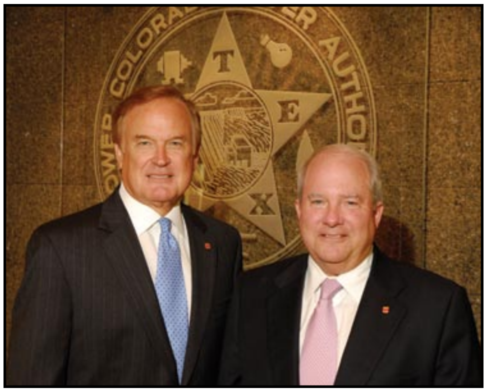
Public Service that Improves the Quality of Life for the People of Texas

Annual Report – Fiscal Year 2006

The mission of the Lower Colorado River Authority (LCRA) is to provide reliable, low-cost utility and public services in partnership with our customers and communities and to use our leadership role and environmental authority to ensure the protection and constructive use of the area's natural resources.

LCRA is a Texas conservation and reclamation district operating with no taxing authority.

The Board of Directors is composed of 15 members appointed by the governor. Directors represent counties in the electric and water service areas. The directors meet regularly to set strategic corporate direction for the general manager and the staff, to approve projects and large expenditures, and to review progress on major activities and industry issues.



Message from Our Leadership

Growth in Central Texas continues to provide opportunities and challenges for the communities and customers served by the Lower Colorado River Authority. In turn, LCRA continues to respond to those growing needs in every area of its business, from planning for future water supply and power generation and transmission needs to helping protect the river and conserve the resources that LCRA was created to manage.

Fiscal year 2006 was a solid financial year for LCRA, with revenues from its electric, water and community services operations exceeding $1 billion, up about 26.8 percent from FY 2005 operating revenues of $803.4 million. Operating expenses of $882.5 million in FY 2006 were up by about 29.51 percent from FY 2005's $681.3 million, due largely to increased fuel costs. LCRA and its affiliates ended the year with debt service coverage of 1.48, compared to 1.42 in FY 2005.

LCRA continued to invest in critical utility infrastructure in a growing region, adapting schedules and budgets to an environment of increasing costs and reduced contractor availability. Net capital assets grew by $188.2 million in FY 2006. Of $305.6 million in capital expenditures, $203.4 million went to improving the reliability, safety and functionality of the electric power transmission grid that serves most of Texas. The LCRA Board in FY 2006 also committed to invest $144.3 million in sulfur-scrubbing technology over several years to reduce emissions from its coal-fired power plant, an essential, cost-effective component of its diverse power generation fleet.

With an eye on the future, LCRA worked this past year with communities throughout its service area to begin planning for anticipated growth along new Central Texas transportation corridors. Studies continued for a significant water conservation and development project that would ensure a reliable water supply for the region well beyond the 50-year planning horizon. It also continued to work with its 43 wholesale electric customers to determine future relationships, and 27 customers have committed so far to buy energy from LCRA through 2041.

LCRA Transmission Services Corporation, the nonprofit corporation that owns and develops LCRA transmission assets, worked closely with the Public Utility Commission of Texas during FY 2006 to review its financial practices and help ensure future success. LCRA also took significant steps in FY 2006 to help improve the long-term financial outlook for its young and growing water and wastewater utility business.

Continuing drought in the region helped area residents recognize the value and importance of the Highland Lakes and LCRA's role in protecting and conserving the lower Colorado River, where water quality remained high. LCRA also updated and tested emergency response plans throughout the organization and broke ground on a new state-of-the-art emergency operations center.

LCRA's nature parks and natural science centers continued to provide educational and outdoor recreation programs that support its environmental stewardship mission while enhancing area economies. LCRA's McKinney Roughs Nature Park in Bastrop County immediately saw significant growth in visitors following the addition of a destination resort adjoining the property, and LCRA continued to make progress on completing key facilities at its Matagorda Bay Nature Park on the Gulf of Mexico. Communities also benefited from strategic planning, leadership development and other services that support local economic development efforts.

FY 2006 was an active and growing year for LCRA and its affiliates, and the organization continued to take many steps that will benefit the region and Texas well into the future.

Ray A. Wilkerson, Board Chair

Joseph J. Beal, P.E., General Manager

LOWER COLORADO RIVER AUTHORITY

FINANCIAL STATEMENTS

YEARS ENDED
JUNE 30, 2006 AND 2005

**With Independent Auditors'
Report**

Report of Management

The management's discussion and analysis, the financial statements and related footnotes included herein are the responsibility of LCRA's management as is other information contained in this annual report. The financial statements are prepared in conformity with generally accepted accounting principals applied on a consistent basis and, in some cases, reflect amounts based on the best estimates and judgments of management, giving due consideration to materiality. Financial information contained elsewhere in this annual report is consistent with that in the financial statements.

Management has developed and maintains a system of accounting and controls, including an internal audit program, designed to provide reasonable assurance that LCRA's assets are protected from improper use and that accounting records provide a reliable basis for the preparation of financial statements. This system is continually reviewed, improved and modified in response to changing business conditions and operations and to recommendations made by the independent auditors and the internal auditors. Due to the inherent limitations of the effectiveness of internal controls, no internal control system can provide absolute assurance that errors and irregularities will not occur. However, management strives to maintain a balance, recognizing that the cost of such a system should not exceed the benefits derived.

LCRA's Board of Directors, appointed by the governor of Texas, oversees LCRA's financial reporting activities through the Audit Committee and Finance and Administration Committee, which are comprised wholly of Board members. The duties of these committees include keeping informed of the financial condition of the LCRA and reviewing its financial policies and procedures, its internal accounting controls, and the objectivity of its financial reporting. Both LCRA's independent and internal auditors may meet directly with the Audit Committee without management concurrence.

The Independent Auditors' Report, included herein, does not limit the responsibility of management for information in the financial statements and elsewhere in the annual report.

Deputy General Manager Chief Financial Officer	Controller	General Manager

Management's Discussion and Analysis

Condensed Balance Sheets

	June 30, 2006	June 30, 2005	June 30, 2004
	(Dollars in Thousands)		
Current assets	$ 386,420	$ 320,935	$ 319,204
Capital assets, net	2,464,871	2,276,623	2,147,019
Other long-term assets	511,772	523,687	476,068
Total Assets	$ 3,363,063	$ 3,121,245	$ 2,942,291
Current liabilities	$ 341,527	$ 442,994	$ 398,237
Long-term liabilities	2,297,207	1,980,167	1,887,402
Total Liabilities	2,638,734	2,423,161	2,285,639
Equity - Invested in capital assets, net of related debt	568,812	533,645	501,613
Equity - Restricted other	29,551	36,467	25,315
Equity - Unrestricted	125,966	127,972	129,724
Total Equity	724,329	698,084	656,652
Total Liabilities and Equity	$ 3,363,063	$ 3,121,245	$ 2,942,291

Condensed Statements of Revenues, Expenses and Changes in Equity

	Year Ended June 30,		
	2006	2005	2004
	(Dollars in Thousands)		
Operating revenues	$ 1,018,684	$ 803,425	$ 693,632
Operating expenses	(882,539)	(681,271)	(598,253)
Operating income	136,145	122,154	95,379
Interest and other income	14,878	14,360	4,858
Interest and other expenses	(120,917)	(120,217)	(100,386)
(Prior costs) costs to be recovered from revenues	(13,715)	17,923	29,715
Income before capital contributions	16,391	34,220	29,566
Capital contributions	11,304	7,212	4,789
Special item - Loss on early defeasance of debt	(1,450)	-	-
Change in equity	26,245	41,432	34,355
Equity, Beginning of Year	698,084	656,652	622,297
Equity, End of Year	$ 724,329	$ 698,084	$ 656,652

Financial Highlights

Current assets increased $65.5 million or 20 percent for fiscal year (FY) 2006. LCRA has increased cash and cash equivalents by $34.7 million in order to have sufficient cash on hand to cover higher gas and purchased power payments in FY 2006. An increase in net receivables of $30.4 million was a result of higher sales to customers as well as higher rates to capture increased fuel costs.

Net capital assets increased $188.2 million or 8 percent for FY 2006, and $129.6 million or 6 percent in FY 2005. The increase in both fiscal years is due primarily to the acquisition and construction of transmission facilities to meet increasing demand for these services. Net utility plant also increased $1.4 million because of asset retirement obligations that were recorded in FY 2006 for potential legal and environmental costs (for additional detail see Note 8 of Notes to the Financial Statements).

In FY 2005, other long term assets increased $47.6 million or 10 percent due to an increase in construction funds and an increase in the balance of costs to be recovered from future revenues that are related to the recent rapid expansion of capital assets.

Current liabilities decreased $101.5 million or 23 percent and long-term liabilities increased by $317 million or 16 percent for FY 2006 primarily due to the issuance of several revenue bonds to refund tax exempt commercial paper.

Operating revenues for FY 2006 increased $215.3 million or 27 percent due to higher electric revenues from an increase in sales and higher fuel costs. LCRA was able to meet increased customer energy demand which resulted in higher sales. In addition, higher fuel revenues resulted from passing on increases in the cost of fuel to customers.

Operating expenses for FY 2006 increased $201.3 million or 30 percent primarily because of higher fuel and purchased power costs. Additionally, greater sales translated to an increase in fuel and purchase power costs.

Interest and other income increased by $9.5 million or 196 percent in FY 2005 primarily due to favorable changes in the fair value of investments and high average investment balances in FY 2005.

(Prior costs) costs to be recovered from future revenues decreased $31.6 million and $11.8 million in FY 2006 and FY 2005 respectively, as more costs were recovered through rates each year compared to the previous year.

In FY 2006, $1.5 million was recorded in Special item due to a loss on an early defeasance of debt. No such activity occurred in FY 2005.

Overview of the Financial Statements

In accordance with Governmental Accounting Standards Board Statement No. 34, "Basic Financial Statements – Management's Discussion and Analysis – for State and Local Governments," LCRA is considered a special-purpose government engaged only in business-type activities. Statement No. 34 requires the following components in a governmental entity's annual report:

Management's Discussion and Analysis

The purpose is to provide an objective and easily readable analysis of the government's financial activities based on currently known facts, decisions or conditions.

Balance Sheet

Assets and liabilities of proprietary funds should be presented to distinguish between current and long-term assets and liabilities.

Statement of Revenues, Expenses and Changes in Equity

This statement provides the operating results broken into the categories of operating revenues and expenses, nonoperating revenues and expenses, and capital contributions.

Notes to the Financial Statements

The notes explain information in the financial statements and provide additional detailed information.

Competition

Senate Bill 7 (SB 7) provided for retail electric competition to open Jan. 1, 2002. Retail customers of investor-owned utilities and retail customers of municipally owned utilities and electric cooperatives that elect to participate in retail competition now can choose their electric provider.

Regulatory Matters

LCRA Transmission Services Corporation

In order to promote electric competition, SB 7 requires all transmission system owners to make their transmission systems available for use by others at prices and terms comparable to each respective owner's use of its system for its own wholesale transactions. Pursuant to the requirements of SB 7, in January 2002 LCRA transferred its existing electric transmission and transformation facilities to LCRA Transmission Services Corporation (LCRA TSC), a component unit of LCRA for accounting purposes. LCRA TSC owns and operates all of LCRA's regulated electric transmission and transformation assets. In accordance with accounting and financial reporting requirements, the assets, liabilities and transactions of LCRA TSC are included in the financial statements of LCRA.

Transmission Cost of Service Rates

FY 2005 transmission revenues of $142.7 million resulted from a rate of $2.55 per kW as a result of PUC commissioners approving an LCRA TSC rate case on May 15, 2005. This rate was retroactively effective for all of FY 2005.

FY 2006 transmission revenues of $156 million are the result of rate changes authorized during the fiscal year. The predominant rate of $2.77 per kW was in place from Sept. 26, 2005 through June 30, 2006. LCRA TSC filed an interim update of wholesale transmission rates with the PUC on July 25, 2005, and the PUC Commissioners approved the new rate of $2.77 per kW on Sept. 26, 2005.

LCRA TSC filed an interim update of wholesale transmission rates with the PUC on July 25, 2006. The filing, Docket No. 32987, was approved by the PUC Commissioners on Sept. 21, 2006. The approved rate is $2.88 per kW, effective as of Sept. 21, 2006.

Capital Expansion and Improvement Program

LCRA's capital improvement program for FY 2007 through FY 2011 is $1.3 billion, with $868 million or 67 percent to be debt funded. The majority of forecasted capital expenditures is for expansion of transmission services, water and wastewater services and generation improvements as well as additional corporate infrastructure and facilities. LCRA TSC continues to increase its transmission system investment due to the need for additional electric transmission capability statewide. LCRA will continue its water and wastewater services capital expansion due to the region's growing population.

The capital budget is expected to be applied as follows:

(1) $468 million for transmission projects.
(2) $411 million for generation and system improvements.
(3) $278 million for dam improvements and modernization, and acquisition and construction of water and wastewater utilities and facilities.
(4) $114 million for parks and corporate facilities.

LCRA's forecasted capital program includes $144.3 million for LCRA's share of the installation of SO_2 scrubbers for two coal-fired generating units jointly owned by LCRA and the City of Austin. The cost of the scrubbers is subject to revision upon the completion of technological evaluations and detailed engineering studies. The scrubbers must be installed by October 2012, under the provisions of a flexible air quality permit received from the Texas Commission on Environmental Quality in 2002.

The capital program will be funded by cash provided by operating activities and proceeds from long-term bond (including LCRA bonds and LCRA bonds issued on behalf of LCRA TSC) and commercial paper issuances.

The forecasted capital program is subject to periodic review and revision and may change significantly because of a number of factors including economic conditions and regulatory constraints.

Capital Asset Activity

- $305.6 million was expended for construction activities in FY 2006. The majority of these expenditures were for acquisition and construction of transmission facilities to meet increasing demand for these services.

- $2.5 million of Asset Retirement Obligations were recorded in FY 2006 for potential legal and environmental costs of future plant retirements.

- $119.9 million of depreciation expense and asset retirements were recorded in FY 2006 on plant in service.

- For additional detail, see Capital Asset Activity table in Note 7 of the Notes to the Financial Statements.

Debt Activity

- On Aug. 16, 2005, LCRA on behalf of LCRA TSC issued $126.1 million of Transmission Contract Refunding Revenue Bonds, Series 2005. The proceeds from the issue were used to refund $120 million of tax-exempt commercial paper.

- On May 25, 2006, LCRA issued $80.3 million of tax-exempt Refunding Revenue Bonds, Series 2006. In addition, LCRA on behalf of LCRA TSC issued $135.9 million of Transmission Contract Refunding Revenue Bonds, Series 2006. The proceeds from the bond issues were used to refund tax-exempt commercial paper.

- During FY 2006, LCRA issued $6.6 million of taxable commercial paper and $59.1 million of tax-exempt commercial paper. In addition, LCRA on behalf of LCRA TSC issued $145 million of tax-exempt commercial paper.

- On May 9, 2006, LCRA defeased approximately $9.7 million from various bond series.

- On April 26, 2006, LCRA on behalf of LCRA TSC defeased approximately $9.6 million from the LCRA TSC Series 2003B and LCRA TSC Series 2003C Contract Refunding Revenue Bonds.

- In FY 2006, LCRA made scheduled principal payments in the amount of $60 million.

- For additional detail, see Note 4 of the Notes to the Financial Statements.

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INDEPENDENT AUDITOR'S REPORT

To the Board of Directors
Lower Colorado River Authority
Austin, Texas

We have audited the accompanying balance sheets of the Lower Colorado River Authority ("LCRA") as of June 30, 2006 and 2005, and the related statements of revenues, expenses and changes in equity, and of cash flows for the years then ended. These financial statements are the responsibility of the LCRA's 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. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the LCRA's internal control over financial reporting. Accordingly, we express no such opinion. 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 above present fairly, in all material respects, the financial position of the LCRA as of June 30, 2006 and 2005, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 8 to the consolidated financial statements, on June 30, 2006, the LCRA changed its method of accounting for conditional asset retirement obligations.

Management's Discussion and Analysis is not a required part of the basic financial statements but is supplementary information required by GASB. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Deloitte & Touche LLP

October 13, 2006

LOWER COLORADO RIVER AUTHORITY
BALANCE SHEETS
(Dollars in Thousands)

	June 30, 2006	June 30, 2005
Assets		
Current Assets		
Cash and cash equivalents	$ 83,574	$ 48,828
Investments	63,972	79,436
Receivables, net	137,638	107,193
Accrued interest receivable	661	981
Inventories	97,626	82,192
Other	2,949	2,305
Total current assets	386,420	320,935
Long-Term Assets		
Restricted cash and cash equivalents	14,245	28,697
Restricted investments	56,901	55,582
Unrestricted investments	47,946	56,146
Capital assets:		
Utility plant in service	3,331,293	3,072,798
Construction work in progress	209,008	208,184
Oil and gas property	28,158	28,158
Other physical property	47,348	42,435
Less accumulated depreciation	(1,150,936)	(1,074,952)
Capital assets, net	2,464,871	2,276,623
Water rights, net	87,397	86,387
Other	10,219	9,383
Deferred charges:		
Costs to be recovered from future revenues	224,844	226,122
Unamortized debt expense	31,253	28,424
Contract extension settlement with major customers	8,132	8,907
Other	30,835	24,039
Deferred charges, net	295,064	287,492
Total long-term assets	2,976,643	2,800,310
Total Assets	$ 3,363,063	$ 3,121,245

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

LOWER COLORADO RIVER AUTHORITY

BALANCE SHEETS

(Dollars in Thousands)

	June 30, 2006	June 30, 2005
Liabilities		
Current Liabilities		
Accounts payable	$ 173,687	$ 137,030
Compensated absences	9,221	8,120
Bonds, notes, and loans payable	158,619	297,844
Total current liabilities	341,527	442,994
Long-Term Liabilities		
Accounts payable from restricted assets	58,680	33,309
Asset retirement obligation	9,270	-
Bonds, notes, and loans payable	2,083,453	1,825,598
Deferred credits	145,804	121,260
Total long-term liabilities	2,297,207	1,980,167
Total liabilities	2,638,734	2,423,161
Equity		
Invested in capital assets, net of related debt	568,812	533,645
Restricted other	29,551	36,467
Unrestricted	125,966	127,972
Total equity	724,329	698,084
Total Liabilities and Equity	$ 3,363,063	$ 3,121,245

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

LOWER COLORADO RIVER AUTHORITY
STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN EQUITY
(Dollars in Thousands)

	Year Ended June 30, 2006	Year Ended June 30, 2005
Operating Revenues		
Electric	$ 927,093	$ 724,282
Water, wastewater and irrigation	52,343	44,313
Other	39,248	34,830
Total operating revenues	1,018,684	803,425
Operating Expenses		
Fuel	435,163	300,604
Purchased power	147,597	75,040
Operations	151,072	167,640
Maintenance	38,103	37,814
Depreciation, depletion and amortization	110,604	100,173
Total operating expenses	882,539	681,271
Operating income	136,145	122,154
Nonoperating Revenues (Expenses)		
Interest and other income	14,878	14,360
Interest and other expenses	(120,917)	(120,217)
Nonoperating revenues (expenses)	(106,039)	(105,857)
Income before costs to be recovered from revenues, capital contributions and special item	30,106	16,297
(Prior Costs) Costs To Be Recovered from Revenues	(13,715)	17,923
Income before capital contributions and special item	16,391	34,220
Capital Contributions	11,304	7,212
Special Item - Loss on Early Defeasance of Debt	(1,450)	-
Change in Equity	26,245	41,432
Total Equity, Beginning of Year	698,084	656,652
Total Equity, End of Year	$ 724,329	$ 698,084

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

LOWER COLORADO RIVER AUTHORITY
STATEMENTS OF CASH FLOWS
(Dollars in Thousands)

	Year Ended June 30, 2006	2005
Cash Flows From Operating Activities		
Received from customers	$ 1,011,979	$ 828,409
Payments for goods and services	(621,441)	(458,507)
Payments to employees	(148,684)	(155,524)
Other revenues	1,906	902
Net cash provided by operating activities	243,760	215,280
Cash Flows From Noncapital Financing Activities		
Grant proceeds received	10,006	1,629
Other expenses	(1,162)	(1,266)
Net cash provided by noncapital financing activities	8,844	363
Cash Flows From Capital and Related Financing Activities		
Expenditures for property, plant and equipment	(283,375)	(268,875)
Proceeds from sale of capital assets	1,116	2,565
Proceeds from installment sale of land	-	2,637
Contributed capital received for capital expenditures	13,330	5,797
Proceeds from bond issues and commercial paper	556,348	421,026
Debt principal payments and commercial paper redemptions	(111,919)	(76,943)
Interest paid	(107,822)	(97,887)
Payments to refund debt and related issue costs	(333,661)	(174,417)
Net cash used in capital and related financing activities	(265,983)	(186,097)
Cash Flows From Investing Activities		
Sale and maturity of investment securities	274,428	261,802
Purchase of investment securities	(253,691)	(287,046)
Interest received	14,532	10,101
Infrastructure financial assistance activity	(1,596)	(1,348)
Net cash provided by (used in) investing activities	33,673	(16,491)
Net Increase in Cash and Cash Equivalents	20,294	13,055
Cash and Cash Equivalents, Beginning of Year	77,525	64,470
Cash and Cash Equivalents, End of Year	$ 97,819	$ 77,525

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

LOWER COLORADO RIVER AUTHORITY
STATEMENTS OF CASH FLOWS
(Dollars in Thousands)

	Year Ended June 30, 2006		Year Ended June 30, 2005	
Reconciliation of Operating Income to Net Cash Provided by Operating Activities				
Operating income	$	136,145	$	122,154
Adjustments to reconcile operating income to net cash provided by operating activities:				
Depreciation, depletion and amortization		110,604		100,173
Changes in assets and liabilities:				
Accounts receivable		(32,323)		17,835
Inventories		(15,434)		(8,853)
Other current assets		(584)		5,597
Current liabilities		36,891		(4,717)
Other deferred charges		(8,053)		(6,750)
Deferred credits and other long-term liabilities		16,514		(10,159)
Net cash provided by operating activities	$	243,760	$	215,280
Noncash Investing Activities				
Investment market adjustments	$	(1,608)	$	(3,483)
Noncash Financing for Property, Plant and Equipment Expenditures				
Purchase of equipment through short-term trade payables	$	24,156	$	24,660
Note receivable received in exchange for asset	$	2,019	$	-
Asset retirement obligation	$	9,270	$	-

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

LOWER COLORADO RIVER AUTHORITY
NOTES TO FINANCIAL STATEMENTS

1. General

The Lower Colorado River Authority (LCRA) is a conservation and reclamation district created by the Texas Legislature in 1934. It receives no state tax money and cannot levy taxes. It operates on revenues from the sale of wholesale electricity, water and other services. The LCRA Board of Directors (Board) is appointed by the governor of the state, with Senate approval, to serve six-year terms. The financial condition of LCRA is not controlled by or dependent on the State or any other political subdivision. Under the criteria set forth in Governmental Accounting Standards Board (GASB) Statement No. 14, "The Financial Reporting Entity," LCRA considers its relationship to the state to be that of a related organization.

LCRA's basic statutory boundaries include a 10-county district comprising the counties of San Saba, Burnet, Llano, Blanco, Travis, Bastrop, Fayette, Colorado, Wharton and Matagorda. LCRA's service area includes all or part of 58 Central Texas counties in which LCRA provides electric utility services, flood management, water and wastewater services, economic development programs, and other public services. LCRA is responsible for regulating the flow of water within its reservoirs for water supply and irrigation, flood management, hydroelectric generation and other useful purposes. LCRA aids in the prevention of flood damage, conserves and protects the forests within the Colorado River watershed, and operates and maintains electric generating plants and 3,953 miles of transmission lines. LCRA also has a comprehensive water quality program along the Colorado River within its 10-county statutory district and owns 40 parks, recreational areas and wildlife preserves adjacent to the Highland Lakes or the Colorado River. Twenty of these parks are leased to or operated by other entities.

LCRA has 2,869 megawatts (MW) of net generating capacity. Hydroelectric net generating capacity of 286 MW is provided by five dams LCRA owns and one it leases. LCRA owns four gas-fired steam boiler generation units with 1,040 MW of net generation and one 500 MW gas-fired combined cycle generation unit. LCRA has full ownership of one coal-fired generating unit with a 445 net MW capacity and a 50 percent ownership interest in two coal-fired units with a combined net capacity of 1,196 MW.

Sales of electricity to LCRA's three largest electric customers represented approximately 45 percent of total electric revenues for fiscal year (FY) 2006 and 40 percent for FY 2005. Electric revenues represented approximately 91 percent of LCRA's operating revenues for FY 2006 and 90 percent for 2005.

Senate Bill 7 (SB 7) allows LCRA to own, build and manage transmission infrastructure statewide with the approval of the Public Utility Commission of Texas. The LCRA Board authorized the creation of LCRA Transmission Services Corporation (LCRA TSC), a nonprofit corporation benefiting and accomplishing public purposes of LCRA. LCRA TSC is governed by a board of directors, which is composed in its entirety of the LCRA Board of Directors. LCRA TSC was created under provisions of Subchapter B of Chapter 152, Texas Water Code and the Texas Non-Profit Corporation Act. Effective Jan. 1, 2002, LCRA TSC began operations subsequent to the transfer of LCRA's transmission and transformation assets to LCRA TSC pursuant to the terms of an Electric Transmission Facilities Contract (the Initial Contractual Commitment) dated Oct. 1, 2001.

LCRA has ownership and operating arrangements for various water and wastewater systems. Some water and wastewater facilities are owned by LCRA and operated by another river authority in connection with an alliance agreement to address immediate and long-term water and wastewater needs in Williamson County and other areas. In addition, LCRA owns three irrigation systems consisting of 791 miles of canal and three low-head dams. The irrigation systems are located in Colorado, Wharton and Matagorda counties.

2. Significant Accounting Policies

Basis of Accounting: The accompanying financial statements of LCRA, a governmental entity, have been prepared utilizing proprietary fund and accrual basis accounting. LCRA implements all applicable GASB pronouncements and all applicable Financial Accounting Standards Board (FASB) pronouncements that do not conflict with or contradict GASB pronouncements. LCRA's accounts are maintained in accordance with the Federal Energy Regulatory Commission's Uniform System of Accounts. The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements, and reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

LCRA considers electric revenues and costs that are directly related to the generation, purchase, transmission and distribution of electricity to be operating revenues and expenses. Water and wastewater revenues and other services related to environmental laboratory operations, licensing, and recreation, and the costs directly related to these services, are also considered operating revenues and expenses. Revenues and expenses related to financing and other activities are reflected as nonoperating.

Newly Adopted Standards for FY 2006 and FY 2005: In FY 2006, LCRA implemented FASB Interpretation No. 47 (FIN No. 47), "Accounting for Conditional Asset Retirement Obligations – an interpretation of FASB Statement No 143." FIN No. 47 clarifies the term, "conditional asset retirement obligation," as used in FASB Statement No. 143. FIN No. 47 mandates that an entity recognize the fair value of a legal obligation to perform an asset retirement activity in which the time and (or) the method of settlement are conditional on a future event that may or may not be within the control of the entity. FIN No. 47 is effective for fiscal years ending after December 15, 2005. LCRA has applied FIN No. 47 as described in Note 8.

In FY 2005, LCRA implemented GASB Statement No. 40, "Deposit and Investment Risk Disclosures, an amendment of GASB Statement No. 3" (GASB No. 40). GASB No. 40 adds to existing disclosure requirements for cash and investments by adding information regarding certain risks associated with cash and investments. GASB No. 40 does not replace or eliminate in their entirety the disclosure requirements of existing pronouncements dealing with cash and investments. The implementation of GASB 40 did not have a material impact on LCRA's financial position or results of operations. GASB 40 disclosures are in Note 3.

GenTex Power Corporation: The GenTex Power Corporation (GenTex), a nonprofit corporation and wholly owned affiliate of LCRA, is governed by a nine-member board appointed by the LCRA Board. GenTex owns a 500-MW gas-fired combined cycle generating unit that began commercial operation in June 2001.

In FY 2000, LCRA entered into an agreement with a public company to jointly construct the generating unit. Each entity had an undivided 50 percent interest in the generating unit. In FY 2004, GenTex purchased the other entity's 50 percent share.

GenTex's share of the initial construction costs of the facility was entirely funded by an LCRA economic development grant. GenTex entered into contracts with LCRA's wholesale customers to sell energy to the customers at a price recovering only operating expenses, excluding depreciation, over the life of the plant. The contracts provide the customers the right of first refusal to purchase the facility and obtain half interest at a price of $975 per customer. Since the initial cost of the facility was funded by an economic development grant provided by LCRA, there is no debt service to recover, and the expected cash flows are intended to recover only the operating costs. The plant is included in the Balance Sheets at the contractual value plus the purchase price of the 50 percent interest acquired in 2004.

Although it is a separate legal entity, GenTex is reported as part of LCRA because its sole purpose is to provide energy to LCRA's 43 long-term wholesale customers in meeting their demands and operating in a competitive market.

ERCOT Settlements Reporting: LCRA reports power balancing transactions, which represent wholesale purchases and sales of power for real-time balancing purposes as measured in 15 minute intervals. These purchases and sales with ERCOT, as the balancing energy clearinghouse agent, are reported net. These amounts have historically represented a net purchase of power to LCRA; however, during FY 2006 and FY 2005 these amounts resulted in net sales of power and ancillary services and are included as a reduction to power production expense. The amounts included in power production expense were $28.8 million for FY 2006 and $8.9 million for FY 2005.

LCRA Transmission Services Corporation: The Corporation is a nonprofit corporation created by LCRA that began operations on Jan. 1, 2002, by engaging in the electric transmission and transformation business activities previously performed by LCRA. Although it is a separate legal entity, the Corporation is reported as part of LCRA because it is governed by a board of directors that is composed in its entirety of the LCRA Board of Directors.

Fayette Power Project: LCRA's coal-fired generating units are located at the Fayette Power Project (FPP) and operate pursuant to a participation agreement with the City of Austin (Austin). LCRA has an undivided 50 percent interest in Units 1 and 2 and wholly owns Unit 3. LCRA's investment is financed with LCRA funds, and its pro-rata share of operations is recorded as if wholly owned. The original cost of LCRA's share of FPP's generation and transmission facilities is recorded in the utility plant accounts of LCRA in accordance with its accounting policies. The equity interest in FPP is calculated pursuant to the participation agreement and is reported in various asset and liability accounts within LCRA's financial statements.

Restricted Funds: Restricted funds consist of construction funds derived from debt issues and system revenues, which have been designated for specific purposes by the Board.

Utility Plant: Utility plant consists of generating plants, electric transmission and distribution facilities, dams, reservoir land, natural gas production and development, irrigation systems, water and wastewater treatment facilities, telecommunications facilities, and related projects under construction. These assets are recorded at cost, which includes materials, labor, overhead, asset retirement obligations and interest capitalized during construction. The costs of repairs and minor replacements are charged to operating expense as incurred. Costs of asset replacements and betterments are capitalized. The cost of depreciable plant retired, along with removal expense less salvage value, is charged to nonoperating expense on the Statement of Revenues, Expenses and Changes in Equity. Gains and losses upon disposition are recorded in the period incurred.

Water Rights: Water rights are stated at cost, net of accumulated amortization of $7.4 million as of June 30, 2006 and 2005. Beginning in FY 2003, in accordance with accounting and reporting requirements, water rights are no longer being amortized but are evaluated annually to determine whether they are impaired and whether an indefinite life is reasonable.

Inventories: Coal is recorded at cost using the last-in, first-out method. Stored natural gas, fuel oil, and materials and supplies are stated at average cost. All nonfuel inventories are stated at the lower of cost or market.

Investments: LCRA's investments are stated at fair value. Any changes, unrealized and realized, in the fair value of financial investments are recorded as investment income.

Refunding and Defeasance of Debt: For debt refundings, the difference between the reacquisition price and the net carrying amount of the old debt is deferred and reported as a deduction from or an addition to the debt liability. For debt defeasances, the difference between the carrying amount of the debt and the amount of funds needed to retire the debt is recognized immediately in the Statements of Revenues, Expenses and Changes in Equity as a special item.

Compensated Absences: LCRA records earned vacation leave as a liability and accrues for certain salary-related expenses associated with the payment of compensated absences.

Rates and Regulations: LCRA's electric, water and wastewater rates are set by LCRA's Board at a level sufficient to recover its operating costs, debt service and debt service coverage requirements. LCRA's bond counsel is of the opinion that a Texas court applying Texas law would ultimately conclude that LCRA's Board has the authority to establish and collect such fees and charges. LCRA's transmission service rates remain regulated by the Public Utility Commission of Texas (PUC). While the LCRA Board has original jurisdiction over its water and wastewater rates, the Texas Commission on Environmental Quality has appellate jurisdiction.

SB 7, passed by the Texas Legislature in 1999, provided for retail electric open competition to begin in January 2002, continued electric transmission open access, and fundamentally redefined and restructured the Texas electric industry. SB 7 directly and indirectly impacts LCRA and its wholesale electric customers. Under SB 7, LCRA has structurally unbundled its electric generation business and assets from its electric transmission business and assets. SB 7 also allows retail customers of investor owned utilities, as well as the retail customers of those municipally owned utilities and electric cooperatives that elect to participate in retail competition, to choose their electric supplier.

Transmission rates within the Electric Reliability Council of Texas (ERCOT) system are determined pursuant to a universal 100 percent "postage stamp" rate that spreads the total annual costs of transmission services among distribution service providers (DSPs) according to their electric loads. The transmission costs are determined pursuant to transmission cost of service (TCOS) rate proceedings required to be filed by all transmission service providers (TSPs), including LCRA TSC. Every electric end-use consumer in the ERCOT system pays a portion of the total cost of maintaining a reliable statewide transmission system. Transmission charges are calculated by multiplying a DSP's share of the statewide electric load by the statewide "postage stamp" rate. The load shares and rates are determined by the PUC through its TCOS regulatory process. Additionally, pursuant to a tariff approved by the PUC, the Corporation collects revenues for transformation services, providing transformers that "step down" voltage from levels appropriate for transmission to lower levels for distribution. A monthly charge for each transformation delivery point is also authorized under the transformation tariff.

FY 2005 transmission revenues of $142.7 million resulted from a rate of $2.55 per kW as a result of PUC commissioners approving an LCRA TSC rate case on May 15, 2005. This rate was retroactively effective for all of FY 2005.

FY 2006 transmission revenues of $156 million are the result of rate changes authorized during the fiscal year. The predominant rate of $2.77 per kW was in place from Sept. 26, 2005 through June 30, 2006. LCRA TSC filed an interim update of wholesale transmission rates with the PUC on July 25, 2005, and the PUC Commissioners approved the new rate of $2.77 per kW on September 26, 2005.

LCRA TSC filed an interim update of wholesale transmission rates with PUC on July 25, 2006. The filing, Docket No. 32987, was approved by the PUC Commissioners on Sept. 21, 2006. The approved rate is $2.88 per kW, effective Sept. 21, 2006.

The greatest potential impact on LCRA from SB 7 could result from actions of its wholesale electric customers. If LCRA's larger wholesale electric customers open their territories to retail competition, there is a potential that such customers could lose end-user customers to other retail electric providers resulting in a reduced electric load, thus reducing the requirements served by LCRA under the existing wholesale power agreements. On the other hand, if LCRA's wholesale electric customers are successful in retaining existing customers and in growing their customer base, requirements served by LCRA under the existing wholesale power agreements could increase.

Regulatory Assets and Liabilities: LCRA applies the accounting requirements of FASB Statement of Financial Accounting Standards No. 71 (SFAS 71), "Accounting for the Effects of Certain Types of Regulation." Accordingly, certain costs may be capitalized as a regulatory asset that would otherwise be charged to expense. A regulatory asset is recorded when it is probable that future revenue in an amount at least equal to the capitalized costs will result from inclusion of those costs in future rates. In addition, rate actions of the regulator may impose a liability on LCRA. A regulatory liability occurs when a regulator requires refunds to customers or provides current rates intended to recover costs that are expected to be incurred in the future. Any regulatory asset is amortized over the life of LCRA's outstanding long-term debt, while a regulatory liability is recognized and charged to income when the associated costs are incurred. LCRA's regulatory assets amounted to $238.3 million and $240.3 million at June 30, 2006 and 2005, respectively. Regulatory liabilities amounted to $1.7 million and $2.1 million at June 30, 2006 and 2005, respectively. The regulatory assets, which are included under deferred charges, consist of depreciation of debt-funded assets and costs related to outstanding debt. Debt-funded costs are deferred pending future recovery through the inclusion of the related debt service in rates. Regulatory liabilities are included in deferred credits and other long-term liabilities.

LCRA has reviewed and will continue to monitor the relevance of SFAS 71 in light of SB 7 and future changes in the Texas electric industry. As of June 30, 2006, and for the foreseeable future, management believes that SFAS 71 will continue to apply and anticipates no material losses from the write-off of regulatory assets.

Capitalized Interest: Interest which is financed by debt proceeds is capitalized as part of the cost of capital assets and deferred charges. During FY 2006 and 2005, LCRA capitalized $13.8 million and $12.9 million of interest, respectively.

Gas Price Management: LCRA enters into futures contracts, swaps and options for energy price risk management purposes. Derivative instruments are recorded on the balance sheet at their fair value. Changes in the fair value of derivatives are recorded each period in current earnings. LCRA is using mark to market accounting as a component of the fuel factor for its derivatives, and gains and losses related to the financial contracts are recognized in current earnings.

Fuel Factor: Revenues from the sale of electricity include amounts collected through the fuel factor. LCRA records over- or under-recoveries of fuel costs, including unrealized gains or losses on financial contracts entered into as part of its gas price management program, as a deferred asset or liability. These costs are a component of the fuel factor. Over-recoveries may result in refunds to customers and, correspondingly, under-recoveries may result in additional assessments to customers.

Natural Gas Development and Production: LCRA has adopted the full-cost method of accounting for natural gas development and production. Under this method, all costs directly associated with acquisition and development of oil and gas properties are capitalized and depleted to expense over the life of proved reserves on a units-of-production method. For both the years ended June 30, 2006 and 2005, depletion expense totaled approximately $0.4 million.

Contract Extension Settlement with Major Customers: According to the terms of a 1987 settlement with two major customers, their wholesale power contracts were extended to 2016, and in return, LCRA reimbursed the customers for their costs incurred in planning generating facilities. These costs are amortized over the period affected by the contract extension.

Impairment: LCRA evaluates the carrying value of its property, plant and equipment, and other long-lived assets when major events or changes in circumstances indicate a decline in an asset's service capacity. Impairment is measured using methods that isolate the asset's service capacity that has been rendered unusable.

Depreciation, Depletion and Amortization: LCRA depreciates its utility plant in service on a straight-line basis over the estimated useful lives of the various classes of these assets. Annual depreciation expense, expressed as a percentage of average depreciable utility plant, was approximately 3 percent for FY 2006 and 2005. Depreciation, depletion and amortization expense for FY 2006 and 2005 was $110.6 million and $100.2 million, respectively.

The estimated useful life of property, plant and equipment by major category is as follows:

Hydraulic Production Plant	20 - 100 years
Steam Production Plant	25 - 40 years
Transmission Plant	35 - 65 years
General Plant	4 - 45 years
Irrigation Plant	15 - 75 years
Sewage and Water Treatment Plant	10 - 50 years
Telecommunication Facilities	10 - 25 years

Water rights are not amortized but are evaluated annually to determine whether they are impaired and whether an indefinite life is reasonable. Gains or losses created by refunding transactions are amortized over the shorter of the remaining terms of the new issues or the refunded bonds. Amortization of debt discount and premium is computed using the interest method over the life of the related bond issues. Amortization of debt issue cost is computed on the straight-line method over the life of the related bond issues, which approximates the interest method. Other deferred charges are amortized on a straight-line basis ranging from 20 to 40 years.

Statements of Cash Flows: All highly liquid investments (including investments in restricted funds) with an original maturity of three months or less are considered cash equivalents.

Reclassifications: Certain amounts in the prior year's financial statements have been reclassified to conform to current year presentation.

3. Financial Instruments

As of June 30, 2006 and 2005, LCRA had the following investments and maturities:

Type of Investment	June 30, 2006 Market Value[1]	June 30, 2006 WAM (Years)[2]	June 30, 2005 Market Value[1]	June 30, 2005 WAM (Years)[2]
Investments				
U.S. Government Securities	$ 158,831	0.85	$ 145,368	1.24
U.S. Agency Discount Notes	9,988	0.50	33,796	0.19
Commercial Paper			12,000	0.25
Cash Equivalents				
U.S. Agency Discount Notes	9,963	0.10		
Commercial Paper	27,500	0.09	38,000	0.14
Money Market Fund	59,749	0.09	41,430	0.07
Total	$ 266,031	0.56	$ 270,594	0.73

[1] Dollars in Thousands
[2] Weighted Average Maturity

External Investments Pool: LCRA investments included a money market fund with TexPool at June 30, 2006 and 2005. The State Comptroller of Public Accounts oversees TexPool, and the pool seeks to maintain a $1 value per share as required by the Texas Public Fund Investment Act. There are no minimum balance requirements for TexPool participants, and there is no limit on the number of accounts per participants.

Interest Risk: LCRA has no formal policy to address exposure to fair value losses resulting from changes in interest rates. However, in accordance with management policy, LCRA manages its exposure to rising interest rates by investing a majority of its investment portfolio in securities with short-term maturities and holding investments to maturity.

Credit Risk: LCRA investment activities are governed by state statute (Public Fund Investment Act) which specifies the type and ratings of investments governmental entities are allowed to purchase. In addition, LCRA Board policy, internal operating procedures and applicable bond resolutions further restrict investment activity. At June 30, 2006 and 2005, LCRA investment in the investment pool (money market) was rated AAAm by Standard & Poor's. Investments in commercial paper were rated A-1+ by Standard & Poor's and P-1 by Moody's Ratings. Investments in US Agencies were rated Aaa by Moody's Ratings.

Estimation of Fair Value: The carrying amounts of receivables and certain other liabilities approximate market value due to the short maturity of these instruments. The estimated market value of long-term debt, based on current market yields was $2.6 billion and $2.5 billion at June 30, 2006 and 2005, respectively.

Hedging Instruments: LCRA's gas activities subject LCRA's earnings to variability based on fluctuations in the market price of natural gas, as measured by changes in the delivered price of natural gas at various points in the system's natural gas grid. In an effort to mitigate the financial and market risk associated with these activities for the customers, LCRA routinely enters into natural gas swaps, futures contracts and options for other than trading purposes. This use of these types of transactions for the purpose of reducing exposure to price risk is generally referred to as hedging, with the results matching the financial impact of these transactions with the cash impact resulting from consummation of the transaction being hedged. These contracts are commitments to either purchase or sell designated quantities of a commodity at a specified price and at a specified date. These contracts may be settled in cash or through delivery of the specified commodity; however, in general, LCRA settles futures contracts in cash. LCRA holds highly liquid contracts with terms ranging up to 18 months. Initial margin requirements, which are flat fees per contract, and daily margin calls are met in cash or short-term liquid government securities. The financial impact of these futures contracts, the effects of which were substantially offset by the physical gas purchases, was to recognize a loss of approximately $17.6 million during 2006 and a gain of approximately $1.2 million during 2005. Net income is not affected because this activity is a component of the fuel costs passed through to the customers and is included in the balance sheet fuel over- or under-recovery account.

All derivative instruments are recorded on the balance sheet at their fair value, which generally reflects the estimated amounts that LCRA would receive or pay to terminate the contracts. At June 30, 2006, the fair value of LCRA's hedging assets and liabilities were $0.4 million and $7.9 million, respectively. Changes in the fair value of the derivatives are recorded in current earnings as a component of the fixed-fuel factor. LCRA has not designated any of the derivatives as hedging instruments, as allowed by FASB 133.

Counterparties expose LCRA to credit-related losses in the event of nonperformance, but LCRA does not expect any counterparties to fail to meet their obligations, given their high credit ratings.

4. Long-Term Debt

Changes during FY 2006 and balances at June 30, 2006 and 2005, of long-term debt, including current portions are as follows (in thousands):

Series	From	To	June 30, 2005	Increases	Decreases	June 30, 2006	in FY 2007
LCRA TSC 2003A (Auction Rate) (1)	2030	2032	$ 50,000	$	$	$ 50,000	$
LCRA TSC 2003B (5.00%-5.375%)	2008	2031	251,975		(14,735)	237,240	
LCRA TSC 2003C (5.00%-5.25%)	2007	2033	131,200		(5,640)	125,560	1,665
LCRA TSC 2004 (3.00%-5.00%)	2007	2034	125,490			125,490	4,075
LCRA TSC 2005 (3.25%-5.00%)	2008	2035	-	126,095		126,095	
LCRA TSC 2006 (4.50%-5.00%)	2008	2036	-	135,925		135,925	
LCRA 2006 (4.00%-5.00%)	2007	2036	-	80,305		80,305	1,610
LCRA 2004 (4.00%-5.00%)	2007	2029	103,150		(2,850)	100,300	2,910
LCRA 2004A (3.50%) (2)	2007	2007	247		(157)	90	90
LCRA 2004B (3.50%) (2)	2006	2006	10		(10)	-	
LCRA 2004D (2.50%-5.00%)	2007	2034	50,880		(1,970)	48,910	830
LCRA 2003 (3.25%-5.25%)	2007	2033	96,250		(5,370)	90,880	4,140
LCRA 2002 (3.50%-5.00%)	2007	2031	118,070		(1,460)	116,610	1,580
LCRA 2001A (5.00%-5.375%)	2007	2032	149,340		(11,135)	138,205	3,305
LCRA 2001 (5.00%-8.00%)	2007	2031	96,430		(675)	95,755	735
LCRA 1999A (5.50%-5.875%)	2014	2020	347,540		(60)	347,480	
LCRA 1999B (5.875%-6.00%)	2007	2014	348,520		(70)	348,450	49,065
LCRA 1999C (7.02%)	2006	2006	30,320		(30,320)	-	
LCRA 1999E (5.00%-5.75%)	2008	2011	21,960		(1,305)	20,655	
LCRA 1999F (5.50%-5.75%)	2008	2012	97,930		(25)	97,905	
LCRA 1999G (3.80%-4.85%) (2) (3)	2006	2016	39,980		(1,875)	38,105	2,125
LCRA 1999H (3.05%-3.65%) (2) (4)	2007	2011	5,765		(1,500)	4,265	1,400
LCRA 1999I (3.30%-4.15%) (4)	2007	2020	3,545		(115)	3,430	130
LCRA TWDB Note Payable (6.05%-6.10%)	2020	2034	10,500			10,500	
LCRA TWDB Note Payable (5.58%-5.83%)	2022	2038	14,040			14,040	
Add: Unamortized Net Premium			39,752	3,323	(7,482)	35,593	783
Subtotal			2,132,894	345,648	(86,754)	2,391,788	74,443
Unamortized Net Losses on Refunded Debt			(256,852) (5)		10,636	(246,216) (6)	(12,324)
Taxable Commercial Paper (Variable Rate)			11,500	6,600		18,100	18,100
Tax-Exempt Commercial Paper (Variable Rate)			235,900	204,100	(361,600)	78,400	78,400
Total			$ 2,123,442	$ 556,348	$ (437,718)	$ 2,242,072	$ 158,619

(1) Rate is reset at auction every 28 days (3.70 percent as of June 30, 2006).

(2) Represents yield rate of Capital Appreciation Bonds.

(3) Maturity Date is July 1.

(4) Maturity Date is January 1.

(5) $201,490 is associated with LCRA 1999 A-I refunding bonds and $55,362 is associated with LCRA TSC 2003A and 2003B refunding bonds.

(6) $193,555 is associated with LCRA 1999 A-I refunding bonds and $52,661 is associated with LCRA TSC 2003A and 2003B refunding bonds.

LCRA's debt as of June 30, 2006, has been rated by Fitch, Moody's, and Standard & Poor's, respectively, as follows:

FITCH, MOODY'S, AND STANDARD & POOR'S

Refunding and Improvement Revenue Bonds: A+, A1 and A (Uninsured)
Commercial Paper: F-1+, P-1, A-1
LCRA Transmission Services Corporation Contract Refunding Revenue Bonds: A, A2, A (Uninsured)
LCRA Transmission Services Corporation Commercial Paper: F1+, P-1, A-1

Bond and note debt payments, excluding commercial paper, are as follows (in thousands):

Fiscal Year Ending June 30	Principal	Interest	Total
2007	$ 73,660	$ 120,958	$ 194,618
2008	100,215	117,374	217,589
2009	101,890	112,107	213,997
2010	106,040	106,847	212,887
2011	111,580	101,209	212,789
2012-2016	643,730	413,062	1,056,792
2017-2021	442,665	261,170	703,835
2022-2026	317,940	155,210	473,150
2027-2031	290,400	81,968	372,368
2032-2036	166,850	18,170	185,020
2037-2038	1,225	108	1,333
	2,356,195	1,488,183	3,844,378
Unamortized Net Discount	35,593		35,593
Total	$ 2,391,788	$ 1,488,183	$ 3,879,971

New and Refunding Bonds: During FY 2006, LCRA issued $6.6 million of taxable commercial paper and $59.1 million of tax-exempt commercial paper. In addition, LCRA on behalf of LCRA TSC issued $145 million of tax-exempt commercial paper.

On May 25, 2006, LCRA issued $80.3 million of tax-exempt Refunding Revenue Bonds, Series 2006. In addition, on May 25, 2006, LCRA on behalf of LCRA TSC issued $135.9 million of Transmission Contract Refunding Revenue Bonds, Series 2006. The proceeds from the bond issues were used to refund tax-exempt commercial paper.

During FY 2006, LCRA deposited funds into an escrow account to defease debt early. On May 9, 2006, LCRA defeased approximately $9.7 million from various bond series. In addition, on April 26, 2006, LCRA on behalf of LCRA TSC defeased approximately $9.6 million from the LCRA TSC Series 2003B and LCRA TSC Series 2003C Contract Refunding Revenue Bonds. Pursuant to the stipulations of the Revenue Bonds and in the opinion of LCRA's Bond Counsel, the repayment of these obligations constitutes a legal defeasance. These defeasances reduce future debt service requirements.

On Aug. 16, 2005, LCRA on behalf of LCRA TSC issued $126.1 million of Transmission Contract Refunding Revenue Bonds, Series 2005. The proceeds from the issue were used to refund $120 million of tax-exempt commercial paper.

On Dec. 16, 2004, LCRA issued $51.3 million of tax-exempt Refunding Revenue Bonds, Series 2004D. In addition, on Dec. 16, 2004, LCRA on behalf of LCRA TSC issued $125.5 million of Transmission Contract Refunding Revenue Bonds, Series 2004. The proceeds from these issues were used to refund tax-exempt commercial paper.

During FY 2005, LCRA issued $55.8 million of tax-exempt commercial paper and $5.9 million of taxable commercial paper to fund various capital projects. In addition, LCRA on behalf of LCRA TSC issued $171.7 million of tax-exempt commercial paper to fund transmission related capital projects.

The principal associated with the bonds that have been previously refunded by LCRA but remain outstanding at June 30, 2006 and 2005, totals $381.8 million and $378.7 million, respectively. Proceeds from these refunding bond issues were escrowed to purchase U.S. government obligations that will mature at such time and yield interest as such amounts so that sufficient monies are available for payment of principal, premium, if any, and interest on the refunded bonds when due. None of these refunded bonds are included in LCRA's outstanding long-term debt at June 30, 2006 and 2005.

Optional Redemption: The Series 2006 bonds that mature on and after May 15, 2012, are redeemable at the option of LCRA, on May 15, 2011 or on any date thereafter, in whole or in part, in principal amounts of $5,000 or integral multiples thereof (and if in part, the particular bonds or portions thereof to be redeemed shall be selected by LCRA in its sole discretion) at a redemption price equal to the principal amount of such bonds to be redeemed, plus accrued interest to the redemption date.

The LCRA TSC Series 2006 bonds that mature on and after May 15, 2012, are redeemable at the option of LCRA, on May 15, 2011 or on any date thereafter, in whole or in part, in principal amounts of $5,000 or integral multiples thereof (and if in part, the particular bonds or portions thereof to be redeemed shall be selected by LCRA in its sole discretion) at a redemption price equal to the principal amount of such bonds to be redeemed, plus accrued interest to the redemption date.

The LCRA TSC Series 2005 bonds that mature on and after May 15, 2012, are redeemable at the option of LCRA, on May 15, 2011 or on any date thereafter, in whole or in part, in principal amounts of $5,000 or integral multiples thereof (and if in part, the particular bonds or portions thereof to be redeemed shall be selected by LCRA in its sole discretion) at a redemption price equal to the principal amount of such bonds to be redeemed, plus accrued interest to the redemption date.

The Series 2004D bonds that mature on and after May 15, 2012, are redeemable at the option of LCRA, on May 15, 2011 or on any date thereafter, in whole or in part, in principal amounts of $5,000 or integral multiples thereof (and if in part, the particular bonds or portions thereof to be redeemed shall be selected by LCRA in its sole discretion) at a redemption price equal to the principal amount of such bonds to be redeemed, plus accrued interest to the redemption date.

The LCRA TSC Series 2004 bonds that mature on and after May 15, 2012, are redeemable at the option of LCRA, on May 15, 2011, or on any date thereafter, in whole or in part, in principal amounts of $5,000 or integral multiples thereof (and if in part, the particular bonds or portions thereof to be redeemed shall be selected by LCRA in its sole discretion) at a redemption price equal to the principal amount of such bonds to be redeemed, plus accrued interest to the redemption date.

The Series 2004 bonds that mature on and after May 15, 2012, are redeemable at the option of LCRA, on May 15, 2011 or on any date thereafter, in whole or in part, in principal amounts of $5,000 or integral multiples thereof (and if in part, the particular bonds or portions thereof to be redeemed shall be selected by LCRA in its sole discretion) at a redemption price equal to the principal amount of such bonds to be redeemed, plus accrued interest to the redemption date.

The Series 2003 bonds that mature on and after May 15, 2014, are redeemable at the option of LCRA, on May 15, 2013, or on any date thereafter, in whole or in part, in principal amounts of $5,000 or integral multiples thereof (and if in part, the particular bonds or portions thereof to be redeemed shall be selected by LCRA in its sole discretion) at a redemption price equal to the principal amount of such bonds to be redeemed, plus accrued interest to the redemption date.

The LCRA TSC Series 2003C bonds that mature on and after May 15, 2014, are redeemable at the option of LCRA, on May 15, 2013, or on any date thereafter, in whole or in part, in principal amounts of $5,000 or integral multiples thereof (and if in part, the particular bonds or portions thereof to be redeemed shall be selected by LCRA in its sole discretion) at a redemption price equal to the principal amount of such bonds to be redeemed, plus accrued interest to the redemption date.

The LCRA TSC Series 2003A bonds are subject to optional redemption by LCRA, upon the written direction of LCRA TSC, in whole or in part, on any interest payment date immediately following an auction period, in authorized denominations at a redemption price equal to the principal amount thereof, plus accrued interest to the redemption date; provided, however, that in the event of a partial redemption of bonds, the aggregate principal amount of bonds that will remain outstanding must equal at least $10 million unless otherwise consented to by the related broker-dealers.

The LCRA TSC Series 2003B bonds that mature on and after May 15, 2013, are redeemable at the option of LCRA, on May 15, 2012, or on any date thereafter, in whole or in part, in principal amounts of $5,000 or integral multiples thereof (and if in part, the particular bonds or portions thereof to be redeemed shall be selected by LCRA in its sole discretion) at a redemption price equal to the principal amount of such bonds to be redeemed, plus accrued interest to the redemption date.

The Series 2002 bonds maturing on and after May 15, 2014, are redeemable at the option of LCRA, on May 15, 2013, or on any date thereafter, in whole or in part, in principal amounts of $5,000 or integral multiples thereof at a redemption price equal to the principal amount of such bonds to be redeemed, plus accrued interest to the redemption date.

The Series 2001A bonds maturing on and after May 15, 2012, are redeemable at the option of LCRA, on May 15, 2011, or on any date thereafter, in whole or in part, in principal amounts of $5,000 or integral multiples thereof at a redemption price equal to the principal amount of such bonds to be redeemed, plus accrued interest to the redemption date.

The Series 2001 bonds maturing on or after May 15, 2011, are callable at the option of LCRA for a period of one year beginning on May 15, 2010, at the price of 101 percent plus accrued interest. These bonds are also callable at LCRA's option on May 15, 2011, or on any date thereafter, in whole or in part, in principal amounts of $5,000 or integral multiples thereof at the price of 100 percent plus accrued interest.

The Series 1999A bonds, Series 1999B bonds, Series 1999E bonds and Series 1999F bonds maturing on or after May 15, 2010, are callable at the option of LCRA for a period of one year beginning on May 15, 2009, at the price of 101 percent plus accrued interest. These bonds are also callable at LCRA's option on May 15, 2010, or on any date thereafter, in whole or in part, in principal amounts of $5,000 or integral multiples thereof at the price of 100 percent plus accrued interest.

The LCRA bonds outstanding as of June 30, 2006 and 2005, are parity Debt under the Master Resolution and are collateralized by a lien on and pledge of the Pledged Revenues. Pledged Revenues are defined to include all amounts received pursuant to Contractual Commitments and all lawfully available funds of LCRA. The LCRA Transmission Contract Revenue Bonds Series 2003A, 2003B, 2003C, 2004, 2005 and 2006 are solely secured by the obligation of LCRA TSC to make Installment Payments to LCRA from the Net Revenues of LCRA TSC (subordinate to first lien on Gross Revenues securing the Purchase Price Payments under the Initial Contractual Commitment). Net revenues are defined as Gross Revenues less any Purchase Price Payments due to LCRA and less the Operating and Maintenance Expenses during the period.

Commercial Paper: LCRA is authorized to issue up to $350 million in short-term tax-exempt obligations and $350 million in short-term taxable obligations to provide system improvements, acquire fuel reserves and facilities, refund outstanding debt, and pay interest on outstanding debt. Outstanding notes were issued in denominations of $100,000 or more with maturities of 270 days or less from their respective issue dates. The Commercial Paper program expires May 15, 2020. It is management's intent to periodically renew outstanding commercial paper upon maturity.

LCRA maintains credit facilities with banks that provide available borrowings sufficient to pay the principal of the notes. LCRA has entered into a revolving credit agreement with a bank that is obligated to lend LCRA amounts of up to $187.5 million for the Tax-Exempt Series. Of the $187.5 million, $112.5 million of this agreement expires on Oct. 13, 2008, and the remaining $75 million expires on June 27, 2008. LCRA has an additional revolving credit agreement with a bank that is obligated to lend LCRA aggregate amounts of up to $40 million for the Taxable Series. This agreement expires on Oct. 13, 2008. Failure by LCRA to meet certain restrictive covenants could result in the withdrawal of the banks' commitments for the unused lines of credit. There were no borrowings under any of the agreements as of June 30, 2006.

LCRA TSC is authorized to issue tax-exempt commercial paper notes in an aggregate amount of principal and interest not to exceed $150 million in short-term tax-exempt obligations. Outstanding notes were issued in denominations of $100,000 or more with maturities of 270 days or less from their respective issue dates. The Commercial Paper program expires May 15, 2042. It is management's intent to periodically renew outstanding commercial paper upon maturity.

LCRA TSC maintains a $150 million credit facility with a bank that provides available borrowings to pay the principal and interest of the commercial paper notes. Of the $150 million total, $137 million is available to pay the principal of the notes, and $13 million is available to pay interest on the notes. The credit facility has an expiration date of Apr. 29, 2009. Failure by LCRA or LCRA TSC to meet certain restrictive covenants could result in the withdrawal of the banks' commitments for the unused line of credit. There were no borrowings under the agreement as of June 30, 2006.

Conduit Debt: At June 30, 2006, there are two series of Pollution Control Revenue Bonds outstanding with an aggregate principal amount payable of $50 million. The bonds mature in April 2027 and 2030, $25 million each year. The bonds were issued to finance the costs of acquiring, constructing and improving certain solid waste and sewage disposal facilities of a private-sector entity. LCRA executed an installment sale agreement with the entity whereby the proceeds of the bonds were used to finance a portion of the project. In turn, the entity agreed to make payments sufficient to pay, when due, the principal and interest on the bonds. The bonds do not constitute a debt or pledge of LCRA, and accordingly, have not been reported in the accompanying financial statements.

Mandatory Redemption: The following term bonds will be subject to mandatory sinking fund redemption prior to maturity on May 15 in each of the following years and in the following amounts at the redemption price equal to the principal amount thereof plus accrued interest to the redemption date, with the particular Bonds or portions thereof to be redeemed, to be selected and designated by LCRA (provided that a portion of a Bond may be redeemed only in an integral multiple of $5,000):

Series 2006

4.625% Term Bond Maturing May 15, 2031

Redemption Date	Amount
May 15, 2027	$ 1,625,000
May 15, 2028	1,790,000
May 15, 2029	1,975,000
May 15, 2030	2,165,000
May 15, 2031	2,370,000

Series 2006

5.00% Term Bond Maturing May 15, 2031

Redemption Date	Amount
May 15, 2027	$ 2,000,000
May 15, 2028	2,000,000
May 15, 2029	2,000,000
May 15, 2030	2,000,000
May 15, 2031	2,000,000

Series 2006
Term Bond Maturing May 15, 2036

Redemption Date	Amount
May 15, 2032	$ 2,315,000
May 15, 2033	2,425,000
May 15, 2034	2,540,000
May 15, 2035	2,665,000
May 15, 2036	2,790,000

LCRA Transmission Services Corporation
Series 2006
Term Bond Maturing May 15, 2031

Redemption Date	Amount
May 15, 2027	$ 4,535,000
May 15, 2028	4,535,000
May 15, 2029	4,535,000
May 15, 2030	4,535,000
May 15, 2031	4,535,000

LCRA Transmission Services Corporation
Series 2006
Term Bond Maturing May 15, 2034

Redemption Date	Amount
May 15, 2032	$ 4,535,000
May 15, 2033	4,535,000
May 15, 2034	4,535,000

LCRA Transmission Services Corporation
Series 2006
Term Bond Maturing May 15, 2036

Redemption Date	Amount
May 15, 2035	$ 4,535,000
May 15, 2036	9,245,000

LCRA Transmission Services Corporation
Series 2005
Term Bond Maturing May 15, 2029

Redemption Date	Amount
May 15, 2026	$ 4,200,000
May 15, 2027	4,200,000
May 15, 2028	4,200,000
May 15, 2029	4,200,000

LCRA Transmission Services Corporation
Series 2005
Term Bond Maturing May 15, 2031

Redemption Date	Amount
May 15, 2030	$ 4,200,000
May 15, 2031	4,200,000

LCRA Transmission Services Corporation
Series 2005
Term Bond Maturing May 15, 2035

Redemption Date	Amount
May 15, 2032	$ 4,195,000
May 15, 2033	4,195,000
May 15, 2034	4,195,000
May 15, 2035	12,745,000

Series 2004D
Term Bond Maturing May 15, 2029

Redemption Date	Amount
May 15, 2026	$ 2,210,000
May 15, 2027	2,525,000
May 15, 2028	2,650,000
May 15, 2029	2,775,000

Series 2004D
Term Bond Maturing May 15, 2034

Redemption Date		Amount
May 15, 2030	$	2,850,000
May 15, 2031		2,995,000
May 15, 2032		2,505,000
May 15, 2033		2,620,000
May 15, 2034		2,745,000

LCRA Transmission Services Corporation
Series 2004
Term Bond Maturing May 15, 2029

Redemption Date		Amount
May 15, 2026	$	4,185,000
May 15, 2027		4,185,000
May 15, 2028		4,185,000
May 15, 2029		4,185,000

LCRA Transmission Services Corporation
Series 2004
Term Bond Maturing May 15, 2033

Redemption Date		Amount
May 15, 2030	$	4,185,000
May 15, 2031		4,185,000
May 15, 2032		4,185,000
May 15, 2033		4,185,000

Series 2004
Term Bond Maturing May 15, 2024

Redemption Date		Amount
May 15, 2023	$	5,120,000
May 15, 2024		5,120,000

Series 2004
Term Bond Maturing May 15, 2026

Redemption Date		Amount
May 15, 2025	$	5,120,000
May 15, 2026		5,120,000

Series 2004
Term Bond Maturing May 15, 2029

Redemption Date		Amount
May 15, 2027	$	5,190,000
May 15, 2028		5,190,000
May 15, 2029		5,200,000

LCRA Transmission Services Corporation
Series 2003C
Term Bond Maturing May 15, 2028

Redemption Date		Amount
May 15, 2026	$	4,515,000
May 15, 2027		4,515,000
May 15, 2028		4,515,000

LCRA Transmission Services Corporation
Series 2003C
Term Bond Maturing May 15, 2033

Redemption Date		Amount
May 15, 2029	$	4,515,000
May 15, 2030		4,515,000
May 15, 2031		4,515,000
May 15, 2032		4,515,000
May 15, 2033		11,165,000

LCRA Transmission Services Corporation
Series 2003B
Term Bond Maturing May 15, 2031

Redemption Date		Amount
May 15, 2026	$	10,985,000
May 15, 2027		10,985,000
May 15, 2028		10,985,000
May 15, 2029		10,985,000
May 15, 2030		7,310,000
May 15, 2031		8,040,000

LCRA Transmission Services Corporation
Series 2003A
Term Bond Maturing May 15, 2032

Redemption Date		Amount
May 15, 2030	$	3,675,000
May 15, 2031		12,325,000
May 15, 2032		34,000,000

Series 2003
Term Bond Maturing May 15, 2028

Redemption Date	Amount
May 15, 2026	$ 3,795,000
May 15, 2027	3,985,000
May 15, 2028	4,185,000

Series 2003
Term Bond Maturing May 15, 2033

Redemption Date	Amount
May 15, 2029	$ 4,340,000
May 15, 2030	4,295,000
May 15, 2031	4,510,000
May 15, 2032	4,740,000
May 15, 2033	4,975,000

Series 2002
Term Bond Maturing May 15, 2031

Redemption Date	Amount
May 15, 2025	$ 780,000
May 15, 2026	815,000
May 15, 2027	6,405,000
May 15, 2028	6,440,000
May 15, 2029	6,525,000
May 15, 2030	8,610,000
May 15, 2031	8,645,000

Series 2001A
Term Bond Maturing May 15, 2026

Redemption Date	Amount
May 15, 2022	$ 6,935,000
May 15, 2023	5,845,000
May 15, 2024	6,145,000
May 15, 2025	6,460,000
May 15, 2026	6,780,000

Series 2001A
Term Bond Maturing May 15, 2032

Redemption Date	Amount
May 15, 2029	$ 4,500,000
May 15, 2030	4,500,000
May 15, 2031	4,500,000
May 15, 2032	4,505,000

Series 2001
Term Bond Maturing May 15, 2031

Redemption Date	Amount
May 15, 2027	$ 1,810,000
May 15, 2028	1,900,000
May 15, 2029	2,000,000
May 15, 2030	2,100,000
May 15, 2031	2,210,000

Series 2001
Term Bond Maturing May 15, 2026

Redemption Date	Amount
May 15, 2024	$ 10,885,000
May 15, 2025	11,210,000
May 15, 2026	3,330,000

Series 1999A
Term Bond Maturing May 15, 2021

Redemption Date	Amount
May 15, 2020	$ 36,330,000

5. Retirement and 401(k) Plans, Deferred Compensation, and Post-Employment Benefits

Retirement Plan: The Lower Colorado River Authority Retirement Plan (Plan) is a single-employer defined benefit pension plan and is administered by the LCRA Retirement Plan Board of Trustees. The Plan issues a stand-alone financial report that is available from the Board of Trustees. As a result of the amendments and restatements of the Plan during FY 2002, the Plan has submitted an application for a determination concerning the qualification of the Plan to the Internal Revenue Service. The previous Plan had received a favorable determination letter from the Internal Revenue Service and was exempt from federal income taxes, under the appropriate section of the Internal Revenue Code. LCRA anticipates that the restated Plan also will qualify for tax-exempt status.

The Plan provides retirement, death and disability benefits. Employees are not required to contribute to the Plan although the Plan retains employee contributions and associated liabilities for years prior to April 1, 1984, when the Plan did require employee contributions. Amendments to the Plan are made only with the authority of the LCRA Board of Directors.

Effective Jan. 1, 2002, the Plan was amended to provide cash balance benefit features. Active employees as of Dec. 31, 2001, were given the opportunity to remain participants under the pension provisions (Retirement Program A) or to elect to become participants under the cash balance provisions (Retirement Program B). Employees hired prior to Jan. 1, 2002, who elected Program A and who worked at least 1,000 hours per annum were eligible plan participants in the Plan upon completion of six months of service and become 100 percent vested after three complete years of service. Any employee that was employed by LCRA prior to Jan. 1, 2002, and who elected Program B were eligible to participate in the cash balance benefit plan as of Jan 1, 2002, and will be 100 percent vested after three complete years of service. Any employee hired after Jan. 1, 2002, who works at least 1,000 hours per annum will automatically be enrolled in Program B, will be eligible to participate in the Plan after three consecutive months of service and will be 100 percent vested after three complete years of service.

Under Program A, employees may retire with unreduced accrued benefits at age 65 with five years of service, or when the total of their age and service equals 80. Retirement benefits are based on years of service and salary levels at retirement. Under Program B, the value of the employee's account will be adjusted by increasing the balance by 4 percent of the employee's compensation paid per year. The value of the account earns an annual interest rate of 7 percent. The retirement benefit for an employee who has reached his or her normal retirement date is a single lump sum payment equal to the participant's accrued balance or monthly payments as provided by the Plan.

The LCRA makes annual contributions to the Plan that are actuarially determined as of each valuation date and consist of a normal cost contribution and an amortization of unfunded actuarial accrued liability contribution using the entry age normal actuarial cost method. Unfunded actuarial accrued liability contributions are determined using a 15- to 30-year level percentage of payroll open amortization methodology. The unfunded actuarial accrued liability is being amortized as a level percentage of payroll over a period of 13 years on an open basis.

The required employer contribution for FY 2006 was 8.4 percent of total employee payroll. The current recommended employer contributions for FY 2007 are 8.7 percent of total employee payroll. The costs of administering the Plan are paid by the Plan and are considered in the determination of the required employer contribution rate.

The required contribution was determined as of the Apr. 1, 2005 actuarial valuation using the entry age normal actuarial cost method. The original actuarial assumptions included (a) an 8 percent investment rate of return, net of administrative expenses and (b) projected salary increases of 4.5 to 12.5 percent varying by entry age group and attained age. Both (a) and (b) reflect an inflation component of 4 percent. Effective Apr. 1, 2006, the minimum recommended employer contributions were determined using an 18 year open amortization period.

Changes in plan provisions that impacted funding were an ad hoc cost of living adjustment to retirees effective Jan. 1, 2002, an increase in maximum benefits and compensation limitations imposed under the Internal Revenue Code, and revised assumptions for withdrawal and retirement due to cash balance benefits. Effective Apr. 1, 2006 changes in plan provisions include an amendment to the plan to include additional supplemental credited service, the number of years of Optional Credited Service that surviving spouses may purchase was increased to 10 years, and the pension plan was amended to include short-term disability pay.

Schedule of Funding Progress

Actuarial Valuation Date	(1) Actuarial Value of Assets[1]	(2) Actuarial Accrued Liability Entry Age	(3) Funded Ratio (1)/(2)	(4) Unfunded Actuarial Accrued Liability (2)-(1)	(5) Annual Covered Payroll[2]	(6) Unfunded Actuarial Accrued Liability as a Percentage of Covered Payroll (4)/(5)
April 1, 2004	$ 239,289,653	$ 319,622,320	74.9	$ 80,332,667	$ 128,454,336	62.5
April 1, 2005	253,994,422	346,643,812	73.3	92,649,390	136,103,586	68.1
April 1, 2006	269,195,679	382,758,278	70.3	113,562,599	143,978,576	78.9

[1] Actuarial value approximates market value.
[2] Based on projected payroll as of valuation date.

Three-Year Annual Pension Cost (APC) Trend Information

Fiscal Year Ending	APC	Percentage of APC Contributed	Net Pension Obligation (NPO)[1]
June 30, 2004	$10,962,373	100%	$ -
June 30, 2005	12,206,319	100	-
June 30, 2006	14,268,341	100	-

[1] NPO is zero since employer contributions have been equivalent to actuarially determined funding requirements for all fiscal years beginning Dec. 15, 1986.

401(k) Plan: LCRA's Retirement Benefits Board of Trustees administers this single-employer defined contribution plan. The Plan is accounted for on the accrual basis and all assets are recorded at fair value. The Plan has received a favorable determination letter from the Internal Revenue Service and is exempt from federal income taxes, under the appropriate section of the Internal Revenue Code.

Employees are eligible to participate in the Plan immediately upon employment. Eligible employees who elect to participate in the Plan may contribute a minimum of 1 percent of their annual compensation, not to exceed $15,000 in 2006. Employees age 50 or over may contribute an additional $5,000 in 2006. Effective Jan. 1, 2002, employees under Program A of the Pension Plan receive an LCRA matching contribution equal to 25 percent of the first 4 percent of compensation that the employee had elected to contribute to the plan. Under Program B of the Pension Plan, LCRA provides matching contributions equal to 100 percent of the first 4 percent of compensation and 50 percent of the next 2 percent of compensation that the employee has elected to contribute to the plan. Contributions made by both the employer and employee are vested immediately. Amendments to the Plan are made only with the authority of the LCRA Board.

Contributions by the LCRA and the employees for the years ended June 30, 2006 and 2005, are presented below:

	2006	2005
	(Dollars in Thousands)	
Employer contributions	$2,414	$1,954
Employee contributions	$8,471	$7,886

Post-Employment Benefits: LCRA provides post-employment health care benefits to retirees and to terminated employees eligible for such benefits. LCRA contributes approximately 78 percent of the retirees' health plan premiums but makes no contributions for terminated employees. These contributions are recognized currently as premiums are paid and totaled approximately $6.2 million and $4.2 million for FY 2006 and 2005, respectively. At June 30, 2006, there were 579 retirees and 12 terminated employees eligible for such benefits.

6. Commitments and Contingencies

Construction: LCRA's construction budget provides for capital improvement projects with cash requirements through FY 2011 of approximately $1.3 billion, including $275.5 million in FY 2007.

Customer Transmission Leases: LCRA leases and operates certain transmission facilities and equipment owned by 12 customers. The leases are the basis for LCRA to provide the same service to all of its customers and for the cost of such service to be shared by all customers on a consistent basis. Payments for the leased facilities vary from year to year and are based on the original cost of the facilities, adjusted for depreciation, and are updated annually to reflect additions, retirements and depreciation. The terms of the leases are perpetual, but may be terminated by LCRA or the lessors upon five years written notice. Lease expenses for FY 2006 and 2005 totaled $11.6 million and $10.9 million, respectively.

Coal and Rail Contracts: For FY 2006, approximately 67 percent of the fuel requirements for the Fayette Power Project Units 1 and 2 (FPP 1 & 2) were supplied by one multi-year contract with mines in Wyoming's Powder River Basin. The contract has a fixed price for its entire term. Further, the annual volume is subject to adjustment based upon railroad performance. In the third quarter of FY 2007, a new multi-year contract will provide coal at a separate fixed price per year with a fixed volume per year. In FY 2007, multi-year contracts will supply approximately 74 percent of FPP 1 & 2's coal needs. During FY 2006 and 2005, LCRA's multi-year contract purchases totaled $11.1 million and $9.7 million, respectively.

For FY 2006 approximately 70 percent of the fuel requirements for Fayette Power Project Unit 3 (FPP 3) were supplied by two multi-year contracts with mines in Wyoming's Powder River Basin. The first contract, which ended in the second quarter of FY 2006, was for an annual volume subject to LCRA's discretion, within a specified range, at a fixed price for its entire term. The second contract has a separate fixed price per year that varies based on which mine supplies the coal and the volume is fixed for each calendar year. LCRA's purchases under these contracts totaled $8.4 and $8.2 million for FY 2006 and 2005, respectively. Starting in the third quarter of FY 2007, two new multi-year contracts will supply part of FPP 3's fuel requirements. The first new multi-year contract has a separate fixed price per year for an annual fixed volume. The second new multi-year contract has a fixed price and annual volume for its term. In FY 2007, these multi-year contracts will supply approximately 72 percent of FPP 3's coal needs.

LCRA and Austin Energy have a multi-year transportation agreement with one rail carrier to ship Powder River Basin coal to all three units at FPP. For the second half of FY 2006 and the first half of FY 2007, FPP committed to ship a specific, minimum volume of coal from the Powder River Basin under a common carrier tariff with a second rail carrier. Freight costs incurred by LCRA were approximately $45 million and $41.9 million in FY 2006 and FY 2005, respectively.

Natural Gas: LCRA has several long-term contracts to provide a portion of the natural gas requirements to its gas-fired generation units, through April 2014. LCRA is committed to buy a fixed amount of gas annually. LCRA's gas purchases under these contracts totaled $142.5 million for FY 2006 and $108.6 million for FY 2005, based on price indices. LCRA also pays approximately $2.3 million per year for firm transportation rights on intrastate pipelines which deliver gas from other supply points.

Purchased Power: LCRA has seventeen contracts with power marketers who provide firm electric energy ranging from 50 MW to 600 MW per month, for the period May 2006 through September 2008. The total minimum commitment from these contracts is more than $2.5 million plus energy payments.

Wind Power: LCRA is committed to purchase 35 MW of wind power capacity from Texas's first commercial wind power plant, the Texas Wind Power Project. LCRA in turn sells 10 MW of this capacity to Austin Energy. During FY 2006, LCRA purchased 30 MW of wind power capacity from the Delaware Mountain Wind Farm. In FY 2006, LCRA also purchased 51 MW of wind power capacity from the Indian Mesa Wind Farm. Total wind power capacity is 116 MW, of which 106 MW is for LCRA and its customers. LCRA expects to pay approximately $9.4 million in FY 2007 for purchases from all wind power plants, increasing to approximately $11.8 million in FY 2014.

Water Project Study: LCRA has entered into an agreement with the San Antonio Water System (SAWS) to study the feasibility of implementing the LCRA-SAWS Water Project. The project addresses long-term water needs in both the lower Colorado River basin and the San Antonio area. As proposed, the project would conserve and develop water in the region through the use of off-channel storage facilities, the conjunctive use of groundwater for agriculture, and agricultural conservation. The project would provide between 50,000 to 150,000 acre-feet of water per year for the San Antonio region, provide a more reliable water supply for agricultural needs in the lower Colorado River basin, address rural water needs above the LCRA Highland Lakes, and increase lake levels in the Lakes Buchanan and Travis over those expected without the project. The study phase, estimated to be completed by March 2010 at a total cost of approximately $43 million, includes engineering feasibility and environmental studies and costs to obtain necessary permits for development and transfer of water. LCRA, in its role as project manager, receives advances from SAWS to fund this study. SAWS has the option to cancel the study, with a 100 percent refund of unexpended funds and a 50 percent refund of expended funds due to SAWS when cancelled. As of June 30, 2006, LCRA has received $20.4 million from SAWS and has expended $16 million in study costs.

Insurance Self-Funding: In addition to the purchase of commercial insurance, LCRA has established a self-insurance program to finance risk of loss. LCRA is exposed to various risks of loss related to torts; theft of, damage to and destruction of assets; errors and omissions; injuries to employees; and natural disasters. LCRA self-funds each worker's compensation claim up to $300,000, and each general liability claim up to a maximum of $2 million dependent on the insurance policy deductible. Self-funding of property damage varies from $100,000 to $2.5 million depending on the insurance deductible. Any claims or damages above self-funded amounts are covered by commercial general insurance. Settled claims have not exceeded commercial insurance coverage in any of the past three fiscal years. Based on an insurance risk analysis, LCRA carries no commercial insurance on transmission lines.

Accrued Liability: The accrued liability presented in the table below is associated with obligations resulting from environmental regulations established by federal, state and local authorities. Although the effect of future environmental regulations upon existing and proposed facilities and operations cannot be determined, LCRA monitors proposed changes and takes actions necessary to mitigate adverse impacts to its operations. At the present, no materially adverse impacts are anticipated.

Changes in the accrued liability amount for FY 2005 and 2006 were as follows:

	Balance Beginning of Year	Changes in Estimates	Payments	Balance End of Year
FY 2005	$ 2,423,000	$ -	$ 437,000	$ 1,986,000
FY 2006	$ 1,986,000	$ 336,000	$ 331,000	$ 1,991,000

Capital Program: LCRA's forecasted capital program includes $144.3 million for LCRA's share of the cost of SO_2 scrubbers for two coal-fired generating units jointly owned by LCRA and the City of Austin. The cost of the scrubbers is subject to revision upon the completion of technological evaluations and detailed engineering studies. The scrubbers must be installed by October 2012, under the provisions of a flexible air quality permit received from the Texas Commission on Environmental Quality in 2002.

Litigation: There are various lawsuits in which LCRA is involved. LCRA's management, including its general counsel, estimates that the potential claims against LCRA not covered by insurance resulting from such litigation would not materially affect LCRA's financial position, results of operations and cash flows.

7. Capital Activity

Capital activity for the year ended June 30, 2006, was as follows:

	Beginning Balance	Additions	Transfers from Construction in Progress	Retirements	Depreciation/ Depletion	Ending Balance
			(Dollars in Thousands)			
Utility plant in service:						
Depreciable assets	$ 3,042,455	$ 2,354	$ 303,310	$ (52,688)	$	$ 3,295,431
Non-depreciable assets	30,343		6,533	(1,014)		35,862
Total Utility Plant in Service	3,072,798	2,354	309,843	(53,702)	-	3,331,293
Construction work in progress:						
Non-depreciable assets	208,184	305,638	(314,627)	9,813		209,008
Oil and gas property:						
Depletable assets	28,158					28,158
Other physical property:						
Depreciable assets	22,362	129	4,784			27,275
Non-depreciable assets	20,073					20,073
Total Other physical property	42,435	129	4,784	-	-	47,348
Less accumulated depreciation	(1,074,952)			33,720	(109,704)	(1,150,936)
Capital assets, net	$ 2,276,623	$ 308,121	$ -	$ (10,169)	$ (109,704)	$ 2,464,871

Capital activity for the year ended June 30, 2005, was as follows:

	Beginning Balance	Additions	Transfers from Construction in Progress	Retirements	Depreciation/ Depletion	Ending Balance
	(Dollars in Thousands)					
Utility plant in service:						
Depreciable assets	$ 2,751,839	$	$ 315,852	$ (25,236)	$	$ 3,042,455
Non-depreciable assets	26,244		3,889	210		30,343
Total Utility Plant in Service	2,778,083	-	319,741	(25,026)	-	3,072,798
Construction work in progress:						
Non-depreciable assets	283,374	238,799	(319,974)	5,985		208,184
Oil and gas property:						
Depletable assets	28,158					28,158
Other physical property:						
Depreciable assets	21,519		881	(38)		22,362
Non-depreciable assets	20,094			(21)		20,073
Total Other physical property	41,613	-	881	(59)	-	42,435
Less accumulated depreciation	(984,209)		(648)	8,034	(98,129)	(1,074,952)
Capital assets, net	$ 2,147,019	$ 238,799	$ -	$ (11,066)	$ (98,129)	$ 2,276,623

8. Asset Retirement Obligations

In fiscal year 2003, LCRA adopted FASB Statement No. 143, “Accounting for Asset Retirement Obligations,” which applies to retirement obligations that result from the acquisitions, construction, development or normal operations of long-lived assets. LCRA concluded that no asset retirement obligations were to be recorded upon implementation of FASB Statement No. 143.

In March 2005, the FASB issued FIN No. 47, “Accounting for Conditional Asset Retirement Obligations – an interpretation of FASB Statement No 143.” FIN No. 47 clarifies the term, “conditional asset retirement obligation,” as used in FASB Statement No. 143. FIN No. 47 mandates that an entity recognize the fair value of a legal obligation to perform an asset retirement activity in which the time and (or) the method of settlement are conditional on a future event that may or may not be within the control of the entity. FIN No. 47 is effective for fiscal years ending after December 15, 2005.

For fiscal year 2006, LCRA has recorded conditional asset retirement obligations totaling $9.3 million, increasing net utility plant in service by $1.4 million and regulatory assets by $7.9 million. Because LCRA is a regulated entity which is subject to the provisions of FASB Statement No. 71, LCRA believes it will recover all cumulative and current year costs in future rates. As a result, there is no net income effect of adopting FIN No. 47 in fiscal year 2006.

LCRA has identified conditional asset retirement obligations which are primarily related to the removal and disposition of asbestos-containing material, the closure of generation facility waste collection ponds, and the closure of natural gas wells and natural gas pipelines.

LCRA has also identified other conditional asset retirement obligations associated with certain underground pipelines that have an indeterminate life. Accordingly, the fair value of the conditional asset retirement obligation is not reasonably estimable. A liability for these obligations will be recorded when a fair value is determinable.

The following table illustrates the effect of FIN No. 47 if the interpretation had been applied beginning fiscal year 2004. Pro forma amounts for the periods prior to adoption of FIN No. 47 were measured using assumptions consistent with the period of adoption.

	2006	2005	2004
		(Dollars in Millions)	
Asset Retirement Obligation beginning balance	8.8	8.4	8.0
Accretion	0.5	0.4	0.4
Additions	-	-	-
Asset Retirement Obligation ending balance	9.3	8.8	8.4

9. Segment Reporting

Governments that use enterprise fund accounting and reporting standards to report their activities are required to present segment information. A segment is an identifiable activity reported as or within an enterprise fund or another stand-alone entity that has one or more bonds outstanding with a revenue stream pledged in support of that debt. In addition, the activity's revenues, expenses, gains and losses, assets, and liabilities are required to be accounted for separately. An external party should impose the requirements for separate accounting. LCRA TSC qualifies as a segment.

LCRA TSC was created by LCRA to comply with the requirements of SB 7. LCRA transferred all of the assets of its regulated electric transmission and transformation businesses to LCRA TSC effective on Jan. 1, 2002.

Segment information for LCRA TSC:

LCRA TRANSMISSION SERVICES CORPORATION -SEGMENT INFORMATION
BALANCE SHEETS
(Dollars in Thousands)

	June 30, 2006	June 30, 2005
Assets		
Current Assets	$ 75,168	$ 54,354
Long-Term Assets		
Restricted cash and cash equivalents	1,271	20,344
Restricted investments	114	220
Accounts receivable from LCRA - restricted	37,552	25,289
Capital assets:		
Utility plant in service	1,211,187	1,048,100
Construction work in progress	87,565	58,718
Less accumulated depreciation	(217,497)	(188,349)
Capital assets, net	1,081,255	918,469
Deferred charges:		
Costs to be recovered from future revenues	41,621	40,149
Issue costs	16,469	13,607
Deferred charges, net	58,090	53,756
Total long-term assets	1,178,282	1,018,078
Total Assets	$ 1,253,450	$ 1,072,432
Liabilities		
Current Liabilities	$ 62,314	$ 165,863
Long-Term Liabilities		
Accounts payable to LCRA from construction fund	29,061	22,584
Accounts payable from restricted assets	48,816	29,040
Asset retirement obligation	68	-
Bonds, notes, and loans payable	973,075	736,551
Total long-term liabilities	1,051,020	788,175
Total liabilities	1,113,334	954,038
Equity		
Invested in capital assets, net of related debt	80,649	74,536
Unrestricted	59,467	43,858
Total equity	140,116	118,394
Total Liabilities and Equity	$ 1,253,450	$ 1,072,432

LCRA TRANSMISSION SERVICES CORPORATION - SEGMENT INFORMATION
STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN EQUITY
(*Dollars in Thousands*)

	Year Ended June 30, 2006	Year Ended June 30, 2005
Operating Revenues		
Transmission	$ 156,249	$ 142,707
Transformation	8,973	8,524
Other	614	131
Total operating revenues	165,836	151,362
Operating Expenses		
Operations	51,988	57,528
Maintenance	10,370	8,805
Depreciation and amortization	32,937	25,581
Total operating expenses	95,295	91,914
Operating income	70,541	59,448
Nonoperating Revenues (Expenses)		
Interest and other income	3,353	2,730
Loss on disposition of property	(5,259)	(10,848)
Interest on debt	(45,196)	(38,082)
Other expenses	(5,026)	(3,660)
Total nonoperating revenues (expenses)	(52,128)	(49,860)
Income before costs to be recovered from revenues, capital contributions, transfers in, and special item	18,413	9,588
Costs To Be Recovered from Revenues	1,419	11,429
Capital Contributions	2,384	99
Income before transfers in and special item	22,216	21,116
Transfers In	829	276
Special Item - Loss on Early Defeasance of Debt	(1,323)	-
Change in Equity	21,722	21,392
Total Equity, Beginning of Year	118,394	97,002
Total Equity, End of Year	$ 140,116	$ 118,394

LCRA TRANSMISSION SERVICES CORPORATION - SEGMENT INFORMATION
STATEMENTS OF CASH FLOWS

(Dollars in Thousands)

	Year Ended June 30, 2006	2005
Cash Flows From Operating Activities		
Cash received from customers	$ 164,919	$ 160,412
Cash payments for goods and services	(65,585)	(79,242)
Net cash provided by operating activities	99,334	81,170
Cash Flows From Noncapital Financing Activities		
Other income and expenses	(5,026)	(3,660)
Net cash used in noncapital financing activities	(5,026)	(3,660)
Cash Flows From Capital and Related Financing Activities		
Expenditures for property, plant and equipment	(174,855)	(163,368)
Issuance costs	(3,683)	(1,897)
Proceeds from long-term debt issues	265,927	128,998
Proceeds from commercial paper	145,000	171,700
Principal payments on long-term debt	(51,749)	(38,282)
Payment to defease and refund debt and related issue costs	(250,000)	(120,500)
Interest paid	(26,572)	(16,881)
Cash received on sale of assets	149	92
Capital contributions	2,384	99
Accounts payable to LCRA	(6,977)	(16,939)
Net cash used in capital and related financing activities	(100,376)	(56,978)
Cash Flows From Investing Activities		
Sale and maturity of investment securities	60,030	34,984
Purchase of investment securities	(68,268)	(46,937)
Interest received	3,916	1,319
Net cash used in investing activities	(4,322)	(10,634)
Net Increase (Decrease) in Cash and Cash Equivalents	(10,390)	9,898
Cash and Cash Equivalents, Beginning of Year	31,608	21,710
Cash and Cash Equivalents, End of Year	$ 21,218	$ 31,608

LCRA TRANSMISSION SERVICES CORPORATION - SEGMENT INFORMATION
STATEMENTS OF CASH FLOWS
(Dollars in Thousands)

	Year Ended June 30, 2006	Year Ended June 30, 2005
Reconciliation of Operating Income to Net Cash Flows Provided by Operating Activities:		
Operating income	$ 70,541	$ 59,448
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation and amortization	32,937	25,581
Changes in assets and liabilities:		
Accounts receivable - trade	(1,834)	9,050
Inventories	(2,524)	(1,096)
Current liabilities	214	1,636
Other deferred charges and long-term liabilities	-	(13,449)
Net cash provided by operating activities	$ 99,334	$ 81,170
Noncash Investing Activities		
Investment market adjustments	$ (573)	$ 111
Noncash Financing for Property, Plant and Equipment Expenditures		
Asset retirement obligation	$ 68	$ -

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