Lancaster Port Authority
Fairfield County, Ohio

Basic Financial Statements

December 31, 2011

(with Independent Auditors' Report)

CLARK SCHAEFER HACKETT
STRENGTH IN NUMBERS

Dave Yost • Auditor of State

Board of Directors
Lancaster Port Authority
104 East Main Street
Lancaster, Ohio 43130

We have reviewed the *Independent Auditors' Report* of the Lancaster Port Authority, Fairfield County, prepared by Clark, Schaefer, Hackett & Co., for the audit period January 1, 2011 through December 31, 2011. Based upon this review, we have accepted these reports in lieu of the audit required by Section 117.11, Revised Code. The Auditor of State did not audit the accompanying financial statements and, accordingly, we are unable to express, and do not express an opinion on them.

Our review was made in reference to the applicable sections of legislative criteria, as reflected by the Ohio Constitution, and the Revised Code, policies, procedures and guidelines of the Auditor of State, regulations and grant requirements. The Lancaster Port Authority is responsible for compliance with these laws and regulations.

Dave Yost

Dave Yost
Auditor of State

June 14, 2012

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INDEPENDENT AUDITORS' REPORT

Board of Directors
Lancaster Port Authority
104 East Main Street
Lancaster, Ohio 43130-3726

We have audited the statement of net assets of the Lancaster Port Authority (the Authority), a component unit of the City of Lancaster, Ohio, as of December 31, 2011 and the related statements of revenues, expenses and changes in net assets and cash flows for the year then ended. These financial statements are the responsibility of the Authority's management. Our responsibility is to express an opinion on these financial statements based on our audit.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Authority as of December 31, 2011, and the changes in its financial position and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated April 27, 2012, on our consideration of the Authority's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on 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.

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Accounting principles generally accepted in the United States of America require that the management's discussion and analysis information on pages 3 through 6 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Clark, Schaefer, Hackett & Co.

Springfield, Ohio
April 27, 2012

The discussion and analysis of the Lancaster Port Authority's (the "Port Authority") financial performance provides an overall review of the Port Authority's financial activities for the year ended December 31, 2011. The intent of this discussion and analysis is to look at the Port Authority's financial performance as a whole; readers should also review the financial statements and notes to the basic financial statements to enhance their understanding of the Port Authority's financial performance.

FINANCIAL HIGHLIGHTS

Key financial highlights for 2011 are as follows:

- Assets increased from $631,511,197 to $647,528,054 due to an increase in the value of the derivative instruments which was only partially offset by prepaid gas deliveries received from Royal Canadian Bank.

- Long-term debt decreased due to scheduled debt service payments made on the Series 2008 Revenue Bonds.

- Other liabilities increased due to the increase in the deferred inflow related to the derivative instruments.

OVERVIEW OF THE FINANCIAL STATEMENTS

This annual report consists of two parts – management's discussion and analysis and the basic financial statements. These statements are organized so the reader can understand the financial position of the Port Authority. Enterprise accounting uses a flow of economic resources measurement focus. With this measurement focus, all assets and all liabilities are included on the statement of net assets. The statement of net assets represents the basic statement of position for the Port Authority. The statement of revenues, expenses, and changes in net assets presents increases (e.g., revenues) and decreases (e.g., expenses) in net total assets. The statement of cash flows reflects how the Port Authority finances and meets its cash flow needs. Finally, the notes to the basic financial statements provide additional information that is essential to a full understanding of the data provided on the basic financial statements.

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Management's Discussion and Analysis
For the Year Ended December 31, 2011 ***Unaudited***

FINANCIAL ANALYSIS OF THE PORT AUTHORITY

The following tables represent the Port Authority's condensed financial information for 2011 and 2010 derived from the statement of net assets and the statement of revenues, expenses, and changes in net assets.

	2011	2010
Current assets	$16,255,587	$16,901,796
Other Assets	630,382,085	613,878,200
Capital assets, Net	890,382	731,201
Total assets	647,528,054	631,511,197
Current liabilities	129,491	95,808
Other Liabilities	364,570,432	332,766,486
Long-term debt outstanding	334,664,136	337,783,060
Total liabilities	699,364,059	670,645,354
Net Assets:		
Invested in capital assets, net of related debt	886,246	678,141
Unrestricted	(52,722,251)	(39,812,298)
Total net assets	($51,836,005)	($39,134,157)

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Changes in Net Assets – The following table shows the changes in net assets for 2011 compared to 2010:

	2011	2010
Revenues		
Gas Supply	$8,624,592	$9,334,154
Other Operating Revenue	1,600	9,706
Total revenues	8,626,192	9,343,860
Expenses		
Supplies and Materials - Cost of Gas Sold	6,221,474	7,570,044
Contractual Services	1,996,076	2,260,364
Depreciation	13,350	10,124
Total expenses	8,230,900	9,840,532
Operating Income (Loss)	395,292	(496,672)
Nonoperating Revenues/(Expenses)		
Investment Earnings	2,230	3,421
Interest and Fiscal Charges	(13,138,370)	(13,348,357)
Other Nonoperating Revenue	0	7,063
Other Nonoperating Expense	(21,000)	0
Capital Contributions	60,000	0
Total Change in Net Assets	(12,701,848)	(13,834,545)
Beginning Net Assets	(39,134,157)	(25,299,612)
Ending Net Assets	($51,836,005)	($39,134,157)

Net assets decreased by $12,701,848. This decrease was primarily the result of recognizing the consumption of the current year portion of the prepaid gas contract.

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets

At the end of 2011 the Port Authority had $890,382 net of accumulated depreciation invested in capital assets. The following table shows 2011 and 2010 balances:

	2011	2010	Increase (Decrease)
Land	$106,200	$106,200	$0
Buildings and Improvements	208,950	95,745	113,205
Infrastructure	614,326	555,000	59,326
Less: Accumulated Depreciation	(39,094)	(25,744)	(13,350)
Totals	$890,382	$731,201	$159,181

Capital assets increased as a result of building a trans-load facility. Additional information on the Port Authority's capital assets can be found in Note 5.

Debt

The following table summarizes the Port Authority's debt outstanding as of December 31, 2011 and 2010:

	2011	2010
Revenue Bonds Payable	$334,660,000	$337,730,000
ORDC Loan	4,136	53,060
Totals	$334,664,136	$337,783,060

Additional information on the Port Authority's long-term debt can be found in Note 6.

ECONOMIC FACTORS

- The Baldwin Run Trans-load Facility was operational in 2011.
- In partnering with the City of Lancaster, a $1.5 million Clean Ohio Revitalization Fund Grant and a $200,000 Federal EPA Fund Grant is being used to environmentally remediate a five (5) acre industrially zoned parcel formerly known as the Ray-O-Vac factory. The Port Authority is creating a small Industrial Park and will sell lots when the area is environmentally sound.

REQUESTS FOR INFORMATION

This financial report is designed to provide our citizens, investors and creditors with a general overview of the Port Authority's finances and to show the Port Authority's accountability for the money it receives. If you have questions about this report or need additional financial information contact R. Michael Pettit, Director of the Lancaster Port Authority.

Statement of Net Assets
December 31, 2011

ASSETS	
Current assets:	
Cash and Cash Equivalents	$527,663
Accounts Receivable	551,819
Prepaid Gas Supply - Current	15,176,105
Total Current Assets	16,255,587
Noncurrent Assets:	
Prepaid Gas Supply - Long Term	255,818,743
Deferred Bond Issuance costs	2,768,557
Fair Value of Derivative Instruments	221,300,167
Deferred Outflow from Derivative Instruments	143,270,265
Restricted Assets:	
Cash and cash equivalents	7,224,353
Capital Assets	
Capital Assets Not Being Depreciated	106,200
Capital Assets Being Depreciated, net	784,182
Total Capital Assets	890,382
Total Noncurrent Assets	631,272,467
Total Assets	647,528,054
LIABILITIES	
Current Liabilities:	
Unearned Revenue	98,400
Accrued Interest	31,091
ORDC Loan Payable-current	4,136
Bond Payable-current	3,200,000
Total Current Liabilities	3,333,627
Noncurrent Liabilities:	
Bond Payable-long term	331,460,000
Fair Value of Derivative Instruments	143,270,265
Deferred Inflow from Derivative Instruments	221,300,167
Total Noncurrent Liabilities	696,030,432
Total Liabilities	699,364,059
Net Assets:	
Invested in Capital Assets, net of related debt	886,246
Unrestricted	(52,722,251)
Total Net Assets	($51,836,005)

See accompanying notes to the basic financial statements

Statement of Revenues, Expenses and Changes in Net Assets
For the Year Ended December 31, 2011

Operating Revenues:	
Gas Supply	$8,624,592
Other Operating Revenue	1,600
Total Operating Revenues	8,626,192
Operating Expenses:	
Materials and Supplies - cost of gas sold	6,221,474
Contractual services	1,996,076
Depreciation	13,350
Total Operating Expenses	8,230,900
Operating Income	395,292
Nonoperating Revenues (Expenses):	
Investment Earnings	2,230
Interest and Fiscal Charges	(13,138,370)
Other Nonoperating Expense	(21,000)
Total Nonoperating Revenues (Expenses)	(13,157,140)
Loss Before Contributions	(12,761,848)
Capital Contributions	60,000
Change in Net Assets	(12,701,848)
Net Assets at Beginning of Year	(39,134,157)
Net Assets at End of Year	($51,836,005)

See accompanying notes to the basic financial statements

Statement of Cash Flows
For the Year Ended December 31, 2011

Cash Flows from Operating Activities:	
Cash Received from Customers	$8,881,810
Cash Received from Swap Providers	9,625,447
Cash Payments for Goods and Services	(2,017,076)
Net Cash Provided by Operating Activities	16,490,181
Cash Flows from Noncapital Financing Activities:	
Principal Payment on Revenue Bond Payable	(3,070,000)
Interest Paid on Debt	(13,097,794)
Net Cash Used by Noncapital Financing Activities	(16,167,794)
Cash Flows from Capital and Related Financing Activities:	
Acquistion and Construction of Capital Assets	(172,531)
Intergovernmental Grant	60,000
Principal Payment on ORDC Loan	(48,924)
Interest Paid on Debt	(819)
Net Cash Used by Capital and Related Financing Activities	(162,274)
Cash Flows from Investing Activities:	
Receipts of Interest Earnings	2,230
Net Cash Provided by Investing Activities	2,230
Net Increase in Cash and Cash Equivalents	162,343
Cash and Cash Equivalents at Beginning of Year	7,589,673
Cash and Cash Equivalents at End of Year	$7,752,016
Reconciliation of Operating Income to Net Cash Provided by Operating Activities:	
Operating Income	$395,292
Adjustments to Reconcile Operating Income to Net Cash Provided by Operating Activities:	
Miscellaneous Nonoperating Expense	(21,000)
Depreciation Expense	13,350
Changes in Assets and Liabilities:	
Decrease in Accounts Receivable	157,218
Decrease in Prepaid Items	15,846,921
Increase in Unearned Revenue	98,400
Total Adjustments	16,094,889
Net Cash Provided by Operating Activities	$16,490,181

See accompanying notes to the basic financial statements

Notes to the Basic Financial Statements
For the Year Ended December 31, 2011

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Lancaster Port Authority (the "Port Authority") was created on December 12, 2005 under the authority of Section 4582.21 et seq. of the Ohio Revised Code which provides that "a municipal corporation, a county or any combination thereof acting jointly, may create a port authority which shall be a body corporate and politic and have territorial limits coterminous with the territorial limits of the political subdivision(s) creating such port authority."

The Port Authority operates under the direction of a five-member Board of Directors appointed by the Mayor of the City of Lancaster (the "City"). The Directors must be qualified electors of, or have their businesses or places of employment in the City. The Port Authority is considered a blended component unit of the City for reporting purposes, in accordance with Governmental Accounting Standards Board (GASB) Statement No. 14 as amended by GASB Statement No. 39. The Port Authority was created for the purpose of enhancing, fostering, providing or promoting transportation, economic development, housing, recreation, education, government operations, and culture and research in the City.

The financial statements are presented as of December 31, 2011 and for the year then ended and have been prepared in conformity with generally accepted accounting principles (GAAP) applicable to local governments. The Governmental Accounting Standards Board (the "GASB") is the standard-setting body for establishing governmental accounting and financial reporting principles, which are primarily set forth in the GASB's Codification of Governmental Accounting and Financial Reporting Standards (GASB Codification).

A. Reporting Entity

The accompanying basic financial statements comply with the provisions of the GASB Statement No. 14, *"The Financial Reporting Entity,"* and GASB Statement No. 39, *"Determining Whether Certain Organizations are Component Units"* in that the financial statements include all organizations, activities, functions and component units for which the Port Authority (the primary government) is financially accountable. The Port Authority is financially accountable for an organization if it has (1) the ability to appoint a voting majority of another entity's governing body and to impose its will on that entity, (2) the potential for that entity to provide specific financial benefits to or impose specific financial burdens on others, and (3) the entity's fiscal dependency on others.

Based on the foregoing, the Port Authority's financial reporting entity has no component units.

B. Basis of Presentation

The Port Authority operates as a self-supporting governmental enterprise and uses accounting policies applicable to governmental enterprise funds. All transactions are accounted for in a single enterprise fund.

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

C. Measurement Focus

The enterprise fund is accounted for on a flow of economic resources measurement focus. All assets and all liabilities associated with the operation of the Port Authority are included on the statement of net assets. The statement of changes in net assets presents increases (i.e., revenues) and decreases (i.e., expenses) in net total assets. The statement of cash flows provides information about how the Port Authority finances and meets the cash flow needs of its enterprise activity.

D. Basis of Accounting

The Port Authority uses the accrual basis of accounting. Revenues are recognized when earned and expenses are recognized when incurred.

E. Cash and Cash Equivalents

Cash and cash equivalents include amounts in demand deposits and money market funds. The Port Authority considers all highly liquid investments with original maturities of three months or less at the time of purchase to be cash equivalents.

F. Prepaid Gas Supply

The Port Authority prepaid for deliveries of natural gas supplies with the proceeds from revenue bonds. Prepaid gas supplies are stated at the present value of the remaining fixed delivery amounts, as determined by the prepay contract.

G. Derivative Instruments

The Port Authority's derivative financial instruments are accounted for in accordance with GASB Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments.* In connection with this Statement, the fair value of the Port Authority's derivative financial instruments is recorded on the Statement of Net Assets, with an offsetting deferred outflow or inflow.

Derivative instruments are utilized by the Port Authority to manage market risk and reduce its exposure resulting from fluctuations in prices of natural gas in order to meet debt service requirements. These instruments include commodity swap agreements which convert index-priced natural gas revenues to fixed prices for servicing outstanding debt obligations and interest rate swap agreements which effectively convert the Port Authority's variable interest rate to a fixed rate. Interest expense in each operating period includes the netting adjustments of the interest rate swap agreements.

Notes to the Basic Financial Statements
For the Year Ended December 31, 2011

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

H. Capital Assets and Depreciation

Capital Assets are defined by the Port Authority as assets with an initial, individual cost of more than $1,000.

Property, plant and equipment acquired is stated at cost (or estimated historical cost), including architectural and engineering fees where applicable. Donated capital assets are recorded at fair market value at the date received.

Depreciation has been provided using the straight-line method over the following estimated useful lives:

Description	Estimated Lives (in years)
Buildings	40
Improvements	20
Infrastructure	75

I. Bond Issuance Costs

Bond issuance costs are deferred and amortized over the term of the bonds on a straight line basis. Issuance costs are recorded as deferred charges.

J. Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results may differ from those estimates.

K. Net Assets

Net assets represent the difference between assets and liabilities. Net assets invested in capital assets, net of related debt, consists of capital assets, net of accumulated depreciation, reduced by the outstanding balances of any borrowings used for the acquisition, construction or improvement of those assets.

L. Operating Revenues and Expenses

Enterprise funds distinguish operating revenues and expenses from nonoperating items. Operating revenues are those revenues that are generated directly from the primary activity of the proprietary funds. For the Port Authority, these revenues are charges for services for sale of natural gas. Operating expenses are necessary costs incurred to provide the good or service that are the primary activity of the fund. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

NOTE 2 – CHANGE IN ACCOUNTING PRINCIPLES

For 2011, the Port Authority implemented GASB Statement No. 62 and GASB Statement No. 64. GASB No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*, establishes one codification for all of governmental GAAP. GASB No. 64, *Derivative Instruments: Application of Hedge Accounting Termination Provisions*, clarifies whether an effective hedging relationship continues after the replacement of a swap counterparty or a swap counterparty's credit support provider. The statement sets forth criteria that establish when the effective hedging relationship continues and hedge accounting should continue to be applied. The implementation of these statements did not result in any change in the Port Authority's financial statements.

NOTE 3 – DEFICIT NET ASSETS

The accumulated deficit at December 31, 2011 of $51,836,005, is the result of recording the prepaid gas supply at the present value of the future shipments and the related bonds payable at outstanding par value. At the end of the contract period, the net result will be zero.

NOTE 4 - CASH, CASH EQUIVALENTS AND INVESTMENTS

Cash resources of the Port Authority are combined to form a pool of cash and investments. The Port Authority has adopted an Investment Policy that follows Ohio Revised Code Chapter 135 and applies the prudent person standard. The prudent person standard requires the Auditor and Treasurer to exercise the care, skill and experience that a prudent person would use to manage his/her personal financial affairs and to seek investments that will preserve principal while maximizing income. Statutes require the classification of funds held by the Port Authority into three categories.

Category 1 consists of "active" funds - those funds required to be kept in "cash" or "near cash" status for immediate use by the Port Authority. Such funds must be maintained either as cash in the Treasury or in depository accounts payable or withdrawable on demand, including negotiable order of withdrawal (NOW) accounts.

Category 2 consists of "inactive" funds - those funds not required for use within the current five year period of designation of depositories. Inactive funds may be deposited or invested only as certificates of deposit maturing no later than the end of the current period of designation of depositories.

NOTE 4 - POOLED CASH, CASH EQUIVALENTS AND INVESTMENTS (Continued)

Category 3 consists of "interim" funds - those funds which are not needed for immediate use, but which will be needed before the end of the current period of designation of depositories. Interim funds may be invested or deposited in the following securities:

- United States treasury notes, bills, bonds, or any other obligation or security issued by the United States treasury or any other obligation guaranteed as to principal or interest by the United States;
- Bonds, notes, debentures, or any other obligations or securities issued by any federal government agency or instrumentality, including but not limited to, the federal national mortgage association, federal home loan bank, federal farm credit bank, federal home loan mortgage corporation, government national mortgage association, and student loan marketing association. All federal agency securities shall be direct issuances of federal government agencies or instrumentalities;
- Written repurchase agreements in the securities listed above provided that the market value of the securities subject to the repurchase agreement must exceed the principal value of the agreement by at least two percent and be marked to market daily, and that the term of the agreement must not exceed thirty days;
- Interim deposits in eligible institutions applying for interim funds;
- Bonds and other obligations of the State of Ohio;
- No-load money market mutual funds consisting exclusively of obligations described in the first two bullets of this section and repurchase agreements secured by such obligations, provided that investments in securities described in this division are made only through eligible institutions, and
- The State Treasury Asset Reserve of Ohio (STAR Ohio).

Deposits

Custodial credit risk is the risk that in the event of bank failure, the government's deposits may not be returned. Protection of Port Authority cash and deposits is provided by the federal deposit insurance corporation as well as qualified securities pledged by the institution holding the assets. Ohio Law requires that deposits be placed in eligible banks or savings and loan associations located in Ohio. Any public depository in which the Port Authority places deposits must pledge as collateral eligible securities of aggregate market value equal to the excess of deposits not insured by the Federal Deposit Insurance Corporation (FDIC). The securities pledged as collateral are pledged to a pool for each individual financial institution in amounts equal to at least 105% of the carrying value of all public deposits held by each institution. Obligations that may be pledged as collateral are limited to obligations of the United States and its agencies and obligations of any state, county, municipal corporation or other legally constituted authority of any other state, or any instrumentality of such county, municipal corporation or other authority. Collateral is held by trustees including the Federal Reserve Bank and designated third party trustees of the financial institutions.

Notes to the Basic Financial Statements
For the Year Ended December 31, 2011

NOTE 4 - POOLED CASH, CASH EQUIVALENTS AND INVESTMENTS (Continued)

At year end the carrying amount of the Port Authority's deposits was $7,752,016 and the bank balance was $7,752,016. Federal depository insurance covered $250,000 of the bank balance, and $7,502,016 was uninsured. Of the remaining uninsured bank balance, the Port Authority was exposed to custodial risk as follows:

	Balance
Uninsured and collateralized with securities held by the pledging institution's trust department not in the Port Authority's name	$7,502,016

NOTE 5 - CAPITAL ASSETS

Summary by Category at December 31, 2011:

Historical Cost:

Class	December 31, 2010	Additions	Deletions	December 31, 2011
Capital assets not being depreciated:				
Land	$106,200	$0	$0	$106,200
Subtotal	106,200	0	0	106,200
Capital assets being depreciated:				
Buildings	95,745	0	0	95,745
Improvements	0	113,205	0	113,205
Infrastructure	555,000	59,326	0	614,326
Subtotal	650,745	172,531	0	823,276
Total Cost	$756,945	$172,531	$0	$929,476

Accumulated Depreciation:

Class	December 31, 2010	Additions	Deletions	December 31, 2011
Buildings	($7,244)	($2,724)	$0	($9,968)
Improvements	0	(2,830)	0	(2,830)
Infrastructure	(18,500)	(7,796)	0	(26,296)
Total Depreciation	($25,744)	($13,350)	$0	($39,094)
Net Value:	$731,201			$890,382

Notes to the Basic Financial Statements
For the Year Ended December 31, 2011

NOTE 6 - LONG-TERM DEBT

Long-term debt obligations of the Port Authority at December 31, 2011 were as follows:

		Balance December 31, 2010	Deletions	Balance December 31, 2011	Amount Due Within One Year
Long-Term Debt					
Variable Rate Revenue Bonds	2008	$337,730,000	($3,070,000)	$334,660,000	$3,200,000
Variable Rate Ohio Rail Development Loan	2008	53,060	(48,924)	4,136	4,136
Total Long-Term Debt		$337,783,060	($3,118,924)	$334,664,136	$3,204,136

	Revenue Bonds Payable		ORDC Loan Payable	
Years	Principal	Interest	Principal	Interest
2012	$3,200,000	$12,334,012	$4,136	$9
2013	3,560,000	12,210,987	0	0
2014	4,045,000	12,071,928	0	0
2015	4,590,000	11,914,185	0	0
2016	5,175,000	11,735,198	0	0
2017-2021	33,925,000	55,295,513	0	0
2022-2026	52,420,000	47,473,251	0	0
2027-2031	76,600,000	35,701,423	0	0
2032-2036	106,915,000	18,922,663	0	0
2037-2038	44,230,000	1,473,833	0	0
Totals	$334,660,000	$219,132,993	$4,136	$9

In 2008 the Port Authority received an Ohio Rail Development Commission Loan in the amount of $145,163 to finance the construction of a railroad spur.

In March, 2008, the Port Authority issued $348,750,000 of gas supply revenue bonds to fund the prepayment of 64,655,785 Mmbtus of gas from Royal Bank of Canada with deliveries beginning April 2008 and ending March 2038. The City of Lancaster will purchase the scheduled monthly gas at a specified index less a discount from such index price for the entire term of April 2008 through March 2038. The revenue bonds are secured by a pledge of the gas supply revenues derived from the related prepay transaction.

The Port Authority entered into an interest rate swap with Royal Bank of Canada in connection with the Series 2008, Gas Supply Revenue Bonds. Under the swap agreement, the Port Authority pays a fixed amount and receives a variable payment computed at a rate equal to that of the bonds. The interest payments reflected in the table above, were calculated based on the interest rate swap agreement which converts this issue to an effective fixed rate of approximately 3.7%.

NOTE 7 - GAS PURCHASE AND SALES AGREEMENTS

The Port Authority has entered into long-term gas purchase and supply contracts for which prepayments have been made and an amount remaining of $270,994,848 is reflected in both current and noncurrent asset categories at December 31, 2011. Long-term sales agreements also exist with the City to take delivery of the natural gas over a period continuing through 2038. The sales price to the City for these contracts is at specified index prices less a discount. Swap agreements are used to convert these variable index prices to fixed prices sufficient to meet debt service requirements.

NOTE 8 - DERIVATIVE INSTRUMENTS

Composition of Derivative Instruments

The fair value balances and notional amounts of derivative instruments outstanding as of December 31, 2011, classified by type, are as follows:

	Notional Amount	Fair Value	Counterparty Credit Rating
Positive Cash Flow Hedge:			
Pay-variable, receive fixed commodity swap	56,563,798 mmbtu	$ 221,300,167	AA-/A-1+
Negative Cash Flow Hedge:			
Pay-fixed, receive variable interest rate swap	$ 334,660,000	$ (143,270,265)	A+/A-1

All fair values are classified as derivative instruments on the Statement of Net Assets. The increase in fair values of these derivatives instruments was $27,313,892 for 2011. As these commodity and interest rate swaps are considered hedging derivatives instruments, the increase in fair value is reflected within deferred outflows and inflows on the Statement of Net Assets. The positive and negative fair values of the commodity and interest rate swaps were not netted. The fair values of the commodity swaps are based on forward prices from established indexes for the applicable region and discounted using established interest rate indexes. The fair values of the interest rate swaps are based on the SIFMA index at year end and discounted using established interest rate indexes.

Notes to the Basic Financial Statements
For the Year Ended December 31, 2011

NOTE 8 - DERIVATIVE INSTRUMENTS (Continued)

Objective and Terms of Hedging Derivative Instruments

The following table displays the objective and terms of the Port Authority hedging derivative instruments outstanding at December 31, 2011:

Type	Objective	Maturity Date	Terms
Pay-fixed receive variable interest rate swap	The Port Authority entered into an interest rate swap in connection with its Series 2008 Bonds, effective on or before the date of the initial issuance of such bonds, to correlate the fixed payments it receives under the related Commodity Swap with its variable rate debt service payment on these bonds.	2038	The interest rate swap extends to the date of the final maturity of these bonds and requires payments based on a notional amount equal to the scheduled outstanding principal amount of these bonds. Under the interest rate swap, the Port Authority pays the counterparty a fixed payment of 3.7%, on the notional amount and receives a variable payment equal to the rate actually borne by the Series 2008 Bonds, which is based upon the SIFMA index.
Pay-variable, receive fixed commodity swap	The Port Authority has entered into a fixed to floating commodity swap in connection with the natural gas prepay transaction. The purpose of the Commodity Swap is to correlate gas sales revenues the Port Authority receives based on floating natural gas indices to a fixed stream of payments necessary to make debt service payments on its Bonds.	2038	The commodity swap extends to the date of the final maturity of the related Natural Gas Supply Agreements. The commodity swap requires monthly payments based on a notional quantity of natural gas that corresponds to the volume of natural gas sold pursuant to the related Natural Gas Supply Agreements. Payments under the commodity swap are based on nationally published gas indices at the gas delivery points.

Notes to the Basic Financial Statements
For the Year Ended December 31, 2011

NOTE 8 - DERIVATIVE INSTRUMENTS (Continued)

Commodity Swap Risks

Termination Risk: The Commodity Swaps terminate in the event of a “triggering event” under the related Prepaid Natural Gas Sales Agreements, in the event of the Port Authority or counterparty nonperformance, and in connection with other specified events. Under the Commodity Swaps no payment, in the amount of the fair value or otherwise, is to be made by the Swap Counterparty in connection with an early termination of such swap. However, if the Commodity Swaps are terminated as a result of the Port Authority’s default or as a result of the termination of the Prepaid Natural Gas Sales Agreements, the Port Authority would be obligated to pay a termination payment to the Swap Counterparty based on the net present value of the remaining notional quantities of gas during the remaining term multiplied by a fixed amount.

Credit Risk: The Commodity Swaps are tied to related gas prepay transactions and terminate in the event such transactions terminate. Therefore, the only credit risk associated with the Commodity Swaps is for margins lost on future commodity deliveries associated with a termination of the related gas prepay transactions in the event of a counterparty’s inability to perform in accordance with the terms of the related Commodity Swaps. Generally, the only amounts due upon termination of the Commodity Swap would be previously accrued but unpaid amounts. If the Swap Counterparty is rated below "A1" by Moody’s Investors Service, Inc., the Swap Counterparty, is permitted to post collateral or post an alternative security arrangement within twenty-five Local Business Days of such downgrade. The Swap Counterparty must provide the Port Authority adequate assurances of Swap Counterparty’s ability to continue performing under all Transactions, which adequate assurances must be satisfactory to the Port Authority.

Interest Rate Swap Risks

Termination Risk: The Interest Rate Swaps terminate in the event of a “triggering event” under the related Prepaid Natural Gas Sales Agreements, in the event of the Port Authority or counterparty nonperformance, and in connection with other specified events. Under the Interest Rate Swaps, no termination payment, in the amount of the fair value or otherwise, is to be made by either party in connection with an early termination of such swap.

Credit risk: The Interest Rate Swaps terminate in the event of a "triggering event" under the related Prepaid Natural Gas Sales Agreements, in the event of the Port Authority or Swap Counterparty nonperformance, and in connection with other specified events. The only amounts due upon termination of the Interest Rate Swaps would be previously accrued but unpaid amounts. If the Swap Counterparty is rated below "A1" by Moody’s Investors Service, Inc., the Swap Counterparty, is permitted to post collateral or post an alternative security arrangement within twenty-five Local Business Days of such downgrade. The Swap Counterparty must provide the Port Authority adequate assurances of Swap Counterparty’s ability to continue performing under all Transactions, which adequate assurances must be satisfactory to the Port Authority.

Notes to the Basic Financial Statements
For the Year Ended December 31, 2011

NOTE 8 - DERIVATIVE INSTRUMENTS (Continued)

Interest Rate Risk: Under the pay-fixed interest rate swap agreement, the Port Authority is required to pay an amount equal to the notional amount times the rate actually borne by the Series 2008 Bonds, and is to receive an amount equal to the SIFMA index. In the event the rate actually borne by the Series 2008 Bonds exceeds the rate paid by the Swap Counterparty, the Port Authority would be required to pay the Swap Counterparty an amount equal to the notational amount times the difference.

NOTE 9 - RISK MANAGEMENT

The Port Authority is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions, injuries to agents and others; and natural disasters. The Port Authority carries commercial insurance, subject to certain limits and deductibles, to reduce the financial impact for claims arising from such matters. Claims have not exceeded this commercial coverage in any of the three preceding years.

NOTE 10 - RELATED PARTY TRANSACTIONS

All of the Port Authority's natural gas sales have been to the City of Lancaster (the "City"). At December 31, 2011, accounts receivable due from the City was $551,819. For 2011, the Port Authority reported gas sales to the City in the amount of $8,624,592.

The Port Authority charges the City an additional fee above the prepaid gas supply purchase price. Seventy-five percent of this fee is set aside for use by the City. These funds are remitted to the City upon City Council passing an ordinance stating the specific use of the funds. In 2011, the Port Authority remitted $247,840 to the City

NOTE 11 - SIGNIFICANT ESTIMATES AND CONCENTRATIONS

Generally accepted accounting principles require disclosure of certain significant estimates and current vulnerabilities due to certain concentrations. Those matters include the following:

Major Suppliers

The Port Authority purchased all of its natural gas supply from the Royal Bank of Canada. There are a limited number of national gas suppliers with which the Port Authority could contract under prepay gas transactions and any disruption of deliveries under the supply contracts could have an impact on the Port Authority's operations.

NOTE 11 - SIGNIFICANT ESTIMATES AND CONCENTRATIONS (Continued)

Current Economic Conditions

The current protracted economic decline continues to present energy companies with difficult circumstances and challenges, which in some cases have resulted in large declines in the fair value of investments and other assets, declines in revenues, constraints on liquidity and difficulty obtaining financing. The financial statements have been prepared using values and information currently available to the Port Authority.

Although the Port Authority has not currently identified any specific circumstances which would cause the difficulties noted above, economic conditions could make it difficult for consumers to maintain demand and usage levels, which could have an adverse impact on the future operating results of the Port Authority.

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CLARK SCHAEFER HACKETT
STRENGTH IN NUMBERS

<u>REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*</u>

Board of Directors
Lancaster Port Authority
104 East Main Street
Lancaster, Ohio 43130-3726

We have audited the accompanying financial statements of the Lancaster Port Authority (the Authority), a component unit of the City of Lancaster, Ohio, as of and for the year ended December 31, 2011, and have issued our report thereon dated April 27, 2012. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

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

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

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, 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 defined above. However, we identified a certain deficiency in internal control over financial reporting, described in the accompanying schedule of findings and responses as item 2011-001 that we consider to be a significant deficiency in internal control over financial reporting. A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

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Compliance and Other Matters

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

We noted certain matters that we reported to management of the Authority in a separate letter dated April 27, 2012.

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

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

Clark, Schaefer, Hackett & Co.

Springfield, Ohio
April 27, 2012

Section I – Summary of Auditors' Results

Financial Statements

Type of auditors' report issued:	Unqualified
Internal control over financial reporting:	
• Material weakness(es) identified?	None noted
• Significant deficiency(ies) identified not considered to be material weakness(es)?	Yes
Noncompliance material to financial statements noted?	None noted

Section II – Financial Statement Findings

2011-001: Significant Deficiency – Segregation of Duties
The segregation of financial duties is important to adequately protect the Authority's assets and ensure accurate financial reporting. Presently, there is not an adequate number of personnel available to properly segregate duties to provide reasonable assurance that no one employee would have access to both physical assets and related accounting records, or to all phases of a transaction. Without proper segregation of duties, the risk increases that errors and fraud could occur and not be detected within a timely basis. Efficient segregation of duties in a small environment is often difficult; however, the Authority's Board should be aware of the risk associated with this lack of duty segregation and attempt to exercise as much oversight control in these areas as possible and feasible.

Management Response: The Port Authority is aware of the segregation of duties issues related to limited and reduced staff and is currently making every attempt to mitigate these risks through separate reviews and oversight of transactions.

Section III – Summary Schedule of Prior Audit Findings

2010-001: Significant Deficiency – The segregation of financial duties is important to adequately protect the Authority's assets and ensure accurate financial reporting.

Status: No Change - see current year finding 2011-001

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At Clark Schaefer Hackett, we are the sum of our individuals. Each team member's training, experience and drive is well-suited to each client's needs and goals. We are committed to providing insightful and flexible service – from efficient compliance to sophisticated consulting – to help each client prosper today and plan for future success

LANCASTER PORT AUTHORITY

FAIRFIELD COUNTY

CLERK'S CERTIFICATION

This is a true and correct copy of the report which is required to be filed in the Office of the Auditor of State pursuant to Section 117.26, Revised Code, and which is filed in Columbus, Ohio.

Susan Babbitt

CLERK OF THE BUREAU

CERTIFIED
JUNE 26, 2012