



Bryan Texas Utilities

Rural Electric System

Annual Financial Statements

For the Fiscal Years Ended September 30, 2010 and 2009

Bryan Texas Utilities
Rural Electric System
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For the Fiscal Years Ended September 30, 2010 and 2009

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**Bryan Texas Utilities
Rural Electric System**

Introduction

For the Fiscal Years Ended September 30, 2010 and 2009
(Unaudited)

Bryan Texas Utilities (BTU) is pleased to present the Annual Financial Report for the fiscal years ended September 30, 2010 and 2009. This report is published to provide the BTU Board, the City of Bryan, the Bondholders, representatives of financial institutions, and other interested parties detailed information concerning the financial condition of BTU.

BTU is an enterprise activity of the City of Bryan, Texas. BTU operates a “City” and “Rural” electric system, (the “City Electric System” and the “Rural Electric System”, respectively). Each system, while operated by a common staff, is maintained separately for accounting and reporting purposes. BTU’s Rural Electric System purchases all of its energy from the City Electric System. BTU’s common staff is employed by the City Electric System and is either direct billed to the Rural Electric System or is billed through the City Electric System’s purchased power rates. Generally, all power supply, customer service and administrative services are billed through purchased power rates, while distribution services are direct billed. Rural purchased power rates are established through City of Bryan ordinance. The accompanying financial statements present only the Rural Electric System and are not intended to present the financial position or results of operations of the City Electric System or the City of Bryan, Texas.

The Rural Electric System provides electric service to the immediate rural area outside the City of Bryan extending to most of Brazos County, all service adjacent to the City of College Station service area, and parts of Burleson, and Robertson counties in a radius of nearly 20 miles from the City of Bryan.

The Rural Electric System is managed by the BTU Board. The BTU Board, established on June 12, 2001, is appointed by the Bryan City Council and is empowered with the management and control of BTU. The Bryan City Council retains authority for approval of the annual budget, rates for electric service, condemnations and debt financing.

BTU management has prepared and is responsible for the financial statements and related information included in this report. Management believes that its policies and procedures provide guidance and reasonable assurance that the Rural Electric System operations are conducted according to management’s intentions and to a high standard of business ethics. In management’s opinion, the financial statements present fairly, in all material respects, the net assets, changes in net assets and cash flows of the Rural Electric System in conformity with accounting principles generally accepted in the United States of America.



INDEPENDENT AUDITOR'S REPORT

To the City Council of City of Bryan, Texas
and Board of Directors of Bryan Texas Utilities

We have audited the accompanying financial statements of the Rural Electric System of Bryan Texas Utilities (BTU) of the City of Bryan, Texas, as of and for the years ended September 30, 2010 and 2009, as listed in the table of contents. These financial statements are the responsibility of BTU's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes 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 the Rural Electric System of BTU and do not purport to, and do not, present fairly the financial position of the City Electric System of BTU, or the City of Bryan, Texas, as of September 30, 2010 and 2009, and the changes in their financial position, or where applicable, their 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 the Rural Electric System of Bryan Texas Utilities of the City of Bryan, Texas, as of September 30, 2010 and 2009, and the changes in financial position and cash flows thereof for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis 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.

Our audits were conducted for the purpose of forming an opinion on the financial statements that collectively comprise the Rural Electric System of BTU's basic financial statements. The information included in the Introduction is presented for the purpose of additional analysis and is not a required part of the basic financial statements. This information has not been subjected to the auditing procedures applied in the audits of the basic financial statements and, accordingly, we do not express an opinion or provide any assurance on it.

Weaver and Tidwell, L.L.P.

WEAVER AND TIDWELL, L.L.P.

Houston, Texas
December 29, 2010

Bryan Texas Utilities
Rural Electric System
Management's Discussion and Analysis
For the Fiscal Years Ended September 30, 2010 and 2009
(Unaudited)

This discussion and analysis of the Rural Electric System financial performance provides an overview of financial activities for the years ended September 30, 2010 and 2009. Please read this information in conjunction with the accompanying financial analysis, the financial report, and the accompanying notes to financial statements.

Overview of Annual Financial Report

The financial statements report information about the Rural Electric System using accrual accounting methods as utilized by similar business activities in the private sector. The Rural Electric System annual reporting period ("fiscal year") ends September 30.

The Statements of Net Assets include the Rural Electric System assets and liabilities and provides information about the nature and amounts of investments in resources (assets) and the obligations to creditors (liabilities). It also provides the basis for the evaluation of capital structure, liquidity, and flexibility of the Rural Electric System.

The Statements of Revenues, Expenses and Changes in Net Assets present the results of the business activities (revenues and expenses) over the course of the fiscal year and can provide information about the Rural Electric System recovery of its costs.

The Statements of Cash Flows present cash receipts, cash disbursements and net changes in cash resulting from operations, financing and related investing activities. This statement provides information such as where cash came from, what cash was used for and what the changes in cash balances were during the reporting period.

The notes to the financial statements provide required disclosures and other information that are essential to a full understanding of material data provided in the statements. The notes present information about the Rural Electric System accounting policies, significant account balances and activities, material risks, obligations, commitments, contingencies and subsequent events, if any.

Bryan Texas Utilities
Rural Electric System
Management's Discussion and Analysis - Continued
For the Fiscal Years Ended September 30, 2010 and 2009
(Unaudited)

Financial Analysis

The following condensed financial statements are for BTU's Rural Electric System, as described in the introduction, and provide key financial data as of and for the fiscal years ended September 30, 2010 and 2009.

| <u>Condensed Statements of Net Assets</u> | <u>2010</u> | <u>2009</u> |
|----------------------------------------------------|----------------------|----------------------|
| Current assets | \$ 6,910,211 | \$ 6,396,288 |
| Capital assets, net | 39,417,240 | 38,006,419 |
| Restricted assets | 6,049,149 | 4,996,191 |
| Other | <u>310,418</u> | <u>342,264</u> |
| Total assets | <u>52,687,018</u> | <u>49,741,162</u> |
| Current liabilities | 2,316,031 | 2,481,995 |
| Current liabilities payable from restricted assets | 3,081,892 | 1,893,492 |
| Noncurrent liabilities | <u>5,903,056</u> | <u>6,165,652</u> |
| Total liabilities | <u>11,300,979</u> | <u>10,541,139</u> |
| Net assets: | | |
| Invested in capital assets | 36,445,747 | 35,016,618 |
| Restricted | 38,750 | 37,500 |
| Unrestricted | <u>4,901,542</u> | <u>4,145,905</u> |
| Total net assets | <u>\$ 41,386,039</u> | <u>\$ 39,200,023</u> |

Condensed Statements of Revenues, Expenses and Changes in Net Assets

| | | |
|---------------------------------|----------------------|----------------------|
| Operating revenues | \$ 30,133,488 | \$ 30,996,152 |
| Operating expenses | <u>27,713,101</u> | <u>29,431,858</u> |
| Operating income | 2,420,387 | 1,564,294 |
| Investment income | 43,002 | 56,851 |
| Interest expense | <u>(277,373)</u> | <u>(281,048)</u> |
| Change in net assets | 2,186,016 | 1,340,097 |
| Net assets, beginning of period | <u>39,200,023</u> | <u>37,859,926</u> |
| Net assets, end of period | <u>\$ 41,386,039</u> | <u>\$ 39,200,023</u> |

Bryan Texas Utilities
Rural Electric System
Management's Discussion and Analysis - Continued
For the Fiscal Years Ended September 30, 2010 and 2009
(Unaudited)

Financial Highlights

- Rural Electric System retail customer base totaled 15,593 and 15,116 customers at September 30, 2010 and 2009, respectively, an increase of 3.2%.
- Retail energy sales were 337,180 MWh's and 306,888 MWh's during the fiscal years ended September 30, 2010 and 2009, respectively, an increase of 9.9%, due primarily to abnormally hot summer and cold winter weather during the fiscal year ended September 30, 2010.
- Operating revenues for fiscal years ended September 30, 2010 and 2009 were \$30,133,488 and \$30,996,152, respectively, a decrease of 2.8%. The decrease is primarily attributable to 2010 fuel revenues being \$2,280,679 less than 2009 due to lower average fuel rates in 2010. BTU lowered the Rural Electric System fuel rate in June 2009. The decrease in fuel revenue was partially offset by increases in base revenue from increased retail sales as describe above.
- Operating expenses for the fiscal years ended September 30, 2010 and 2009 were \$27,713,101 and \$29,431,858 respectively, a decrease of 5.8%. The decrease was primarily due to lower fuel rates in 2010 as described above and lower general and administrative expenses. As described in Note 1- Summary of Significant Accounting Policies, the difference between fuel revenues billed and fuel expense incurred is recorded as an addition or a reduction to fuel and purchased power expense, with a corresponding entry to accounts payable - over recovered fuel or accounts receivable - under recovered fuel, whichever is appropriate.
- Net assets for the fiscal years ended September 30, 2010 and 2009 were \$41,386,039 and \$39,200,023, respectively. The increase of 5.6% was the result of higher volume of sales and further expansion of the distribution system.

Capital Assets

The Rural Electric System net utility plant was \$39,417,240 and \$38,006,419 for the fiscal years ended September 30, 2010 and 2009, respectively, an increase of 3.7%. The increase in capital assets is primarily the result of construction expenditures supporting new customer growth.

General Trends and Significant Events

Although at a slower pace in 2010 compared to 2009, the economy in the local area continues to grow. The service area supplied by the Rural Electric System is positioned for further customer growth, especially in new subdivisions south of the City of College Station service area.

**Bryan Texas Utilities
Rural Electric System**

Management's Discussion and Analysis - Continued
For the Fiscal Years Ended September 30, 2010 and 2009
(Unaudited)

Requests for Information

This financial report is designed to provide readers with a general overview of BTU's Rural Electric System finances. Questions concerning any of the information provided in this report or requests for additional information should be addressed to Bryan Texas Utilities, P.O. Box 8000, Bryan, Texas 77805.

Group Managers:

Joe Hegwood
Gary Miller
Kean Register

General Manager:

Dan Wilkerson

**Bryan Texas Utilities
Rural Electric System**
Statements of Net Assets
At September 30, 2010 and 2009

| | September 30, | |
|-----------------------------------------------------|----------------------|---------------|
| <u>Assets</u> | 2010 | 2009 |
| Current assets: | | |
| Cash and cash equivalents | \$ 3,644,779 | \$ 3,166,149 |
| Account receivable | 3,455,671 | 3,437,690 |
| Less allowance for uncollectible accounts | (190,239) | (207,551) |
| Total current assets | 6,910,211 | 6,396,288 |
| Noncurrent assets: | | |
| Restricted cash and cash equivalents | 3,044,349 | 1,973,691 |
| Restricted investments | 3,004,800 | 3,022,500 |
| Capital assets | 58,181,679 | 55,906,952 |
| Less accumulated depreciation | (18,764,439) | (17,900,533) |
| Unamortized bond issuance expenses and other assets | 310,418 | 342,264 |
| Total noncurrent assets | 45,776,807 | 43,344,874 |
| Total assets | \$ 52,687,018 | \$ 49,741,162 |

The accompanying notes are an integral part of the financial statements.

**Bryan Texas Utilities
Rural Electric System**
Statements of Net Assets - Continued
At September 30, 2010 and 2009

| | September 30, | |
|-------------------------------------------------------------|----------------------|---------------|
| Liabilities | 2010 | 2009 |
| Current liabilities: | | |
| Accounts payable | \$ 79,026 | \$ 246,796 |
| Accrued liabilities | 88,933 | 94,679 |
| Due to other funds | 2,083,158 | 2,065,751 |
| Deferred credits and other liabilities | 64,914 | 74,769 |
| Total current liabilities | 2,316,031 | 2,481,995 |
| Current liabilities payable from restricted assets: | | |
| Accrued interest | 65,575 | 66,887 |
| Over recovered fuel | 2,104,289 | 972,392 |
| Revenue bonds – current | 155,000 | 150,000 |
| Customer deposits | 757,028 | 704,213 |
| Total current liabilities payable from restricted assets | 3,081,892 | 1,893,492 |
| Noncurrent liabilities: | | |
| Revenue bonds payable | 5,900,000 | 6,055,000 |
| Bond discounts | (54,481) | (56,775) |
| Deferred credits and other liabilities | 57,537 | 167,427 |
| Total noncurrent liabilities | 5,903,056 | 6,165,652 |
| Total liabilities | 11,300,979 | 10,541,139 |
| Net Assets | | |
| Net Assets: | | |
| Invested in capital assets, net of related debt | 36,445,747 | 35,016,618 |
| Restricted for debt service | 38,750 | 37,500 |
| Unrestricted | 4,901,542 | 4,145,905 |
| Total net assets | \$ 41,386,039 | \$ 39,200,023 |

The accompanying notes are an integral part of the financial statements.

Bryan Texas Utilities
Rural Electric System
Statements of Revenues, Expenses
And Changes in Net Assets
For the Fiscal Years Ended September 30, 2010 and 2009

| | <u>FY2010</u> | <u>FY2009</u> |
|-----------------------------------------|----------------------|----------------------|
| Operating revenues: | | |
| Electrical system | \$ 30,133,488 | \$ 30,996,152 |
| | <u>30,133,488</u> | <u>30,996,152</u> |
| Total operating revenues | | |
| Operating expenses: | | |
| Personnel services | 403,671 | 388,139 |
| Electric operations | 25,140,935 | 26,941,707 |
| Maintenance | 434,886 | 371,173 |
| General and administrative | 103,518 | 188,679 |
| Total operating expenses | <u>26,083,010</u> | <u>27,889,698</u> |
| before depreciation | | |
| Operating income before depreciation | 4,050,478 | 3,106,454 |
| Depreciation | <u>1,630,091</u> | <u>1,542,160</u> |
| Operating income | <u>2,420,387</u> | <u>1,564,294</u> |
| Non-operating revenues (expenses): | | |
| Investment income | 43,002 | 56,851 |
| Interest expense | (277,373) | (281,048) |
| Total non-operating revenues (expenses) | <u>(234,371)</u> | <u>(224,197)</u> |
| Increase in net assets | 2,186,016 | 1,340,097 |
| Net assets, beginning of period | <u>39,200,023</u> | <u>37,859,926</u> |
| Net assets, end of period | <u>\$ 41,386,039</u> | <u>\$ 39,200,023</u> |

The accompanying notes are an integral part of the financial statements.

Bryan Texas Utilities
Rural Electric System
Statements of Cash Flows
For the Fiscal Years Ended September 30, 2010 and 2009

| | <u>FY2010</u> | <u>FY2009</u> |
|------------------------------------------------------------------------|----------------------|----------------------|
| <u>Cash flows from operating activities</u> | | |
| Receipts from customers | \$ 30,149,934 | \$ 31,046,025 |
| Payments to suppliers | (24,406,492) | (23,656,331) |
| Payments to employees | (415,206) | (393,319) |
| | <u>5,328,236</u> | <u>6,996,375</u> |
| <u>Cash flows from capital and related financing activities</u> | | |
| Purchases of capital assets | (3,414,805) | (4,075,862) |
| Principal paid on capital debt | (150,000) | (90,000) |
| Interest paid on capital debt | (240,526) | (270,701) |
| | <u>(3,805,332)</u> | <u>(4,436,563)</u> |
| <u>Cash flows from investing activities</u> | | |
| Proceeds from sales of investments | 6,000,000 | 3,000,000 |
| Purchase of investments | (6,009,322) | (6,025,847) |
| Investment earnings | 35,705 | 52,826 |
| | <u>26,383</u> | <u>(2,973,021)</u> |
| Net cash provided (used) by investing activities | <u>26,383</u> | <u>(2,973,021)</u> |
| Net increase (decrease) in cash and cash equivalents | 1,549,288 | (413,209) |
| Balances-beginning of the year | <u>5,139,840</u> | <u>5,553,049</u> |
| Balances-end of the year | <u>\$ 6,689,128</u> | <u>\$ 5,139,840</u> |
| <u>Reconciliation of Ending Cash Balance</u> | | |
| Cash and cash equivalents | \$ 3,644,779 | \$ 3,166,149 |
| Cash and cash equivalents – restricted | <u>3,044,349</u> | <u>1,973,691</u> |
| Balances-end of year | <u>\$ 6,689,128</u> | <u>\$ 5,139,840</u> |

The accompanying notes are an integral part of the financial statements.

**Bryan Texas Utilities
Rural Electric System**
Statements of Cash Flows - continued
For the Fiscal Years Ended September 30, 2010 and 2009

**Reconciliation of operating income to net cash
provided by operating activities:**

| | <u>FY2010</u> | <u>FY2009</u> |
|-------------------------------------------------------------------------------------------|----------------------|----------------------|
| Operating income | \$ 2,420,387 | \$ 1,564,294 |
| Adjustments to reconcile operating income to net cash provided by operating activities | | |
| Depreciation | 1,630,091 | 1,542,160 |
| Bad debts | 31,378 | 75,347 |
| Change in assets and liabilities: | | |
| Accounts receivable | (36,369) | (330,551) |
| Under recovered fuel | - | 3,097,078 |
| Accounts payable | 17,520 | (6,598) |
| Accrued liabilities | (5,746) | (5,493) |
| Over recovered fuel | 1,131,897 | 972,392 |
| Customer deposits | 52,815 | 380,424 |
| Due to other funds | 92,052 | (292,991) |
| Accrued vacation and other | (5,789) | 313 |
| Net cash provided by operating activities | <u>\$ 5,328,236</u> | <u>\$ 6,996,375</u> |

The accompanying notes are an integral part of the financial statements.

Bryan Texas Utilities
Rural Electric System
Notes to Financial Statements
For the Fiscal Years Ended September 30, 2010 and 2009

1. Summary of Significant Accounting Policies

Reporting Entity - Bryan Texas Utilities (BTU) is a municipally owned utility system that operates as an enterprise activity of the City of Bryan, Texas. BTU operates a city and rural electric system, (the "City Electric System" and the "Rural Electric System", respectively). Each system, while operated by a common staff, is maintained separately for accounting and reporting purposes. The Rural Electric System is the reporting entity. These financial statements present only the Rural Electric System and are not intended to present the financial position of BTU's City Electric System or the City of Bryan, Texas (the "City") nor the results of their operations and cash flows in conformity with generally accepted accounting principles.

Financial Statements - The financial statements for BTU (a proprietary fund) are reported using the economic resources measurement focus and the accrual basis of accounting. All assets and liabilities (whether current or noncurrent) are included on the Statement of Net Assets. The Statement of Revenues, Expenses and Changes in Net Assets present increases (revenues) and decreases (expenses) in net total assets. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows.

The Statement of Revenues, Expenses and Changes in Net Assets distinguishes operating revenues and expenses from non-operating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. Operating expenses for BTU include the cost of sales and services, administrative expenses and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

Basis of Accounting - The Rural Electric System is accounted for on the flow of economic resources measurement focus and uses the accrual basis of accounting. Accounting records are maintained in accordance with accounting principles generally accepted in the United States of America. BTU prepares its financial statements as a business-type activity in conformity with applicable pronouncements of the Governmental Accounting Standards Board (GASB). Pursuant to GASB Statement No. 20, BTU has elected to apply the provisions of all relevant pronouncements of the Financial Accounting Standards Board (FASB) that were issued on or before November 30, 1989, to the extent they do not conflict with or contradict GASB pronouncements. BTU has elected not to follow FASB guidance issued subsequent to this date.

Implementation of New Accounting Principles - For the fiscal years ended September 30, 2009 and 2010, GASB issued no pronouncements applicable to BTU's Rural Electric System financial reporting.

Restricted Funds

Restricted funds consist of construction funds derived from debt issues, system revenues that have been designated for specific purposes by the BTU Board or other funds with legal or contractual constraints. When both restricted and unrestricted resources are available for use, it is BTU's policy to use restricted resources first, then unrestricted resources as they are needed.

**Bryan Texas Utilities
Rural Electric System**

Notes to Financial Statements - continued
For the Fiscal Years Ended September 30, 2010 and 2009

Use of Estimates - In preparing financial statements in conformity with generally accepted accounting principles, management is required to make estimates and assumptions that affect the reported amount of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and revenues and expenses during the reporting period. Actual results could differ from these estimates.

Utility Revenues and Fuel Recovery - Customers are billed on the basis of monthly cycle billings. At fiscal year end, the Rural Electric System accrues estimated unbilled revenues (excluding fuel). The Rural Electric System is allowed to recover purchased power cost through fuel revenue rates. The difference between fuel revenues billed and fuel expense incurred is recorded as an addition or a reduction to fuel and purchased power expense, with a corresponding entry to accounts payable - over recovered fuel or accounts receivable - under recovered fuel, whichever is appropriate. At September 30, 2010 and 2009, the Rural Electric System reflected a current liability – Over recovered fuel of \$2,104,289 and \$972,392, respectively.

Capital Assets - Capital assets are stated at the historical cost, net of contributions from third parties (principally developers). Also, to the extent the construction is performed by the Rural Electric System, the cost includes payroll and related costs and certain general and administrative expenses. Interest is not capitalized in these accounts because interest is recovered concurrently in the utility rate structure. Maintenance, repairs and minor replacements are charged to operating expense, while major property replacements are capitalized. Except for certain assets that may become impaired, the cost of depreciable plant retired, plus removal cost and less salvage, is charged to accumulated depreciation. Per the financial reporting requirements of GASB Statement No. 42, *Accounting for Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries*, any losses associated with capital asset impairments will be charged to operations, not accumulated depreciation. Depreciation is recorded on a straight-line basis over estimated service lives ranging from 5 to 40 years.

Cash and Cash Equivalents – For purposes of cash flows, the Rural Electric System considers all highly liquid investments with an original maturity of three months or less to be cash equivalents. Cash and cash equivalents from restricted assets are also included.

Bond Issuance Expenses - Bond issuance expenses are amortized on a straight-line basis over the period of the related maturities, which approximates the interest method.

Reclassifications – Certain reclassifications have been made to the prior period's financial statements in order to conform them to the classification used in the current year. Such reclassifications had no effect on the change in net assets as previously reported.

2. Cash and Investments

Rural Electric System cash is managed by BTU and deposited into separate revenue and operating accounts at the City's depository bank in the name of the BTU, Rural Electric System. All Rural Electric System cash is deposited in accounts that receive interest credit or is invested in permissible securities pursuant to BTU's investment policy. Investments are stated at fair value based on quoted market prices provided by the custodian.

**Bryan Texas Utilities
Rural Electric System**

Notes to Financial Statements - continued
For the Fiscal Years Ended September 30, 2010 and 2009

Deposits

The Rural Electric System demand deposits for the fiscal years ended September 30, 2010 and 2009 were held at Citibank, N.A. These deposits were entirely covered by federal depository insurance or by collateral equal to at least 105% of the deposits. For deposits that were collateralized, the securities were in accordance with the Texas Public Funds Collateral Act.

Investments

The BTU investment program is guided by Texas state laws, by various City ordinances, and by BTU's investment policy which prescribes how the Rural Electric System will operate its investment program in accordance with applicable laws and regulations. This policy further sets forth (1) the basic principles governing the investment of funds; (2) the objectives of the investment program; and (3) the authority, responsibilities, limitations, documentation, and requirements to be used in the administration and operation of the investment program.

Investments authorized by the investment policy are those approved by the revised State of Texas Public Funds Investment Act of 1997 and the Texas Public Funds Collateral Act of 1989. These investments include the following:

- a. Obligations of the United States or its agencies and instrumentalities;
- b. Direct obligations of the State of Texas or its agencies;
- c. Other obligations, the principal of and interest on which is unconditionally guaranteed or insured by the State of Texas or the United States or its agencies or instrumentalities;
- d. Obligations of states, agencies, counties, cities and other political subdivisions of any state having been rated as to investment quality by a nationally recognized investment rating firm and having received a rating of not less than A or its equivalent;
- e. Certificates of deposit issued by state and national banks domiciled in Texas that are secured by obligations qualified as acceptable collateral;
- f. Certificates of deposit issued by savings and loan associations domiciled in Texas that are secured by obligations qualified as acceptable collateral;
- g. Prime domestic bankers' acceptances;
- h. Commercial paper with a stated maturity of 180 days or less from the date of issuance that is rated not less than A-1, P-1 or its equivalent;

**Bryan Texas Utilities
Rural Electric System**

Notes to Financial Statements - continued
For the Fiscal Years Ended September 30, 2010 and 2009

- i. Fully collateralized repurchase agreements that have a defined termination date of 90 days or less, secured by qualified obligations, pledged with a third party, and placed through a primary government securities dealer as defined by the Federal Reserve, or a bank domiciled in Texas;
- j. Money-market mutual funds that are SEC registered no-load funds with a maximum stated maturity of 13 months and dollar-weighted average stated maturity of no more than 90 days;
- k. AAA-rated local government investment pools;
- l. Hedging contracts and related security insurance agreements in relation to BTU fuel and energy supplies to protect against loss due to price fluctuations.

Collateralized Mortgage Obligations (“CMO’s”) and other derivatives such as inverse floaters and other mortgage-backed securities that pay only interest or principal portion of the mortgage payment are not authorized BTU investments.

The Rural Electric System’s cash, cash equivalents and investments are summarized as follows:

| | <u>FY2010</u> | <u>FY2009</u> |
|------------------------------------|----------------------|----------------------|
| Demand deposits | \$ 6,689,128 | \$ 5,139,840 |
| Investments in treasury securities | 3,004,800 | 3,022,500 |
| Total | <u>\$ 9,693,928</u> | <u>\$ 8,162,340</u> |

In accordance with GASB Statement No. 40, additional disclosures are provided below that address investment exposure to interest rate risk and credit risk including custodial credit risk and concentrations of credit risk. Because BTU does not hold foreign investments, foreign currency risk is not discussed.

As of September 30, 2010, BTU had the following investments:

| <u>Investment Types</u> | <u>Fair Value</u> | <u>Investment Maturity</u> <u>(in Years)</u> | | |
|--------------------------------|--------------------------|---------------------------------------------------------------|---------------------|------------------------------|
| | | <u>Less Than 1</u> | <u>1 - 5</u> | <u>Greater Than 5</u> |
| Treasury securities | \$ 3,004,800 | \$ 3,004,800 | \$ - | \$ - |
| Total fair value | <u>\$ 3,004,800</u> | <u>\$ 3,004,800</u> | <u>\$ -</u> | <u>\$ -</u> |

Interest rate risk – As a means of limiting its exposure to fair value losses arising from rising interest rates, BTU’s investment policy limits investments in securities of more than five years, unless matched by a specific cash flow. Additionally, in accordance with its investment policy BTU manages its exposure to interest rate risk by limiting its investment to those held to maturity.

**Bryan Texas Utilities
Rural Electric System**

Notes to Financial Statements - continued
For the Fiscal Years Ended September 30, 2010 and 2009

Credit Risk – As described above, it is BTU’s policy to limit its investment to high grade instruments including obligations of the United States or its agencies.

Custodial Credit Risk – For deposits, custodial credit risk is the risk that in an event of a bank failure, the government’s deposits may not be returned to it. Demand deposits held in BTU’s name are required to be collateralized with securities equal to at least 105% of deposits held in a custodian bank, or be covered by federal depository insurance. For investments, this is the risk that in the event of the failure of the counterparty, the government will not be able to recover the value of its investments or collateral securities that are in possession of an outside party. BTU’s investment policy requires that all security transactions be conducted on a delivery versus payment basis and that all securities be held by a third party custodian and evidenced by safekeeping receipts.

Concentration of Credit Risk – BTU’s investment policy places some limits on the amount that may be invested in any one issuer. Investments in any single money market fund or investment pool shall never exceed ten percent of the total assets of the money market fund or pool.

Restricted Cash and Investments

In 2010, cash and investments of \$9.7 million exceeded amounts required to be restricted by \$3.6 million. Amounts required to be restricted at September 30, 2010 and 2009 are as follows:

| | <u>FY2010</u> | <u>FY2009</u> |
|---------------------------------|---------------------|---------------------|
| Debt service | \$ 104,325 | \$ 104,388 |
| Bond series 2008 reserve | 3,083,507 | 3,215,198 |
| Over recovered fuel | 2,104,289 | 972,392 |
| Customer deposits | <u>757,028</u> | <u>704,213</u> |
| Restricted cash and investments | <u>\$ 6,049,149</u> | <u>\$ 4,996,191</u> |

3. Capital Assets

General Description – Assets reflected in plant-in-service include distribution facilities.

Impairments – As discussed in Note 1, BTU adopted GASB Statement No. 42, *Accounting for Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries* in 2006. The statement provides guidance for determining if any assets have been impaired and for calculating the appropriate write-downs in value for any assets found to be impaired. An internal company-wide review of capital assets, in accordance with GASB Statement No. 42, concluded that BTU had no impaired capital assets at September 30, 2010.

**Bryan Texas Utilities
Rural Electric System**

Notes to Financial Statements - continued
For the Fiscal Years Ended September 30, 2010 and 2009

Capital asset activity for the fiscal year ended September 30, 2010 was as follows:

| | Beginning Balance | Increases | Decreases | Ending Balance |
|-------------------------------------------------|----------------------|--------------|--------------|-------------------|
| Capital assets, not being depreciated: | | | | |
| Land | \$ 111,483 | \$ - | \$ - | \$ 111,483 |
| Construction in progress | 3,010,636 | 3,255,189 | 4,681,223 | 1,584,602 |
| Total capital assets, not being depreciated | 3,122,119 | 3,255,189 | 4,681,223 | 1,696,085 |
| Capital assets, being depreciated: | | | | |
| Distribution plant | 51,763,593 | 4,507,876 | 48,013 | 56,223,456 |
| General plant | 1,021,240 | - | 759,102 | 262,138 |
| Total capital assets, being depreciated | 52,784,833 | 4,507,876 | 807,115 | 56,485,594 |
| Less accumulated depreciation for: | | | | |
| Distribution plant | 17,068,574 | 1,610,139 | 7,083 | 18,671,630 |
| General plant | 831,959 | 19,952 | 759,102 | 92,809 |
| Total accumulated depreciation | 17,900,533 | 1,630,091 | 766,185 | 18,764,439 |
| Total capital assets, being depreciated, net | 34,884,300 | 2,877,785 | 40,930 | 37,721,155 |
| Total capital assets, net | \$ 38,006,419 | \$ 6,132,974 | \$ 4,722,153 | \$ 39,417,240 |

4. Long-Term Debt

The City reserves the right at any time to merge the City Electric System and Rural Electric System into a single operating electric utility system. The merger of the Rural Electric System would not have an adverse impact on the bondholders.

In 2008, the Rural Electric System issued revenue bonds dated April 15, 2008, totaling \$6,295,000 and maturing serially on July 1, 2009, through July 1, 2034, with coupon rates ranging from 3.50% to 4.75%. Proceeds of the 2008 bond issue are restricted to the construction of distribution facilities and to pay bond costs. At September 30, 2010, there was \$6,055,000 of Rural Electric System revenue bonds outstanding payable from revenues of the Rural Electric System.

**Bryan Texas Utilities
Rural Electric System**

Notes to Financial Statements - continued
For the Fiscal Years Ended September 30, 2010 and 2009

The Rural Electric System revenue bonds outstanding are summarized as follows:

Series 2008 Bonds

| Ending September 30 | Principal | Interest | Total |
|--------------------------------|---------------------|---------------------|----------------------|
| 2011 | \$ 155,000 | \$ 262,300 | \$ 417,300 |
| 2012 | 160,000 | 256,875 | 416,875 |
| 2013 | 165,000 | 251,275 | 416,275 |
| 2014 | 175,000 | 245,500 | 420,500 |
| 2015 | 180,000 | 239,375 | 419,375 |
| 2016-2020 | 995,000 | 1,092,475 | 2,087,475 |
| 2021-2025 | 1,225,000 | 871,094 | 2,096,094 |
| 2026-2030 | 1,510,000 | 572,925 | 2,082,925 |
| 2031-2034 | 1,490,000 | 181,213 | 1,671,213 |
| Total | \$ 6,055,000 | \$ 3,973,032 | \$ 10,028,032 |

All net revenues of the Rural Electric System are pledged for the payment of debt service of the revenue bonds. Net revenues, as defined by the bond resolution include all of the revenues and expenses of the Rural Electric System other than depreciation and amortization expenses. The bond resolutions further require that the net revenues, as defined, equal at least 1.20 times the average annual debt service on all revenue bonds. The Rural Electric System is in compliance with these requirements, at September 30, 2010.

Under the terms of the bond covenants, Rural Electric System is required to maintain minimum reserve fund requirements equal to approximately one year of debt service requirements. The reserve fund requirements may be satisfied by cash, a letter of credit or an insurance policy. The reserve fund requirements for the Series 2008 Bonds are satisfied with insurance policies.

Long-term debt activity for the year ended September 30, 2010 was as follows:

| | Beginning Balance | Additions | Reductions | Ending Balance | Due Within One Year |
|-----------------------------|----------------------|-----------|------------|-------------------|------------------------|
| Revenue Bonds - Series 2008 | \$ 6,205,000 | \$ - | \$ 150,000 | \$ 6,055,000 | \$ 155,000 |
| Total | \$ 6,205,000 | \$ - | \$ 150,000 | \$ 6,055,000 | \$ 155,000 |

In the Statement of Revenues, Expenses and Changes in Net Assets for the fiscal years ended September 30, 2010 and 2009, interest expense in the amount of \$277,373 and \$281,048, respectively, is included as a non-operating expense.

Bryan Texas Utilities
Rural Electric System

Notes to Financial Statements - continued
For the Fiscal Years Ended September 30, 2010 and 2009

5. Risk Management

The Rural Electric System is covered for risk of losses related to general liability and worker's compensation through the City's risk management program. The City has established an "Insurance Fund" whereby the costs of providing claims servicing and claims payment are funded by charging a "premium" based upon a percentage of estimated current year payroll and management's estimate of projected current costs. For the fiscal years ended September 30, 2010 and 2009, the Rural Electric System paid the City \$42,823 and \$80,004, respectively, for participation in the City's risk management program.

6. Related Party Transactions

BTU operates the Rural Electric System which provides electric service to the immediate rural area outside the City of Bryan, extending to most of Brazos County, adjacent to the City of College Station service area, and parts of Burleson, and Robertson counties in a radius of nearly 20 miles from the City of Bryan. BTU's Rural Electric System purchases all of its energy from the City Electric System. BTU's common staff is employed by the City Electric System and is either direct billed to the Rural Electric System or is billed through the City Electric System's purchased power rates. Generally, all power supply, customer service and administrative services are billed through purchased power rates, while distribution services are direct billed. Rural purchased power rates are established through City ordinance. Non-fuel Rural purchased power rates were last adjusted in December 2006. Fuel rates are adjusted monthly to reflect actual cost. For the fiscal years ended September 30, 2010 and 2009, the Rural Electric System's purchased power totaled \$23,971,508 and \$22,841,070, respectively, and had payables to the City Electric System in the amount of \$2,083,158 and \$2,065,751 respectively.