



Bryan Texas Utilities

Rural Electric System

Annual Financial Statements

For the Fiscal Years Ended September 30, 2012 and 2011

Bryan Texas Utilities
Rural Electric System
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For the Fiscal Years Ended September 30, 2012 and 2011

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**Bryan Texas Utilities
Rural Electric System**

Introduction

Bryan Texas Utilities (BTU) is pleased to present the Annual Financial Report for the fiscal years ended September 30, 2012 and 2011. 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, service adjacent to and including portions of the City of College Station, 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, 2012 and 2011, 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, 2012 and 2011, 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 BTU of the City of Bryan, Texas, as of September 30, 2012 and 2011, 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 on pages 4 through 7 be presented to supplement the financial statements. Such information, although not part of the financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the 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 principally 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 financial statements, and other knowledge we obtained during our audit of the 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 financial statements. The information included in the Introduction is presented for the purpose of additional analysis and is not a required part of the financial statements. This information has not been subjected to the auditing procedures applied in the audits of the 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 18, 2012

**Bryan Texas Utilities
Rural Electric System**

Management's Discussion and Analysis

This discussion and analysis of the Rural Electric System financial performance provides an overview of financial activities for the years ended September 30, 2012 and 2011. 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, 2012 and 2011
(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, 2012 and 2011.

<u>Condensed Statements of Net Assets</u>	<u>2012</u>	<u>2011</u>
Current assets	\$ 9,102,190	\$ 8,133,214
Capital assets, net	46,057,221	41,865,079
Restricted assets	5,635,308	10,906,185
Other	365,939	449,590
Total assets	<u>61,160,658</u>	<u>61,354,068</u>
Current liabilities	3,197,918	3,760,370
Current liabilities payable from restricted assets	5,411,206	5,431,624
Noncurrent liabilities	8,086,440	8,536,414
Total liabilities	<u>16,695,564</u>	<u>17,728,408</u>
Net assets:		
Invested in capital assets, net of related debt	37,779,032	38,398,598
Restricted	422,292	416,042
Unrestricted	6,263,770	4,811,020
Total net assets	<u>\$ 44,465,094</u>	<u>\$ 43,625,660</u>

**Condensed Statements of Revenues, Expenses
And Changes in Net Assets**

Operating revenues	\$ 31,495,841	\$ 31,851,185
Operating expenses	28,250,732	29,375,342
Operating income	3,245,109	2,475,843
Investment income	82,333	53,347
Interest expense	(352,876)	(289,569)
Excess before special items	2,974,566	2,239,621
Special items - loss on disposal of legacy meters	(2,135,132)	-
Change in net assets	839,434	2,239,621
Net assets, beginning of period	<u>43,625,660</u>	<u>41,386,039</u>
Net assets, end of period	<u>\$ 44,465,094</u>	<u>\$ 43,625,660</u>

Bryan Texas Utilities
Rural Electric System
Management's Discussion and Analysis - continued
For the Fiscal Years Ended September 30, 2012 and 2011
(Unaudited)

Financial Highlights

- Rural Electric System retail customer base totaled 16,881 and 16,033 customers at September 30, 2012 and 2011, respectively, an increase of 5.3%.
- Retail energy sales were 339,800 MWh and 358,080 MWh during the fiscal years ended September 30, 2012 and 2011, respectively, a decrease of 5.1%, due primarily to more normal weather during the fiscal year ended September 30, 2012. The fiscal year ended September 30, 2011, experienced more weather extremes than typical.
- Operating revenues for fiscal years ended September 30, 2012 and 2011 were \$31,495,841 and \$31,851,185, respectively, a decrease of 1.1%. The decrease is primarily attributable to lower retail sales in 2012 as described above.
- Operating expenses for the fiscal years ended September 30, 2012 and 2011 were \$28,250,732 and \$29,375,342, respectively, a decrease of 3.8%. The decrease was primarily due to lower purchased power expense in 2012 due to decreased sales as described above.
- Net assets for the fiscal years ended September 30, 2012 and 2011 were \$44,465,094 and \$43,625,660, respectively. The increase of 1.9% was the result of further expansion of the distribution system.

Capital Assets

The Rural Electric System net utility plant was \$46,057,221 and \$41,865,079 for the fiscal years ended September 30, 2012 and 2011, respectively, an increase of 10.0%. The increase in capital assets is primarily the result of construction expenditures supporting new customer growth.

Long-Term Debt

On June 28, 2011, the Rural Electric System issued revenue bonds ("2011 Bonds") totaling \$3,045,000. The 2011 Bonds mature serially on July 1, 2012, through July 1, 2021, with coupon rates ranging from 2.00% to 4.00%. The proceeds from the sale of the 2011 Bonds are restricted to costs associated with the implementation of automated metering equipment.

General Trends and Significant Events

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.

Automated Metering Infrastructure –

- During 2012, BTU completed the installation phase of Automated Metering Infrastructure (AMI). Over 16,000 AMI meters were installed in BTU's Rural service territory allowing remote meter readings, service turn-ons and service turn-offs. Reflected in the Statement of Revenues, Expenses and Changes in Net Assets is the write off of the book values of legacy meters totaling \$2,135,132.

Bryan Texas Utilities
Rural Electric System
Management's Discussion and Analysis - continued
For the Fiscal Years Ended September 30, 2012 and 2011
(Unaudited)

Rates –

- On October 1, 2011, BTU implemented phase one of a two phase wholesale electric rate adjustment billable to the Rural Electric System. Simultaneously, the Rural Electric System implemented new electric rates for its retail customers. The new Rural Electric System wholesale rate payable to the City Electric System reflected an overall 2.9% reduction from prior rates. The new Rural Electric System retail rates reflect an 8.7% increase in base rates which was partially offset by a reduction in fuel rates.

Subsequent Events

On October 1, 2012, the City Electric System implemented phase two of a two phase wholesale electric rate adjustment billable to the Rural Electric System. Simultaneously, the Rural Electric System implemented phase two electric rates for its retail customers. The new Rural Electric System wholesale rate payable to the City Electric System reflected an overall 3.1% reduction from prior rates. The new Rural Electric System phase two rates reflect a 10.1% increase in base rates which were largely offset by a reduction in fuel rates. BTU had an over-recovered fuel balance of \$4,106,642 at September 30, 2012. Overall, the new October 1, 2012 combined base and fuel retail rates reflect a 0.2% increase from phase one rates.

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.

BTU Group Managers:

Randy Trimble
David Werley

BTU Interim General Manager:

Gary Miller

City of Bryan:

Kean Register, City Manager
Joe Hegwood, Chief Financial Officer

Bryan Texas Utilities
Rural Electric System
 Statements of Net Assets
 At September 30, 2012 and 2011

	September 30,	
<u>Assets</u>	2012	2011
Current assets:		
Cash and cash equivalents	\$ 5,676,052	\$ 4,528,007
Accounts receivable	3,592,053	3,768,573
Less allowance for uncollectible accounts	(165,915)	(163,366)
Total current assets	9,102,190	8,133,214
Non-current assets:		
Restricted cash and cash equivalents	2,634,008	7,902,675
Restricted investments	3,001,300	3,003,510
Capital assets	67,540,145	61,761,331
Less accumulated depreciation	(21,482,924)	(19,896,252)
Unamortized bond issuance expenses and other	365,939	449,590
Total noncurrent assets	52,058,468	53,220,854
Total assets	\$ 61,160,658	\$ 61,354,068

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, 2012 and 2011

	September 30,	
	2012	2011
<u>Liabilities</u>		
Current liabilities:		
Accounts payable	\$ 608,947	\$ 177,773
Accrued liabilities	99,443	59,987
Due to other funds	2,434,409	3,453,109
Deferred credits and other current liabilities	55,119	69,501
Total current liabilities	3,197,918	3,760,370
Current liabilities payable from restricted assets:		
Accrued interest	82,500	85,200
Over-recovered fuel	4,106,642	4,215,557
Revenue bonds - current portion	445,000	420,000
Customer deposits	777,064	710,867
Total current liabilities payable from restricted assets	5,411,206	5,431,624
Non-current liabilities:		
Revenue bonds payable	8,080,000	8,525,000
Bond premiums	6,440	11,414
Total noncurrent liabilities	8,086,440	8,536,414
Total liabilities	16,695,564	17,728,408
<u>Net Assets</u>		
Net Assets		
Invested in capital assets, net of related debt	37,779,032	38,398,598
Restricted for debt service	422,292	416,042
Unrestricted	6,263,770	4,811,020
Total net assets	\$ 44,465,094	\$ 43,625,660

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, 2012 and 2011

	FY2012	FY2011
Operating revenues:		
Electrical system	\$ 31,495,841	\$ 31,851,185
Total operating revenues	31,495,841	31,851,185
 Operating expenses:		
Personnel services	465,852	389,398
Electric operations	25,229,274	26,715,321
Maintenance	457,088	414,918
General and administrative	196,137	105,156
Depreciation	1,902,381	1,750,549
Total operating expenses	28,250,732	29,375,342
Operating income	3,245,109	2,475,843
 Non-operating revenues (expenses):		
Investment income	82,333	53,347
Interest expense	(352,876)	(289,569)
Total non-operating revenues (expenses)	(270,543)	(236,222)
Income before special items	2,974,566	2,239,621
Special items - loss on disposal of legacy meters	(2,135,132)	-
Increase in net assets	839,434	2,239,621
 Net assets, beginning of period	43,625,660	41,386,039
 Net assets, end of period	\$ 44,465,094	\$ 43,625,660

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, 2012 and 2011

	<u>FY2012</u>	<u>FY2011</u>
<u>Cash flows from operating activities</u>		
Receipts from customers	\$ 31,756,110	\$ 31,395,935
Payments to suppliers	(27,481,455)	(24,108,048)
Payments for personnel services	(426,396)	(418,344)
	<u>3,848,259</u>	<u>6,869,543</u>
Net cash provided by operating activities		
<u>Cash flows from capital and related financing activities</u>		
Purchases of capital assets	(7,284,124)	(3,773,497)
Proceeds from capital debt	-	3,045,000
Principal paid on capital debt	(420,000)	(155,000)
Interest paid on capital debt	(311,402)	(269,578)
	<u>(8,015,526)</u>	<u>(1,153,075)</u>
Net cash used by capital and related financing activities		
<u>Cash flows from investing activities</u>		
Proceeds from sales and maturities of investments	6,000,000	6,000,000
Purchases of investments	(6,027,188)	(6,019,805)
Interest and dividends received	73,833	44,891
	<u>46,645</u>	<u>25,086</u>
Net cash provided by investing activities		
Net increase (decrease) in cash and cash equivalents	(4,120,622)	5,741,554
Balance-beginning of the year	<u>12,430,682</u>	<u>6,689,128</u>
Balance-end of the year	<u>\$ 8,310,060</u>	<u>\$ 12,430,682</u>
<u>Reconciliation of ending cash balance</u>		
Cash and cash equivalents	\$ 5,676,052	\$ 4,528,007
Cash and cash equivalents – restricted	2,634,008	7,902,675
Balances-end of year	<u>\$ 8,310,060</u>	<u>\$ 12,430,682</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, 2012 and 2011

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

	<u>FY2012</u>	<u>FY2011</u>
Operating income	\$ 3,245,109	\$ 2,475,843
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation	1,902,381	1,750,549
Bad debts	57,398	25,222
Change in assets and liabilities:		
Accounts receivable	194,072	(409,089)
Accounts payable	47,659	96,794
Accrued liabilities	39,456	(28,946)
Over/(under) recovered fuel	(108,915)	2,111,268
Customer deposits	66,197	(46,161)
Due to other funds	<u>(1,595,098)</u>	<u>894,063</u>
Net cash provided by operating activities	<u>\$ 3,848,259</u>	<u>\$ 6,869,543</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, 2012 and 2011

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 the Rural Electric System (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 presents 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 the Rural Electric System 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. The Rural Electric System 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, 2012 and 2011, 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, 2012 and 2011

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, 2012 and 2011, the Rural Electric System reflected a current liability – over recovered fuel of \$4,106,642 and \$4,215,557, 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.

Special Items – Special items are those transactions or events within the control of management that are either unusual in nature or infrequent in occurrence. The Rural Electric System recognized as a special item the loss on disposal of assets related to switching out legacy meters for the AMI project. At the fiscal year ended September 30, 2012, the Rural Electric System reported a one-time special item loss of \$2,135,132, which represented the net book value of the existing meters removed from service, less any salvage proceeds.

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.

**Bryan Texas Utilities
Rural Electric System**

Notes to Financial Statements - continued
For the Fiscal Years Ended September 30, 2012 and 2011

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.

Deposits

The Rural Electric System demand deposits for the fiscal years ended September 30, 2012 and 2011 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 City of Bryan 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 and the Texas Public Funds Collateral Act. Investments authorized under the policy include the following:

- a. Direct obligations of the United States government;
- b. Debentures or discount notes issued by, guaranteed by, or for which the credit of any Federal Agencies and Instrumentalities is pledged for payment;
- c. Bonds or other interest bearing obligations for which the principal and interest are guaranteed by the full faith and credit of the United States government;
- d. Time Certificates of Deposit, insured by the Federal Deposit Insurance Corporation (FDIC) or its successor, in state or national banks or state or federally chartered savings and loan associations located within the State of Texas;
- e. Repurchase Agreements with a defined termination date of 90 days or less based upon U.S. Treasury securities collateralized at a minimum of 102%;
- f. Reverse repurchase agreements with a defined termination date of 90 days or less;
- g. Bankers Acceptances eligible for discounting with the Federal Reserve maturing within 90 days;
- h. Commercial Paper maturing within 180 days carrying a rating of A-1, P-1 or F-1;

**Bryan Texas Utilities
Rural Electric System**

Notes to Financial Statements - continued
For the Fiscal Years Ended September 30, 2012 and 2011

- i. Money Market Mutual Funds that are registered with and regulated by the Securities and Exchange Commission, are no load with a maximum stated maturity of 13 months and dollar-weighted average stated maturity of no more than 90 days;
- j. AAA-rated local government investment pools;

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

	<u>FY2012</u>	<u>FY2011</u>
Demand deposits	\$ 8,310,060	\$ 12,430,682
Investments in agency securities	3,001,300	-
Investments in treasury securities	-	3,003,510
Total	<u><u>\$ 11,311,360</u></u>	<u><u>\$ 15,434,192</u></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, 2012, BTU had the following investments:

<u>Investment Types</u>	<u>Fair Value</u>	<u>Investment Maturity (in Years)</u>		
		<u>Less Than 1</u>	<u>1 - 5</u>	<u>Greater Than 5</u>
Agency securities	\$ 3,001,300	\$ -	\$ 3,001,300	\$ -
Total fair value	<u><u>\$ 3,001,300</u></u>	<u><u>\$ -</u></u>	<u><u>\$ 3,001,300</u></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.

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.

**Bryan Texas Utilities
Rural Electric System**

Notes to Financial Statements - continued
For the Fiscal Years Ended September 30, 2012 and 2011

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 2012, cash and investments of \$11.3 million exceeded amounts required to be restricted by \$5.7 million. Amounts required to be restricted at September 30, 2012 and 2011 are as follows:

	<u>FY2012</u>	<u>FY2011</u>
Debt service	\$ 193,750	\$ 190,200
Debt reserve	311,042	311,042
Bond funds for construction	246,810	5,478,519
Over-recovered fuel	4,106,642	4,215,557
Customer deposits	<u>777,064</u>	<u>710,867</u>
Restricted cash and investments	<u><u>\$ 5,635,308</u></u>	<u><u>\$ 10,906,185</u></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, 2012.

**Bryan Texas Utilities
Rural Electric System**

Notes to Financial Statements - continued
For the Fiscal Years Ended September 30, 2012 and 2011

Capital asset activity for the fiscal year ended September 30, 2012 was as follows:

	Beginning Balance	Increases	Decreases	Ending Balance
Capital assets, not being depreciated:				
Land	\$ 111,483	\$ -	\$ -	\$ 111,483
Construction in progress	1,017,229	8,271,027	4,627,460	4,660,796
Total capital assets, not being depreciated	1,128,712	8,271,027	4,627,460	4,772,279
Capital assets, being depreciated:				
Distribution plant	60,307,707	4,605,556	2,492,214	62,421,049
General plant	324,912	21,905	-	346,817
Total capital assets, being depreciated	60,632,619	4,627,461	2,492,214	62,767,866
Less accumulated depreciation for:				
Distribution plant	19,783,107	1,877,449	315,709	21,344,847
General plant	113,145	24,932	-	138,077
Total accumulated depreciation	19,896,252	1,902,381	315,709	21,482,924
Total capital assets, being depreciated, net	40,736,367	2,725,080	2,176,505	41,284,942
Total capital assets, net	\$ 41,865,079	\$ 10,996,107	\$ 6,803,965	\$ 46,057,221

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.

During the fiscal year ended September 30, 2011, the Rural Electric System issued revenue bonds dated June 28, 2011 ("2011 Bonds") totaling \$3,045,000. The 2011 Bonds mature serially on July 1, 2012 through July 1, 2021, with coupon rates ranging from 2.00% to 4.00%. The proceeds from the sale of the 2011 Bonds are restricted for the acquisition, equipment, improvement, and expansion of the Rural Electric System.

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, 2012, there was \$8,525,000 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, 2012 and 2011

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

Year Ending September 30	Principal	Interest	Total
2013	\$ 445,000	\$ 330,000	\$ 775,000
2014	460,000	318,625	778,625
2015	475,000	306,800	781,800
2016	485,000	294,600	779,600
2017	495,000	280,625	775,625
2018-2022	2,400,000	1,136,213	3,536,213
2023-2027	1,330,000	761,806	2,091,806
2028-2032	1,655,000	428,313	2,083,313
2033-2034	780,000	56,050	836,050
	<u>\$ 8,525,000</u>	<u>\$ 3,913,032</u>	<u>\$12,438,032</u>

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, 2012.

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 2011 Bonds are satisfied with restricted funds which are reported on Rural Electric System's Statement of Net Assets as restricted for debt service. The reserve fund requirements for the Series 2008 Bonds are satisfied with insurance policies.

Long-term debt activity for the year ended September 30, 2012 was as follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Revenue Bonds - Series 2008	\$ 5,900,000	\$ -	\$ 160,000	\$ 5,740,000	\$ 165,000
Revenue Bonds - Series 2011	3,045,000	-	260,000	2,785,000	280,000
	<u>\$ 8,945,000</u>	<u>\$ -</u>	<u>\$ 420,000</u>	<u>\$ 8,525,000</u>	<u>\$ 445,000</u>

In the Statement of Revenues, Expenses and Changes in Net Assets for the fiscal years ended September 30, 2012 and 2011, interest expense in the amount of \$352,876 and \$289,569, 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, 2012 and 2011

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, 2012 and 2011, the Rural Electric System paid the City \$98,204 and \$46,622, 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 and including portions of the City of College Station, 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. Fuel rates are adjusted monthly to reflect actual cost. For the fiscal years ended September 30, 2012 and 2011, the Rural Electric System's purchased power totaled \$25,311,824 and \$24,526,558, respectively, and had payables to the City Electric System in the amount of \$2,434,409 and \$3,453,109 respectively.

7. Subsequent Events

On October 1, 2012, the City Electric System implemented phase two of a two phase wholesale electric rate adjustment billable to the Rural Electric System. Simultaneously, the Rural Electric System implemented phase two electric rates for its retail customers. The new Rural Electric System wholesale rate payable to the City Electric System reflected an overall 3.1% reduction from prior rates. The new Rural Electric System phase two retail rates reflect a 10.1% increase in base rates which were largely offset by a reduction in fuel rates. BTU had an over-recovered fuel balance of \$4,106,642 at September 30, 2012. Overall, the new October 1, 2012 combined base and fuel retail rates reflect a 0.2% increase from phase one rates.