes Long Distance	24.95	-
Unlimited Minutes Long Distance	29.95	-
Cable Television		
Expanded Basic	39.95	39.95
Digital:		
Basic	49.95	49.95
Bronze	59.95	59.95
Silver	67.95	67.95
Gold	72.95	72.95
Spanish Tier	4.95	-
High Definition Tier	9.95	6.95
Sports Tier	4.00	4.00
Pay-Per-View Movies:		
New release	3.95	3.95
Library	2.95	2.95
Premium Packages:		
Cinemax	9.95	9.95
HBO	11.95	11.95
Showtime	11.95	11.95
STARZ	9.95	9.95
Internet		
64K Tier	16.95	16.95
1.5 Mbps Tier (1 Mbps in 2006)	29.95	29.95
3 Mbps Tier (2 Mbps in 2006)	39.95	39.95
5 Mbps Tier (4 Mbps in 2006)	49.95	49.95

Note 1: Summarized from internal records.

Note 2: Cable and Internet services commenced in 2006.

Note 3: Telephone service commenced in 2007.

Bristol Tennessee Essential Services

Schedule of Principal Customers Ranked by Kwh Usage (Unaudited)

Current Year and Nine Years Ago

Name	2007 Rank	1998 Rank
Exide Corporation	1	1
Modern Forge of Tennessee	2	4
Wellmonth BRMC	3	3
City of Bristol, Tennessee	4	5
GlaxoSmithKline Laboratories	5	6
Royal Mouldings	6	—
King Pharmaceuticals	7	—
Amerace Corporation	8	8
Bristol Metals, Inc.	9	7
HSN Fulfillment LLC	10	—
Raytheon Company	—	2
Fingerhut	—	9
Sprint	—	10

Note 1: Summarized from internal records.

Bristol Tennessee Essential Services

Schedule of Employees (Last Ten Years) (Unaudited)

Fiscal Years 2007 - 1998

Fiscal Year	Full Time	Part Time	Total
2007	60	7	67
2006	60	5	65
2005	60	5	65
2004	60	8	68
2003	60	9	69
2002	60	5	65
2001	60	6	66
2000	60	6	66
1999	62	6	68
1998	62	6	68

Note 1: Summarized from internal records.

BRISTOL TENNESSEE ESSENTIAL SERVICES**STATISTICS - JUNE 2007**

2470 Volunteer Parkway, Bristol, TN 37620

P. O. Box 549, Bristol, TN 37621

Telephone: 423-968-1526

FAX Number: 423-793-5545

Power Outage Number: 423-968-BTES (968-2837)

Miles of Line 1,251

NUMBER OF CUSTOMERS

Large General Power (>50 kW)..... 636

Small General Power (<50 kW)..... 3,500

Residential28,166

Street and Outdoor Lighting201

Total32,503**Employees/1000 Customers1.91****NUMBER OF FIBER OPTIC CUSTOMERS**

Residential Cable Television Customers3,483

Commercial Cable Television Customers119

Residential Internet Customers2,476

Commercial Internet Customers89

Residential Telephone Customers.....1,697

Commercial Telephone Customers56

Total Services7,920**Total Homes and Businesses Served4,013**

**BRISTOL TENNESSEE ESSENTIAL SERVICES
CLIMATOLOGICAL DATA
FISCAL YEARS 2007-1998**

Fiscal Year	Heating Degree Days *	Cooling Degree Days *
2007	4140	1120
2006	4038	1163
2005	4222	1068
2004	4141	1027
2003	4064	1132
2002	3921	1189
2001	4539	933
2000	4019	1082
1999	4312	951
1998	4142	904

SOURCE: U.S. Department of Commerce, National Oceanic and Atmospheric Administration

* Degree Day is a unit measuring the extent to which the average of the daily high and daily low temperature varies from a standard reference temperature. Based on a reference temperature of 65 degrees Fahrenheit, if the average of the daily high and daily low temperature (high plus low divided by 2) for a day is 70, then there are five cooling degree days for that day. Likewise, if the average of the daily high and daily low temperature was 60, then there were five heating degree days. This historical information can be used for forecasting system load and planning unit maintenance outages, to name a few.

**BRISTOL TENNESSEE ESSENTIAL SERVICES
DEMOGRAPHIC AND ECONOMIC STATISTICS
TRI-CITIES, TENNESSEE-VIRGINIA MSA
CALENDAR YEARS 2006-1997**

Calendar Year	Population	Per Capita Income	Median Age	Unemployment Rate
2006	493,796	\$26,671	40.7	4.3%
2005	490,238	\$27,163	42.0	4.6%
2004	479,830	\$25,299	39.6	4.8%
2003	485,884	\$23,878	39.2	5.9%
2002	485,300	\$22,302	40.2	5.3%
2001	484,900	\$22,302	39.7	5.0%
2000	480,091	\$22,119	39.7	4.5%
1999	465,700	\$21,201	39.4	4.4%
1998	464,900	\$19,896	39.1	4.4%
1997	459,963	\$19,503	37.6	4.1%

Information obtained from First Tennessee Development District.

Information for 2007 is not available.



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

Board of Directors
Bristol Tennessee Essential Services

We have audited the financial statements of the Bristol Tennessee Essential Services ("BTES"), an enterprise fund of the City of Bristol, Tennessee, as of and for the year ended June 30, 2007, and have issued our report thereon dated November 7, 2007. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States of America.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered BTES' internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of BTES' internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of BTES' internal control over financial reporting.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects BTES' ability to initiate, authorize, record, process, or report financial data reliably in accordance with accounting principles generally accepted in the United States of America ("GAAP") such that there is more than a remote likelihood that a misstatement of BTES' financial statements that is more than inconsequential will not be prevented or detected by BTES' internal control.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by BTES' internal control.

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as described above.



Board of Directors
Bristol Tennessee Essential Services

Compliance and Other Matters

As part of obtaining reasonable assurance about whether BTES' financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations and contracts, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

This report is intended solely for the information and use of the Board of Directors, management and the State of Tennessee Comptroller of the Treasury and is not intended to be and should not be used by anyone other than these specified parties.

Coulter & Justus, P. C.

November 7, 2007