

MUSCATINE POWER AND WATER

A Component Unit of the City of Muscatine, Iowa

FINANCIAL STATEMENTS

December 31, 2011 and 2010

MUSCATINE POWER AND WATER

A Component Unit of the City of Muscatine, Iowa

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INDEPENDENT AUDITORS' REPORT

To the Board of Water, Electric, and Communications Trustees
Muscatine Power and Water
Muscatine, Iowa

We have audited the accompanying statements of net assets and the related statements of revenues, expenses and changes in net assets (deficit) and cash flows of Muscatine Power and Water (utility), a component unit of the City of Muscatine, Iowa, as identified in the accompanying table of contents, as of and for the years ended December 31, 2011 and 2010. These financial statements are the responsibility of management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the financial statements referred to in the first paragraph present fairly, in all material respects, the financial position of the utility as of December 31, 2011 and 2010, and the changes in its financial position and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated March 22, 2012 on our consideration of Muscatine Power and Water's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, grant agreements, and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audits.

To the Board of Water, Electric, and Communications Trustees
Muscatine Power and Water

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis and Schedules of Funding Progress information as listed in the table of contents be presented to supplement the financial statements. Management's discussion and analysis does not include a discussion of changes in financial position between 2009 and 2010. Such information, although not a part of the financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the financial statements in an appropriate operational, economical, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the financial statements, and other knowledge we obtained during our audit of the financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Our audits were conducted for the purpose of forming opinions on the financial statements taken as a whole. The supplemental information as identified in the table of contents is presented for purposes of additional analysis and is not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements taken as a whole.

Baker Tilly Virchow Krause, LLP

Madison, Wisconsin
March 22, 2012

MANAGEMENT'S DISCUSSION AND ANALYSIS
MUSCATINE POWER AND WATER

MUSCATINE POWER AND WATER

MANAGEMENT'S DISCUSSION AND ANALYSIS

December 31, 2011 and 2010

(Unaudited)

We are providing this discussion to you, the reader of our financial statements, to explain the activities, plans and events which impacted our financial position during 2011 and 2010. This overview from management should provide the reader with information that is one of the three components of the entire financial statement. The other two components audited by Baker Tilly Virchow Krause, LLP, Muscatine Power and Water's (MP&W's) auditors, are the financial statements and notes to the financial statements. Please read the entire document to understand the events and conditions impacting MP&W.

OVERVIEW OF THE FINANCIAL STATEMENTS

The Statements of Revenues, Expenses and Changes in Net Assets report all revenues and expenses for the year. The Statements of Net Assets include all assets and liabilities, and indicate those that are restricted by the Board of Water, Electric, and Communications Trustees (Board). The Statements of Cash Flows report the cash from operating activities, as well as cash from noncapital financing activities, investing activities, and capital and related financing activities.

Condensed Statements of Net Assets

<i>In thousands \$</i>	<u>2011</u>	<u>2010</u>
Current Assets		
Unrestricted	\$ 37,131	\$ 38,249
Restricted	11,111	38,036
Total Current Assets	<u>48,242</u>	<u>76,285</u>
Non-Current Assets		
Capital Assets	131,660	140,389
Other Assets	36,233	37,058
Total Non-Current Assets	<u>167,893</u>	<u>177,447</u>
Total Assets	<u>\$ 216,135</u>	<u>\$ 253,732</u>
Current Liabilities	\$ 8,518	\$ 22,582
Non-Current Liabilities	43,495	57,913
Deferred Revenue	10,350	17,155
Total Liabilities and Deferred Revenue	<u>62,363</u>	<u>97,650</u>
Net Assets		
Invested in capital and intangible assets, net of related debt	125,470	109,080
Restricted	10,998	37,297
Unrestricted	17,304	9,705
Total Net Assets	<u>153,772</u>	<u>156,082</u>
Total Liabilities, Deferred Revenue, and Net Assets	<u>\$ 216,135</u>	<u>\$ 253,732</u>

Over time, the difference between the assets and liabilities may indicate a change in the financial picture for MP&W, but the financial statements must be viewed from the perspective of the entire document.

MUSCATINE POWER AND WATER

MANAGEMENT'S DISCUSSION AND ANALYSIS December 31, 2011 and 2010 (Unaudited)

OVERVIEW OF THE FINANCIAL STATEMENTS (CONT.)

Condensed Statements of Revenues, Expenses and Changes in Net Assets

<i>In thousands \$</i>	2011	2010
Operating Revenues	\$ 106,268	\$ 111,595
Operating Expenses	(107,866)	(110,686)
Operating Income (Loss)	<u>(1,598)</u>	<u>909</u>
Non-operating Revenues	1,463	1,455
Non-operating Expenses	(2,250)	(2,806)
Net Non-operating Expenses	<u>(787)</u>	<u>(1,351)</u>
Net Loss before Capital Contributions	(2,385)	(442)
Capital Contributions	<u>75</u>	<u>172</u>
Change in Net Assets	(2,310)	(270)
Net Assets – Beginning of Year	<u>156,082</u>	<u>156,352</u>
Net Assets – End of Year	<u><u>\$ 153,772</u></u>	<u><u>\$ 156,082</u></u>

Condensed Statements of Cash Flows

<i>In thousands \$</i>	2011	2010
Cash Flows from Operating Activities	\$ 5,008	\$ 16,770
Cash Flows from Non-Capital Financing Activities	1,870	624
Cash Flows from Capital and Related Financing Activities	(34,577)	(14,477)
Cash Flows from Investing Activities	<u>16,530</u>	<u>8,308</u>
Net Change in Cash and Cash Equivalents	(11,169)	11,225
Cash and Cash Equivalents – Beginning of Year	<u>22,861</u>	<u>11,636</u>
Cash and Cash Equivalents – End of Year	<u><u>\$ 11,692</u></u>	<u><u>\$ 22,861</u></u>

MUSCATINE POWER AND WATER

MANAGEMENT'S DISCUSSION AND ANALYSIS December 31, 2011 and 2010 (Unaudited)

UTILITY FINANCIAL ANALYSIS

ELECTRIC UTILITY

In 2011, the Electric Utility became debt-free, making its final principal and interest payment on nearly \$800 million of debt that arose from construction of Unit #9 (completed in 1983), refinancings, and various capital projects financed with long-term debt over the years. MP&W's unenhanced electric revenue bond rating was last indicated as "A+" by Standard & Poor's and Fitch Ratings.

The electric utility experienced significantly lower wholesale electric sales in 2011 due to a soft market and the planned extended maintenance outage of the Unit #9 turbine/generator.

Overall rate adjustments of 5.0%, effective August 1, 2011, and 4.0%, effective July 1, 2010, were in response to the depressed wholesale energy market and higher delivered coal costs.

Statements of Net Assets

<i>In thousands \$</i>	2011	2010
Current Assets		
Unrestricted	\$ 29,238	\$ 29,813
Restricted	10,113	38,008
Total Current Assets	<u>39,351</u>	<u>67,821</u>
Non-Current Assets		
Capital Assets	105,652	113,512
Other Assets	35,450	35,490
Total Non-Current Assets	<u>141,102</u>	<u>149,002</u>
Total Assets	<u>\$ 180,453</u>	<u>\$ 216,823</u>
Current Liabilities	\$ 6,032	\$ 20,577
Non-Current Liabilities	2,011	15,249
Deferred Revenue	10,033	17,155
Total Liabilities and Deferred Revenue	<u>18,076</u>	<u>52,981</u>
Net Assets		
Invested in capital, net of related debt	105,652	87,683
Restricted	10,113	37,297
Unrestricted	46,612	38,862
Total Net Assets	<u>162,377</u>	<u>163,842</u>
Total Liabilities, Deferred Revenue, and Net Assets	<u>\$ 180,453</u>	<u>\$ 216,823</u>

2011 Compared to 2010

- Total assets decreased \$36.4 million primarily due to:
 - final bond principal and interest payments of \$27.3 million in 2011;
 - net utility plant decreasing \$7.9 million due to depreciation and retirements exceeding capital expenditures;
 - decrease of \$2.2 million due to the hedge asset termination;
 - decrease in customer accounts receivable of \$2.2 million; offset by an increase in coal inventory of \$4.5 million expected to be burned down in future years.

MUSCATINE POWER AND WATER

MANAGEMENT'S DISCUSSION AND ANALYSIS

December 31, 2011 and 2010

(Unaudited)

UTILITY FINANCIAL ANALYSIS (CONT.)

ELECTRIC UTILITY (CONT.)

- Current liabilities decreased \$14.5 million primarily due to:
 - \$13.3 million reduction in current portion of debt and accrued interest payable;
 - \$2.2 million decrease due to the hedge liability expiring; and
 - trade accounts payable increasing \$1.2 million primarily due to rail car repairs billed at year end.
- Non-current liabilities decreased by \$13.2 million primarily due to debt payment.
- Deferred revenue decreased due to a draw down on the Extraordinary Operation & Maintenance Account of \$7.1 million for:
 - Unit #9 generator's extended maintenance outage; and
 - to offset reduced wholesale sales due to the outage.

Additional information on changes in utility plant and long-term obligations are provided in notes 3 and 5, respectively.

Statements of Revenues, Expenses and Changes in Net Assets

<i>In thousands \$</i>	2011	2010
Operating Revenues	\$ 90,334	\$ 96,440
Operating Expenses	(92,367)	(95,429)
Operating Income	(2,033)	1,011
Non-operating Revenues	1,316	1,444
Non-operating Expenses	(760)	(1,491)
Net Non-operating Expenses	556	(47)
Net Income before Capital Contributions	(1,477)	964
Capital Contributions	12	79
Change in Net Assets	(1,465)	1,043
Net Assets – Beginning of Year	163,842	162,799
Net Assets – End of Year	\$ 162,377	\$ 163,842

2011 Compared to 2010

- Operating revenues decreased \$6.1 million or 6.3%.
 - Retail sales were \$1.5 million higher due to the impact of a 5.0% rate increase on August 1, 2011 offset by 0.4% lower kWh usage.
 - Wholesale electric sales decreased \$12.9 million due to a soft market with 8.4% lower prices and a 25.4% decrease in kWh sales, which was partially due to the extended Unit #9 maintenance outage.
 - Steam sales with MP&W's largest industrial customer, Grain Processing Corporation (GPC), decreased by \$1.3 million or 11.7% due to lower pass-through costs for emissions allowances.

MUSCATINE POWER AND WATER

MANAGEMENT'S DISCUSSION AND ANALYSIS December 31, 2011 and 2010 (Unaudited)

UTILITY FINANCIAL ANALYSIS (CONT.)

ELECTRIC UTILITY (CONT.)

- Utilization of previously deferred revenue was \$7.1 million in 2011 compared to \$748,000 in 2010.
- Operating expenses decreased \$3.1 million or 3.2%.
 - \$722,000 lower production fuel costs, resulted from a 20% increase in cost of coal burned per ton offset by lower net generation of 25.4%;
 - Net generation was down due to the Unit #9 maintenance outage and the soft wholesale market.
 - \$2.6 million lower purchased power costs due to a 9.6% lower price.
 - Emissions allowances due to the GPC steam sales contract were \$360,000 lower.
 - Maintenance expenses increased \$4.1 million primarily due to a planned, extended maintenance outage of Unit #9 turbine/generator.
 - Depreciation expense decreased by \$3.2 million due to updating the estimated useful lives of the generation plant assets.

Statements of Cash Flows

<i>In thousands \$</i>	2011	2010
Cash Flows from Operating Activities	\$ 531	\$ 13,386
Cash Flows from Non-Capital Financing Activities	1,871	624
Cash Flows from Capital and Related Financing Activities	(30,346)	(15,215)
Cash Flows from Investing Activities	<u>15,528</u>	<u>12,477</u>
Net Change in Cash and Cash Equivalents	(12,416)	11,272
Cash and Cash Equivalents – Beginning of Year	<u>21,616</u>	<u>10,344</u>
Cash and Cash Equivalents – End of Year	<u>\$ 9,200</u>	<u>\$ 21,616</u>

2011 Compared to 2010

- Cash flows from operations decreased by \$12.9 million due to:
 - Unit #9's planned extended maintenance outage;
 - lower wholesale electric sales; and
 - higher coal and coal transportation costs; offset by
 - higher retail sales.
- Non-capital financing activities are comprised of interest on the note receivable from the communications utility.
 - Three six-month interest payments were made in 2011; one six-month payment was made in 2010.

MUSCATINE POWER AND WATER

MANAGEMENT'S DISCUSSION AND ANALYSIS December 31, 2011 and 2010 (Unaudited)

UTILITY FINANCIAL ANALYSIS (CONT.)

ELECTRIC UTILITY (CONT.)

- Cash flows from capital and related financing activities include:
 - Capital expenditures of \$3.1 million in 2011 and \$1.6 million in 2010; and
 - bond principal and interest payments of \$27.3 million in 2011 and \$13.7 million in 2010.
- Cash flows from investing activities include:
 - Investment maturities in 2011 and 2010 used to partially fund operations, capital expenditures as well as bond principal and interest payments due to lower cash generated from operating activities.

WATER UTILITY

The Board approved water rate increases of 4.0%, effective April 1, 2011, and 3.0%, effective April 1, 2010, in response to an increase in capital requirements necessary to provide for fire protection, community growth, and higher operation and maintenance costs.

MP&W's industrial customers account for approximately 49% of water sales.

Draw downs on the loan from Iowa Finance Authority were complete in 2011, bringing the total amount borrowed to \$306,000, net of the \$93,000 forgivable portion, with an outstanding balance of \$274,000 at the end of 2011. The interest rate on the loan is 3.0%, plus a 0.25% servicing fee, with a 10-year repayment term.

Statements of Net Assets

<i>In thousands \$</i>	2011	2010
Current Unrestricted Assets	\$ 1,391	\$ 1,218
Capital Assets	14,968	14,921
Total Assets	\$ 16,359	\$ 16,139
Current Liabilities	\$ 652	\$ 437
Non-Current Liabilities	2,027	2,311
Total Liabilities	2,679	2,748
Net Assets		
Invested in capital, net of related debt	12,786	12,668
Unrestricted	894	723
Total Net Assets	13,680	13,391
Total Liabilities and Net Assets	\$ 16,359	\$ 16,139

2011 Compared to 2010

- Total assets increased \$220,000 or 1.4%.
 - Current unrestricted assets increased by \$173,000 primarily due to higher cash and investment balances.
 - Capital assets increased \$47,000, net of retirements, due to normal capital spending for utility construction and acquisition projects.

MUSCATINE POWER AND WATER

MANAGEMENT'S DISCUSSION AND ANALYSIS December 31, 2011 and 2010 (Unaudited)

UTILITY FINANCIAL ANALYSIS (CONT.)

WATER UTILITY (CONT.)

- Current liabilities increased by \$215,000 primarily due to the current portion of customer advances for construction increasing by \$209,000.
- Non-current liabilities decreased by \$284,000 primarily due to the reclassification to current liabilities plus no new advances for construction granted.

Additional information on changes in utility plant and long-term obligations are provided in notes 3 and 5, respectively.

Statements of Revenues, Expenses and Changes in Net Assets

<i>In thousands \$</i>	2011	2010
Operating Revenues	\$ 4,459	\$ 4,235
Operating Expenses	(4,209)	(4,013)
Operating Income	<u>250</u>	<u>222</u>
Non-operating Revenues	-	1
Non-operating Expenses	(9)	(13)
Net Non-operating Expenses	<u>(9)</u>	<u>(12)</u>
Net Income before Capital Contributions	241	210
Capital Contributions	<u>48</u>	<u>92</u>
Change in Net Assets	289	302
Net Assets – Beginning of Year	<u>13,391</u>	<u>13,089</u>
Net Assets – End of Year	<u>\$ 13,680</u>	<u>\$ 13,391</u>

2011 Compared to 2010

- Operating revenues increased \$224,000 or 5.3%.
 - Total water sales revenue was higher by \$221,000 primarily due to a 4% rate adjustment effective April 1, 2011.
 - Overall, gallons sold increased by 1.3% in 2011. Gallons of water sold were higher for industrial, residential and commercial classes, but were lower for the power plant due to the generating units running less and energy conservation efforts.
- Operating expense increased \$196,000 or 4.9% primarily due to:
 - \$86,000 higher main repair cost; and
 - \$100,000 for a water system infrastructure assessment.
- 2011 capital contributions reflect developer-financed water main construction projects. The 2010 capital contribution is the forgivable portion of the Iowa Finance Authority loan.

MUSCATINE POWER AND WATER

MANAGEMENT'S DISCUSSION AND ANALYSIS December 31, 2011 and 2010 (Unaudited)

UTILITY FINANCIAL ANALYSIS (CONT.)

WATER UTILITY (CONT.)

Statement of Cash Flows

<u>In thousands \$</u>	<u>2011</u>	<u>2010</u>
Cash Flows from Operating Activities	\$ 795	\$ 678
Cash Flows from Capital and Related Financing Activities	(617)	(714)
Cash Flows from Investing Activities	-	253
Net Change in Cash and Cash Equivalents	178	217
Cash and Cash Equivalents – Beginning of Year	422	205
Cash and Cash Equivalents – End of Year	<u>\$ 600</u>	<u>\$ 422</u>

2011 Compared to 2010

- Cash flows from operating activities increased \$117,000 or 17.3% due to:
 - a 4% rate adjustment, effective April 1, 2011;
 - 1.3% higher gallons sold;
 - \$38,000 lower pumping power cost;
 - \$37,000 lower chemical expense; offset by
 - \$86,000 higher cost of main repairs; and \$100,000 for a water system infrastructure assessment.
- Cash flows from capital and related financing activities include:
 - capital expenditures of \$617,000 in 2011 and \$1,059,000 in 2010;
 - loan proceeds of \$41,000 and \$350,000 in 2011 and 2010, respectively; and
 - principal and interest payments of \$41,000 in 2011 and \$5,000 in 2010.
- Cash flows from investing activities
 - Proceeds from investment maturities were used to partially fund capital additions in 2010.

MUSCATINE POWER AND WATER

MANAGEMENT'S DISCUSSION AND ANALYSIS December 31, 2011 and 2010 (Unaudited)

UTILITY FINANCIAL ANALYSIS (CONT.)

COMMUNICATIONS UTILITY

Rate adjustments for the communications utility were approved by the Board for both 2011 and 2010. MPW Basic service and MPW Digital TV Select service rates increased by 5.0% and 5.5%, respectively, effective January 1, 2011. Effective January 1, 2010, MPW Digital TV Basic and Select cable service charges increased approximately 5.0%. These increases were primarily due to continued rising programming costs, debt service requirements, and other general inflationary factors.

The digital transition project which began in 2008 was essentially completed by the end of 2011. The project benefits customers by providing bandwidth capacity for the addition of more standard digital and HD programming as well as enhanced Internet speeds, among other features. The cost of the conversion was estimated at \$5.6 million; however, the actual amount spent was approximately \$4.2 million at the end of 2011. A loan of \$4.8 million with three local banks was utilized to finance this project at an annual interest rate of 4.7%. Semi-annual interest payments began July 1, 2009 with principal repayment beginning January 1, 2012.

Statements of Net Assets (Deficit)

<i>In thousands \$</i>	2011	2010
Current Assets		
Unrestricted	\$ 6,503	\$ 7,218
Restricted	998	28
Total Current Assets	<u>7,501</u>	<u>7,246</u>
Non-Current Assets		
Capital Assets	11,040	11,956
Other Assets	782	1,568
Total Non-Current Assets	<u>11,822</u>	<u>13,524</u>
Total Assets	<u>\$ 19,323</u>	<u>\$ 20,770</u>
Current Liabilities	\$ 1,835	\$ 1,568
Non-Current Liabilities	39,457	40,354
Deferred Revenue	317	-
Total Liabilities and Deferred Revenue	<u>41,609</u>	<u>41,922</u>
Net Deficit		
Invested in capital, net of related debt	7,031	8,729
Restricted	885	-
Unrestricted	(30,202)	(29,881)
Total Net Deficit	<u>(22,286)</u>	<u>(21,152)</u>
Total Liabilities, Deferred Revenue, and Net Deficit	<u>\$ 19,323</u>	<u>\$ 20,770</u>

2011 Compared to 2010

- Total assets decreased \$1.4 million or 7.0% due to:
 - depreciation and retirements exceeding capital expenditures, resulting in a reduction in capital assets of \$916,000 or 7.7%;

MUSCATINE POWER AND WATER

MANAGEMENT'S DISCUSSION AND ANALYSIS December 31, 2011 and 2010 (Unaudited)

UTILITY FINANCIAL ANALYSIS (CONT.)

COMMUNICATIONS UTILITY (CONT.)

- other assets, primarily the intangible asset described in note 14, decreasing \$786,000; offset by
- \$118,000 higher cash and investment balances; and
- \$166,000 higher receivable balances resulting from higher December 2011 retail sales and higher interest receivable from investments.
- Current liabilities increased \$267,000 due to:
 - recognition of \$885,000 of the current portion of notes payable to bank; and
 - \$624,000 decrease in interest due on the electric utility loan.
- Noncurrent liabilities decreased \$580,000 due to:
 - a reclassification to current liabilities of \$885,000 of the current portion of notes payable to bank; and
 - a 20-year contract to lease dark fiber to Iowa Health System resulting in \$317,000 in deferred revenue.

Additional information on changes in utility plant and long-term obligations are provided in notes 3 and 5, respectively.

Statements of Revenues, Expenses and Changes in Net Deficit

<i>In thousands \$</i>	2011	2010
Operating Revenues	\$ 11,476	\$ 10,920
Operating Expenses	(11,290)	(11,244)
Operating Income	186	(324)
Non-operating Revenues	147	9
Non-operating Expenses	(1,482)	(1,301)
Net Non-operating Expenses	(1,335)	(1,292)
Net Loss before Capital Contributions	(1,149)	(1,616)
Capital Contributions	15	-
Change in Net Deficit	(1,134)	(1,616)
Net Deficit – Beginning of Year	(21,152)	(19,536)
Net Deficit – End of Year	\$ (22,286)	\$ (21,152)

2011 Compared to 2010

- Operating revenues increased \$556,000 or 5.1%.
 - CATV operating revenues, excluding advertising sales, increased by \$304,000 or 4.4% due to:
 - cable television rate adjustments of 5.0% for Basic and 5.5% for the Select services; offset by
 - a decrease in the total number of CATV subscribers (7,360 at the end of 2011 vs. 7,572 at the end of 2010).

MUSCATINE POWER AND WATER

MANAGEMENT'S DISCUSSION AND ANALYSIS December 31, 2011 and 2010 (Unaudited)

UTILITY FINANCIAL ANALYSIS (CONT.)

COMMUNICATIONS UTILITY (CONT.)

- an increase in the number of data/internet subscribers (6,843 at the end of 2011 vs. 6,690 at the end of 2010) resulting in an increase of internet revenues of \$179,000 or 5.5%.
- an increase in the number of MME/MAN subscribers (31 at the end of 2011 vs. 17 at the end of 2010) resulting in increased revenues of \$48,000 or 14.2%.
- Operating expenses increased overall by \$46,000 or 0.4%.
 - Operations expense decreased by \$48,000, primarily due to lower data/Internet access charges, customer service expenses and administrative and general salaries, offset by higher CATV programming costs.
 - Depreciation expense increased by \$90,000 due to the large number of CATV digital converters and headend equipment purchases in 2010 incurred for the digital conversion transition project.

Statements of Cash Flows

<i>In thousands \$</i>	2011	2010
Cash Flows from Operating Activities	\$ 3,681	\$ 2,705
Cash Flows from Capital and Related Financing Activities	(3,614)	1,452
Cash Flows from Investing Activities	1,002	(4,422)
Net Change in Cash and Cash Equivalents	1,069	(265)
Cash and Cash Equivalents – Beginning of Year	823	1,088
Cash and Cash Equivalents – End of Year	\$ 1,892	\$ 823

2011 Compared to 2010

- Cash flows from operating activities have increased in 2011 primarily due to the CATV rate adjustments and growth in Internet subscribers.
- Capital and related financing activities include:
 - capital expenditures in 2011 and 2010 totaling \$1.6 million and \$1.8 million, respectively;
 - loan proceeds in 2010 of \$3.9 million; and
 - interest paid on notes payable of \$2.0 million in 2011 and \$665,000 in 2010.
- Cash flows from investing activities include:
 - Proceeds of \$1.0 million in investment maturities used to partially fund capital additions in 2011; and
 - Investment of \$3.9 million in debt proceeds in 2010.

MUSCATINE POWER AND WATER

MANAGEMENT'S DISCUSSION AND ANALYSIS

December 31, 2011 and 2010

(Unaudited)

CONTACTING UTILITY MANAGEMENT

This financial report is designed to provide a general overview of MP&W's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the Director, Finance & Administrative Services, at 3205 Cedar Street, Muscatine, Iowa 52761.

MUSCATINE POWER AND WATER

STATEMENTS OF NET ASSETS
December 31, 2011 and 2010

	ELECTRIC UTILITY		WATER UTILITY		COMMUNICATIONS UTILITY		TOTALS	
	2011	2010	2011	2010	2011	2010	2011	2010
ASSETS								
CURRENT ASSETS								
Unrestricted Assets								
Cash	\$ 3,012	\$ 5,108	\$ 600,151	\$ 422,229	\$ 894,530	\$ 794,865	\$ 1,497,693	\$ 1,222,202
Investments	-	-	-	-	3,960,251	4,912,000	3,960,251	4,912,000
Receivables:								
Customer accounts	6,372,787	8,627,628	478,183	482,781	1,171,334	1,102,347	8,022,304	10,212,756
Interest	3,996	668,380	5	5	103,828	6,685	107,829	675,070
Inventories:								
Fuel	15,618,770	11,118,587	-	-	-	-	15,618,770	11,118,587
Emission allowances	178,369	209,739	-	-	-	-	178,369	209,739
Materials and supplies	6,562,755	6,450,081	285,362	289,486	310,874	284,994	7,158,991	7,024,561
Prepaid and deferred expenses	497,771	537,516	27,003	23,351	62,172	117,057	586,946	677,924
Hedge asset	-	2,196,100	-	-	-	-	-	2,196,100
Total Unrestricted Assets	<u>29,237,460</u>	<u>29,813,139</u>	<u>1,390,704</u>	<u>1,217,852</u>	<u>6,502,989</u>	<u>7,217,948</u>	<u>37,131,153</u>	<u>38,248,939</u>
Restricted Assets								
Cash	9,196,715	21,610,535	-	-	997,802	28,019	10,194,517	21,638,554
Investments	<u>916,621</u>	<u>16,397,650</u>	-	-	-	-	<u>916,621</u>	<u>16,397,650</u>
Total Restricted Assets	<u>10,113,336</u>	<u>38,008,185</u>	<u>-</u>	<u>-</u>	<u>997,802</u>	<u>28,019</u>	<u>11,111,138</u>	<u>38,036,204</u>
Total Current Assets	<u>39,350,796</u>	<u>67,821,324</u>	<u>1,390,704</u>	<u>1,217,852</u>	<u>7,500,791</u>	<u>7,245,967</u>	<u>48,242,291</u>	<u>76,285,143</u>
NON-CURRENT ASSETS								
Capital Assets								
Utility plant in service	406,637,670	404,829,179	24,022,226	23,497,236	30,529,966	29,035,507	461,189,862	457,361,922
Construction work in progress	339,892	242,626	3,170	47,281	5,995	70,300	349,057	360,207
Less: accumulated depreciation	<u>(301,325,190)</u>	<u>(291,559,776)</u>	<u>(9,057,117)</u>	<u>(8,623,443)</u>	<u>(19,496,154)</u>	<u>(17,149,844)</u>	<u>(329,878,461)</u>	<u>(317,333,063)</u>
Total Capital Assets	<u>105,652,372</u>	<u>113,512,029</u>	<u>14,968,279</u>	<u>14,921,074</u>	<u>11,039,807</u>	<u>11,955,963</u>	<u>131,660,458</u>	<u>140,389,066</u>
Other Assets								
Unamortized debt issuance costs	-	-	-	-	9,370	21,906	9,370	21,906
Note receivable from communications utility	35,327,000	35,327,000	-	-	-	-	35,327,000	35,327,000
Joint venture rights	123,220	162,532	-	-	-	-	123,220	162,532
Intangible assets, net of accumulated amortization								
2011 - \$6,957,776; 2010 - \$6,184,639	-	-	-	-	773,136	1,546,273	773,136	1,546,273
Total Other Assets	<u>35,450,220</u>	<u>35,489,532</u>	<u>-</u>	<u>-</u>	<u>782,506</u>	<u>1,568,179</u>	<u>36,232,726</u>	<u>37,057,711</u>
Total Non-Current Assets	<u>141,102,592</u>	<u>149,001,561</u>	<u>14,968,279</u>	<u>14,921,074</u>	<u>11,822,313</u>	<u>13,524,142</u>	<u>167,893,184</u>	<u>177,446,777</u>
TOTAL ASSETS	<u>\$ 180,453,388</u>	<u>\$ 216,822,885</u>	<u>\$ 16,358,983</u>	<u>\$ 16,138,926</u>	<u>\$ 19,323,104</u>	<u>\$ 20,770,109</u>	<u>\$ 216,135,475</u>	<u>\$ 253,731,920</u>

See accompanying notes to financial statements.

	ELECTRIC UTILITY		WATER UTILITY		COMMUNICATIONS UTILITY		TOTALS	
<i>LIABILITIES, DEFERRED REVENUE, AND NET ASSETS (DEFICIT)</i>	2011	2010	2011	2010	2011	2010	2011	2010
CURRENT LIABILITIES								
Payable From Unrestricted Assets								
Trade accounts payable	\$ 2,719,645	\$ 1,479,372	\$ 170,177	\$ 158,143	\$ 487,137	\$ 564,107	\$ 3,376,959	\$ 2,201,622
Customer advances for construction	-	-	287,157	77,811	-	-	287,157	77,811
Accrued interest payable	-	-	-	-	-	623,521	-	623,521
Accrued expenses	2,720,944	3,007,785	166,443	167,872	332,746	352,418	3,220,133	3,528,075
Deferred revenue	-	-	-	-	16,991	-	16,991	-
Customer deposits	591,265	597,792	-	-	-	-	591,265	597,792
Hedge liability	-	2,196,100	-	-	-	-	-	2,196,100
Total Payable From Unrestricted Assets	<u>6,031,854</u>	<u>7,281,049</u>	<u>623,777</u>	<u>403,826</u>	<u>836,874</u>	<u>1,540,046</u>	<u>7,492,505</u>	<u>9,224,921</u>
Payable From Restricted Assets								
Current portion of long-term debt	-	12,585,000	27,000	32,000	885,000	-	912,000	12,617,000
Accrued interest payable	-	711,013	1,193	1,192	112,800	28,019	113,993	740,224
Total Payable From Restricted Assets	<u>-</u>	<u>13,296,013</u>	<u>28,193</u>	<u>33,192</u>	<u>997,800</u>	<u>28,019</u>	<u>1,025,993</u>	<u>13,357,224</u>
Total Current Liabilities	<u>6,031,854</u>	<u>20,577,062</u>	<u>651,970</u>	<u>437,018</u>	<u>1,834,674</u>	<u>1,568,065</u>	<u>8,518,498</u>	<u>22,582,145</u>
NON-CURRENT LIABILITIES AND DEFERRED REVENUE								
Long term debt, net of current portion	-	13,271,301	247,000	233,096	-	-	247,000	13,504,397
Notes payable to banks	-	-	-	-	3,915,000	4,800,000	3,915,000	4,800,000
Note payable to electric utility	-	-	-	-	35,327,000	35,327,000	35,327,000	35,327,000
Deferred revenue	10,032,866	17,155,162	-	-	317,488	-	10,350,354	17,155,162
Post-employment health benefit provision	139,991	118,166	13,930	11,756	24,673	20,799	178,594	150,721
Health & dental care provision	1,871,417	1,858,882	144,731	155,346	189,979	205,987	2,206,127	2,220,215
Customer advances for construction	-	-	1,621,299	1,910,502	-	-	1,621,299	1,910,502
Total Non-Current Liabilities and Deferred Revenue	<u>12,044,274</u>	<u>32,403,511</u>	<u>2,026,960</u>	<u>2,310,700</u>	<u>39,774,140</u>	<u>40,353,786</u>	<u>53,845,374</u>	<u>75,067,997</u>
NET ASSETS (DEFICIT)								
Invested in capital and intangible assets, net of related debt	105,652,372	87,683,011	12,785,823	12,667,665	7,031,319	8,729,618	125,469,514	109,080,294
Restricted	10,113,336	37,297,172	-	-	885,002	-	10,998,338	37,297,172
Unrestricted	<u>46,611,552</u>	<u>38,862,129</u>	<u>894,230</u>	<u>723,543</u>	<u>(30,202,031)</u>	<u>(29,881,360)</u>	<u>17,303,751</u>	<u>9,704,312</u>
Total Net Assets (Deficit)	<u>162,377,260</u>	<u>163,842,312</u>	<u>13,680,053</u>	<u>13,391,208</u>	<u>(22,285,710)</u>	<u>(21,151,742)</u>	<u>153,771,603</u>	<u>156,081,778</u>
TOTAL LIABILITIES, DEFERRED REVENUE, AND NET ASSETS (DEFICIT)	<u>\$ 180,453,388</u>	<u>\$ 216,822,885</u>	<u>\$ 16,358,983</u>	<u>\$ 16,138,926</u>	<u>\$ 19,323,104</u>	<u>\$ 20,770,109</u>	<u>\$ 216,135,475</u>	<u>\$ 253,731,920</u>

See accompanying notes to financial statements.

MUSCATINE POWER AND WATER

STATEMENTS OF REVENUES, EXPENSES AND
CHANGES IN NET ASSETS (DEFICIT)
For the Years Ended December 31, 2011 and 2010

	ELECTRIC UTILITY		WATER UTILITY		COMMUNICATIONS UTILITY		TOTALS	
	2011	2010	2011	2010	2011	2010	2011	2010
OPERATING REVENUES								
Retail sales	\$ 44,428,703	\$ 42,960,985	\$ 4,429,274	\$ 4,207,885	\$ 11,372,169	\$ 10,831,375	\$ 60,230,146	\$ 58,000,245
Wholesale electric sales	27,669,624	40,535,035	-	-	-	-	27,669,624	40,535,035
Steam sales	9,790,795	11,089,012	-	-	-	-	9,790,795	11,089,012
Other	1,322,161	1,107,239	29,403	26,759	103,876	89,063	1,455,440	1,223,061
Utilization of previously deferred revenue	7,122,296	748,000	-	-	-	-	7,122,296	748,000
Total Operating Revenues	<u>90,333,579</u>	<u>96,440,271</u>	<u>4,458,677</u>	<u>4,234,644</u>	<u>11,476,045</u>	<u>10,920,438</u>	<u>106,268,301</u>	<u>111,595,353</u>
OPERATING EXPENSES								
Production fuel	22,518,807	23,240,870	-	-	-	-	22,518,807	23,240,870
Purchased power	24,756,612	27,314,007	-	-	-	-	24,756,612	27,314,007
Emissions allowance	299,625	659,927	-	-	-	-	299,625	659,927
Other operating expenses	20,401,173	20,711,508	2,966,053	2,951,414	7,295,270	7,343,509	30,662,496	31,006,431
Maintenance	13,331,578	9,268,167	695,594	540,423	841,834	837,231	14,869,006	10,645,821
Depreciation	11,059,272	14,234,724	547,452	520,845	2,379,876	2,290,464	13,986,600	17,046,033
Amortization	-	-	-	-	773,137	773,137	773,137	773,137
Total Operating Expenses	<u>92,367,067</u>	<u>95,429,203</u>	<u>4,209,099</u>	<u>4,012,682</u>	<u>11,290,117</u>	<u>11,244,341</u>	<u>107,866,283</u>	<u>110,686,226</u>
Operating Income (Loss)	<u>(2,033,488)</u>	<u>1,011,068</u>	<u>249,578</u>	<u>221,962</u>	<u>185,928</u>	<u>(323,903)</u>	<u>(1,597,982)</u>	<u>909,127</u>
NONOPERATING REVENUES (EXPENSES)								
Investment income	68,820	197,786	220	948	147,082	9,205	216,122	207,939
Interest income on note receivable from communications utility	1,247,043	1,247,043	-	-	-	-	1,247,043	1,247,043
Gain on land disposal	490	-	-	-	-	-	490	-
Interest expense	(759,976)	(1,491,345)	(8,744)	(13,226)	(1,481,649)	(1,301,406)	(2,250,369)	(2,805,977)
Net Nonoperating Revenues (Expenses)	<u>556,377</u>	<u>(46,516)</u>	<u>(8,524)</u>	<u>(12,278)</u>	<u>(1,334,567)</u>	<u>(1,292,201)</u>	<u>(786,714)</u>	<u>(1,350,995)</u>
Net income (loss) before capital contributions	(1,477,111)	964,552	241,054	209,684	(1,148,639)	(1,616,104)	(2,384,696)	(441,868)
CAPITAL CONTRIBUTIONS	<u>12,059</u>	<u>79,102</u>	<u>47,791</u>	<u>92,081</u>	<u>14,671</u>	<u>-</u>	<u>74,521</u>	<u>171,183</u>
CHANGE IN NET ASSETS (DEFICIT)	(1,465,052)	1,043,654	288,845	301,765	(1,133,968)	(1,616,104)	(2,310,175)	(270,685)
NET ASSETS (DEFICIT) - Beginning of Year	<u>163,842,312</u>	<u>162,798,658</u>	<u>13,391,208</u>	<u>13,089,443</u>	<u>(21,151,742)</u>	<u>(19,535,638)</u>	<u>156,081,778</u>	<u>156,352,463</u>
NET ASSETS (DEFICIT) - END OF YEAR	<u>\$ 162,377,260</u>	<u>\$ 163,842,312</u>	<u>\$ 13,680,053</u>	<u>\$ 13,391,208</u>	<u>\$ (22,285,710)</u>	<u>\$ (21,151,742)</u>	<u>\$ 153,771,603</u>	<u>\$ 156,081,778</u>

See accompanying notes to financial statements.

MUSCATINE POWER AND WATER

STATEMENTS OF CASH FLOWS For the Years Ended December 31, 2011 and 2010

	ELECTRIC UTILITY		WATER UTILITY		COMMUNICATIONS UTILITY		TOTALS	
	2011	2010	2011	2010	2011	2010	2011	2010
CASH FLOWS FROM OPERATING ACTIVITIES								
Cash received from retail sales	\$ 44,425,467	\$ 42,509,061	\$ 4,424,868	\$ 4,162,282	\$ 11,036,955	\$ 10,731,097	\$ 59,887,290	\$ 57,402,440
Cash received from wholesale electric sales	31,081,934	39,918,749	-	-	-	-	31,081,934	39,918,749
Cash received from steam sales	10,413,345	9,672,985	-	-	-	-	10,413,345	9,672,985
Cash received from advertising sales	-	-	-	-	266,269	296,553	266,269	296,553
Cash received from other operating sources	1,516,818	1,989,432	27,874	33,369	554,643	239,310	2,099,335	2,262,111
Cash paid for coal	(25,003,331)	(22,648,740)	-	-	-	-	(25,003,331)	(22,648,740)
Cash paid for purchased power	(26,565,742)	(27,113,822)	-	-	-	-	(26,565,742)	(27,113,822)
Cash paid to suppliers	(13,662,828)	(9,548,587)	(1,664,574)	(1,526,211)	(5,043,985)	(5,334,153)	(20,371,387)	(16,408,951)
Cash paid for employee payroll, taxes and benefits	(21,913,430)	(21,619,228)	(1,993,090)	(1,991,898)	(3,132,336)	(3,227,453)	(27,038,856)	(26,838,579)
Reimbursements by related parties for expenses paid	239,042	226,619	-	-	-	-	239,042	226,619
Net Cash Flows From Operating Activities	<u>531,275</u>	<u>13,386,469</u>	<u>795,078</u>	<u>677,542</u>	<u>3,681,546</u>	<u>2,705,354</u>	<u>5,007,899</u>	<u>16,769,365</u>
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES								
Interest received on note receivable from communications utility	1,870,565	623,522	-	-	-	-	1,870,565	623,522
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES								
Capital expenditures	(3,085,629)	(1,587,191)	(617,536)	(1,059,385)	(1,602,402)	(1,797,406)	(5,305,567)	(4,443,982)
Proceeds from sale of assets	35,625	52,209	-	929	-	2,575	35,625	55,713
Loan proceeds	-	-	40,904	349,769	-	3,912,000	40,904	4,261,769
State revolving loan fund principal payments	-	-	(32,000)	-	-	-	(32,000)	-
Bond principal payments	(25,855,000)	(11,930,000)	-	-	-	-	(25,855,000)	(11,930,000)
Bond interest payments	(1,440,863)	(1,750,100)	-	-	-	-	(1,440,863)	(1,750,100)
Interest paid on notes payable	-	-	(8,744)	(4,880)	(2,011,383)	(665,258)	(2,020,127)	(670,138)
Net Cash Flows From Capital and Related Financing Activities	<u>(30,345,867)</u>	<u>(15,215,082)</u>	<u>(617,376)</u>	<u>(713,567)</u>	<u>(3,613,785)</u>	<u>1,451,911</u>	<u>(34,577,028)</u>	<u>(14,476,738)</u>
CASH FLOWS FROM INVESTING ACTIVITIES								
Proceeds from investments matured and sold	49,316,125	83,230,770	-	541,359	1,000,000	2,328,447	50,316,125	86,100,576
Investments purchased	(33,941,330)	(71,422,448)	-	(290,359)	(48,251)	(6,753,447)	(33,989,581)	(78,466,254)
Purchase of joint venture rights	(62,600)	(58,780)	-	-	-	-	(62,600)	(58,780)
Interest received on investments	215,916	770,424	220	2,131	49,938	3,538	266,074	776,093
Accrued interest purchased	-	(42,773)	-	-	-	(618)	-	(43,391)
Net Cash Flows From Investing Activities	<u>15,528,111</u>	<u>12,477,193</u>	<u>220</u>	<u>253,131</u>	<u>1,001,687</u>	<u>(4,422,080)</u>	<u>16,530,018</u>	<u>8,308,244</u>
Net Increase (Decrease) in Cash and Cash Equivalents	<u>(12,415,916)</u>	<u>11,272,102</u>	<u>177,922</u>	<u>217,106</u>	<u>1,069,448</u>	<u>(264,815)</u>	<u>(11,168,546)</u>	<u>11,224,393</u>
CASH AND CASH EQUIVALENTS - Beginning of Year								
Current unrestricted cash	5,108	120,252	422,229	205,123	794,865	1,066,831	1,222,202	1,392,206
Current restricted cash	<u>21,610,535</u>	<u>10,223,289</u>	<u>-</u>	<u>-</u>	<u>28,019</u>	<u>20,868</u>	<u>21,638,554</u>	<u>10,244,157</u>
	<u>21,615,643</u>	<u>10,343,541</u>	<u>422,229</u>	<u>205,123</u>	<u>822,884</u>	<u>1,087,699</u>	<u>22,860,756</u>	<u>11,636,363</u>
CASH AND CASH EQUIVALENTS - END OF YEAR								
Current unrestricted cash	3,012	5,108	600,151	422,229	894,530	794,865	1,497,693	1,222,202
Current restricted cash	<u>9,196,715</u>	<u>21,610,535</u>	<u>-</u>	<u>-</u>	<u>997,802</u>	<u>28,019</u>	<u>10,194,517</u>	<u>21,638,554</u>
	<u>\$ 9,199,727</u>	<u>\$ 21,615,643</u>	<u>\$ 600,151</u>	<u>\$ 422,229</u>	<u>\$ 1,892,332</u>	<u>\$ 822,884</u>	<u>\$ 11,692,210</u>	<u>\$ 22,860,756</u>

See accompanying notes to financial statements.

	ELECTRIC UTILITY		WATER UTILITY		COMMUNICATIONS UTILITY		TOTALS	
	2011	2010	2011	2010	2011	2010	2011	2010
RECONCILIATION OF OPERATING INCOME TO NET CASH FLOWS FROM OPERATING ACTIVITIES								
Operating income (loss)	\$ (2,033,488)	\$ 1,011,068	\$ 249,578	\$ 221,962	\$ 185,928	\$ (323,903)	\$ (1,597,982)	\$ 909,127
Noncash items in operating income								
Depreciation	11,059,272	14,234,724	547,452	520,845	2,379,876	2,290,464	13,986,600	17,046,033
Amortization of joint venture rights and intangible assets	101,911	93,759	-	-	773,137	773,137	875,048	866,896
Converter/modem net write-off	-	-	-	-	18,611	12,825	18,611	12,825
Utilization of previously deferred revenue	(7,122,296)	(748,000)	-	-	-	-	(7,122,296)	(748,000)
Changes in assets and liabilities								
Customer accounts receivable	2,254,841	(2,257,549)	4,598	(44,118)	(68,987)	(122,681)	2,190,452	(2,424,348)
Other receivable	-	-	-	-	-	-	-	-
Inventories	(4,581,487)	2,117,305	4,124	(2,373)	(25,879)	14,353	(4,603,242)	2,129,285
Prepaid and deferred expenses	12,462	(41,286)	(3,652)	2,604	58,415	(32,393)	67,225	(71,075)
Trade accounts payable	1,103,212	87,864	2,848	(26,073)	57,772	77,280	1,163,832	139,071
Accrued expenses	(256,625)	(1,088,745)	(9,870)	4,695	302,673	16,272	36,178	(1,067,778)
Customer deposits	(6,527)	(22,671)	-	-	-	-	(6,527)	(22,671)
NET CASH FLOWS FROM OPERATING ACTIVITIES	\$ 531,275	\$ 13,386,469	\$ 795,078	\$ 677,542	\$ 3,681,546	\$ 2,705,354	\$ 5,007,899	\$ 16,769,365
SUPPLEMENTAL SCHEDULE OF NONCASH CAPITAL AND RELATED FINANCING AND INVESTING ACTIVITIES								
Unrealized gain (loss) in investments	\$ (106,233)	\$ (239,229)	\$ -	\$ -	\$ -	\$ -	\$ (106,233)	\$ (239,229)
Amortization of bond discounts/premium, deferred loss on debt refunding and bond/debt issue costs	25,982	37,611	-	7,382	9,006	5,477	34,988	50,470
Unpaid capital expenditures	240,065	103,004	27,915	18,728	26,498	161,240	294,478	282,972
Non-cash capital contributions	-	-	47,791	-	-	-	47,791	-

See accompanying notes to financial statements.

NOTES TO FINANCIAL STATEMENTS

MUSCATINE POWER AND WATER

NOTES TO FINANCIAL STATEMENTS December 31, 2011 and 2010

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

ORGANIZATION AND BASIS OF ACCOUNTING

Muscatine Power and Water (utility) is a municipal utility serving the City of Muscatine, Iowa (municipality) and surrounding areas whose rates are set by the Board of Water, Electric, and Communications Trustees (Board). The electric utility is engaged in the generation, transmission, and distribution of electric power and steam and other related activities. The water utility is engaged in the supply, purification, and distribution of water and other related activities. The communications utility is engaged in providing cable, Internet, and network services and other related activities. The equity of the utility is vested in the City of Muscatine, Iowa.

The financial statements of the utility are presented in conformity with accounting principles generally accepted in the United States of America. In reporting financial activity, the utility applies all applicable Government Accounting Standards Board (GASB) pronouncements, as well as private-sector standards of accounting and financial reporting issued on or before November 30, 1989, except for those that conflict with or contradict GASB pronouncements. The utility has elected not to follow private-sector standards of accounting and financial reporting issued after that date. In addition, the electric and water utilities meet the criteria and, accordingly, follow the accounting and reporting requirements of FASB ASC 980, "Regulated Operations", which requires that the effects of the rate-making process be recorded in the financial statements.

REPORTING ENTITY

The utility is reported as a component unit in the City of Muscatine, Iowa's Comprehensive Annual Financial Report.

MEASUREMENT FOCUS, BASIS OF ACCOUNTING AND FINANCIAL STATEMENT PRESENTATION

The financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Under the accrual basis of accounting, revenues are recognized when earned and expenses are recorded when the liability is incurred or economic asset used. Revenues, expenses, gains, losses, assets and liabilities resulting from exchange and exchange-like transactions are recognized when the exchange takes place, except when the utility applies the accounting and reporting requirements of ASC 980 in deferring revenues for recognition in future periods or recognition of deferred revenues in the current period.

In June 2008, the GASB issued Statement No. 53 - Accounting and Financial Reporting for Derivative Instruments. This statement addresses the recognition, measurement and disclosure of information regarding derivative instruments entered into by state and local governments. The utility made the decision to implement this standard effective January 1, 2010.

Preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

MUSCATINE POWER AND WATER

NOTES TO FINANCIAL STATEMENTS December 31, 2011 and 2010

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont.)

CASH AND CASH EQUIVALENTS

The utility's cash and cash equivalents are considered to be general checking, saving and money market accounts. For purposes of the statements of cash flows, cash and cash equivalents have original maturities of 90 days or less from December 31, 2011 and 2010.

RECEIVABLES

An allowance for doubtful accounts is recorded annually based on historical experience and management's evaluation of receivables at the end of the year.

INVENTORIES

Inventories consist of fuel (coal), emission allowances, and materials and supplies valued at weighted-average cost. Materials and supplies are generally used for construction, operation and maintenance work, not for resale.

CAPITAL ASSETS

Capital assets are stated at original cost, which includes the cost of contracted services, material, labor, overhead and, on significant projects, an allowance for borrowed funds used during construction.

Capital assets are generally defined by the utility as assets with an initial, individual cost of more than \$1,000 and an estimated useful life in excess of one year.

Replacements and betterments of depreciable property units are charged to capital assets. Routine maintenance and repairs are charged to expense as incurred. At the time depreciable property units are retired, the original cost of the unit plus cost of removal less salvage is charged to the accumulated provision for depreciation.

Depreciation of capital assets is provided using the straight-line method over the estimated useful lives of the respective assets. In 2011, generation assets' useful lives were lengthened to reflect a more accurate estimate. The composite depreciation rates for 2011 and 2010 are as follows:

	<u>2011</u>	<u>2010</u>
Electric Utility		
Generation plant	2.3%	3.2%
Transmission and distribution plant	3.9	3.8
General plant	7.7	7.8

MUSCATINE POWER AND WATER

NOTES TO FINANCIAL STATEMENTS December 31, 2011 and 2010

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont.)

CAPITAL ASSETS (cont.)

	<u>2011</u>	<u>2010</u>
Water Utility		
Source of supply	3.3%	3.3%
Pumping equipment	3.3	3.2
Purification system	2.7	2.7
Distribution system	2.2	2.2
General plant	2.7	2.5
Communications Utility		
CATV	8.9%	9.1%
Data/Internet	7.8	7.7
MAN	5.4	3.6
General plant	6.8	8.0

On an ongoing basis, the utility reviews capital assets for impairment whenever events or circumstances indicate that carrying amounts may not be recoverable. If such events or changes in circumstances occur, the utility will recognize an impairment loss. No such loss was recognized in 2011 or 2010.

CUSTOMER ADVANCES FOR CONSTRUCTION

Customer advances for water construction projects are recorded as water utility plant and a liability at the time the asset is contributed to the utility. The utility reimburses the customer by annually refunding a portion of the advance over a contracted period of time. At the end of the contract, any remaining liability is reclassified as a capital contribution.

AMORTIZATION OF DEBT DISCOUNTS/PREMIUMS AND BOND ISSUANCE COSTS

Debt discounts/premiums and bond issuance costs are being amortized over the life of the bonds/debt using the effective interest method.

COMPENSATED ABSENCES

Under terms of employment, employees are granted vacation in varying amounts. Only benefits considered to be vested are disclosed in these statements.

DEFERRED REVENUE

The Board may, at its discretion, set aside earnings to help maintain stability in the electric utility's long-term rate structure. These earnings may be used for extraordinary operating expenses and debt service when deemed necessary by the Board. In 2011, \$7,122,296 was used for extraordinary operating expenses and debt service, and in 2010, \$748,000 was used for debt service.

MUSCATINE POWER AND WATER

NOTES TO FINANCIAL STATEMENTS December 31, 2011 and 2010

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont.)

DEFERRED REVENUE (cont.)

The communications utility's deferred revenue is a result of a 20-year contract to lease dark fiber to Iowa Health System.

CHARGES FOR SERVICES

Electric and water billings are rendered and recorded monthly based on metered usage. Communications billings are rendered and recorded monthly based on the type of service provided. Rates were approved by the Board of Trustees as follows:

Current electric rates were approved on April 26, 2011 and effective for service beginning August 1, 2011.

Current water rates were approved on November 30, 2010 and effective for service beginning April 1, 2011.

Current communications rates were approved on November 30, 2010 and effective for service beginning January 1, 2011.

OPERATING REVENUES AND EXPENSES

The utility distinguishes operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with the utility's principal ongoing operations. The principal operating revenues of the utility are charges to customers for sales and services. Operating expenses include the cost of sales and services, administrative expenses and depreciation/amortization on capital assets. All revenues and expenses not meeting this definition are reported as nonoperating revenues, capital contributions or nonoperating expenses.

Revenues are recorded as services are rendered to customers. The electric and water utilities' revenues include an estimate of unbilled revenues for services rendered only to certain residential and small commercial customers from the date of the last meter reading to year-end. The communications utility's revenues include amounts billed to customers for cable and Internet services, installations, advertising and other services. Revenues from cable and Internet services, installation, and other services are recognized when the services are provided to the customers. Advertising sales are recognized in the period that the advertisements are exhibited. The communications utility's revenues include an estimate of unbilled revenues for service rendered only to certain residential and small commercial customers from the date of their previous bill's generation to year-end. The unbilled revenue recorded in 2011 for the electric, water, and communications utilities are \$377,122, \$51,917, and \$76,456, respectively. The unbilled revenue recorded in 2010 for the electric, water, and communications utilities are \$378,203, \$51,298, and \$87,821, respectively.

CAPITAL CONTRIBUTIONS

Cash and capital assets are contributed to the utility from customers, the municipality or external parties. The value of property contributed to the utility is reported as revenue on the statements of revenues, expenses, and changes in net assets.

MUSCATINE POWER AND WATER

NOTES TO FINANCIAL STATEMENTS December 31, 2011 and 2010

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont.)

INCOME TAX STATUS

The utility is exempt from federal and state income taxes under the applicable tax codes.

RECLASSIFICATIONS

Certain amounts in the 2010 financial statements may have been reclassified in order to conform to the 2011 presentation.

NOTE 2 – DEPOSITS AND INVESTMENTS

State statute, the 1992 electric bond resolution and the utility's written investment policy authorize the utility to invest in certain certificates of deposit, interest bearing savings accounts, money market accounts, obligations of the United States of America or any of its agencies and instrumentalities, prime bankers' acceptances, commercial paper and perfected repurchase agreements. The utility's written investment policy provides additional guidelines as to portfolio mix, maturity and quality of investments.

Deposits and investments consist primarily of U.S. Treasury obligations, Federal agency obligations and certificates of deposit. Investments are stated at fair value, which is the amount at which an investment could be exchanged in a current transaction between willing parties. Fair values are based on quoted market prices. No investments are reported at amortized cost. Adjustments necessary to record investments at fair value are recorded in the statements of revenues, expenses, and changes in net assets as increases or decreases in investment income. Investment income is allocated to the electric, water, and communications utilities' revenue funds as appropriate.

CUSTODIAL CREDIT RISK

Deposits (cash, checking accounts, money markets, non-negotiable certificates of deposits)

Custodial credit risk is the risk that in the event of a financial institution failure, the utility's deposits may not be returned to the utility. The utility's deposits at year-end were covered by federal depository insurance or insured by the state through pooled collateral, state sinking funds and by the state's ability to assess for lost funds in accordance with Chapter 12C of the Code of Iowa.

It is the policy of the utility to maintain all deposits and investments in authorized investment vehicles that are insured or registered in the utility's name or which are collateralized by or evidenced by securities held by the utility or its agent in the utility's name.

Investments

For an investment, custodial credit risk is the risk that, in the event of the failure of the counterparty, the utility will not be able to recover the value of its investment or collateral securities that are in the possession of an outside party. All investments held at December 31, 2011 and 2010 were considered to be in risk category one (investments held in trust on behalf of the utility), therefore, not subject to custodial credit risk.

MUSCATINE POWER AND WATER

NOTES TO FINANCIAL STATEMENTS December 31, 2011 and 2010

NOTE 2 – DEPOSITS AND INVESTMENTS (cont.)

CUSTODIAL CREDIT Risk (cont.)

Investments (cont.)

It is the policy of the utility to maintain all deposits and investments in authorized investment vehicles that are insured or registered in the utility's name or which are collateralized by or evidenced by securities held by the utility or its agent in the utility's name.

CREDIT RISK

Credit risk is the risk an issuer or other counterparty to an investment will not fulfill its obligations.

As of December 31, 2011, the utility's investments were rated as follows:

<u>Investment Type</u>	<u>Standard & Poor's</u>	<u>Moody's</u>
US agencies	A+	Aaa

It is the policy of the utility to have securities held by the utility or a third party custodian and rated within the highest or second highest rating category of a nationally recognized rating agency.

CONCENTRATION OF CREDIT RISK

Concentration of credit risk is the risk of loss attributed to the magnitude of an investment in a single issuer.

At December 31, 2011 and 2010, investments held with issuers, each totaling more than 5 percent of the total portfolio, were concentrated as follows:

<u>Issuer</u>	<u>% of Portfolio</u>	
	<u>2011</u>	<u>2010</u>
US Treasury Bills	-	37.3 %
Federal Home Loan Bank	-	53.1 %
Federal Home Loan Mortgage Corporation	59.4 %	5.8 %
FNMA	25.1 %	-
GNMA	15.5 %	-

It is the policy of the utility to diversify its investment portfolio. Assets are diversified to eliminate the risk of loss resulting from over-concentration of assets in a specific maturity, a specific issuer, or a specific class of securities.

Although there is investment concentration at December 31, 2011 and December 31, 2010, the utility believes the risk to be minimal. Investments held are issued by U.S. Treasuries or federal agencies and rated AA+ by Standard & Poor's and Aaa by Moody's.

MUSCATINE POWER AND WATER

NOTES TO FINANCIAL STATEMENTS December 31, 2011 and 2010

NOTE 2 – DEPOSITS AND INVESTMENTS (cont.)

INTEREST RATE RISK

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment.

At December 31, 2011, the utility's investments were as follows:

Investment Type	Maturity In Years			
	Fair Value	Less than 1 Year	1 – 5 Years	Greater than 5 Years
US agencies	\$ 916,621	\$ -	\$ 16,357	\$ 900,264

At December 31, 2010, the utility's investments were as follows:

Investment Type	Maturity In Years			
	Fair Value	Less than 1 Year	1 – 5 Years	Greater than 5 Years
US Treasuries	\$ 4,998,600	\$ 4,998,600	\$ -	\$ -
US agencies	8,399,050	7,118,204	41,396	1,239,450
Totals	\$ 13,397,650	\$ 12,116,804	\$ 41,396	\$ 1,239,450

The utility's investment policy addresses maturity limitations by requiring operating funds to be invested in instruments that mature within 397 days. Non-operating funds may be invested in instruments with maturities longer than 397 days as long as the maturities are consistent with the needs and use of the utility. One of the investment policy's primary objectives is to maintain the necessary liquidity to match expected liabilities.

MUSCATINE POWER AND WATER

NOTES TO FINANCIAL STATEMENTS December 31, 2011 and 2010

NOTE 3 – CAPITAL ASSETS

ELECTRIC UTILITY

A summary of changes in electric capital assets for 2011 follows:

	Balance 1/01/11	Additions/ Reclassifications	Retirements	Transfers	Balance 12/31/11
Land and land rights ⁽¹⁾	\$ 1,874,600	\$ -	\$ (10)	\$ -	\$ 1,874,590
Generation plant	327,947,420	(3,285)	(866,747)	1,409,775	328,487,163
Transmission and distribution plant	55,983,205	591,205	(200,595)	605,177	56,978,992
General plant	<u>19,023,954</u>	<u>45,922</u>	<u>(252,972)</u>	<u>480,021</u>	<u>19,296,925</u>
Total Utility Plant in Service	404,829,179	633,842	(1,320,324)	2,494,973	406,637,670
Construction work in progress ⁽¹⁾	<u>242,626</u>	<u>2,748,326</u>	<u>(156,087)</u>	<u>(2,494,973)</u>	<u>339,892</u>
Total Electric Utility Plant	<u>405,071,805</u>	<u>\$ 3,382,168</u>	<u>\$ (1,476,411)</u>	<u>\$ -</u>	<u>406,977,562</u>
Less: Accumulated depreciation					
Generation plant	234,443,467	\$ 7,444,500	\$ (861,977)	\$ -	241,025,990
Transmission and distribution plant	41,112,372	2,153,652	(178,909)	-	43,087,115
General plant	<u>16,003,937</u>	<u>1,461,120</u>	<u>(252,972)</u>	-	<u>17,212,085</u>
Total Accumulated Depreciation	<u>291,559,776</u>	<u>\$ 11,059,272</u>	<u>\$ (1,293,858)</u>	<u>\$ -</u>	<u>301,325,190</u>
Net Electric Capital Assets	<u>\$ 113,512,029</u>				<u>\$ 105,652,372</u>

(1) – Capital assets not being depreciated

MUSCATINE POWER AND WATER

NOTES TO FINANCIAL STATEMENTS December 31, 2011 and 2010

NOTE 3 – CAPITAL ASSETS (cont.)

ELECTRIC UTILITY (cont.)

A summary of changes in electric capital assets for 2010 follows:

	Balance 1/01/10	Additions/ Reclassifications	Retirements	Transfers	Balance 12/31/10
Land and land rights ⁽¹⁾	\$ 1,874,600	\$ -	\$ -	\$ -	\$ 1,874,600
Generation plant	327,558,492	(38,150)	(72,548)	499,626	327,947,420
Transmission and distribution plant	55,256,794	440,596	(88,784)	374,599	55,983,205
General plant	19,104,771	39,674	(339,180)	218,689	19,023,954
Total Utility Plant in Service	403,794,657	442,120	(500,512)	1,092,914	404,829,179
Construction work in progress ⁽¹⁾	182,430	1,356,540	(203,430)	(1,092,914)	242,626
Total Electric Utility Plant	403,977,087	\$ 1,798,660	\$ (703,942)	\$ -	405,071,805
Less: Accumulated depreciation					
Generation plant	223,873,066	\$ 10,622,868	\$ (52,467)	\$ -	234,443,467
Transmission and distribution plant	39,040,947	2,124,624	(53,199)	-	41,112,372
General plant	14,875,351	1,487,232	(358,646)	-	16,003,937
Total Accumulated Depreciation	277,789,364	\$ 14,234,724	\$ (464,312)	\$ -	291,559,776
Net Electric Capital Assets	\$ 126,187,723				\$ 113,512,029

(1) – Capital assets not being depreciated

MUSCATINE POWER AND WATER

NOTES TO FINANCIAL STATEMENTS December 31, 2011 and 2010

NOTE 3 – CAPITAL ASSETS (cont.)

WATER UTILITY

A summary of changes in water capital assets for 2011 follows:

	Balance 1/01/11	Additions/ Reclassifications	Retirements	Transfers	Balance 12/31/11
Land and land rights ⁽¹⁾	\$ 1,052,321	\$ -	\$ -	\$ -	\$ 1,052,321
Source of supply	1,850,907	179,222	(46,302)	143,978	2,127,805
Pumping equipment	2,094,230	(179,222)	(24,151)	152,393	2,043,250
Purification equipment	1,051,289	-	-	-	1,051,289
Distribution system	16,348,906	72,243	(25,128)	212,528	16,608,549
General plant	1,099,583	6,797	(18,366)	50,998	1,139,012
Total Utility Plant in Service	23,497,236	79,040	(113,947)	559,897	24,022,226
Construction work in progress ⁽¹⁾	47,281	528,342	(12,556)	(559,897)	3,170
Total Water Utility Plant	23,544,517	\$ 607,382	\$ (126,503)	\$ -	24,025,396
Less: Accumulated depreciation					
Source of supply	1,143,098	\$ 61,692	\$ (46,302)	\$ -	1,158,488
Pumping equipment	436,896	68,124	(24,151)	-	480,869
Purification system	747,371	28,055	-	-	775,426
Distribution system	5,226,523	359,556	(25,127)	-	5,560,952
General plant	1,069,555	30,024	(18,197)	-	1,081,382
Total Accumulated Depreciation	8,623,443	\$ 547,451	\$ (113,777)	\$ -	9,057,117
Net Water Capital Assets	\$ 14,921,074				\$ 14,968,279

(1) – Capital assets not being depreciated

MUSCATINE POWER AND WATER

NOTES TO FINANCIAL STATEMENTS December 31, 2011 and 2010

NOTE 3 – CAPITAL ASSETS (cont.)

WATER UTILITY (cont.)

A summary of changes in water capital assets for 2010 follows:

	Balance 1/01/10	Additions/ Reclassifications	Retirements	Transfers	Balance 12/31/10
Land and land rights ⁽¹⁾	\$ 1,052,321	\$ -	\$ -	\$ -	\$ 1,052,321
Source of supply	1,874,664	-	(23,757)	-	1,850,907
Pumping equipment	1,620,083	(537)	(80,091)	554,775	2,094,230
Purification equipment	1,052,164	-	(875)	-	1,051,289
Distribution system	15,959,962	48,511	(27,545)	367,978	16,348,906
General plant	1,089,736	12,510	(20,181)	17,518	1,099,583
Total Utility Plant in Service	22,648,930	60,484	(152,449)	940,271	23,497,236
Construction work in progress ⁽¹⁾	93,873	921,767	(28,088)	(940,271)	47,281
Total Water Utility Plant	22,742,803	\$ 982,251	\$ (180,537)	\$ -	23,544,517
Less: Accumulated depreciation					
Source of supply	1,107,811	\$ 62,484	\$ (27,197)	\$ -	1,143,098
Pumping equipment	476,404	52,272	(91,780)	-	436,896
Purification system	720,294	28,080	(1,003)	-	747,371
Distribution system	4,902,414	350,726	(26,617)	-	5,226,523
General plant	1,062,403	27,333	(20,181)	-	1,069,555
Total Accumulated Depreciation	8,269,326	\$ 520,895	\$ (166,778)	\$ -	8,623,443
Net Water Capital Assets	\$ 14,473,477				\$ 14,921,074

(1) – Capital assets not being depreciated

MUSCATINE POWER AND WATER

NOTES TO FINANCIAL STATEMENTS December 31, 2011 and 2010

NOTE 3 – CAPITAL ASSETS (cont.)

COMMUNICATIONS UTILITY

A summary of changes in communications capital assets for 2011 follows:

	Balance 1/01/11	Additions/ Reclassifications	Retirements	Transfers	Balance 12/31/11
CATV	\$ 20,615,825	\$ 689,888	\$ (2,568)	\$ 224,839	\$ 21,527,984
Data/Internet	3,330,893	142,934	(30,163)	89,151	3,532,815
MAN	3,760,607	61,611	(18,438)	246,715	4,050,495
General plant	<u>1,328,182</u>	<u>18,115</u>	<u>(15,891)</u>	<u>88,266</u>	<u>1,418,672</u>
Total Utility Plant in Service	29,035,507	912,548	(67,060)	648,971	30,529,966
Construction work in progress ⁽¹⁾	<u>70,300</u>	<u>585,159</u>	<u>(493)</u>	<u>(648,971)</u>	<u>5,995</u>
Total Communications Utility Plant	<u>29,105,807</u>	<u>\$ 1,497,707</u>	<u>\$ (67,553)</u>	<u>\$ -</u>	<u>30,535,961</u>
Less: Accumulated depreciation					
CATV	12,056,645	\$ 1,827,216	\$ 26,344	\$ -	13,910,205
Data/Internet	2,204,054	259,188	(25,581)	-	2,437,661
MAN	2,132,004	202,704	(18,438)	-	2,316,270
General plant	<u>757,141</u>	<u>90,768</u>	<u>(15,891)</u>	<u>-</u>	<u>832,018</u>
Total Accumulated Depreciation	<u>17,149,844</u>	<u>\$ 2,379,876</u>	<u>\$ (33,566)</u>	<u>\$ -</u>	<u>19,496,154</u>
Net Communications Capital Assets	<u>\$ 11,955,963</u>				<u>\$ 11,039,807</u>

(1) – Capital assets not being depreciated

MUSCATINE POWER AND WATER

NOTES TO FINANCIAL STATEMENTS December 31, 2011 and 2010

NOTE 3 – CAPITAL ASSETS (cont.)

COMMUNICATIONS UTILITY (cont.)

A summary of changes in communications capital assets for 2010 follows:

	Balance 1/01/10	Additions/ Reclassifications	Retirements	Transfers	Balance 12/31/10
CATV	\$ 19,760,755	\$ 993,151	\$ (171,477)	\$ 33,396	\$ 20,615,825
Data/Internet	3,150,648	135,106	(99,309)	144,448	3,330,893
MAN	4,382,145	37,056	(948,413)	289,819	3,760,607
General plant	<u>1,285,179</u>	<u>3,984</u>	<u>(48,217)</u>	<u>87,236</u>	<u>1,328,182</u>
Total Utility Plant in Service	28,578,727	1,169,297	(1,267,416)	554,899	29,035,507
Construction work in progress ⁽¹⁾	<u>67,517</u>	<u>563,710</u>	<u>(6,028)</u>	<u>(554,899)</u>	<u>70,300</u>
Total Communications Utility Plant	<u>28,646,244</u>	<u>\$ 1,733,007</u>	<u>\$ (1,273,444)</u>	<u>\$ -</u>	<u>29,105,807</u>
Less: Accumulated depreciation					
CATV	10,406,360	\$ 1,788,492	\$ (138,207)	\$ -	12,056,645
Data/Internet	2,055,910	241,884	(93,740)	-	2,204,054
MAN	2,922,738	157,680	(948,414)	-	2,132,004
General plant	<u>702,950</u>	<u>102,408</u>	<u>(48,217)</u>	<u>-</u>	<u>757,141</u>
Total Accumulated Depreciation	<u>16,087,958</u>	<u>\$ 2,290,464</u>	<u>\$ (1,228,578)</u>	<u>\$ -</u>	<u>17,149,844</u>
Net Communications Capital Assets	<u>\$ 12,558,286</u>				<u>\$ 11,955,963</u>

(1) – Capital assets not being depreciated

MUSCATINE POWER AND WATER

NOTES TO FINANCIAL STATEMENTS December 31, 2011 and 2010

NOTE 4 – RESTRICTED ASSETS

Restricted assets represent amounts set aside under the terms of the bond resolutions relating to the electric revenue bonds, or under the terms of the communications loan agreement, or by the utility's Board of Trustees restriction. In accordance with the covenants of the bond resolutions, the amounts have been segregated into various funds or accounts. The extraordinary operation and maintenance account may be used for extraordinary operating expenses and debt service at the discretion of the Board. In accordance with the communications loan agreement, the communications system loan repayment sinking fund is used solely for the purpose of paying the interest on and principal of the bank loans. The composition of the restricted assets at December 31, 2011 and 2010 is as follows:

	Electric Utility		Communications Utility	
	2011	2010	2011	2010
Restricted Assets:				
Sinking fund	\$ -	\$ 13,296,013	\$ 997,802	\$ 28,019
Debt service reserve fund	-	7,500,767	-	-
Extraordinary operation and maintenance account	10,113,336	17,211,405	-	-
Total Restricted Assets	<u>\$ 10,113,336</u>	<u>\$ 38,008,185</u>	<u>\$ 997,802</u>	<u>\$ 28,019</u>

NOTE 5 – NON-CURRENT LIABILITIES AND DEFERRED REVENUE

NON-CURRENT LIABILITIES AND DEFERRED REVENUE SUMMARY – ELECTRIC

The following revenue bonds were paid in full in 2011:

Issue Date	Original Amount	Purpose
October 2, 2001	\$49,090,000	Advance Refunding of a portion of the 1992 Series bonds

MUSCATINE POWER AND WATER

NOTES TO FINANCIAL STATEMENTS December 31, 2011 and 2010

NOTE 5 – NON-CURRENT LIABILITIES AND DEFERRED REVENUE (cont.)

NON-CURRENT LIABILITIES AND DEFERRED REVENUE SUMMARY – ELECTRIC (cont.)

Non-current liabilities and deferred revenue activity for the year ended December 31, 2011:

	Balance 1/01/11	Additions	Payments/ Amortization/ Reclassifications	Balance 12/31/11	Due Within One Year
Series 2001 revenue bonds	\$ 25,855,000	\$ -	\$ (25,855,000)	\$ -	\$ -
Unamortized portion of deferred loss on refundings	(72,370)	-	72,370	-	-
Unamortized portion of revenue bond premiums	73,671	-	(73,671)	-	-
Total Long-Term Debt	25,856,301	-	(25,856,301)	-	-
Less: Current installments	(12,585,000)	-	12,585,000	-	-
Long-Term Debt, Net of Current Portion	13,271,301	-	(13,271,301)	-	-
Deferred revenue	17,155,162	-	(7,122,296)	10,032,866	-
Post-employment health benefit provision	118,166	21,825	-	139,991	-
Health care provision	1,858,882	12,535	-	1,871,417	-
Non-Current Liabilities and Deferred Revenue	\$ 32,403,511	\$ 34,360	\$ (20,393,597)	\$ 12,044,274	\$ -

Non-current liabilities and deferred revenue activity for the year ended December 31, 2010:

	Balance 1/01/10	Additions	Payments/ Amortization/ Reclassifications	Balance 12/31/10	Due Within One Year
Series 2001 revenue bonds	\$ 37,785,000	\$ -	\$ (11,930,000)	\$ 25,855,000	\$ 12,585,000
Unamortized portion of deferred loss on refundings	(213,378)	-	141,008	(72,370)	(72,370)
Unamortized portion of revenue bond premiums	230,225	-	(156,554)	73,671	73,671
Total Long-Term Debt	37,801,847	-	(11,945,546)	25,856,301	12,586,301
Less: Current installments	(11,930,000)	-	(655,000)	(12,585,000)	-
Long-Term Debt, Net of Current Portion	25,871,847	-	(12,600,546)	13,271,301	12,586,301
Deferred revenue	17,903,162	-	(748,000)	17,155,162	-
Post-employment health benefit provision	-	118,166	-	118,166	-
Health care provision	1,993,284	-	(134,402)	1,858,882	-
Non-Current Liabilities and Deferred Revenue	\$ 45,768,293	\$ 118,166	\$ (13,482,948)	\$ 32,403,511	\$ 12,586,301

MUSCATINE POWER AND WATER

NOTES TO FINANCIAL STATEMENTS December 31, 2011 and 2010

NOTE 5 – NON-CURRENT LIABILITIES AND DEFERRED REVENUE (cont.)

NON-CURRENT LIABILITIES AND DEFERRED REVENUE SUMMARY – ELECTRIC (cont.)

In prior years, the utility provided for the advance refunding of certain revenue bonds. In connection with these advance refunding, the utility deposited certain amounts in irrevocable trust funds for the repayment of all principal and interest on the advance refunded bonds. The utility is contingently liable for repayment of these bonds, which in the aggregate amounted to \$29,680,000 at December 31, 2011. The bonds and corresponding trust funds are not included on the Statements of Net Assets at December 31, 2011 and 2010 as the outstanding bonds are considered defeased.

NON-CURRENT LIABILITIES SUMMARY – WATER

On November 18, 2009, the utility closed on a loan from the Iowa Department of Natural Resources' State Drinking Water Revolving Loan Fund for the well motor control project. The loan is administered by the Iowa Finance Authority. The loan agreement provided for the borrowing of up to \$494,000; total amount borrowed was \$399,000. The project qualified for ARRA (Stimulus Act) funding as a "green" water project and is eligible for \$93,000 loan forgiveness. The interest rate on the loan is 3.0% interest, plus a 0.25% servicing fee, with a 10-year repayment term. Interest payments are payable semi-annually and began June 1, 2010; principal payments began June 1, 2011 and are due annually. Total outstanding loan payable at December 31, 2011 was \$274,000.

MUSCATINE POWER AND WATER

NOTES TO FINANCIAL STATEMENTS December 31, 2011 and 2010

NOTE 5 – NON-CURRENT LIABILITIES AND DEFERRED REVENUE (cont.)

NON-CURRENT LIABILITIES SUMMARY – WATER (cont.)

Non-current liabilities activity for the year ending December 31, 2011:

	Balance 1/01/11	Additions/ (Reductions)	Payments/ Amortization/ Reclassifications	Balance 12/31/11	Due Within One Year
Long term debt	\$ 265,096	\$ 40,904	\$ (32,000)	\$ 274,000	\$ 27,000
Less: Current installments	(32,000)	-	5,000	(27,000)	-
Long-Term Debt, Net of Current Portion	233,096	40,904	(27,000)	247,000	27,000
Post-employment health benefit provision	11,756	2,174	-	13,930	-
Health care provision	155,346	(10,615)	-	144,731	-
Customer advances for construction	1,910,502	(257,137)	(32,066)	1,621,299	-
 Non-Current Liabilities	 <u>\$ 2,310,700</u>	 <u>\$ (224,674)</u>	 <u>\$ (59,066)</u>	 <u>\$ 2,026,960</u>	 <u>\$ 27,000</u>

Non-current liabilities activity for the year ending December 31, 2010:

	Balance 1/01/10	Additions/ (Reductions)	Payments/ Amortization/ Reclassifications	Balance 12/31/10	Due Within One Year
Long term debt	\$ 7,407	\$ 257,689	\$ -	\$ 265,096	\$ 32,000
Less: Current installments	-	-	(32,000)	(32,000)	-
Long-Term Debt, Net of Current Portion	7,407	257,689	(32,000)	233,096	32,000
Post-employment health benefit provision	-	11,756	-	11,756	-
Health care provision	174,876	(19,530)	-	155,346	-
Customer advances for construction	1,983,846	(43,682)	(29,662)	1,910,502	-
 Non-Current Liabilities	 <u>\$ 2,166,129</u>	 <u>\$ 206,233</u>	 <u>\$ (61,662)</u>	 <u>\$ 2,310,700</u>	 <u>\$ 32,000</u>

MUSCATINE POWER AND WATER

NOTES TO FINANCIAL STATEMENTS December 31, 2011 and 2010

NOTE 5 – NON-CURRENT LIABILITIES AND DEFERRED REVENUE (cont.)

NON-CURRENT LIABILITIES SUMMARY – WATER (cont.)

Non-Current Liabilities Maturity Schedule – Water

Year Ending December 31	Principal Amount	Iowa Finance Authority Loan		Total
		Interest 3.00%	Servicing fee 0.25%	
2012	\$ 27,000	\$ 7,826	\$ 685	\$ 35,511
2013	28,000	6,990	618	35,608
2014	29,000	6,135	548	35,683
2015	29,000	5,265	475	34,740
2016	30,000	4,380	402	34,782
2017	31,000	3,465	328	34,793
2018	32,000	2,520	250	34,770
2019	33,000	1,545	170	34,715
2020	35,000	525	87	35,612
Totals	\$ 274,000	\$ 38,651	\$ 3,563	\$ 316,214

All water utility revenues, net of specified operating expenses, are pledged as security of the water debt until fully paid. Principal and interest paid in 2011, interest paid in 2010, and water utility net revenues are as follows:

	2011	2010
Principal and interest paid	\$ 40,744	\$ 4,880
Net revenues	797,250	743,755

Annual future principal and interest payments are expected to require 4% of water utility net revenues.

NON-CURRENT LIABILITIES AND DEFERRED REVENUE SUMMARY – COMMUNICATIONS

In December 2008, the communications utility acquired loans from three local banks to cover the digital transition project and other capital costs. The loan agreement allowed the communications utility to draw down a total amount of up to \$4,800,000 through December 31, 2010, at an annual interest rate of 4.7%. Interest is payable semi-annually and began July 1, 2009; principal repayment is payable annually beginning January 1, 2012. As of December 31, 2010, the communications utility borrowed the entire \$4,800,000.

MUSCATINE POWER AND WATER

NOTES TO FINANCIAL STATEMENTS December 31, 2011 and 2010

NOTE 5 – NON-CURRENT LIABILITIES AND DEFERRED REVENUE (cont.)

NON-CURRENT LIABILITIES AND DEFERRED REVENUE SUMMARY – COMMUNICATIONS (cont.)

The electric utility has advanced \$35,327,000 to the communications utility for capital improvements and acquisition of a cable television system. Effective November 28, 2006, the interest rate was fixed at 3.53% beginning January 1, 2007 by action of the Board. Semi-annual payments of interest only are due each January 1 and July 1. A Board resolution, which passed November 25, 2008, approved an annual principal repayment schedule with payments beginning January 1, 2016 over a 30 year period. This debt, as to both principal and interest, is and shall be junior and subordinate in all respects to the bank loans and interest thereon during the term of the bank loan agreement.

Non-current liabilities and deferred revenue activity for the year ending December 31, 2011:

	Balance 1/01/11	Additions/ (Reductions)	Payments/ Amortization/ Reclassifications	Balance 12/31/11	Due Within One Year
Notes payable to banks	\$ 4,800,000	\$ -	\$ -	\$ 4,800,000	\$ 885,000
Note payable to electric utility	35,327,000	-	-	35,327,000	-
Total Long-Term Debt	40,127,000	-	-	40,127,000	-
Less: Current installments	-	-	(885,000)	(885,000)	-
Long-Term Debt, Net of Current Portion	40,127,000	-	(885,000)	39,242,000	-
Deferred revenue	-	350,000	(32,512)	317,488	17,500
Post-employment health benefit provision	20,799	3,874	-	24,673	-
Health care provision	205,987	(16,008)	-	189,979	-
Non-Current Liabilities	<u>\$ 40,353,786</u>	<u>\$ 337,866</u>	<u>\$ (917,512)</u>	<u>\$ 39,774,140</u>	<u>\$ 902,500</u>

Non-current liabilities activity for the year ending December 31, 2010:

	Balance 1/01/10	Additions/ (Reductions)	Payments/ Amortization/ Reclassifications	Balance 12/31/10	Due Within One Year
Post-employment health benefit provision	\$ -	\$ 20,799	\$ -	\$ 20,799	\$ -
Health care provision	242,391	(36,404)	-	205,987	-
Notes payable to banks	888,000	3,912,000	-	4,800,000	-
Note payable to electric utility	35,327,000	-	-	35,327,000	-
Non-Current Liabilities	<u>\$ 36,457,391</u>	<u>\$ 3,896,395</u>	<u>\$ -</u>	<u>\$ 40,353,786</u>	<u>\$ -</u>

MUSCATINE POWER AND WATER

NOTES TO FINANCIAL STATEMENTS December 31, 2011 and 2010

NOTE 5 – NON-CURRENT LIABILITIES AND DEFERRED REVENUE (cont.)

NON-CURRENT LIABILITIES MATURITY SCHEDULE – COMMUNICATIONS

Communications loan debt service requirements to maturity follow as of December 31, 2011:

Year Ending December 31	Electric Utility Loan			Bank Loans		
	Principal Amount	Interest 3.53%	Total	Principal Amount	Interest 4.7%	Total
2012	\$ -	\$ 623,522	\$ 623,522	\$ 885,000	\$ 204,803	\$ 1,089,803
2013	-	1,247,043	1,247,043	915,000	162,502	1,077,502
2014	-	1,247,043	1,247,043	960,000	118,440	1,078,440
2015	-	1,247,043	1,247,043	1,005,000	72,263	1,077,263
2016 - 2020	3,653,811	5,921,712	9,575,523	1,035,000	24,322	1,059,322
2021 - 2025	4,345,874	5,217,434	9,563,308	-	-	-
2026 - 2030	5,169,020	4,379,758	9,548,778	-	-	-
2031 - 2035	6,148,077	3,383,422	9,531,499	-	-	-
2036 - 2040	7,312,576	2,198,369	9,510,945	-	-	-
2041 - 2045	8,697,642	788,858	9,486,500	-	-	-
Totals	<u>\$ 35,327,000</u>	<u>\$ 26,254,204</u>	<u>\$ 61,581,204</u>	<u>\$ 4,800,000</u>	<u>\$ 582,330</u>	<u>\$ 5,382,330</u>

All communications utility revenues, net of specified operating expenses, are pledged as security of the communications debt until fully paid. Principal and interest paid in 2011 and 2010, and communications utility net revenues are as follows:

	2011	2010
Principal and interest paid	\$ 2,011,383	\$ 665,258
Net revenues	3,486,023	2,748,903

Annual future principal and interest payments are expected to require 56% of communications utility net revenues.

MUSCATINE POWER AND WATER

NOTES TO FINANCIAL STATEMENTS December 31, 2011 and 2010

NOTE 6 – DERIVATIVE INSTRUMENT

The derivative instrument, entered into on September 16, 2010, expired in 2011. Its purpose was to lock in on a price of \$30.00 per MWH for energy that would be purchased to meet native system needs during the Unit 9's scheduled outage from March 1 through April 30, 2011. No money was exchanged in 2010. This contract was evaluated pursuant to GASB No. 53 to determine whether it met the definition of a derivative instrument and if so, whether it effectively hedged the expected fair value associated with commodity price risk exposure. The utilities apply hedge accounting for derivatives that are deemed effective hedges. The derivative instrument was determined to be effective. The fair value of this contract was estimated by comparing the contract price to forward market prices quoted by an independent external pricing service.

The fair value, change in fair value and notional amount of the derivative instrument outstanding at December 31, 2010 is as follows:

Classification	Change in Fair Value	Fair Value	Notional
HEDGING DERIVATIVE INSTRUMENT- ELECTRICITY	\$2,196,100	\$2,196,100	73,200 MWH

Objective and terms of hedging derivative instruments – The objectives and terms of the utilities' hedging derivative instrument that was outstanding at December 31, 2010 is summarized in the table below. The table shows the utilities' trading strategy.

	Notional Amount	Beginning Date	Ending Date	Minimum Price	Maximum Price
Electricity	73,200 mWh	03/1/11	04/30/11	\$23.75	\$36.75

The utility is subject to the following risks when entering into derivative instruments.

Credit risk – Credit risk is the exposure resulting when the counterparty is unable or unwilling to fulfill its present and future financial obligations. The counterparty to this transaction is Tenaska Power Services Co. (TPS); TPS is not publicly rated.

Basis risk – Basis risk is the risk that arises when variable rates or prices of a derivative instrument and a hedged item are based on different reference rates. This transaction has no basis risk.

Termination risk – Termination risk is the risk that a derivative instrument's unscheduled end will affect the utility's asset and liability strategy or will present the utility with potentially unscheduled termination payments to the counterparty. One aspect of termination risk is that the utility would lose the hedging benefit of the derivative that become subject to a termination event. Another termination risk is that if at the time of the termination event the mark to market value of the derivative is a liability that the utility would be required to pay that amount. This transaction had no such termination payment terms.

MUSCATINE POWER AND WATER

NOTES TO FINANCIAL STATEMENTS December 31, 2011 and 2010

NOTE 6 – DERIVATIVE INSTRUMENT (cont.)

Rollover risk – Rollover risk is the risk that a derivative instrument associated with a hedged item does not extend to the maturity of that hedged item. This transaction had no rollover provisions.

Market access risk – Market access risk is the risk that the utility will not be able to enter credit markets or that credit will become more costly. A strong credit rating tends to broaden an entity's credit market access and bond-holder base while achieving lower-cost funding. The utility's unenhanced electric revenue bond rating is indicated as "A+" by Standard & Poor's and Fitch Ratings as of December 31, 2011.

NOTE 7 – NET ASSETS

GASB No. 34 requires the classification of net assets into three components - invested in capital assets, net of related debt; restricted; and unrestricted. These classifications are defined as follows:

Invested in capital assets, net of related debt - This component of net assets consists of capital assets, including restricted capital assets, net of accumulated depreciation and reduced by the outstanding balances of any external bonds, mortgages, notes, or other borrowings that are attributable to the acquisition, construction, or improvement of those assets. If there are significant unspent related debt proceeds at year-end, the portion of the debt attributable to the unspent proceeds are not included in the calculation of invested in capital assets, net of related debt. Rather, that portion of the debt is included in the same net assets component as the unspent proceeds.

Restricted - This component of net assets consists of constraints placed on net asset use through external constraints imposed by creditors (such as through debt covenants), grantors, contributors, or laws or regulations of other governments or constraints imposed by law through constitutional provisions or enabling legislation, including restrictions by the utility's Board of Trustees.

Unrestricted net assets - This component of net assets consists of net assets that do not meet the definition of "restricted" or "invested in capital assets, net of related debt."

When both restricted and unrestricted resources are available for use for the same purpose, it is the utility's policy to use unrestricted resources first (except for principal and interest on debt), then restricted resources as they are needed.

MUSCATINE POWER AND WATER

NOTES TO FINANCIAL STATEMENTS December 31, 2011 and 2010

NOTE 7 – NET ASSETS (cont.)

The following calculation supports the electric net assets invested in capital assets, net of related debt:

	<u>2011</u>	<u>2010</u>
Plant in Service	\$ 406,637,670	\$ 404,829,179
Construction Work in Progress	339,892	242,626
Accumulated Depreciation	<u>(301,325,190)</u>	<u>(291,559,776)</u>
Sub-Totals	<u>105,652,372</u>	<u>113,512,029</u>
Less: Capital Related Debt		
Current portion of capital related long term debt	-	12,585,000
Long-term portion of capital related long term debt	-	13,270,000
Unamortized debt issuance costs	-	(27,283)
Unamortized debt premium	-	73,671
Unamortized loss on advance refunding	<u>-</u>	<u>(72,370)</u>
Sub-Totals	<u>-</u>	<u>25,829,018</u>
Total Net Assets Invested in Capital Assets, Net of Related Debt	<u>\$ 105,652,372</u>	<u>\$ 87,683,011</u>

The following calculation supports the water net assets invested in capital assets:

	<u>2011</u>	<u>2010</u>
Plant in Service	\$ 24,022,226	\$ 23,497,236
Construction Work in Progress	3,170	47,281
Accumulated Depreciation	<u>(9,057,117)</u>	<u>(8,623,443)</u>
Sub-Totals	<u>14,968,279</u>	<u>14,921,074</u>
Less: Capital Related Debt		
Customer advances for construction	1,908,456	1,988,313
Current portion of capital related long term debt	27,000	32,000
Long-term portion of capital related long term debt	<u>247,000</u>	<u>233,096</u>
Sub-Totals	<u>2,182,456</u>	<u>2,253,409</u>
Total Net Assets Invested in Capital Assets	<u>\$ 12,785,823</u>	<u>\$ 12,667,665</u>

MUSCATINE POWER AND WATER

NOTES TO FINANCIAL STATEMENTS December 31, 2011 and 2010

NOTE 7 – NET ASSETS (cont.)

The following calculation supports the communications net assets invested in capital and intangible assets:

	<u>2011</u>	<u>2010</u>
Plant in Service	\$ 30,529,966	\$ 29,035,507
Construction Work in Progress	5,995	70,300
Accumulated Depreciation	<u>(19,496,154)</u>	<u>(17,149,844)</u>
Sub-Totals	<u>11,039,807</u>	<u>11,955,963</u>
Intangible Assets	7,730,912	7,730,912
Accumulated Amortization	<u>(6,957,776)</u>	<u>(6,184,639)</u>
Sub-Totals	<u>773,136</u>	<u>1,546,273</u>
Less: Capital Related Debt		
Current portion of capital related long term debt	885,000	-
Long-term portion of capital related long term debt	3,915,000	4,800,000
Unamortized debt issuance costs	<u>(18,376)</u>	<u>(27,382)</u>
Sub-Totals	<u>4,781,624</u>	<u>4,772,618</u>
Total Net Assets Invested in Capital and Intangible Assets	<u>\$ 7,031,319</u>	<u>\$ 8,729,618</u>

DEFICIT BALANCES

Generally accepted accounting principles require disclosure of individual funds that have deficit balances at year end.

As of December 31, 2011 and 2010 the Communications Utility had a net deficit of \$22.3 million and \$21.2 million, respectively. This deficit is anticipated to be funded with future customer revenues in excess of expenses.

MUSCATINE POWER AND WATER

NOTES TO FINANCIAL STATEMENTS December 31, 2011 and 2010

NOTE 8 – OTHER POSTEMPLOYMENT BENEFITS

The utility's group health insurance plan provides coverage to active employees and retirees (or other qualified terminated employees) at blended premium rates. This coverage results in an other-postemployment benefit (OPEB) for the retirees, commonly referred to as an implicit rate subsidy.

Retirees participating in the plan contribute 100% of the blended premium. The utility, by contributing its portion of the blended premium for active employees, in effect contributes the difference between the blended premium and a retiree age adjusted premium.

For fiscal years 2011 and 2010, the utility contributed \$2,472,000 and \$2,512,000, respectively, to the plan for claim payments plus administrative costs, net of payments received from employees and retirees for premiums.

The following OPEB obligation is based on the actuarial valuation report as of December 31, 2010.

	2011	2010
Annual required contribution	\$ 44,566	\$ 53,581
Interest on net OPEB obligation	10,493	1,392
Adjustment to annual required contribution	(14,586)	(1,935)
Annual OPEB cost	40,473	53,038
Contributions made	(12,600)	(14,400)
Increase in net OPEB obligation	27,873	38,638
Net OPEB Obligation - Beginning of Year	150,721	112,083
Net OPEB Obligation - End of Year	\$ 178,594	\$ 150,721

The utility's annual OPEB cost, the percentage of annual OPEB cost contributed to the plan, and the net OPEB obligation for December 31, 2011 and December 31, 2010 was as follows:

Fiscal Year Ending	Annual OPEB Cost	% of Annual OPEB Cost Contributed	Net OPEB Obligation
12/31/11	\$ 40,473	31%	\$ 178,594
12/31/10	53,038	27%	150,721

MUSCATINE POWER AND WATER

NOTES TO FINANCIAL STATEMENTS December 31, 2011 and 2010

NOTE 8 – OTHER POSTEMPLOYMENT BENEFITS (cont.)

The funded status of the plan as of December 31, 2010, the most recent actuarial valuation date, was as follows:

Actuarial accrued liability (AAL)	\$ 475,530
Actuarial value of plan assets	<u>-</u>
Unfunded Actuarial Accrued Liability (UAAL)	<u>\$ 475,530</u>
Funded ratio (actuarial value of plan assets/AAL)	-
Covered payroll (active plan members)	\$ 18,811,367
UAAL as a percentage of covered payroll	2.5%

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

Projections of benefits for financial reporting purposes are based on the substantive plan (the plan as understood by the employer and plan members) and include the types of benefits provided at the time of each valuation and the historical pattern of sharing benefit costs between the employer and plan members to that point. The methods and assumptions used include techniques that are designed to reduce short-term volatility in actuarial accrued liabilities and the actuarial value of assets, consistent with the long-term perspective of the calculations.

In the actuarial valuation, the projected unit credit actuarial cost method was used. The actuarial assumptions include a 4% investment rate of return and an annual healthcare cost trend rate of 9% initially, reduced by decrements to an ultimate rate of 5% after six years. The plan's unfunded actuarial accrued liability is being amortized as a level percentage of projected payroll on an open basis. The remaining amortization period at December 31, 2010, was 29 years.

MUSCATINE POWER AND WATER

NOTES TO FINANCIAL STATEMENTS December 31, 2011 and 2010

NOTE 9 – PENSION PLAN

The utility provides a defined benefit pension plan with benefits to eligible vested full-time utility and part-time utility employees at separation of service. Eligible employees are those who are not participants in the Iowa Public Employees' Retirement System (IPERS). Participants are 100% vested at the completion of five years of service. Benefits are generally equal to 1.5% of the employee's average highest five consecutive years of compensation (Average Compensation) multiplied by credited years of service. An additional benefit is available in an amount equal to 0.5% of the employee's Average Compensation in excess of Social Security Covered Compensation, if any, multiplied by credited years of service, up to 35 years. Benefit provisions are established under the Muscatine Water and Electric Employees' Pension Plan as adopted by the utility's Board of Trustees. The funding is approved by the utility's Board of Trustees.

The annual pension costs of \$2,236,473 for 2011; \$1,933,274 for 2010; \$1,670,289 for 2009; and \$1,104,964 for 2008; (including MAGIC-see note 16) were equal both to the utility's annual required contribution and actual contributions made by the utility. Accordingly, the utility has no net pension obligation at December 31, 2011. The electric, water, and communications utilities' portions of the 2011 Plan contribution were \$1,856,460, \$97,882, and \$267,302, respectively

The annual required contribution is equal to normal cost plus level-dollar amortization of unfunded actuarial accrued liability over 20 years. The annual required contribution for 2011 was determined as part of the January 1, 2011 actuarial valuation using the projected unit credit cost method. The actuarial assumptions included; (a) a 7.75% investment rate of return (net of administrative expenses), (b) projected salary increases of 5.0%, and (c) the later of attained age of 65 or 5 years of plan participation. The utility's actuary issues an annual Financial Accounting Disclosure Report to fulfill the reporting requirements of these financial statement notes as required by the Governmental Accounting Standards Board.

Six –Year Trend Information for the entire Plan (including MAGIC employees):

<u>Fiscal Year Ending</u>	<u>Annual Required Cost (ARC)</u>	<u>% of ARC Contributed</u>	<u>Net Pension Obligation</u>
12/31/06	\$ 882,170	100	\$ -
12/31/07	979,179	100	-
12/31/08	1,104,964	100	-
12/31/09	1,670,289	100	-
12/31/10	1,933,274	100	-
12/31/11	2,236,473	100	-

MUSCATINE POWER AND WATER

NOTES TO FINANCIAL STATEMENTS December 31, 2011 and 2010

NOTE 9 – PENSION PLAN (cont.)

Schedule of Funding Progress of the entire Plan (including MAGIC employees):

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Liability (AAL) (b)	Unfunded (Overfunded) AAL (UAAL/OAAL) (b-a)	Funded Ratio (a/b)	Annual Covered Payroll (c)	UAAL/OAAL as a Percentage of Covered Payroll ((b-a)/c)
01/01/06	\$ 35,065,410	\$ 32,739,278	\$ (2,326,132)	107.1%	\$ 15,947,709	(14.6)%
01/01/07	38,984,729	36,020,200	(2,964,529)	108.2	17,216,510	(17.2)
01/01/08	42,579,530	38,845,371	(3,734,159)	109.6	17,770,750	(21.0)
01/01/09	41,901,750	43,004,091	1,102,341	97.4	18,811,367	5.9
01/01/10	41,554,008	44,893,762	3,339,754	92.6	18,760,186	17.8
01/01/11	42,035,773	48,101,789	6,066,016	87.4	19,310,355	31.4

The water utility also contributes to IPERS for full time utility employees who have elected not to participate in the Plan provided by the utility. IPERS is a cost-sharing multi-employer defined benefit pension plan administered by the State of Iowa. IPERS provides retirement and death benefits which are established by State statute to plan members and beneficiaries. IPERS issues a publicly available financial report that includes financial statements and required supplementary information. The report may be obtained by writing to IPERS, P.O. Box 9117, Des Moines, Iowa, 50306-9117.

IPERS members were required to contribute 4.3% through June 30, 2010; 4.5% from July 1, 2010 through June 30, 2011; and 5.38% beginning July 1, 2011 of their annual covered salary and the utility was required to contribute 6.65% through June 30, 2010; 6.95% from July 1, 2010 through June 30, 2011; and 8.07% beginning July 1, 2011 of employees' covered salary. Contribution requirements are established by State statute. The utility's contributions to IPERS for the years ended December 31, 2011 and 2010 were \$48,018 and \$39,764, respectively, equal to the required contributions for those years.

NOTE 10 – SIGNIFICANT CUSTOMERS

Approximately \$25,290,000 or 28% in 2011 and \$26,044,000 or 27% in 2010 of the electric utility's operating revenues were derived from sales to one customer. Approximately \$2,035,000 or 46% in 2011 and \$1,918,000 or 45% in 2010 of the water utility's operating revenues were derived from sales to one customer.

MUSCATINE POWER AND WATER

NOTES TO FINANCIAL STATEMENTS December 31, 2011 and 2010

NOTE 11 – COMMITMENTS AND CONTINGENCIES

The utility has committed to purchasing 250,000 tons of coal in 2012 on the spot market under five different contracts with four different suppliers.

The utility has rail transportation agreements with two separate companies for the delivery of coal through December 31, 2017 and December 31, 2016. The utility's first agreement is for coal shipped from the Powder River Basin (PRB), Wyoming to an interchange with the local delivery carrier. The contract term is from July 1, 2011 through December 31, 2017 where the rate is adjusted quarterly beginning January 2012 plus monthly fuel surcharges. The utility's minimum requirement is 100% of the tons shipped from the PRB up to the utility's annual tonnage nomination. In the event the utility does not meet their nominated tons, the utility has agreed to pay a per ton penalty for the shortfall.

Shipment of coal from the interchange point to the utility's generating station is covered by one agreement that expires 12/31/2012 and another that begins January 1, 2013 and expires December 31, 2016. The first agreement covers the shipment of coal from the interchange to the utility's electric generating station. The contract rate is determined by the interchange that the train travels through, and is adjusted quarterly. There is no annual minimum tonnage requirement. The second rail agreement covers the shipment of coal from the interchange to the utility's electric generating station. The contract rate is adjusted quarterly. There is no minimum annual shipping requirement; however, the utility will nominate their needs by November 1 of the preceding year. In the event the utility does not meet their nominated tons, the utility has agreed to pay a per ton penalty for the shortfall.

The utility has contracted to sell steam to a local customer. The ten-year agreement began July 1, 2000. The customer is obligated to take a minimum annual quantity of steam each year (2,338,920 kilo pounds). The contract was amended in 2007 to add an additional ten years to the agreement. The amendment obligates the customer to certain environmental capital costs (approximately \$2 million) and ongoing SO₂, NO_x and mercury emission allowance costs. If the contract is cancelled during the amendment period, the customer has agreed to reimburse the utility for any of the unrecovered environmental capital costs.

The utility has Board-approved open contracts for approximately \$174,000. As of December 31, 2011, approximately \$169,000 of this amount has been expended.

NOTE 12 – ENVIRONMENTAL REGULATIONS

All generating units are in compliance with current state and federal regulations. Management anticipates that any additional costs incurred related to on-going compliance with current or new environmental regulations will be recovered through rates charged to its customers.

MUSCATINE POWER AND WATER

NOTES TO FINANCIAL STATEMENTS December 31, 2011 and 2010

NOTE 13 – INTERFUND AND RELATED PARTY TRANSACTIONS

The electric utility sold power to the water utility amounting to approximately \$728,500 in 2011 and \$764,500 in 2010. The electric utility sold power to the communications utility amounting to approximately \$17,000 in 2011 and \$16,000 in 2010. The electric utility purchased water from the water utility amounting to approximately \$330,800 and \$322,700 for 2011 and 2010, respectively. The electric utility purchased communications services from the communications utility amounting to approximately \$165,400 for 2011 and \$168,900 for 2010, and advertising amounting to \$8,900 and \$4,800 in 2011 and 2010, respectively.

The electric utility rents space to the water utility and the communications utility at the Administration/Operations Center. This amounted to \$62,916 in 2011 and \$75,576 in 2010 for the water utility's rent, and \$95,424 in 2011 and \$114,636 in 2010 for the communications utility's rent.

Electric utility amounts receivable from the water utility were \$67,593 and \$64,516 at December 31, 2011 and 2010, respectively. Electric utility amounts payable to the water utility were \$28,836 and \$26,681 at December 31, 2011 and 2010, respectively. Electric utility amounts receivable from the communications utility were \$17,605 and \$16,228 at December 31, 2011 and 2010, respectively. Electric utility amounts payable to the communications utility were \$13,846 and \$875 at December 31, 2011 and 2010, respectively.

Prior to 2002, the electric utility loaned the communications utility \$21,400,000 for the financing of the initial construction and operation of the communications utility. Prior to July 1, 2004 additional amounts totaling \$13,927,000 were approved for the financing of the expansion of the communications utility, increasing the total loan to \$35,327,000.

Effective November 28, 2006, the interest rate was fixed at 3.53% beginning January 1, 2007 by action of the Board. Semi-annual payments of interest only are due each January 1 and July 1. A Board resolution, which passed November 25, 2008, approved an annual principal repayment schedule, with payments beginning January 1, 2016. This debt as to both principal and interest is and shall be junior and subordinate in all respects to the bank loans and interest thereon during the term of the bank loan agreement.

All or any portion of such loan may be prepaid at any time by the communications utility without penalty.

At December 31, 2011 and 2010, electric utility interest receivable from the communications utility was \$0 and \$623,522, respectively. Interest income on the loan amounted to \$1,247,043 for 2011 and 2010.

Costs incurred on a combined basis among the utilities are allocated to each utility on the basis of revenues, utility plant in service, labor expense, and/or number of customers.

Members of the Board of Trustees are also officers of companies that are customers of the utility. Most employees are also customers of the utility.

MUSCATINE POWER AND WATER

NOTES TO FINANCIAL STATEMENTS December 31, 2011 and 2010

NOTE 14 – ACQUISITION

On January 3, 2003, the utility acquired a cable television system and the related assets serving subscribers in and around the Cities of Muscatine and Fruitland, Iowa at a price of \$9,000,000. Of this amount, \$7.7 million was considered an intangible asset and is being amortized over 10 years, ending in 2012.

NOTE 15 – RISK MANAGEMENT

The utility is exposed to various risks of loss related to destruction of assets and natural disasters. The utility is also exposed to various risks of loss relating to torts, errors and omissions, health, and injuries to employees. The utility purchases commercial insurance for claims related to these risks subject to certain deductibles. Open claims and an estimate for incurred but not reported claims are accrued up to deductible limits. Settled claims have not exceeded reserves in the last three years. There were no significant reductions in coverage compared to the prior year.

<i>(Thousands of dollars)</i>	<u>2011</u>	<u>2010</u>
Health/dental care self insurance reserve		
Reserve liability, beginning of year	\$ 2,518	\$ 2,687
Add: Provision for reserve, current year	3,201	3,223
Less: Payments on reserve	<u>(3,262)</u>	<u>(3,392)</u>
Total Reserve Liability, end of year	2,457	2,518
Incurred but not reported claims	<u>(251)</u>	<u>(298)</u>
 Non-Current Reserve Liability, End of Year	 <u>\$ 2,206</u>	 <u>\$ 2,220</u>
 <i>(Thousands of dollars)</i>	 <u>2011</u>	 <u>2010</u>
Workers compensation self insurance reserve		
Reserve liability, beginning of year	\$ 279	\$ 144
Add: Provision for reserve	190	333
Less: Payments on reserve	<u>(261)</u>	<u>(198)</u>
 Reserve Liability, End of Year	 <u>\$ 208</u>	 <u>\$ 279</u>

MUSCATINE POWER AND WATER

NOTES TO FINANCIAL STATEMENTS December 31, 2011 and 2010

NOTE 16 – JOINT VENTURE

The utility is a member organization along with the City of Muscatine and the County of Muscatine in a joint venture under Chapter 28E of the Iowa Code to operate the Muscatine Area Geographic Information Consortium (MAGIC). The purpose of MAGIC is to improve the efficiency and effectiveness of its member organizations through the coordinated development of geographic and land information systems technology and data. MAGIC is governed by a six-member board composed of two appointees from each member organization. Each member organization has one vote on all matters. MAGIC's board determines the funding required by each member organization. Upon dissolution of the joint venture, the net assets of MAGIC will be distributed on a prorata basis based on funding. Complete financial statements for MAGIC can be obtained from the Muscatine Power and Water Administration/Operations Center, 3205 Cedar Street, Muscatine, Iowa 52761.

The utility accounts for this investment under the equity method since it has the ability to exercise significant influence over the joint venture and it has an explicit equity interest in the joint venture. The utility has rights to the information systems technology and data and the cost of such rights are amortized over their expected average useful life of 26 years. The utility's share of MAGIC's operating expenses is expensed as incurred.

NOTE 17 – SUBSEQUENT EVENTS

ELECTRIC RATES

In April 2011, a 5% electric rate increase was approved by the Board to become effective August 1, 2012.

WATER RATES

In November 2011, a 5% water rate increase was approved by the Board to become effective with water usage starting April 1, 2012.

COMMUNICATIONS RATES

In November 2011, a communications utility cable television rate adjustment of 2.4% and 2.6%, respectively, for MPW Basic service and MPW Digital TV Select service was approved by the Board to become effective January 1, 2012. In addition, the Board approved rate adjustments of between 1.6% and 2.2% for Internet services effective January 1, 2012.

REQUIRED SUPPLEMENTAL INFORMATION

MUSCATINE POWER AND WATER

REQUIRED SUPPLEMENTARY INFORMATION
SCHEDULE OF FUNDING PROGRESS - PENSION PLAN
December 31, 2011
(UNAUDITED)

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) (b)	Unfunded (Overfunded) AAL (UAAL/OAAL) (b-a)	Funded Ratio (a/b)	Annual Covered Payroll (c)	UAAL/OAAL as a Percentage of Covered Payroll ((b-a)/c)
01/01/06	\$ 35,065,410	\$ 32,739,278	\$ (2,326,132)	107.1%	\$ 15,947,709	(14.6)%
01/01/07	38,984,729	36,020,200	(2,964,529)	108.2	17,216,510	(17.2)
01/01/08	42,579,530	38,845,371	(3,734,159)	109.6	17,770,750	(21.0)
01/01/09	41,901,750	43,004,091	1,102,341	97.4	18,811,367	5.9
01/01/10	41,554,008	44,893,762	3,339,754	92.6	18,760,186	17.8
01/01/11	42,035,773	48,101,789	6,066,016	87.4	19,310,355	31.4

REQUIRED SUPPLEMENTARY INFORMATION
SCHEDULE OF FUNDING PROGRESS - OPEB PLAN
December 31, 2011
(UNAUDITED)

Actuarial Valuation Date*	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) (b)	Unfunded (Overfunded) AAL (UAAL/OAAL) (b-a)	Funded Ratio (a/b)	Annual Covered Payroll (c)	UAAL/OAAL as a Percentage of Covered Payroll ((b-a)/c)
12/31/08	\$ -	\$ 430,836	\$ 430,836	0%	\$ 18,811,367	2.3%
12/31/10	-	475,530	475,530	0	19,310,355	2.5

*The utility plans to have actuarial valuations performed every other year as required by GASB 45.

INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL
OVER FINANCIAL REPORTING AND ON COMPLIANCE AND
OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS
PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*

To the Board of Water, Electric and Communications Trustees
Muscatine Power and Water
Muscatine, Iowa

We have audited the financial statements of Muscatine Power and Water as of and for the year ended December 31, 2011, and have issued our report thereon dated March 22, 2012. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

Management of Muscatine Power and Water is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered Muscatine Power and Water's internal control over financial reporting as a basis for designing our audit procedures for the purpose of expressing an opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of Muscatine Power and Water's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of Muscatine Power and Water's internal control over financial reporting.

Our consideration of the internal control over financial reporting was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses and, therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined below.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A material weakness is a deficiency, or combination of deficiencies, in internal controls such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

To the Board of Water, Electric and Communications Trustees
Muscatine Power and Water
Muscatine, Iowa

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the financial statements of Muscatine Power and Water are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

This report is intended solely for the information and use of utility management, others within the entity, federal and state awarding agencies and pass-through entities and is not intended to be, and should not be, used by anyone other than these specified parties.

Baker Tilly Virchow Krause, LLP

Madison, Wisconsin
March 22, 2012

MUSCATINE POWER AND WATER

SCHEDULE OF FINDINGS RELATED TO GOVERNMENT AUDITING STANDARDS AND REQUIRED STATUTORY REPORTING Year Ended December 31, 2011

FINDINGS RELATED TO REQUIRED STATUTORY REPORTING

- A-02 Official Depositories – A resolution naming official depositories has been approved by the utility. The maximum deposit amounts stated in the resolution were not exceeded during the year ended December 31, 2011.
- B-02 Certified Budget – Disbursements during the year ended December 31, 2011, did not exceed the amounts budgeted.
- C-02 Questionable Disbursements – No disbursements that we believe may not meet the requirements of public purpose as defined in an Attorney General's opinion dated April 25, 1979 were noted.
- D-02 Travel Expense – No disbursements of utility money for travel expenses of spouses of city officials or employees were noted.
- E-02 Business Transactions – No business transactions between the utility and utility officials or employees were noted.
- F-02 Bond Coverage – Surety bond coverage of city officials and employees is in accordance with statutory provisions. The amount of coverage should be reviewed annually to ensure that coverage is adequate for current operations.
- G-02 Board Minutes – No transactions were found that we believe should have been approved in the Board minutes but were not.
- H-02 Deposits and Investments – No instances of non-compliance with the deposit and investment provisions of Chapter 12B and 12C of the Code of Iowa and the utility's investment policy were noted.
- I-02 Revenue Bonds – The utility has complied with all provisions of the Revenue Electric Bond Covenants. All required payments to the sinking, reserve and improvement funds were made.
- J-02 Code of Iowa Communications Legislation Requirements – Nothing came to our attention that the utility was not in compliance with the requirements of the Code of Iowa Section 388.10 *Municipal Utility Providing Telecommunications Services* regarding the subsidization of telecommunications operations by the electric and water utilities.
- K-02 The audit identified the following material weakness:
 No material weaknesses were noted during the audit.

SUPPLEMENTAL INFORMATION

MUSCATINE POWER AND WATER

Schedule of Insurance Coverage

December 31, 2011

Insurer	Type of Coverage	Policy's Expiration Date	Amount of Coverage	
FM Global Insurance Company	All risks:	4/1/2012		
	Named locations		\$705,000,000	Blanket
	Gross earnings-Communications Utility		Included in Blanket	
	Acts of terrorism - certified		Included in Blanket	
	Accounts receivable		\$100,000,000	
	Debris removal		\$100,000,000	
	Demolition & increased cost of construction		\$100,000,000	
	Earth movement		\$100,000,000	
	Errors and omissions		\$100,000,000	
	Fine arts		\$100,000,000	
	Flood		\$100,000,000	
	Automatic coverage (90 days)		\$100,000,000	
	Valuable papers and records		\$100,000,000	
	Data programs or software and computer systems		\$10,000,000	
	Decontamination costs		\$10,000,000	
	Expediting expense and extra expense		\$10,000,000	
	Ingress/egress (30 days)		\$10,000,000	
	Miscellaneous unnamed locations		\$10,000,000	
	Soft costs		\$10,000,000	
	Transportation		\$10,000,000	
	Logistics Extra Cost		\$5,000,000	
	Railroad rolling stock		\$5,000,000	ACV
	Mobile equipment (FKA contractors equipment)		\$3,500,000	ACV
	Land and water cleanup		\$50,000	
Cincinnati Insurance Company	Money & Securities	4/1/2012	100,000	No deductible
Cincinnati Insurance Company	Blanket Fidelity Bond, All Employees except Treasurer	4/1/2012	250,000	No deductible
Cincinnati Insurance Company	Treasurer's Bond	4/1/2012	250,000	No deductible

MUSCATINE POWER AND WATER

Schedule of Insurance Coverage (cont.)

December 31, 2011

Insurer	Type of Coverage	Policy's Expiration Date	Amount of Coverage		
AEGIS	Excess liability: Automobile liability Product liability and completed operations Failure to supply Pollution liability Medical malpractice Emergency assistance agreements Joint venture liability (pro rata ownership) Employers liability Standards board activity Community service activity Employment practices (12/31/98 retroactive date)	12/31/2011	\$ 35,000,000	\$ 1,000,000	Retention
			\$500,000 SIR each claimant; \$1,000,000 SIR each occurrence		
Federal Insurance Company Chubb Group of Insurance Companies	Fiduciary & employee benefit liability	12/31/2011	10,000,000	250,000	Retention
Travelers Casualty & Surety Company of America	Excess fiduciary & employee benefit liability	12/31/2011	10,000,000	250,000	Retention
Midwest Employers Casualty Company	Excess workers compensation	12/31/2011	Statutory	1,250,000	Each accident SIR