



Bryan Texas Utilities

Rural Electric System

Annual Financial Report

For the Fiscal Years Ended September 30, 2017 and 2016

Bryan Texas Utilities
Rural Electric System
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For the Fiscal Years Ended September 30, 2017 and 2016

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**Bryan Texas Utilities
Rural Electric System**

Introduction

Bryan Texas Utilities (BTU) is pleased to present the Annual Financial Report for the fiscal years ended September 30, 2017 and 2016. 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 accounting and reporting purposes. BTU’s Rural Electric System purchases all of its energy from the City Electric System. BTU’s common staff is employed by the City Electric System and is either direct billed to the Rural Electric System or is billed through the City Electric System’s purchased power rates. Generally, all power supply, customer service and administrative services are billed through purchased power rates, while distribution services are direct billed. Rural purchased power rates are established through City of Bryan ordinance. The accompanying financial statements present only the Rural Electric System and are not intended to present the financial position or results of operations of the City Electric System or the City of Bryan, Texas.

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

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

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



Independent Auditor's Report

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

We have audited the accompanying financial statements of the Rural Electric System of Bryan Texas Utilities (BTU) of the City of Bryan, Texas, as of and for the years ended September 30, 2017 and 2016, and the related notes to the financial statements, which collectively comprise the Rural 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.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Rural Electric System of BTU of the City of Bryan, Texas, as of September 30, 2017 and 2016, and the changes in its financial position and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

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

Emphasis of Matter

As discussed in Note 1, the financial statements present only the Rural Electric System of BTU, and do not purport to, and do not present fairly the financial position of the City Electric System of BTU, or the City of Bryan, Texas, as of September 30, 2017 and 2016, 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 4-8 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 Rural 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.

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 12, 2018

**Bryan Texas Utilities
Rural Electric System**

Management's Discussion and Analysis

This discussion and analysis of the Rural Electric System financial performance provides an overview of financial activities for the years ended September 30, 2017 and 2016. Please read this information in conjunction with the accompanying financial analysis, the financial report, and the notes to financial statements.

Overview of Annual Financial Report

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

The Statements of Net Position include the Rural 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). It also provides the basis for the evaluation of capital structure, liquidity, and flexibility of the Rural Electric System.

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

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

**Bryan Texas Utilities
Rural Electric System**
Management's Discussion and Analysis - continued
For the Fiscal Years Ended September 30, 2017 and 2016

Condensed Statements of Net Position

	September 30,		
	2017	2016	2015
Current assets	\$ 11,277,991	\$ 10,917,277	\$ 11,302,049
Capital assets, net	75,591,453	70,620,151	64,415,669
Restricted assets	9,125,221	10,901,132	2,312,495
Other	-	-	7,910
Total assets	<u>95,994,665</u>	<u>92,438,560</u>	<u>78,038,123</u>
Current liabilities	3,753,116	4,872,191	5,798,256
Current liabilities payable from restricted assets	4,565,507	2,600,918	1,833,884
Noncurrent liabilities	<u>21,943,108</u>	<u>23,043,290</u>	<u>11,751,705</u>
Total liabilities	30,261,731	30,516,399	19,383,845
Deferred inflows	8,897,380	7,717,972	6,258,505
Net position:			
Net investment in capital assets	48,738,241	47,592,141	46,433,208
Restricted	572,436	566,963	450,862
Unrestricted	<u>7,524,877</u>	<u>6,045,085</u>	<u>5,511,703</u>
Total net position	<u>\$ 56,835,554</u>	<u>\$ 54,204,189</u>	<u>\$ 52,395,773</u>

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

	Fiscal Year Ended September 30,		
	2017	2016	2015
Operating revenues	\$ 44,224,725	\$ 41,931,026	\$ 39,287,075
Operating expenses	<u>40,930,733</u>	<u>39,189,303</u>	<u>35,717,091</u>
Operating income	3,293,992	2,741,723	3,569,984
Investment income	70,839	41,114	75,800
Interest expense	<u>(733,466)</u>	<u>(974,421)</u>	<u>(497,426)</u>
Change in net position	2,631,365	1,808,416	3,148,358
Net position, beginning of period	<u>54,204,189</u>	<u>52,395,773</u>	<u>49,247,415</u>
Net position, end of period	<u>\$ 56,835,554</u>	<u>\$ 54,204,189</u>	<u>\$ 52,395,773</u>

Bryan Texas Utilities
Rural Electric System
Management's Discussion and Analysis - continued
For the Fiscal Years Ended September 30, 2017 and 2016

Customer Count

FY2017 - The Rural Electric System's retail customer base of 21,121 increased by 966 customers, or 4.8%, compared to FY2016. The economy in the local area continues to grow which has caused the Rural Electric System's service load to expand; especially, in new subdivisions south of the City of College Station service area and in surrounding areas of Brazos County.

FY2016 - The Rural Electric System's retail customer base of 20,155 increased by 1,087 customers, or 5.7%, compared to FY2015. The economy in the local area continues to grow as described above.

Retail Sales

FY2017 - Retail energy sales of 407,418 MWh increased by 12,705 MWh, or 3.2%, compared to FY2016; due primarily to customer growth during the fiscal year ended September 30, 2017.

FY2016 - Retail energy sales of 394,713 MWh decreased by 10,694 MWh, or 2.6%, compared to FY2015; due primarily to milder weather during the fiscal year ended September 30, 2016.

Operating Revenue

FY2017 - Operating revenues of \$44,224,725 were \$2,293,699, or 5.5%, above the FY2016 total of \$41,931,026. The increase was primarily attributable to the following activity:

	Impact (\$ millions)
Base revenue (higher rates & customer growth)	\$ 1.6
Fuel revenue (customer growth)	0.5
Regulatory revenue (customer growth)	0.2
Total	\$ 2.3

FY2016 - Operating revenues of \$41,931,026 were \$2,643,951, or 6.7%, above the FY2015 total of \$39,287,075. The increase was primarily attributable to the following activity:

	Impact (\$ millions)
Base revenue (higher rates & customer growth offset mild weather)	\$ 0.3
Fuel revenue (higher rates & customer growth)	1.7
Regulatory revenue (higher rates & customer growth)	0.6
Total	\$ 2.6

**Bryan Texas Utilities
Rural Electric System**
Management's Discussion and Analysis - continued
For the Fiscal Years Ended September 30, 2017 and 2016

Operating Expenses

FY2017 - Operating expenses of \$40,930,733 were \$1,741,430, or 4.4%, above the FY2016 total of \$39,189,303. The increase was primarily attributable to the following activity:

	Impact (\$ millions)
Increased base purchased power costs	\$ 0.8
Increased fuel costs	0.5
Increased regulatory charges	0.2
All other	0.2
Total	\$ 1.7

FY2016 - Operating expenses of \$39,189,303 were \$3,472,212, or 9.7%, above the FY2015 total of \$35,717,091. The increase was primarily attributable to the following activity:

	Impact (\$ millions)
Increased base purchased power costs	\$ 0.5
Increased fuel costs	1.7
Increased regulatory charges	0.6
All other	0.7
Total	\$ 3.5

Capital Assets

FY2017 - Net utility plant at September 30, 2017, of \$75,591,453 was \$4,971,302, or 7.0%, higher than the balance of \$70,620,151 at September 30, 2016. The increase in capital assets was primarily the result of construction expenditures supporting continued customer growth.

FY2016 - Net utility plant at September 30, 2016, of \$70,620,151 was \$6,204,482, or 9.6%, higher than the balance of \$64,415,669 at September 30, 2015. The increase in capital assets was primarily the result of construction expenditures supporting continued customer growth.

Significant Events

Long-Term Debt -

The Rural Electric System did not issue debt in the fiscal year ended September 30, 2017. For the fiscal year ended September 30, 2016, the City of Bryan issued revenue refunding and improvement bonds dated July 13, 2016 ("2016 Revenue Bonds") totaling \$15,770,000 for the Rural Electric System. The 2016 Revenue Bonds mature serially beginning July 1, 2017, through July 1, 2041, with coupon rates ranging from 2.000% 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 Rural Electric System; capital assets, facilities, equipment incident and related to the operation, maintenance, or administration of the Rural Electric System; and refunding portions of Rural Electric System's outstanding bonds for debt service savings.

Bryan Texas Utilities
Rural Electric System
Management's Discussion and Analysis - continued
For the Fiscal Years Ended September 30, 2017 and 2016

Rates –

On October 1, 2015 & October 1, 2016 the City Electric System implemented phases two and three respectively of a three phase wholesale electric rate adjustment billable to the Rural Electric System. Simultaneously, the Rural Electric System implemented an electric rate adjustment for its retail customers. The three phases, effective on October 1, 2014, 2015, and 2016, were designed to produce a 9.9% increase in base rates over three years.

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.

On October 1, 2015, the Rural Electric System increased the Power Supply Adjustment (PSA) component of electric rates for its 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 Rural Electric System increased the PSA \$0.0050/kWh (16.5%) for its 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 Rural 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 Executive Directors:
Randy Trimble
David Werley

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

Bryan Texas Utilities
Rural Electric System
Statements of Net Position
At September 30, 2017 and 2016

<u>Assets</u>	<u>2017</u>	<u>2016</u>
Current assets:		
Cash and cash equivalents	\$ 6,588,707	\$ 6,277,122
Accounts receivable	4,809,712	4,608,645
Less allowance for uncollectible accounts	(120,428)	(120,581)
Under-recovered fuel	-	45,437
Under-recovered regulatory fee	-	106,654
Total current assets	11,277,991	10,917,277
Non-current assets:		
Restricted assets:		
Cash and cash equivalents	8,126,883	8,899,842
Investments	998,338	2,001,290
Capital assets	108,328,016	100,738,675
Less accumulated depreciation	(32,736,563)	(30,118,524)
Total noncurrent assets	84,716,674	81,521,283
Total assets	\$ 95,994,665	\$ 92,438,560

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

Bryan Texas Utilities
Rural Electric System
Statements of Net Position - continued
At September 30, 2017 and 2016

	2017	2016
<u>Liabilities</u>		
Current liabilities:		
Accounts payable	\$ 481,254	\$ 1,056,954
Accrued liabilities	26,437	23,862
Due to other funds	3,138,675	3,672,858
Other current liabilities	106,750	118,517
Total current liabilities	3,753,116	4,872,191
Current liabilities payable from restricted assets:		
Accrued interest	184,113	137,533
Over-recovered fuel	1,856,435	-
Over-recovered regulatory fee	49,703	-
Bonds - current portion	1,030,000	1,060,000
Customer deposits	1,445,256	1,403,385
Total current liabilities payable from restricted assets	4,565,507	2,600,918
Non-current liabilities:		
Bonds payable	20,445,000	21,475,000
Bond premiums	1,498,108	1,568,290
Total noncurrent liabilities	21,943,108	23,043,290
Total liabilities	\$ 30,261,731	\$ 30,516,399
<u>Deferred Inflows</u>		
Deferred regulatory liability	\$ 8,897,380	\$ 7,717,972
<u>Net Position</u>		
Net investment in capital assets	48,738,241	47,592,141
Restricted for debt service	572,436	566,963
Unrestricted	7,524,877	6,045,085
Total net position	\$ 56,835,554	\$ 54,204,189

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

Bryan Texas Utilities
Rural Electric System
Statements of Revenues, Expenses
And Changes in Net Position
For the Fiscal Years Ended September 30, 2017 and 2016

	FY2017	FY2016
Operating revenues:		
Electrical system	\$ 44,224,725	\$ 41,931,026
Total operating revenues	44,224,725	41,931,026
Operating expenses:		
Personnel services	534,865	596,486
Electric operations	36,417,788	34,892,666
Maintenance	900,524	876,625
General and administrative	202,965	183,038
Depreciation	2,874,591	2,640,488
Total operating expenses	40,930,733	39,189,303
Operating income	3,293,992	2,741,723
Non-operating revenues (expenses):		
Investment income	70,839	41,114
Interest expense	(733,466)	(974,421)
Total non-operating revenues (expenses)	(662,627)	(933,307)
Increase in net position	2,631,365	1,808,416
Net position, beginning of period	54,204,189	52,395,773
Net position, end of period	\$ 56,835,554	\$ 54,204,189

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

Bryan Texas Utilities
Rural Electric System
Statements of Cash Flows
For the Fiscal Years Ended September 30, 2017 and 2016

	FY2017	FY2016
<u>Cash flows from operating activities</u>		
Receipts from customers	\$ 44,084,724	\$ 42,082,486
Payments to suppliers	(35,593,351)	(35,741,500)
Payments to employees	(544,061)	(678,723)
	7,947,312	5,662,263
<u>Cash flows from capital and related financing activities</u>		
Purchases of capital assets	(7,665,410)	(7,398,544)
Proceeds from capital debt	-	12,137,346
Principal paid on capital debt	(1,060,000)	(705,000)
Interest paid on capital debt	(757,068)	(496,009)
Bond issuance costs	-	(234,396)
	(9,482,478)	3,303,397
<u>Cash flows from investing activities</u>		
Proceeds from sales and maturities of investments	1,000,000	-
Interest and dividends received	73,792	43,443
	1,073,792	43,443
Net cash provided by investing activities	1,073,792	43,443
Net increase (decrease) in cash and cash equivalents	(461,374) -	9,009,103
Balance-beginning of the year	15,176,964	6,167,861
Balance-end of the year	\$ 14,715,590	\$ 15,176,964
<u>Reconciliation of ending cash balance</u>		
Cash and cash equivalents	\$ 6,588,707	\$ 6,277,122
Cash and cash equivalents – restricted	8,126,883	8,899,842
Balances-end of year	\$ 14,715,590	\$ 15,176,964

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

Bryan Texas Utilities
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Statements of Cash Flows - continued
For the Fiscal Years Ended September 30, 2017 and 2016

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

	FY2017	FY2016
Operating income	\$ 3,293,992	\$ 2,741,723
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation	2,874,591	2,640,488
Bad debts	30,356	24,711
Change in assets and liabilities:		
Accounts receivable	(231,575)	(230,796)
Under-recovered regulatory fee	106,654	32,218
Under-recovered fuel	45,437	984,687
Accounts payable	(534,231)	508,333
Accrued liabilities	(9,196)	(82,237)
Over-recovered fuel and regulatory fees	1,906,138	-
Customer deposits	41,871	382,257
Due to other funds	423,275	(1,339,120)
	\$ 7,947,312	\$ 5,662,263
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 Rural Electric System debt issued in 2006. Proceeds of \$5,043,214 were deposited directly into an irrevocable trust for the defeasance of \$4,845,000 of outstanding revenue bond principal and accrued interest there

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

**Bryan Texas Utilities
Rural Electric System**

Notes to Financial Statements - continued
For the Fiscal Years Ended September 30, 2017 and 2016

1. Summary of Significant Accounting Policies

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

Financial Statements - The financial statements for the Rural Electric System (a proprietary fund) are reported using the economic resources measurement focus and the accrual basis of accounting. All assets, deferred outflows of resources, liabilities, and deferred inflows of resources (whether current or noncurrent) are included on the Statement of Net Position. The Statement of Revenues, Expenses and Changes in Net Position presents 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 Statement of Revenues, Expenses and Changes in Net Position distinguishes operating revenues and expenses from non-operating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. Operating expenses for the Rural Electric System include the cost of sales and services, administrative expenses and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

Basis of Accounting - The Rural Electric System is accounted for on the flow of economic resources measurement focus and uses the accrual basis of accounting. Accounting records are maintained in accordance with accounting principles generally accepted in the United States of America. The Rural Electric System prepares its financial statements as a business-type activity in conformity with applicable pronouncements of the Governmental Accounting Standards Board (GASB).

New Accounting Pronouncements, Changes in Accounting Principles and Restatements:

For the fiscal year ended September 30, 2017, the Rural Electric System did not adopt any new accounting pronouncements.

The following guidance issued by GASB is effective for years following FY 2017 and is expected to be applicable to the Rural Electric System:

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
Rural Electric System**

Notes to Financial Statements - continued
For the Fiscal Years Ended September 30, 2017 and 2016

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 Rural Electric System will implement this guidance in FY 2019.

GASB Statement No. 86, *Certain Debt Extinguishment Issues*. The primary objective of this statement is to improve consistency in accounting and financial reporting for in-substance defeasance of debt by providing guidance for transactions in which cash and other monetary assets acquired with only existing resources—resources other than the proceeds of refunding debt—are placed in an irrevocable trust for the sole purpose of extinguishing debt. This Statement also improves accounting and financial reporting for prepaid insurance on debt that is extinguished and notes to financial statements for debt that is defeased in substance. The requirements of this statement are effective for reporting periods beginning after June 15, 2017.

GASB Statement No. 87, *Leases*. The objective of this Statement is to better meet the information needs of financial statement users by improving accounting and financial reporting for leases by governments. This Statement increases the usefulness of governments' financial statements by requiring recognition of certain lease assets and liabilities for leases that previously were classified as operating leases and recognized as inflows of resources or outflows of resources based on the payment provisions of the contract. It establishes a single model for lease accounting based on the foundational principle that leases are financings of the right to use an underlying asset. Under this Statement, a lessee is required to recognize a lease liability and an intangible right-to-use lease asset, and a lessor is required to recognize a lease receivable and a deferred inflow of resources, thereby enhancing the relevance and consistency of information about governments' leasing activities. The requirements of this statement are effective for reporting periods beginning after December 15, 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 fiscal year end, the Rural Electric System accrues estimated unbilled revenues (excluding fuel). The Rural Electric System is allowed to recover purchased power cost through fuel revenue rates. The difference between fuel revenues billed and fuel expense incurred is

**Bryan Texas Utilities
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Notes to Financial Statements - continued
For the Fiscal Years Ended September 30, 2017 and 2016

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, 2017 and 2016, the Rural Electric System reflected a current liability – over-recovered fuel of \$1,856,435 and a current asset – under-recovered fuel of \$45,437, 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, 2017 and 2016, the Rural Electric System reported a current liability – over-recovered regulatory fee of \$49,703 and current asset – under-recovered regulatory fee of \$106,654, respectively.

Capital Assets - Capital assets are stated at the historical cost. Also, to the extent the construction is performed by the Rural Electric System, the cost includes payroll and related costs and certain general and administrative expenses. 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 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 33 years.

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

Bond Issuance Expenses - 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. For the fiscal year ended September 30, 2017, the Rural Electric did not incur any bond issuance costs. For the fiscal year ended September 30, 2016, the Rural Electric System incurred \$234,396 in bond issuance costs.

Deferred Regulatory Liability – To better align certain benefits received with BTU’s retail rate design, the Rural 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 Rural 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 accumulated depreciation over the life of the asset constructed.

During the fiscal years ended September 30, 2017 and 2016, the Rural Electric System collected \$1,457,451 and \$1,700,653, respectively, of AIC. The amortization of the deferred regulatory liability was \$278,043 and \$241,187 for 2017 and 2016 respectively.

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Rural Electric System**

Notes to Financial Statements - continued
For the Fiscal Years Ended September 30, 2017 and 2016

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

Rural Electric System cash is managed by BTU and deposited into separate revenue and operating accounts at the City’s depository bank in the name of the BTU Rural Electric System. All Rural Electric System cash is deposited in accounts that receive interest credit, 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. The Rural Electric System demand deposits for the fiscal years ended September 30, 2017 and 2016 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 laws, by various City ordinances, and by City of Bryan investment policy which prescribes how the Rural Electric System will operate its investment program in accordance with applicable laws and regulations.

The City’s policy, which was adopted on August 23, 2016 for the fiscal year ending September 30, 2017, sets forth (1) the basic principles governing the investment of funds; (2) the objectives of the investment program; and (3) the authority, responsibilities, limitations, documentation, and requirements to be used in the administration and operation of the investment program.

Investments authorized by the investment policy are those approved by the revised State of Texas Public Funds Investment Act, 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;

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Notes to Financial Statements - continued
For the Fiscal Years Ended September 30, 2017 and 2016

- 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.

The fair market value of the Rural Electric System’s cash, cash equivalents and investments at September 30, 2017 and 2016 are summarized as follows:

	<u>2017</u>	<u>2016</u>
Demand deposits	\$ 14,715,590	\$ 15,176,964
Investments in agency securities	998,338	2,001,290
Total	\$ 15,713,928	\$ 17,178,254

The Rural 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

**Bryan Texas Utilities
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Notes to Financial Statements - continued
For the Fiscal Years Ended September 30, 2017 and 2016

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 Rural Electric System has recurring fair value measurements as presented in the table below. The investment balances at September 30, 2017 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>
U.S. Agency Bonds	\$ 998,338	\$ -	\$ 998,338	\$ -
Total	<u>\$ 998,338</u>	<u>\$ -</u>	<u>\$ 998,338</u>	<u>\$ -</u>

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>
U.S. Agency Bonds	\$ 2,001,290	\$ -	\$ 2,001,290	\$ -
Total	<u>\$ 2,001,290</u>	<u>\$ -</u>	<u>\$ 2,001,290</u>	<u>\$ -</u>

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

As of September 30, 2017, the Rural Electric System had the following investments:

<u>Investment Types</u>	<u>Fair Value</u>	Investment Maturity (in Years)		
		<u>Less Than 1</u>	<u>1 - 5</u>	<u>Greater Than 5</u>
Investments in agency securities	\$ 998,338	\$ 998,338	\$ -	\$ -
Total fair value	<u>\$ 998,338</u>	<u>\$ 998,338</u>	<u>\$ -</u>	<u>\$ -</u>

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

**Bryan Texas Utilities
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Notes to Financial Statements - continued
For the Fiscal Years Ended September 30, 2017 and 2016

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 2017, cash and investments of \$15.7 million exceeded amounts required to be restricted by \$6.6 million.

Amounts required to be restricted at September 30, 2017 and 2016 are as follows:

	<u>2017</u>	<u>2016</u>
Debt service	\$ 394,349	\$ 342,296
Debt reserve	362,200	362,200
Bond funds for construction	5,017,278	8,793,251
Over-recovered regulatory fee	49,703	-
Over-recovered fuel	1,856,435	-
Customer deposits	<u>1,445,256</u>	<u>1,403,385</u>
Restricted cash and investments	<u>\$ 9,125,221</u>	<u>\$ 10,901,132</u>

3. Capital Assets

General Description – Assets reflected in plant-in-service include distribution 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 42, concluded that the Rural Electric System had no impaired capital assets at September 30, 2017.

**Bryan Texas Utilities
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Notes to Financial Statements - continued
For the Fiscal Years Ended September 30, 2017 and 2016

Capital asset activity for the fiscal year ended September 30, 2017 was as follows:

	Beginning Balance	Increases	Decreases	Ending Balance
Capital assets, not being depreciated:				
Land	\$ 111,483	\$ 4,041	\$ -	\$ 115,524
Construction in Progress	1,043,029	6,291,959	6,551,525	783,463
Total capital assets, not being depreciated	1,154,512	6,296,000	6,551,525	898,987
Capital assets, being depreciated:				
Distribution Plant	90,897,126	6,530,071	160,070	97,267,127
General Plant	8,687,037	1,474,865	-	10,161,902
Total capital assets, being depreciated	99,584,163	8,004,936	160,070	107,429,029
Less accumulated depreciation for:				
Distribution Plant	29,290,971	2,851,187	534,595	31,607,563
General Plant	827,553	301,447	-	1,129,000
Total accumulated depreciation	30,118,524	3,152,634	534,595	32,736,563
Total capital assets, being depreciated, net	69,465,639	4,852,302	(374,525)	74,692,466
Total capital assets, net	\$ 70,620,151	\$ 11,148,303	\$ 6,177,001	\$ 75,591,453

Depreciation expense for the fiscal year ended September 30, 2017 was \$2,874,591. Depreciation expense for the fiscal year ended September 30, 2016 was \$2,640,488.

4. Long-Term Debt

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

The Rural Electric System did not issue debt in the fiscal year ended September 30, 2017.

For the fiscal year ended September 30, 2016, the City of Bryan issued revenue refunding and improvement bonds dated July 13, 2016 ("2016 Revenue Bonds") totaling \$15,770,000 for the Rural Electric System. The 2016 Revenue Bonds mature serially beginning July 1, 2017, through July 1, 2041, with coupon rates ranging from 2.000% 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 Rural Electric System; capital assets, facilities, and equipment incident and related to the

**Bryan Texas Utilities
Rural Electric System**

Notes to Financial Statements - continued
For the Fiscal Years Ended September 30, 2017 and 2016

operation, maintenance, or administration of the Rural Electric System; and refunding portions of Rural Electric System's outstanding bonds for debt service savings. Proceeds from the sale of the bonds were used to refund \$4,845,000 of the Series 2008 revenue bonds. The refunding represented debt service savings of \$880,520, and a net present value benefit savings of \$696,190.

In prior fiscal years, the Rural 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 Rural Electric System's financial statements. As of September 30, 2017 and 2016, the Rural Electric System had outstanding revenue bonds totaling \$0, and \$4,845,000, respectively, which were considered defeased.

At September 30, 2017, there was \$21,475,000 of Rural Electric System long-term debt, consisting of revenue bonds and certificates of obligation; payable from revenues of the Rural Electric System.

Changes to long term debt during fiscal year 2017, 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 2008	4.000 - 4.750	2034	190,000	\$ -	\$ 190,000	\$ -	\$ -
Series 2011	2.500 - 4.000	2021	1,625,000	-	305,000	1,320,000	315,000
Series 2016	2.000 - 5.000	2041	15,770,000	-	340,000	15,430,000	485,000
Total Revenue Bonds			17,585,000	-	835,000	16,750,000	800,000
<u>Certificates of Obligation:</u>							
Series 2013	3.000 - 4.250	2033	4,950,000	-	225,000	4,725,000	230,000
Total Certificates of Obligation			4,950,000	-	225,000	4,725,000	230,000
Total long-term debt			\$ 22,535,000	\$ -	\$ 1,060,000	\$ 21,475,000	\$ 1,030,000

All net revenues of the Rural Electric System are pledged for the payment of debt service of the revenue bonds. Net revenues, as defined by the bond resolution include all of the revenues and expenses of the Rural Electric System other than depreciation and amortization expenses. The bond resolutions further require that the net revenues, as defined, equal at least 1.20 times the annual debt service on all revenue bonds. The Rural Electric System is in compliance with these requirements at September 30, 2017 and 2016.

Under the terms of the revenue bond covenants, the Rural 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 requirement for the Series 2011 Bonds is satisfied with restricted funds which are reported on Rural Electric System's Statements of Net Position as restricted for debt service. The reserve fund requirement for the Series 2016 Bonds is satisfied with an insurance policy. There are no reserve fund requirements for the 2013 Certificates.

**Bryan Texas Utilities
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Notes to Financial Statements - continued
For the Fiscal Years Ended September 30, 2017 and 2016

In the Statement of Revenues, Expenses and Changes in Net Position for the fiscal years ended September 30, 2017 and 2016, interest expense is recorded in the amount of \$733,466 and \$974,421, respectively, and is included as a non-operating expense.

Debt service requirements to maturity for the Rural 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>
2018	\$ 800,000	\$ 606,700	\$ 1,406,700
2019	815,000	587,550	1,402,550
2020	845,000	568,000	1,413,000
2021	865,000	544,400	1,409,400
2022	530,000	520,200	1,050,200
2023 - 2027	3,065,000	2,176,750	5,241,750
2028 - 2032	3,850,000	1,378,850	5,228,850
2033 - 2037	3,460,000	662,700	4,122,700
2038 - 2041	2,520,000	192,000	2,712,000
Total	<u>\$ 16,750,000</u>	<u>\$ 7,237,150</u>	<u>\$ 23,987,150</u>

<u>Certificates of Obligation</u>			
<u>Year Ending</u>			
<u>September 30</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2018	\$ 230,000	\$ 188,059	\$ 418,059
2019	230,000	178,859	408,859
2020	240,000	169,659	409,659
2021	245,000	160,059	405,059
2022	255,000	150,259	405,259
2023 - 2027	1,405,000	601,574	2,006,574
2028 - 2032	1,725,000	303,781	2,028,781
2033	395,000	16,788	411,788
Total	<u>\$ 4,725,000</u>	<u>\$ 1,769,038</u>	<u>\$ 6,494,038</u>

**Bryan Texas Utilities
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Notes to Financial Statements - continued
For the Fiscal Years Ended September 30, 2017 and 2016

<u>Total Debt</u> Year Ending September 30	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2018	\$ 1,030,000	\$ 794,759	\$ 1,824,759
2019	1,045,000	766,409	1,811,409
2020	1,085,000	737,659	1,822,659
2021	1,110,000	704,459	1,814,459
2022	785,000	670,459	1,455,459
2023 - 2027	4,470,000	2,778,324	7,248,324
2028 - 2032	5,575,000	1,682,631	7,257,631
2033 - 2037	3,855,000	679,488	4,534,488
2038 - 2041	2,520,000	192,000	2,712,000
Total	<u>\$ 21,475,000</u>	<u>\$ 9,006,188</u>	<u>\$ 30,481,188</u>

5. Risk Management

The Rural Electric System is covered for risk of losses related to general liability and worker's compensation through the City's risk management program. The City has established an Insurance Fund whereby the costs of providing claims servicing and claims payment are funded by charging a premium based upon a percentage of estimated current year payroll and management's estimate of projected current costs. For the fiscal years ended September 30, 2017 and 2016, the Rural Electric System paid the City \$137,318 and \$122,639, respectively, for participation in the City's risk management program.

6. Related Party Transactions

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 rates are established through City ordinance. Fuel and regulatory rates may be adjusted monthly to reflect actual cost. For the fiscal years ended September 30, 2017 and 2016, the Rural Electric System's purchased power, fuel, and regulatory charges were the following:

	<u>FY2017</u>	<u>FY2016</u>
Purchased power cost	\$ 17,162,790	\$ 16,374,791
Fuel cost	12,503,648	12,948,679
Regulatory charges	4,622,901	4,508,399
Total	<u>\$ 34,289,339</u>	<u>\$ 33,831,869</u>

The Rural Electric System had payables to the City Electric System, as of September 30, 2017 and 2016, in the amount of \$3,138,675 and \$3,672,858 respectively.