

BANDERA ELECTRIC COOPERATIVE, INC.

BANDERA, TEXAS

FINANCIAL STATEMENTS WITH ACCOMPANYING INFORMATION

FOR THE YEARS ENDED DECEMBER 31, 2008 AND 2007

AND

REPORT OF CERTIFIED PUBLIC ACCOUNTANTS

BOLINGER, SEGARS, GILBERT & MOSS, L.L.P.

**CERTIFIED PUBLIC ACCOUNTANTS
LUBBOCK, TEXAS**

BANDERA ELECTRIC COOPERATIVE, INC.

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BANDERA, TEXAS**

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FOR THE YEARS ENDED DECEMBER 31, 2008 AND 2007**

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BOLINGER, SEGARS, GILBERT & MOSS, L.L.P.

CERTIFIED PUBLIC ACCOUNTANTS

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INDEPENDENT AUDITORS' REPORT

**Board of Directors
Bandera Electric Cooperative, Inc.
Bandera, Texas**

We have audited the accompanying balance sheet of Bandera Electric Cooperative, Inc. as of December 31, 2008 and 2007, and the related statements of income and patronage capital and cash flows for the years then ended. These financial statements are the responsibility of the Cooperative's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit 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 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 audit provides 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 Bandera Electric Cooperative, Inc. as of December 31, 2008 and 2007, and the results of its operations and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Bolinger, Segars, Gilbert & Moss LLP

Certified Public Accountants

March 11, 2009

BANDERA ELECTRIC COOPERATIVE, INC.

Exhibit A

BALANCE SHEET
DECEMBER 31, 2008 AND 2007

ASSETS

	December 31,	
	2008	2007
UTILITY PLANT AT COST		
Electric Plant in Service	\$ 146,500,363	\$ 138,085,698
Construction Work in Progress	7,334,024	6,176,602
	\$ 153,834,387	\$ 144,262,300
Less: Accumulated Provision for Depreciation	30,601,804	28,111,034
	\$ 123,232,583	\$ 116,151,266
OTHER PROPERTY AND INVESTMENTS - AT COST OR STATED VALUE		
Investments in Associated Organizations	\$ 3,277,098	\$ 3,104,282
Other Investments	24,578	43,267
	\$ 3,301,676	\$ 3,147,549
CURRENT ASSETS		
Cash - General	\$ 1,154,681	\$ 483,666
Other Investments - Life Insurance - Current		1,219,197
Accounts Receivable (Less allowance for uncollectibles of \$183,716 in 2008 and \$173,017 in 2007)	3,294,543	4,541,968
Underbilled Fuel Cost Recovery		46,115
Accrued Unbilled Revenue	1,726,251	
Materials and Supplies Inventory	179,002	170,034
Other Current and Accrued Assets	252,403	256,376
Total Current Assets	\$ 6,606,880	\$ 6,717,356
DEFERRED CHARGES	\$ 60,991	\$ 132,740
TOTAL ASSETS	\$ 133,202,130	\$ 126,148,911

EQUITIES AND LIABILITIES

EQUITIES		
Memberships	\$ 508,400	\$ 499,025
Patronage Capital	46,436,560	45,004,922
Other Equities	593,434	540,788
Accumulated Other Comprehensive Loss	(700,941)	(776,989)
	\$ 46,837,453	\$ 45,267,746
LONG-TERM DEBT		
CFC Mortgage Notes Less Current Maturities	\$ 61,385,341	\$ 56,854,826
ACCUMULATED PROVISION FOR PENSIONS AND BENEFITS	\$ 5,452,356	\$ 5,109,330
CURRENT LIABILITIES		
Current Maturities of Long-Term Debt	\$ 1,990,387	\$ 2,550,446
Advances on Line of Credit - CFC		1,100,286
Accounts Payable - Other	4,325,688	3,789,354
Consumer Deposits and Prepayments	498,668	519,678
Accrued Power Cost	878,362	
Accrued Taxes	1,413	
Other Current and Accrued Liabilities	843,625	771,456
Overbilled Fuel Cost Recovery	1,660,992	
Total Current Liabilities	\$ 10,199,135	\$ 8,731,220
DEFERRED CREDITS	\$ 9,327,845	\$ 10,185,789
TOTAL EQUITIES AND LIABILITIES	\$ 133,202,130	\$ 126,148,911

See accompanying notes to financial statements.

BANDERA ELECTRIC COOPERATIVE, INC.

Exhibit B

STATEMENT OF INCOME AND PATRONAGE CAPITAL
FOR THE YEARS ENDED DECEMBER 31, 2008 AND 2007

	December 31,				Increase (Decrease)
	2008		2007		
	Amount	%	Amount	%	
OPERATING REVENUES					
Residential	\$ 42,073,573	67.9	\$ 35,737,627	71.1	\$ 6,335,946
Irrigation	76,622	0.1	35,008	0.1	41,614
Commercial and Industrial	15,519,709	25.1	12,034,844	23.9	3,484,865
Public Street and Highway Lighting	48,890	0.1	42,600	0.1	6,290
Unbilled Revenue	1,726,251	2.8			1,726,251
Other Operating Revenues	2,486,654	4.0	2,409,527	4.8	77,127
Total Operating Revenues	\$ 61,931,699	100.0	\$ 50,259,606	100.0	\$ 11,672,093
OPERATING EXPENSES					
Purchased Power	\$ 42,487,092	68.6	\$ 31,586,573	62.8	\$ 10,900,519
Transmission - Operation	142,637	0.1	102,407		40,230
Distribution - Operation	1,954,661	3.2	2,203,668	4.4	(249,007)
Distribution - Maintenance	3,102,511	5.0	2,494,327	5.0	608,184
Consumer Accounts	1,447,201	2.3	1,456,331	2.9	(9,130)
Customer Service and Information	142,953	0.2	113,951	0.2	29,002
Administrative and General	4,114,305	6.6	3,618,827	7.2	495,478
Depreciation and Amortization	4,204,686	6.8	3,890,180	7.7	314,506
Taxes	100	0.0		0.0	100
Other Interest	23,450	0.0	23,324		126
Miscellaneous Income Deductions	119,024	0.2	126,695	0.3	(7,671)
Total Operating Expenses	\$ 57,738,620	93.1	\$ 45,616,283	90.5	\$ 12,122,337
OPERATING MARGINS - Before Fixed Charges	\$ 4,193,079	6.9	\$ 4,643,323	9.4	\$ (450,244)
FIXED CHARGES					
Interest on Long-Term Debt	\$ 3,323,903	5.4	\$ 3,009,110	6.0	\$ 314,793
Amortization of Gain on Reacquired Debt	(251,256)	(0.4)	(261,641)	(0.5)	10,385
	\$ 3,072,647	5.0	\$ 2,747,469	4.3	\$ 325,178
OPERATING MARGINS - After Fixed Charges	\$ 1,120,432	1.9	\$ 1,895,854	5.1	\$ (775,422)
Capital Credits	700,090	1.1	484,135	1.0	215,955
NET OPERATING MARGINS	\$ 1,820,522	3.0	\$ 2,379,989	6.1	\$ (559,467)
NONOPERATING MARGINS					
Interest Income	\$ 42,170	0.1	\$ 34,296	0.1	\$ 7,874
Other Nonoperating Income	22,304		17,526		4,778
Gain on Sale of Property			9,800		(9,800)
	\$ 64,474	0.1	\$ 61,622	0.1	\$ 2,852
NET MARGINS	\$ 1,884,996	3.1	\$ 2,441,611	6.2	\$ (556,615)
OTHER COMPREHENSIVE INCOME (LOSS)					
FASB Statement 158	76,048		(776,989)		
COMPREHENSIVE INCOME	\$ 1,961,044		\$ 1,664,622		
FASB Statement 158	(76,048)		776,989		
NET MARGINS	\$ 1,884,996		\$ 2,441,611		
PATRONAGE CAPITAL - BEGINNING OF YEAR	45,004,922		43,067,194		
Patronage Capital Retired	(453,358)		(503,883)		
PATRONAGE CAPITAL - END OF YEAR	\$ 46,436,560		\$ 45,004,922		

See accompanying notes to financial statements.

BANDERA ELECTRIC COOPERATIVE, INC.

Exhibit C

**STATEMENT OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2008 AND 2007**

	December 31,	
	2008	2007
CASH FLOWS FROM OPERATING ACTIVITIES		
Net Margins	\$ 1,884,996	\$ 2,441,611
Adjustments to Reconcile Net Margins to Net Cash Provided by Operating Activities		
Depreciation and Amortization	4,463,124	4,063,908
Amortized Gain on Retirement of RUS Debt	(251,256)	(261,641)
Capital Credits - Non Cash	(370,108)	(223,006)
Accumulated Provision for Pensions and Benefits Accrual	617,508	617,508
Deferred Charges	71,749	(31,662)
Deferred Credits	(606,689)	372,420
Accounts Receivable	(478,826)	(411,296)
Power Cost Adjustments Over Collected	1,707,108	(81,234)
Inventories and Prepaid Expenses	(4,995)	(28,776)
Payables and Accrued Expenses	1,467,268	410,591
Net Cash Provided by Operating Activities	\$ 8,499,879	\$ 6,868,423
CASH FLOWS FROM INVESTING ACTIVITIES		
Additions to Utility Plant	\$ (11,286,296)	\$ (11,793,734)
Plant Removal Costs (in Excess of) Salvage and Other Credits	(258,145)	(440,538)
Other Property and Investments	1,435,178	(54,621)
Net Cash Used in Investing Activities	\$ (10,109,263)	\$ (12,288,893)
CASH FLOWS FROM FINANCING ACTIVITIES		
Short-Term Lines of Credit Activity - Net	\$ (1,100,286)	\$ 970,207
Payments on Long-Term Debt to CFC	(2,529,544)	(2,562,732)
Advances on CFC Long-Term Debt	6,500,000	8,000,000
Payments on Accumulated Provision for Pensions and Benefits	(198,434)	(194,629)
Other Equities	52,646	66,294
Retirement of Patronage Capital	(453,358)	(503,883)
Increase in Memberships - Net	9,375	7,230
Net Cash Provided by Financing Activities	\$ 2,280,399	\$ 5,782,487
INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	\$ 671,015	\$ 362,017
CASH AND CASH EQUIVALENTS - BEGINNING OF YEAR	483,666	121,649
CASH AND CASH EQUIVALENTS - END OF YEAR	\$ 1,154,681	\$ 483,666
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION		
Cash Paid During the Year for:		
Interest on Long-Term Debt	\$ 3,298,602	\$ 2,926,786
Income Taxes	\$ 0	\$ 0

See accompanying notes to financial statements.

BANDERA ELECTRIC COOPERATIVE, INC.

NOTES TO FINANCIAL STATEMENTS

1. Nature of Operations and Summary of Significant Accounting Policies

Nature of Operations

Bandera Electric Cooperative, Inc. (the Cooperative) is a non-profit company organized to provide electric service at the retail level to primarily residential and commercial accounts in a designated service area. Power delivered at retail is purchased wholesale from the Lower Colorado River Authority and other suppliers. Any revenues earned in excess of costs incurred are allocated to members of the Cooperative and are reflected as patronage capital in the balance sheet.

System of Accounts

The accounting records of the Cooperative are maintained in accordance with the Uniform System of Accounts as prescribed by the Federal Energy Regulatory Commission for Class A and B electric utilities modified for electric borrowers of the National Rural Utilities Cooperative Finance Corporation (CFC).

Electric Plant, Maintenance, and Depreciation

Electric plant is stated at the original cost of construction which includes the cost of contracted services, direct labor, materials, and overhead items. Contributions from others toward the construction of electric plant are credited to the applicable plant accounts.

When property which represents a retirement unit is replaced or removed, the average cost of such property as determined from the continuing property records is credited to electric plant and such cost, together with cost of removal less salvage, is charged to the accumulated provision for depreciation.

Maintenance and repairs, including the renewal of minor items of plant not comprising a retirement unit, are charged to the appropriate maintenance accounts, except that repairs of transportation and service equipment are charged to clearing accounts and redistributed to operating expense and other accounts.

Cash and Cash Equivalents

For purposes of the statement of cash flows, cash and temporary cash investments are considered cash and cash equivalents.

Accounts Receivable

In the normal course of business the Cooperative recognizes accounts receivable for energy delivered and billed. The Cooperative allows 16 days from the date of the bill for payment to be received or the service is considered delinquent. Delinquent accounts receive a penalty of five percent. If no payment is received within 24 days or a deferred payment agreement is not in place, the account is subject to disconnect.

The Cooperative provides an allowance for doubtful accounts to recognize the portion of receivables considered uncollectible. The Cooperative accrues amounts monthly to the allowance. The allowance is estimated based on historical trends, aging of receivables and review of potential bad debts. The Board of Directors reviews delinquent accounts annually and charges off accounts over two years old.

BANDERA ELECTRIC COOPERATIVE, INC.

NOTES TO FINANCIAL STATEMENTS

Inventories

Materials and supplies inventories are valued at average unit cost.

Electric Revenues

Certain aspects of the Cooperative's operations are under the jurisdiction of the Public Utility Commission of Texas; however, the Cooperative is no longer regulated for ratemaking purposes. The Cooperative records electric revenues as billed to customers on a monthly basis. Revenue is also accrued for power delivered but not billed at the end of each month.

The Cooperative's tariffs for electric service include power cost adjustment clauses under which billings to customers are adjusted to reflect changes in the cost of purchased power. In order to match power cost and related revenues, underbilled power cost to be billed to consumers in subsequent periods is recognized as a current asset - "Power Cost Adjustment - Undercollected" and as an increase of classified operating revenues on the statement of income and patronage capital. Also, overbilled power cost to be credited to consumers in subsequent periods is recognized as a current liability - "Power Cost Adjustments - Overcollected" – and as a reduction of classified operating revenues on the statement of income and patronage capital. The Cooperative had overcollected \$1,660,992 and undercollected power cost of \$46,115 at December 31, 2008 and 2007, respectively.

Income Tax Status

The Cooperative is an exempt organization for federal income tax purposes under Section 501(c)(12) of the Internal Revenue Code.

Group Concentration of Credit Risk

The Cooperative's headquarters facility is located in Bandera, Texas. The service area includes members located in all or parts of a seven county area surrounding the city of Bandera. The Cooperative records a receivable for electric revenues as billed on a monthly basis. The Cooperative may require a deposit from new members upon connection which is applied to unpaid bills and fees in the event of default. The deposit accrues interest annually and is returned along with accrued interest after one year of prompt payments. As of December 31, 2008 and 2007, deposits on hand totaled \$498,668 and \$519,678, respectively.

The Cooperative maintains its cash balances in institutions insured by the Federal Deposit Insurance Corporation (FDIC). The cash balances exceeded applicable insurance coverages at times during the year.

Patronage Capital Certificates

Patronage capital from associated organizations is recorded at the stated amount of the certificate.

Use of Estimates in the Preparation of Financial Statements

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

BANDERA ELECTRIC COOPERATIVE, INC.

NOTES TO FINANCIAL STATEMENTS

2. Assets Pledged

All assets are pledged as security for the long-term debt due the National Rural Utilities Cooperative Finance Corporation.

3. Electric Plant

The major classes of electric plant are as follows:

	December 31,	
	2008	2007
Transmission Plant	\$ 11,818,671	\$ 11,685,968
Distribution Plant	122,565,286	114,927,303
General Plant	12,116,406	11,472,427
Total Electric Plant in Service	\$ 146,500,363	\$ 138,085,698
Construction Work in Progress	7,334,024	6,176,602
 Total Electric Plant	 <u>\$ 153,834,387</u>	 <u>\$ 144,262,300</u>

Provision for depreciation of electric plant is computed using straight-line rates as follows:

Transmission Plant	2.75%
Distribution Plant	2.75%
General Plant	
Structures and Improvements	2.0%
Office Furniture and Fixtures	7.0% - 33.3%
Transportation Equipment	20.0% - 33.3%
Store Equipment	20.0%
Power Operated Equipment	10.0% - 20.0%
Communications Equipment	5.4% - 33.3%
Miscellaneous Equipment	6.0% - 33.3%
Tools, Shop, and Garage Equipment	6.0% - 33.3%
Laboratory Equipment	6.0% - 33.3%

Depreciation and amortization for the years ended December 31, 2008 and 2007, was \$4,463,124 and \$4,063,908, respectively, of which \$4,204,686 and \$3,890,180, was charged to depreciation expense and \$258,438 and \$173,728, was allocated to other accounts.

BANDERA ELECTRIC COOPERATIVE, INC.

NOTES TO FINANCIAL STATEMENTS

4. Investments in Associated Organizations

Investments in associated organizations consisted of:

	<u>December 31,</u>	
	<u>2008</u>	<u>2007</u>
CFC		
Capital Term Certificates	\$ 1,578,778	\$ 1,558,187
Patronage Capital	787,466	711,146
Hill Country Telephone		
Patronage Capital	69,122	66,231
Texas Electric Cooperatives, Inc.		
Patronage Capital	821,169	698,708
Other	20,563	70,010
	<u> </u>	<u> </u>
Total	<u>\$ 3,277,098</u>	<u>\$ 3,104,282</u>

5. Inventories

Materials and supplies inventories consisted of:

	<u>December 31,</u>	
	<u>2008</u>	<u>2007</u>
Construction Materials and Supplies	\$ 107,147	\$ 107,147
Resale Material	69,164	59,425
Transportation Supplies	2,691	3,462
	<u> </u>	<u> </u>
Total	<u>\$ 179,002</u>	<u>\$ 170,034</u>

Texas Electric Cooperative sells material to the Cooperative as needed, thus reducing the need to carry large inventory balances.

6. Deferred Charges

Deferred charges included the following:

	<u>December 31,</u>	
	<u>2008</u>	<u>2007</u>
Work Plans	\$ 60,991	\$ 132,198
Other		542
	<u> </u>	<u> </u>
Total	<u>\$ 60,991</u>	<u>\$ 132,740</u>

BANDERA ELECTRIC COOPERATIVE, INC.

NOTES TO FINANCIAL STATEMENTS

7. Return of Capital

The mortgage agreements contain provisions that must be met for the Cooperative to make patronage capital retirements. These provisions include minimum equity, debt service, and earnings ratios. The Cooperative is in compliance with these provisions at December 31, 2008 and 2007. Patronage capital totaling \$453,358 and \$503,883 was retired during 2008 and 2007, respectively.

8. Patronage Capital

	December 31,	
	<u>2008</u>	<u>2007</u>
Assigned	\$ 44,551,564	\$ 42,563,312
Assignable	<u>1,884,996</u>	<u>2,441,610</u>
Total	<u>\$ 46,436,560</u>	<u>\$ 45,004,922</u>

9. Other Equities

	December 31,	
	<u>2008</u>	<u>2007</u>
Capital Credits Payable - Under \$5	\$ 18,620	\$ 14,555
Retired Capital Credits - Gain - Estates	<u>574,814</u>	<u>526,233</u>
Total	<u>\$ 593,434</u>	<u>\$ 540,788</u>

10. Mortgage Notes – CFC

Following is a summary of long-term debt due CFC and maturing at various times from 2009 to 2045:

	December 31,	
	<u>2008</u>	<u>2007</u>
Variable Rate Notes - Currently 5.40%	\$ 7,591,398	\$ 1,136,415
Fixed Rate Notes - 4.55% to 7.19%	<u>55,784,330</u>	<u>58,268,857</u>
	63,375,728	59,405,272
Less: Current Maturities	<u>\$ 1,990,387</u>	<u>\$ 2,550,446</u>
Total	<u>\$ 61,385,341</u>	<u>\$ 56,854,826</u>

BANDERA ELECTRIC COOPERATIVE, INC.

NOTES TO FINANCIAL STATEMENTS

Principal and interest installments on the above notes are due quarterly. Annual maturities of long-term debt due CFC for the next five years are as follows:

2009	1,990,387
2010	2,104,394
2011	2,225,088
2012	2,351,699
2013	2,488,092

The Cooperative has \$30,335,000 available from unadvanced funds.

11. Short-Term Borrowing

The Cooperative has a line of credit at a variable interest rate with CFC not to exceed \$20,000,000. The balance outstanding at December 31, 2008 and 2007, was \$0 and \$1,100,286, respectively. Subsequent to year end the Cooperative increased it's line of credit with CFC to \$30,000,000.

12. Operating Leases

The Cooperative leases certain vehicles with various base monthly rental amounts. These leases expire at various times from 2009 through 2010. Lease expense under all operating leases totaled \$93,398 for 2008 and \$324,910 for 2007.

Minimum lease payments on operating leases by year, and in aggregate at December 31, 2008, are as follows:

2009	\$ 78,626
2010	<u>24,053</u>
	<u>\$ 102,679</u>

BANDERA ELECTRIC COOPERATIVE, INC.

NOTES TO FINANCIAL STATEMENTS

13. Deferred Credits

Deferred credits include the following:

	<u>December 31,</u>	
	<u>2008</u>	<u>2007</u>
Refundable Aid to Construction	\$ 5,662,497	\$ 6,249,183
Undeliverable Checks Returned	96,382	93,305
Scholarship Fund	59,341	64,490
Unamortized Gain on Reacquired Debt	2,445,307	2,696,562
LCRA Power Bill Credits	188,000	386,676
Other	<u>876,318</u>	<u>695,573</u>
 Total	 <u>\$ 9,327,845</u>	 <u>\$ 10,185,789</u>

The Cooperative realized a gain in 1987 of \$8,767,919 from the discount realized on the buyout of long-term debt to RUS. This amount is classified as a deferred credit and will be amortized over the remaining life of the prepaid RUS debt. Amortization for 2008 and 2007 was \$251,256 and \$261,641, respectively.

14. Litigation and Commitments

There was no litigation pending against the Cooperative at December 31, 2008, that could have a material effect on the financial statements.

The Cooperative is committed to purchase 76% of its electric power and energy requirements from the Lower Colorado River Authority (LCRA) through June of 2010. This commitment can vary through 2016.

15. Pension Benefits

Substantially all employees of the Cooperative participate in the National Rural Electric Cooperative Association (NRECA) Retirement & Security Program, a defined benefit pension plan qualified under Section 401 and tax-exempt under Section 501(a) of the Internal Revenue Code. The defined benefit plan, a multi-employer plan, is available to all member cooperatives of NRECA, and the accumulated benefits and plan assets are not determined or allocated by individual employer. The plan is tax exempt under the Internal Revenue Code. The Cooperative makes monthly contributions equal to the amounts accrued for pension expense. The defined benefit plan has periodically been under moratorium due to the plan reaching full funding limitation. Total pension cost for the year ended December 31, 2008 and 2007, was \$362,669 and \$351,041, respectively.

BANDERA ELECTRIC COOPERATIVE, INC.

NOTES TO FINANCIAL STATEMENTS

In addition, the Cooperative provides retirement benefits through a 401k plan that is administered by NRECA SelectRe Pension plan. The Cooperative provides matching funds up to three percent of an employee's salary. The cost of this plan for 2008 and 2007 was \$100,255 and \$103,360, respectively.

16. Post-retirement Benefits Other Than Pensions

On September 29, 2006, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 158, *Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans – an amendment of FASB Statement No. 87, 88, 106, and 132(R)*. SFAS No. 158 requires an employer that sponsors a defined benefit postretirement plan to report the current economic status (the overfunded or underfunded status) of the plan in its balance sheet, to measure the plan assets and plan obligations as of the balance sheet date, and to include enhanced disclosures about the plan. The Cooperative adopted the recognition and disclosure provisions of SFAS No. 158 for the fiscal year ending December 31, 2007. The Cooperative adopted the measurement date provision for the fiscal year ending December 31, 2008.

Benefits are paid on behalf of retirees and are a function of medical insurance costs and number of retirees. Benefits paid for the years ended December 31, 2008 and 2007, were \$198,434 and \$194,629, respectively.

The measurement date used for the current valuation is January 1, 2005.

Amounts recognized in the Cooperative's financial statements and funded status of the plan are as follows:

BANDERA ELECTRIC COOPERATIVE, INC.

NOTES TO FINANCIAL STATEMENTS

	December 31,	
	2008	2007
Accumulated Post-retirement Benefit Obligation (APBO)		
Balance at Beginning of Year	\$ 5,109,330	\$ 4,762,499
Service Cost	302,360	302,360
Interest Cost	239,100	239,100
Less Premiums Paid	<u>(198,434)</u>	<u>(194,629)</u>
Net Post-retirement Benefit Obligation at Year End	<u>\$ 5,452,356</u>	<u>\$ 5,109,330</u>
Net Periodic Post-retirement Benefit Cost Includes:		
Service Cost	\$ 302,360	\$ 302,360
Interest Cost	239,100	239,100
Amortization of Gain or Loss	13,448	13,448
Amortization of Transition Obligation	<u>62,600</u>	<u>62,600</u>
Total	<u>\$ 617,508</u>	<u>\$ 617,508</u>
Accumulated Other Comprehensive Loss		
Actuarial Loss - Beginning of Year	\$ (776,989)	\$ (853,037)
Transition Obligation	62,600	62,600
Net Loss	<u>13,448</u>	<u>13,448</u>
Other Comprehensive Loss	<u>\$ (700,941)</u>	<u>\$ (776,989)</u>

A 7% annual increase for medical and a five percent annual increase for dental benefits in per capita costs was assumed for 2008, gradually decreasing to 5% by the year 2010. Increasing the assumed healthcare cost trend rates by one percentage point in each year would have resulted in an increase in the APBO of \$525,249 and an increase in the net periodic post-retirement benefit cost of \$80,333. A weighted average discount rate of six percent was used to determine the APBO.

The Cooperative has not funded any plan assets as of December 31, 2008 or 2007.

Estimated future benefit payments for the next five years cannot be reasonably estimated as of December 31, 2008.

17. Disclosures About Fair Value of Financial Instruments

Many of the Cooperative's financial instruments lack an available market with similar terms, conditions, and maturities as those reflected in the carrying amount recorded. Accordingly, significant assumptions, estimations, and present value calculations were used for purposes of this disclosure.

BANDERA ELECTRIC COOPERATIVE, INC.

NOTES TO FINANCIAL STATEMENTS

Estimated Fair Value has been determined by calculating the present value of financial instruments using the best available data available.

Fair Value for some amounts carried on the financial statements has not been calculated for the following reasons:

Patronage Capital from Associated Organizations – The right to receive cash is an inherent component of a financial instrument. The Cooperative holds no right to receive cash since any payments are at the discretion of the governing body for the associated organizations. As such, Patronage Capital from Associated Organizations are not considered financial instruments.

CFC Capital Term Certificates – It is not practicable to estimate fair value for these financial instruments given the lack of a market and their long holding period. Relevant information with respect to these are as follows:

<u>AMOUNT</u>	<u>INTEREST RATE</u>	<u>MATURITY</u>
\$ 86,668	3.00%	2025 -2030
603,511	5.00%	2075-2090
808,599	0.00%	2018-2037
80,000	0.00%	No Expiration

The estimated fair value of the Cooperative's financial instruments is as follows:

CFC Long-Term Debt – The fair value of the Cooperative's CFC long-term fixed rate debt is calculated by computing the present value of the individual notes to maturity. The discount rate used is the currently available CFC fixed interest rate available for long-term debt maturing at the same time as the CFC debt.

	<u>CARRYING VALUE</u>	<u>FAIR VALUE</u>
As of December 31, 2008	\$ <u>55,784,329</u>	\$ <u>49,154,342</u>

ACCOMPANYING INFORMATION

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CERTIFIED PUBLIC ACCOUNTANT

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**INDEPENDENT AUDITORS' REPORT ON
ACCOMPANYING INFORMATION**

Our audits of the basic financial statements presented in the preceding section of this report were made for the purpose of forming an opinion on such financial statements taken as a whole. The accompanying information shown on pages 16 through 21 is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audits of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

Bolinger, Segars, Gilbert & Moss LLP

Certified Public Accountants

March 11, 2009

BANDERA ELECTRIC COOPERATIVE, INC.

Schedule 1

**ELECTRIC PLANT
FOR THE YEAR ENDED DECEMBER 31, 2008**

	Balance 1/1/2008	Additions	Retirements	Balance 12/31/2008
CLASSIFIED ELECTRIC PLANT IN SERVICE				
Transmission Plant				
Land and Land Rights	\$ 50,324	\$	\$	\$ 50,324
Structures and Improvements	172,820	132,703		305,523
Station Equipment	4,326,207			4,326,207
Poles, Towers, and Fixtures	3,396,288			3,396,288
Overhead Conductors and Devices	3,740,329			3,740,329
Total	<u>\$ 11,685,968</u>	<u>\$ 132,703</u>	<u>\$ 0</u>	<u>\$ 11,818,671</u>
Distribution Plant				
Land and Land Rights	\$ 121,244	\$ 2,165	\$	\$ 123,409
Structures and Improvements	916,416			916,416
Station Equipment	11,459,352	261,118		11,720,470
Poles, Towers, and Fixtures	38,136,132	2,307,822	373,693	40,070,261
Overhead Conductors and Devices	32,453,664	3,186,330	341,901	35,298,093
Underground Conductors and Devices	4,175,220	610,467	13,201	4,772,486
Line Transformers	20,787,069	2,132,576	331,217	22,588,428
Services	1,525,354	47,835	6,742	1,566,447
Meters	3,772,572	206,954	152,983	3,826,543
Installations on Consumer Premises	1,568,695	141,253	38,800	1,671,148
Street Lighting	11,585			11,585
Total	<u>\$ 114,927,303</u>	<u>\$ 8,896,520</u>	<u>\$ 1,258,537</u>	<u>\$ 122,565,286</u>
General Plant				
Land and Land Rights	\$ 109,297	\$	\$	\$ 109,297
Structures and Improvements	6,004,708	22,500	20,875	6,006,333
Office Furniture and Equipment	3,049,965	320,211	279,818	3,090,358
Transportation Equipment	742,416	235,616		978,032
Store Equipment	2,537			2,537
Tools, Shop, and Garage Equipment	151,335	19,845	309	170,871
Laboratory Equipment	179,476	26,877		206,353
Power Operated Equipment	1,036,740	461,120	153,461	1,344,399
Communications Equipment	120,685	3,820	1,209	123,296
Miscellaneous Equipment	75,268	9,662		84,930
Total	<u>\$ 11,472,427</u>	<u>\$ 1,099,651</u>	<u>\$ 455,672</u>	<u>\$ 12,116,406</u>
Total Classified Electric Plant in Service	\$ 138,085,698	\$ 10,128,874	\$ 1,714,209	\$ 146,500,363
Construction Work in Progress	<u>6,176,602</u>	<u>1,157,422</u>		<u>7,334,024</u>
Total Utility Plant	<u><u>\$ 144,262,300</u></u>	<u><u>\$ 11,286,296</u></u>	<u><u>\$ 1,714,209</u></u>	<u><u>\$ 153,834,387</u></u>

BANDERA ELECTRIC COOPERATIVE, INC.

Schedule 2

**SCHEDULE OF ACCUMULATED PROVISION FOR DEPRECIATION
FOR THE YEAR ENDED DECEMBER 31, 2008**

	Balance 1/1/2008	Accruals	Retirements	Balance 12/31/2008
Transmission Plant	\$ 2,941,966	\$ 320,682	\$	\$ 3,262,648
Distribution Plant	\$ 21,587,148	\$ 3,250,346	\$ 1,643,110	\$ 23,194,384
General Plant				
Structures and Improvements	\$ 700,111	\$ 138,306	\$ 20,875	\$ 817,542
Office Furniture and Fixtures	1,759,848	405,884	279,818	1,885,914
Transportation Equipment	300,463	203,407		503,870
Store Equipment	899	333		1,232
Tools, Shop, and Garage Equipment	95,095	12,792	309	107,578
Laboratory Equipment	92,051	14,064		106,115
Power Operated Equipment	707,371	71,955	141,011	638,315
Communication Equipment	73,262	7,236	1,209	79,289
Miscellaneous Equipment	36,963	16,378		53,341
Outage Management Equipment	32,203	21,741		53,944
Total General Plant	\$ 3,798,266	\$ 892,096	\$ 443,222	\$ 4,247,140
Total Classified Electric Plant in Service	\$ 28,327,380	\$ 4,463,124	\$ 2,086,332	\$ 30,704,172
Retirement Work in Progress	(216,346)		(113,978)	(102,368)
Total	\$ 28,111,034	\$ 4,463,124	\$ 1,972,354	\$ 30,601,804

(1)

(2)

(1)	Depreciation		
	Charged to Expense	\$ 4,204,686	
	Charged to Clearing	258,438	
		<u>\$ 4,463,124</u>	

(2)	Net Loss on Retirement		
	Original Cost		\$ 1,714,209
	Cost of Removal		290,307
	Less: Salvage and Other Credits		<u>32,162</u>
			<u>\$ 1,972,354</u>

BANDERA ELECTRIC COOPERATIVE, INC.

Schedule 3

**OTHER PROPERTY AND INVESTMENTS
FOR THE YEARS ENDED DECEMBER 31, 2008 AND 2007**

	<u>December 31,</u>	
	<u>2008</u>	<u>2007</u>
INVESTMENTS IN ASSOCIATED ORGANIZATIONS		
Memberships		
Associated Organizations	\$ 2,760	\$ 2,760
Patronage Capital		
NRUCFC	787,466	711,146
NRTC	16,476	15,923
Texas Electric Cooperatives, Inc.	821,169	698,708
Guadalupe Valley	1,327	1,327
Hill Country Telephone	69,122	66,231
Capital Term Certificates		
CFC	1,578,778	1,558,187
UTI - 10 Shares		50,000
Total	<u>\$ 3,277,098</u>	<u>\$ 3,104,282</u>

BANDERA ELECTRIC COOPERATIVE, INC.

Schedule 4

**PATRONAGE CAPITAL
FOR THE YEAR ENDED DECEMBER 31, 2008**

<u>Calendar Year</u>	<u>Assignable</u>	<u>Assigned</u>	<u>Balance</u>
1982	\$	\$ 196,248	\$ 196,248
1983		931,222	931,222
1984		1,043,172	1,043,172
1985		1,374,653	1,374,653
1986		1,259,421	1,259,421
1987		1,315,261	1,315,261
1988		1,179,816	1,179,816
1989		1,147,653	1,147,653
1990		958,733	958,733
1991		1,326,784	1,326,784
1992		1,542,041	1,542,041
1993		1,969,069	1,969,069
1994		1,444,465	1,444,465
1995		1,627,986	1,627,986
1996		1,615,237	1,615,237
1997		1,480,062	1,480,062
1998		1,359,206	1,359,206
1999		1,093,191	1,093,191
2000		839,338	839,338
2001		4,152,280	4,152,280
2002		3,098,698	3,098,698
2003		2,953,494	2,953,494
2004		4,141,946	4,141,946
2005		2,199,336	2,199,336
2006		2,124,478	2,124,478
2007		2,177,774	2,177,774
2008	<u>1,884,996</u>		<u>1,884,996</u>
	<u>\$ 1,884,996</u>	<u>\$ 44,551,564</u>	<u>\$ 46,436,560</u>

BANDERA ELECTRIC COOPERATIVE, INC.

Schedule 5

**CFC MORTGAGE NOTES
DECEMBER 31, 2008**

<u>Note Number</u>	<u>Maturity Date</u>	<u>Interest Rate</u>	<u>Principal Amount</u>	<u>Amount Unadvanced</u>	<u>Principal Repayments</u>	<u>Net Obligation</u>
9003001	3/1/2015	6.04%	\$ 675,000	\$	\$ 426,454	\$ 248,546
9006001	6/1/2017	6.09%	1,011,000		516,854	494,146
9007001	12/1/2018	6.19%	1,010,000		503,317	506,683
9008001	9/1/2021	6.28%	3,290,323		1,242,437	2,047,886
9013001	11/30/2018	6.19%	213,340		79,905	133,435
9013002	11/30/2018	6.19%	1,786,660		668,518	1,118,142
9014001	2/29/2028	7.19%	3,000,000		936,263	2,063,737
9015001	11/30/2018	4.55%	3,000,000		1,142,218	1,857,782
9016001	11/30/2019	4.85%	3,000,000		1,021,742	1,978,258
9017001	2/28/2030	7.19%	3,000,000		673,436	2,326,564
9018001	2/28/2030	7.19%	3,000,000		673,436	2,326,564
9019001	8/31/2021	4.55%	3,000,000		778,958	2,221,042
9020001	11/30/2022	4.85%	3,000,000		677,726	2,322,274
9021001	11/30/2022	4.85%	3,000,000		677,726	2,322,274
9022001	11/30/2023	5.20%	3,000,000		548,166	2,451,834
9023001	11/30/2023	5.20%	1,986,530		351,974	1,634,556
9023002	5/31/2024	5.25%	1,013,470		174,887	838,583
9024001	5/31/2024	5.25%	1,756,545		246,095	1,510,450
9024002	5/31/2030	6.30%	1,243,455		117,677	1,125,778
9025001	8/31/2024	5.15%	1,939,410		277,728	1,661,682
9025002	5/31/2030	6.30%	1,060,590		88,157	972,433
9026001	2/28/2034	5.65%	1,171,600		313,559	858,041
9026002	2/28/2034	6.25%	1,285,330		218,719	1,066,611
9026003	5/31/2030	6.30%	543,070		73,529	469,541
9027001	2/28/2034	6.65%	1,240,510		106,004	1,134,506
9027002	11/30/2024	5.40%	1,249,690		158,292	1,091,398
9027003	5/31/2030	6.30%	509,800		40,259	469,541
9028001	5/31/2030	6.30%	1,106,870		67,472	1,039,398
9028002	5/31/2030	6.20%	1,893,130		116,852	1,776,278
9029001	8/31/2035	6.20%	2,165,000		155,035	2,009,965
9029002	11/30/2036	6.90%	835,000		15,959	819,041
9032001	11/30/2036	6.90%	915,000		17,488	897,512
9032002	11/30/2036	6.95%	1,750,000		33,141	1,716,859
9032003	11/30/2036	7.00%	1,750,000		32,837	1,717,163
9032004	11/30/2036	7.00%	1,750,000		32,837	1,717,163
9032005	11/30/2037	6.20%	2,000,000		18,038	1,981,962
9032006	11/30/2037	6.40%	3,000,000		26,071	2,973,929
9032007	11/30/2037	6.45%	3,000,000		25,829	2,974,171
9032008	11/30/2043	5.40%	2,338,318			2,338,318
9032009	11/30/2043	5.40%	2,283,448			2,283,448
9032010	11/30/2043	5.40%	1,212,234			1,213,234
9033001	11/30/2043	5.40%	528,448			528,448
9033002	11/30/2043	5.40%	136,552			136,552
Unadvanced			<u>30,335,000</u>	<u>30,335,000</u>		
Total CFC			<u>\$ 106,985,323</u>	<u>\$ 30,335,000</u>	<u>\$ 13,275,595</u>	<u>\$ 63,375,728</u>

BANDERA ELECTRIC COOPERATIVE, INC.

Schedule 6

**ADMINISTRATIVE AND GENERAL EXPENSES
FOR THE YEARS ENDED DECEMBER 31, 2008 AND 2007**

	December 31,	
	<u>2008</u>	<u>2007</u>
Administrative and General Salaries	\$ 1,195,525	\$ 1,037,524
Office Supplies and Expenses	427,835	412,549
Outside Services Employed	295,858	154,379
Workmen's Compensation, General Liability, and Other Insurance	137,225	173,609
Employee Benefits	1,062,533	1,035,228
Directors' Fees and Expenses	231,672	221,885
Institutional and Goodwill Advertising	23,193	22,449
Dues to Associated Organizations	75,508	75,825
Annual Meeting Expense	47,227	42,803
Miscellaneous General Expenses	324,879	218,837
Regulatory Commission Expense	100,649	79,779
Maintenance of General Plant	<u>192,201</u>	<u>143,960</u>
Total	<u>\$ 4,114,305</u>	<u>\$ 3,618,827</u>

COMPLIANCE SECTION

BOLINGER, SEGARS, GILBERT & MOSS, L.L.P.

CERTIFIED PUBLIC ACCOUNTANTS

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8215 NASHVILLE AVENUE

LUBBOCK, TEXAS 79423-1954

**LETTER TO BOARD OF DIRECTORS REGARDING POLICIES
CONCERNING AUDITS OF CFC BORROWERS**

Board of Directors
Bandera Electric Cooperative, Inc.
Bandera, Texas

We have audited, in accordance with auditing standards generally accepted in the United States of America, the balance sheet of Bandera Electric Cooperative, Inc. as of December 31, 2008, and the related statements of income and patronage capital and cash flows for the year then ended, and have issued our report thereon dated March 11, 2009.

In connection with our audit, nothing came to our attention that caused us to believe that the Cooperative failed to comply with the terms of Article V of the National Rural Utilities Cooperative Finance Corporation Loan Agreement insofar as they relate to accounting matters. However, our audits were not directed primarily toward obtaining knowledge of such noncompliance.

This report is intended solely for the information and use of the Boards of Directors and management of Bandera Electric Cooperative, Inc. and the National Rural Utilities Cooperative Finance Corporation and is not intended to be and should not be used by anyone other than these specified parties.

Bolinger, Segars, Gilbert & Moss L.L.P.

Certified Public Accountants

March 11, 2009