

Under Existing Law, any owner who has purchased such Original Issue Discount Bond in the initial public offering is entitled to exclude from gross income (as defined in section 61 of the Code) an amount of income with respect to such Original Issue Discount Bond equal to that portion of the amount of such original issue discount allocable to the accrual period. For a discussion of certain collateral federal tax consequences, see discussion set forth below.

In the event of the redemption, sale or other taxable disposition of such Original Issue Discount Bond prior to stated maturity, however, the amount realized by such owner in excess of the basis of such Original Issue Discount Bond in the hands of such owner (adjusted upward by the portion of the original issue discount allocable to the period for which such Original Issue Discount Bond was held by such initial owner) is includable in gross income.

Under Existing Law, the original issue discount on each Original Issue Discount Bond is accrued daily to the stated maturity thereof (in amounts calculated as described below for each six-month period ending on the date before the semiannual anniversary dates of the date of the Bonds and ratably within each such six-month period) and the accrued amount is added to an initial owner's basis for such Original Issue Discount Bond for purposes of determining the amount of gain or loss recognized by such owner upon the redemption, sale or other disposition thereof. The amount to be added to basis for each accrual period is equal to (a) the sum of the issue price and the amount of original issue discount accrued in prior periods multiplied by the yield to stated maturity (determined on the basis of compounding at the close of each accrual period and properly adjusted for the length of the accrual period) less (b) the amounts payable as current interest during such accrual period on such Original Issue Discount Bond.

The federal income tax consequences of the purchase, ownership, redemption, sale or other disposition of Original Issue Discount Bonds which are not purchased in the initial offering at the initial offering price may be determined according to rules which differ from those described above. All owners of Original Issue Discount Bonds should consult their own tax advisors with respect to the determination for federal, state and local income tax purposes of the treatment of interest accrued upon redemption, sale or other disposition of such Original Issue Discount Bonds and with respect to the federal, state, local and foreign tax consequences of the purchase, ownership, redemption, sale or other disposition of such Original Issue Discount Bonds.

Collateral Federal Income Tax Consequences

The following discussion is a summary of certain collateral federal income tax consequences resulting from the purchase, ownership or disposition of the Bonds. This discussion is based on existing statutes, regulations, published rulings and court decisions, all of which are subject to change or modification, retroactively.

The following discussion is applicable to investors, other than those who are subject to special provisions of the Code, such as financial institutions, property and casualty insurance companies, life insurance companies, owners of interests in a FASIT, individual recipients of Social Security or Railroad Retirement benefits, individuals allowed an earned income credit, certain S corporations with Subchapter C earnings and profits and taxpayers who may be deemed to have incurred or continued indebtedness to purchase tax-exempt obligations.

THE DISCUSSION CONTAINED HEREIN MAY NOT BE EXHAUSTIVE. INVESTORS, INCLUDING THOSE WHO ARE SUBJECT TO SPECIAL PROVISIONS OF THE CODE, SHOULD CONSULT THEIR OWN TAX ADVISORS AS TO THE TAX TREATMENT WHICH MAY BE ANTICIPATED TO RESULT FROM THE PURCHASE, OWNERSHIP AND DISPOSITION OF TAX-EXEMPT OBLIGATIONS BEFORE DETERMINING WHETHER TO PURCHASE THE BONDS.

Interest on the Bonds will be includable as an adjustment for "adjusted current earnings" to calculate the alternative minimum tax imposed on corporations by section 55 of the Code. Section 55 of the Code imposes a tax equal to 20 percent for corporations, or 26 percent for noncorporate taxpayers (28 percent for taxable income exceeding \$175,000), of the taxpayer's "alternative minimum taxable income," if the amount of such alternative minimum tax is greater than the taxpayer's regular income tax for the taxable year.

Interest on the Bonds may be subject to the "branch profits tax" imposed by section 884 of the Code on the effectively-connected earnings and profits of a foreign corporation doing business in the United States.

Under section 6012 of the Code, holders of tax-exempt obligations, such as the Bonds, may be required to disclose interest received or accrued during each taxable year on their returns of federal income taxation.

Section 1276 of the Code provides for ordinary income tax treatment of gain recognized upon the disposition of a tax-exempt obligation, such as the Bonds, if such obligation was acquired at a "market discount" and if the fixed maturity of such obligation is equal to, or exceeds, one year from the date of issue. Such treatment applies to "market discount bonds" to the

extent such gain does not exceed the accrued market discount of such bonds; although for this purpose, a de minimis amount of market discount is ignored. A "market discount bond" is one which is acquired by the holder at a purchase price which is less than the stated redemption price at maturity or, in the case of a bond issued at an original issue discount, the "revised issue price" (i.e., the issue price plus accrued original issue discount). The "accrued market discount" is the amount which bears the same ratio to the market discount as the number of days during which the holder holds the obligation bears to the number of days between the acquisition date and the final maturity date.

State, Local and Foreign Taxes

Investors should consult their own tax advisors concerning the tax implications of the purchase, ownership or disposition of the Bonds under applicable state or local laws. Foreign investors should also consult their own tax advisors regarding the tax consequences unique to investors who are not United States persons.

REGISTRATION AND QUALIFICATION OF BONDS FOR SALE

The sale of the Bonds has not been registered under the Federal Securities Act of 1933, as amended, in reliance upon the exemption provided thereunder by Section 3(a)(2); and the Bonds have not been qualified under the Securities Act of Texas in reliance upon various exemptions contained therein; nor have the Bonds been qualified under the securities acts of any jurisdiction. The Issuer assumes no responsibility for qualification of the Bonds under the securities laws of any jurisdiction in which the Bonds may be sold, assigned, pledged, hypothecated or otherwise transferred. This disclaimer of responsibility for qualification for sale or other disposition of the Bonds shall not be construed as an interpretation of any kind with regard to the availability of any exemption from securities registration or qualification provisions in such other jurisdictions.

LEGAL INVESTMENTS AND ELIGIBILITY TO SECURE PUBLIC FUNDS IN TEXAS

Pursuant to Section 49.186 of the Water Code, bonds, notes or other obligations issued by a water control and improvement district "shall be legal and authorized investments for all banks, trust companies, building and loan associations, savings and loan associations, insurance companies of all kinds and types, fiduciaries, and trustees, and for all interest and sinking funds and other public funds of the State, and all agencies subdivisions, and instrumentalities of the State, including all counties, cities, towns, villages, school district and all other kinds and types of districts, public agencies and bodies politic." Additionally, Section 49.186 of the Water Code provides that bonds, notes or other obligations issued by a water control and improvement district are eligible and lawful security for all deposits of public funds of the State and all agencies, subdivisions and instrumentalities of the State. For political subdivisions in Texas which have adopted investment policies and guidelines in accordance with the Public Funds Investment Act (Texas Government Code, Chapter 2256), the Bonds may have to be assigned a rating of not less than "A" or its equivalent as to investment quality by a national rating agency before such obligations are eligible investments for sinking funds and other public funds. See "RATINGS" and "MUNICIPAL BOND INSURANCE."

The District makes no representation that the Bonds will be acceptable to banks savings and loan associations, or public entities for investment purposes or to secure deposits of public funds. The District has made no investigation of other laws, regulations or investment criteria which might apply or to otherwise limit the availability of the Bonds for investment or collateral purposes. Prospective purchasers are urged to carefully evaluate the investment quality of the Bonds and as to the acceptability of the Bonds for investment or collateral purposes.

RATING

Moody's Investors Service, Inc. ("Moody's"), has assigned its municipal bond rating of "Aaa" to the Bonds as a result of a financial guaranty insurance policy issued by Ambac Assurance Corporation. An explanation of the rating may be obtained from Moody's. The rating reflects only the views of the organization and the District makes no representation as to the appropriateness of the rating. There is no assurance that such rating will continue for any given period of time or that they will not be revised downward or withdrawn entirely by such rating agency if in the judgment of the agency circumstances so warrant. Any such downward revision or withdrawal of such ratings may have an adverse effect on the market price of the Bonds.

LITIGATION

In the opinion of certain officials of the Issuer, the Issuer is not a party to any litigation or other proceeding pending or, to their knowledge, threatened, in any court, agency or other administrative body (either state or federal) which, if decided adversely to the Issuer, would have a material adverse effect on the financial condition of the Issuer.

UNDERWRITING

The Underwriters have agreed, subject to certain conditions, to purchase the Bonds from the District at a purchase price, exclusive of accrued interest, of \$4,522,006.60 (which includes an underwriting discount of \$31,944.20 and a net premium of \$43,950.80). The Underwriters will be obligated to purchase all of the Bonds if any Bonds are purchased. The Bonds to be offered to the public may be offered and sold to certain dealers (including the Underwriters and other dealers depositing Bonds into investment trusts) at prices lower than the public offering prices of such Bonds, and such public offering prices may be changed from time to time by the Underwriters.

The Underwriters have provided the following sentence for inclusion in this Official Statement. The Underwriters have reviewed the information in the Official Statement in accordance with, and as part of, their responsibility to investors under the federal securities laws as applied to the facts and circumstances of this transaction, but the Underwriters do not guarantee the accuracy or completeness or such information.

VERIFICATION OF ARITHMETICAL AND MATHEMATICAL CALCULATIONS

Grant Thornton LLP will verify from the information provided to them the mathematical accuracy as of the date of the closing on the Bonds of (1) the computations contained in the provided schedules to determine that the anticipated receipts from the securities and cash deposits listed in the Financial Advisor's schedules, to be held in escrow, will be sufficient to pay, when due, the principal, interest and call premium payment requirements, if any, of the Refunded Bonds, and (2) the computations of yield on both the securities and the Bonds contained in the provided schedules used by Bond Counsel in their determination that the interest on the Bonds is exempt from tax. Grant Thornton LLP will express no opinion on the assumptions provided to them, nor as to the exemption from taxation of the interest on the Bonds.

LEGAL OPINIONS

The District will furnish a complete transcript of proceedings incident to the authorization and issuance of the Bonds, including the unqualified approving legal opinion of the Attorney General of the State of Texas to the effect that the initial Bonds are valid and binding obligations of the District payable from the proceeds of an annual ad valorem tax levied, without legal limit as to rate or amount upon all taxable property within the District. Issuance of the Bonds is also subject to the legal opinion of McCall, Parkhurst & Horton L.L.P. ("Bond Counsel") with respect to the Bonds issued in compliance with the provisions of the Bond Order, which opinion is attached to this Official Statement as Appendix D. Bond Counsel was not requested to participate, and did not take part, in the preparation of the Official Statement, and such firm has not assumed any responsibility with respect thereto or undertaken independently to verify any of the information contained therein, except that, in its capacity as Bond Counsel, such firm has reviewed the information under the captions "PLAN OF FINANCING" (except in the subheadings "Purpose," and "Sources and Uses of Funds"), "DESCRIPTION OF THE BONDS" (except in the subheading "Book-Entry-Only System"), "SECURITY FOR THE BONDS," "SUMMARY OF SELECTED PROVISIONS OF THE BOND DOCUMENTS," "TAX MATTERS," "REGISTRATION AND QUALIFICATION OF BONDS FOR SALE," "LEGAL INVESTMENTS AND ELIGIBILITY TO SECURE PUBLIC FUNDS IN TEXAS," "LEGAL OPINIONS," and "CONTINUING DISCLOSURE OF INFORMATION" (except in the subheading "Compliance with Prior Undertakings") and is of the opinion that the information relating to the Bonds and the Bond Order contained therein fairly and accurately describes the provisions thereof and is correct as to matters of law. The legal opinion will accompany the Bonds deposited with DTC or will be printed on the Bonds in the event of the discontinuance of the Book-Entry-Only System. In connection with the transaction described in this Official Statement, McCall, Parkhurst & Horton L.L.P. has been engaged by, and only represents, the District. Certain legal matters will be passed upon for the Underwriters by Andrews & Kurth L.L.P.

The legal fees to be paid Bond Counsel for services rendered in connection with the issuance of the Bonds are based upon a percentage of Bonds actually issued, sold and delivered, and therefore, such fees are contingent upon the sale and delivery of the Bonds. The legal opinions to be delivered concurrently with the delivery of the Bonds express the professional judgment of the attorneys rendering the opinions as to the legal issues explicitly addressed therein. In rendering a legal opinion, the attorney does not become an insurer or guarantor of that expression of professional judgment, of the transaction opined upon, or of the future performance of the parties to the transaction. Nor does the rendering of an opinion guarantee the outcome of any legal dispute that may arise out of the transaction.

FORWARD-LOOKING STATEMENTS

The statements contained in this Official Statement, and in any other information provided by the District and the City, that are not purely historical, are forward-looking statements, including statements regarding the District and City's expectations, hopes, intentions, or strategies regarding the future. Readers should not place undue reliance on forward-looking statements. All forward-looking statements included in this Official Statement are based on information available to the District and City of the date hereof, and the District and City assume no obligation to update any such forward-looking statements. The District and City's actual results could differ materially from those discussed in such forward-looking statements.

The forward-looking statements included herein are necessarily based on various assumptions and estimates and are inherently subject to various risks and uncertainties, including risks and uncertainties relating to the possible invalidity of the underlying assumptions and estimates and possible changes or developments in social, economic, business, industry, market, legal, and regulatory circumstances and conditions and actions taken or omitted to be taken by third parties, including customers, suppliers, business partners and competitors, and legislative, judicial, and other governmental authorities and officials. Assumptions related to the foregoing involve judgments with respect to, among other things, future economic, competitive, and market conditions and future business decisions, all of which are difficult or impossible to predict accurately and many of which are beyond the control of the District and City. Any of such assumptions could be inaccurate and, therefore, there can be no assurance that the forward-looking statements included in this Official Statement will prove to be accurate.

CONTINUING DISCLOSURE OF INFORMATION

Continuing Disclosure Undertaking of the District

General In the Bond Order, the District has made the following agreement for the benefit of the Registered and Beneficial Owners (the "Owners") of the Bonds. The District is required to observe the agreement for so long as it remains obligated to advance funds to pay the Bonds. Under the agreement, the District will be obligated to provide certain updated financial information and operating data annually, and timely notice of specified material events, to certain information vendors. This information will be available to securities brokers and others who subscribe to receive the information from the vendors.

Annual Reports The District will provide certain updated financial information and operating data to certain information vendors annually. The information to be updated includes all quantitative financial information and operating data with respect to the District of the general type included in this Official Statement under Table 1. The District will update and provide this information within six months after the end of each fiscal year ending in or after 2003. The District will provide the updated information to each nationally recognized municipal securities information repository ("NRMSIR") and to any state information depository ("SID") that is designated by the State of Texas and approved by the staff of the United States Securities and Exchange Commission (the "SEC").

The District may provide updated information in full text or may incorporate by reference certain other publicly available documents, as permitted by SEC Rule 15c2-12 (the "Rule"). The updated information will include annual audited financial statements for the Issuer, if the Issuer commissions an audit and it is completed by the required time. If audited financial statements are not available by the required time, the Issuer will provide unaudited statements and audited financial statements when and if such audited financial statements become available. Any such financial statements of the Issuer will be prepared in accordance with the accounting principles described in Appendix A hereof or such other accounting principles as the District may be required to employ from time to time pursuant to state law or regulation.

The District's current fiscal year end is September 30, 2003. Accordingly, it must provide updated information by March 31 in each year, unless the District changes its fiscal year. If the District changes its fiscal year, it will notify each NRMSIR and any SID of the change.

Material Event Notices The District will also provide timely notices of certain events to certain information vendors. The District will provide notice of any of the following events with respect to the Bonds if such event is material to a decision to purchase or sell Bonds: (1) principal and interest payment delinquencies; (2) non-payment related defaults; (3) unscheduled draws on debt service reserves reflecting financial difficulties; (4) unscheduled draws on credit enhancements reflecting financial difficulties; (5) substitution of credit or liquidity providers, or their failure to perform; (6) adverse tax opinions or events affecting the tax-exempt status of the Bonds; (7) modifications to rights of holders of the Bonds; (8) Bond calls; (9) defeasances; (10) release, substitution, or sale of property securing repayment of the Bonds; and (11) rating changes. Neither the Bonds nor the Bond Order make any provision for debt service reserves, redemption, or liquidity enhancement. In addition, the Issuer will

provide timely notice of any failure by the Issuer to provide information, data, or financial statements in accordance with its agreement described above under "Annual Reports". The Issuer will provide each notice described in this paragraph to any SID and to either each NRMSIR or the Municipal Securities Rulemaking Board ("MSRB").

Continuing Disclosure Undertaking of City

General Pursuant to resolution, the City has made the following agreement for the benefit of the Owners of the Bonds. The City will be required to observe the agreement for so long as the City remains obligated to advance funds to pay the Bonds. Under the agreement, the City will be obligated to provide certain updated financial information and operating data annually to certain information vendors. This information will be available to securities brokers and others who subscribe to receive the information from the vendors.

Annual Reports The City will provide certain updated financial information and operating data to certain information vendors annually. The information to be updated includes all quantitative financial information and operating data with respect to the City of the general type included in the numbered tables appearing in Appendix A of this Official Statement and the annual financial report of the City incorporated by reference in Appendix A. The City will update and provide this information within six months after the end of each fiscal year. The City will provide the updated information to each NRMSIR and to any SID.

The City may provide updated information in full text or may incorporate by reference certain other publicly available documents, as permitted by Rule 15c2-12. The updated information will include audited financial statements, if the City commissions audits and such are completed by the required time. If audited financial statements are not available by the required time, the City will provide unaudited financial statements by the required time, and will provide audited financial statements when and if such audit report becomes available. Any such financial statements will be prepared in accordance with the accounting principles as the City may be required to employ from time to time pursuant to state law or regulation.

The City's current fiscal year end is September 30. Accordingly, updated information must be provided by March 31 in each year, unless the City changes its fiscal year. If the City changes its fiscal year, it will notify each NRMSIR and any SID or the change.

Material Event Notices The City will provide timely notice of any failure by the City to provide information, data or financial statements in accordance with its agreement described above under "Annual Reports." The City will provide each notice described in this paragraph to any SID and to either each NRMSIR or the MSRB.

Availability of Information from NRMSIRs and SID

The District and the City have agreed to provide the foregoing information only to NRMSIRs or the MSRB and any SID. The information will be available to holders of Bonds only if the holders comply with the procedures and pay the charges established by such information vendors or obtain the information through securities brokers who do so.

The Municipal Advisory Council of Texas has been designated by the State of Texas as a SID, and recognized by the staff of the SEC as a SID. The address of the Municipal Advisory Council is 600 West 8th Street, P.O. Box 2177, Austin, Texas 78768-2177, and its telephone number is 512/476-6947. Its internet address is www.mactexas.com.

Limitations and Amendments

The District and the City have agreed to update information and to provide notices of material events only as described above. Neither has agreed to provide other information that may be relevant or material to a complete presentation of the financial results of operations, condition, or prospects of the Issuer, or agreed to update any information that is provided, except as described above. Neither makes any representation or warranty concerning such information or concerning its usefulness to a decision to invest in or sell Bonds at any future date. Each disclaims any contractual or tort liability for damages resulting in whole or in part from any breach of its continuing disclosure agreement or from any statement made pursuant to its agreement, although holders of Bonds may seek a writ of mandamus to compel the District and the City to comply with this agreement.

The District and the City may amend their continuing disclosure agreement to adapt to changed circumstances that arise from a change in legal requirements, a change in law, or a change in the identity, nature, status, or type of operations of the District and the City, if the agreement, as amended, would have permitted an underwriter to purchase or sell Bonds in the offering described herein in compliance with the Rule, taking into account any amendments or interpretations of the Rule to the date of such amendment, as well as such changed circumstances, and either the holders of a majority in aggregate principal amount of the outstanding Bonds consent or any person unaffiliated with the District and the City (such as nationally-recognized bond counsel)

determines that the amendment will not materially impair the interests of the beneficial owners of the Bonds. The District and the City may also repeal or amend the provisions of their continuing disclosure agreement if the SEC amends or repeals the applicable provisions of the Rule or any court of final jurisdiction enters judgment that such provisions of the Rule are invalid, and the District and the City also may amend these provisions in their discretion in any *other manner or circumstance*, but in either case, only if and to the extent, that the provisions of this sentence would not have prevented an underwriter from lawfully purchasing or selling the Bonds in the primary offering of the Bonds, giving effect to (a) such provisions as so amended and (b) any amendments or interpretations of the Rule. If the District and the City amend their agreement, they must include with the next financial information and operating data provided in accordance with their agreement described above under "Annual Reports" an explanation, in narrative form, of the reasons for the amendment and of the impact of any change in the type of information and data provided.

Compliance with Prior Agreements

The District became obligated in 1999 to make annual disclosure of certain financial information in connection with the District's Unlimited Tax and Revenue Bonds, Series 1999. The District updated the pertinent information and has made filings each year with the SID but inadvertently failed to file the reports with the NRMSIRS on a timely basis for the years 2000 and 2001. The District has made a "Material Event" filing on May 22, 2003 concerning this matter with the SID and the NRMSIRS. In addition, the District has established procedures to assure future compliance in a timely manner by engaging the District's Financial Advisor to assist with continue disclosure filings.

During the past five years, the City has complied in all material respects with continuing disclosure agreements made by it in accordance with SEC Rule 15c2-12.

PREPARATION OF THE OFFICIAL STATEMENT

Financial Advisor

Coastal Securities is employed as the Financial Advisor to the District to render certain professional services, including advising the Issuer on a plan of financing and assisting in the preparation of the Official Statement, for the sale of the Bonds. In its capacity as Financial Advisor, Coastal Securities has assisted in compiling certain financial information and editing this Official Statement. The Financial Advisor has not, however, independently verified the factual information contained in this Official Statement nor has it conducted an investigation into the affairs of persons or firms referred to in this Official Statement for the purpose of passing upon the accuracy or completeness of this Official Statement. The fees for Financial Advisor are contingent upon the issuance, sale and delivery of the Bonds.

Sources of Information

The financial data and other information contained in this Official Statement has been obtained primarily from the District's records, the City's records, the Engineer, and information from other sources. All of these sources are believed to be reliable, but no guarantee is made by the Issuer as to the accuracy or completeness of the information derived from such sources, and its inclusion herein is not to be construed as a representation on the part of the District to such effect. Furthermore, there is no guarantee that any of the assumptions or estimates contained herein will be realized. The summaries of the agreements, reports, statutes, orders, engineering and other related information set forth in the Official Statement are included herein subject to all of the provisions of such documents. These summaries do not purport to be complete statements of such provisions, and reference is made to such documents for further information.

The District has not, however, independently verified the factual information contained in this Official Statement nor has it conducted an investigation into the affairs of persons or firms referred to in this Official Statement for the purpose of passing upon the accuracy or completeness of this Official Statement.

MISCELLANEOUS

All estimates, statements and assumptions in this Official Statement and the Appendices hereto have been made on the basis of the best information available and are believed to be reliable and accurate. Any statements in this Official Statement involving matters of opinion or estimates, whether or not expressly so stated, are intended as such and not as representations of fact, and no representation is made that any such statements will be realized.

This Official Statement was approved by the Board of Directors of North Austin Municipal Utility District No. 1, as of the date shown on the cover page.

/s/ Terry Ripperda
President, Board of Directors
North Austin Municipal Utility District No. 1

ATTEST:

/s/ Chuck Simms
Secretary, Board of Directors
North Austin Municipal Utility District No. 1

Schedule I
Schedule of Refunded Bonds

| Bond | Maturity Date | Interest Rate | Par Amount | Call Date | Call Price |
|------------------|----------------------|----------------------|-------------------|------------------|-------------------|
| Contract Revenue | 11/15/2004 | 4.70% | \$1,230,000 | 11/15/2003 | 100.00 |
| Refunding Bonds, | 11/15/2005 | 4.80% | 1,305,000 | 11/15/2003 | 100.00 |
| Series 1994 | 11/15/2006 | 4.90% | 1,385,000 | 11/15/2003 | 100.00 |
| | 11/15/2007 | 5.00% | 1,465,000 | 11/15/2003 | 100.00 |
| | 11/15/2008 | 5.00% | 1,545,000 | 11/15/2003 | 100.00 |
| | 11/15/2009 | 5.00% | 1,740,000 | 11/15/2003 | 100.00 |

APPENDIX A

Information Regarding the City of Austin's Combined Utility Systems

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APPENDIX A

City of Austin Information Generally

The City of Austin has heretofore filed with each NRMSIR and the SID its official statement with respect to that certain issue of \$121,500,000 City of Austin, Texas Water and Wastewater System Revenue Refunding Bonds, Series 2003. The date of such official statement is February 6, 2003. In such official statement, under the heading CONTINUING DISCLOSURE OF INFORMATION, the City has agreed to update annually quantitative financial information and operating data with respect to the Systems of the general type included in the main text of such official statement within the numbered tables only and to provide annual updates to the excerpts of the City's annual financial reports incorporated by reference in the next paragraph of this Appendix A.

The above-described financial information, operating data and financial report with respect to the City of Austin is hereby incorporated by reference into this Official Statement. Copies of the aforesaid official statement and financial report of the City of Austin may be examined at the offices of each NRMSIR and the SID in accordance with applicable rules of each such entity governing the examination of such official statement.

Excerpts of the City's Official Statement

Below are excerpts of certain information of the City as set forth in the City's February 6, 2003 official statement. Numbered tables appearing in this Appendix A are numbered in accordance with numbering used by the City of Austin in the above-referenced official statement (and not in the order of their appearance herein).

THE SYSTEMS

The City owns and operates an Electric Utility System (also referred to herein as "Austin Energy") and a Water and Wastewater System (also referred to herein as the Water and Wastewater Utility) which provide the City, adjoining areas of Travis County and certain adjacent areas of Williamson County with electric, water and wastewater services. The City owns all the facilities of the Water and Wastewater System. The City jointly participates with other electric utilities in the ownership of coal-fired electric generation facilities and a nuclear powered electric generation facility. Additionally, the City individually owns gas/oil-fired electric generation facilities, which are available to meet system demand. The City constructed a new 180 MW gas fired peaking facility in partnership with Enron North America Corporation which became commercial in June 2001. Under the Agreement with Enron, the City will have complete ownership of the plant in November 2003. The Electric Utility System had approximately 1,376 full-time regular employees as of September 30, 2002. The Water and Wastewater System had approximately 881 full-time regular employees as of the same date.

THE WATER AND WASTEWATER SYSTEM

Management

| Name | Title | Length of Service with City |
|----------------------|--|-----------------------------|
| Chris Lippe, P.E. | Director, Water and Wastewater Utility | 18 Years, 8 Months |
| Perwez Moheet, CPA | Assistant Director, Finance and Business Services | 23 Years, 8 Months |
| Jane Burazer | Assistant Director, Treatment | 9 Years, 2 Months |
| Reynaldo Cantu, P.E. | Assistant Director, Engineering | 12 Years, 6 Months |
| Andrew Covar, P.E. | Assistant Director, Water Resource Planning and Analysis | 9 Years, 6 Months* |
| David Juarez, P.E. | Assistant Director, Operations and Maintenance | 11 Years, 9 Months* |

*Length of service not continuous.

WATER SYSTEM

Service Area

The City supplies treated water to residential and commercial customers within the corporate limits of the City and to a portion of Travis and Williamson Counties. The presently defined service area totals approximately 450 square miles. The City also has contracted to supply treated water on a wholesale basis to seven municipal utility districts (MUDs), one water

control and improvement district, seven water supply corporations, one private utility, and the Cities of Rollingwood, Pflugerville and Sunset Valley.

The City has previously acquired the systems and assets of eleven water control and improvement districts. The City has paid off and canceled the bonded indebtedness of eight of these districts and is presently paying, from surplus revenues of the Water and Wastewater Utility, the unpaid bonded indebtedness of the other three districts. The Texas Commission on Environmental Quality (TCEQ, the successor agency to the Texas Natural Resource Conservation Commission, which was the successor agency to the Texas Water Commission) is empowered to grant the City a certificate of convenience and necessity to provide water and wastewater service to retail customers outside the City's boundaries. The City is not required to obtain such a certificate. References to the TCEQ in this Official Statement are intended to include agencies whose duties and responsibilities have been assumed by the TCEQ.

Water Supply

In 1888, City leaders campaigned successfully for the first Austin Dam across the Colorado River, which was completed early in 1893. In 1934, a \$4,500,000 loan and grant was obtained from the Public Works Administration to complete the Buchanan Dam. LCRA finished the dam (which is 150 feet high, 11,200 feet long), and the lake it forms is thirty-two miles long and two miles wide, covering 23,000 surface acres.

Since that time, a stairway of lakes was created by building five additional dams, giving the area 150 miles of lakes. The Tom Miller Dam is within the City limits, and forms Lake Austin, which covers 3,000 surface acres; Mansfield Dam, the fifth largest masonry dam in the world, impounds Lake Travis, which covers 42,000 acres; Marble Falls Dam creates Lake Marble Falls, which spreads over 900 acres; Lake Lyndon B. Johnson, held by Alvin Wirtz Dam, has an area of 6,300 acres; and Roy Inks Dam forms Inks Lake, with a surface of 900 acres. The City owns Tom Miller Dam and has leased it to LCRA through December 31, 2020. The other dams are owned by LCRA.

The combined storage capacity of the six lakes is around 3,300,000 acre-feet of water, or more than a trillion gallons. Approximately 800,000 acre feet of this is reserved for flood control. Of the six dams on the Colorado River, two form major impounding reservoirs for the control of flood water; however, Mansfield Dam is the only designated flood control structure.

The City has also constructed Longhorn Dam on the Colorado River just downstream of Lake Austin, and Decker Dam on Decker Creek, a tributary of the Colorado River that joins the river downstream of Longhorn Dam. Town Lake, which has a capacity of approximately 3,500 acre-feet, is created by Longhorn Dam. Decker Dam creates Lake Walter E. Long, which has a capacity of approximately 34,000 acre-feet.

United States Geological Survey records at Austin gauging station No. 08158000 show the following flows for the water year (October 1 through September 30).

| | | |
|----------------------------|----------------------------|----------------------------|
| 1973 - 896,400 Acre Feet | 1983 - 587,000 Acre Feet | 1993 - 978,000 Acre Feet |
| 1974 - 1,463,000 Acre Feet | 1984 - 764,000 Acre Feet | 1994 - 708,200 Acre Feet |
| 1975 - 3,039,000 Acre Feet | 1985 - 751,000 Acre Feet | 1995 - 896,700 Acre Feet |
| 1976 - 992,600 Acre Feet | 1986 - 886,500 Acre Feet | 1996 - 758,300 Acre Feet |
| 1977 - 1,956,000 Acre Feet | 1987 - 3,399,000 Acre Feet | 1997 - 3,013,512 Acre Feet |
| 1978 - 885,100 Acre Feet | 1988 - 834,000 Acre Feet | 1998 - 1,313,831 Acre Feet |
| 1979 - 867,200 Acre Feet | 1989 - 667,900 Acre Feet | 1999 - 803,240 Acre Feet |
| 1980 - 803,500 Acre Feet | 1990 - 692,300 Acre Feet | 2000 - 627,370 Acre Feet |
| 1981 - 1,626,000 Acre Feet | 1991 - 829,700 Acre Feet | 2001 - 1,371,435 Acre Feet |
| 1982 - 1,356,000 Acre Feet | 1992 - 5,419,000 Acre Feet | 2002 - 1,674,985 Acre Feet |

Using the twenty-five years from 1978-2002, the average flow was 1,300,551 acre feet per year. Using the lowest year, 1983, the flow for the Colorado River at Austin was 587,000 acre feet, or 192 billion gallons, which is over 4 times the amount of water treated for distribution (50.2 billion gallons) by the City for the fiscal year ended September 30, 2001.

Water Rights. The City holds independent rights to impound, divert and use the waters of the Colorado River and its tributaries, and additional rights to such water pursuant to agreements with LCRA.

The City's independent water rights have been adjudicated before the TCEQ in accordance with the Texas Water Right Adjudication Act, Texas Water Code Section 11.301, et seq. The City's rights, as determined by the TCEQ, are set forth in the Final Determination of all claims of Water Rights in the Lower Colorado River Segment of the Colorado River Basin

issued by the TCEQ on July 29, 1985. Both the City and LCRA appealed the Final Determination, seeking additional rights and contesting the rights awarded to each other, in a proceeding styled In Re: The Exceptions of the Lower Colorado River Authority and the City of Austin to the Adjudication of Water Rights in the Lower Colorado River Segment of the Colorado River Basin, Cause No. 115,414-A-1 in the District Court of Bell County, Texas, 264th Judicial District ("Cause No. 115,414-A-1").

The City and LCRA entered into a Comprehensive Water Settlement Agreement (the "Settlement Agreement") in settlement of Cause No. 115 414-A-1 on December 10, 1987. The Settlement Agreement generally improves the independent water rights of both the City and LCRA. Such rights for the City include: the rights to maintain Tom Miller Dam and Lake Austin, Longhorn Dam and Town Lake, and Decker Dam and Lake Walter E. Long; the right to divert and use 271,403 run of the river acre-feet of water per year from Lake Austin and Town Lake for municipal purposes; the right to divert and circulate an unlimited amount of water per year from Town Lake for industrial purposes, so, as to consumptively use not to exceed 24,000 acre-feet per year; the right to divert and circulate water from Lake Walter E. Long for industrial purposes, so as to consumptively use not to exceed 16,156 acre-feet per year; and the right to divert and use water through Tom Miller Dam for the generation of hydroelectric power. LCRA's independent water rights, as determined by the TCEQ, include the rights to maintain Lakes Travis and Buchanan and to divert and use water therefrom. Pursuant to the Settlement Agreement and the final judgment in Cause No. 115,414-A-1, certain other pending water-related disputes between the City and LCRA were settled. LCRA was granted an option to acquire up to a 50% undivided interest in the City's proposed Water Treatment Plant No. 4 (discussed under "Water Treatment Plants", below). The District Court issued a final judgment consistent with the Settlement Agreement. Certificates of Adjudication have been issued by the TCEQ.

Pursuant to previous agreements between the City and LCRA, LCRA has agreed to supply the City additional water from storage in Lakes Travis and Buchanan. The City also has leased Tom Miller Dam, and the City's right to divert and use water for the generation of hydroelectric power through Tom Miller Dam, to LCRA. The Settlement Agreement provided for the City to receive water from Lake Travis for the proposed Water Treatment Plant No. 4, and for additional water for municipal and other purposes of use downstream of Lake Travis.

The City and LCRA executed the First Amendment to the December 10, 1987 Comprehensive Water Settlement Agreement (the "First Amendment") on October 7, 1999. This First Amendment extends the existing Settlement Agreement through the year 2050, and gives the City a 50-year assured water supply by providing additional water that the City can take from the Highland Lakes, a chain of lakes formed on the Colorado River that includes Lake Travis, Lake Austin and Town Lake. Additionally, the First Amendment includes an option for the City to renew the Settlement Agreement through the year 2100, a full century of water supply. The City paid a discounted amount of \$100.0 million to the LCRA as part of the First Amendment contract provisions. The \$100.0 million payment to LCRA included compensation for the following terms:

- Pre-paid reservation fee for an additional 75,000 firm acre-feet of water supply, which increased the City's total water supply from 250,000 firm acre-feet to 325,000 firm acre-feet for the additional 50-year period with an option to renew for another additional 50-year period.
- Pre-paid water use charges that would be paid by the City for water use above 150,000 firm acre-feet up to 201,000 firm acre-feet.

As a result of this amendment, the City will not have to pay any additional raw water costs to the LCRA until such time as the City begins diverting over 201,000 firm acre-feet per year. The City projects water usage above 201,000 firm acre-feet in approximately the year 2021. The amendment also had numerous provisions that benefited the City. Also, a legal issue regarding the building of Water Treatment Plant No. 4 was settled. The First Amendment provides for mutual release of the City and LCRA from any claims or causes of action relating to the delayed construction of Water Treatment Plant No. 4.

Water Treatment Plants

The City's Water and Wastewater Utility has three water treatment plants (Green, Davis and Ullrich) which have a rated capacity of 260 million gallons per day ("mgd"). The water treatment plants have a combined clear well storage capacity of 38.8 million gallons on site. The City's Water and Wastewater Utility includes a water distribution system having 2,872 miles of water mains of varying diameters, distribution storage facilities with an effective storage capacity of 250 million gallons, 26,303 fire hydrants and forty-two booster pump stations.

The City receives its water supply from the Colorado River through the three water treatment plants. The Green Plant takes water from Town Lake, which is located near the downtown area of the City. The Davis Plant and the Ullrich Plant both take water from Lake Austin.

The Green Plant is located east of Shoal Creek near its junction with the Colorado River and has a rated capacity of 35 mgd. An intake station on the river contains four traveling water screens and four raw water pumps. The Green Plant was

constructed in 1924 and expanded in 1935, 1938, 1949 and 1985. The firm pumping capacity (i.e., with one of the largest pumps out of service) is 42 mgd. Water is pumped through a forty-two inch line to the chemical feed building, where it is split into two parallel treatment units. The Green Plant operates on a site that limits any major expansion or upgrading of treatment processes. Its capacity can be replaced by the planned expansion of the Ullrich Plant. If the requirements for the Safe Drinking Water Act ("SDWA") Phase II Disinfection/Disinfection By-Products Rule require expensive space consuming modifications, the aging Green Plant may need to be replaced by the year 2005. Without the restrictions of this proposed rule, it could continue in service.

The Davis Plant, located at Mount Bonnell Road and West 35th Street, has a rated capacity of 118 mgd. The plant is of conventional design, with rapid mix basins, flocculation basins, sedimentation basins, gravity filters, clearwell storage, and raw water and finished water pumping stations. The plant was constructed in 1954 and expanded in 1963, 1975 and 1986.

The Ullrich Plant, located on a site south of Red Bud Trail and Forest View Drive, has a rated capacity of 100 mgd. The existing plant facilities consist of an intake and raw water pumping station, raw water transmission main, six upflow-solids contact clarifiers, twelve filters, chlorine disinfection, clearwell reservoir, high service pumping station, and sludge handling facilities. A 60 mgd upgrade to the Ullrich Plant is currently in the engineering design phase with construction scheduled to be completed in 2005. This expansion will increase the rated capacity of the plant to 160 mgd.

Construction of Water Treatment Plant No. 4 will add incremental initial capacity of up to 50-75 million gallons per day with an intake structure rated at 100 to 300 million gallons per day. Based on revised growth projections, the City anticipates that construction of Water Treatment Plant No. 4 will begin within the next 5 years. \$141 million of bonds have been authorized for this project based on an earlier schedule under which the plant would have already been built. That project was deferred in the late 1980's. Additional costs incurred due to the revised timing are anticipated to be funded with current revenues and additional bond authority the Water and Wastewater Utility will seek in a future bond election.

Water Conservation Plan

The Water and Wastewater Utility developed a water conservation plan for emergency purposes in the early 1980's after experiencing an equipment failure in the distribution system during a high summer demand period. Although the problems were short lived, they had sufficient impact to cause the development of a plan for any potential future problems. The plan is designed to educate customers to use water effectively and to reduce the peak demands on the Water and Wastewater Utility. The contingency plan, which is in effect from May 1 to September 30 of each year, has three stages with progressively more restrictive water use provisions. The plan is presently designed to shift from voluntary to mandatory stages when daily pumpage exceeds a specific limit established by the City Manager which relates to treatment capacity. If higher levels of pumpage should occur, the plan would move to one of the more restrictive mandatory levels. Currently, the treatment facilities have a rated capacity of 260 mgd. Mandatory water restrictions were required during the extreme drought conditions of July through September 2000. Inclining block rates implemented April 1, 1994, are designed to promote water conservation by Single Family Residential Customers. Seasonal rates implemented in 2000 are also designed to promote water conservation.

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Water Storage and Pumping Facilities

In addition to the water treatment plants, the Water and Wastewater Utility owns and operates the following storage facilities and major water pump stations.

| | Total Storage Capacity (Millions of Gallons) | Firm Pumping Capacity (Gallons per Minute) |
|--------------------------|--|---|
| North System | | |
| Anderson Mill (1) | 3 | n/a |
| East Austin | 12 | 33,300 |
| Forest Ridge | 3 | 5,000 |
| Four Points (ground) | 7 | 0 |
| Four Points (elevated) | 1 | 3,600 |
| Guilford Cove | 0.275 | 600 |
| Highland Park | 2 | 1,000 |
| Howard Lane | 20 | 50,000 |
| Jollyville | 11 | 51,000 |
| Martin Hill (1) | 34 | n/a |
| North Austin | 10 | 39,800 |
| Pond Springs (1) | 3 | n/a |
| Spicewood Springs | 10 | 59,000 |
| South System | | |
| Capital of Texas Hwy (1) | 0.5 | n/a |
| Center Street | 8 | 31,400 |
| Davis Lane | 20 | 29,500 |
| La Crosse (1) | 2 | n/a |
| Leuthan Lane | 3 | 13,170 |
| Lookout Lane | 0.3 | 3,000 |
| Loop 360 | 0.439 | 3,200 |
| Mt. Larson | 0.1 | 100 |
| Never Bend Cove | 0.06 | 1,600 |
| Pilot Knob (1) | 10 | n/a |
| Slaughter Lane | 6 | 15,000 |
| Thomas Springs (1) | 1.25 | n/a |
| Westlake Drive | 0.010 | 500 |

(1) Storage only, no pumps.

Source: City's Water and Wastewater Utility.

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Historical Water Pumpage - TABLE EIGHT

The following table summarizes historical demand and maximum day water pumpage from fiscal years 1988 through 2002.

| <u>Fiscal Year</u> | <u>Total Pumpage (Millions of Gallons)</u> | <u>Percent Change</u> | <u>Maximum Day Pumpage (Million of Gallons)</u> |
|--------------------|--|-----------------------|---|
| 1988 | 36,332 | 6.800 | 162 |
| 1989 | 38,300 | 5.400 | 178 |
| 1990 | 38,311 | .029 | 177 |
| 1991 | 36,125 | (5.700) | 161 |
| 1992 | 36,989 | 2.400 | 169 |
| 1993 | 39,824 | 7.700 | 189 |
| 1994 | 39,766 | (0.100) | 199 |
| 1995 | 39,542 | (0.700) | 192 |
| 1996 | 45,835 | 15.900 | 205 |
| 1997 | 42,812 | (6.600) | 195 |
| 1998 | 46,438 | 8.500 | 211 |
| 1999 | 46,422 | (0.030) | 216 |
| 2000 | 52,194 | 12.400 | 227 |
| 2001 | 50,140 | (3.940) | 243 |
| 2002 | 50,883 | 1.500 | 214 |

Source: City's Water and Wastewater Utility.

Projected Water Pumpage - TABLE NINE

The following table, based on actual operating experience, summarizes the peak day and total annual water pumpage requirements projected by the City.

| <u>Fiscal Year</u> | <u>Total Pumpage (Million of Gallons)</u> | <u>Maximum Day Pumpage (Million of Gallons)</u> |
|--------------------|---|---|
| 2003 | 49,471 | 241 |
| 2004 | 49,733 | 247 |
| 2005 | 50,528 | 253 |
| 2006 | 51,375 | 259 |
| 2007 | 52,239 | 265 |
| 2008 | 53,159 | 271 |
| 2009 | 54,427 | 277 |
| 2010 | 55,509 | 281 |
| 2011 | 57,737 | 285 |
| 2012 | 58,834 | 289 |

Source: City's Water and Wastewater Utility.

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Information Concerning Water Sales - TABLE TEN

| | Fiscal Year Ended September 30 | | | | | | | | | | | |
|--|--------------------------------|-------------------|----------|-----------|-------------------|----------|-----------|-------------------|----------|-----------|-------------------|----------|
| | 2002 | | | 2001 | | | 2000 | | | 1999 | | |
| | Average | Thousand | Thousand | Average | Thousand | Thousand | Average | Thousand | Thousand | Average | Thousand | Thousand |
| | Customers | Gallons | Gallons | Customers | Gallons | Gallons | Customers | Gallons | Gallons | Customers | Gallons | Gallons |
| Thousand Gallons Pumped | | | | | | | | | | | | |
| Less: Sales to Other Water Utilities (1) | | 50,883,130 | | | 50,184,839 | | | 52,326,065 | | | 46,679,391 | |
| Thousand Gallons to System | | <u>3,476,482</u> | | | <u>3,639,468</u> | | | <u>3,863,466</u> | | | <u>3,146,201</u> | |
| | | <u>47,406,648</u> | | | <u>46,824,307</u> | | | <u>48,462,599</u> | | | <u>43,825,592</u> | |
| Water Sales: | | | | | | | | | | | | |
| Urban | 168,292 | 36,577,034 | | | 37,653,186 | | | 41,973,466 | | | 35,594,247 | |
| Rural | <u>12,909</u> | <u>2,338,385</u> | | | <u>2,219,216</u> | | | <u>2,435,328</u> | | | <u>1,852,000</u> | |
| | 181,201 | 38,915,619 | | | 39,872,402 | | | 44,408,794 | | | 37,446,247 | |
| City Departments | | <u>616,715</u> | | | <u>588,880</u> | | | <u>650,006</u> | | | <u>619,553</u> | |
| Total Sales to Ultimate Consumer | <u>392</u> | <u>39,532,394</u> | | | <u>40,461,282</u> | | | <u>45,058,800</u> | | | <u>38,065,800</u> | |
| Used by Water Utility | <u>181,593</u> | <u>1,529,717</u> | | | <u>1,531,430</u> | | | <u>1,613,380</u> | | | <u>1,422,526</u> | |
| Other Unmetered Usage | | 3,448,000 | | | | | | | | | | |
| Loss and Unaccounted For | | 2,896,537 | | | 4,552,659 | | | 1,790,419 | | | 4,044,864 | |
| Thousand Gallons to System | | <u>47,406,648</u> | | | <u>46,824,307</u> | | | <u>48,462,599</u> | | | <u>43,825,592</u> | |
| Maximum Daily Consumption | | 206,125 | | | 240,285 | | | 220,305 | | | 204,746 | |
| Average Daily Consumption in | | | | | | | | | | | | |
| Thousands of Gallons | | 122,024 | | | 125,020 | | | 132,774 | | | 119,269 | |
| (1) Includes sales to all wholesale customers. | | | | | | | | | | | | |

[The remainder of this page is intentionally left blank.]

Large Water Customers - TABLE ELEVEN

Water and Wastewater Utility
Large Water Customers
Five Year Comparative Data (1998 - 2002)

| | Fiscal Year Ended September 30 (Gallons and Dollars in Thousands) (2) | | | | | | | | | | | |
|---|--|-----------------|--|------------------|-----------------|--|------------------|-----------------|--|------------------|-----------------|--|
| | 2002 | | | 2001 | | | 2000 | | | 1999 | | |
| | Gallons | Revenue | | Gallons | Revenue | | Gallons | Revenue | | Gallons | Revenue | |
| Motorola, Inc. (1) | 1,277,560 | \$ 3,202 | | 1,931,463 | \$ 4,886 | | 1,814,060 | \$ 4,031 | | 1,781,016 | \$ 3,855 | |
| Advanced Micro Devices | 911,042 | 2,319 | | 1,135,801 | 4,094 | | 1,044,510 | 2,082 | | 1,186,752 | 2,570 | |
| University of Texas | 863,720 | 2,319 | | 979,919 | 2,340 | | 1,029,359 | 2,341 | | 908,424 | 2,056 | |
| Travis County Water Control and Improvement District No. 10 | 773,882 | 1,604 | | 848,672 | 1,666 | | 901,248 | 1,831 | | 699,180 | 1,416 | |
| Wells Branch Municipal Utility District | 575,113 | 1,092 | | 587,057 | 1,076 | | 646,054 | 1,328 | | 544,046 | 1,107 | |
| Anderson Mill Municipal Utility District | 477,297 | 757 | | 492,533 | 1,153 | | 546,213 | 936 | | 510,713 | 872 | |
| Sansung | 495,548 | 1,246 | | 486,185 | 851 | | 462,139 | 1,005 | | 353,927 | 768 | |
| North Austin Municipal Utility District | 367,626 | 910 | | 364,580 | 712 | | 406,345 | 850 | | 297,789 | 622 | |
| Lost Creek Municipal Utility District | 293,571 | 612 | | 303,592 | 608 | | 355,547 | 758 | | 282,637 | 600 | |
| Shady Hollow MUD | 224,608 | 523 | | 247,103 | 496 | | 300,277 | 800 | | 217,346 | 576 | |
| | <u>6,259,967</u> | <u>\$14,556</u> | | <u>7,376,905</u> | <u>\$17,882</u> | | <u>7,505,752</u> | <u>\$15,962</u> | | <u>6,781,830</u> | <u>\$14,442</u> | |
| | | | | | | | | | | <u>7,092,486</u> | <u>\$14,510</u> | |

(1) Totals for Motorola, Inc. include their east Austin plant site and their west Austin plant sites.

(2) These columns may not add to the totals provided due to rounding.

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WASTEWATER SYSTEM

Service Area

The Water and Wastewater Utility provides wastewater service to customers within the corporate limits of the City and a portion of Travis and Williamson Counties. The City has entered into wholesale service contracts with ten municipal utility districts, one private utility, the Eanes Independent School District, and the cities of Sunset Valley and Rollingwood to provide wastewater service.

Facilities

The Water and Wastewater Utility has three main wastewater treatment plants with a permitted capacity of 130 mgd, one sludge treatment and disposal facility, over 2,635 miles of sanitary wastewater mains and lines, and 114 lift stations. The three treatment plants are the Walnut Creek Wastewater Treatment Plant which began operations in 1977, the Govalle Wastewater Treatment Plant constructed in 1936, and the South Austin Regional Wastewater Treatment Plant completed in 1986. The Hornsby Bend Treatment Plant operates as a sludge treatment and disposal facility and was placed in operation in 1956. In 2001 and 2002, the City received from the TCEQ and the U.S. Environmental Protection Agency renewals of discharge permits (TPDES permits) for all its wastewater treatment plants. The permits are renewable again in 2004.

The Walnut Creek Wastewater Treatment Plant is currently permitted to discharge an average flow of 60 mgd. During 2002 average flow was 49 mgd. Sludge from this plant is pumped to the anaerobic digesters at Hornsby Bend for stabilization and disposal. A 15 mgd upgrade to this plant is currently in the engineering design phase with construction scheduled to be completed in approximately 2004.

The Govalle Wastewater Treatment Plant was initially constructed in 1937 and has undergone several expansions. It now has a permitted capacity of 20 mgd. During 2002 average flow was 10 mgd. Sludge from this plant is also pumped to the anaerobic digesters at Hornsby Bend. Extensive modernization completed in 1986 and subsequent improvements completed in 1988 have enabled the Govalle plant to reliably produce the quality of effluent required by state and federal permits. A major interceptor tunnel completed in 1988 diverts any excess flows from Govalle to the South Austin Wastewater Treatment Regional Plant.

The South Austin Regional Wastewater Treatment Plant, which replaced the Williamson Creek Treatment Plant, began operation in April 1986. The plant is now permitted to discharge at a rate of 50 mgd. During 2002 average flow was 32 mgd. A major interceptor transports the wastewater to the South Austin plant from the site of the former Williamson Creek plant. Waste sludge is pumped to the Hornsby Bend facility to anaerobic digesters which were constructed simultaneously with the plant. A 25 mgd upgrade to this plant is currently in the engineering design phase with construction scheduled to be completed in approximately 2005.

The Hornsby Bend Treatment Plant serves as the City's central sludge treatment and disposal facility. Waste sludge from the Walnut Creek, South Austin Regional and Govalle plants is pumped to anaerobic digesters at Hornsby Bend. A greenhouse enclosed aquaculture pond is used to treat the pond water prior to its use for irrigation on utility owned land at the site. Major improvements recently completed at Hornsby Bend include sludge thickening facilities. Sludge received at Hornsby Bend is thickened, anaerobically digested, dewatered in sludge drying basins and composted for marketing and distribution. Some dried sludge is applied to on-site agricultural land. A Center for Environmental Research has been established with the cooperation of the City, the University of Texas and Texas A&M University. The City provides laboratory, offices and research facilities at Hornsby Bend for the two universities to conduct environmental research.

In 1985, the City entered into a contract with the Brushy Creek Water Control and Improvement District No. 1, Williamson County MUD No. 2, Williamson County MUD No. 3 and the City of Round Rock to fund, construct, and operate a regional wastewater collection and treatment system (the "Project") serving the upper Brushy Creek watershed. In 1994, the Project participants terminated the agreement. The City and the City of Round Rock entered an interlocal agreement where the two cities assumed the obligations and divided the Project assets and entered an interim operations and maintenance agreement. LCRA and Brazos River Authority ("BRA") have purchased Round Rock's share in the Project and have also purchased a portion of Austin's share relating to the area now included in the City of Cedar Park's extraterritorial jurisdiction. The City of Cedar Park entered into a wastewater service agreement with LCRA and BRA in 1997. Final negotiations were completed, selling Austin's remaining assets to the LCRA, effective October 1, 2000, with Austin becoming a customer of the LCRA and BRA wastewater system. The agreement, which requires Austin to pay for its portion of capital expansions and operations and maintenance costs on an annual basis, reserves enough wastewater capacity to adequately serve all of the portions of Austin's city limits or extraterritorial jurisdiction within the Brushy Creek watershed. Stormwater is collected in an entirely separate gravity feed storm wastewater system and is segregated from the sanitary wastewater system. The storm wastewater system is operated and maintained by the City's Department of Public Works and Transportation.

Lift Stations

In addition to the wastewater treatment plants, the Water and Wastewater Utility owns and operates the following major lift stations.

| <u>Name</u> | <u>Firm Capacity (Gallons per Minute)</u> |
|------------------|---|
| Montopolis (1) | 22,000 |
| Boggy Creek East | 16,400 |
| Shoal Creek | 9,000 |
| Tracor | 5,580 |
| Canterbury (1) | 3,475 |
| Taylor Slough | 3,400 |
| Barton Creek | 5,800 |
| Lake Creek | 4,200 |
| Davis Springs | 3,600 |
| Springfield | 2,400 |

(1) These lift stations control flow to the Govalle and South Austin Regional Wastewater Treatment Plants.

Historical Wastewater Flows - TABLE TWELVE

The following table summarizes the historical wastewater flows to the City's wastewater treatment facilities from fiscal years 1993 through fiscal year 2002.

| <u>Fiscal Year</u> | <u>Total Wastewater Flow (Millions of Gallons)</u> | <u>Percent Change</u> |
|--------------------|--|-----------------------|
| 1993 | 26,797 | (11.1) |
| 1994 | 25,257 | (5.7) |
| 1995 | 30,038 | 18.9 |
| 1996 | 28,140 | (6.3) |
| 1997 | 32,898 | 16.9 |
| 1998 | 31,609 | (3.9) |
| 1999 | 34,298 | 8.5 |
| 2000 | 30,684 | (10.5) |
| 2001 | 34,289 | 11.7 |
| 2002 | 33,361 | (2.7) |

Projected Wastewater Flows - TABLE THIRTEEN

The following table summarizes the wastewater flows projected to be received at the City's wastewater treatment plants.

| <u>Fiscal Year</u> | <u>Total Wastewater Flow (Millions of Gallons)</u> |
|--------------------|--|
| 2003 | 33,705 |
| 2004 | 34,213 |
| 2005 | 34,874 |
| 2006 | 35,580 |
| 2007 | 36,295 |
| 2008 | 37,040 |
| 2009 | 38,082 |
| 2010 | 38,806 |
| 2011 | 39,543 |
| 2012 | 40,294 |

Source: City's Water and Wastewater Utility. Such projections are based on actual operating experience.

To meet these projections, the capacity of the Walnut Creek Wastewater Treatment Plant is expected to be increased from 60 mgd to 75 mgd by the year 2004 and the South Austin Regional Wastewater Treatment Plant is expected to be expanded to a capacity of 75 mgd by the year 2005.

COMBINED WATER AND WASTEWATER SYSTEM INFORMATION

Future Capital Improvements for Water and Wastewater System

During the next five years, it is anticipated that the Water and Wastewater System will require approximately \$701.2 million for system improvements. Such improvements will include treatment facilities, reservoir, pump station and lift station improvements, and major transmission distribution and collection improvements. It is anticipated that such improvements will be financed as follows: (1) the issuance of \$549.0 million additional Parity Water/Wastewater Obligations and (2) the application of \$152.2 million of anticipated transfers from current revenues and amounts on hand.

Services Financed by Utility Districts

On August 19, 1981, the City Council enacted an ordinance establishing the basic requirements for the City's consent to the creation of a Municipal Utility District ("MUD"), a Water Control and Improvement District ("WCID"), a Fresh Water Supply District or any other water district created under State law for the purpose of supplying water and/or wastewater service to land within the extra-territorial jurisdiction or the City limits of the City. That ordinance has been modified by the City's enactment of its Land Development Code, which contains provisions relating to the City's consent to MUDs and WCIDs.

MUDs and WCIDs supply water and wastewater service to areas within and outside the City limits and function as a financing mechanism for development of land.

Under the current process, the City consents to the formation of a district by approval of a consent ordinance, a consent agreement, and a utility construction contract, if necessary. These contracts between the City, the petitioners seeking formation of the district and the district itself establish a detailed set of requirements and policy statements governing the construction within, operation of and issuance of bonds by such district.

The City has previously entered into contractual commitments with fourteen municipal utility districts for the construction of improvements to and extensions of the City's Water and Wastewater System. The commitments for the financing of such improvements and extensions exist in the form in which the district issues bonds and constructs the improvements. The City generally becomes the owner of such improvements upon completion of construction. The City makes payments equal to its pro rata share of total debt service on the bonds from the City's user fees charged to customers using such improvements, surplus Net Revenues from the Water and Wastewater System and, if necessary, City ad valorem taxes. The district pays its pro-rata share of the debt service due on bonds directly to the City.

Some of the contractual commitments of the City with the most recently approved districts vary from the process described above in that the issuance by the district of bonds for such improvements and extensions creates a lien on and pledge of the Net Revenues of the Water and Wastewater System to cover the City's payments on the total debt service. The lien is known as a Separate Lien Obligation and is on a parity, with respect to the lien on and pledge of the Net Revenues of the Water and Wastewater System, with the Subordinate Lien Bonds already issued by the City or to be issued in the future. No pledge of the City's ad valorem taxes is made. The City will own, operate and maintain the facilities after completion of the project. In addition, the City may request that some of the districts finance improvements to the City's water and/or wastewater treatment facilities.

Under the creation agreements with the districts, the districts may be annexed separately and dissolved by the City. Upon annexation and dissolution of the districts, the City would assume the district's outstanding debts and other obligations, which pursuant to State law would become payable from ad valorem taxes levied and collected within the City or, in some cases, from a surcharge fee assessed by the City to utility users within the boundaries of the annexed district. Upon annexation, the City is empowered to issue any authorized but unissued bonds of the district and to use the proceeds for improvements within the annexed district. Alternatively, some of the districts may be annexed but not dissolved at the option of the City. If so, the City would be required only to provide services other than water and wastewater services and not to assume the district's outstanding debt. In December 1997, the City annexed ten MUD's and thereby assumed their outstanding utility system debt.

The City previously consented to the creation of twelve MUDs inside the City's corporate limits, of which ten have been dissolved. Three of the twelve MUDs had their annexation status changed from full purpose to limited dissolved. Moore's Crossing MUD also had its annexation status changed from full purpose to limited purpose and Northwest Austin MUD 1 is annexed for full purposes. The creation of the inside City districts were approved by the TCEQ. They receive retail water and wastewater services as well as other services from the City and will issue bonds and levy an ad valorem tax to finance internal water, wastewater and drainage facilities. Under existing law, the City will not have to assume any of the debt issued for these City districts, so long as they are not dissolved.

Water and Wastewater Rates

The City is not subject to regulation by the TCEQ with regard to the rates charged for water and wastewater services to customers within the boundaries of the City. The TCEQ has appellate jurisdiction to determine municipal water and wastewater rates outside the City's boundaries.

Texas law allows water districts to appeal the City's water and wastewater rates to the TCEQ.

The following schedules present the monthly retail and wholesale customer water and wastewater rates.

Water Service Rates Effective November 1, 2001 TABLE FOURTEEN

Monthly Customer Charges

| <u>Customer Account Charge</u> | <u>Equivalent Meter Charge</u> | | | |
|--|--|--|--|--|
| | <u>Customer Account Charge per Month</u> | <u>Meter Size</u> | <u>Retail Meter Charge per Month</u> | <u>Wholesale Meter Charge per Month</u> |
| Retail Customer Account Charge (\$/Month) | \$1.53 | 5/8 3/4 | \$ 1.79 2.32 | \$ 1.79 2.32 |
| Wholesale Customer Account Charge (\$/Month) | \$1.53 | 1 1 1/4 1 1/2 2 3 4 6 8 10 12 | 3.07 4.14 5.20 7.34 16.72 27.39 54.06 80.74 107.41 123.41 | 3.07 4.14 5.20 7.34 16.72 27.39 54.06 80.74 107.41 123.41 |

Volume Unit Charge (1)

| <u>Unit Cost per 1,000 Gallons</u> | <u>Inside City</u> | <u>Outside City</u> |
|--------------------------------------|--------------------|---------------------|
| <u>Single-Family Residential (2)</u> | | |
| 0 - 2,000 Gallons | \$0.70 | \$0.70 |
| 2,001 - 9,000 Gallons | 2.00 | 2.00 |
| 9,001 - 15,000 Gallons | 3.50 | 3.50 |
| 15,001 - Over Gallons | 6.12 | 6.02 |
| <u>Multifamily (3)</u> | | |
| Off Peak | \$2.27 | \$2.13 |
| Peak | 2.47 | 2.34 |
| <u>Commercial (3)</u> | | |
| Off Peak | \$2.79 | \$2.52 |
| Peak | 3.00 | 2.77 |
| <u>Large Volume/Industrial (3)</u> | | |
| Off Peak | \$2.44 | |
| Peak | 2.67 | |
| <u>Golf Courses (3)</u> | | |
| Off Peak | \$2.79 | \$2.52 |
| Peak | 3.00 | 2.77 |

(1) Wholesale unit charges vary between \$1.72 and \$2.43 for each 1,000 gallons.

(2) The City of Austin has approved an inclining block rate structure to promote water conservation for the Single Family Residential customers. These rates will be administered on the basis of 100 gallon increments.

(3) Off Peak (November 1 - June 30 Bills). Peak (July 1 - October 31 Bills).

Wastewater Service Rates Effective November 1, 2001 – TABLE FIFTEEN

Customer Account Charge

| Customer Account Charge (\$/month) | <u>Inside City</u> | <u>Outside City</u> | <u>Wholesale Customers</u> |
|------------------------------------|--------------------|---------------------|----------------------------|
| | \$2.60 | \$2.60 | \$2.60 |

Volumes Unit Charge

| | <u>Unit Cost per 1,000 Gallons (1)</u> | |
|-------------------------|--|---------------------|
| | <u>Inside City</u> | <u>Outside City</u> |
| Retail Inside City: | | |
| Single-Family | | |
| 0 - 2,000 Gallons | \$2.10 | \$3.00 |
| 2,001 - Over Gallons | 4.76 | 5.40 |
| Multifamily | 3.73 | 3.73 |
| Commercial | 4.09 | 4.09 |
| Large Volume/Industrial | 3.59 | N/A |
| Golf Courses | 4.09 | 4.09 |

Wholesale unit charges vary between \$2.61 and \$3.34 for each 1,000 gallons.

(1) Applied to average water consumption during December, January and February billing periods, or actual water consumption, whichever is lower.

Water and Wastewater Capital Recovery Fees

On September 3, 1982, the City Council adopted an ordinance, under which all new non-industrial and non-commercial customers of the Water and Wastewater System must pay a Capital Recovery Fee at the time that the customer's new tap is purchased. The fee has been revised a number of times since that date and is currently applied to all connections added to the Water and Wastewater System unless expressly waived by the City Council. In 1989, the City Council appointed an Impact Fee Advisory Committee and reauthorized the Capital Recovery Fee in compliance with procedures and methodology established by State law. The total Water and Wastewater Capital Recovery Fee was implemented August 5, 1999 as shown below. There are a number of express exemptions from payment of these fees. The City's current policy is to restrict the use of Capital Recovery Fee receipts to finance growth related capital improvement projects, thus reducing the amount required to be debt financed and saving the Water and Wastewater Utility the related financing costs. The fees listed below are based on one service unit (5/8" meter).

| | <u>Water</u> | <u>Wastewater</u> | <u>Total</u> |
|--|--------------|-------------------|--------------|
| Drinking Water Protection Zone in the City's extraterritorial jurisdiction | \$1,700 | \$1,300 | \$3,000 |
| Drinking Water Protection Zone in the City limits | 1,500 | 1,200 | 2,700 |
| Desired Development Zone in the City's extraterritorial jurisdiction | 1,300 | 800 | 2,100 |
| Desired Development Zone in the City limits | 700 | 400 | 1,100 |
| Urban watersheds | 600 | 400 | 1,000 |
| Central urban redevelopment combining district area and the area bounded by Town Lake, Lamar Boulevard, 15 th Street, and IH-35 | 500 | 300 | 800 |
| Outside of Austin extraterritorial jurisdiction | 1,700 | 1,300 | 3,000 |

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Analysis of Water Bills - TABLE NINE A

| | Fiscal Year Ended September 30 | | | | |
|---|--------------------------------|-----------|-----------|-----------|-----------|
| | 2002 | 2001 | 2000 | 1999 | 1998 |
| <u>Average Monthly Bill Per Customer - Water</u> | | | | | |
| Inside City (Urban) | | | | | |
| Residential | \$ 24.43 | \$ 24.64 | \$ 30.13 | \$ 23.50 | \$ 24.38 |
| Multi-Family | 316.09 | 306.69 | 338.37 | 306.97 | 287.39 |
| Commercial | 207.39 | 186.12 | 199.83 | 166.96 | 167.04 |
| Industrial | 103,166.21 | 86,254.81 | 95,352.85 | 90,525.34 | 90,635.15 |
| City Departments | 431.17 | 342.98 | 321.34 | 315.39 | 273.08 |
| Outside City (Rural) | | | | | |
| Residential | 30.22 | 33.47 | 42.02 | 33.95 | 37.50 |
| Multi-Family | 229.36 | 194.34 | 193.96 | 168.54 | 181.26 |
| Commercial | 204.28 | 187.77 | 178.16 | 127.26 | 136.67 |
| Average Monthly Bill | | | | | |
| Above Customers | 51.56 | 50.53 | 57.71 | 48.23 | 49.24 |
| Sales to Other Water Utilities* | 31,499.61 | 29,057.09 | 38,611.80 | 31,045.89 | 30,633.76 |
| Average Monthly Bill | | | | | |
| All Customers | \$ 54.86 | \$ 53.80 | \$ 61.50 | \$ 51.32 | \$ 52.99 |
| <u>Average Monthly Use in 1000 Gallons - Water</u> | | | | | |
| Inside City (Urban) | | | | | |
| Residential | 8.38 | 8.73 | 10.13 | 8.25 | 8.84 |
| Multi-Family | 132.28 | 132.98 | 138.10 | 125.51 | 123.52 |
| Commercial | 71.52 | 67.99 | 81.34 | 67.58 | 71.32 |
| Industrial | 41,127.10 | 36,881.81 | 43,836.58 | 41,787.88 | 43,884.04 |
| City Departments | 135.77 | 137.21 | 154.26 | 147.32 | 130.30 |
| Outside City (Rural) | | | | | |
| Residential | 9.59 | 9.96 | 11.98 | 9.87 | 11.11 |
| Multi-Family | 101.43 | 85.62 | 82.78 | 71.81 | 77.44 |
| Commercial | 78.82 | 71.80 | 76.62 | 54.05 | 58.24 |
| Average Monthly Use | | | | | |
| Above Customers | 18.58 | 19.01 | 21.76 | 18.62 | 19.79 |
| Sales to Other Water Utilities* | 15,576.82 | 15,164.45 | 18,938.56 | 15,422.55 | 15,821.91 |
| Average Monthly Use | | | | | |
| All Customers | 20.21 | 20.71 | 23.62 | 20.15 | 21.73 |
| <u>Average Revenue Per 1000 Gallons - Water</u> | | | | | |
| Inside City (Urban) | | | | | |
| Residential | \$2.92 | \$2.82 | \$2.97 | \$2.85 | \$2.76 |
| Multi-Family | 2.39 | 2.31 | 2.45 | 2.45 | 2.33 |
| Commercial | 2.90 | 2.74 | 2.46 | 2.47 | 2.34 |
| Industrial | 2.51 | 2.34 | 2.18 | 2.17 | 2.07 |
| City Departments | 3.18 | 2.50 | 2.08 | 2.14 | 2.10 |
| Outside City (Rural) | | | | | |
| Residential | 3.15 | 3.36 | 3.51 | 3.44 | 3.37 |
| Multi-Family | 2.26 | 2.27 | 2.34 | 2.35 | 2.34 |
| Commercial | 2.59 | 2.62 | 2.33 | 2.35 | 2.35 |
| Average Revenue | | | | | |
| Above Customers | 2.78 | 2.66 | 2.65 | 2.59 | 2.49 |
| Sales to Other Water Utilities* | 2.02 | 1.92 | 2.04 | 2.01 | 1.94 |
| Average Revenue | | | | | |
| All Customers | 2.71 | 2.60 | 2.60 | 2.55 | 2.44 |

* Includes all wholesale customers.

Analysis of Wastewater Bills - TABLE NINE B

| <u>Average Monthly Bill Per Customer - Wastewater</u> | <u>2002</u> | <u>2001</u> | <u>2000</u> | <u>1999</u> | <u>1998</u> |
|---|-------------|-------------|-------------|-------------|-------------|
| Inside City (Urban) | | | | | |
| Residential | \$ 20.26 | \$ 19.87 | \$ 23.13 | \$ 19.82 | \$ 18.21 |
| Multi-Family | 408.21 | 385.39 | 477.69 | 413.23 | 379.55 |
| Commercial | 191.68 | 197.82 | 255.88 | 191.99 | 176.54 |
| Industrial | 128,387.33 | 110,619.51 | 127,044.30 | 118,340.25 | 119,765.31 |
| City Departments | 194.64 | 203.92 | 176.25 | 169.76 | 217.44 |
| Outside City (Rural) | | | | | |
| Residential | 25.29 | 23.51 | 28.91 | 23.50 | 21.62 |
| Multi-Family | 373.49 | 322.64 | 373.97 | 295.60 | 305.84 |
| Commercial | 584.21 | 561.31 | 668.53 | 634.63 | 490.90 |
| Average Monthly Bill | | | | | |
| Above Customers | 48.46 | 48.98 | 58.34 | 50.14 | 47.80 |
| Sales to Other Utilities* | 27,609.36 | 29,393.59 | 28,359.53 | 23,816.54 | 21,793.24 |
| Average Monthly Bill | | | | | |
| All Customers | \$ 49.95 | \$ 50.42 | \$ 60.15 | \$ 51.66 | \$ 49.43 |
| <u>Average Monthly Use in 1000 Gallons - Wastewater</u> | | | | | |
| Inside City (Urban) | | | | | |
| Residential | 4.78 | 4.89 | 6.08 | 5.24 | 5.10 |
| Multi-Family | 108.65 | 105.94 | 122.67 | 106.47 | 102.36 |
| Commercial | 46.49 | 49.83 | 56.71 | 47.68 | 45.90 |
| Industrial | 37,470.02 | 32,622.39 | 38,611.97 | 36,108.57 | 38,260.31 |
| City Departments | 54.56 | 56.14 | 52.01 | 50.10 | 65.96 |
| Outside City (Rural) | | | | | |
| Residential | 5.06 | 5.04 | 6.46 | 5.26 | 5.18 |
| Multi-Family | 101.05 | 88.53 | 95.76 | 75.88 | 82.27 |
| Commercial | 132.12 | 142.72 | 168.11 | 160.33 | 129.87 |
| Average Monthly Use | | | | | |
| Above Customers | 12.16 | 12.76 | 14.66 | 13.25 | 13.31 |
| Sales to Other Wastewater Utilities* | 9,288.69 | 11,207.18 | 10,550.50 | 8,919.36 | 8,780.43 |
| Average Monthly Use | | | | | |
| All Customers | 12.66 | 13.32 | 15.33 | 13.81 | 13.97 |
| <u>Average Revenue Per 1000 Gallons - Wastewater</u> | | | | | |
| Inside City (Urban) | | | | | |
| Residential | \$4.24 | \$4.06 | \$3.80 | \$3.79 | \$3.57 |
| Multi-Family | 3.76 | 3.64 | 3.89 | 3.88 | 3.71 |
| Commercial | 4.12 | 3.94 | 4.95 | 4.03 | 3.85 |
| Industrial | 3.43 | 3.39 | 3.29 | 3.28 | 3.13 |
| City Departments | 3.57 | 3.63 | 3.39 | 3.39 | 3.30 |
| Outside City (Rural) | | | | | |
| Residential | 5.00 | 4.66 | 4.48 | 4.47 | 4.17 |
| Multi-Family | 3.70 | 3.64 | 3.91 | 3.90 | 3.72 |
| Commercial | 4.42 | 3.93 | 3.98 | 3.96 | 3.78 |
| Average Revenue | | | | | |
| Above Customers | 3.98 | 3.84 | 3.98 | 3.79 | 3.59 |
| Sales to Other Utilities* | 2.87 | 2.62 | 2.69 | 2.67 | 2.48 |
| Average Revenue | | | | | |
| All Customers | 3.94 | 3.79 | 3.92 | 3.74 | 3.54 |

* Includes all wholesale customers.

**THE ELECTRIC UTILITY SYSTEM
"AUSTIN ENERGY"**

Management

| <u>Name</u> | <u>Title</u> | <u>Length of Service with City</u> |
|--------------------------|--|------------------------------------|
| Juan Garza | General Manager | 2 Years, 2 Months |
| Al Lujan | Senior Vice President Regulated Operations | 2 Years, 8 Months |
| Andy Ramirez, P.E. | Senior Vice President Power Production | 6 Years, 3 Months |
| Bob Kahn | Vice President Legal Services | 10 Years, 8 Months |
| Elaine Hart Kuhlman, CPA | Senior Vice President Finance and Corporate Services | 14 Years, 5 Months* |
| Roger Duncan | Vice President Governmental Relations, Energy and Environmental Policy | 12 Years, 9 Months |
| Michael McCluskey | Senior Vice President Wholesale and Retail Markets | 16 Years, 6 Months |
| Harvey Winkelmann, CPA | Vice President Finance | 18 Years, 4 Months |

* Length of service not continuous.

Competitive Positioning

With increasing competition in the electric utility industry due to regulatory and market changes, the City continues its initiatives at both the policy level and departmental level to strengthen its electric utility's competitive position. In December 1996, the City Council approved financial targets for Austin Energy to achieve over the next six years. In September 1999, these targets were updated and extended through 2003 and are outlined below.

- Complete an annual competitive pricing rate analysis to evaluate its rate structure for all customer classes, using the Electric Reliability Council of Texas ("ERCOT") average retail price as a standard.
- Complete an annual review of operations and competitive position.
- Direct all excess electric utility cash to a debt management fund to achieve a debt-to-capital ratio of 62% by the year 2003 and allow use of the fund to improve the competitive position of the electric utility.
- Continue to reduce operating expenses per kWh.
- Decrease the transfer to the General Fund as necessary to achieve competitive pricing establishing a range between 6.6% and 9.1% of total revenue.
- Adjust conservation spending for the electric utility as necessary to achieve competitive pricing using the ERCOT average retail price as a standard and cost effective conservation programs are targeted as the first priority in meeting new load growth requirements.
- Establish a renewable energy goal of five percent of the energy mix coming from renewable sources by December 31, 2004.

Austin Energy's competitive position has been improved through reduced costs and improved customer service through the initial joint work of a management consulting firm and electric utility management, which was completed in 1998, as well as the ongoing efforts of electric utility management. The electric utility is meeting these long-range financial targets. The electric utility adopted a "Doing Business As" (DBA) during 1998 in order to establish a positive, consumer-focused brand and name recognition. Its trademark name is "Austin Energy®".

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Generation – TABLE ONE

The present generating facilities, or interest of Austin Energy therein, are as follows.

| <u>Unit</u> | <u>Year Installed</u> | <u>Nameplate Rating (MW)</u> | <u>Fuel</u> |
|---|---------------------------|----------------------------------|-----------------------------|
| Fayette Power Project | | | |
| Unit No. 1 | 1979 | 285.0 | Coal |
| Unit No. 2 | 1980 | 285.0 | Coal |
| Holly Street Power Plant | | | |
| Unit No. 1 | 1960 | 100.0 | Gas/No. 2 oil backup |
| Unit No. 2 | 1964 | 100.0 | Gas/No. 2 oil backup |
| Unit No. 3 | 1966 | 165.0 | Gas/No. 2 oil backup |
| Unit No. 4 | 1974 | 193.0 | Gas/No. 2 oil backup |
| Photovoltaic Plant (PV300) | 1986 | 0.3 | Solar |
| Decker Power Station | | | |
| Unit No. 1 | 1970 | 325.0 | Gas/No. 2 oil backup |
| Unit No. 2 | 1977 | 405.0 | Gas or Nos. 1 through 5 oil |
| Gas Turbines | 1988 | 200.0 | Gas/No. 1 oil backup |
| Sand Hill Energy Center | 2001 | 80.0 | Gas |
| South Texas Project Electric Generating Station | | | |
| Unit No. 1 | 1988 | 200.0 | Nuclear |
| Unit No. 2 | 1989 | <u>200.0</u> | Nuclear |
| Total Capacity | | 2,538.3 | |

See Table Six "Generation and Use Data – System Peak Demand" for further description of peak demand to generation capacity. Generation capacity is adequate to meet native load.

Conventional System Improvements

In September 2002, the 2003-2007 Capital Improvements Spending Plan was approved by the City Council in the amount of \$734,985,000. Austin Energy's five-year spending plan provides continued funding for distribution and street lighting additions including line extensions for new service, system modifications for increased load, and relocations or replacements of distribution facilities in the central business district and along major thoroughfares. It also includes funding for transmission, generation and other general additions. Funding for the total Capital Plan is provided from current revenues and commercial paper.

In 2001 Austin Energy rebuilt the existing Austrop to Fayette 345 kV single circuit line to add a second 345 kV circuit. This rebuild along with the addition of the new Lost Pines 345 kV Switchyard (located near Bastrop, Texas) was undertaken to accommodate the new Lost Pines Power Park I Generation Plant and to relieve existing transmission congestion between the Fayette Power Plant and Austin. Lost Pines Power Park is jointly owned by Lower Colorado River Authority ("LCRA") and Calpine Corporation, an independent power producer. ERCOT requires that the transmission provider in that service area provide the necessary interconnection. Austin Energy was designated by ERCOT as the transmission provider since they already own the existing 345 kV transmission line in the area. The Lost Pines 345 kV switchyard and all the 345 kV transmission lines were completed between January 2001 and July 2001. Austin Energy is also continuing a vigorous construction program of non-345 kV related transmission and substation projects to accommodate Austin's growth. The City is currently proceeding with construction of a 300 MW combined cycle gas-fired electric generating facility at the Sand Hill Energy Center. The estimated cost of the facility is \$145 million and will be paid with cash on hand. It is expected to begin commercial operation in fall 2003. The capital budget for 2003 is \$38.7 million for transmission and substations that are recoverable through Transmission Cost of Service ("TCOS").

In 1995, the Public Utility Commission of Texas ("PUCT") adopted new rules governing the transmission system in ERCOT, which, at the time, was an organization made up of major investor-owned and municipal systems, a state river authority, a municipal joint agency, energy marketers, independent power producers and a number of cooperatives. As part of these new rules, the PUCT established a means for the transmission owners in ERCOT to recover TCOS. TCOS is based on the principle of equal transmission access for all loads and generation in ERCOT. Each load serving entity in ERCOT has been assigned a share of the total cost of transmission in ERCOT based upon the ratio of that load serving entity's load to the entire load in ERCOT. The funds recovered through this mechanism are distributed to transmission owners in ERCOT based upon a ratio of the transmission owner's investment in transmission facilities to the entire transmission investment in ERCOT. Austin Energy's load represents approximately 4.0% of ERCOT and Austin Energy's transmission cost of service is approximately 4.1 % of ERCOT's total transmission cost of service. For 2002, this will result in a net gain of \$1.5 million dollars from TCOS.

Transmission and Distribution System

The transmission and distribution lines of the Electric Utility System as of September 30, 2002, are as follows:

| Miles | Description |
|-------|--|
| 114 | 345 kV transmission line (Fayette Power Project) |
| 94 | 345 kV transmission line (South Texas Project) |
| 61 | 345 kV transmission line (Fayette Power Project) (50% ownership with LCRA) |
| 332 | 69 kV and 138 kV transmission lines |
| 9,635 | Overhead and underground distribution lines |

Austin Energy owns the following transmission substations:

| | | |
|--------------|-------------|----------------|
| Austrop | Holman | Lytton Springs |
| Decker Plant | Holly Plant | Pilot Knob |
| Garfield | Sand Hill | Lost Pines |

Austin Energy owns the following distribution substations:

| Name | Capacity (MVA) | Name | Capacity (MVA) |
|---------------|----------------|----------------|----------------|
| Angus Valley | 60 | Lakeshore | 60 |
| Austin Dam | 60 | Lakeway | 60 |
| Barton | 120 | McNeil | 120 |
| Bee Creek | 60 | Magnesium | 90 |
| Bergstrom | 60 | North | 60 |
| Brackenridge | 210 | Northland | 100 |
| Brodie | 90 | Oak Hill | 90 |
| Burleson | 90 | Onion Creek | 60 |
| Cameron | 90 | Patton Lane | 130 |
| Cardinal Lane | 90 | Pedemales | 60 |
| Carson Creek | 60 | River Place | 40 |
| Commons Ford | 60 | Salem Walk | 90 |
| Daffin Gin | 30 | Seaholm | 300 |
| Dessau | 130 | Slaughter Lane | 60 |
| Ed Bluestein | 200 | Sprinkle | 30 |
| Fiskville | 60 | Steck | 90 |
| Grove | 90 | Summit | 180 |
| Hamilton | 120 | Techridge | 60 |
| HiCross | 90 | Trading Post | 30 |
| Howard Lane | 60 | Walnut Creek | 60 |
| Jett | 60 | Warren | 60 |
| Jollyville | 90 | Wheless Lane | 90 |
| Kingsbery | 60 | Williamson | 120 |
| Koenig Lane | 110 | Zilker | 20 |
| Fiesta | 60 | Hidden Valley | 30 |

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The City and LCRA entered into the Fayette Power Project Transmission Agreement dated March 17, 1977 setting forth the duties, obligations and responsibilities with respect to the transmission of energy from the Fayette Power Project. The City has also entered into the South Texas Project 345 kV Transmission Line Agreement dated as of January 1, 1976 with the participants in STP setting forth the duties, obligations and responsibilities with respect to transmission facilities associated with STP.

Austin Energy is interconnected with LCRA, with whom Austin Energy has a power interchange agreement. Austin Energy is also interconnected with Reliant Energy, Inc. ("Reliant"), City Public Service Board of San Antonio and American Electric Power. Austin Energy is a member of ERCOT. As a participant in ERCOT, Austin Energy is able to provide and be provided with a reliable backup supply of generation under emergency conditions. The diversification of fuel sources of the member systems increases the potential for economic interchanges among the respective systems. Sale and purchase transactions generally maximize the use of the less expensive fuel sources by all members of the interconnected system.

Historically, electric utilities operating in Texas have not had any significant interstate connections, and hence investor owned utilities have not been subject to regulation by the Federal Energy Regulatory Commission ("FERC") and its predecessor agencies under the Federal Power Act. Over the past several years, successful efforts have been made to provide interstate connections. These efforts have resulted in protracted judicial and administrative proceedings involving ERCOT members. The settlement of such proceedings permits the ERCOT members to avoid federal regulation as the result of any interstate interconnection with another interstate connected utility.

Power and Energy Sales Contracts

Austin Energy has twenty-nine enabling agreements in place with various market participants. The agreements are designed to facilitate energy transactions by providing a standard agreement and may be cancelled by either party upon thirty days written notice. Any transactions are by mutual agreement; no party is obligated to ever offer, sell or buy energy under the agreements. At certain times, Austin Energy has surplus capacity and energy and is an active participant in the Texas wholesale power market.

Power and Energy Purchase Contracts

The City has signed four long-term energy purchase agreements for wind and landfill gas (Methane) electric generation. A fifth contract was recently executed to provide additional West Texas wind generation upon completion of the necessary generating facilities, which are expected to be complete in late 2003.

Wind Power Purchase . . . In March 1995, the City signed a 25-year contract with LCRA to purchase up to 39,000 MWh of electric energy per year from the Texas Wind Power Project located in the Delaware Mountains east of El Paso. The project went into commercial operation in September 1995.

In December 1999, Austin Energy signed a 10-year contract to purchase the output of a 20 MW wind energy project built by Texas Wind Power Corporation in Upton County. The original contract provided Austin Energy an option to increase the project capacity by an additional 78.4 MW. On October 26, 2000, the City Council approved execution of a contract amendment representing a partial exercise of that option and increasing the project capacity by an additional 56.7 MW. On December 19, 2000 King Wind L.P. assigned the contract to FPL Energy, Inc. The 76.7 MW wind farm began full-scale operation in September 2001.

In January 2003, Austin Energy entered into a 10-year contract with Cielo Windpower Corporation for the purchase of energy from a 25 MW wind project located in Borden County, Texas.

Landfill Gas (Methane) Power Purchase . . . In December 1994, the City signed a contract with Alternative Power Limited Partnership (APLP), an affiliate of Browning-Ferris Industries ("BFI"), to purchase energy from a 3-megawatt landfill gas plant in Austin.

In December 1999, Austin Energy signed two contracts for purchase of energy from landfill methane-recovery projects to be developed by Ecogas Inc. and Energy Developments, Inc. ("EDI"). Ecogas Inc. assigned its rights to EDI in October 2000. In October 2002, EDI brought on the first 5.2 MW of a projected total of 7.8 MW of landfill methane generation at its Tessman Road facilities located in San Antonio, Texas. EDI is also pursuing the development of another 2.6 MW of landfill methane generation from its Hutchins, Texas facility.

Annual Summary of Customer Consumption and Average Price – TABLE FOUR

Austin Energy delivers electricity to an average of approximately 347,000 customers within its service area. The kilowatt-hour sales distributed by customer classification served by Austin Energy are shown in the following table.

| | Fiscal Year Ended September 30 | | | | |
|-----------------------------------|--------------------------------|-----------|-----------|-----------|-----------|
| | 2002 | 2001 | 2000 | 1999 | 1998 |
| All Customers* | | | | | |
| Average Monthly kWh Per Customer | 2,393 | 2,507 | 2,588 | 2,377 | 2,289 |
| Average Monthly Bill Per Customer | \$159.76 | \$181.07 | \$179.91 | \$153.37 | \$152.87 |
| Average Monthly Revenues Per kWh | \$0.06675 | \$0.07224 | \$0.06950 | \$0.06452 | \$0.06678 |
| Residential Customers | | | | | |
| Average Monthly kWh Per Customer | 951 | 1,008 | 1,032 | 945 | 941 |
| Average Monthly Bill Per Customer | \$72.76 | \$81.64 | \$83.17 | \$71.03 | \$72.06 |
| Average Monthly Revenues Per kWh | \$0.07652 | \$0.08099 | \$0.08062 | \$0.07514 | \$0.07656 |
| General Customers** | | | | | |
| Average Monthly kWh Per Customer | 13,876 | 14,264 | 14,480 | 13,716 | 12,941 |
| Average Monthly Bill Per Customer | \$844.40 | \$952.57 | \$909.80 | \$798.62 | \$784.47 |
| Average Monthly Revenues Per kWh | \$0.06085 | \$0.06678 | \$0.06283 | \$0.05823 | \$0.06062 |

* Excludes UT and Nightwatchman.

** Excludes UT, Nightwatchman and the City.

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Generation and Use Data -- TABLE SIX

| | Fiscal Year Ended September 30 | | | | | |
|--|--------------------------------|-----------------------|-----------------------|----------------------|----------------------|----------------------|
| | 2002 | 2001 | 2000 | 1999 | 1998 | |
| Net kWh Generated | | | | | | kWh |
| kWh Received from ERCOT(1) | 9,914,797,000 | 10,671,549,000 | 10,627,483,000 | 10,084,296,000 | 9,770,302,000 | 518,184,000 |
| Less: kWh Delivered to ERCOT | 1,027,954,000 | 499,596,000 | 263,551,000 | 236,149,000 | (43,721,000) | (532,916,000) |
| Less: kWh Delivered to Other Utilities | (135,995,000) | (53,171,000) | (31,160,000) | (36,200,000) | (354,082,000) | 9,711,849,000 |
| Total kWh Delivered to Service Area | <u>(43,394,000)</u> | <u>(46,778)</u> | <u>(355,454,000)</u> | <u>9,900,163,000</u> | <u>9,711,849,000</u> | |
| | <u>10,763,362,000</u> | <u>11,117,927,222</u> | <u>10,504,420,000</u> | | | |
| Service Area Energy Use: | | | | | | |
| Residential | 315,009 | 3,594,055,810 | 3,736,146,850 | 3,415,342,333 | 292,269 | 3,301,122,584 |
| General Service (Less UT & ENW) | <u>37,254</u> | <u>6,203,425,889</u> | <u>6,346,850,890</u> | <u>5,890,650,390</u> | <u>34,665</u> | <u>5,383,228,534</u> |
| | <u>352,263</u> | <u>9,797,481,699</u> | <u>10,082,997,740</u> | <u>9,305,992,723</u> | <u>326,934</u> | <u>8,684,351,118</u> |
| Public Street Lighting | 4 | 34,241,705 | 33,737,705 | 33,226,385 | 3 | 28,174,152 |
| City Utility Departments | 182 | 202,600,427 | 200,713,675 | 195,756,743 | 220 | 204,290,381 |
| Other City Departments | <u>626</u> | <u>106,051,939</u> | <u>111,991,407</u> | <u>95,255,030</u> | <u>498</u> | <u>84,043,151</u> |
| | <u>812</u> | <u>342,894,071</u> | <u>346,442,787</u> | <u>324,238,158</u> | <u>721</u> | <u>316,507,684</u> |
| Total Service Area Sales | 353,075 | 10,140,375,770 | 10,429,440,527 | 9,630,230,881 | 327,655 | 9,000,858,802 |
| Sales to UT & ENW (Nightwatchman) | | 12,354,690 | 11,911,011 | 11,074,895 | | 10,196,845 |
| Loss and Unaccounted For | | <u>610,621,540</u> | <u>676,575,684</u> | <u>258,857,224</u> | | <u>700,793,353</u> |
| Total kWh Delivered to Service Area | <u>353,075</u> | <u>11,117,927,222</u> | <u>10,504,420,000</u> | <u>9,900,163,000</u> | <u>327,655</u> | <u>9,711,849,000</u> |
| System Peak Demand (kW) | 2,247,000(7) | 2,211,000 (6) | 2,183,000(4) | 2,239,000(3) | | 2,389,000(2) |

- (1) Electric Reliability Council of Texas (formerly Texas Interconnected System).
(2) Includes 2,070,000 kW Peak Demand delivered to service area plus net coincidental demand of 319,000 kW delivered to other utilities.
(3) Includes 2,132,000 kW Peak Demand delivered to service area plus net coincidental demand of 107,000 kW delivered to other utilities.
(4) Includes 2,284,000 kW Peak Demand delivered to service area.
(5) Reduction in number of customers is due to the installation of a new billing system in 2000 that changed the way customers are counted rather than customer loss.
(6) Includes 2,171,000 kW Peak Demand delivered to service area.
(7) Includes 2,158,000 kW Peak Demand delivered to service area.

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Electric Rates – TABLE SEVEN

The following electric rates are effective March 17, 1997 by Ordinance 970306-P. See "Rate Regulation" below.

| Customer Class | Fuel Adjustment Clause (1) | Customer Charge | 1 st 500 kWh | Energy Charge | |
|---|----------------------------|------------------|-------------------------|--|---|
| | | | | Winter | Summer |
| Residential Service (E01) | All kWh | \$6.00 | \$.0355 Per kWh | November – April \$.0602 All kWh Above 500 kWh .0464 All kWh .0319 All kWh | May - October \$.0782 All kWh Above 500 kWh .0644 All kWh .0499 All kWh |
| General Service Non-Demand (E02) | All kWh | 6.00 | | | |
| State Accounts Non-Demand (E13) | All kWh | 6.00 | | | |
| | | Minimum Bill (2) | | | |
| Water and Wastewater (E03) | All kWh | \$12.00 | | .0277 All kWh | .0648 All kWh |
| Other City (Including Electric) (E04) | All kWh | 12.00 | | .0354 All kWh | .0521 All kWh |
| Streetlight/Traffic (E05) | All kWh | 12.00 | | .1498 All kWh | .1498 All kWh |
| | | | | | |
| General Service Demand (E06) | All kWh | 12.00 | | \$12.65 All kW | \$14.03 All kW |
| General Service Demand - Public Schools (E10) (3) | All kWh | 12.00 | | 5.68 All kW | 7.95 All kW |
| Primary Service (E07) | All kWh | 12.00 | | 11.11 All kW | 12.10 All kW |
| Large Primary Service (E08) (3) | All kWh | 12.00 | | 11.81 All kW | 12.60 All kW |
| State Accounts – Demand Secondary Service (E14) | All kWh | 12.00 | | 10.94 All kW | 11.64 All kW |
| State Accounts – Primary Service (E17) | All kWh | 12.00 | | 10.94 All kW | 11.64 All kW |
| State/Large Primary Service (E15) (3) | All kWh | 12.00 | | 10.94 All kW | 11.64 All kW |
| Transmission Service (E11) | All kWh | 12.00 | | 10.98 All kW | 11.72 All kW |
| Nightwatchman | | | | | |
| 175 Watt Mercury Vapor | Fuel Charge | | | | Customer Charge |
| 100 Watt High Pressure Sodium | 60 kWh Per Light | | | | \$ 7.34 Per Light |
| 400 Watt Mercury Vapor | 35 kWh Per Light | | | | 4.28 Per Light |
| 250 Watt High Pressure Sodium | 140 kWh Per Light | | | | 17.11 Per Light |
| | 90 kWh Per Light | | | | 11.00 Per Light |

(1) The Fuel Adjustment Clause recovers fuel costs. The calculation of the Fuel Adjustment Clause is described in the Rate Ordinance.

(2) Minimum Bill is applied when the sum of energy, demand and fuel charges is less than \$12.00.

(3) Does not include special contracts, time-of-use and economic development rates.

Annual Adjustment Clause

The City assesses an Annual Adjustment Clause charge based on a formula designed to recover the actual cost of fuel, purchased power, and wholesale fees and charges to meet the City's service area obligations. The intent of the fuel formula is to avoid any over or under recovery of costs associated with fuel.

Green Choice Energy Rider

In March 2001, Austin Energy adopted a Green Choice Energy charge for renewable energy. Customers who subscribe to the wind and methane gas energy will pay a renewable energy charge in lieu of the fuel adjustment factor as determined by Austin Energy.

Fuel

Coal . . . Coal supplies are procured through a portfolio of contracts with transportation specifically managed to minimize cost. Typically several months of coal inventory are maintained to protect against disruptions.

Natural Gas and Oil . . . Austin Energy manages its gas contracts in an effort to diversify risk and minimize cost. In case of a curtailment in natural gas supplies, fuel oil is used to replace the natural gas shortfall. Austin Energy maintains an oil reserve equivalent to several days of operation.

Nuclear . . . Nuclear fuel is procured through a jointly owned operating company.

Rate Regulation

The City's rates, except for wholesale transmission, are regulated by the City Council. Ratepayers can appeal rate changes to the PUCT under section 33.101 of the Public Utility Regulatory Act ("PURA") by the filing of a petition with the PUCT containing the requisite number of valid signatures from residential ratepayers who take service outside the City's corporate limits.

The Texas courts have held that the PUCT may apply the same ratemaking standards to the City as are applied to utilities over which the PUCT has original jurisdiction.

The Electric Utility System of the City initiated a local rate proceeding in response to the increasing competitive nature of the electric utility industry. Austin Energy proposed a reduction or elimination of certain rates, the creation of new tariffs, and amendment of existing tariffs and the customer service regulations. The changes were designed to offer customers more choice and value. Basic electric rates did not increase as a result of the proposed changes. The last increase in base rates was in 1994. The City Council approved most of the proposals in December 1996 and March 1997.

In 1995, PURA was amended as it pertains to the PUCT's original jurisdiction over the City's provision of wholesale transmission service. The PUCT now has exclusive jurisdiction over rates and terms and conditions for the provision of transmission services by the City. Section 35.004 of PURA requires the City to provide transmission service at wholesale to another utility, a qualifying facility, an exempt wholesale generator, a power marketer, power generation company, or a retail electric provider. Section 35.004 of PURA requires the City to provide wholesale services at rates, terms of access, and conditions that are not unreasonably preferential, discriminatory, predatory, or anti-competitive. The PUCT adopted rules relating to wholesale transmission service. The City participated in the rulemaking. The current rules have been challenged in two original petitions filed by Reliant (formerly Houston Lighting & Power Co.) and City Public Service Board of San Antonio seeking a declaratory judgment holding the transmission pricing methodology in the PUCT's new transmission rules invalid and seeking a remand of the rulemaking. The City intervened in the proceedings in defense of the rulemaking. The two proceedings were consolidated and on April 20, 1998, the 98th District Court of Travis County entered final judgment against the plaintiffs, declaring the PUCT rules to be "valid, constitutional, and fully effective". The plaintiffs then appealed to the Third Court of Appeals in Austin. On January 6, 2000, the Third Court of Appeals invalidated those parts of the PUCT rules dealing with transmission rates, reversing the trial court and rendered judgment for the appellants. The City and others petitioned the Supreme Court of Texas for a review of the Third Court of Appeals opinion and the Supreme Court issued a ruling on June 28, 2001 affirming the ruling of the Third Court of Appeals. The PUCT has not taken any action based on the Supreme Court's ruling. However, Reliant and City Public Service Board of San Antonio filed two separate actions in Travis County District Court in January 2002 seeking a declaration by the court as to the amount of refunds due to them as a result of the ruling by the Supreme Court. Austin Energy intends to vigorously defend in this matter.

The City filed with the PUCT a filing package delineating transmission cost of service and costs for ancillary services related to transmission service. The PUCT entered a Final Order on the filing by the City effective January 1, 1997. The Final Order increased net income to the system by approximately \$6.0 million on an annual basis. However, because the City's ratio of transmission investment has decreased over time, as compared to other transmission providers, the net income received on annual basis has decreased.

An Independent System Operator ("ISO") was established for ERCOT as a part of the rules that were adopted by the PUCT to open access to the wholesale electric market in Texas and was approved by the PUCT on August 21, 1996. The ISO received approval on May 5, 2000, of its certification under Senate Bill 7 ("SB7"). The ISO's primary mission is to act as an impartial third party operator and planning coordinator for the ERCOT bulk electric system. The City is a member of ERCOT.

In addition, the 1995 PURA revisions required the creation of a committee to investigate the most economical, reliable and efficient means to interconnect the alternating current electric facilities of ERCOT to similar electric utility facilities within the Southwest Power Pool reliability area. A final report was issued to the Legislature during the 1999 session. No further action has been taken on interconnection by the Legislature.

During the 1999 Legislative Session PURA was amended by SB 7 providing for deregulation of the electric utility industry in Texas. SB 7 opened retail competition for investor owned utilities beginning January 1, 2002. SB 7 allows local authorities to choose when to bring retail competition to their Municipally Owned Utilities ("MOU"), and leaves key municipal utility decisions (like local rate setting and utility policies) in the hands of those who have a stake in the local community. Once a resolution to "opt in" for retail competition is adopted by the municipal utility's governing body, the decision is irrevocable.

General Market Framework: There is a strong ISO established, with clear and enforceable market power protections: no utility can control more than 20% of ERCOT generation. Starting on January 1, 2002, a "Price-to-Beat" for the incumbent Investor Owned Utilities (IOU) rates includes a 6% reduction through 2005 or until 40% of IOU residential and small commercial customers choose a new supplier. There are protections against over-recovery of stranded investment by IOUs and protections against anti-competitive practices and predatory pricing. Retail competitors are required to sell to the residential market (minimum 5% of their business with residential if they sell more than 300 MWs). The air quality provisions require clean up of older "grandfathered power plants".

MOUs Which Do Not Choose Retail Competition

- There is no retail choice for MOU customers. MOU cannot sell at retail outside its area.
- Current regulatory scheme continues.
- Continued MOU access to buy and sell power in the wholesale market.

MOUs Choosing Retail Competition On or After January 1, 2002

(City councils or governing boards make an affirmative choice to bring retail competition to their MOU)

- Retail competitors can sell "generation" to MOU customers. MOU provides "wires" access to its distribution system for Retail Electric Providers, other MOUs and Electric Cooperatives. MOU has an "obligation to connect" and provides wire services and local reliability. Wires are not subject to competition.
- MOU can sell at retail outside its service area, per prevailing market rules.

MOU Local Control Preserved

- Exclusive MOU jurisdiction to set local distribution and other rates. Local wires services and rates remain in exclusive jurisdiction of the MOU.
- Local determination of the stranded investment amount and recovery mechanism.
- MOUs are not required to unbundle (structurally separate functions).
- Local authorities determine and provide customer services and protections.
- Local control of MOU power resource acquisition.
- Customers in multi-certified areas cannot switch wires companies to avoid stranded investment charges.
- Securitization is available to MOUs.

Participation By MOU In Markets Outside Its Area

- Limited PUCT jurisdiction over terms and conditions for access not rates.
- Subject to market power limits and PUCT anti-competitive code of conduct.

Metering And Billing

- MOU retains metering.
- Customers with another generation supplier choose either one consolidated bill from the MOU, or two separate bills (one for wires, one for generation).
- Under SB 7, a System Benefit Fund will be established for consumer education programs, low-income customer programs and loss of tax revenue by school districts resulting from a devaluation of generation assets in the competitive market. A system benefit fee will be added to the utility bills of IOU customers to provide funding for the System Benefit Fund. MOUs are not required to bill their customers this system benefit fee until six months prior to the MOU "opt-in" date, if the MOU governing body elects to "opt-in." The System Benefit Fund will expire September 2007.

Other Key MOU Provisions

- Existing contracts are preserved. Tax-exempt status is preserved. MOU "competitiveness provisions" were included in SB 7 to "level" the field for MOUs when preparing for competition including relaxation of open meetings/records and purchasing provisions. No mandated MOU rate reductions.
- The City has not yet made a decision whether to "opt in" for retail competition or not, and the City cannot predict the short term or long term impact on the Electric Utility System or its revenues resulting from a decision to "opt in" or not, or resulting from the deregulation process in general.

Real Estate Taxes

Austin Energy pays no real property taxes on facilities inside or outside the City, nor payments in lieu of taxes with respect to Austin Energy.

Service Area

The service area for Austin Energy was established by the PUCT pursuant to a certificate of convenience and necessity on April 3, 1978. The City's service area encompasses 206.41 square miles within the City itself and 230.65 square miles of surrounding Travis and Williamson Counties. The establishment of such a service area entitles Austin Energy to provide electric service within such area. As presently constituted, the City's service area overlaps with approximately 11 square miles of the service area of TXU in Travis and Williamson Counties.

The City may not extend the service area for Austin Energy to an area receiving similar utility service without first obtaining a certificate of convenience and necessity from the PUCT. The City has no plans to expand its present service area.

Federal Regulation

Rate Regulation and Wholesale Wheeling . . . Austin Energy is not subject to Federal regulation in the establishment of rates, the issuance of securities or the operation, maintenance or expansion of Austin Energy under current Federal statutes and regulations. Austin Energy submits various reports to FERC and voluntarily utilizes the FERC System of Accounts in maintaining its books of accounts and records. On April 24, 1996, the FERC issued a Final Rule (the "Rule") proposing significant changes regarding transmission service performed by electric utilities subject to the FERC's jurisdiction under sections 205 and 206 of the Federal Power Act. Among other things, the FERC requires utilities to submit open-access, mandatory transmission tariffs. The goal of the Rule, according to the FERC, is to deny to an owner of transmission facilities any unfair advantage over its competitors that exists by virtue of such owner's control of its transmission system.

Although municipally-owned utilities, including Austin Energy, are not subject to the FERC's jurisdiction under sections 205 and 206 of the Federal Power Act, the proposals in the Rule could have a significant effect on those utilities. The FERC stated that its overall objective was to ensure that all participants in wholesale electricity markets have non-discriminatory open access to transmission service, including network transmission service and ancillary services. The FERC also indicated that it intends to apply the principles set forth in the Rule to the maximum extent to municipal and other non-jurisdictional utilities, both in deciding cases brought under sections 211 and 212 of the Federal Power Act and by requiring such utilities to agree to provide open access transmission service as a condition to securing transmission service from jurisdictional investor-owned utilities under open access tariffs.

According to the Rule, an open access transmission tariff must provide for functional unbundling of utility service, so that the filing utility will be obliged to purchase transmission service to meet its native load under the same transmission tariff it offers to others. A conforming tariff must be available to any entity eligible to request a section 211 order, must provide for expansion of the transmission system when necessary to provide service, must offer firm point-to-point and network service as well as non-firm transmission service, and must offer to provide such ancillary services (e.g., reactive power, loss compensation, scheduling and

dispatch, system protection and energy imbalance services) as the transmission provider provides to itself. Transmission capacity must be subject to reassignment and sale on a secondary market. Transmission owners must also make available to potential users an index of capacity owners and information about the transmission capacity available for sale.

The FERC also ruled that it will permit utilities that file conforming open access transmission tariffs to recover their legitimate and verifiable stranded costs from wholesale sales customers who had been parties to sales contracts executed before July 11, 1994 which did not contain an exit fee or other provision relating to stranded cost recovery and who exercised their option to become transmission customers and purchase their electricity needs off-system. In order to recover stranded costs, the FERC said, a utility would be required to demonstrate that it had a "reasonable expectation" of continuing to serve the former customer's requirements for electric sales service and would also be required to demonstrate that it had attempted to mitigate its stranded costs.

Recovery of stranded costs resulting from retail wheeling initially would be the responsibility of state regulatory commissions, which could not permit such recovery in interstate transmission rates but must, instead, use such mechanisms as a surcharge upon rates for local distribution or an exit fee for departing retail customers to compensate utilities for stranded costs stemming from retail wheeling. If, however, a state commission lacked legal authority to provide for compensating utilities for stranded costs resulting from retail wheeling or if the stranded costs result from a formerly retail sale customer becoming a wholesale customer (e.g., by municipalization), the FERC itself would permit the recoverable stranded costs to be recovered in interstate transmission rates.

Although the Rule does not directly regulate non-jurisdictional utilities such as Austin Energy, the Rule could have a significant impact on such utilities' operations. It could significantly change the competitive climate in which they operate, giving their customers much greater access to alternative sources of electric sales service. It would require them to provide open access transmission service conforming to the requirements for investor-owned utilities whenever they are properly requested to do so under sections 211 and 212 of the Federal Power Act or as a condition of taking transmission service from an investor owned utility. In certain circumstances, it would require non-jurisdictional utilities to pay compensation to their present suppliers of wholesale power and energy for the stranded investment that may arise when the non-jurisdictional utilities exercise their option to switch to an alternative supplier of electricity.

On December 20, 1999, the FERC issued "Order No. 2000" (the "Order") related to the formation of voluntary Regional Transmission Organizations ("RTOs"). The Order requires all utilities subject to the FERC's authority under section 205 (Rates and Charges; Schedules; Suspension of New Rates) and 206 (Fixing Rates and Charges; Determination of Cost of Production or Transportation) of the Federal Power Act to file by October 2000 a proposal to participate in an RTO or an alternative describing plans to participate in an RTO. The essential characteristics of an RTO are its independence from individual market participants, a regional scope, operational authority of transmission facilities under the RTO's control, and authority over short-term system reliability. The essential functions of an RTO are tariff administration, congestion management, parallel path flow, administering ancillary services, operating Open Access Scheduling Information System ("OASIS"), market monitoring, planning and expansion, and interregional coordination. In their October 2000 compliance filings, utilities proposed RTOs across the country incorporating a wide variety of organizational forms. RTO proposals will be reviewed by the FERC for approval.

Austin Energy is not subject to the FERC's jurisdiction under section 205 and 206 of the Federal Power Act. Nevertheless, Austin Energy participates in a stakeholder organization that is similar to the RTOs envisioned in Order 2000 and which predates Order 2000 by several years. ERCOT is a stakeholder organization that includes stakeholders from all segments of the Texas' electric market. The ISO formed by ERCOT in 1996 and mandated by State law in 1999 carries out many of the functions of the RTO discussed in Order 2000.

Environmental

General . . . Austin Energy's Environmental Policy commits that Austin Energy shall maintain its status as a leader in environmental stewardship and continually improve its environmental performance. Austin Energy's operations are subject to environmental regulation by Federal, State and local authorities. Austin Energy has processes in place for assuring compliance with applicable environmental regulations. Austin Energy maintains a staff of educated and trained environmental compliance professionals that are responsible for establishing and maintaining compliance programs throughout the utility. Environmental Services has determined the existing Federal, State and local regulations and routinely track changes to regulations, which affect Austin Energy processes. Austin Energy has prepared documentation which details roles and responsibilities for environmental compliance throughout the organization. Environmental Services staff and facility personnel monitor conformance with the environmental requirements and report deficiencies to facility management. Environmental Services is also responsible for conducting environmental training for the organization.

Air Emissions . . . Congress enacted the Clean Air Act Amendments of 1990, which included permitting requirements for power production facilities. All of Austin Energy's generating units are required to have Federal Operating Permits and Federal Acid Rain Permits. With the exception of the new Sand Hill Energy Center (which is currently being permitted), all Austin Energy generating units have been issued Federal Operating Permits and Federal Acid Rain Permits by the Texas Commission on Environmental Quality ("TCEQ"). References to the TCEQ in this Official Statement are intended to include agencies whose duties and responsibilities have been assumed by the TCEQ.

In 1999, as part of SB 7, the Texas Legislature imposed new environmental regulations on power plants constructed prior to 1971 (30 TAC 116, Electric Generating Facility Permits, and 30 TAC 101.330, Emissions Banking and Trading of Allowances). Austin Energy's units were "grandfathered" from State permitting requirements at the time of the passage of the Texas Clear Air Act in 1971. SB 7 instituted a "cap and trade" program for NOx emissions. "Grandfathered" units were allocated allowances of NOx based on an emission rate of 0.14 lbs. of NOx per mmBtu times the 1997 heat input to the unit. Austin Energy's SB 7 permitted units must have enough SB 7 emission allowances available to cover the actual emissions from these units on a yearly basis. If the total NOx emissions from these plants exceed the total system allocation, Austin Energy must purchase the additional allowances needed to cover its emissions. The emission-trading program will also allow Austin Energy to sell in the open market emission allowances derived from excess NOx reductions.

The TCEQ has implemented further NOx reduction rules under 30 TAC 117 which will primarily impact Austin Energy's coal burning Fayette Power Plant Units 1 and 2, in each of which Austin Energy owns a 50% interest. The TCEQ is requiring that "grandfathered units" such as these units reduce NOx to 0.165 lb/mmBtu by 2005. Modifications are currently being made to the units so that they will achieve these emission rates before the compliance deadline. Furthermore, Austin Energy and the co-owner, LCRA have agreed under a flexible permit arrangement with the TCEQ and EPA to place scrubbers on Units 1 and 2 within the next 10 years. In return, Fayette Power Plant is allowed to make modifications and perform maintenance on the units without having to first obtain permission from TCEQ.

Water

Wastewater discharges are regulated pursuant to the Clean Water Act National Pollution Discharge Elimination System ("NPDES"). Stormwater run-off is similarly regulated. The EPA has granted the TCEQ authority to implement these programs in Texas. All of Austin Energy's power generation facilities have NPDES and Stormwater Permits, which require monitoring and limitations of discharges. EPA has also developed proposed regulations for cooling water intake structures on existing facilities. These proposed regulations will affect all Austin Energy power plants, but the extent cannot be determined at this time due to litigation between utilities and EPA on the rulemaking.

Other

Austin Energy has implemented a program for removing distribution electrical equipment at risk for having polychlorinated biphenyls (PCBs) from its service area. Austin Energy crews are testing electrical equipment for PCBs and removing equipment found to have PCBs. Furthermore, substation equipment and soils are routinely tested prior to construction activities in the event that there is contamination from historical activities. Austin Energy will complete the decommissioning of the Seaholm Power Plant in the next year, which includes the removal of power plant equipment and contaminated concrete.

Austin Energy will continue to make the necessary changes to assure future compliance with the evolving regulatory requirements. Non-compliance with environmental standards or deadlines could result in reduced operating levels. Further compliance with environmental standards or deadlines could increase capital and operating costs.

Nuclear

Nuclear generation facilities are subject to regulation by the Nuclear Regulatory Commission ("NRC") and are required to obtain liability insurance and a United States Government indemnity agreement in order for the NRC to issue operating licenses. This primary insurance and the retrospective assessment discussed below are to insure against the maximum liability under the Price-Anderson Act for any public claims arising from a nuclear incident which occurs at any of the licensed nuclear reactors located in the United States.

STP is still protected by provisions of the Price-Anderson Act, a comprehensive statutory arrangement providing limitations on nuclear liability and governmental indemnities even though the statutory protections for many non-commercial reactors expired on August 1, 2002. The limit of liability under the Price-Anderson Act for licensees of nuclear power plants is \$9.34 billion per incident. The maximum amount that each licensee may be assessed following a nuclear incident at any insured facility is \$83.9 million, subject to adjustment for inflation, for the number of operating nuclear units and for each licensed reactor, payable at \$10

million per year per reactor for each nuclear incident. The City and each of the other participants of STP are subject to such assessments, which will be borne on the basis of their respective ownership interests in STP. For purposes of the assessments, STP has two licensed reactors. The participants have purchased the maximum limits of nuclear liability insurance, as required by law, and have executed indemnification agreements with the NRC, in accordance with the financial protection requirements of the Price-Anderson Act.

A Master Worker Nuclear Liability policy, with a maximum limit of \$400 million for the nuclear industry as a whole, provides protection from nuclear-related claims of workers employed in the nuclear industry after January 1, 1988 who do not use the workers' compensation system as sole remedy and bring suit against another party.

NRC regulations require licensees of nuclear power plants to obtain on-site property damage insurance in a minimum amount of \$1.06 billion. NRC regulations also require that the proceeds from this insurance be used first to ensure that the licensed reactor is in a safe and stable condition so as to prevent any significant risk to the public health or safety, and then to complete any decontamination operations that may be ordered by the NRC. Any funds remaining would then be available for covering direct losses to property.

The owners of STP currently maintain \$2.75 billion of nuclear property insurance, which is above the legally required amount of \$1.06 billion, but is less than the total amount available for such losses. The \$2.75 billion of nuclear property insurance consists of \$500 million in primary property damage insurance and \$2.25 billion of excess property damage insurance, both subject to a retrospective assessment being paid by all members of Nuclear Electric Insurance Limited (NEIL). In the event that property losses as a result of an accident at any nuclear plant insured by NEIL exceed the accumulated fund available to NEIL, a retrospective assessment could occur. The maximum aggregate assessment under current policies for both primary and excess property damage insurance is \$12.9 million during any one-policy year.

Finally, the NRC maintains its regulations setting forth minimum amounts required to demonstrate reasonable financial assurance of funds for decommissioning of nuclear reactors. Beginning in 1990, each holder of an operating license was required to submit to the NRC a report indicating how reasonable assurance would be provided. The City provided the required report to the NRC and determined that the minimum amount for decommissioning is \$105 million (January 1986 dollars). This minimum is required to be adjusted annually in accordance with the adjustment factor formula set forth in the regulations. The report provided by the City based reasonable assurance on the minimum amount (January 1986 dollars) as adjusted by the adjustment factor formula set forth in the regulations. The City has established an external irrevocable trust for decommissioning with Bank One, National Association. The City has been collecting for decommissioning through its rates since Fiscal Year 1989. The decommissioning account balance at September 30, 2002 was \$81,726,716 (unaudited). For Fiscal Year 2003, Austin Energy estimates that it will continue to collect approximately \$4,958,221 for decommissioning expense.

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**COMPARATIVE ANALYSIS OF ELECTRIC UTILITY SYSTEM
AND WATER AND WASTEWATER SYSTEM OPERATIONS
OCTOBER 1, 1997 TO SEPTEMBER 30, 2002**
(Thousands Rounded)

| | Fiscal Year Ended September 30 | | | |
|---|--------------------------------|-------------------|-------------------|------------------|
| | (Unaudited) 2002 (e) | 2001 | 2000 | 1999 |
| INCOME | | | | |
| Revenue | \$1,028,019 | \$1,087,541 | \$1,070,558 | \$918,508 |
| Operating Expense | <u>513,772</u> | <u>561,097</u> | <u>516,441</u> | <u>429,926</u> |
| Balance Available for Debt Service Depreciation and Amortization Expense | 514,240 | 526,444 | 554,117 | 496,766 |
| | <u>145,601</u> | <u>138,068</u> | <u>133,393</u> | <u>125,272</u> |
| Earnings Before Interest Expense | 368,639 | 388,376 | 420,724 | 371,487 |
| Interest Incurred on Debt | <u>(172,111)</u> | <u>(187,296)</u> | <u>(183,653)</u> | <u>(177,327)</u> |
| Other | <u>(3,720)</u> | <u>(1,052)</u> | <u>(2,174)</u> | <u>(9,661)</u> |
| INCOME (LOSS) BEFORE OPERATING TRANSFERS (a) (b) | <u>\$ 192,808</u> | <u>\$ 200,021</u> | <u>\$ 234,897</u> | <u>\$184,499</u> |
| PERCENTAGES | | | | |
| Revenue | 100.00% | 100.00% | 100.00% | 100.00% |
| Operating Expense | <u>49.98%</u> | <u>51.59%</u> | <u>48.24%</u> | <u>45.07%</u> |
| Balance Available for Debt Service | 50.02% | 48.41% | 51.76% | 53.61% |
| Depreciation and Amortization Expense | <u>14.16%</u> | <u>12.70%</u> | <u>12.46%</u> | <u>13.52%</u> |
| Earnings Before Interest Expense | 35.86% | 35.71% | 39.30% | 40.09% |
| Interest Incurred on Debt | <u>-16.74%</u> | <u>-17.22%</u> | <u>-17.15%</u> | <u>-19.14%</u> |
| Other | <u>-0.36%</u> | <u>0.10%</u> | <u>-0.20%</u> | <u>-1.04%</u> |
| INCOME BEFORE EXTRAORDINARY GAIN (LOSS) (a) (c) | <u>18.76%</u> | <u>18.39%</u> | <u>21.95%</u> | <u>19.91%</u> |
| (d) | | | | |

(a) Income before transfers to the General Fund and Other Funds, for 12 months ended September 30, 2002, which are as follows:
Transfer to General Fund \$88,924,092

Transfers to Other Funds \$ 3,243,070

(b) Excludes Combined Utility Funds' deferred costs of (\$14,550,536) for twelve months ended September 30, 2002.

(c) There was no extraordinary gain or loss during this twelve-month period.

(d) Excludes capital contributions of \$31,149,182 for twelve months ended September 30, 2002.

(e) Audited numbers expected to be available prior to April 15, 2003.

**OPERATING STATEMENT
ELECTRIC UTILITY SYSTEM AND WATER AND WASTEWATER SYSTEM**

| | Fiscal Year Ended September 30 | | | |
|--|--------------------------------|------------------------|------------------------|----------------------|
| | (Unaudited) 2002 (1) | 2001 | 2000 | 1999 |
| REVENUE | | | | |
| ELECTRIC UTILITY | | | | |
| Service Area Sales | \$ 669,603,761 | \$756,246,287 | \$723,260,135 | \$622,488,907 |
| Sales to Other Utilities (Including Capacity Contract) | 41,624,993 | 33,134,735 | 50,780,027 | 51,565,929 |
| Rent from Electric Property | 2,002,436 | 995,375 | 851,352 | 870,118 |
| Customers' Forfeited Discounts and Penalties | 4,738,299 | (36,129) | 1,557,559 | 3,982,395 |
| Miscellaneous | 32,156,404 | 15,970,414 | 6,280,055 | 3,614,356 |
| Total Electric Utility | \$ 750,125,893 | \$806,310,682 | \$782,729,128 | \$668,371,051 |
| WATER UTILITY | | | | |
| Urban | \$ 104,258,577 | \$ 98,746,345 | \$ 109,962,989 | \$ 91,861,270 |
| Rural | 6,837,030 | 6,438,710 | 7,413,123 | 5,581,758 |
| City Utility Departments | 0 | 0 | 0 | 309,925 |
| City General Government Departments | 0 | 0 | (42,206) | 1,086,946 |
| Sales to Other Water Utilities | 7,218,149 | 7,238,838 | 7,940,351 | 6,386,790 |
| Water Connections | 300,079 | 237,280 | 207,742 | 232,980 |
| Customers' Forfeited Discounts and Penalties | 784,257 | (5,253) | 263,506 | 605,178 |
| Miscellaneous | 2,636,398 | 2,016,478 | 4,443,174 | 3,556,202 |
| Total Water Utility | \$ 122,034,490 | \$ 114,672,398 | \$ 130,188,679 | \$105,897,158 |
| WASTEWATER UTILITY | | | | |
| Urban | \$ 92,717,674 | \$ 92,293,455 | \$ 97,895,552 | \$ 91,671,869 |
| Rural | 3,311,487 | 2,810,219 | 2,630,647 | 2,228,573 |
| City Utility Departments | 0 | 1,166 | 6,670 | 546,246 |
| City General Government Departments | 0 | 0 | 0 | 41,788 |
| Service to Other Utilities | 3,168,940 | 3,337,932 | 3,252,372 | 3,030,741 |
| Wastewater Connections | 275,298 | 217,507 | 190,430 | 216,338 |
| Customers' Forfeited Discounts and Penalties | 733,320 | (3,312) | 260,173 | 573,446 |
| Miscellaneous | 7,292,633 | 6,585,139 | 6,054,111 | 6,112,737 |
| Total Wastewater Utility | \$ 107,499,352 | \$ 105,242,106 | \$ 110,289,955 | \$104,421,738 |
| Interest | \$ 48,359,533 | \$ 61,315,883 | \$ 47,350,612 | \$ 30,561,222 |
| TOTAL REVENUE | \$1,028,019,268 | \$1,087,541,069 | \$1,070,558,374 | \$918,508,145 |

(1) Audited numbers expected to be available prior to April 15, 2003.

**OPERATING STATEMENT
ELECTRIC UTILITY SYSTEM AND WATER AND WASTEWATER SYSTEM – (Continued)**

| | Fiscal Year Ended September 30 | | | |
|---|--------------------------------|---------------|---------------|---------------|
| | (Unaudited) 2002 (2) | 2001 | 2000 | 1999 |
| EXPENSE | | | | |
| ELECTRIC | | | | |
| Total Electric Utility | \$401,439,239 | \$458,685,525 | \$420,074,862 | \$342,914,020 |
| WATER | | | | |
| Purification | \$ 16,701,681 | \$ 15,302,623 | \$ 14,225,476 | \$ 12,649,706 |
| Distribution | 20,896,684 | 20,196,995 | 18,246,648 | 15,575,024 |
| Customers' Accounting and Collection | 6,377,532 | 5,202,484 | 5,456,698 | 3,908,047 |
| Jobbing and Contract Work | (78,292) | 51,692 | 14,214 | (27,468) |
| Design Engineering | 800,574 | 425,250 | 1,921,976 | 1,251,519 |
| Administrative and General | 15,296,306 | 12,405,831 | 12,938,784 | 10,764,449 |
| Total Water Utility | \$ 59,994,485 | \$ 53,584,875 | \$ 52,803,796 | \$ 44,121,277 |
| WASTEWATER | | | | |
| Wastewater Lines | \$ 6,298,911 | \$ 6,175,380 | \$ 7,591,689 | \$ 8,562,780 |
| Sewage Treatment Plant | 21,405,291 | 19,171,921 | 17,115,187 | 17,633,822 |
| Customers' Accounting and Collection | 3,017,134 | 4,374,495 | 4,406,215 | 2,482,971 |
| Jobbing and Contract Work | 24,057 | 86,683 | 68,505 | 55,906 |
| Design Engineering | 7,437,170 | 6,846,189 | 1,998,054 | 2,312,461 |
| Administrative and General | 14,163,441 | 12,172,179 | 12,382,295 | 11,842,412 |
| Total Wastewater Utility | \$ 52,346,004 | \$ 48,826,847 | \$ 43,561,945 | \$ 42,890,352 |
| TOTAL EXPENSE (1) | \$513,779,728 | \$561,097,247 | \$516,440,603 | \$413,938,513 |
| NET REVENUE AVAILABLE FOR DEBT SERVICE | \$514,239,540 | \$526,443,822 | \$554,117,771 | \$496,765,948 |
| Electric Customers | 359,368 | 354,302 | 350,382 | 363,178 |
| Water Customers | 182,977 | 178,608 | 176,096 | 173,038 |
| Wastewater Customers | 168,159 | 163,610 | 151,744 | 159,157 |

(1) Interest expense, depreciation, amortization and other non-operating items are not included in total expense.

(2) Audited numbers expected to be available prior to April 15, 2003.

DISCUSSION OF OPERATING STATEMENT

Austin Energy Revenues

Variations in total Austin Energy revenues for the period beginning with the fiscal year ("FY") FY98 through FY02 were attributable to changes in cost of fuel for power generation and weather variations. Total fuel costs are passed through to the consumer.

Water and Wastewater System Revenues

Variations in Water and Wastewater System revenues for the period FY98 through FY02, were largely attributable to weather and system rate changes.

Austin Energy Expenses

Changes in Austin Energy expenses for the period FY98 through FY02 were largely attributable to changes in the cost of fuel for power generation and general inflationary increases in other expense categories.

Water and Wastewater System Expenses

Changes in Water and Wastewater System expenses for the period FY98 through FY02 were primarily attributable to inflationary increases in the cost of power, and chemicals, along with system growth.

In June 1999, the Governmental Accounting Standards Board issued Statement No. 34 (GASB 34), Basic Financial Statements- and Management's Discussion and Analysis (MD&A) - for State and Local Governments. Subsequently, the GASB issued related Statement Nos. 37, 38 and 39. The objective of these Statements is to enhance the clarity and usefulness of the general-purpose external financial reports of state and local governments to the citizenry, legislative and oversight bodies, and investors and creditors. The Statements require a new reporting model for financial statements for governments, with a focus on the entity as a whole.

The City will implement GASB 34 and the related statements for the fiscal year ending September 30, 2002, in compliance with GASB 34 timelines. While adoption of this Statement will alter the presentation of the City's financial information, City management does not believe that the adoption of GASB 34 will have any material adverse impact on the City's financial position, results of operation, or cash flows. Consistent with GASB 34, the City will not present restated prior fiscal year data for the purpose of providing comparative data. In future years, the City will present comparative data in the financial statements.

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The Electric Utility System and Water and Wastewater System - TABLE SEVENTEEN

As of September 30

| | (Unaudited) 2002 (4) | 2001 | 2000 | 1999 | 1998 |
|--|-------------------------|------------------------|------------------------|------------------------|------------------------|
| Plant Cost | | | | | |
| Utility Systems | | | | | |
| Electric | \$3,238,841,489 | \$3,067,649,886 | \$2,842,927,082 | \$2,693,237,524 | \$2,625,217,308 |
| Water | 1,229,543,897 | 1,169,574,534 | 1,090,911,586 | 1,003,650,278 | 893,668,714 |
| Wastewater | 1,139,027,206 | 1,080,758,935 | 1,032,885,331 | 976,681,032 | 921,580,649 |
| Total Cost | <u>\$5,607,412,592</u> | <u>\$5,317,983,355</u> | <u>\$4,966,723,999</u> | <u>4,673,568,834</u> | <u>4,440,466,671</u> |
| Allowance for Depreciation: | | | | | |
| Electric | 1,209,333,262 | \$1,131,860,735 | \$1,048,947,313 | 972,367,880 | 895,154,272 |
| Water | 287,657,206 | 264,352,217 | 242,395,336 | 220,477,506 | 202,674,479 |
| Wastewater | <u>353,176,892</u> | <u>328,639,983</u> | <u>304,151,983</u> | <u>280,008,297</u> | <u>256,629,792</u> |
| Total Depreciation | <u>1,850,167,360</u> | <u>1,724,852,935</u> | <u>1,595,494,632</u> | <u>1,472,853,683</u> | <u>1,354,458,543</u> |
| Cost after Depreciation | <u>\$3,757,245,232</u> | <u>\$3,593,130,420</u> | <u>\$3,371,229,367</u> | <u>\$3,200,715,151</u> | <u>\$3,086,008,128</u> |
| City's Equity in the Systems | | | | | |
| Utility Systems | \$5,607,412,592 | \$5,317,983,355 | \$4,966,723,999 | \$4,673,568,834 | \$4,440,466,671 |
| Plus: Inventories, Materials and Supplies (1) | 32,980,392 | 34,688,816 | 32,904,657 | 32,227,327 | 31,950,001 |
| Net Construction Assets and Unamortized Bond Issue Cost(2) | <u>125,857,831</u> | <u>154,575,909</u> | <u>126,423,265</u> | <u>145,027,887</u> | <u>129,476,175</u> |
| Less: | <u>5,766,250,815</u> | <u>5,507,248,080</u> | <u>5,126,051,921</u> | <u>4,850,824,048</u> | <u>4,601,892,847</u> |
| Allowance for Depreciation | 1,850,167,360 | 1,724,852,935 | 1,595,494,632 | 1,472,853,683 | 1,354,458,543 |
| Construction Contract Payable | 0 | 279,041 | 1,149,032 | 2,127,799 | 2,222,064 |
| Total | <u>1,850,167,360</u> | <u>1,725,131,976</u> | <u>1,596,643,664</u> | <u>1,474,981,482</u> | <u>1,356,680,607</u> |
| Utility Systems, Net | <u>3,916,083,455</u> | <u>3,782,116,104</u> | <u>3,529,408,257</u> | <u>3,375,842,566</u> | <u>3,245,212,240</u> |
| Revenue Bonds and Other Debt Service (3) | 3,006,436,202 | 2,988,903,972 | 2,932,066,283 | 2,865,320,460 | 2,818,680,622 |
| Less: Bond Retirement and Reserve Funds | <u>147,637,319</u> | <u>170,699,819</u> | <u>161,597,147</u> | <u>160,866,775</u> | <u>169,005,087</u> |
| Net Debt | <u>2,858,798,883</u> | <u>2,818,204,103</u> | <u>2,770,469,136</u> | <u>2,704,453,685</u> | <u>2,649,675,535</u> |
| Equity in Utility's Systems | <u>\$1,057,284,572</u> | <u>\$, 963,912,001</u> | <u>\$, 758,939,121</u> | <u>\$, 671,388,881</u> | <u>\$, 595,536,705</u> |
| Percentage of City's Equity in Utility Systems | 27.00% | 25.49% | 21.50% | 19.89% | 18.35% |

(1) Does not include fuel oil or coal inventories of approximately \$16,664,276 at September 30, 2002. Consists primarily of spare parts inventory at Fayette Plant and South Texas Project.

(2) Includes investment in municipal utility districts of \$1,388,838.

(3) Includes Revenue Bonds and Tax and Revenue Bonds of \$2,587,056,073 (net of discounts and inclusive of premiums); Contract Revenue Bonds of \$22,755,000 (net of discounts); Capital Lease Obligation Bonds of \$16,636,520, Commercial Paper of \$358,351,276 (net of discounts); General Obligation Bonds of \$13,337,512; (net of discounts and inclusive of premiums); and Contractual Obligations of \$8,299,821.

(4) Audited numbers anticipated to be available prior to April 15, 2003.

LITIGATION

A number of claims against the City, as well as certain other matters of litigation are pending with respect to various matters arising in the normal course of the City's operations. The City Attorney and the City Management are of the opinion that resolution of the claims pending will not have a material effect on the City's financial condition or the financial condition of the Electric Utility System and/or the Water and Wastewater System.

Electric Utility System Litigation

On October 15, 1990, the four STP owners: City of Austin, City of San Antonio, Reliant, and CPL jointly filed a lawsuit against Westinghouse Electric Corporation ("Westinghouse") and two of its employees in the District Court of Matagorda County, Texas, 130th Judicial District, Cause of Action No. 90-5-0684A-C. This litigation alleged that Westinghouse knowingly sold the STP owners a nuclear steam supply system containing a steam generator tubing that is susceptible to stress corrosion cracking, that Westinghouse had failed to meet its warranty obligations and that Westinghouse violated the Texas Deceptive Trade Practices Act. A jury trial began in Bay City, Texas in July 1995 and continued until the parties reached a negotiated settlement on December 7, 1995. This settlement, which has been sealed pursuant to an order of the trial court, is viewed by STP owners as providing significant assurances that STP can continue operating economically for many years to come.

On February 22, 1994, the City of Austin filed a lawsuit in State District Court in Harris County, 162nd Judicial District, Cause of Action No. 94-007946, against Houston Lighting and Power (Reliant's predecessor). This lawsuit alleged that Reliant breached its contractual duties to operate, maintain and manage STP and was negligent in operating the plant. The City contended that these operational and management failures resulted in an extended shut down of both STP units beginning in early February 1993 and lasting well into 1994. Trial began on March 6, 1996, and the case went to jury on April 22, 1996. With the jury apparently deadlocked, Austin and Reliant reached a settlement on April 30, 1996. This settlement required Reliant to pay Austin \$20,000,000 plus court costs and replace Reliant as STP Project Manager by a new non-profit operating company.

Austin Energy and Enron Sandhill Limited Partnership have entered into a joint operation agreement (the Sandhill Power Project). Although Enron Sandhill is not in bankruptcy, its guarantor, Enron North America Corporation is currently under Chapter 11 protection. Prior to the bankruptcy filing, Austin Energy issued a notice of default to Enron Sandhill and Enron North America Corporation stating that Enron and the partnership were in anticipatory breach of their obligations under the joint operation agreement because of past due invoices. The letter also stated that Austin Energy would decline any requests to schedule delivery of energy from Sandhill Energy Center until payment of delinquent invoices have been received and authorized written assurances are given that future invoices will be paid in a timely manner. Austin Energy suspended all bilateral transactions with Enron Corporation, its affiliates and related entities in early November 2001 and no additional energy transactions are contemplated with Enron. Austin Energy does not anticipate that the Enron bankruptcy proceedings, in which Austin Energy is listed as an unsecured creditor, will have a material adverse affect on the operation of the Sandhill Energy Center.

A discussion of the litigation regarding the challenge of Reliant and City Public Services Board of San Antonio to the PUCT rules relating to the wholesale transmission service is contained in the rate regulation section.

A number of claims against the City are pending with respect to various matters arising in the normal course of the City's operations. Legal counsel and City management are of the opinion that the settlement of these claims and pending litigation will not have a material adverse effect on the City's financial condition. The City has accrued liabilities in the Liability Reserve Fund for claims payable at September 30, 2002.

APPENDIX B

Form of Opinion of Bond Counsel

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August 28, 2003

**NORTH AUSTIN MUNICIPAL UTILITY DISTRICT NO. 1
CITY OF AUSTIN, TEXAS CONTRACT REVENUE REFUNDING BONDS,
SERIES 2003
IN THE AGGREGATE PRINCIPAL AMOUNT OF \$4,510,000**

AS BOND COUNSEL FOR THE NORTH AUSTIN MUNICIPAL UTILITY DISTRICT NO. 1 (the "District") of the bonds described above (the "Bonds"), we have examined into the legality and validity of the Bonds, which bear interest from the dates specified in the text of the Bonds, until maturity or redemption, at the rates and payable on the dates specified in the text of the Bonds all in accordance with the order of the Board of Directors of the District adopted on May 21, 2003, authorizing the issuance of the Bonds (the "Order").

WE HAVE EXAMINED the Constitution and laws of the State of Texas, certified copies of the proceedings of the District, and other documents authorizing and relating to the issuance of said Bonds, including one of the executed Bonds (Bond Numbered T-1) and specimens of Bonds to be authenticated and delivered in exchange for the Bonds.

BASED ON SAID EXAMINATION, IT IS OUR OPINION THAT the Bonds have been authorized and issued and the Bonds delivered concurrently with this opinion have been duly delivered, and that, assuming due authentication, Bonds issued in exchange therefor will have been duly delivered, in accordance with law, and that said Bonds, except as may be limited by laws applicable to the District relating to bankruptcy, reorganization and other similar matters affecting creditors' rights, constitute valid and legally binding obligations of the District, payable, together with the District's outstanding City of Austin, Texas Contract Revenue Refunding Bonds, Series 1994 from and secured by a first lien on and pledge of City Contract Payments to be made by the City of Austin, Texas pursuant to a Utility Construction Contract, as amended between the District and the City. Such City Contract Payments are to be made in amounts sufficient to pay principal of, premium, if any, and interest on the Bonds.

THE DISTRICT reserves the right to issue additional bonds which will be payable from City Contract Payments on a parity with the Bonds.

IT IS FURTHER OUR OPINION, except as discussed below, that the interest on the Bonds is excludable from the gross income of the owners thereof for federal income tax purposes under the statutes, regulations, published rulings, and court decisions existing on the date of this opinion. We are further of the opinion that the Bonds are not "private activity bonds" and that accordingly, interest on the Bonds will not be included as an individual or corporate alternative minimum tax preference item under Section 57(a)(5) of the Internal Revenue Code of 1986 (the "Code"). In expressing the aforementioned opinions, we have relied on the verification report of Grant Thornton LLP, and assume compliance by the District with, certain representations and covenants regarding the use and investment of the proceeds of the Bonds. We call your attention to the fact that failure by the District to comply with such representations and covenants may cause the interest on the Bonds to become includable in gross income retroactively to the date of issuance of the Bonds.

WE CALL YOUR ATTENTION TO THE FACT that the interest on tax-exempt obligations, such as the Bonds, is (a) included in a corporation's alternative minimum taxable income for purposes of determining the alternative minimum tax and the environmental tax imposed on corporations by Sections 55 and 59A of the Code, (b) subject to the branch profits tax imposed on foreign corporations by Section 884 of the Code and (c) included in the passive investment income of the subchapter S corporation and subject to the tax imposed by Section 1375 of the Code.

OUR OPINIONS ARE BASED on existing law, which is subject to change. Such opinions are further based on our knowledge of facts as of the date hereof. We assume no duty to update or supplement our opinions to reflect any facts or circumstances that may thereafter come to our attention or to reflect any changes in any law that may thereafter occur or become effective. Moreover, our opinions are not a guarantee of result and are not binding on the Internal Revenue Service (the "Service"); rather, such opinions represent our legal judgment based upon our review of existing law and in reliance upon the representations and covenants referenced above that we deem relevant to such opinions. The Service has an ongoing audit program to determine compliance with rules that relate to whether interest on state or local obligations is includable in gross income for federal income tax purposes. No assurance can be given whether or not the Service will commence an audit of the Bonds. If an audit is commenced, in accordance with its current published procedures the Service is likely to treat the District as the taxpayer. We observe that the District has covenanted not to take any action, or omit to take any action within its control, that if taken or omitted, respectively, may result in the treatment of interest on the Bonds as includable in gross income for federal income tax purposes.

EXCEPT AS STATED ABOVE, we express no opinion as to any other federal, state, or local tax consequences of acquiring, carrying, owning or disposing of the Bonds.

WE EXPRESS NO OPINION as to any insurance policies issued with respect to the payments due for the principal of and interest on the Bonds, nor as to any such insurance policies issued in the future.

OUR SOLE ENGAGEMENT in connection with the issuance of the Bonds is as Bond Counsel for the District, and, in that capacity, we have been engaged by the District for the sole

purpose of rendering an opinion with respect to the legality and validity of the Bonds under the Constitution and laws of the State of Texas, and with respect to the exclusion from gross income of the interest on the Bonds for federal income tax purposes, and for no other reason or purpose. The foregoing opinions represent our legal judgment based upon a review of existing legal authorities that we deem relevant to render such opinions and are not a guarantee of a result. We have not been requested to investigate or verify, and have not independently investigated or verified any records, data, or other material relating to the financial condition or capabilities of the District, or the disclosure thereof in connection with the sale of the Bonds, and have not assumed any responsibility with respect thereto. We express no opinion and make no comment with respect to the marketability of the Bonds and have relied solely on certificates executed by officials of the District regarding the revenues to support payment of the Bonds. Our role in connection with the District's Official Statement prepared for use in connection with the sale of the Bonds has been limited as described therein.

WE HAVE ACTED AS BOND COUNSEL for the District for the sole purpose of rendering an opinion with respect to the legality and validity of the Bonds described above under the Constitution and laws of the State of Texas, and with respect to the exclusion from gross income of the interest on such Bonds for federal income tax purposes, and for no other reason or purpose. We have not been requested to investigate or verify, and have not investigated or verified, any records, data, or other material relating to the financial condition or capabilities of the District, and have not assumed any responsibility with respect thereto.

THE FOREGOING OPINIONS represent our legal judgment based upon a review of existing legal authorities that we deem relevant to render such opinions and are not a guarantee of a result.

Respectfully,

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