

**BOARD OF PUBLIC UTILITIES
CITY OF McPHERSON**

FINANCIAL REPORT

**FOR THE YEARS ENDED
DECEMBER 31, 2010 AND 2009**

Board of Public Utilities - McPherson, Kansas

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SWINDOLL
JANZEN
HAWK &
LOYD, LLC

Certified Public Accountants

Celebrating *75th*
Our Anniversary
1936 - 2011

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INDEPENDENT AUDITOR'S REPORT

Board of Public Utilities
of McPherson, Kansas

We have audited accompanying financial statements of the Board of Public Utilities of McPherson, Kansas (BPU) a part of the primary government of the City of McPherson, Kansas as of and for the years ended December 31, 2010 and 2009, as listed in the table of contents. These financial statements are the responsibility of the BPU's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

As discussed in Note 1, the financial statements present only the operations of the electric and water funds and do not purport to, and do not, present fairly the financial position of the City of McPherson, Kansas as of December 31, 2010 and 2009 and the changes in its financial position, or where applicable, its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Board of Public Utilities of McPherson, Kansas as of December 31, 2010 and 2009, and the changes in financial position and, where applicable, cash flows thereof for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Accounting principles generally accepted in the United States of America require that Management's Discussion and Analysis be presented to supplement the 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 operation, 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.

Accounting principles generally accepted in the United States of America require that the Schedule of Funding Progress – Postemployment 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 were unable to apply certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America because of underlying actuarial calculations performed by a third party. We do not express an opinion or provide any assurance on the information.

Our audits were conducted for the purpose of forming an opinion on the financial statements taken as a whole. The additional information and comments and operating statistics listed in the accompanying table of contents are presented for purposes of additional analysis and are not a required part of the basic financial statements of the Board of Public Utilities of McPherson, Kansas. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The additional information has been subjected to the auditing procedures applied in the audits of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the basic financial statements taken as a whole. The comments and operating statistics have not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we express no assurance on them.

Swindoll, Janyon, Hawk & Loyd, LLC

Certified Public Accountants

June 8, 2011

MANAGEMENT'S DISCUSSION AND ANALYSIS

The McPherson Board of Public Utilities (the BPU) is a quasi-municipality of the City of McPherson, Kansas. The electric and water funds are reflected as enterprise funds on the City of McPherson, Kansas' financial statements consisting of the Summary of Cash Receipts, Expenditures and Unencumbered Cash, Summary of Expenditures – Actual and Budget, and Summary of Cash Receipts and Expenditures. This Management Discussion and Analysis of the BPU's financial report presents our discussion and analysis of the BPU's financial performance for the year that ended December 31, 2010. This analysis should be read in conjunction with the financial statements and notes thereto.

The following table summarizes the financial condition and operations of the BPU as of and for the years ended December 31, 2010, 2009, and 2008.

Condensed Balance Sheet

	2010			2009	2008
	Electric	Water	Totals	Totals	Totals
Assets					
Capital assets	\$ 40,269,584	\$ 19,681,485	\$ 59,951,069	\$ 57,280,659	\$ 51,983,898
Other assets	<u>28,420,762</u>	<u>10,324,902</u>	<u>38,745,664</u>	<u>40,977,773</u>	<u>43,969,997</u>
Total Assets	<u>\$ 68,690,346</u>	<u>\$ 30,006,387</u>	<u>\$ 98,696,733</u>	<u>\$ 98,258,432</u>	<u>\$ 95,953,895</u>
Liabilities					
Long-term debt outstanding	\$ 11,930,452	\$ 11,872,953	\$ 23,803,405	\$ 24,465,612	\$ 25,782,821
Other liabilities	<u>3,592,642</u>	<u>1,042,950</u>	<u>4,635,592</u>	<u>5,488,428</u>	<u>4,988,480</u>
Total Liabilities	<u>15,523,094</u>	<u>12,915,903</u>	<u>28,438,997</u>	<u>29,954,040</u>	<u>30,771,301</u>
Net Assets					
Net assets invested in capital assets, net of related debt	28,761,643	9,531,546	38,293,189	35,133,251	34,229,892
Restricted	4,860,199	297,083	5,157,282	5,364,984	5,697,437
Unrestricted	<u>19,545,410</u>	<u>7,261,855</u>	<u>26,807,265</u>	<u>27,806,157</u>	<u>25,255,265</u>
Total Net Assets	<u>53,167,252</u>	<u>17,090,484</u>	<u>70,257,736</u>	<u>68,304,392</u>	<u>65,182,594</u>
Total Liabilities and Net Assets	<u>\$ 68,690,346</u>	<u>\$ 30,006,387</u>	<u>\$ 98,696,733</u>	<u>\$ 98,258,432</u>	<u>\$ 95,953,895</u>

Condensed Statement of Revenues, Expenses and Changes in Net Assets

	2010			2009	2008
	Electric	Water	Totals	Totals	Totals
Operating revenues:					
Residential	\$ 4,993,963	\$ 1,588,956	\$ 6,582,919	\$ 5,902,500	\$ 5,904,534
Commercial and Industrial	28,571,613	1,799,550	30,371,163	28,790,660	29,098,329
Other	5,471,605	83,846	5,555,451	5,796,685	6,759,140
Total operating revenue	<u>39,037,181</u>	<u>3,472,352</u>	<u>42,509,533</u>	<u>40,489,845</u>	<u>41,762,003</u>
Operating expenses:					
Fuel	447,920	-	447,920	838,736	1,660,246
Purchased power	26,459,806	-	26,459,806	24,740,416	25,323,931
Production	2,981,164	399,435	3,380,599	2,100,432	2,135,130
Distribution and transmission	3,431,329	761,913	4,193,242	4,036,358	3,756,041
Administrative and general	1,789,860	207,751	1,997,611	2,126,283	2,021,960
Depreciation and amortization	2,037,621	323,067	2,360,688	2,321,804	2,278,360
Total operating expenses	<u>37,147,700</u>	<u>1,692,166</u>	<u>38,839,866</u>	<u>36,164,029</u>	<u>37,175,668</u>
Operating income	1,889,481	1,780,186	3,669,667	4,325,816	4,586,335
Nonoperating income (expenses)	(286,564)	87,741	(198,823)	166,982	931,097
Transfers in lieu of taxes	<u>(1,445,000)</u>	<u>(72,500)</u>	<u>(1,517,500)</u>	<u>(1,371,000)</u>	<u>(1,357,000)</u>
Increase in net assets	157,917	1,795,427	1,953,344	3,121,798	4,160,432
Net assets, beginning	<u>53,009,335</u>	<u>15,295,057</u>	<u>68,304,392</u>	<u>65,182,594</u>	<u>61,022,162</u>
Net assets, ending	<u>\$ 53,167,252</u>	<u>\$ 17,090,484</u>	<u>\$ 70,257,736</u>	<u>\$ 68,304,392</u>	<u>\$ 65,182,594</u>

Financial Highlights

2010 Compared to 2009

- In 2010, the water department continued construction on the new blending plant and completed construction of a new one million gallon water tower for the system. These projects are being financed by the \$12 million 2007 Series water bond issue. By December 31, 2010, the water department had spent \$8,933,241 on the blending plant and \$2,242,202 on the new water tower. The blending plant was completed in February, 2011. Remaining bond proceeds of \$323,250 will be transferred to the water department principal and interest account for future payments.
- Debt to equity ratio for the water department improved in 2010 to 0.76:1 compared with 0.88:1 for 2009. For the electric department, the ratio changed to 0.29:1 in 2010 from 0.31:1 in 2009.
- The debt service coverage ratios for both the electric and water departments were 2.78 and 1.71 times the required amounts respectively. The ratios were much higher than the 1.25 times required by the bond covenant agreements. For 2009, these ratios for the electric and water departments were 2.76 and 2.00 times, respectively.
- Available cash and investments for 2010 decreased by 19% in the electric department and increased by 145% in the water department compared to 2009.
- Interest income decreased by 69.09% for the electric department and decreased by 53.67% for the water department in 2010 compared to 2009.

- Gross water revenue for 2010 was up 14.25% with quantity sales higher by 18.90% compared to 2009. For 2009, gross water revenues were down 4.42% and gallons sold were down 5.85% compared to 2008.
- Electric revenue was up 4.23% with an energy sales increase of 1.2% in 2010. The year 2009, saw an electric revenue decrease of 2.93% and energy sales increase of 0.56%
- The electric department hired a professional engineering firm, Burns and McDonnell, to perform a cost of service study for the utility. The consultants determined that an 18.2% average increase was necessary to provide adequate revenues for the utility over the next five years. The utility board authorized the recommended rate increase December 13, 2010, to be implemented January 1, 2011.
- The BPU board added Addendum #5 to Westar Energy contract extending the purchase power agreement to the year 2039 and agreed to begin paying transmission charges based on a Federal Energy Regulatory Commission approved formula tariff. Also included in the Addendum was a provision that Westar Energy will vary the capacity charge based on cost of the generating units included in the base capacity charge, allowing recovery of expenditures for new emissions equipment.
- In 2006, the BPU authorized the remodeling of a former power plant building for use as administrative offices for the utilities. Utility employees have been working over several years to remove old steam turbines and clear the building for renovation. A contract was signed with a local construction company in January, 2010 for \$1,717,372 to complete the project. The utility moved to the new location on March 21, 2011.

2009 Compared to 2008

- The water department continued construction on the new blending plant and on a 1,000,000 gallon water tower for the system. These projects are being financed by the 2007 Series water bond issue. By December 31, 2009, the water department had spent \$10,077,781 of the \$12,000,000 borrowed for the project. These projects are expected to be completed during 2010.
- Debt to equity ratio for the water department improved in 2009 to 0.88:1 compared with 1.03:1 for 2008. For the electric department, the ratio changed to 0.31:1 in 2009 from 0.33:1 in 2008.
- The debt service coverage ratios for both the electric and water departments were 2.76 and 2.00 times the amounts required, respectively. The ratios were much higher than the 1.25 times required by the bond covenant agreements. For 2008 these ratios for the electric and water departments were 4.15 and 2.53 times respectively.
- Available cash and investments for 2009 increased by 130% in the electric department and by 213% in the water department compared to 2008.
- Interest income decreased by 50.04% for the electric department and by 69.52% for the water department in 2009 compared to 2008. The water department issued bonds of \$12,000,000 in 2007 and invested the unspent proceeds during the year. It is anticipated that the bond proceeds will be spent by the end of 2010.
- Electric revenue was down 2.93% with an energy sales increase of 0.56% in 2009. For 2008, the electric revenue was up 6.05% and energy sales were down by 0.13%.
- Gross water revenue for 2009 was down by 4.42% with quantity sales lower by 5.85% compared to 2008. For 2008, gross water revenues were up 4.5% and gallons sold were down 9.63% compared to 2007.

2008 Compared to 2007

- An ice storm moved through the McPherson area December 10-11, 2007 leaving major damage to power poles and lines causing outages to over 3,000 customers. Restoration expenses of \$225,644 were recorded in 2007 and \$107,066 in 2008. The storm was declared a national disaster by the federal government. An application was made to the Federal Emergency Management Agency (FEMA) and the utility was reimbursed \$282,803 in 2008.

- March 1, 2008 the electric department called the remaining outstanding Series 1999 revenue bonds of \$4,550,000. The bonds were called with cash of \$3,500,000 released from the Long Range Electric Supply funds and \$1,050,000 from current investments. As a result of the call, the electric department recorded a loss of \$125,262 for the remaining "Cost of Issuance" being amortized over the life of the bond issue.
- The electric department debt to equity ratio improved in 2008 to .33:1 compared with .45:1 due mainly to the Series 1999 bond call. In the water department the debt to equity ratio decreased in 2008 to 1.03:1 as compared with 1.25:1 for 2007.
- The debt service coverage ratios for 2008 for both the electric and water departments were 4.15 and 2.53 times the required amounts, respectively. The ratios are much higher than the 1.25 times required by the bond covenant agreements. For 2007 these ratios for the electric and water departments were 3.11 and 2.09 times respectively.
- Available cash and investments for 2008 increased by 174% in the water department, but decreased by 68% in the electric department compared to 2007.
- Interest income decreased 24% for the electric department and increased 95% for the water department in 2008 compared to 2007. The water department issued bonds of \$12,000,000 in 2007 and has invested the unspent proceeds during the year. The water construction funds should be completely spent by 2010.
- Gross water revenues were up 4.5% in 2008 compared to 2007.
- Electric revenue was up 6.04% in 2008 with an energy sales decrease of .13%. The year 2007 had electric revenue up 3.4% with energy sales also up by 3.9%.
- The electric department registered the former Power Plant 1 building with the Kansas State Historical Society. This building is being rehabilitated for a new administration office and will qualify for state tax credits. The BPU has signed an agreement to sell the tax credits to a Kansas bank. Estimated completion of the project is 2011.
- In 2007 the water department issued Series 2007 bonds for \$12,000,000 for the purpose of financing the construction of a blending plant and related appurtenances, raw water piping and finish water piping modifications allowing the BPU to blend water with a high level of nitrates with water with a low level of nitrates and dilute the nitrates to an acceptable level. At December 31, 2008, \$4,533,500 had been spent on the project.
- In 2008 the electric department applied with FEMA for reimbursement of costs for the repair of four miles of conductor also damaged during the ice storm that moved through the BPU service territory December 10-11, 2007. The claim was denied at the time. In February 2009, the BPU was contacted by FEMA stating that the damage does qualify for reimbursement by the federal government. The electric department spent \$354,428 in 2008 and \$31,018 in 2009 for a total of \$385,446 in repairs. The Utility set up an accrued receivable at December 31, 2008 of \$301,263.

Contacting McPherson BPU Management

This financial report is designed to provide our citizens, customers, taxpayers, bondholders, and creditors with a general overview of the BPU's finances and to show accountability for the money it receives. Financial information for the BPU is also presented in the financial statements of the primary government, the City of McPherson, Kansas. If you have questions about this report or need additional financial information, contact the City of McPherson, 401 West Kansas, McPherson, Kansas 67460.

Board of Public Utilities - McPherson, Kansas

BALANCE SHEETS
December 31, 2010
(With comparative totals for December 31, 2009)

	<u>ASSETS</u>			
	<u>Electric</u>	<u>Water</u>	<u>Totals</u>	
			<u>2010</u>	<u>2009</u>
ASSETS				
Current assets				
Cash and cash equivalents	\$ 4,777,990	\$ 2,759,738	\$ 7,537,728	\$ 8,971,835
Kansas Municipal Investment Pool- certificates of deposit	1,700,000	-	1,700,000	700,000
Certificates of deposit	10,190,000	4,675,000	14,865,000	14,745,000
Accounts receivable, customer and other	3,372,307	457,038	3,829,345	3,775,316
Inventories	1,676,344	272,390	1,948,734	2,086,462
Accrued interest on investments	25,876	7,815	33,691	72,845
Postemployment benefit asset	<u>73,537</u>	<u>8,171</u>	<u>81,708</u>	<u>63,682</u>
Total current assets	<u>21,816,054</u>	<u>8,180,152</u>	<u>29,996,206</u>	<u>30,415,140</u>
Noncurrent assets				
Restricted cash and cash equivalents	447,957	58,485	506,442	593,313
Kansas Municipal Investment Pool- cash and cash equivalents	-	343,071	343,071	1,899,661
Kansas Municipal Investment Pool- certificates of deposit	1,750,000	-	1,750,000	-
Restricted certificates of deposit	3,260,000	1,406,750	4,666,750	6,535,378
Capital Assets				
Land	488,728	1,339,147	1,827,875	1,797,981
Buildings and equipment	86,538,812	14,001,167	100,539,979	97,554,907
Construction in process	5,991,663	9,643,731	15,635,394	13,691,223
Less accumulated depreciation	(52,749,619)	(5,302,560)	(58,052,179)	(55,763,452)
Industrial development property, at cost	711,740	-	711,740	711,740
Bond issue costs, net	422,511	336,444	758,955	810,041
Other Assets	<u>12,500</u>	<u>-</u>	<u>12,500</u>	<u>12,500</u>
Total noncurrent assets	<u>46,874,292</u>	<u>21,826,235</u>	<u>68,700,527</u>	<u>67,843,292</u>
TOTAL ASSETS	<u>\$ 68,690,346</u>	<u>\$ 30,006,387</u>	<u>\$ 98,696,733</u>	<u>\$ 98,258,432</u>

Board of Public Utilities - McPherson, Kansas

BALANCE SHEET
December 31, 2010
(With comparative totals for December 31, 2009)

LIABILITIES AND NET ASSETS

	Electric	Water	Totals	
			2010	2009
LIABILITIES				
Current liabilities				
Accounts payable	\$ 2,197,867	\$ 40,584	\$ 2,238,451	\$ 2,470,143
Current maturities of revenue bonds	250,000	530,000	780,000	1,435,000
Accrued interest on revenue bonds	196,079	124,653	320,732	334,277
Customer meter and other deposits	399,296	-	399,296	381,886
Self-insurance claims payable	45,281	6,469	51,750	54,000
Accrued payroll	501,736	41,057	542,793	507,751
Accrued interest on customer meter deposits	2,383	-	2,383	4,043
Due to City of McPherson	-	225,621	225,621	216,636
Total current liabilities	<u>3,592,642</u>	<u>968,384</u>	<u>4,561,026</u>	<u>5,403,736</u>
Long-term debt - revenue bonds				
Principal	<u>11,930,452</u>	<u>11,872,953</u>	<u>23,803,405</u>	<u>24,465,612</u>
Total long-term debt	<u>11,930,452</u>	<u>11,872,953</u>	<u>23,803,405</u>	<u>24,465,612</u>
Other liabilities				
Water meter advances	<u>-</u>	<u>74,566</u>	<u>74,566</u>	<u>84,692</u>
TOTAL LIABILITIES	<u>15,523,094</u>	<u>12,915,903</u>	<u>28,438,997</u>	<u>29,954,040</u>
NET ASSETS				
Invested in capital assets, net of related debt	28,761,643	9,531,546	38,293,189	35,133,251
Restricted for debt service	4,860,199	297,083	5,157,282	5,364,984
Unrestricted	<u>19,545,410</u>	<u>7,261,855</u>	<u>26,807,265</u>	<u>27,806,157</u>
TOTAL NET ASSETS	<u>53,167,252</u>	<u>17,090,484</u>	<u>70,257,736</u>	<u>68,304,392</u>
TOTAL LIABILITIES AND NET ASSETS	<u>\$ 68,690,346</u>	<u>\$ 30,006,387</u>	<u>\$ 98,696,733</u>	<u>\$ 98,258,432</u>

Board of Public Utilities - McPherson, Kansas

STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET FUND ASSETS

December 31, 2010

(With comparative totals for the year ended December 31, 2009)

	Electric	Water	Totals	
			2010	2009
OPERATING REVENUE				
Electric				
Metered sales	\$ 35,376,672	\$ -	\$ 35,376,672	\$ 33,296,546
Street lighting	176,808	-	176,808	215,311
Sales to interconnection	3,483,701	-	3,483,701	3,938,631
Water				
Sale of water	-	3,472,352	3,472,352	3,039,357
Total operating revenue	<u>39,037,181</u>	<u>3,472,352</u>	<u>42,509,533</u>	<u>40,489,845</u>
OPERATING EXPENSE				
Fuel	447,920	-	447,920	838,736
Purchased power	26,459,806	-	26,459,806	24,740,416
Production	2,981,164	399,435	3,380,599	2,100,432
Distribution and transmission	3,431,329	761,913	4,193,242	4,036,358
Administrative and general	1,789,860	207,751	1,997,611	2,126,283
Depreciation and amortization	2,037,621	323,067	2,360,688	2,321,804
Total operating expense	<u>37,147,700</u>	<u>1,692,166</u>	<u>38,839,866</u>	<u>36,164,029</u>
OPERATING INCOME	<u>1,889,481</u>	<u>1,780,186</u>	<u>3,669,667</u>	<u>4,325,816</u>
NONOPERATING INCOME (EXPENSE)				
Interest income	133,736	65,707	199,443	567,386
Revenues from merchandising, jobbing and contract work and miscellaneous income	274,052	45,580	319,632	497,531
Less cost of merchandising	(93,559)	(9,030)	(102,589)	(221,472)
Refuse collection and sewer service fees	66,169	7,357	73,526	73,080
Penalties, earned discounts and other	49,886	-	49,886	49,633
Farm rents, net of expense	(1,979)	52,567	50,588	46,066
Gain (loss) on disposal of assets	4,800	-	4,800	(11,961)
Interest on debt	(719,669)	(74,440)	(794,109)	(833,281)
Total nonoperating income (expense)	<u>(286,564)</u>	<u>87,741</u>	<u>(198,823)</u>	<u>166,982</u>
INCOME BEFORE OPERATING TRANSFERS	1,602,917	1,867,927	3,470,844	4,492,798
TRANSFER: PAYMENTS IN LIEU OF TAXES	<u>(1,445,000)</u>	<u>(72,500)</u>	<u>(1,517,500)</u>	<u>(1,371,000)</u>
CHANGES IN NET ASSETS	157,917	1,795,427	1,953,344	3,121,798
TOTAL NET ASSETS, BEGINNING OF YEAR	<u>53,009,335</u>	<u>15,295,057</u>	<u>68,304,392</u>	<u>65,182,594</u>
TOTAL NET ASSETS, END OF YEAR	<u>\$ 53,167,252</u>	<u>\$ 17,090,484</u>	<u>\$ 70,257,736</u>	<u>\$ 68,304,392</u>

The notes to the financial statements are an integral part of this statement.

Board of Public Utilities - McPherson, Kansas

STATEMENT OF CASH FLOWS

December 31, 2010

(With comparative totals for the year ended December 31, 2009)

	Electric	Water	Totals	
			2010	2009
CASH FLOWS FROM OPERATING ACTIVITIES				
Receipts from customers	\$ 39,403,913	\$ 3,545,223	\$ 42,949,136	\$ 41,530,977
Payments to suppliers	(30,084,332)	(427,299)	(30,511,631)	(27,883,429)
Payments to employees	(5,140,794)	(993,933)	(6,134,727)	(6,097,600)
Other receipts (payments)	(1,445,000)	(72,500)	(1,517,500)	(1,371,000)
Net cash provided from (used in) operating activities	<u>2,733,787</u>	<u>2,051,491</u>	<u>4,785,278</u>	<u>6,178,948</u>
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES				
Purchase of property, plant and equipment	(3,059,487)	(1,478,554)	(4,538,041)	(7,183,531)
Proceeds from sale of equipment	4,800	-	4,800	40,368
Principal payments on bonds	(920,000)	(515,000)	(1,435,000)	(920,000)
Interest paid on debt	(615,836)	(515,994)	(1,131,830)	(1,159,571)
Net cash provided from (used in) capital and related financing activities	<u>(4,590,523)</u>	<u>(2,509,548)</u>	<u>(7,100,071)</u>	<u>(9,222,734)</u>
CASH FLOWS FROM INVESTING ACTIVITIES				
Purchase of investments	(23,149,150)	(5,583,026)	(28,732,176)	(40,877,454)
Proceeds from sale of investments	22,649,150	5,081,654	27,730,804	44,902,239
Interest received	162,009	76,588	238,597	710,838
Net cash provided from (used in) investing activities	<u>(337,991)</u>	<u>(424,784)</u>	<u>(762,775)</u>	<u>4,735,623</u>
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS				
	(2,194,727)	(882,841)	(3,077,568)	1,691,837
CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR				
	<u>7,420,674</u>	<u>4,044,135</u>	<u>11,464,809</u>	<u>9,772,972</u>
CASH AND CASH EQUIVALENTS, END OF YEAR				
	<u>\$ 5,225,947</u>	<u>\$ 3,161,294</u>	<u>\$ 8,387,241</u>	<u>\$ 11,464,809</u>

Board of Public Utilities - McPherson, Kansas

STATEMENT OF CASH FLOWS

December 31, 2010

(With comparative totals for the year ended December 31, 2009)

	Electric	Water	Totals	
			2010	2009
RECONCILIATION OF OPERATING INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES				
Operating income	\$ 1,889,481	\$ 1,780,186	\$ 3,669,667	\$ 4,325,816
Adjustments to reconcile operating income to net cash provided by operating activities:				
Depreciation and amortization	2,037,620	323,066	2,360,686	2,321,804
Other nonoperating income	299,369	96,474	395,843	432,877
(Gain) loss on disposal of fixed assets	(4,800)	-	(4,800)	11,961
Payment in lieu of taxes	(1,445,000)	(72,500)	(1,517,500)	(1,371,000)
Changes in:				
Accounts and notes receivable	(21,396)	(32,633)	(54,029)	374,822
Inventories	137,935	(207)	137,728	153,537
Accounts payable	(207,186)	(24,506)	(231,692)	17,545
Accrued expenses	46,577	(6,460)	40,117	32,165
Postemployment benefit asset	(16,223)	(1,803)	(18,026)	(93,722)
Water meter advances	-	(10,126)	(10,126)	(27,165)
Customer meter deposits	17,410	-	17,410	308
Net cash provided from operating activities	<u>\$ 2,733,787</u>	<u>\$ 2,051,491</u>	<u>\$ 4,785,278</u>	<u>\$ 6,178,948</u>
NONCASH FINANCING ACTIVITIES				
Amortization of defeased bond costs	<u>\$ 113,033</u>	<u>\$ 4,760</u>	<u>\$ 117,793</u>	<u>\$ 117,792</u>

BOARD OF PUBLIC UTILITIES - McPHERSON, KANSAS

NOTES TO FINANCIAL STATEMENTS

December 31, 2010 and 2009

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Board of Public Utilities of McPherson, Kansas (the BPU) consists of the municipal electric and water funds that provide services to approximately 8,500 electric and 5,700 water customers. The BPU's operational control and administration is under a three member appointed Board of Directors (the Board). However, the BPU is owned by and is a part of the primary government of the City of McPherson, Kansas (the City) because the City holds the corporate powers of the BPU. The accompanying financial statements include only those operations related to the electric and water utilities.

The following is a summary of the more significant accounting policies applicable to the BPU.

(a) Basis of Accounting and Budgeting

The Board of Public Utilities maintains its accounts in accordance with accounting principles generally accepted in the United States of America for utility accounting and follows the uniform system of accounts as prescribed by the Federal Energy Regulatory Commission. The Board operates separate electric and water utility funds. General management, administrative offices and personnel are common to both the electric and water funds. Administrative overhead expenses are allocated between the two funds on a percentage approximating their respective gross receipts. Interfund transactions which are material have been eliminated. The BPU accounts for its transactions on the flow of economic resources measurement focus and uses the accrual basis of accounting under which revenues are recognized when earned and expenses are recorded when liabilities are incurred. In reporting its financial activity, the BPU applies all applicable Governmental Accounting Standards Board (GASB) pronouncements as well as the following pronouncements issued on or before November 30, 1989, unless these pronouncements conflict with or contradict GASB pronouncements: Financial Accounting Standards Board Statements and Interpretations; Accounting Principles Board Opinions; and Accounting Research Bulletins of the Committee on Accounting Procedure. In accordance with accounting principles generally accepted in the United States of America for rate regulated enterprises, certain costs or credits may be recorded as deferred charges or credits when it is probable, based on historical precedents and Board resolutions, that future rates established by the Board will recover or return such costs or credits. The BPU follows the uniform system of accounts as prescribed by the Federal Energy Regulatory Commission and FASB Codification, Section 980 *Regulated Operations*.

Although the BPU is required to adopt an annual budget, there is no reporting requirement. Therefore, budgetary information has not been included in this report.

(b) Cash and Cash Equivalents

Cash and cash equivalents in the accompanying statement of cash flows include all highly liquid investments (including restricted assets) with an original maturity of three months or less.

(c) Revenue Recognition

Operating revenues include revenues from the provision and delivery of electricity and water to customers. Operating expenses consist of costs incurred through the provision and delivery of electricity and water to customers. Meters are read and bills rendered on a cycle basis. Nonoperating revenues are those related to capital and related financing, noncapital financing and investing activities, as well as those that do not meet the definition of operating revenues. Revenues earned after meters are read are estimated and accrued as unbilled revenues at the end of each accounting period.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont.)

(d) Accounts Receivable and Revenue

Accounts receivable include open trade receivables representing claims for utility services sold or other special services sold in the ordinary course of business. Utility accounts receivable are considered delinquent after 28 days and a 2% late fee on the current month's charges is added for each month the account is delinquent. Other accounts receivable become delinquent after 30 days and interest accrues at an annual rate of 18% until payment is received in full. After one year, interest ceases to accrue on other receivables and the account is turned over for collection.

The BPU utilizes cycle billing and accrues the amount of revenues for sales unbilled at the end of each reporting period. Fuel and purchased power costs in excess of or less than those reflected in base rates are adjusted subsequent to the period in which such excess costs were incurred through production cost adjustment clauses.

(e) Allowance for Doubtful Accounts

The BPU considers accounts receivable to be fully collectible. Accordingly, no provision has been established for doubtful accounts. If amounts become uncollectible they will be charged to operations when that determination is made.

(f) Inventories

Inventories are carried at cost substantially valued on an average cost method. Materials and supplies are essentially repair and replacement items for the maintenance of the two systems. Inventories at December 31st consist of the following:

	Water	Electric	Totals	
			2010	2009
Fuel	\$ -	\$ 455,509	\$ 455,509	\$ 526,302
Materials and supplies	272,390	1,220,835	1,493,225	1,560,160
Total	\$ 272,390	\$ 1,676,344	\$ 1,948,734	\$ 2,086,462

(g) Capital Assets and Depreciation

Capital assets are stated at actual purchased cost or cost of construction, including payroll-related costs. All completed and purchased utility property is depreciated on the straight-line method over lives recommended for the different classes of assets by the Federal Energy Regulatory Commission and independent engineers. The BPU has a policy to capitalize all purchases over \$5,000. The average annual composite depreciation rates are 1.5% to 15%. Repairs and maintenance are expensed as incurred.

(h) Estimates and Assumptions

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Significant items subject to such estimates and assumptions include the useful lives of fixed assets; allowances for doubtful accounts, fixed assets, inventory, investments, notes receivable; and reserves for employee benefit obligations, environmental liabilities, and other contingencies. The current economic environment has increased the degree of uncertainty inherent in those estimates and assumptions.

(i) Deferred Charges

Bond issuance costs are amortized over the life of the bonds using the straight-line method.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont.)

(j) *Vacation and Sick Leave*

Vacation - Vacation leave shall be accrued from the employee's date of employment as stipulated hereinafter. Vacation leave, if not taken, shall accrue from year to year up to maximum provided depending upon the employee's years of service. No vacation leave shall be taken until a new employee has completed the probationary period.

Each permanent full-time employee will accrue vacation leave as follows:

<u>Maximum Years of Service</u>	<u>Hours Accrued Per Year</u>	<u>Maximum Accumulation</u>
0 to 5 years	80 working hours	120 working hours
5 to 15 years	120 working hours	180 working hours
15 to 25 years	160 working hours	240 working hours
After 25 years	200 working hours	300 working hours

An employee shall be paid for all accumulated unused vacation leave upon termination. The liability for accumulated vacation at December 31, 2010 for the electric fund and the water fund of \$339,362 and \$36,344, respectively, and at December 31, 2009 for the electric fund and the water fund of \$331,993 and \$34,750, respectively, has been accrued in the accompanying financial statements.

Sick leave - All employees who work not less than one-half time shall be entitled to sick leave with pay for absences resulting from personal illness, injuries, accidents or other physical incapacities, occurring either on or off the job. Full-time employees shall earn one working day of sick leave for each full month of service. Part-time employees shall receive the equivalent of a regularly scheduled day for each full month of service. Other employees shall not have paid sick leave. An employee beginning work on or before the 15th of the month shall get credit for a full month. On termination of employment an employee shall not be paid for accumulative sick leave. Accordingly, no provision for accumulated sick leave has been made in the accompanying financial statements.

(k) *Interest Capitalization*

It is BPU's policy to capitalize net interest costs on funds borrowed to finance construction of major capital additions. For the year ended December 31, 2010, the BPU's total interest expense was \$1,236,078. Net interest cost of \$441,969 (interest cost of \$442,562 reduced by interest income of \$593) was capitalized in connection with construction in progress during 2010. For the year ended December 31, 2009, interest cost of \$436,216 was capitalized. The BPU's policy is in accordance with the FASB Codification, Section 835 *Interest* which requires capitalization of interest cost of the restricted tax exempt borrowings less any interest earned on investment of the proceeds during the construction period.

(l) *Impairment of Long-Lived Assets and Long-Lived Assets to Be Disposed Of*

GASB Statement No. 42, *Accounting and Financial Reporting for Impairment of Capital Assets* establishes accounting and financial reporting standards for impairment of capital assets. A capital asset is considered impaired when its service to the utility has declined significantly and unexpectedly. This statement also clarifies and establishes accounting requirements for insurance recoveries. This Statement requires governments to report the effects of capital asset impairments in their financial statements when they occur rather than as a part of the ongoing depreciation expense for the capital asset or upon disposal of the capital asset. The BPU has not recorded any impairment of long-lived assets in 2010 or 2009.

(m) *Net Assets*

In the financial statements, equity is displayed in three components as follows:

- Invested in Capital Assets, Net of Related Debt—This consists of capital assets, net of accumulated depreciation, less the outstanding balances of any bonds, notes, or other borrowings that are attributable to the acquisition, construction, or improvement of those assets.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont.)

(m) Net Assets

- Restricted—This consists of net assets that are legally restricted by outside parties or by law through constitutional provisions or enabling legislation. When both restricted and unrestricted resources are available for use, it is generally the BPU's policy to use restricted resources first, then unrestricted resources as they are needed.
- Unrestricted—This consists of net assets that do not meet the definition of "restricted" or "invested in capital assets, net of related debt."

(n) New Accounting Pronouncements

BPU has adopted GASB No. 51 (GASB 51) Accounting & Financial Reporting for Intangible Assets. GASB 51 establishes standards for reporting intangible assets. For the year ended December 31, 2010, this statement does not have any effect on the financial statements of BPU.

2. RISK MANAGEMENT

The BPU is exposed to various risks of loss related to tort claims; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters.

The BPU self-insures for health care claims. Under the self-insured plan, the BPU, along with the City of McPherson, is responsible for a potential liability up to \$50,000 per individual per year for health care claims. At December 31, 2010, the BPU has established a liability of \$51,750 that is recorded on the balance sheet for claims arising out of the self-insurance program. At December 31, 2009, this liability was \$54,000. Management believes claims incurred, but not reported, are insignificant at December 31, 2010.

3. COMMITMENTS

The BPU has contract commitments for the water blending plant, for the remodel work on the administrative building, for financial software replacement, and for Plant #3 gas turbine repairs, for a total amount of \$4,486,957. As of December 31, 2010, payments of \$3,876,332 had been made toward these commitments, with a remaining balance due of \$610,625. At December 31, 2009, the BPU had outstanding commitments in the amount of \$1,565,853.

4. DEPOSITS AND INVESTMENTS

K.S.A. 9-1401 establishes the depositories which may be used by the BPU. The statute requires banks eligible to hold the BPU's funds have a main or branch bank in the county in which the BPU is located, or in an adjoining county if such institution has been designated an official depository, and the banks provide an acceptable rate of return on funds. In addition, K.S.A. 9-1402 requires the banks to pledge securities for deposits in excess of FDIC coverage. The BPU has no other policies that would further limit interest rate risk.

K.S.A. 12-1675 limits the BPU's investment of idle funds to time deposits, open accounts, and certificates of deposit with allowable financial institutions; U.S. government securities; temporary notes; no fund warrants; repurchase agreements; and the Kansas Municipal Investment Pool. The BPU has no investment policy that would further limit investment choices. The rating of the BPU's investments is noted below

Concentration of Credit Risk. State statutes place no limit on the amount the BPU may invest in any one issue as long as the investments are adequately secured under K.S.A. 9-1402 and 9-1405. At December 31, 2010 and 2009, the BPU held 100% of their investments in the Kansas Municipal Investment Pool.

Custodial Risk – deposits. Custodial credit risk is the risk that in the event of bank failure, the BPU's deposits may not be returned to it. State statutes require the BPU's deposits in financial institutions to be entirely covered by federal depository insurance or by collateral held under a joint custody receipt issued by a bank with the State of Kansas, the Federal Reserve Bank of Kansas City, or the Federal Home Loan Bank of Topeka. Deposits were under-secured at one bank at year end in violation of K.S.A. 9-1402 and K.S.A. 9-1405.

4. DEPOSITS AND INVESTMENTS (cont.)

Custodial Credit Risk – investments. For an investment, this is the risk that, in the event of the failure of the issuer or counterparty, the BPU will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. State statutes require investments to be adequately secured.

(a) Deposits

At December 31, 2010 and 2009, the carrying amount of the BPU's deposits, including certificates of deposit, was \$29,575,321 and \$30,844,926, respectively, and the bank balance was \$30,609,635 and \$30,983,839, respectively. The bank balance was held by six banks resulting in a concentration of credit risk. Of the bank balance, \$1,250,000 was secured by federal depository insurance and \$29,278,616 was collateralized with securities held by the pledging financial institutions agents in the BPU's name and deposit surety bonds. The third-party bank holding the pledged securities is independent of the pledging bank. The pledged securities are held under a tri-party custodial agreement signed by all three parties: the BPU, the pledging bank, and the independent third-party bank holding the pledged securities. At December 31, 2010, \$81,019 was not adequately collateralized.

(b) Investments

At December 31, 2010 and 2009, the BPU had invested in funds in the State's Municipal Investment Pool. The municipal investment pool is under the oversight of the Pooled Money Investment Board. The board is comprised of the State Treasurer and four additional members appointed by the State Governor. The board reports annually to the Kansas legislature. State pooled monies may be invested in direct obligations that are insured as to principal and interest, by the U.S. government or any agency thereof, with maturities up to four years. No more than ten percent of those funds may be invested in mortgage-backed securities. In addition, the State pool may invest in repurchase agreements with Kansas banks or with primary government securities dealers.

As of December 31, 2010 and 2009, the BPU had the following investments.

Investment Type	Fair Value 2010	Investment Maturities (In Years)	2009	Rating
		Less than 1 year		
Kansas Municipal Investment Pool	\$ 3,793,071	\$ 3,793,071	\$ 2,599,661	S&P AAAF/SLT

Deposits and investments are shown on the combined balance sheets at December 31, 2010 and 2009, as follows:

	2010	2009
Current assets		
Cash and cash equivalents	\$ 7,537,728	\$ 8,971,835
Investments	16,565,000	15,445,000
Noncurrent assets		
Cash and cash equivalents	849,513	2,492,974
Investments	6,416,750	6,535,378
Total	\$ 31,368,991	\$ 33,445,187

4. DEPOSITS AND INVESTMENTS (cont.)

A summary of investments, deposits and cash at December 31, 2010 and 2009, is as follows:

	<u>2010</u>	<u>2009</u>
Total investments	\$ 3,793,071	\$ 2,599,661
Total deposits	27,575,320	30,844,926
Cash on hand	<u>600</u>	<u>600</u>
Total	<u>\$ 31,368,991</u>	<u>\$ 33,445,187</u>

(c) Designated Assets

Certain unrestricted cash and investment amounts that have been designated by Board policy for specific purposes are as follows at December 31:

	<u>Electric</u>	<u>Water</u>	<u>Totals</u>	
			<u>2010</u>	<u>2009</u>
Long Range Electric Supply	\$ 12,684,041	\$ -	\$ 12,684,041	\$ 12,628,075
Long Range Water Supply	-	4,242,703	4,242,703	3,992,703
Workers Comp Insurance Fund	387,829	20,412	408,241	403,113
Office Remodeling	-	-	-	1,000,000
Insurance Reserves	<u>725,000</u>	<u>-</u>	<u>725,000</u>	<u>725,000</u>
Total	<u>\$ 13,796,870</u>	<u>\$ 4,263,115</u>	<u>\$ 18,059,985</u>	<u>\$ 18,748,891</u>

(d) Restricted Assets

Restricted assets were held in the following funds at December 31:

	<u>Electric</u>	<u>Water</u>	<u>Totals</u>	
			<u>2010</u>	<u>2009</u>
Bond Reserve Fund	\$ 1,750,000	\$ 1,043,500	\$ 2,793,500	\$ 2,793,500
Bond Emergency Fund	2,580,000	100,000	2,680,000	2,620,000
Bond and Interest Fund	300,000	263,250	563,250	841,878
Bond Construction Fund	-	343,071	343,071	1,899,661
Health Insurance Fund	429,661	61,380	491,041	463,643
Customer Deposit Fund	398,296	-	398,296	380,886
Refuse Fund	-	(4,890)	(4,890)	5,316
Sewer Fund	<u>-</u>	<u>1,996</u>	<u>1,996</u>	<u>23,467</u>
Total	<u>\$ 5,457,957</u>	<u>\$ 1,808,307</u>	<u>\$ 7,266,264</u>	<u>\$ 9,028,351</u>

The BPU is permitted to invest restricted funds in specified types of investments in accordance with their investment policy until the time such funds are required to be disbursed for their designated purposes.

5. RESERVE FUNDS

In September 1983, the Board established a reserve fund in the water department for long-range water supplies. During 2010 and 2009, \$250,000 and \$250,000, respectively, were transferred into this Board-designated fund. The \$4,242,703 and \$3,992,703 fund balances at December 31, 2010 and 2009, respectively, may be increased or decreased as the Board desires.

5. RESERVE FUNDS (cont.)

In February 1989, the Board established a reserve fund in the electric department for long-range electric requirements. An initial reserve of \$1,500,000 was established with an additional \$1,500,000 to be added annually for ten years. This reserve will also be increased by the income earned on the respective investments. The \$12,684,0041 and \$12,628,075 fund balances at December 31, 2010 and 2009, respectively, may be increased or decreased as the Board desires.

In December 2003, the Board established a reserve fund in the electric department for property and casualty insurance. This reserve was funded from earned surplus. The \$725,000 fund balance at December 31, 2010 and 2009 in this designated fund may be increased or decreased as the Board desires.

6. CAPITAL ASSETS

The following is a summary of capital assets at December 31, 2010:

	Electric Department				
	Balance	Additions	Deletions	Transfers	Balance
	December 31, 2009				December 31, 2010
Land and improvements	\$ 488,728	\$ -	\$ -	\$ -	\$ 488,728
Production plants	48,163,949	-	-	-	48,163,949
Transmission and distribution	36,918,192	662,454	(20,873)	-	37,559,773
General plant	807,030	8,060	-	-	815,090
Construction in progress	3,602,690	3,105,229	(88,310)	(627,946)	5,991,663
	89,980,589	3,775,743	(109,183)	(627,946)	93,019,203
Less accumulated depreciation	(50,764,168)	(2,006,324)	20,873	-	(52,749,619)
Total	\$ 39,216,421	\$ 1,769,419	\$ (88,310)	\$ (627,946)	\$ 40,269,584

	Water Department				
	Balance	Additions	Deletions	Transfers	Balance
	December 31, 2009				December 31, 2010
Land and improvements	\$ 1,309,253	\$ 29,894	\$ -	\$ -	\$ 1,339,147
Production plants	1,281,318	-	-	-	1,281,318
Transmission and distribution	10,346,162	-	-	2,334,535	12,680,697
General plant	38,256	896	-	-	39,152
Construction in progress	10,088,533	1,261,787	-	(1,706,589)	9,643,731
	23,063,522	1,292,577	-	627,946	24,984,046
Less accumulated depreciation	(4,999,284)	(303,276)	-	-	(5,302,560)
Total	\$ 18,064,238	\$ 989,301	\$ -	\$ 627,946	\$ 19,681,486

6. CAPITAL ASSETS (cont.)

The following is a summary of capital assets at December 31, 2009:

	Electric Department				Balance December 31, 2009
	Balance December 31, 2008	Additions	Deletions	Transfers	
Land and improvements	\$ 488,728	\$ -	\$ -	\$ -	\$ 488,728
Production plants	48,615,644	-	(164,413)	(287,282)	48,163,949
Transmission and distribution	36,698,002	544,849	(354,302)	29,643	36,918,192
General plant	493,081	59,586	(32,919)	287,282	807,030
Construction in progress	1,889,684	1,742,649	-	(29,643)	3,602,690
	88,185,139	2,347,084	(551,634)	-	89,980,589
Less accumulated depreciation	<u>(49,284,238)</u>	<u>(1,979,234)</u>	<u>499,304</u>	<u>-</u>	<u>(50,764,168)</u>
Total	<u>\$ 38,900,901</u>	<u>\$ 367,850</u>	<u>\$ (52,330)</u>	<u>\$ -</u>	<u>\$ 39,216,421</u>

	Water Department				Balance December 31, 2009
	Balance December 31, 2008	Additions	Deletions	Transfers	
Land and improvements	\$ 1,309,253	\$ -	\$ -	\$ -	\$ 1,309,253
Production plants	1,281,318	-	-	-	1,281,318
Transmission and distribution	9,985,725	4,292	-	356,145	10,346,162
General plant	35,597	2,659	-	-	38,256
Construction in progress	5,178,965	5,265,713	-	(356,145)	10,088,533
	17,790,858	5,272,664	-	-	23,063,522
Less accumulated depreciation	<u>(4,707,861)</u>	<u>(291,423)</u>	<u>-</u>	<u>-</u>	<u>(4,999,284)</u>
Total	<u>\$ 13,082,997</u>	<u>\$ 4,981,241</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 18,064,238</u>

6. CAPITAL ASSETS (cont.)

Depreciation expense for the year ended December 31, 2010 for the electric and water departments is \$2,006,324 and \$303,276, respectively, as illustrated in the following table:

	Electric Department			Accumulated Depreciation December 31, 2010
	Accumulated Depreciation December 31, 2009	Additions	Transfers/ Deletions	
Production plants	\$ 27,983,653	\$ 882,749	\$ -	\$ 28,866,402
Transmission and distribution	22,141,348	1,070,137	(20,873)	23,190,612
General plant	639,167	53,438	-	692,605
	<u>\$ 50,764,168</u>	<u>\$ 2,006,324</u>	<u>\$ (20,873)</u>	<u>\$ 52,749,619</u>

	Water Department			Accumulated Depreciation December 31, 2010
	Accumulated Depreciation December 31, 2009	Additions	Deletions	
Production plants	\$ 1,122,233	\$ 34,844	\$ -	\$ 1,157,077
Transmission and distribution	3,843,965	266,301	-	4,110,266
General plant	33,086	2,131	-	35,217
	<u>\$ 4,999,284</u>	<u>\$ 303,276</u>	<u>\$ -</u>	<u>\$ 5,302,560</u>

Depreciation expense for the year ended December 31, 2009 for the electric and water departments is \$1,979,234 and \$291,423, respectively, as illustrated in the following table:

	Electric Department			Accumulated Depreciation December 31, 2009
	Accumulated Depreciation December 31, 2008	Additions	Deletions	
Production plants	\$ 27,542,223	\$ 885,420	\$ (443,990)	\$ 27,983,653
Transmission and distribution	21,386,200	1,064,468	(309,320)	22,141,348
General plant	355,815	29,346	254,006	639,167
	<u>\$ 49,284,238</u>	<u>\$ 1,979,234</u>	<u>\$ (499,304)</u>	<u>\$ 50,764,168</u>

	Water Department			Accumulated Depreciation December 31, 2009
	Accumulated Depreciation December 31, 2008	Additions	Deletions	
Production plants	\$ 1,076,409	\$ 45,824	\$ -	\$ 1,122,233
Transmission and distribution	3,599,999	243,966	-	3,843,965
General plant	31,453	1,633	-	33,086
	<u>\$ 4,707,861</u>	<u>\$ 291,423</u>	<u>\$ -</u>	<u>\$ 4,999,284</u>

7. LEASE COMMITMENTS - Non-cancelable Operating Leases

In conjunction with the issuance of \$1,100,000 of Public Building Commission, McPherson, Kansas Revenue Bonds, Series 1994, the BPU entered into a sublease agreement with the City of McPherson. The underlying lease agreement between the Public Building Commission of McPherson, Kansas and the City of McPherson provides for the remodeling, expansion and furnishing of the existing municipal center for occupancy by the City and BPU. The terms of the sublease agreement provide that the BPU assume 50% of the City's obligations, payments and responsibilities under the lease agreement between the Public Building Commission and the City, including specifically the obligation to pay basic rent, additional rent and maintenance costs. On April 1, 2002, the Public Building Commission issued Refunding Revenue, Series 2002 bonds in the amount of \$650,000 to refund Revenue Bonds, Series 1994. Subsequently, the sublease agreement with the City of McPherson was modified to reflect the new payment amounts.

This lease is not subject to cancellation by the BPU so long as any of the bonds remain outstanding. During the year ended December 31, 2009, these bonds were retired. Thus, the lease became cancelable on final bond payment.

For the years ended 2010 and 2009, lease expense was \$60,000 and \$110,000, respectively.

8. INDUSTRIAL DEVELOPMENT PROPERTY

Industrial development property consists of the accumulated costs in various tracts of land held for system expansion or industrial use.

9. POWER SALES AGREEMENTS

In 1972, the BPU entered into a power sales agreement with Westar Energy, formally Kansas Power and Light Company. The agreement, as amended in October 1977 and September 1978, provides that the BPU purchase all of its energy requirements from Westar Energy for resale to its retail and wholesale customers. In return, the BPU is obligated to sell all of its energy production to Westar Energy. The contract specifies that all sales between the entities be sold at fuel cost plus twelve percent. In addition, Westar Energy has agreed to pay the BPU an annual capacity charge that obligates the BPU to have its system available to Westar Energy at all times. The current contract expires in 2027. In April, 2010 the contract was amended to extend the contract 12 years to 2039 and also agreed to begin paying transmission charges based on a Federal Energy Regulatory Commission approved formula tariff.

10. CLAIMS AND JUDGMENTS

The BPU is subject to various laws and regulations with respect to environmental matters such as air and water quality. The effect of any future changes in environmental laws and/or regulations cannot be estimated. However, compliance with such changes may necessitate substantial expenditures.

During the ordinary course of its operations, the BPU is a party to various claims, legal actions and complaints. It is the opinion of the BPU's management and legal counsel that these matters are not anticipated to have a material impact on the Utility.

The BPU is exposed to various risks of loss related to property loss, torts, errors and omissions. The BPU has purchased commercial insurance for these potential risks. There have been no significant reductions in insurance coverage from 2009 to 2010 and there were no settlements that exceeded insurance coverage in the past three years.

11. REVENUE BONDS

The various bond ordinances require that certain restricted funds be established to ensure the payment of bonds and interest and to enable the BPU to meet future needs arising from unusual maintenance requirements or income shortfalls. The ordinances also require the BPU, among other things, to establish rates and collect charges sufficient to pay the operating maintenance and debt service costs of the utilities and to provide net operating income before depreciation and payment in lieu of taxes, of at least 125% for the electric department and 125% for the water department of the maximum annual debt service due on the outstanding bonds. As of December 31, 2010, the BPU exceed this coverage requirement by \$1,800,000 and \$900,000 for electric and water debt, respectively. As of December 31, 2009, the BPU exceeded this coverage requirement by \$2,300,000 and \$769,000, for electric and water debt, respectively. All of the BPU's utility plant facilities are pledged under the terms of the ordinances. The BPU was in compliance with all other requirements of the revenue bond ordinances at December 31, 2010 and 2009.

11. REVENUE BONDS (cont.)

A schedule of the bonded indebtedness of the BPU and a maturity schedule of retirements is as follows:

SCHEDULE OF INDEBTEDNESS

	Original Amount Issued	Interest Rate	Maturity	Water 12-31-10	Electric 12-31-10	Total Outstanding 12-31-10
Water Utility System						
Refunding and Improvement Revenue Bonds, Series 2007	\$ 14,000,000	3.35 to 4.35%	10-01-2027	\$ 12,445,000	\$ -	\$ 12,445,000
Electric Utility System						
Refunding and Improvement Revenue Bonds, Series 2004	\$ 16,705,000	1.15 to 4.50%	3-01-2024	-	13,725,000	13,725,000
				12,445,000	13,725,000	26,170,000
Less unamortized loss on advance refunding				(42,047)	(1,544,548)	(1,586,595)
				12,402,953	12,180,452	24,583,405
Less current maturities				(530,000)	(250,000)	(780,000)
Long-term portion of bonds payable				<u>\$ 11,872,953</u>	<u>\$ 11,930,452</u>	<u>\$ 23,803,405</u>

SUMMARY OF CHANGES IN LONG-TERM DEBT

	Outstanding 12-31-09	Issued	Retired	Refunding	Outstanding 12-31-10
Water Utility System					
Series 2007	\$ 12,960,000	\$ -	\$ 515,000	\$ -	\$ 12,445,000
Electric Utility System					
Series 2004	14,645,000	-	920,000	-	13,725,000
	27,605,000	-	1,435,000	-	26,170,000
Less unamortized loss on refundings	(1,704,388)	-	(117,793)	-	(1,586,595)
	<u>\$ 25,900,612</u>	<u>\$ -</u>	<u>\$ 1,317,207</u>	<u>\$ -</u>	<u>\$ 24,583,405</u>
	Outstanding 12-31-08	Issued	Retired	Refunding	Outstanding 12-31-09
Water Utility System					
Series 2007	\$ 13,455,000	\$ -	\$ 495,000	\$ -	\$ 12,960,000
Electric Utility System					
Series 2004	15,070,000	-	425,000	-	14,645,000
	28,525,000	-	920,000	-	27,605,000
Less unamortized loss on refundings	(1,822,179)	-	(117,791)	-	(1,704,388)
	<u>\$ 26,702,821</u>	<u>\$ -</u>	<u>\$ 802,209</u>	<u>\$ -</u>	<u>\$ 25,900,612</u>

11. REVENUE BONDS (cont.)

Years Ending December 31,	2007 WATER ISSUE			2004 ELECTRIC ISSUE		
	Bonds	Interest	Total	Bonds	Interest	Total
2011	\$ 530,000	\$ 498,612	\$ 1,028,612	\$ 250,000	\$ 588,236	\$ 838,236
2012	550,000	480,592	1,030,592	155,000	579,736	734,736
2013	570,000	461,618	1,031,618	735,000	574,156	1,309,156
2014	590,000	441,668	1,031,668	755,000	546,594	1,301,594
2015	610,000	420,723	1,030,723	785,000	517,378	1,302,378
2016 - 2020	3,430,000	1,742,000	5,172,000	4,860,000	2,071,978	6,931,978
2021 - 2025	4,210,000	983,357	5,193,357	6,185,000	710,502	6,895,502
2026 - 2029	1,955,000	128,542	2,083,542	-	-	-
Total	\$12,445,000	\$ 5,157,112	\$17,602,112	\$13,725,000	\$ 5,588,580	\$19,313,580

12. PAYMENT IN LIEU OF TAXES

The payment of funds to the City of McPherson from the electric department is calculated at the rate of 1.75 and 1.60 mils per kilowatt hours sold for the years ended December 31, 2010 and 2009, respectively. This rate increased to 1.75 mils in April 2010. Payments to the City from the water department are calculated at \$.06 per thousand gallons of water sold for the year ended December 31, 2010 and 2009, respectively. The BPU was required to remit \$1,445,000 and \$1,325,000 in 2010 and 2009 from the electric department. The BPU was required to remit \$72,500 in 2010 and \$46,000 in 2010 and 2009 from the water department. Payments are made quarterly and are deemed to be payments in lieu of taxes.

As a municipal utility, The Board of Public Utilities is exempt from federal and state income taxes.

13. DEFERRED COMPENSATION PLAN

The BPU offers its employees a deferred compensation plan created in accordance with Internal Revenue Code Section 457. The plan is available to all employees who qualify under the plan terms, and permits employees to defer a portion of their salary until future years. The deferred compensation is not available to employees until termination, retirement, death or unforeseeable emergency.

14. EMPLOYEES' RETIREMENT PENSION PLAN

The BPU participates in the Kansas Public Employees Retirement System (KPERS), a cost-sharing multiple-employer defined benefit pension plan as provided by K.S.A. 74-4901, *et seq.* KPERS provides retirement benefits, life insurance, disability income benefits, and death benefits. Kansas law establishes and amends benefit provisions. KPERS issues a publicly available financial report that includes financial statements and required supplementary information. That report may be obtained by writing to KPERS (611 S. Kansas, Suite 100, Topeka, KS 66603) or by calling 1-888-275-5737.

K.S.A. 74-4919 establishes the KPERS member-employee contribution rate at 4% of covered salary. The employer collects and remits member-employee contributions according to the provisions of section 414(h) of the Internal Revenue Code. State law provides that the employer contribution rate be determined annually based on the results of an annual actuarial valuation. KPERS is funded on an actuarial reserve basis. State law sets a limitation on annual increases in the contribution rates for KPERS employers. The employer rate established by statute for calendar year 2010 is 7.14% for the period from January 1, 2010 to December 31, 2010. Included in these rates is the contribution for Group Death and Disability Insurance of 1.0% for the period of January 1, 2010 to December 31, 2010. The BPU employer contributions to KPERS for the years ending December 31, 2010, 2009, and 2008 were \$324,757, \$273,499 and \$262,758, respectively, equal to the required contributions for each year.

15. PRINCIPAL CUSTOMERS

Electric sales to the BPU's five largest customers for the years ended December 31 were as follows:

	2010			
	<u>Sales</u>	<u>Percent of Total Sales</u>	<u>KWH (000)</u>	<u>Percent of Total KWH</u>
National Cooperative Refinery Assoc.	\$ 11,054,068	31.1%	292,775	35.0%
Johns Manville Corp.	5,342,881	15.0%	141,516	16.9%
Hospira	1,725,864	4.9%	45,920	5.5%
Certainteed Corp.	1,372,821	3.9%	35,543	4.2%
Moundridge City	1,332,051	3.8%	29,808	3.6%
Total	<u>\$ 20,827,685</u>	<u>58.7%</u>	<u>545,562</u>	<u>65.1%</u>

	2009			
	<u>Sales</u>	<u>Percent of Total Sales</u>	<u>KWH (000)</u>	<u>Percent of Total KWH</u>
National Cooperative Refinery Assoc.	\$ 11,381,708	34.0%	326,200	39.4%
Johns Manville Corp.	4,871,733	14.5%	132,335	16.0%
Certainteed Corp.	1,532,924	4.6%	42,263	5.1%
Hospira	1,198,903	3.6%	26,957	3.3%
Moundridge City	1,056,818	3.2%	27,298	3.3%
Total	<u>\$ 20,042,086</u>	<u>59.8%</u>	<u>555,053</u>	<u>67.1%</u>

16. POSTEMPLOYMENT HEALTHCARE BENEFITS

Effective January 1, 2008, the BPU adopted GASB Statement No. 45. This statement requires the accounting for the annual cost of other postemployment benefits and the related outstanding liability using an actuarial approach similar to pensions. The BPU implemented prospectively (zero net obligation at transition).

(a) Plan Description

The BPU provides certain postemployment healthcare benefits to eligible retirees and their spouses in accordance with the provisions established by the BPU's Board of Directors. The plan is a single-employer defined benefit healthcare plan self-insured by the City and BPU and administrated by Blue Cross and Blue Shield of Kansas. The plan does not issue separate financial statements. Employees may elect to continue coverage paying 100% of the premium cost the day they retire. To qualify for retirement an employee must be either age 65 with one year of service credit, be age 62 with 10 years of service credit, or at any age when age and years of service equal 85 points. The retiree plan is a comprehensive major medical with a \$200 deductible per person or \$400 per family. The plan pays 80% of the next \$2,500 allowed charges per person or \$5,000 per family with 100% thereafter. The plan has a lifetime maximum of \$2,000,000. Benefits cease at the earlier date the retired employee attains age 65 or death. Retirees become ineligible for health insurance coverage when they qualify for coverage under another health insurance group. Spouse benefits end at the earlier of the date the spouse attains age 65, the date the employee attains age 65, or the spouse's death. There were 76 participants eligible to receive benefits under this plan as of the last valuation date, (December 31, 2008).

(b) Funding Policy

The contribution requirements of plan members and the BPU are established and can be amended by the BPU's board of directors. Contributions are made to the plan on a pay-as-you-go basis. For the years ended December 31, 2010 and 2009, the BPU paid \$64,817 and \$139,056, respectively, for retirees.

16. POSTEMPLOYMENT HEALTHCARE BENEFITS (cont.)

The BPU annual OPEB cost (expense) is calculated based on the annual required contribution of the employer (ARC), and amount actuarially determined in accordance with the parameters 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 amortize any unfunded actuarial liabilities (or funding excess) over a period not to exceed 30 years. The PBU's annual OPEB cost, the percentage of annual OPEB cost contributed to the plan and the net OPEB obligation (asset) for 2010 and 2009 are as follows:

	<u>Annual OPEB Cost</u>	<u>Percentage of Annual OPEB Contributed</u>	<u>Net OPEB Obligation (Asset)</u>
Year Ended:			
December 31, 2009	\$ 45,334	307%	\$ (63,682)
December 31, 2010	46,791	139%	(81,708)

The following table shows the components of BPU's annual OPEB cost for the year, the amount actually contributed to the plan, and changes in the BPU's net OPEB obligation:

	<u>2010</u>	<u>2009</u>
Annual required contribution	\$ 46,791	\$ 45,334
Contributions made	<u>(64,817)</u>	<u>(139,056)</u>
Increase (decrease) in OPEB obligation	(18,026)	(93,722)
Net OPEB obligation (asset) - beginning of year	<u>(63,682)</u>	<u>30,040</u>
Net OPEB obligation (asset) - end of year	<u>\$ (81,708)</u>	<u>\$ (63,682)</u>

(c) Funding Status and Funding Progress

The funded status of the plan as of the most recent valuation date (January 1, 2008) is as follows:

Actuarial accrued liability (AAL)	\$ 459,916
Actuarial value of plan assets	-
Unfunded actuarial accrued liability (UAAL)	\$ 459,916
Funded ratio	0%
Covered payroll	\$ 4,520,743
UAAL as a percentage of covered payroll	10.2%

(d) Actuarial Methods and Assumptions

Actuarial valuations on an ongoing plan involve estimates of the value reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the healthcare trend. Amounts determined regarding the funded status of the plan and the annual required contributions of the employer are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future. The schedule of funding progress, presented as required supplementary information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liabilities for benefits.

Projections of benefits for financial reporting purposes are based on the substantive plan (the plan as understood by the employer and the plan members) and include benefits provided at the time of each valuation and the historical pattern of sharing benefits costs between the employer and plan member to that point. The actuarial methods used include techniques that are designed to reduce the effects of short-term volatility in actuarial accrued liabilities and the actuarial value of assets, consistent with the long-term perspective of the calculations. In the January 1, 2008, actuarial valuation, the Projected Unit Credit actuarial cost method was used. The actuarial assumptions included a 4.5% projected investment rate of return and an annual healthcare cost trend of 8% initially, reduced by decrements to an ultimate rate of 5.0% after six years. The projected salary increase is 3.0%. The unfunded actuarial accrued liability is being amortized over 30 years as a level percent of payroll.

17. SUBSEQUENT EVENT

Management has evaluated the effects on the financial statements of subsequent events occurring through June 8, 2011 which is the date at which the financial statements were available to be issued.

Effective January 1, 2011, the BPU increased electric rates approximately 18.2% to primarily cover increased transmission costs as agreed to in Addendum #5 of the Westar purchase power agreement.

On April 18, 2011, the consensus of the Board was to be ready to call one-half of the 2004 Electric Revenue Bonds in September, 2011.

REQUIRED SUPPLEMENTARY INFORMATION

Board of Public Utilities - McPherson, Kansas

REQUIRED SUPPLEMENTARY INFORMATION
Schedule of Funding Progress - Postemployment

As of the Latest Valuation Date
 December 31, 2008
 (Unaudited)

<u>Actuarial Valuation Date, January 1</u>	<u>Actuarial Value of Assets</u>	<u>Actuarial Accrued Liability (AAL)</u>	<u>Funded Ratio</u>	<u>Unfunded (Overfunded) AAL (UAAL)</u>	<u>Covered Payroll</u>	<u>UAAI as a Percentage of Covered Payroll</u>
2008	\$ -	\$ 459,916	0%	\$ 459,916	\$ 4,520,743	10.2%

ADDITIONAL INFORMATION

Board of Public Utilities - McPherson, Kansas
Summary of Combined Statement of Revenues and Expenses
 Last Ten Fiscal Years

Fiscal Year	Operating Revenues	Operating Expenses	Operating Income	Nonoperating Income (Expense)	Income Before Operating Transfers	Transfers	Change in Net Assets
2001	\$ 30,830,812	\$ 27,753,758	\$ 3,077,054	\$ 600,313	\$ 3,677,367	\$ (1,134,500)	\$ 2,542,867
2002	29,101,084	26,315,328	2,785,756	(215,696)	2,570,060	(1,137,500)	1,432,560
2003	30,243,973	27,348,522	2,895,451	(531,112)	2,364,339	(1,160,000)	1,204,339
2004	31,470,280	28,436,239	3,034,041	363,599	3,397,640	(1,387,000)	2,010,640
2005	33,676,865	30,961,272	2,715,593	(240,873)	2,474,720	(1,225,000)	1,249,720
2006	39,467,165	35,783,700	3,683,465	83,836	3,767,301	(1,332,000)	2,435,301
2007	41,857,772	37,211,221	4,646,551	739,672	5,386,223	(1,371,000)	4,015,223
2008	41,762,003	37,175,668	4,586,335	931,097	5,517,432	(1,357,000)	4,160,432
2009	40,489,845	36,164,029	4,325,816	166,982	4,492,798	(1,371,000)	3,121,798
2010	42,509,533	38,839,866	3,669,667	(198,823)	3,470,844	(1,517,500)	1,953,344

SCHEDULE 2

Board of Public Utilities - McPherson, Kansas
Combined Operating Expenses
 Last Ten Fiscal Years

Fiscal Year	Purchased Power		Production	Distribution and Transmission	Administrative and General	Depreciation and Amortization	Total Operating Expense
	Fuel	\$					
2001	\$ 1,741,603	\$ 16,676,982	\$ 2,243,931	\$ 3,240,696	\$ 1,431,433	\$ 2,419,113	\$ 27,753,758
2002	745,562	16,127,755	2,065,041	3,469,702	1,464,855	2,442,413	26,315,328
2003	946,994	17,081,273	2,291,812	3,070,065	1,492,120	2,466,258	27,348,522
2004	1,011,867	18,036,214	2,434,083	3,106,372	1,612,181	2,235,522	28,436,239
2005	1,344,109	19,513,918	2,348,386	3,692,874	1,653,662	2,408,323	30,961,272
2006	3,048,305	21,990,290	2,943,253	3,616,724	1,705,548	2,479,580	35,783,700
2007	3,474,640	23,012,482	2,452,315	4,201,739	1,738,087	2,331,958	37,211,221
2008	1,660,246	25,323,931	2,135,130	3,756,041	2,021,960	2,278,360	37,175,668
2009	838,736	24,740,416	2,100,432	4,036,358	2,126,283	2,321,804	36,164,029
2010	447,920	26,459,806	3,380,599	4,193,242	1,997,611	2,360,688	38,839,866

SCHEDULE 3

See accompanying independent auditors' report.

**ADDITIONAL INFORMATION
(UNAUDITED)**

Board of Public Utilities - McPherson, Kansas

**COMMENTS AND OPERATING STATISTICS
(UNAUDITED)**

<u>Electric Utility:</u>	<u>2010</u>	<u>2009</u>	<u>Difference Inc. (Dec.)</u>	<u>Percent Inc. (Dec.)</u>
Kilowatt hours (in thousands) -				
Gross generation KWH	4,735	13,810	(9,075)	-65.71%
Purchased from KPL	858,834	848,000	10,834	1.28%
Total generated and purchased	863,569	861,810	1,759	0.20%
Station power generated	150	150	-	0.00%
Sales KWH (000) -				
Residential	70,572	64,229	6,343	9.88%
Commercial	97,067	91,777	5,290	5.76%
Industrial	603,196	610,537	(7,341)	-1.20%
Rural	24,820	23,163	1,657	7.15%
Wholesale	36,261	32,984	3,277	9.94%
Street lighting	3,017	3,029	(12)	-0.40%
Water utility	2,588	1,852	736	39.74%
KPL sales	4,585	13,658	(9,073)	-66.43%
Total sales and station power	842,256	841,379	877	0.10%
System losses	21,313	20,431	882	4.32%
Total customers served (2010 - 8,505; 2009 - 8,480)				
Operating revenue -				
Residential	\$ 3,688,703	\$ 3,227,773		
Commercial	5,255,302	4,862,605		
Industrial	23,316,311	22,384,586		
Rural	1,325,258	1,206,860		
Wholesale	1,641,590	1,486,380		
Street lighting	176,809	215,310		
Water utility	113,119	91,997		
KPL interconnection	3,483,701	3,938,631		
Light rental	36,388	36,346		
Total	\$ 39,037,181	\$ 37,450,488		

The electric department's operations may be separated into two segments. In accordance with a contract entered into with Kansas Power and Light in 1972, the fund purchases all of its energy requirements from KPL for resale to its retail and wholesale customers. In return, the BPU is obligated to sell all of the System's energy production to KPL. In February 1997, the BPU signed an addendum extending the current agreement to 2027. In April 2010 the contract was extended to 2039.

Sales, other than KPL, are segregated between customers inside and outside a three mile limit from the City. Those sales outside the three mile limit are subject to jurisdiction of the Kansas Corporation Commission and such sales approximated 8.40% of total sales in 2010. Expenses attributable to such sales are allocated on the same percentage as sales.

Water Utility:

The water department serves 5,070 residential, 607 commercial and various other city and wholesale customers. Water pumped in 2010 was 1,287,120,000 gallons which was approximately 17% less than 2009. Gross revenue increased 14% from the prior year.