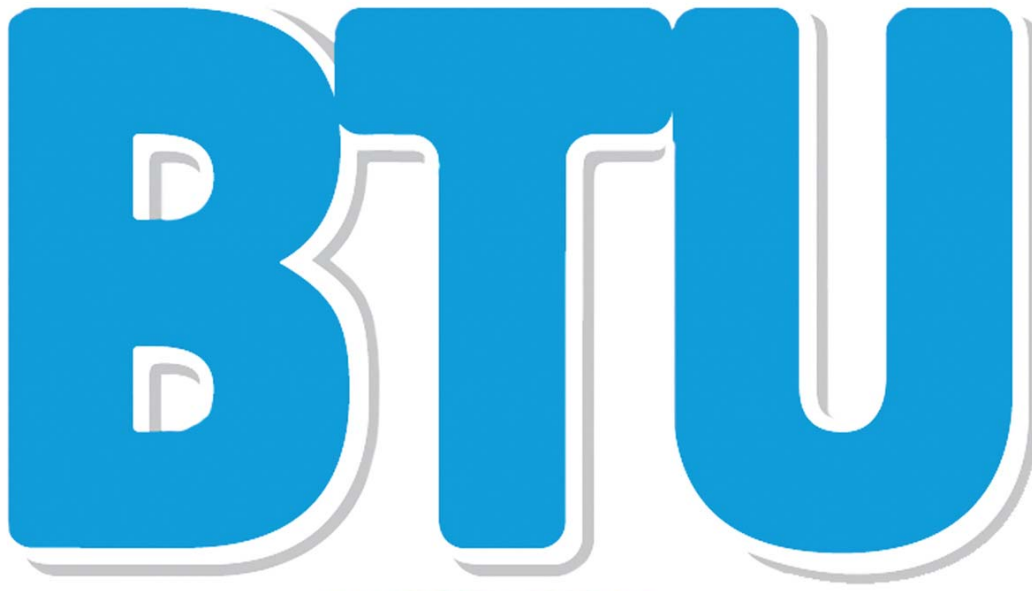


BRYAN TEXAS UTILITIES



THE DIFFERENCE IS **YOU**

Bryan Texas Utilities

City Electric System

Annual Financial Report

For the Fiscal Years Ended September 30, 2016 and 2015

Bryan Texas Utilities
City Electric System
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For the Fiscal Years Ended September 30, 2016 and 2015

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**Bryan Texas Utilities
City Electric System**

Introduction

Bryan Texas Utilities (BTU) is pleased to present its Annual Financial Report for the fiscal years ended September 30, 2016 and 2015. This report is published to provide the BTU Board of Directors (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 internal and external accounting and reporting purposes. The accompanying financial statements present only the City Electric System and its blended component unit, BTU QSE Services, Inc. (QSE), a separate legal entity. These financial statements are not intended to present the financial position or results of operations of the Rural Electric System or the City of Bryan, Texas.

The City 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 BTU 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 position, changes in net position and cash flows of the City 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 City Electric System of Bryan Texas Utilities (BTU) of the City of Bryan, Texas, as of and for the years ended September 30, 2016 and 2015, and the related notes to the financial statements, which collectively comprise City Electric System's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

BTU's management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

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 from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the City Electric System of BTU of the City of Bryan, Texas, as of September 30, 2016 and 2015, and the respective changes in financial position and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As discussed in Note 1, the financial statements present only the City Electric System of BTU, and do not purport to, and do not present fairly the financial position of the Rural Electric System of BTU, or the City of Bryan, Texas, as of September 30, 2016 and 2015, and the respective changes in their financial position and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 5-13, schedule of contributions on page 52, and the schedule of changes in the City's net pension liability and related ratios on page 53 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.

Other Information

Our audits were conducted for the purpose of forming an opinion on the financial statements that collectively comprise the City Electric System of BTU of the City of Bryan, Texas' basic financial statements. The introduction section is presented for purposes of additional analysis and is not a required part of the basic financial statements.

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

The introduction section has not been subjected to the auditing procedures applied in the audit 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
January 23, 2017

**Bryan Texas Utilities
City Electric System**

Management's Discussion and Analysis
(unaudited)

This discussion and analysis of the City Electric System financial performance provides an overview of financial activities for the fiscal years ended September 30, 2016 and 2015. 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 City Electric System and its blended component unit, BTU QSE Services, Inc. The QSE exists to perform qualified scheduling services of electrical generation for BTU according to the Electric Reliability Council of Texas (ERCOT) protocols. Although the QSE is a separate legal entity, it is considered a blended component unit and is reported as if it were a part of the City Electric System.

The financial statements are prepared using accrual accounting methods as utilized by similar business activities in the private sector. The City Electric System annual reporting period (fiscal year) ends September 30 of each year.

The Statements of Net Position include the City Electric System assets, deferred outflows of resources, liabilities, and deferred inflows of resources and provides information about the nature and amounts of investments in resources (assets) and the obligations to creditors (liabilities). They also provide the basis for the evaluation of capital structure, liquidity, and flexibility of the City Electric System.

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

The Statements of Cash Flows present cash receipts, cash disbursements and net changes in cash resulting from operating, financing and 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 City Electric System accounting policies, significant account balances and activities, material risks, obligations, commitments, contingencies and subsequent events, if any.

Bryan Texas Utilities
City Electric System
Management's Discussion and Analysis - continued
For the Fiscal Years Ended September 30, 2016, 2015, and 2014
(Unaudited)

Condensed Statements of Net Position

	September 30,		
	2016	2015	2014
Current assets	\$ 87,199,030	\$ 82,206,093	\$ 79,578,063
Capital assets, net	297,224,234	282,513,849	276,316,592
Restricted assets	89,501,234	36,642,710	49,355,577
Other	12,426,256	20,739,694	29,078,867
Total assets	<u>486,350,754</u>	<u>422,102,346</u>	<u>434,329,100</u>
Deferred outflows	18,028,336	19,834,806	16,717,295
Current liabilities	16,352,603	19,037,571	20,055,660
Current liabilities payable from restricted assets	23,353,173	21,606,636	24,542,078
Noncurrent liabilities	279,395,014	219,415,190	224,052,888
Total liabilities	<u>319,100,790</u>	<u>260,059,398</u>	<u>268,650,626</u>
Deferred inflows	2,110,548	1,303,862	844,222
Net position:			
Net investment in capital assets	116,349,514	111,918,177	112,682,327
Restricted	15,965,808	22,172,233	17,922,763
Unrestricted	50,852,430	46,483,482	50,946,456
Total net position	<u>\$ 183,167,752</u>	<u>\$ 180,573,892</u>	<u>\$ 181,551,546</u>

Bryan Texas Utilities
City Electric System
Management's Discussion and Analysis - continued
For the Fiscal Years Ended September 30, 2016, 2015, and 2014
(Unaudited)

Condensed Statements of Revenues, Expenses, and Changes in Net Position

	Fiscal Year Ended September 30,		
	2016	2015	2014
Operating revenues	\$ 187,624,655	\$ 186,223,521	\$ 183,923,241
Operating expenses	165,938,721	162,698,348	161,614,102
Operating income	21,685,934	23,525,173	22,309,139
Investment income	652,368	770,945	414,342
Interest expense	(9,351,573)	(8,761,732)	(8,486,837)
Income before operating transfers & special items	12,986,729	15,534,386	14,236,644
Special items - gain on sale of fuel oil	-	-	2,493,174
Special items - gain on sale of power plant equipment	-	505,000	-
Transfers, net	(10,392,869)	(9,881,598)	(9,266,855)
Changes in net position	2,593,860	6,157,788	7,462,963
Net position, beginning of period	180,573,892	181,551,546	174,088,583
Prior period adjustment - changes in net pension liability	-	(7,135,442)	-
Net position, beginning of period, restated	180,573,892	174,416,104	174,088,583
Net position, end of period	<u>\$ 183,167,752</u>	<u>\$ 180,573,892</u>	<u>\$ 181,551,546</u>

**Bryan Texas Utilities
City Electric System**

Management's Discussion and Analysis - continued
For the Fiscal Years Ended September 30, 2016, 2015, and 2014
(Unaudited)

Customer Count

FY2016 - The City Electric System's retail customer base of 35,716 increased by 542 customers, or 1.5%, compared to FY2015.

FY2015 - The City Electric System's retail customer base of 35,174 increased by 565 customers, or 1.6%, compared to FY2014.

Operating Revenue

FY2016 - Operating revenues of \$187,624,655 were \$1,401,134, or 0.8%, above the FY2015 total of \$186,223,521. Year over year variances in operating revenue were primarily attributable to the following activity:

	Impact (\$ millions)
Base revenue (mild weather offset impact of customer growth)	\$ (0.6)
Fuel revenue (impact of low market rates on wholesale revenues)	(3.3)
Regulatory revenue (higher rates, customer growth)	2.3
Higher transmission cost of service revenue	3.8
All other	(0.8)
Total	<u>\$ 1.4</u>

FY2015 - Operating revenues of \$186,223,521 were \$2,300,280, or 1.3%, above the FY2014 total of \$183,923,241. Year over year variances in operating revenue were primarily attributable to the following activity:

	Impact (\$ millions)
Base revenue (higher rates, customer growth, weather)	\$ 5.8
Higher transmission cost of service revenue	2.8
Regulatory revenue (higher rates, customer growth, weather)	2.5
Lower fuel revenues (wholesale & retail)	(9.5)
All other	0.7
Total	<u>\$ 2.3</u>

**Bryan Texas Utilities
City Electric System**

Management's Discussion and Analysis - continued
For the Fiscal Years Ended September 30, 2016, 2015, and 2014
(Unaudited)

Operating Expenses

FY2016 - Operating expenses of \$165,938,721 were \$3,240,373, or 2.0%, above the FY2015 total of \$162,698,348. Year over year variances in operating expenses were primarily attributable to the following activity:

	Impact (\$ millions)
Increased TMPA demand charges	\$ 2.8
Transmission cost of service increases	2.3
Lower fuel and purchased power costs	(3.3)
All other	1.4
Total	<u>\$ 3.2</u>

FY2015 - Operating expenses of \$162,698,348 were \$1,084,246, or 0.7%, above the FY2014 total of \$161,614,102. Year over year variances in operating expenses were primarily attributable to the following activity:

	Impact (\$ millions)
Higher TMPA demand charges	\$ 5.2
Transmission cost of service increases	2.5
Non-fuel generation costs	1.8
Lower fuel & purchased power costs	(9.5)
All other	1.1
Total	<u>\$ 1.1</u>

Capital Assets

FY2016 - Net utility plant at September 30, 2016, of \$297,224,234 was \$14,710,385, or 5.2%, higher than the balance of \$282,513,849 at September 30, 2015. The increase in capital assets was primarily the result of transmission and distribution construction expenditures supporting continued customer growth and reliability.

FY2015 - Net utility plant at September 30, 2015, of \$282,513,849 was \$6,197,256, or 2.2%, higher than the balance of \$276,316,593 at September 30, 2014. The increase in capital assets was primarily the result of transmission and distribution construction expenditures supporting continued customer growth and reliability.

**Bryan Texas Utilities
City Electric System**

Management's Discussion and Analysis - continued
For the Fiscal Years Ended September 30, 2016, 2015, and 2014
(Unaudited)

Net Position

FY2016 - Net position at September 30, 2016, was \$183,167,752, of which \$50,852,430 were available to meet the City Electric System's ongoing obligations. The change in net position for the fiscal year ended September 30, 2016, was \$2,593,860.

FY2015 - Net position at September 30, 2015, was \$180,573,892, of which \$46,483,482 were available to meet the City Electric System's ongoing obligations. The change in net position for the fiscal year ended September 30, 2015, was \$6,157,788.

Significant Events

Long-Term Debt -

For the fiscal year ended September 30, 2016, the City of Bryan issued general obligation refunding bonds dated July 12, 2016 ("2016 Revenue Bonds") totaling \$71,435,000 for the City Electric System. The 2016 Revenue Bonds mature serially beginning July 1, 2017, through July 1, 2041, with coupon rates ranging from 3.000% to 5.000%. The proceeds from the sale of the 2016 Revenue Bonds are restricted to acquisition or construction of improvements, additions, or extensions to the City Electric System; capital assets, facilities, and equipment incident and related to the operation, maintenance, or administration of the City Electric System; and refunding portions of City Electric System's outstanding bonds for debt service savings.

For the fiscal year ended September 30, 2015, the City of Bryan issued general obligation refunding bonds dated July 28, 2015 ("2015 Refunding Bonds") totaling \$7,735,000 for the City Electric System. The 2015 Refunding Bonds mature serially beginning August 15, 2016, through August 15, 2025, with coupon rates ranging from 2.00% to 4.00%. The proceeds from the sale of the 2015 Refunding Bonds are restricted to refunding portions of the City Electric System's outstanding debt and thus lowering its overall debt service requirements.

At September 30, 2016, there was \$212,820,000, \$33,020,000, and \$7,005,000 of City Electric System revenue bonds, certificates of obligation, and general obligation refunding bonds, respectively, outstanding payable from revenues of the City Electric System.

At September 30, 2015, there was \$161,770,000, \$34,025,000, and \$7,735,000 of City Electric System revenue bonds, certificates of obligation, and general obligation refunding bonds, respectively, outstanding payable from revenues of the City Electric System.

Rates –

On October 1, 2015, BTU implemented phase two of a three phase electric rate adjustment for the City Electric System which includes City of Bryan retail customers and the Rural Electric System wholesale rate. The three phases, effective on October 1, 2014, 2015, and 2016, will produce a 2.4% increase in base rates over three years.

Bryan Texas Utilities
City Electric System

Management's Discussion and Analysis - continued
For the Fiscal Years Ended September 30, 2016, 2015, and 2014
(Unaudited)

On October 1, 2015, the City Electric System increased the Regulatory Charge (RC) component of its rates for retail customers and the Rural Electric System wholesale rate. The RC is used to recover BTU's full cost of the Wholesale Transmission Service Charges as established by the Public Utility Commission of Texas and for other fees assessed by regulatory bodies. The City Electric System increased the RC 20% for all retail customer classes and the Rural Electric System wholesale rate to eliminate the projected under recovery of regulatory costs.

Power Supply – TMPA

In January 2016, the Board of Directors authorized a request for proposals for the sale of the Gibbons Creek Steam Electric Station ("Gibbons Creek") and the 345 kV transmission system located in Grimes, Brazos, and Robertson counties (the "Southern 345 kV Transmission System"). The Southern 345 kV Transmission System comprises approximately 25% of the TMPA transmission system. Submitted as a joint proposal, TMPA received a proposal from Clean Energy Technology Association, Inc. ("CETA") for Gibbons Creek and a proposal from GridLiance Texas Transco, LLC ("GridLiance") for the Southern 345 kV Transmission System. While the governing boards of the Member Cities and the TMPA Board of Directors have expressed interest in pursuing these proposed transactions, no definitive agreement has been signed by the parties, and details are still in the process of negotiation and resolution. In November, 2016, the Board of Directors adopted a resolution which outlined the major components of the proposed transactions. The CETA transaction would involve the sale of Gibbons Creek for a purchase price of \$57.5 million, plus an amount for working capital. In addition, CETA would provide \$35 million in funding for an environmental escrow, and provide a \$25 million letter of credit for environmental purposes. The GridLiance transaction would involve the sale of the Southern 345 kV Transmission System for net book value, plus certain additional amounts as set out in the proposed transaction documents.

In anticipation of the expiration of the TMPA Member Cities' Power Sales Contract with TMPA in 2018, TMPA and the Member Cities entered into a Joint Operating Agreement ("JOA") effective September 1, 2016. The JOA replaces the Power Sales Contract. The JOA will remain in effect until the dissolution of TMPA or termination by the Member Cities. The JOA accounts for a number of issues that were not clearly addressed in the Power Sales Contract including the separation of TMPA's generation, transmission and mining operations into distinct business categories and the ability to continue operations or dispose of each separately.

Power Supply – Other

In August 2015, during a routine inspection, BTU staff discovered a small surface crack in the Lake Bryan dam and immediately began remedial repair work. Water from Lake Bryan is used to cool BTU's Dansby 1 generating unit. Over time, the crack worsened and eventually spanned approximately 600 horizontal feet of the 17,500 feet long earthen structure. During fiscal years 2016 and 2015, the City System incurred approximately \$1.3 million and \$1.6 million, respectively, in expenses to reinforce and stabilize the dam, which are reported as maintenance expenses in the Statement of Revenues, Expenses, and Changes in Net Position. Initial stabilization work was completed in February 2016, and no subsequent degradation has been noted. BTU staff continues to regularly monitor the status of the dam. If the dam remains stable, no material future expenditures are anticipated. If the current structure degrades, or if the Texas Commission on Environmental Quality mandates remediation, additional strengthening of the dam may be required in future fiscal years and could exceed \$3,000,000.

**Bryan Texas Utilities
City Electric System**

Management's Discussion and Analysis - continued
For the Fiscal Years Ended September 30, 2016, 2015, and 2014
(Unaudited)

On October 6, 2015, following a resource planning study, BTU executed forward market power purchases for the years 2018 through 2022. Spread over five years, BTU transacted with four counterparties for the total purchase of approximately 949,000 MWh.

Transmission Construction -

During 2016, BTU completed construction of several major transmission projects. Additions include Phase 1 Atkins to Briarcrest and Nall to Rayburn Line replacements, consisting of approximately 2 miles of new and upgraded transmission lines. Also in 2016, construction was substantially completed on the System Operations Center, which will house system operations and transmission personnel. The new facilities increase system reliability and allow BTU to better serve system growth. Transmission projects in 2016 added \$5.6 million to Plant in Service in 2016.

Special Items – Asset Sales

On January 12, 2015, BTU entered a contract with KSH Services, LLC (KSH) for the sale and removal of retired power plant equipment from the Atkins generation facility. KSH paid BTU \$505,000 in consideration for the equipment which was fully depreciated on the City Electric System's Statement of Net Position. Reflected in the Statements of Revenues, Expenses, and Changes in Net Position is a gain on the transaction totaling \$505,000.

Other –

On August 11, 2016, BTU experienced an all time high summer peak load of 323MW. This was above the fiscal year 2015 summer peak load of 319MW. BTU experienced a winter peak load of 224MW on January 28, 2016, which was lower than the fiscal year 2015 winter peak load of 253MW.

On August 11, 2015, BTU experienced a summer peak load of 319MW. This was above the fiscal year 2014 summer peak load of 303MW due to extreme hot weather and the addition of Axis Pipe and Tube, a 5MW transmission level customer, in 2015. BTU experienced a winter peak load of 253MW on January 8, 2015, which was slightly lower than the fiscal year 2014 winter peak load of 259MW.

BTU did not transfer any amounts from the Rate Stabilization Fund for the fiscal years ended September 30, 2016 or 2015.

Subsequent Events

Electric Rates –

On October 1, 2016, BTU implemented phase three of a three phase electric rate adjustment for the City Electric System which includes City of Bryan retail customers and the Rural Electric System wholesale rate. Base rates have increased 2.4% over the three year phase in period.

**Bryan Texas Utilities
City Electric System**

Management's Discussion and Analysis - continued
For the Fiscal Years Ended September 30, 2016, 2015, and 2014
(Unaudited)

Power Supply Adjustment –

On October 1, 2015, the City Electric System increased the Power Supply Adjustment (PSA) component of its rates for retail customers. The PSA is used to recover fuel costs, net purchased power costs, and adjustments for the over or under recovery for such costs from preceding periods. The City Electric System increased the PSA \$0.0025/kWh (an average of 8.5%) for retail customers to eliminate the projected under recovery of fuel and purchased power costs.

Requests for Information

This financial report is designed to provide readers with a general overview of BTU's City Electric System finances. For questions concerning any of the information provided in this report or requests for additional information, contact Bryan Texas Utilities, P.O. Box 1000, Bryan, Texas 77805, or <http://www.btutilities.com/contact-us/>

BTU General Manager:
Gary Miller

BTU Group Managers:
Randy Trimble
David Werley

City of Bryan:
Kean Register, City Manager
Joe Hegwood, Chief Financial Officer
Bernie Acre, Chief Information Officer

Bryan Texas Utilities
City Electric System
Statements of Net Position
At September 30, 2016 and 2015

<u>Assets</u>	<u>2016</u>	<u>2015</u>
Current assets:		
Cash and cash equivalents	\$ 51,901,097	\$ 47,165,143
Accounts receivable	17,628,991	16,447,363
Less allowance for uncollectible accounts	(618,900)	(709,738)
Accrued interest receivable	122,690	83,618
Inventory	5,038,932	3,852,895
Due from other funds	3,672,858	4,858,109
Prepaid energy costs	8,300,717	8,300,717
Under-recovered regulatory fee	-	1,200,665
Other assets	1,152,645	1,007,321
Total current assets	87,199,030	82,206,093
Non-current assets:		
Restricted assets:		
Cash and cash equivalents	51,145,986	8,323,674
Investments	38,355,248	28,319,036
Prepaid energy costs	12,426,256	20,726,973
Capital assets	449,227,825	427,546,016
Less accumulated depreciation	(152,003,591)	(145,032,167)
Other noncurrent assets	-	12,721
Total noncurrent assets	399,151,724	339,896,253
Total assets	\$ 486,350,754	\$ 422,102,346
 <u>Deferred Outflows</u> 		
Accumulated decrease in fair value of hedging derivatives	\$ 11,909,400	\$ 17,801,026
Pensions	6,118,936	2,033,780
Total deferred outflows	\$ 18,028,336	\$ 19,834,806

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

Bryan Texas Utilities
City Electric System
Statements of Net Position - continued
At September 30, 2016 and 2015

	2016	2015
<u>Liabilities</u>		
Current liabilities:		
Accounts payable	\$ 9,259,608	\$ 10,120,562
Accrued liabilities	571,757	845,653
Due to other funds	572,056	1,461,252
Derivative financial instruments - current portion	5,234,418	6,009,018
Other current liabilities	714,764	601,087
Total current liabilities	16,352,603	19,037,572
Current liabilities payable from restricted assets:		
Accrued interest	2,332,827	2,098,535
Over-recovered fuel	4,352,049	2,173,575
Over-recovered regulatory fee	22,052	-
Bonds - current portion	12,500,000	13,240,000
Customer deposits	4,146,245	4,094,526
Total current liabilities payable from restricted assets	23,353,173	21,606,636
Non-current liabilities:		
Bonds payable	240,345,000	190,290,000
Bond premium, net	16,850,612	6,450,082
Derivative financial instruments	6,674,982	11,792,008
Net pension liability	14,584,858	10,004,206
Other post employment benefits	633,211	572,543
Other noncurrent liabilities	306,351	306,351
Total noncurrent liabilities	279,395,014	219,415,190
Total liabilities	\$ 319,100,790	\$ 260,059,398
<u>Deferred Inflows</u>		
Deferred regulatory liability	\$ 1,536,028	\$ 943,521
Pensions	574,520	360,341
Total deferred inflows	\$ 2,110,548	\$ 1,303,862
<u>Net Position</u>		
Net investment in capital assets	116,349,514	111,918,177
Restricted for:		
Debt reserve	9,216,230	10,552,883
Debt service	2,879,034	3,252,939
Rate stabilization	1,691,508	1,687,392
Collateral deposits	2,179,036	6,679,019
Unrestricted	50,852,430	46,483,482
Total net position	\$ 183,167,752	\$ 180,573,892

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

**Bryan Texas Utilities
City Electric System**

Statements of Revenues, Expenses, and Changes in Net Position
For the Fiscal Years Ended September 30, 2016 and 2015

	<u>FY2016</u>	<u>FY2015</u>
Operating revenues:		
Electrical system	\$ 186,149,563	\$ 184,252,089
Other	1,475,092	1,971,432
Total operating revenues	<u>187,624,655</u>	<u>186,223,521</u>
Operating expenses:		
Personnel services	11,380,761	10,154,424
Electric operations	125,273,722	122,456,678
Maintenance	3,185,797	4,525,063
Other services and charges	838,914	985,529
Other expenses	1,693,681	1,851,048
General and administrative	2,764,086	2,421,146
Depreciation and amortization	20,801,760	20,304,460
Total operating expenses	<u>165,938,721</u>	<u>162,698,348</u>
Operating income	21,685,934	23,525,173
Non-operating revenues (expenses):		
Investment income	652,368	770,945
Interest expense	(9,351,573)	(8,761,732)
Total non-operating revenues (expenses)	<u>(8,699,205)</u>	<u>(7,990,787)</u>
Income before operating transfers and special items	12,986,729	15,534,386
Special items - gain on sale of power plant equipment	-	505,000
Transfers:		
City of Bryan administrative payment	1,515,748	1,529,782
"Right of Way" payment to City of Bryan	(11,908,617)	(11,411,380)
Transfers, net	<u>(10,392,869)</u>	<u>(9,881,598)</u>
Change in net position	2,593,860	6,157,788
Net position, beginning of period	<u>180,573,892</u>	<u>181,551,546</u>
Prior period adjustment - changes in net pension liability	-	(7,135,442)
Net position, beginning of period, restated	<u>180,573,892</u>	<u>174,416,104</u>
Net position, end of period	<u>\$ 183,167,752</u>	<u>\$ 180,573,892</u>

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

Bryan Texas Utilities
City Electric System
Statements of Cash Flows
For the Fiscal Years Ended September 30, 2016 and 2015

	FY2016	FY2015
<u>Cash flows from operating activities</u>		
Receipts from customers	\$ 186,350,662	\$ 187,678,205
Payments to suppliers	(130,713,283)	(138,508,368)
Payments to employees	(10,770,635)	(10,102,494)
Net cash provided by operating activities	44,866,744	39,067,343
<u>Cash flows from non-capital financing activities</u>		
Operating subsidies and transfers from other funds	1,515,748	1,529,782
Operating subsidies and transfers to other funds	(11,908,617)	(11,411,380)
Net cash used by non-capital financing activities	(10,392,869)	(9,881,598)
<u>Cash flows from capital and related financing activities</u>		
Purchases of capital assets	(28,090,590)	(17,445,453)
Proceeds from capital debt	64,703,685	46,675
Principal paid on capital debt	(4,360,000)	(12,560,000)
Interest paid on capital debt	(8,854,217)	(9,804,526)
Bond issuance costs	(891,218)	(44,691)
Net cash provided by (used by) capital and related financing activities	22,507,660	(39,807,994)
<u>Cash flows from investing activities</u>		
Proceeds from sales and maturities of investments	-	2,000,000
Proceeds from sale of capital assets	-	505,000
Purchases of investments	(10,014,673)	(7,993,406)
Interest and dividends received	591,404	493,568
Net cash used by investing activities	(9,423,269)	(4,994,838)
Net increase/(decrease) in cash and cash equivalents	47,558,266	(15,617,087)
Balance-beginning of the year	55,488,817	71,105,904
Balance-end of the year	\$ 103,047,083	\$ 55,488,817
<u>Reconciliation of Ending Cash Balance</u>		
Cash and cash equivalents	\$ 51,901,097	\$ 47,165,143
Cash and cash equivalents – restricted	51,145,986	8,323,674
Balances-end of year	\$ 103,047,083	\$ 55,488,817

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

Bryan Texas Utilities
City Electric System
Statements of Cash Flows - continued
For the Fiscal Years Ended September 30, 2016 and 2015

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

	FY2016	FY2015
Operating income	\$ 21,685,934	\$ 23,525,173
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation and amortization	20,801,760	20,304,460
Bad debts	66,319	125,520
Change in assets and liabilities:		
Accounts receivable	(1,325,712)	1,332,743
Inventory	(1,186,037)	409,173
Under-recovered regulatory fee	1,200,665	(67,227)
Other assets	(145,327)	(45,895)
Deferred outflows/inflows of resources - pensions	(4,085,156)	(1,673,439)
Due from other funds	1,031,382	(920,269)
Accounts payable	764,585	(2,418,609)
Accrued liabilities	(99,549)	7,309
Over-recovered fuel	2,178,474	(3,404,415)
Over-recovered regulatory fee	22,052	-
Customer deposits	51,719	121,942
Net pension obligation and other post-employment benefits	4,794,831	1,447,684
Due to other funds	(889,196)	323,193
	\$ 44,866,744	\$ 39,067,343
Net cash provided by operating activities		

Non-cash capital and financing activities:

During the fiscal year ended September 30, 2016, the City of Bryan issued general obligation refunding bonds to refund City Electric System debt issued in 2006. Proceeds of \$8,960,085 were deposited immediately into an irrevocable trust for the defeasance of \$8,880,000 of outstanding revenue bond principal and accrued interest thereon.

During the fiscal year ended September 30, 2015, the City of Bryan issued general obligation refunding bonds to refund City Electric System debt issued in 2005. Proceeds of \$8,055,248 were deposited immediately into an irrevocable trust for the defeasance of \$7,980,000 of outstanding revenue bond principal and accrued interest thereon.

Bryan Texas Utilities
City Electric System
Notes to Financial Statements
For the Fiscal Years Ended September 30, 2016 and 2015

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 (the City). BTU operates a city and rural electric system. Each system, while operated by a common staff, is maintained separately for accounting and reporting purposes. BTU's City Electric System (the City Electric System) is the reporting entity and includes BTU's Qualified Scheduling Entity (QSE), a separate legal entity considered a blended component unit because its primary purpose is to provide a service to BTU and the BTU Board of Directors serves as the board of the QSE. The financial statements present only the City Electric System of BTU and are not intended to present the financial position of BTU's Rural Electric System or the City and the results of their operations and cash flows in conformity with generally accepted accounting principles.

The condensed combined statements of net position for the City Electric System and QSE as of September 30, 2016 are as follows:

	September 30, 2016		
	BTU City	QSE	Combined
Current assets	\$ 83,037,748	\$ 4,161,283	\$ 87,199,030
Capital assets, net	297,143,466	80,768	297,224,234
Restricted assets	89,501,234	-	89,501,234
Other	12,426,256	-	12,426,256
Total assets	482,108,704	4,242,050	486,350,754
Deferred outflows	18,028,336	-	18,028,336
Current liabilities	14,261,661	2,090,942	16,352,603
Current liabilities payable from restricted assets	23,353,173	-	23,353,173
Noncurrent liabilities	279,395,014	-	279,395,014
Total liabilities	317,009,848	2,090,942	319,100,790
Deferred inflows	2,110,548	-	2,110,548
Net position:			
Net investment in capital assets	116,268,746	80,768	116,349,514
Restricted	15,965,808	-	15,965,808
Unrestricted	48,782,090	2,070,340	50,852,430
Total net position	\$ 181,016,644	\$ 2,151,108	\$ 183,167,752

**Bryan Texas Utilities
City Electric System**

Notes to Financial Statements - continued
For the Fiscal Years Ended September 30, 2016 and 2015

The condensed combined statements of net position for the City Electric System and QSE as of September 30, 2015 are as follows:

	September 30, 2015		
	BTU City	QSE	Combined
Current assets	\$ 77,942,963	\$ 4,263,130	\$ 82,206,093
Capital assets, net	282,313,937	199,912	282,513,849
Restricted assets	36,642,710	-	36,642,710
Other	20,739,694	-	20,739,694
Total assets	<u>417,639,304</u>	<u>4,463,042</u>	<u>422,102,346</u>
Deferred outflows	19,834,806	-	19,834,806
Current liabilities	16,695,162	2,342,410	19,037,572
Current liabilities payable from restricted assets	21,606,636	-	21,606,636
Noncurrent liabilities	219,415,190	-	219,415,190
Total liabilities	<u>257,716,988</u>	<u>2,342,410</u>	<u>260,059,398</u>
Deferred inflows	1,303,862	-	1,303,862
Net position:			
Net investment in capital assets	111,718,265	199,912	111,918,177
Restricted	22,172,233	-	22,172,233
Unrestricted	44,562,762	1,920,720	46,483,482
Total net position	<u>\$ 178,453,260</u>	<u>\$ 2,120,632</u>	<u>\$ 180,573,892</u>

The condensed combined statements of revenues, expenses, and changes in net position for the City Electric System and QSE for the year ended September 30, 2016, are as follows:

	Fiscal Year Ended September 30, 2016		
	BTU City	QSE	Combined
Operating revenues	\$ 186,165,511	\$ 1,459,144	\$ 187,624,655
Operating expenses	164,479,576	1,459,144	165,938,721
Operating income	<u>21,685,934</u>	<u>-</u>	<u>21,685,934</u>
Investment income	652,368	-	652,368
Interest expense	(9,351,573)	-	(9,351,573)
Income before operating transfers & special items	<u>12,986,729</u>	<u>-</u>	<u>12,986,729</u>
Special items	-	-	-
Transfers, net	(10,392,869)	-	(10,392,869)
Changes in net position	<u>2,593,860</u>	<u>-</u>	<u>2,593,860</u>
Net position, beginning of period	<u>178,453,260</u>	<u>2,120,632</u>	<u>180,573,892</u>
Net position, end of period	<u>\$ 181,047,121</u>	<u>\$ 2,120,632</u>	<u>\$ 183,167,752</u>

**Bryan Texas Utilities
City Electric System**

Notes to Financial Statements - continued
For the Fiscal Years Ended September 30, 2016 and 2015

The condensed combined statements of revenues, expenses, and changes in net position for the City Electric System and QSE for the year ended September 30, 2015, are as follows:

	Fiscal Year Ended September 30, 2015		
	BTU City	QSE	Combined
Operating revenues	\$ 184,541,033	\$ 1,682,488	\$ 186,223,521
Operating expenses	161,015,859	1,682,488	162,698,348
Operating income	23,525,173	-	23,525,173
Investment income	770,945	-	770,945
Interest expense	(8,761,732)	-	(8,761,732)
Income before operating transfers & special items	15,534,386	-	15,534,386
Special items	505,000	-	505,000
Transfers, net	(9,881,598)	-	(9,881,598)
Changes in net position	6,157,788	-	6,157,788
Net position, beginning of period	179,430,914	2,120,632	181,551,546
Prior period adjustment	(7,135,442)	-	(7,135,442)
Net position, beginning of period, restated	172,295,472	2,120,632	174,416,104
Net position, end of period	\$ 178,453,260	\$ 2,120,632	\$ 180,573,892

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

The Statements of Revenues, Expenses and Changes in Net Position distinguish 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 City 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 City 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 City Electric System prepares its financial statements as a business-type activity in conformity with applicable pronouncements of the Governmental Accounting Standards Board (GASB).

**Bryan Texas Utilities
City Electric System**

Notes to Financial Statements - continued
For the Fiscal Years Ended September 30, 2016 and 2015

New Accounting Pronouncements, Changes in Accounting Principles, and Restatements

For the fiscal year ended September 30, 2016, the City Electric System adopted:

GASB Statement No. 72, *Fair Value Measurement and Application (GASB 72)*, addresses accounting and financial reporting issues related to fair value measurements. The definition of *fair value* is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. This Statement provides guidance for determining a fair value measurement for financial reporting purposes. This Statement also provides guidance for applying fair value to certain investments and disclosures related to all fair value measurements.

GASB Statement No. 76, *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments*. The objective of this Statement is to identify—in the context of the current governmental financial reporting environment—the hierarchy of generally accepted accounting principles (GAAP). The “GAAP hierarchy” consists of the sources of accounting principles used to prepare financial statements of state and local governmental entities in conformity with GAAP and the framework for selecting those principles. This Statement reduces the GAAP hierarchy to two categories of authoritative GAAP and addresses the use of authoritative and nonauthoritative literature in the event that the accounting treatment for a transaction or other event is not specified within a source of authoritative GAAP. This statement supersedes Statement No. 55, *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments*.

GASB Statement No. 79, *Certain External Investment Pools and Pool Participants*. This statement addresses accounting and financial reporting for certain external investment pools and pool participants. Specifically, it establishes criteria for an external investment pool to qualify for making the election to measure all of its investments at amortized cost for financial reporting purposes.

An external investment pool qualifies for that reporting if it meets all of the applicable criteria established in this Statement. The specific criteria address (1) how the external investment pool transacts with participants; (2) requirements for portfolio maturity, quality, diversification, and liquidity; and (3) calculation and requirements of a shadow price. Significant noncompliance prevents the external investment pool from measuring all of its investments at amortized cost for financial reporting purposes. Professional judgment is required to determine if instances of noncompliance with the criteria established by this Statement during the reporting period, individually or in the aggregate, were significant.

This Statement establishes additional note disclosure requirements for qualifying external investment pools that measure all of their investments at amortized cost for financial reporting purposes and for governments that participate in those pools. Those disclosures for both the qualifying external investment pools and their participants include information about any limitations or restrictions on participant withdrawals. The City Electric System participates in some investment pools and adopted this guidance in FY 2016.

**Bryan Texas Utilities
City Electric System**

Notes to Financial Statements - continued
For the Fiscal Years Ended September 30, 2016 and 2015

The following guidance issued by GASB are effective for fiscal years after FY 2016 and are expected to be applicable to the City Electric System:

GASB Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits other than Pensions (OPEB)*. The primary objective of this Statement is to improve accounting and financial reporting by state and local governments for postemployment benefits other than pensions (other postemployment benefits or OPEB). It also improves information provided by state and local governmental employers about financial support for OPEB that is provided by other entities. This Statement results from a comprehensive review of the effectiveness of existing standards of accounting and financial reporting for all postemployment benefits (pensions and OPEB) with regard to providing decision-useful information, supporting assessments of accountability and interperiod equity, and creating additional transparency.

This statement replaces the requirements of Statements No. 45, Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions, as amended, and No. 57, OPEB Measurements by Agent Employers and Agent Multiple-Employer Plans, for OPEB. Statement No. 74, Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans, establishes new accounting and financial reporting requirements for OPEB plans. This new guidance is effective for fiscal years beginning after June of 2017. Therefore, the City will adopt this guidance for FY 2018.

GASB Statement No. 82, *Pension Issues – An Amendment of GASB Statements No. 67, No. 68, and No. 73*. The objective of this Statement is to address certain issues that have been raised with respect to Statements No. 67, Financial Reporting for Pension Plans, No. 68, Accounting and Financial Reporting for Pensions, and No. 73, Accounting and Financial Reporting for Pensions and Related Assets That Are Not within the Scope of GASB Statement 68, and Amendments to Certain Provisions of GASB Statements 67 and 68. Specifically, this Statement addresses issues regarding (1) the presentation of payroll-related measures in required supplementary information, (2) the selection of assumptions and the treatment of deviations from the guidance in an Actuarial Standard of Practice for financial reporting purposes, and (3) the classification of payments made by employers to satisfy employee (plan member) contribution requirements.

Prior to the issuance of this Statement, Statements 67 and 68 required presentation of covered-employee payroll, which is the payroll of employees that are provided with pensions through the pension plan, and ratios that use that measure, in schedules of required supplementary information. This Statement amends Statements 67 and 68 to instead require the presentation of covered payroll, defined as the payroll on which contributions to a pension plan are based, and ratios that use that measure. The requirements of this statement are effective for reporting periods beginning after June 15, 2016, except for the requirements of this Statement for the selection of assumptions in a circumstance in which an employer's pension liability is measured as of a date other than the employer's most recent fiscal year-end. In that circumstance, the requirements for the selection of assumptions are effective for that employer in the first reporting period in which the measurement date of the pension liability is on or after June 15, 2017.

GASB Statement No. 83, *Certain Asset Retirement Obligations*. This statement addresses accounting and financial reporting for certain asset retirement obligations (AROs). An ARO is a legally enforceable liability associated with the retirement of a tangible capital asset. A government that has legal obligations to perform future asset retirement activities related to its tangible capital assets should recognize a liability based on the guidance in this Statement. This Statement establishes criteria for determining the timing and pattern of recognition of a liability and a corresponding deferred outflow of resources for AROs.

**Bryan Texas Utilities
City Electric System**

Notes to Financial Statements - continued
For the Fiscal Years Ended September 30, 2016 and 2015

This statement requires that recognition occur when the liability is both incurred and reasonably estimable. The determination of when the liability is incurred should be based on the occurrence of external laws, regulations, contracts, or court judgments, together with the occurrence of an internal event that obligates a government to perform asset retirement activities. Laws and regulations may require governments to take specific actions to retire certain tangible capital assets at the end of the useful lives of those capital assets, such as decommissioning nuclear reactors and dismantling and removing sewage treatment plants. Other obligations to retire tangible capital assets may arise from contracts or court judgments. Internal obligating events include the occurrence of contamination, placing into operation a tangible capital asset that is required to be retired, abandoning a tangible capital asset before it is placed into operation, or acquiring a tangible capital asset that has an existing ARO. The requirements of this Statement are effective for reporting periods beginning after June 15, 2018. Therefore, if applicable, the City will implement this guidance in FY 2019.

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.

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, deferred outflows of resources, liabilities, and deferred inflows of resources 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, Fuel Recovery, and Regulatory Recovery - Customers are billed on the basis of monthly cycle billings. At year end, the City Electric System accrues estimated unbilled revenues for the period ended September 30. The difference between fuel revenue 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, 2016 and 2015, the City Electric System reported a current liability – over recovered fuel of \$4,352,049 and \$2,173,575, respectively.

The difference between regulatory revenue billed and regulatory expense incurred is recorded as an addition or a reduction to transmission cost of service expense, with a corresponding entry to accounts payable – over recovered regulatory fee or accounts receivable – under recovered regulatory fee, whichever is appropriate. At September 30, 2016 and 2015, the City Electric System reported a current liability – over recovered regulatory fee of \$22,052 and a current asset – under recovered regulatory fee of \$1,200,665, respectively.

Prepaid Energy Costs - The Texas Municipal Power Agency's ("TMPA") rates for the purchase of electricity billed to the City Electric System are designed to cover TMPA's annual system costs including debt service costs. As further discussed in Note 10 – Texas Municipal Power Agency, during the fiscal year ended September 30, 2010, the City Electric System, along with other TMPA member cities, issued debt in their own names to refund a portion of TMPA debt and to finance certain capital improvements of TMPA. Such amounts have been accounted for as a prepayment of future energy costs on the Statements of Net Position and are amortized through 2019, the life of the associated debt. Additionally, as discussed in Note 12 – Commitments and Contingencies, in 2007, BTU entered into a purchase power agreement with a subsidiary of Shell Energy North America (U.S.), L.P. As a part of the agreement, BTU prepaid \$14,000,000 of generation capacity costs. The prepayment is being amortized over the life of the agreement which extends through December 31, 2017. The amortization of prepaid energy costs is reported on the Statements of Revenues, Expenses

**Bryan Texas Utilities
City Electric System**

Notes to Financial Statements - continued
For the Fiscal Years Ended September 30, 2016 and 2015

and Changes in Net Position in depreciation and amortization and totaled \$8,300,717 for each of the fiscal years ended September 30, 2016 and 2015.

Capital Assets - Capital assets are stated at historical cost. Also, to the extent the construction is performed by the City Electric System, the cost includes payroll and related costs and certain general and administrative expenses. Assets constructed utilizing funds collected from customers and developers as contributions of aid in construction (AIC) are also capitalized. Interest is not capitalized in these accounts because interest is recovered concurrently in the utility rate structure. Maintenance, repairs and minor renewals and 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 City 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.

Inventory - Inventory is valued at average cost and is accounted for using the consumption method.

Bond Issuance Expenses – According to the financial reporting requirements of GASB Statement No. 65, *Items Previously Reported as Assets and Liabilities*, bond issuance expenses are to be expensed as incurred. Issuance expenses are reported on the Statements of Revenues, Expenses and Changes in Net Position in interest expense and totaled \$891,219 and \$44,691 for the fiscal years ended September 30, 2016 and 2015, respectively.

Pensions - For purposes of measuring the net pension liability, deferred outflows of resources and deferred inflows of resources related to pensions, and pension expense, information about the Fiduciary Net Position of the Texas Municipal Retirement System (TMRS) and additions to/deductions from TMRS's Fiduciary Net Position have been determined using the flow of economic resources measurement focus and the full accrual basis of accounting. For this purpose, plan contributions are recognized in the period that compensation is reported for the employee, which is when contributions are legally due. Benefit payments and refunds are recognized when due and payable in accordance with the benefit terms. Investments are reported at fair value.

Deferred Regulatory Liability – To better align certain benefits received with BTU's retail rate design, the City Electric System utilizes regulatory accounting treatment for the funds it collects from customers and developers as contributions of aid in construction (AIC) under GASB Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB & AICPA Pronouncements*. The City Electric System recognizes AIC received as a deferred regulatory liability in the deferred inflows section of the Statements of Net Position. The deferred regulatory liability is amortized to depreciation expense over the life of the asset constructed.

During the fiscal years ended September 30, 2016 and 2015, the City Electric System collected \$640,508 and \$320,599, respectively, of AIC.

**Bryan Texas Utilities
City Electric System**

Notes to Financial Statements - continued
For the Fiscal Years Ended September 30, 2016 and 2015

Accrued Vacation Pay - Employees earn vacation pay at rates of 10 to 25 days per year and may accumulate an unlimited number of days, depending on their length of employment. Upon termination, the respective employees are paid for any unused accumulated vacation pay. The City Electric System accrues vacation pay when the liability is incurred.

Special Items - Special items are those transactions or events within the control of management that are either unusual in nature or infrequent in occurrence. On January 12, 2015, BTU entered a contract with KSH Services, LLC (KSH) for the sale and removal of power plant equipment from the Atkins generation facility. KSH paid BTU \$505,000 in consideration for the equipment which was fully depreciated on the City Electric System's Statement of Net Position. Reflected in the Statements of Revenues, Expenses, and Changes in Net Position is a gain on the transaction totaling \$505,000 for the year ended September 30, 2015.

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 position or ending net position as previously reported.

2. Cash and Investments

City Electric System cash managed by BTU is deposited into separate insured money market, revenue, and operating accounts in the name of the BTU City Electric System. All City Electric System cash is deposited in accounts that receive interest credit, a fee allowance, 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

State statutes require that all deposits in financial institutions be fully collateralized with depository insurance or by U.S. Government obligations or its agencies and instrumentalities; or direct obligations of Texas or its agencies and instrumentalities that have a market value of not less than the principal amount of the deposits. City Electric System demand deposits for the fiscal years ended September 30, 2016 and 2015 were held at Branch Banking & Trust Company. 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 statutes, by various City ordinances, and by City of Bryan investment policy which amplifies those guidelines and prescribes how the City Electric System will operate its investment program in accordance with applicable laws and regulations.

The City's policy, which was adopted on August 25, 2015 for the fiscal year ending September 30, 2016, 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.

**Bryan Texas Utilities
City Electric System**

Notes to Financial Statements - continued
For the Fiscal Years Ended September 30, 2016 and 2015

Investments authorized by the investment policy are those approved by the revised State of Texas Public Funds Investment Act, Chapter 2256. These investments include the following:

- a. Direct obligations of the United States government or its agencies and instrumentalities;
- 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. Direct obligations of the State of Texas or its agencies;
- d. Bonds or other obligations, the principal and interest of which is guaranteed by the full faith and credit of the United States;
- e. Certificates of Deposit issued by state and national banks within the state of Texas that are secured by obligations qualified as acceptable collateral;
- f. Bankers Acceptances eligible for discounting with the Federal Reserve maturing within 90 days;
- g. 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, F-1 or its equivalent;
- h. Fully collateralized repurchase agreements having 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;
- i. Money Market Mutual Funds that are SEC registered no-load funds with dollar-weighted average portfolio maturity of 90 days or less;
- j. Local government investment pools rated no lower than AAA or AAA-m from at least one nationally recognized rating agency;
- k. Hedging contracts and related security insurance agreements in relation to fuel oil, natural gas, coal, nuclear fuel, and electric energy to protect against loss due to price fluctuations;
- l. Reverse repurchase agreements are allowed only if the term does not exceed 90 days after delivery, and money received is used to acquire additional authorized investments with a maturity date not to exceed the expiration date stated in the agreement.

The City of Bryan's investment policy prohibits the substitution of collateral on repurchase agreements without prior approval of the City.

**Bryan Texas Utilities
City Electric System**

Notes to Financial Statements - continued
For the Fiscal Years Ended September 30, 2016 and 2015

The fair market value of the City Electric System's cash, cash equivalents and investments at September 30, 2016 and 2015 is summarized as follows:

	<u>FY2016</u>	<u>FY2015</u>
Demand deposits	\$ 100,868,047	\$ 48,809,798
Investment in government pool	3,018,172	3,008,940
Collateral deposits with counterparty	2,179,036	6,679,019
Investments in agency securities	<u>35,337,076</u>	<u>25,310,096</u>
Total	<u>\$ 141,402,331</u>	<u>\$ 83,807,853</u>

The City Electric System categorizes its fair value measurements within the fair value hierarchy established by generally accepted accounting principles. GASB Statement No. 72 provides a framework for measuring fair value which establishes a three-level fair value hierarchy that describes the inputs that are used to measure assets and liabilities.

- Level 1 inputs are quoted prices (unadjusted) for identical assets or liabilities in active markets that a government can access at the measurement date.
- Level 2 inputs are inputs—other than quoted prices included within Level 1—that are observable for an asset or liability, either directly or indirectly.
- Level 3 inputs are unobservable inputs for an asset or liability.

The fair value hierarchy gives the highest priority to Level 1 inputs and the lowest priority to Level 3 inputs. If a price for an identical asset or liability is not observable, a government should measure fair value using another valuation technique that maximizes the use of relevant observable inputs and minimizes the use of unobservable inputs. If the fair value of an asset or a liability is measured using inputs from more than one level of the fair value hierarchy, the measurement is considered to be based on the lowest priority level input that is significant to the entire measurement.

The City Electric System has recurring fair value measurements as presented in the table below. The investment balances at September 30, 2016 are as follows:

	<u>Value at FYE</u>	Fair Value Measurements		
		<u>Level 1 Inputs</u>	<u>Level 2 Inputs</u>	<u>Level 3 Inputs</u>
Investments measured at net asset value (NAV)				
Investment Pools				
TexStar	\$ 3,018,172	\$ -	\$ -	\$ -
Investments by fair value level				
U.S. Agency Bonds	<u>35,337,076</u>	<u>-</u>	<u>35,337,076</u>	<u>-</u>
Total	<u>\$ 38,355,248</u>	<u>\$ -</u>	<u>\$ 35,337,076</u>	<u>\$ -</u>

**Bryan Texas Utilities
City Electric System**

Notes to Financial Statements - continued
For the Fiscal Years Ended September 30, 2016 and 2015

The investment balances at September 30, 2015 are as follows:

	<u>Value at FYE</u>	<u>Level 1 Inputs</u>	<u>Level 2 Inputs</u>	<u>Level 3 Inputs</u>
Investments measured at net asset value (NAV)				
Investment Pools				
TexStar	\$ 3,008,940	\$ -	\$ -	\$ -
Investments by fair value level				
U.S. Agency Bonds	25,310,096	-	25,310,096	-
Total	<u>\$ 28,319,036</u>	<u>\$ -</u>	<u>\$25,310,096</u>	<u>\$ -</u>

The investment in TexStar is measured at net asset value which approximates fair value. Investments recorded at net asset value are exempt from reporting in the fair value hierarchy. U.S. Government Agency Securities classified in Level 2 of the fair value hierarchy are valued using a matrix pricing technique. Matrix pricing is used to value securities based on the securities' relationship to benchmark quoted prices.

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 the City Electric System does not hold foreign investments, foreign currency risk is not discussed.

As of September 30, 2016, the City Electric System 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>
Investments in agency securities	\$ 35,337,076	\$7,016,498	\$ 28,320,578	\$ -
Investment in government pool	3,018,172	3,018,172	-	-
Total fair value	<u>\$ 38,355,248</u>	<u>\$ 10,034,670</u>	<u>\$ 28,320,578</u>	<u>\$ -</u>

The City Electric System's investment in government pool includes deposits in TexSTAR. "TexSTAR" is a local government investment pool created and jointly managed by First Southwest Asset Management, Inc. and JPMorgan Chase Bank to invest funds on behalf of Texas political subdivisions. TexSTAR operates on a \$1.00 net asset value basis and allows same day or next day redemptions and deposits. Interest is allocated daily based on portfolio earnings and participant account balances. The City Electric System's investment in TexSTAR is stated at net asset value, which approximates fair value. The fair value of the City Electric System's investment is the same as the value of the pool shares. This pool is not managed by the City Electric System and the City Electric System does not possess securities that exist in either physical or book entry form. The investment in TexSTAR is rated AAAM by Standard and Poors. TexSTAR has a redemption notice of one day, no maximum transaction amount, and the investment pool authority cannot impose liquidity fees.

**Bryan Texas Utilities
City Electric System**

Notes to Financial Statements - continued
For the Fiscal Years Ended September 30, 2016 and 2015

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 investments to those held to maturity.

Credit Risk – As described above, it is BTU’s policy to limit its investments to high grade instruments including obligations of the United States or its agencies and commercial paper holding the top ratings issued by nationally recognized statistical rating organizations.

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 2016, cash and investments of \$141.4 million exceeded amounts required to be restricted by \$51.9 million. In 2015, cash and investments of \$83.8 million exceeded amounts required to be restricted by \$47.2 million. The City Electric System did not transfer rate stabilization funds to unrestricted assets in 2016 or 2015.

Amounts required to be restricted at September 30, 2016 and 2015 are as follows:

	<u>FY2016</u>	<u>FY2015</u>
Rate stabilization fund	\$ 1,691,508	\$ 1,687,392
Debt reserve	9,216,230	10,552,883
Debt service	5,211,861	5,351,474
Bond funds for construction	62,682,254	6,103,841
Over-recovered fuel expense	4,352,049	2,173,575
Over-recovered regulatory fee	22,052	-
Customer deposits	4,146,245	4,094,526
Collateral deposits	2,179,036	6,679,019
Restricted cash and investments	<u>\$ 89,501,234</u>	<u>\$ 36,642,710</u>

3. **Capital Assets**

General Description – At September 30, 2016, production plant included Dansby and Atkins power plants located in Brazos County, which are solely owned and operated by BTU. In total, BTU production plants include four gas-fired generating units representing 226 megawatts of available

**Bryan Texas Utilities
City Electric System**

Notes to Financial Statements - continued
For the Fiscal Years Ended September 30, 2016 and 2015

generating capacity. Other assets reflected in total capital assets include transmission, distribution and general plant facilities.

Impairments – BTU annually evaluates capital assets as required by GASB Statement No. 42, *Accounting for Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries*.

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 the City Electric System had no impaired capital assets at September 30, 2016.

Capital asset activity for the fiscal year ended September 30, 2016 was as follows:

	Beginning Balance	Increases	Decreases	Ending Balance
Capital assets, not being depreciated:				
Land	\$ 6,021,381	\$ -	\$ -	\$ 6,021,381
Construction in Progress	9,003,716	26,835,656	21,997,246	13,842,126
Retirement in Progress	317,806	752,737	873,150	197,393
Total capital assets, not being depreciated	15,342,903	27,588,393	22,870,396	20,060,900
Capital assets, being depreciated:				
Production Plant	104,406,787	3,910,060	3,173,086	105,143,761
Transmission Plant	158,626,551	5,617,707	1,423,913	162,820,345
Distribution Plant	127,464,132	9,110,871	283,256	136,291,747
General Plant (including QSE)	21,705,644	3,363,739	158,311	24,911,072
Total capital assets, being depreciated	412,203,114	22,002,377	5,038,566	429,166,925
Less accumulated depreciation for:				
Production Plant	48,283,025	2,249,240	3,022,385	47,509,880
Transmission Plant	32,259,562	4,832,608	1,632,518	35,459,652
Distribution Plant	51,882,884	4,131,468	773,293	55,241,059
General Plant (including QSE)	12,606,697	1,335,728	149,425	13,793,000
Total accumulated depreciation	145,032,168	12,549,044	5,577,621	152,003,591
Total capital assets, being depreciated, net	267,170,946	9,453,333	(539,055)	277,163,334
Total capital assets, net	\$ 282,513,849	\$ 37,041,726	\$ 22,331,341	\$ 297,224,234

Depreciation and amortization totals \$20.8 million and \$20.3 million, for the fiscal years ended September 30, 2016 and 2015, respectively, which includes \$8.3 million in both fiscal years related to amortization of prepaid energy. Cash paid for removal costs were approximately \$753,000 and \$880,000 for the years ended September 30, 2016 and 2015, respectively.

Bryan Texas Utilities
City Electric System

Notes to Financial Statements - continued
For the Fiscal Years Ended September 30, 2016 and 2015

4. Long-Term Debt

For the fiscal year ended September 30, 2016, the City of Bryan issued revenue refunding and improvement bonds dated July 12, 2016 (“2016 Revenue Bonds”) totaling \$71,435,000 for the City Electric System. The 2016 Revenue Bonds mature serially beginning July 1, 2017, through July 1, 2041, with coupon rates ranging from 3.000% to 5.000%. The proceeds from the sale of the 2016 Revenue Bonds are restricted to acquisition or construction of improvements, additions, or extensions to the City Electric System; capital assets, facilities, and equipment incident and related to the operation, maintenance, or administration of the City Electric System; and refunding portions of City Electric System’s outstanding bonds for debt service savings. Proceeds from the sale of the bonds were used to refund \$8,880,000 of the Series 2006 revenue bonds. The refunding represented debt service savings of \$1,683,252 and a net present value benefit savings of \$1,409,683.

For the fiscal year ended September 30, 2015, the City of Bryan issued general obligation refunding bonds dated July 28, 2015 (“2015 Refunding Bonds”) totaling \$7,735,000 for the City Electric System. The 2015 Refunding Bonds mature serially beginning August 15, 2016, through August 15, 2025, with coupon rates ranging from 2.00% to 4.00%. The proceeds from the sale of the 2015 Refunding Bonds are restricted to refunding portions of the City Electric System’s outstanding debt and thus lowering its overall debt service requirements. Proceeds from the sale of the bonds were used to refund \$7,980,000 of the Series 2005 revenue bonds. The refunding represented debt service savings of \$1,000,290 and a net present value benefit savings of \$909,343.

In the fiscal year-ended 2016 and prior years, the City Electric System defeased certain outstanding revenue bonds by placing the proceeds of new bonds in irrevocable trusts to provide for all future debt service payments on the old debt. Accordingly, the trust account assets and the liability for the defeased bonds are not included in the City Electric System’s financial statements. As of September 30, 2016, no City Electric System outstanding revenue bonds were defeased.

**Bryan Texas Utilities
City Electric System**

Notes to Financial Statements - continued
For the Fiscal Years Ended September 30, 2016 and 2015

Changes to long term debt during fiscal year 2016, including current portion are as follows:

	Interest Rates (%)	Series Matures	Beginning Balance	Additions	Reductions	Ending Balance	Due in One Year
<u>Revenue Bonds:</u>							
Series 2006	4.000 - 5.000	2031	\$ 9,295,000	\$ -	\$ 9,295,000	\$ -	\$ -
Series 2007	4.500 - 5.250	2032	25,665,000	-	1,000,000	24,665,000	1,050,000
Series 2008	4.000 - 5.250	2033	26,940,000	-	960,000	25,980,000	1,000,000
Series 2009	4.000 - 5.000	2034	21,025,000	-	735,000	20,290,000	765,000
Series 2010	5.000	2019	26,765,000	-	3,380,000	23,385,000	2,030,000
Series 2012	3.125 - 5.000	2037	52,080,000	-	5,015,000	47,065,000	5,510,000
Series 2016	3.000 - 5.000	2041	-	71,435,000	-	71,435,000	390,000
Total Revenue Bonds			161,770,000	71,435,000	20,385,000	212,820,000	10,745,000
<u>Certificates of Obligation:</u>							
Series 2014	2.000 - 5.000	2039	34,025,000	-	1,005,000	33,020,000	1,025,000
Total Certificates of Obligation			34,025,000	-	1,005,000	33,020,000	1,025,000
<u>General Obligation Bonds</u>							
Series 2015	2.000 - 4.000	2025	7,735,000	-	730,000	7,005,000	730,000
Total General Obligation Bonds			7,735,000	-	730,000	7,005,000	730,000
Total long-term debt			\$ 203,530,000	\$ 71,435,000	\$ 22,120,000	\$ 252,845,000	\$ 12,500,000

All net revenues of the City 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 City Electric System other than certain interest income and expense and depreciation and amortization. The bond resolutions further require that the net revenues, as defined, equal at least 1.10 times the annual debt service on all revenue bonds. The City Electric System is in compliance with these requirements at September 30, 2016 and 2015.

Under the terms of the revenue bond covenants, City Electric System is required to maintain minimum reserve fund requirements equal to approximately one year of revenue bond 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, 2009, 2010, and 2012 Bonds are satisfied with restricted funds which are reported on the City Electric System's Statements of Net Position as debt reserve. The reserve fund requirements for the Series 2007 and Series 2016 Bonds are satisfied with insurance policies. There are no reserve fund requirements for the 2014 Certificates or 2015 Refunding Bonds.

**Bryan Texas Utilities
City Electric System**

Notes to Financial Statements - continued
For the Fiscal Years Ended September 30, 2016 and 2015

Debt service requirements to maturity for the City Electric System's revenue bonds and certificates of obligation are summarized as follows:

<u>Revenue Bonds</u>			
<u>Year Ending</u>			
<u>September 30</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2017	\$ 10,745,000	\$ 9,520,244	\$ 20,265,244
2018	6,120,000	9,334,207	15,454,207
2019	28,525,000	9,076,182	37,601,182
2020	7,410,000	7,689,032	15,099,032
2021	7,770,000	7,329,219	15,099,219
2022 - 2026	40,570,000	31,029,319	71,599,319
2027 - 2031	50,300,000	20,308,600	70,608,600
2032 - 2036	39,070,000	8,521,412	47,591,412
2037 - 2041	22,310,000	2,220,600	24,530,600
Total	<u>\$ 212,820,000</u>	<u>\$ 105,028,815</u>	<u>\$ 317,848,815</u>

<u>Certificates of Obligation</u>			
<u>Year Ending</u>			
<u>September 30</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2017	\$ 1,025,000	\$ 1,082,641	\$ 2,107,641
2018	1,045,000	1,062,141	2,107,141
2019	1,070,000	1,041,241	2,111,241
2020	1,090,000	1,019,841	2,109,841
2021	1,115,000	998,041	2,113,041
2022 - 2026	6,125,000	4,420,056	10,545,056
2027 - 2031	7,190,000	3,349,854	10,539,854
2032 - 2036	8,490,000	2,054,923	10,544,923
2037 - 2039	5,870,000	450,688	6,320,688
Total	<u>\$ 33,020,000</u>	<u>\$ 15,479,426</u>	<u>\$ 48,499,426</u>

<u>General Obligation Bonds</u>			
<u>Year Ending</u>			
<u>September 30</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2017	\$ 730,000	\$ 201,225	\$ 931,225
2018	750,000	186,625	936,625
2019	725,000	167,875	892,875
2020	740,000	153,375	893,375
2021	765,000	123,775	888,775
2022 - 2025	3,295,000	258,300	3,553,300
Total	<u>\$ 7,005,000</u>	<u>\$ 1,091,175</u>	<u>\$ 8,096,175</u>

**Bryan Texas Utilities
City Electric System**

Notes to Financial Statements - continued
For the Fiscal Years Ended September 30, 2016 and 2015

<u>Total Debt</u> Year Ending September 30	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2017	\$ 12,500,000	\$ 10,804,110	\$ 23,304,110
2018	7,915,000	10,582,973	18,497,973
2019	30,320,000	10,285,298	40,605,298
2020	9,240,000	8,862,248	18,102,248
2021	9,650,000	8,451,035	18,101,035
2022 - 2026	49,990,000	35,707,675	85,697,675
2027 - 2031	57,490,000	23,658,454	81,148,454
2032 - 2036	47,560,000	10,576,335	58,136,335
2037 - 2041	28,180,000	2,671,288	30,851,288
Total	<u>\$ 252,845,000</u>	<u>\$ 121,599,416</u>	<u>\$ 374,444,416</u>

In the Statements of Revenues, Expenses and Changes in Net Position for the fiscal years ended September 30, 2016 and 2015, interest expense is recorded in the amount of \$9,351,573 and \$8,761,732, respectively, and is included as a non-operating expense.

5. Retirement Plan

BTU is an integral part of the City, and as such, provides pension benefits for all its full-time employees through the City retirement plan. The following covers the City's retirement plan as a whole, unless indicated otherwise.

Plan Description

The City of Bryan participates as one of 866 plans in the nontraditional, joint contributory, hybrid defined benefit pension plan administered by the Texas Municipal Retirement System (TMRS). TMRS is an agency created by the State of Texas and administered in accordance with the TMRS Act, Subtitle G, Title 8, Texas Government Code (the TMRS Act) as an agent multiple-employer retirement system for municipal employees in the State of Texas. The TMRS Act places the general administration and management of the System with a six-member Board of Trustees. Although the Governor, with the advice and consent of the Senate, appoints the Board, TMRS is not fiscally dependent on the State of Texas. TMRS's defined benefit pension plan is a tax-qualified plan under Section 401 (a) of the Internal Revenue Code. TMRS issues a publicly available comprehensive annual financial report (CAFR) that can be obtained at www.tmrs.com. All eligible employees of the City are required to participate in TMRS.

Benefits Provided

TMRS provides retirement, disability, and death benefits. Benefit provisions are adopted by the governing body of the City, within the options available in the state statutes governing TMRS.

At retirement, the benefit is calculated as if the sum of the employee's contributions, with interest, and the City-financed monetary credits with interest were used to purchase an annuity. Members may choose to receive their retirement benefit in one of seven payments options. Members may also

**Bryan Texas Utilities
City Electric System**

Notes to Financial Statements - continued
For the Fiscal Years Ended September 30, 2016 and 2015

choose to receive a portion of their benefit as a Partial Lump Sum Distribution in an amount equal to 12, 24, or 36 monthly payments, which cannot exceed 75% of the member's deposits and interest.

Benefits depend upon the sum of the employee's contributions to the plan, with interest, and the City-financed monetary credits, with interest. At the date the plan began, the City granted monetary credits for service rendered before the plan began of a theoretical amount equal to two times what would have been contributed by the employee, with interest, prior to establishment of the plan. Monetary credits for service since the plan began are a percent (100%, 150%, or 200%) of the employee's accumulated contributions. In addition, the City can grant, as often as annually, another type of monetary credit referred to as an updated service credit which is a theoretical amount which, when added to the employee's accumulated contributions and the monetary credits for service since the plan began, would be the total monetary credits and employee contributions accumulated with interest if the current employee contribution rate and City matching percentage had always been in existence and if the employee's salary had always been the average of his salary in the last three years that are one year before the effective date. At retirement, the benefit is calculated as if the sum of the employee's accumulated contributions with interest and the employer-financed monetary credits with interest were used to purchase an annuity.

Members can retire at ages 60 and above with 5 or more years of service or with 20 years of service regardless of age. A member is vested after 5 years. The plan provisions are adopted by the governing body of the City, within the options available in the state statutes governing TMRS and within the actuarial constraints also in the statutes.

Employees covered by benefit terms

At the December 31, 2015 valuation and measurement date, the following employees were covered by the benefit terms:

Inactive employees or beneficiaries currently receiving benefits	531
Inactive employees entitled to but not yet receiving benefits	435
Active employees	<u>858</u>
Total	1,824

Contributions

The contribution rates for employees in TMRS are either 5%, 6%, or 7% of employee gross earnings, and the City matching percentages are either 100%, 150%, or 200%, both as adopted by the governing body of the City. Under the state law governing TMRS, the contribution rate for each city is determined annually by the actuary, using the Entry Age Normal (EAN) actuarial cost method. The actuarially determined rate is the estimated amount necessary to finance the cost of benefits earned by employees during the year, with an additional amount to finance any unfunded accrued liability.

Employees for the City of Bryan were required to contribute 7% of their annual gross earnings during the fiscal year. The contribution rates for the City of Bryan were 15.50% and 15.04% in calendar

**Bryan Texas Utilities
City Electric System**

Notes to Financial Statements - continued
For the Fiscal Years Ended September 30, 2016 and 2015

years 2015 and 2016, respectively. The City's contributions to TMRS for the year ended September 30, 2016, of which \$2,149,227 represented contributions from the City Electric System, were \$8,279,509, and were equal to the required contributions.

Net Pension Liability

The City's Net Pension Liability (NPL) was measured as of December 31, 2015, and the Total Pension Liability (TPL) used to calculate the Net Pension Liability was determined by an actuarial valuation as of that date.

Actuarial assumptions:

The Total Pension Liability in the December 31, 2015 actuarial valuation was determined using the following actuarial assumptions:

Inflation	2.5% per year
Overall payroll growth	3.0% per year
Investment Rate of Return	6.75%, net of pension plan investment expense, including inflation

Salary increases were based on a service-related table. Mortality rates for active members, retirees, and beneficiaries were based on the gender-distinct RP2000 Combined Healthy Mortality Table, with male rates multiplied by 109% and female rates multiplied by 103% with a 3-year set-forward for both males and females. In addition, a 3% minimum mortality rate is applied to reflect the impairment for younger members who become disabled. The rates are projected on a fully generational basis by scale BB to account for future mortality improvements subject to the 3% floor.

Actuarial assumptions used in the December 31, 2015, valuation were based on the results of actuarial experience studies. The experience study in TMRS was for the period December 31, 2010 through December 31, 2014. Healthy post-retirement mortality rates and annuity purchase rates were updated based on a Mortality Experience Investigation Study covering 2009 through 2011, and dated December 31, 2013. These assumptions were first used in the December 31, 2013 valuation, along with a change to the Entry Age Normal (EAN) actuarial cost method. Assumptions are reviewed annually. No additional changes were made for the 2014 valuation. After the Asset Allocation Study analysis and experience investigation study, the Board amended the long-term expected rate of return on pension plan investments from 7% to 6.75%. Plan assets are managed on a total return basis with an emphasis on both capital appreciation as well as the production of income, in order to satisfy short-term and long-term funding needs of TMRS.

The long-term expected rate of return on pension plan investments was determined using a building-block method in which best estimate ranges of expected future real rates of return (expected returns, net of pension plan investment expense and inflation) are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and by adding expected inflation. In determining their best estimate of a recommended investment return assumption under the various alternative asset allocation portfolios, GRS focused on the area between (1) arithmetic mean (aggressive) without an adjustment for the time (conservative) and (2) the geometric mean (conservative) with an adjustment for time (aggressive). At its meeting on July 30, 2015, the TMRS Board approved a new portfolio target allocation.

**Bryan Texas Utilities
City Electric System**

Notes to Financial Statements - continued
For the Fiscal Years Ended September 30, 2016 and 2015

The target allocation and best estimates of real rates of return for each major asset class are summarized in the following table:

	<u>Target Allocation</u>	<u>Long-Term Expected Real Rate of Return (Arithmetic)</u>
Domestic Equity	17.5%	4.55%
International Equity	17.5%	6.10%
Core Fixed Income	10.0%	1.00%
Non-Core Fixed Income	20.0%	3.65%
Real Return	10.0%	4.03%
Real Estate	10.0%	5.00%
Absolute Return	10.0%	4.00%
Private Equity	5.0%	8.00%
Total	<u>100%</u>	

Discount Rate

The discount rate used to measure the Total Pension Liability was 6.75%. The projection of cash flows used to determine the discount rate assumed that employee and employer contributions will be made at the rates specified in statute. Based on that assumption, the pension plan's Fiduciary Net Position was projected to be available to make all projected future benefit payments of current active and inactive employees. Therefore, the long-term expected rate of return on pension plan investments was applied to all periods of projected benefit payments to determine the Total Pension Liability.

**Bryan Texas Utilities
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Notes to Financial Statements - continued
For the Fiscal Years Ended September 30, 2016 and 2015

Changes in the Net Pension Liability

	<u>Total Pension Liability (a)</u>	<u>Plan Fiduciary Net Position (b)</u>	<u>Net Pension Liability (a) - (b)</u>
Balance at 12/31/2014	\$ 275,672,153	\$ 236,784,515	\$ 38,887,638
Changes for the year:			
Service Cost	7,796,505	-	7,796,505
Interest	19,160,943	-	19,160,943
Change of benefit terms	-	-	-
Difference between expected and actual experience	(1,545,768)	-	(1,545,768)
Changes of assumptions	3,577,731	-	3,577,731
Contributions - employer	-	7,727,068	(7,727,068)
Contributions - employee	-	3,490,130	(3,490,130)
Net investment income	-	349,403	(349,403)
Benefit payments, including refunds of employee contributions	(11,685,311)	(11,685,311)	-
Administrative expense	-	(212,814)	212,814
Other changes	-	(10,511)	10,511
Net changes	17,304,100	(342,034)	17,646,134
Balance at 12/31/2015	<u>\$ 292,976,253</u>	<u>\$ 236,442,481</u>	<u>\$ 56,533,772</u>

Balance at 12/31/15 - BTU City Electric System

\$ 14,584,858

The portion of the net pension liability, deferred inflows, deferred outflows, and pension expense allocated to the City Electric System was determined by the ratio of the City Electric System contributions to TMRS as a percentage of City-wide contributions to TMRS. The ratio was approximately 26% for the year ended September 30, 2016.

Sensitivity of the net pension liability to changes in the discount rate

The following presents the net pension liability of the City Electric System, calculated using the discount rate of 6.75%, as well as what the City Electric System's net pension liability would be if it were calculated using a discount rate that is 1-percentage-point lower (5.75%) or 1-percentage-point higher (7.75%) than the current rate:

	<u>1% Decrease in Discount Rate (5.75%)</u>	<u>Discount Rate (6.75%)</u>	<u>1% Increase in Discount Rate (7.75%)</u>
City Electric System's net pension liability	\$ 25,980,265	\$ 14,584,858	\$ 5,467,698

**Bryan Texas Utilities
City Electric System**

Notes to Financial Statements - continued
For the Fiscal Years Ended September 30, 2016 and 2015

Pension Plan Fiduciary Net Position

Detailed information about the pension plan's Fiduciary Net Position is available in a separately-issued TMRS financial report. That report may be obtained on the Internet at www.tmr.com.

Pension Expense and Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions

For the year ended September 30, 2016 the City Electric System recognized pension expense of \$2,858,901.

At September 30, 2016 the City Electric System reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

	Deferred Outflows of Resources	Deferred Inflows of Resources
Differences between expected and actual economic experience	\$ -	\$ (574,520)
Changes in actuarial assumptions	722,796	-
Difference between projected and actual investment earnings	3,817,009	-
Contributions subsequent to the measurement date	1,579,131	-
Total	<u>\$ 6,118,936</u>	<u>(574,520)</u>

\$1,579,131 reported as deferred outflows of resources related to pensions resulting from contributions subsequent to the measurement date will be recognized as a reduction of the net pension liability for the year ending September 30, 2017. Other amounts reported as deferred outflows and inflows of resources related to pensions will be recognized in pension expense as follows:

	<u>Year Ended December 31</u>
2017	\$ 1,010,234
2018	1,010,234
2019	1,042,727
2020	902,090
2021	-
Thereafter	-
Total	<u>\$ 3,965,285</u>

6. Other Post-Employment Benefits

Effective January 1, 1991, by action of the City Council, the City began offering post-retirement health care benefits to employees. Effective January 1, 1993, retiree spouses were granted eligibility for benefits. Dependents were granted eligibility effective January 1, 1994. This plan is a single employer defined benefit, other post-employment benefit plan. A separate, audited GAAP-basis post-employment benefit plan report is not available.

To qualify for healthcare an employee must be at least 60 years of age and have five years of TMRS service credit or have at least 20 years of service credit. In order to be eligible, employees must elect

**Bryan Texas Utilities
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Notes to Financial Statements - continued
For the Fiscal Years Ended September 30, 2016 and 2015

to retire at time of separation, must elect in writing to continue health benefits coverage at the time of separation, and must pay the appropriate premium. Coverage can continue for life.

Employees terminating before normal retirement conditions are not eligible for retiree health coverage. Employees who retire under a disability retirement are not eligible for retiree health coverage.

Eligible retirees may continue health insurance benefits for eligible spouses and dependents covered at the time of retirement. A dependent not covered under the plan at this time is not eligible for coverage. If the retiree elects to continue coverage for any dependent and on any subsequent date elects to discontinue coverage, the dependent is no longer eligible for coverage.

Survivors of employees who die while actively employed are not eligible for retiree health coverage. However, surviving spouses and dependents of Texas public officers (as defined by Texas Government Code, Chapter 615) killed in the line of duty are entitled to purchase continued health insurance benefits. The surviving spouse is entitled to continue to purchase health insurance coverage until the date the surviving spouse becomes eligible for federal Medicare benefits. Surviving dependent minor children are entitled to continue health insurance coverage until the dependent reaches the age of 18 years or a later date to the extent required by state or federal law. A surviving dependent who is not a minor child is entitled to continue health insurance coverage until the earlier of: (1) the date the dependent becomes eligible for group health insurance through another employer or (2) the date the dependent becomes eligible for federal Medicare benefits. Eligible survivors are entitled to purchase the continued coverage at the group rate for that coverage that exists at the time of payment.

Surviving covered spouses and dependents of deceased retired employees may continue health care coverage for up to 36 months through COBRA.

Once the retiree or spouse is enrolled in Medicare, the City's plan becomes the secondary payer. Retiree is responsible for payment of any Medicare premiums. The City does not provide any cash payment in lieu of electing the City's health care plan. Retirees who do not elect to continue coverage at time of separation are not eligible to opt back in.

The City does not offer life insurance coverage for retirees or their dependents. Employees who retire are eligible to convert their group life insurance coverage to a Whole Life Policy without accidental death and dismemberment until the employee reaches age 100 or a Group Term Life with AD&D until the employee reaches age 70.

The City's health care plan includes medical, dental, and prescription coverage. Retiree health plan coverage is the same as coverage provided to active City employees in accordance with the terms and conditions of the current City of Bryan Health Plan. The City also offers a fully insured optional vision plan that retirees and their dependents may purchase. The City reserves the right to modify premium amounts, to modify eligibility requirements and to modify or discontinue retiree health benefits.

During the year ended September 30, 2016, retirees paid \$582,645 in premiums and \$1,231,508 in claims were paid for post-retirement health care and administrative charges. As of September 30, 2016, the City has 32 retirees, 40 retirees and spouses, 8 retirees and families and 4 retirees and child(ren) participating in the health plan, out of the 419 employees eligible to participate upon retirement. Expenses are recognized as retirees submit claims.

**Bryan Texas Utilities
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Notes to Financial Statements - continued
For the Fiscal Years Ended September 30, 2016 and 2015

The City also provides health benefits as required by the Federal Government under the Consolidated Omnibus Budget Reconciliation Act of 1985 (“COBRA”). COBRA requires employers that sponsor group health plans to provide continuation of group coverage to employees and their dependents under certain circumstances where coverage would otherwise end. Terminated employees who qualify under COBRA pay premium costs for themselves and dependents.

Expenses are recognized as claims when submitted. COBRA participants are reimbursed at the same levels as active employees. Participants paid premiums of \$17,817 and incurred claims and administrative expenses of \$24,845 during the year ended September 30, 2016. As of September 30, 2016, the City has 1 COBRA participant.

Future year estimated claims for all health plan participants are actuarially determined by the reinsurer. All assets of the Employee Benefits Trust Fund are available for future claim payments for health plan participants.

Prior to January 1, 2010, all retirees electing health plan coverage received a health premium subsidy averaging 40%. Beginning January 1, 2010, the City implemented new eligibility requirements for subsidized retiree premiums. The new eligibility requirements require retirees to meet the ‘Rule of 80’ (sum of age plus years of service at retirement must equal to at least 80), in order to receive the subsidized retiree premium. Retirees not meeting the ‘Rule of 80’ may still elect the City’s retiree health plan coverage, but will not receive a subsidy.

The Governmental Accounting Standards Board (GASB) issued GASB Statement No. 45, *Accounting and Financial Reporting for Employers for Postemployment Benefits Other than Pensions*, which establishes standards for the measurement, recognition and display of other postemployment benefit expenditures and related liabilities, and note disclosures in the financial report. Basically, public-sector employers must accrue the cost of other postemployment benefits (OPEB) over the active service life of benefiting employees. This statement was effective for the City for the fiscal year ending September 30, 2008.

Funding Policy and Annual OPEB Cost

The City’s annual other post-employment benefits (OPEB) cost is calculated based on the annual required contribution of the employer (ARC), an amount actuarially determined in accordance with the parameter of GASB Statement No. 45. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and to amortize any unfunded actuarial liabilities (or funding excess) over a period not to exceed thirty years. The City had its most recent OPEB valuation performed as of December 31, 2015, as required by GASB.

**Bryan Texas Utilities
City Electric System**

Notes to Financial Statements - continued
For the Fiscal Years Ended September 30, 2016 and 2015

The City's annual OPEB cost for the current year and prior two years is as follows:

	FY 2016	FY 2015	FY 2014
Annual required contribution (ARC)	\$ 920,004	\$ 900,753	\$ 874,517
Interest on OPEB obligation	120,575	126,299	96,503
Adjustment to ARC	<u>(117,460)</u>	<u>(117,015)</u>	<u>(89,409)</u>
Annual OPEB cost	923,119	910,042	881,611
Contributions made	<u>(648,865)</u>	<u>(702,316)</u>	<u>(219,484)</u>
Increase (decrease) in net OPEB obligation	274,254	207,726	662,127
Net OPEB obligation, beginning of year	<u>3,014,364</u>	<u>2,806,638</u>	<u>2,144,511</u>
Net OPEB obligation/(asset), end of year	<u><u>\$ 3,288,618</u></u>	<u><u>\$ 3,014,364</u></u>	<u><u>\$ 2,806,638</u></u>
 Net OPEB obligation/(asset), end of year - City Electric System	 <u><u>\$ 633,211</u></u>	 <u><u>\$ 572,543</u></u>	 <u><u>\$ 527,920</u></u>

The City's annual OPEB cost, the percentage of annual OPEB cost contributed to the plan and the net OPEB obligation for fiscal year ending September 30, 2015, and the preceding two fiscal years were as follows:

Fiscal Year	Annual OPEB Cost	Employer Amount Contributed	Percentage Contributed	Net OPEB Obligation
2014	\$ 881,611	\$ 219,484	24.9%	\$ 2,806,638
2015	910,042	702,316	77.2%	3,014,364
2016	923,119	648,865	70.3%	3,288,618

Funding status and funding progress

The City had actuarial valuations performed as of December 31, 2015 and December 31, 2013. The funded status of the City's retiree health care plan, under GASB Statement No. 45, is as follows:

	FY 2016	FY 2015	FY 2014
Actuarial value of plan assets	\$ -	\$ -	\$ -
Actuarial accrued liability (AAL)	11,248,356	10,704,428	10,704,428
Unfunded AAL	(11,248,356)	(10,704,428)	(10,704,428)
Funded Ratio	-	-	-
Covered Payroll	54,614,239	48,991,679	46,907,165
UAAL as a % of Covered Payroll	21%	22%	23%

Under the reporting parameters, the City's retiree health care plan is 0% funded with an estimated actuarial accrued liability exceeding actuarial assets by \$11,248,356 at December 31, 2015.

**Bryan Texas Utilities
City Electric System**

Notes to Financial Statements - continued
For the Fiscal Years Ended September 30, 2016 and 2015

Actuarial methods and assumptions

The Projected Unit Credit actuarial cost method is used to calculate the GASB ARC for the City's retiree health care plan. Using the plan benefits, the present health premiums and a set of actuarial assumptions, the anticipated future payments are projected. The entry age normal method then provides for a systematic recognition of the cost of these anticipated payments. The yearly ARC is computed to cover the cost of benefits being earned by covered members as well as to amortize a portion of the unfunded accrued liability.

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

Inflation rate	- 2.50% per annum
Investment rate of return	- 4.00%, net of expenses
Actuarial cost method	- Projected Unit Credit Cost Method
Amortization method	- Level as a percentage of employee payroll
Amortization period	- 30-year, open amortization
Payroll growth	- 3.00% per annum
Healthcare cost trend rate	- Initial rate of 7.50% declining to an ultimate rate of 4.50% after 13 years

Actuarial valuations involve estimates of the value of reported amounts and assumptions about the probability of events in the future. Amounts determined regarding the funded status and the annual required contributions of the City's retiree health care plan are subject to continual revision as actual results are compared to past expectations and new estimates are made about the future. The required schedule of funding progress presented as required supplementary information provides multiyear trend information that shows whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liability for benefits.

7. Risk Management

The City Electric System is covered for risk of losses related to general liability and workers' 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 years ended September 30, 2016 and 2015, the City Electric System paid the City \$538,668 and \$476,024, respectively, for participation in the City's risk management program.

**Bryan Texas Utilities
City Electric System**

Notes to Financial Statements - continued
For the Fiscal Years Ended September 30, 2016 and 2015

8. Financial Hedging

BTU's Energy Risk Management Policy (Risk Policy) allows for the purchase and sale of certain financial instruments defined as hedge instruments. The essential goal of the Risk Policy is to provide a framework for the operation of a fuel and energy purchasing and hedging program to better manage BTU's risk exposures in order to stabilize pricing and costs for the benefit of BTU's customers.

BTU applies GASB Statement No. 53 – *Accounting and Financial Reporting for Derivative Instruments* (“GASB 53”), which addresses the recognition, measurement, and disclosures related to derivative instruments. BTU utilizes natural gas commodity swaps to hedge its exposure to fluctuating fuel prices. Since these derivatives are entered into for risk mitigation purposes, the instruments are considered potential hedging derivative instruments under GASB 53.

In accordance with the requirements of GASB 53, the City Electric System reports all fuel hedges on the Statements of Net Position at fair value. The fair value of swap transactions is calculated as the difference between the closing futures price at the end of the reporting period, and the futures price at the time the positions were established, less applicable commissions.

BTU evaluated all potential hedging derivative instruments for effectiveness as of September 30, 2016, and determined the derivatives to be effective in substantially offsetting the changes in cash flows of the hedgeable items. BTU's hedgeable items are expected HSC natural gas purchases to serve budgeted load. BTU projects total natural gas needs as part of a 5-year forecast. This forecast is the basis for the procurement amount of the hedgeable item. BTU's potential hedging derivatives are NYMEX and HSC indexed commodity swaps. These derivatives act as cash flow hedges.

BTU utilized regression analysis to test effectiveness of its NYMEX hedges. Testing was based on the extent of correlation between historical NYMEX index and HSC natural gas prices for the prompt months of January 2003, to September 2016. The correlation coefficient of (0.8560) exceeds the minimum standard established by GASB 53 and indicates a strong linear relationship between the NYMEX and HSC prices. The calculated R² value of 0.9605 indicates that the changes in cash flows of the hedge substantially offset the changes in cash flows of the hedgeable item.

The City Electric System also utilizes HSC indexed gas commodity swaps to hedge its open exposure after a NYMEX-based swap contract month settles. The City Electric System entered into Platts Gas Daily daily swaps to hedge this exposure. These HSC indexed swaps are hedging the physical purchases of natural gas also based on the HSC index and are effective cash flow hedges under the consistent critical terms method as defined by GASB 53. The swap is for the purchase of virtually the same quantity of the hedgeable item, has zero fair value at inception, and the reference rate of the swap and the hedgeable item are the same (HSC index).

For the fiscal years ended September 30, 2016 and 2015, the total fair value of outstanding hedging derivative instruments was a net liability of \$11,909,400 and \$17,801,026, respectively. The fair value of those instruments maturing within one year are reported on the Statements of Net Position in current liabilities as derivative financial instruments and were \$5,234,418 and \$6,009,018 at September 30, 2016 and 2015, respectively. The fair value of those instruments with maturities exceeding one year are reported on the Statements of Net Position in noncurrent liabilities as derivative financial instruments and were \$6,674,982 and \$11,792,008 at September 30, 2016 and 2015, respectively.

**Bryan Texas Utilities
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Notes to Financial Statements - continued
For the Fiscal Years Ended September 30, 2016 and 2015

Hedge accounting treatment outlined in GASB 53 and GASB 63 requires changes in the fair value of derivative instruments deemed effective in offsetting changes in cash flows of hedged items be reported as deferred (inflows) outflows of resources on the Statements of Net Position. During the fiscal year ended September 30, 2016, the fair value of the City Electric System's hedging derivative instruments - NYMEX-based commodity swaps - increased by \$5,891,626; which is reported in the Statements of Net Position as a decrease of deferred outflows of resources. The deferred outflows are reported until respective contract expirations occur in conjunction with hedged expected physical fuel purchases. When fuel purchase transactions occur, the deferred balance associated with the expired fuel hedging contract is recorded as an adjustment to fuel expense. At September 30, 2016 and 2015, the deferred outflows of resources related to hedging derivatives were \$11,909,400 and \$17,801,026, respectively, and are reported on the Statements of Net Position.

The following information details the City Electric System's hedging derivative instruments as of September 30, 2016:

Type	Terms	Volume Hedged (MMBtu)	Effective Dates	Maturity Dates	Reference Index	Fair Value
Commodity Swaps	BTU pays prices of \$2.925 - 6.42	7,026,000	Sep 2010 - July 2016	Oct 2016 - Dec 2020	NYMEX	\$(11,909,400)
		7,026,000				\$(11,909,400)

The following information details the City Electric System's hedging derivative instruments as of September 30, 2015:

Type	Terms	Volume Hedged (MMBtu)	Effective Dates	Maturity Dates	Reference Index	Fair Value
Commodity Swaps	BTU pays prices of \$3.072 - 6.49	5,678,000	June 2010 - Apr 2015	Oct 2015 - Dec 2018	NYMEX	\$(17,801,026)
		5,678,000				\$(17,801,026)

The estimated fair value of the hedging derivative instruments is classified as a level 2 measurement under the hierarchy estimated by GASB 72 and are valued at the difference between the closing futures price at the end of the reporting period, and the futures price at the time the positions were established, less applicable commissions.

Fuel swap contracts represent a financial obligation to buy or sell the underlying settlement point price. If held to expiration, as is BTU's policy, the financial difference determined by mark-to-market valuation must be settled on a cash basis.

Credit Risk - BTU's hedging derivative instruments generate exposure to a certain amount of risk that could give rise to financial loss. Since current hedges have a net liability position, BTU is not exposed to counterparty credit risk. However, it is BTU's policy to require full collateralization of the fair value of derivative instruments in asset positions should the counterparty's credit ratings fall below investment grade.

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Notes to Financial Statements - continued
For the Fiscal Years Ended September 30, 2016 and 2015

Basis Risk - BTU is exposed to basis risk because the expected gas purchases being hedged will settle based on a pricing point (HSC) different than the pricing point of the hedge transactions (NYMEX). For September 2016, prompt month prices were \$2.853/MMBtu and \$2.928/MMBtu, for NYMEX and HSC, respectively.

Termination Risk - Exposure to termination risk occurs because BTU or its counterparties may terminate a derivative instrument if the other party fails to perform under the terms of the contract. BTU's fuel hedges are exchange-traded instruments, and consequently, termination risk is mitigated by rules established by NYMEX, which is governed by the Commodity Futures Trade Commission.

9. Employee Benefits

The City established the Employee Benefits Trust Fund effective October 1, 1986, covering health benefits for eligible employees. At that time the Council approved a formal trust agreement establishing the Fund. Employee premium costs are shared by the City and the employee, while dependent coverage is paid by the employee. The City's contract with its third party administrator and reinsurer sets an individual stop loss deductible in the amount of \$150,000 and a maximum aggregate stop loss deductible of \$10,002,092 for the twelve month period which began January 1, 2016 and ends December 31, 2016. These stop loss levels apply to both medical and prescription drug coverage. Prescription drug and dental coverage is not included. There were no significant reductions in insurance coverage in the current year from coverage in the prior year. For the City's aggregate stop loss coverage, there have been no settlements that have exceeded insurance coverage for the past three calendar years. However, the City has paid out \$116,383 for calendar year 2014, \$278,601 for calendar year 2015, and \$103,397 for calendar year 2016 to date in settlements that exceed insurance coverage applicable to individual stop loss coverage.

The following schedule represents the changes in claims liabilities for the year:

	FY 2016	FY 2015
Beginning balance unpaid claims	\$ 995,718	\$ 859,163
Incurred claims	8,052,689	8,047,486
Claim payments	(7,985,400)	(7,910,931)
Ending balance unpaid claims	\$ 1,063,007	\$ 995,718
Amounts due in one year	\$ 1,063,007	\$ 995,718

10. Texas Municipal Power Agency

The Texas Municipal Power Agency ("TMPA") was created in July 1975 by concurrent ordinances of the Texas cities of Bryan, Denton, Garland, and Greenville ("Member Cities") pursuant to Acts 1995 64th Leg. Ch. 143, sec 1 (the "Act"). Under the provisions of the Act, TMPA is a separate municipal corporation. TMPA is exempt from federal income tax under section 115 of the Internal Revenue Code.

TMPA operates the Gibbons Creek Steam Electric Station ("Gibbons Creek"), a coal-fired generating plant located in Grimes County, Texas with a net generating capability of 462 MW within the jurisdiction of the Electric Reliability Council of Texas (ERCOT). The plant began commercial operation October 1, 1983. Additionally, TMPA owns and operates 250 miles of transmission lines

**Bryan Texas Utilities
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Notes to Financial Statements - continued
For the Fiscal Years Ended September 30, 2016 and 2015

and 14 substations within ERCOT. TMPA also owns 10,500 acres of land adjacent to the plant previously used to mine lignite for generation.

In September 1976, TMPA entered into identical Power Sales Contracts (the “PSC”) with each of the Member Cities for the purpose of obtaining the economic advantages of jointly financing, constructing and operating large electric generating units and related facilities to supply the Member Cities’ future energy needs. Under the PSC, the Member Cities are required to pay, for the benefits received or to be received by them from such activities, an amount sufficient to recover TMPA’s operating and maintenance expenses and the Bond Fund, Reserve Fund and Contingency Fund requirements of the Revenue Bond Resolutions. In addition, the Member Cities are obligated to guarantee the payment of TMPA’s bonds and commercial paper. The PSC, as amended in 1997, is a take-or-pay contract, under which each Member City is obligated to take or pay for a specified percentage of electricity from TMPA’s generating facility. Those percentages are Bryan 21.7%; Denton 21.3%; Garland 47%; and Greenville 10%.

Effective September 1, 2016, TMPA and the Member Cities entered into a Joint Operating Agreement (the “JOA”). In general, the purposes of the JOA include: (i) funding TMPA operations such as mine reclamation, transmission service, and plant decommissioning following expiration of the PSC (ii) subject to certain exceptions, requiring Member City approval for the issuance of new debt, the execution of certain significant contracts, and the sale of property exceeding \$10 million in value (iii) specifying provisions for determining how costs of TMPA and proceeds from the sale of assets are to be allocated among the Member Cities (iv) providing for the establishment by TMPA of reserve funds for the decommissioning of the plant and the indemnification of TMPA Board Members and Member City officials, employees, contractors, and agents and (v) dividing the operations of TMPA into three business functions-mine, generation, and transmission-and requiring separate budgets and books for each business function. As of September 30, 2016, in accordance with the JOA, funds in the amount of \$1,664,000 that would have been refunded back to the Member Cities prior to the JOA will be used to fund a reserve account. The PSC provides that upon dissolution of TMPA, the assets of TMPA will automatically be transferred to the Member Cities, with each Member City receiving an undivided interest in the assets of TMPA in proportion to the amount paid by the Member City to TMPA. The JOA requires TMPA to periodically make this calculation for each business unit, and sets out formulas for making these calculations. Under the JOA, these ownership calculations are relevant not only to the allocation of assets upon dissolution of TMPA, but also to the allocation of certain proceeds from the sale of assets, and in some cases, the allocation of TMPA costs. At the request of a majority of the Member Cities, TMPA is required by the JOA to transfer a divided interest in the transmission system to each Member City. Under this partition process, the objective is for each City to receive ownership of transmission facilities in the vicinity of the Member City, and in proportion to the Member City’s ownership interest in the transmission business. Any such transfer of transmission assets must be in compliance with relevant bond covenants, including those requiring defeasance of all or a portion of transmission debt.

The JOA includes a reclamation plan for the mine, requires the development of a decommissioning plan, and sets out standards for environmental remediation. TMPA is required to comply with these plans and standards.

Under the JOA, in discharging its contractual obligations, including mine reclamation, decommissioning, transmission service, environmental remediation, indemnification, and other obligations, TMPA is rendering services to the Member Cities. The JOA obligates each Member City to pay the cost of these services, and to collect rates and charges for electric service sufficient to enable it to pay to TMPA all amounts due under the JOA for these services. A Member City’s

**Bryan Texas Utilities
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For the Fiscal Years Ended September 30, 2016 and 2015

payment obligations under the JOA are payable exclusively from such electric utility revenues, and constitute an operating expense of its electric system.

Unless terminated earlier through the mutual consent of all parties, the JOA remains in effect until the dissolution of TMPA and the winding up of its affairs.

Effective September 1, 2016, the JOA was amended. The primary purposes of the amendment were to authorize the sale of Gibbons Creek and the sale of the Southern 345 kV Transmission System, as described below, and to authorize the issuance of refunding bonds in connection with such sales.

In January 2016, the Board of Directors authorized a request for proposals for the sale of the Gibbons Creek and the 345 kV transmission system located in Grimes, Brazos, and Robertson counties (the "Southern 345 kV Transmission System"). The Southern 345 kV Transmission System comprises approximately 25% of the TMPA transmission system. Submitted as a joint proposal, TMPA received a proposal from Clean Energy Technology Association, Inc. ("CETA") for Gibbons Creek and a proposal from GridLiance Texas Transco, LLC ("GridLiance") for the Southern 345 kV Transmission System. While the governing boards of the Member Cities and the TMPA Board of Directors have expressed interest in pursuing these proposed transactions, no definitive agreement has been signed by the parties, and details are still in the process of negotiation and resolution. In November, 2016, the Board of Directors adopted a resolution which outlined the major components of the proposed transactions. The CETA transaction would involve the sale of Gibbons Creek for a purchase price of \$57.5 million, plus an amount for working capital. In addition, CETA would provide \$35 million in funding for an environmental escrow, and provide a \$25 million letter of credit for environmental purposes. The GridLiance transaction would involve the sale of the Southern 345 kV Transmission System for net book value, plus certain additional amounts as set out in the proposed transaction documents.

At September 30, 2016, BTU's portion of outstanding TMPA bonds and commercial paper was approximately \$77.3 million and \$19.3 million, respectively.

During the years ended September 30, 2016 and 2015 the City Electric System paid TMPA \$47,823,937 and \$49,561,344 respectively for power purchases and related activity under the contract. As of September 30, 2016 and 2015 the City Electric System had payables to TMPA amounting to \$1,001,817 and \$1,189,070, respectively.

The TMPA's Comprehensive Annual Financial Report for the year ended September 30, 2016 reported the following:

	FY2016
Total Assets	\$ 580,482,000
Total Deferred Outflows of Resources	843,000
Total Liabilities	548,931,000
Total Deferred Inflows of Resources	-
Total Net Position	32,394,000
Change in Net Position for year ended September 30, 2016	(\$1,682,000)

TMPA's audited financial statements may be obtained by writing TMPA, P.O. Box 7000, Bryan, TX 77805.

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Notes to Financial Statements - continued
For the Fiscal Years Ended September 30, 2016 and 2015

11. 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, administrative services, and regulatory fees are billed through purchased power and regulatory charge rates, while distribution services are direct billed. Rural purchased power and regulatory charge rates are established through City ordinance. Fuel rates are adjusted monthly to reflect actual cost. For the fiscal years ended September 30, 2016 and 2015, the Rural Electric System's purchased power, fuel, and regulatory charges were the following:

	FY2016	FY2015
Purchased power cost	\$ 16,374,791	\$ 15,878,278
Fuel cost	12,948,679	14,360,247
Regulatory charges	4,508,399	3,947,680
Total	\$ 33,831,869	\$ 34,186,175

The Rural Electric System had payables to the City Electric System, as of September 30, 2016 and 2015, in the amount of \$3,672,858 and \$4,858,109 respectively.

In addition to the \$11,908,617 and \$11,411,380 transferred to the City of Bryan for right of way in 2016 and 2015, respectively, the City Electric System paid the City of Bryan \$773,705 and \$881,813 for administrative functions performed by City personnel for the years ended September 30, 2016 and 2015, respectively. These amounts are included in the other expenses in the accompanying financial statements.

The City of Bryan transferred to City Electric System \$1,515,748 and \$1,529,782 in 2016 and 2015, respectively, for billing services performed by the City Electric System for water, wastewater and solid waste services and joint capital projects that benefited both BTU's and City of Bryan's customers.

12. Commitments and Contingencies

BTU purchase and construction commitments approximate \$322.4 million at September 30, 2016. This amount primarily includes provisions for future fuel and energy purchases.

On October 6, 2015, following a resource planning study, BTU executed forward market power purchases for the years 2018 through 2022. Spread over five years, BTU transacted with four counterparties for the total purchase of approximately 949,000 MWh.

On August 28, 2014, BTU entered into a 25 year power purchase agreement with Los Vientos Windpower, LLC, a subsidiary of Duke Energy. Under the agreement, BTU purchases 33% of the output from wind turbines with a generating capacity of 110 MW from the Los Vientos V wind project in Starr County, Texas; which began commercial operation in December, 2015.

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Notes to Financial Statements - continued
For the Fiscal Years Ended September 30, 2016 and 2015

On October 14, 2010, BTU entered into a 15 year power purchase agreement with Peñascal II Wind Power, LLC, a subsidiary of Iberdrola Renewables; now known as Avangrid Texas Renewables, LLC (Avangrid). Under the agreement, which extends from January 1, 2011 to December 31, 2025, BTU will purchase the output from wind turbines representing 30MW of generating capacity from Avangrid's existing Peñascal 2 Wind Project in Kenedy County, Texas.

On April 30, 2010, BTU entered into a 25 year power purchase agreement with Fotowatio Renewable Ventures (FRV). FRV owns and operates a photovoltaic solar power plant in Presidio County, Texas. Under the agreement, which extends from 2013 to 2037, BTU will purchase the output from the 10MW facility.

On November 16, 2007, BTU entered into a 10 year purchased power agreement with a subsidiary of Shell Energy North America (U.S.), L.P. The agreement, which extends from January 1, 2008 to December 31, 2017, allows BTU to schedule up to 50MW of energy on a day-ahead basis. Under the agreement, BTU must make specified minimum monthly non-fuel payments which are included in the \$322.4 million of purchase and construction commitments.

On August 29, 2007, BTU entered into a 10 year fixed price purchased power agreement with Credit Suisse Energy, L.L.C. (Credit Suisse) to supply energy to a wholesale customer under a corresponding 10 year fixed price full requirements sale agreement extending from January 1, 2008 to December 31, 2017. This agreement was transferred by Credit Suisse to J.P. Morgan Ventures Energy Corporation (J.P. Morgan) in January 2012. J.P. Morgan transferred the physical power transactions associated with the agreement to Mercuria Energy America, Inc. on September 1, 2015.

In August 2015, during a routine inspection, BTU staff discovered a small surface crack in the Lake Bryan dam and immediately began remedial repair work. Water from Lake Bryan is used to cool BTU's Dansby 1 generating unit. Over time, the crack worsened and eventually spanned approximately 600 horizontal feet of the 17,500 feet long earthen structure. During fiscal years 2016 and 2015, the City System incurred approximately \$1.3 million and \$1.6 million, respectively, in expenses to reinforce and stabilize the dam, which are reported as maintenance expenses in the Statement of Revenues, Expenses, and Changes in Net Position. Initial stabilization work was completed in February 2016, and no subsequent degradation has been noted. BTU staff continues to regularly monitor the status of the dam. If the dam remains stable, no material future expenditures are anticipated. If the current structure degrades, or if the Texas Commission on Environmental Quality mandates remediation, additional strengthening of the dam may be required in future fiscal years and could exceed \$3,000,000.

There is currently pending only one litigation matter in which the City Electric System is involved. In the event of an unfavorable outcome in this lawsuit, the City Electric System would be covered by insurance and the financial statements of the City Electric System would not be materially affected.

13. Subsequent Events

On October 1, 2016, BTU implemented phase three of a three phase electric rate adjustment for the City Electric System which includes City of Bryan retail customers and the Rural Electric System wholesale rate. Base rates have increased 2.4% over the three year phase in period.

**Bryan Texas Utilities
City Electric System**
Required Supplementary Information

City of Bryan Schedule of Contributions – Texas Municipal Retirement System
Last Ten Fiscal Years (will ultimately be displayed)

	2015	2016
Actuarially Determined Contribution	\$ 7,686,872	\$ 8,279,509
Contributions in relation to the actuarially determined contribution	7,686,872	8,279,509
Contribution deficiency (excess)	\$ -	\$ -
Covered employee payroll	\$ 48,991,679	\$ 54,614,239
Contributions as a percentage of employee covered payroll	15.69%	15.16%

Notes to Schedule of Contributions

For the fiscal year ended September 30, 2016, included in the City of Bryan’s contributions to TMRS of \$8,279,509, were \$2,149,227 in contributions from BTU.

Only two years of data is presented in accordance with GASB Standard No. 68 as the data for the years other than 2015 and 2016 is not available. Additionally, GASB Standard No. 68 requires that the information on this schedule correspond with the period covered as of the City's current fiscal year end of September 30, 2016.

Methods and Assumptions Used to Determine the Contribution Ratio

Acutarial Cost Method	Entry Age Normal
Amortization method	Level Percentage of Payroll, Closed
Remaining Amortization period	30 Years
Asset Valuation Method	10 Year smoothed market; 15% soft corridor
Inflation	2.5%
Salary Increases	3.5% to 10.5% including inflation
Investment Rate of Return	6.75%
Retirement Age	Experience-based table of rates that are specific to the City's plan of benefits. Last updated for the 2015 valuation pursuant to an experience study of the period 2010-2014
Mortality	RP2000 Combined Mortality Table with Blue Collar Adjustment with male rates multiplied by 109% and female rates multiplied by 109% and projected on a fully generational basis with scale BB.

Other Information

Notes: There were no benefit changes this year.

**Bryan Texas Utilities
City Electric System**
Required Supplementary Information - continued

**City of Bryan Schedule of Changes in the City's Net Pension Liability & Related Ratios –
Texas Municipal Retirement System**

Last Ten Years (will ultimately be displayed)

	2014	2015
Total Pension Liability		
Service Cost	\$ 7,088,933	\$ 7,796,505
Interest (on the Total Pension Liability)	18,281,849	19,160,943
Changes of benefit terms	-	-
Difference between expected and actual experience	(1,764,543)	(1,545,768)
Change of assumptions	-	3,577,731
Benefit payments, including refunds of employee contributions	(11,117,789)	(11,685,311)
Net Change in Total Pension Liability	12,488,450	17,304,100
Total Pension Liability - Beginning	263,183,703	275,672,153
Total Pension Liability - Ending (a)	<u>\$ 275,672,153</u>	<u>\$ 292,976,253</u>
Plan Fiduciary Net Position		
Contributions - Employer	\$ 7,667,195	\$ 7,727,068
Contributions - Employee	3,312,987	3,490,130
Net Investment Income	12,827,812	349,403
Benefit payments, including refunds of employee contributions	(11,117,789)	(11,685,311)
Administrative expense	(133,929)	(212,814)
Other	(11,011)	(10,511)
Net Change in Plan Fiduciary Net Position	12,545,265	(342,034)
Plan Fiduciary Net Position - Beginning	224,239,250	236,784,515
Plan Fiduciary Net Position - Ending (b)	<u>\$ 236,784,515</u>	<u>\$ 236,442,481</u>
Net Pension Liability - Ending (a) - (b)	\$ 38,887,638	\$ 56,533,772
Plan Fiduciary Net Position as a Percentage of Total Pension Liability	85.89%	80.70%
Covered Employee Payroll	\$ 47,328,382	\$ 49,849,779
Net Pension Liability as a Percentage of Covered Payroll	82.17%	113.41%

Notes to Schedule of Changes in the City's Net Pension Liability and Related Ratios

Only two years of data is presented in accordance with GASB Standard No. 68 as the data for the years other than calendar years 2014 and 2015 is not available. Additionally, GASB Standard No. 68 requires that the information on this schedule correspond with the period covered as of the end of December 31, 2015.

The net pension liability allocated to the City Electric System was \$14,585,006 which was determined by the ratio of the City Electric System contributions to TMRS as a percentage of City-wide contributions to TMRS. The ratio was approximately 26% for the year ended September 30, 2016.