

FINANCIAL STATEMENTS WITH
REPORT OF INDEPENDENT AUDITORS

TEX-LA ELECTRIC COOPERATIVE
OF TEXAS, INC.

December 31, 2010 and 2009

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REPORT OF INDEPENDENT AUDITORS

The Board of Directors
Tex-La Electric Cooperative
of Texas, Inc.
Nacogdoches, Texas

We have audited the accompanying balance sheets of Tex-La Electric Cooperative of Texas, Inc. (the "Cooperative") as of December 31, 2010 and 2009 and the related statements of revenue and expenses, 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 audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards for financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States. These 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 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 Tex-La Electric Cooperative of Texas, Inc. as of December 31, 2010 and 2009 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.

In accordance with *Government Auditing Standards*, we have also issued our report dated April 15, 2011, on our consideration of the Cooperative's internal control over financial reporting and our tests of its compliance with certain laws, regulations, contracts and grants. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

Lufkin, Texas
April 15, 2011


CERTIFIED PUBLIC ACCOUNTANTS

TEX-LA ELECTRIC COOPERATIVE OF TEXAS, INC.
BALANCE SHEETS
December 31, 2010 and 2009

	2010	2009
ASSETS		
Utility plant, net	\$ 11 782 482	\$ 12 517 311
Investments and Other Assets:		
Investments in associated organizations	18 938 650	14 907 110
Other investments - RUS Cushion of Credit	3 372 463	3 208 981
Assumed long-term indebtedness - TXU Corp. less current portion	82 794 021	91 815 499
	105 105 134	109 931 590
Current Assets:		
Cash and cash equivalents	9 820 239	15 987 952
Accounts receivable from member cooperatives	15 371 828	8 573 818
Accounts receivable - Other	97 380	519 347
Accrued interest receivable	1 296 302	356 477
Prepaid expenses	42 094	42 084
Assumed long-term indebtedness - TXU Corp.	9 934 994	8 210 700
	36 562 837	33 690 378
Deferred debits	17 404	1 209 872
	\$ 153 467 857	\$ 157 349 151
EQUITIES AND LIABILITIES		
Equity and Margin:		
Memberships	\$ 700	\$ 700
Patronage capital	36 966 833	31 141 677
Other equities	400 000	400 000
	37 367 533	31 542 377
Long-term debt	94 538 182	104 987 564
Current Liabilities:		
Accounts payable - Purchased power	8 333 902	10 497 587
Accounts payable - Other	241 336	216 292
Accrued expenses	1 441 683	450 197
Derivative instruments	-	146 666
Current maturities of long-term debt	11 472 206	9 508 468
	21 489 127	20 819 210
Deferred credits	73 015	-
	\$ 153 467 857	\$ 157 349 151

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

TEX-LA ELECTRIC COOPERATIVE OF TEXAS, INC.
STATEMENTS OF REVENUE AND EXPENSES
For the Years Ended December 31, 2010 and 2009

	2010	2009
Operating Revenues:		
Power sales	\$ 103 529 365	\$ 86 437 545
Operating Expenses:		
Purchased power	98 883 168	81 912 663
Transmission - Operations	492 039	290 223
Transmission - Maintenance	559 249	268 342
Administrative and general	1 584 380	2 005 481
Depreciation	734 829	734 828
	102 253 665	85 211 537
OPERATING MARGINS BEFORE INTEREST EXPENSE	1 275 700	1 226 008
Interest expense	176 434	148 515
OPERATING MARGINS	1 099 266	1 077 493
Nonoperating Margins:		
Interest income	268 460	244 849
Generation and transmission capital credits	3 802 470	1 980 567
Capital credits - Associated organizations	654 960	702 066
NET MARGINS	\$ 5 825 156	\$ 4 004 975

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

TEX-LA ELECTRIC COOPERATIVE OF TEXAS, INC.
 STATEMENTS OF PATRONAGE CAPITAL
 For the Years Ended December 31, 2010 and 2009

	<u>MEMBERSHIPS</u>	<u>PATRONAGE CAPITAL</u>	<u>OTHER EQUITIES</u>	<u>TOTAL</u>
Balance, December 31, 2008	\$ 700	\$ 27 136 702	\$ 400 000	\$ 27 537 402
Net margin	-	4 004 975	-	4 004 975
Balance, December 31, 2009	700	31 141 677	400 000	31 542 377
Net margin	-	5 825 156	-	5 825 156
Balance, December 31, 2010	<u>\$ 700</u>	<u>\$ 36 966 833</u>	<u>\$ 400 000</u>	<u>\$ 37 367 533</u>

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

TEX-LA ELECTRIC COOPERATIVE OF TEXAS, INC.
STATEMENTS OF CASH FLOWS
For the Years Ended December 31, 2010 and 2009

	2010	2009
Operating Activities:		
Net margin	\$ 5 825 156	\$ 4 004 975
Adjustments to Reconcile Net Income to Net Cash Provided by Operating Activities:		
Depreciation	734 829	734 828
Patronage capital credits - Non-cash	(4 032 012)	(2 226 229)
Cash Provided by (Used for) the Change in:		
Accounts receivable - Members	(6 798 010)	1 175 021
Accounts receivable - Other	421 967	(21 953)
Accrued interest receivable	(939 825)	31 442
Prepaid expense	(10)	(2 693)
Deferred debits	1 045 802	(289 998)
Accounts payable - Purchased power	(2 163 685)	2 849 105
Accounts payable - Other	25 044	(131 713)
Accrued expenses	991 486	58 604
Deferred credits	73 015	-
NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES	(4 816 243)	6 181 389
Investing Activities:		
CFC Member capital securities	-	(1 000 000)
Other investments	(163 010)	(155 523)
NET CASH USED BY INVESTING ACTIVITIES	(163 010)	(1 155 523)
Financing Activities:		
Principal payments on long-term debt	(1 188 460)	(1 180 499)
NET CASH USED BY FINANCING ACTIVITIES	(1 188 460)	(1 180 499)
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(6 167 713)	3 845 367
Cash and cash equivalents - Beginning of year	15 987 952	12 142 585
CASH AND CASH EQUIVALENTS - END OF YEAR	\$ 9 820 239	\$ 15 987 952
Supplemental Disclosures of Cash Flow Information:		
Cash Paid During the Year For:		
Interest	\$ 25 305	\$ 147 504

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

TEX-LA ELECTRIC COOPERATIVE OF TEXAS, INC.
NOTES TO FINANCIAL STATEMENTS

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Nature of Operations:

Tex-La Electric Cooperative of Texas, Inc. (the "Cooperative") is an electric generating and transmission cooperative formed and operating pursuant to the Texas Electric Cooperative Corporation Act. The Cooperative provides wholesale electric service to its member distribution cooperatives, Cherokee County Electric Cooperative Association, Deep East Texas Electric Cooperative, Inc., Houston County Electric Cooperative, Inc., Jasper-Newton Electric Cooperative, Inc., Rusk County Electric Cooperative, Inc., Sam Houston Electric Cooperative, Inc. and Wood County Electric Cooperative, Inc. ("Members").

The Cooperative was formed principally to provide dependable power to its Members at the lowest cost possible. In doing so, the Cooperative works closely with its Members in determining their power requirements.

Use of Estimates:

The preparation of the financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses and disclosure of contingent assets and liabilities. The estimates and assumptions used in the accompanying financial statements are based upon management's evaluation of the relevant facts and circumstances as of the date of the financial statements. Actual results may differ from the estimates and assumptions used in preparing the accompanying financial statements.

System of Accounts:

The Cooperative maintains its accounting records in accordance with the Federal Energy Regulatory Commission's Uniform System of Accounts as adopted by the USDA Rural Development's Rural Utilities Service ("RUS"), which conforms with U.S. generally accepted accounting principles in all material respects. The more significant accounting policies are described below.

Revenue Recognition:

Revenues from the sale of electricity are recorded based on billings to Members.

Cash Flow Statement:

Cash and cash equivalents, for purposes of the cash flow statement, consist of all cash and temporary investments with original maturities of three months or less.

Accounts Receivable:

The Cooperative considers accounts receivable to be fully collectible; accordingly, no allowance for doubtful accounts has been established. If accounts become uncollectible, they will be charged to operations when that determination is made.

Utility Plant:

The utility plant is stated at original cost. The cost of additions to the electric plant includes contracted work, direct labor, materials, allocable overhead and interest on debt used for construction. The cost of maintenance and repairs, including renewals of minor items of property, is charged to operating expense. The cost of units replaced or retired, including cost of removal, net of any salvage value, is charged to accumulated depreciation.

TEX-LA ELECTRIC COOPERATIVE OF TEXAS, INC.
NOTES TO FINANCIAL STATEMENTS - CONTINUED

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

Depreciation of the utility plant is provided on the composite straight-line method over the estimated useful lives of the depreciable assets. The method and rates are prescribed by RUS or as approved for rate-making purposes. The annual depreciation rates are:

Transmission	2.75%
Office building	2.00%
Distribution	3.00%
Telemetry	6.67%

Long-lived assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. If the sum of the expected future undiscounted cash flows is less than the carrying amount of the asset, a loss is recognized for the difference between the fair value and carrying value of the asset. At December 31, 2010 the Cooperative had not recognized any losses resulting from the impairment of long-lived assets.

Investments in Associated Organizations:

Investments in patronage capital credits of associated organizations are accounted for under the equity method. Patronage capital is recorded at the stated amount of the certificate when allocated by the associated organization.

Income Taxes:

The Cooperative is exempt from Federal income taxes under the provisions of Section 501(c)(12) of the Internal Revenue Code of 1986.

Comprehensive Income:

Professional standards have been established for the reporting and display of comprehensive income and its components in the financial statements. There were no items of other comprehensive income in 2010 and 2009, and thus, net income is equal to comprehensive income for each of those years.

Deferred Debits/Credits:

In accordance with Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") 980: *Regulated Operations* (formerly FASB Statement No. 71, *Accounting for the Effects of Certain Types of Regulation*), certain costs have been capitalized as deferred assets that would otherwise be charged to expense. Such deferred assets are 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.

Derivative Instruments:

The accounting standards for derivative instruments and hedging activities require that all derivatives be recognized at fair value on the balance sheet, either as assets or liabilities, unless they meet the normal purchase, normal sales criteria. The changes in the fair value of recognized derivatives are recorded each period in current margins or other comprehensive income, depending on whether a derivative is designated as part of a hedge transaction and the type of hedge transaction.

TEX-LA ELECTRIC COOPERATIVE OF TEXAS, INC.
NOTES TO FINANCIAL STATEMENTS - CONTINUED

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

The Cooperative makes limited use of derivative instruments for the purpose of managing commodity price risk related to forecasted purchases of natural gas. The Cooperative's objective in using derivative instruments is to reduce the variability of the cash flows of the forecasted purchases of natural gas. At December 31, 2009, the Cooperative held over-the-counter natural gas swaps that expired monthly through May 2010 and financially settled against NYMEX futures. The Cooperative believes it is not practical to designate these contracts as cash flow hedges, as defined under ASC 815: *Derivatives and Hedging* (formerly FASB Statement No. 133, *Accounting for Derivative Instruments and Hedging Activities*). Therefore, in accordance with ASC 815, the Cooperative adjusts the contracts to the current market value through the statement of revenue and expense. Unrealized gains and losses on derivative instruments outstanding as of December 31, 2009 are deferred on a net basis as a regulatory asset or liability in accordance with ASC 980: *Regulated Operations*. These amounts are subsequently reclassified as purchased power in the Statement of Revenue and Expense as the power is delivered and the contract settles. A current liability of \$146,666 was recognized on the Cooperative's Balance Sheet at December 31, 2009 for the mark-to-market adjustment and a corresponding regulatory asset was recognized. During the year ended December 31, 2010 and December 31, 2009, losses in the amounts of approximately \$538,000 and \$726,000, respectively were recognized in purchased power cost for derivative instruments. At December 31, 2010, the Cooperative did not hold any derivative instruments.

Derivative instruments are reported on the Balance Sheet at fair value. The measurement of fair value is based on actively quoted market prices and is considered a Level 1 fair value measurement.

Subsequent Events:

Management has evaluated subsequent events through April 15, 2011, the date the financial statements were available to be issued.

NOTE 2 - UTILITY PLANT

The following summarizes utility plant at December 31, 2010 and 2009:

	2010	2009
Utility Plant, at Cost:		
Transmission	\$ 23 088 076	\$ 23 088 076
Office building	208 818	208 818
Distribution and telemetering	480 565	480 565
	23 777 459	23 777 459
Less accumulated depreciation	(11 994 977)	(11 260 148)
	\$ 11 782 482	\$ 12 517 311

NOTE 3 - INVESTMENTS

Investments in associated organizations at December 31, 2010 and 2009 consisted of the following:

	2010	2009
Patronage capital - National Rural Utilities Cooperative Finance Corporation ("CFC")	\$ 25 315	\$ 25 315
CFC Member Capital Securities	1 000 000	1 000 000
Memberships	6 000	6 000
Patronage capital - National Bank for Cooperatives ("CoBank")	5 046 584	4 817 513
Patronage capital - East Texas Electric Cooperative, Inc. ("ETEC")	12 860 751	9 058 282
	\$ 18 938 650	\$ 14 907 110

TEX-LA ELECTRIC COOPERATIVE OF TEXAS, INC.
NOTES TO FINANCIAL STATEMENTS - CONTINUED

NOTE 3 - INVESTMENTS - CONTINUED

Capital credit and patronage capital allocations reported in the Statements of Revenue and Expenses in the amount of \$4,457,430 and \$2,682,633 for the fiscal years ended December 31, 2010 and 2009, respectively, represent Patronage Capital allocations from CFC, CoBank and capital credits from a wholesale power supplier of the Cooperative, East Texas Electric Cooperative, Inc.

NOTE 4 - OTHER INVESTMENTS - RUS CUSHION OF CREDIT

The Cooperative maintains a Cushion of Credit Account with RUS. The account represents voluntary payments to RUS in excess of amounts due and is intended to enable the Cooperative to have funds available to make scheduled payments on RUS debt. By law, the account earns five percent interest annually and can only be used to make installments on RUS mortgage notes.

NOTE 5 - DEFERRED DEBITS/CREDITS

The following is a summary of the amounts recorded as deferred debits/credits as of December 31, 2010 and 2009:

	2010	2009
DEFERRED DEBITS		
Unamortized refinancing expenses	\$ 17 404	\$ 46 093
Unrealized loss on derivative instruments	-	146 666
Due from Members - Levelized billing	-	1 017 113
	\$ 17 404	\$ 1 209 872
DEFERRED CREDITS		
Due from Members - Levelized billing	\$ 73 015	\$ -
	\$ 73 015	\$ -

Unrealized gains and losses on derivative instruments are deferred in accordance with ASC 980: *Regulated Operations*. The unrealized gains and losses are subsequently reclassified and recorded as purchased power costs when the instruments settle.

The Cooperative's tariff includes a levelized billing rate plan. Under the levelized billing rate plan, each of the Cooperative's Members has the option to pay a monthly levelized bill computed using the actual kilowatt-hours and a levelized billing rate. The difference between the actual monthly power cost computed under the Cooperative's Board approved wholesale rate and the amount paid to the Cooperative under the levelized billing rate plan is recorded on monthly billing statements to the Members and accumulated by the Cooperative in a designated deferred account.

Under the levelized billing plan, a Member's levelized billing factor is recalculated each month. The new levelized billing rate is calculated using actual data for the year to date and projected figures for the remainder of the year. At the end of each twelve-month period, the Cooperative computes a new projected cost of power. The new projected cost of power and the accumulated deferred billing for the previous twelve-month period are combined to determine the levelized billing rate for the next twelve-month period. The Board of Directors of the Cooperative may revise the levelized billing rate due to unforeseen fluctuations in the cost of purchased power.

TEX-LA ELECTRIC COOPERATIVE OF TEXAS, INC.
NOTES TO FINANCIAL STATEMENTS - CONTINUED

NOTE 6 - PATRONAGE CAPITAL

The details of patronage capital at December 31, 2010 and 2009 are as follows:

	<u>2010</u>	<u>2009</u>
Patronage Capital:		
Assignable	\$ 5 825 156	\$ 4 004 975
Assigned	33 641 677	29 636 702
	<u>39 466 833</u>	<u>33 641 677</u>
Less: Retired	2 500 000	2 500 000
	<u>\$ 36 966 833</u>	<u>\$ 31 141 677</u>

The bylaws of the Cooperative provide that all amounts received and receivable from the furnishing of electric energy in excess of the sum of operating costs and expenses are to be assigned to Members' patronage capital credit accounts on a patronage basis. The bylaws permit the offsetting of current year operating margins against operating deficits of prior years.

The details of other equities at December 31, 2010 and 2009 are as follows:

	<u>2010</u>	<u>2009</u>
Appropriated margins	\$ <u>400 000</u>	\$ <u>400 000</u>

The bylaws also provide that nonoperating margins be used initially to offset any losses incurred during the current or any prior fiscal year. Upon recovery of any losses, a fund in the amount of \$400,000 shall be accumulated from these remaining nonoperating margins and funded each year, if necessary, to maintain the \$400,000 balance and to the extent not needed for that purpose allocated to the Members' patronage capital credit accounts on a patronage basis. Subsequent to the year ended December 31, 2010, the Cooperative amended its bylaw concerning patronage capital to eliminate the requirement that a \$400,000 fund be maintained out of nonoperating margins and to clarify how the Board may deal with losses. The amended bylaw provides the Board the ability to allocate losses to Members, offset losses with margins from future years, or offset losses with certain nonoperating margins from current or future years.

Under provision of the agreements relating to the RUS mortgage notes, until the total of equities and margins equal or exceed 40% of total assets, the distribution of capital contributed by members in each year is limited generally to 25% of patronage capital and margins of the preceding year provided that, after giving effect to such distribution, the total equity will equal or exceed 20% of total assets. The Cooperative did not retire any patronage capital during 2010 or 2009.

NOTE 7 - LONG-TERM DEBT

Long-term debt at December 31, 2010 and 2009 consisted of the following:

	<u>2010</u>	<u>2009</u>
Mortgage notes payable to FFB, interest at 7.294% to 9.392% due in quarterly installments through December 2021	\$ 52 285 388	\$ 55 271 032
Note payable to RUS Grantor Trust, interest at 6.806%, due December 2019	53 725 000	59 225 000
	<u>106 010 388</u>	<u>114 496 032</u>
Less current maturities	11 472 206	9 508 468
	<u>\$ 94 538 182</u>	<u>\$ 104 987 564</u>

TEX-LA ELECTRIC COOPERATIVE OF TEXAS, INC.
NOTES TO FINANCIAL STATEMENTS - CONTINUED

NOTE 7 - LONG-TERM DEBT - CONTINUED

In 1981, the Cooperative entered into a loan agreement (guaranteed by RUS) payable to the Federal Financing Bank ("FFB") to finance its ownership in the Comanche Peak Steam Electric Station ("Comanche Peak"). In 1988, pursuant to a loan agreement with CFC, the Cooperative refinanced \$102,203,000 of long-term debt. The terms of the agreement provided for the formation of grantor trusts with each being formed under a separate trust agreement among CFC, RUS, the Cooperative, and the Bank of New York ("Trustee"). The Cooperative issued notes in an aggregate amount of \$102,203,000, each guaranteed by RUS, to the separate trusts.

In 1997, the Cooperative refinanced the balance of the grantor trusts owed, \$94,750,000, pursuant to a loan agreement with CoBank. The prepayment costs associated with the refinancing amounted to \$4,445,555, which resulted in an effective rate of 7.467% charged by CoBank. Interest is payable to the Trustee semiannually on June 4th and December 4th; principal payments are due December 4th of each year. As a result of the refinancing, related costs were also incurred. The net deferred costs related to the refinancing amounted to \$390,839, and are being systematically amortized to expense over the life of the related long-term debt (Note 5).

The Cooperative had a 2.17% undivided ownership interest in Comanche Peak pursuant to a joint ownership agreement with TXU Corp. (now Energy Future Holdings) dated December 9, 1980. Delays in construction and project cost overruns resulted in litigation between TXU Corp., the Cooperative and other minority owners. In 1990, the Cooperative signed agreements that, among other matters, settled the litigation. Pursuant to the agreement, TXU Corp. purchased all of the Cooperative's interest in Comanche Peak.

In connection with the settlement of the Comanche Peak litigation, TXU Corp. assumed \$174,721,065 of the Cooperative's indebtedness to the Federal Financing Bank and the Rural Electric Cooperative Grantor Trust. The debt assumption by TXU Corp. did not release the Cooperative as a primary obligor in connection with the Comanche Peak indebtedness. As required by generally accepted accounting principles, the assumption of a portion of the Cooperative's Comanche Peak indebtedness by TXU Corp. is not an extinguishment of debt. Under the terms of the agreement, TXU Corp. makes payments directly to the RUS and the Trustee for its portion of the Comanche Peak debt assumed. The remaining balance of the debt assumed by TXU Corp. was \$92,729,015 and \$100,026,199 at December 31, 2010 and 2009, respectively. As a result of this transaction not meeting the requirements for a debt extinguishment, the Cooperative has recorded the gross amount of the indebtedness on their balance sheet and has recorded a note receivable from TXU Corp. for TXU's related portion of the debt. However, to reflect the substance of this transaction, the Cooperative's Statement of Revenues and Expenses reflects interest expense net of any payments made by TXU Corp.

The approximate annual maturities of long-term debt are as follows:

2011	\$	11 472 206
2012		11 456 000
2013		12 617 000
2014		13 902 000
2015		15 274 000

The Cooperative has a \$12,000,000 line of credit with National Rural Utilities Cooperative Finance Corporation that matures in August 2011. At December 31, 2010 and 2009, no funds were advanced or owed under this line of credit.

Substantially all assets are pledged as collateral for the above-mentioned debt to the RUS and FFB.

NOTE 8 - POWER CONTRACTS

The Cooperative has wholesale power contracts with each of its Members which require the Members to buy and receive from the Cooperative all their power requirements at specified delivery points and require the Cooperative to sell and deliver power and energy in satisfaction of such requirements. The contracts extend to December 31, 2044, and thereafter, until terminated by either party giving not less than six months written notice. The power sales by the Cooperative to the Members for the years ended December 31, 2010 and 2009 were \$103,529,365 and \$86,437,545, respectively.

The Cooperative is a party to power supply agreements to acquire power from Southwestern Power Administration ("SWPA"), American Electric Power ("AEP"), and Entergy Texas, Inc. ("ETI"). These power supply agreements terminate at various dates from 2012 to 2018.

The Cooperative is a member of ETEC. ETEC was formed by the Cooperative, Northeast Texas Electric Cooperative, Inc. ("NTEC") and Sam Rayburn G & T Electric Cooperative, Inc. ("SRG&T") for the purpose of developing power supply alternatives and coordinating these alternatives with the power supply requirements of its members. The Cooperative has a wholesale power contract (the "Contract") with ETEC whereby ETEC supplies wholesale power to the Cooperative over and above the power the Cooperative receives from SWPA and AEP. During 2010 and 2009, the Cooperative paid approximately \$66,921,000 and \$48,371,000, respectively, to ETEC for the purchase of wholesale power. At December 31, 2010 and 2009, approximately \$5,299,795 and \$4,825,000, respectively, was due to ETEC for wholesale power purchased.

NOTE 9 - RETIREMENT PLANS

All employees of the Cooperative participate in the National Rural Electric Cooperative Association ("NRECA") Retirement & Security Program ("Program"), a defined benefit pension plan qualified under section 401 and tax-exempt under section 501(a) of the Internal Revenue Code. The Cooperative makes annual contributions to the Program equal to the amounts accrued for pension expense. In this multiemployer plan, which is available to all member cooperatives of NRECA, the actuarial present value of accumulated plan benefits to participants of the plan and the net assets available for those benefits for the Cooperative is not presented. Contributions to the retirement and security program were \$109,880 and \$79,801 in 2010 and 2009, respectively.

The Cooperative participates in a 401(k) plan offered to similar cooperatives by the NRECA. The Cooperative matches certain employee contributions. Such matching contributions amounted to \$12,781 and \$14,990 in 2010 and 2009, respectively.

NOTE 10 - RELATED PARTY TRANSACTIONS

The Cooperative, ETEC and SRG&T share office facilities and personnel. ETEC and SRG&T reimburse the Cooperative for their proportionate share of the related expenses and equipment purchases. ETEC's share of costs for the years ended December 31, 2010 and 2009 was \$515,788 and \$453,516, respectively. SRG&T's share of costs for the years ended December 31, 2010 and 2009 was \$120,268 and \$109,273, respectively. At December 31, 2010 and 2009, \$66,118 and \$56,706, respectively, was due from ETEC and SRG&T for administrative expenses and equipment purchases. Certain members of the Cooperative are also members of SRG&T and NTEC.

The Cooperative pays maintenance expenses associated with certain transmission facilities owned by Deep East Texas Electric Cooperative ("DETEC"), a member cooperative. In 2010 and 2009, \$154,223 and \$129,021, respectively, was paid to DETEC for maintenance of transmission facilities.

NOTE 11 - RATE MATTERS

In 1999, the Texas Legislature approved Senate Bill 7, which provided for the restructuring of the Texas electric industry for the purpose of creating a competitive electric power market. The legislation provided that the pricing and supply of the generation of electricity would be unregulated beginning in January 2002. Under special provisions for cooperatives, the Cooperative's rates for the sale of wholesale power were no longer regulated by the Public Utility Commission of Texas ("PUCT"). Similarly, the rates of the Members for the sale of electricity are no longer regulated by the PUCT. The law permits cooperatives' boards of directors to set rates.

Investor-owned utilities in the Electric Reliability Council of Texas ("ERCOT") were required to allow their retail customers to select generation suppliers of electricity as of January 2002. The law gives cooperatives' boards of directors sole authority to allow, or not allow, generating suppliers to attempt to sell electricity to retail customers of a cooperative. Allowing retail customer choice is called "opting in". Even if a cooperative's board decided to opt in, retail customers will continue to use the transmission and distribution facilities of the Cooperative's Members. The Cooperative will closely monitor whether any of its Members will decide to opt in and thus evaluate the potential effects of a change in generation sales. The law allows the Cooperative to recover stranded costs if it experiences a loss of load which would impair payment of debt service and payment of purchased power fixed charges. As of December 31, 2010, none of the Cooperative's Members have elected to opt in.

NOTE 12 - COMMITMENTS AND CONTINGENCIES

In October of 2007, Kohlberg, Kravis Roberts & Co. ("KKR") and Texas Pacific Group ("TPG"), two of the nation's leading private equity firms, reached a definitive merger agreement with TXU Corp. under which KKR and TPG acquired TXU Corp. A new entity was formed under the name Energy Future Holdings. Since the merger, the financial condition of Energy Future Holdings has deteriorated. Legal counsel has advised the Cooperative that the debt assumed (see Note 7) by TXU Corp. has been assigned to Energy Future Holdings and the Cooperative is a secured creditor.

The electric utility industry is subject to standards and procedures under government laws and regulations related to environmental and other matters. These standards and procedures are subject to change and uncertainties and as a result, outcomes are not predictable with assurance. The Cooperative is unaware of any noncompliance with current governmental laws and regulations related to environmental matters.

In the normal course of business, the Cooperative may be involved in various claims and litigation. In the opinion of management and the Cooperative's legal counsel, there is no material pending or threatened litigation against the Cooperative.

NOTE 13 - CONCENTRATION OF CREDIT RISK

The Cooperative's financial instruments that are exposed to concentrations of credit risk consist primarily of cash equivalents and accounts receivable.

The Cooperative places its cash and cash equivalents on deposit with financial institutions in the United States of America. The Federal Deposit Insurance Corporation (FDIC) insurance coverage limit is \$250,000 for substantially all depository accounts. Also, the FDIC temporarily provides unlimited coverage for non-interest bearing transaction accounts through December 31, 2012. At various times during the year, cash balances may exceed insured limits. The Cooperative has not experienced any losses in such accounts.

TEX-LA ELECTRIC COOPERATIVE OF TEXAS, INC.
NOTES TO FINANCIAL STATEMENTS - CONTINUED

NOTE 13 - CONCENTRATION OF CREDIT RISK - CONTINUED

The Cooperative's accounts receivable are subject to concentration of credit risk due to the Cooperative's customer base. A significant portion of the accounts receivable balance is due from the Cooperative's seven Members. The Cooperative believes the risk of loss related to this credit risk is remote.

NOTE 14 - DISCLOSURES ABOUT FAIR VALUE OF FINANCIAL INSTRUMENTS

The carrying amount of the Cooperative's cash investments, trade receivables and payables approximates their fair value because of the short maturities of these financial instruments.

Due to restrictions on repricing of the Cooperative's long-term debt and related assumptions, the fair value of these financial instruments is estimated by management to approximate the carrying value.

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

The Board of Directors
Tex-La Electric Cooperative of Texas, Inc.
Nacogdoches, Texas

We have audited the financial statements of Tex-La Electric Cooperative of Texas, Inc. as of and for the years ended December 31, 2010 and 2009 and have issued our report thereon dated April 15, 2011. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Governmental Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control

In planning and performing our audit, we considered the Cooperative's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion of the effectiveness of the Cooperative's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Cooperative's internal control over financial reporting.

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

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined below.

Compliance

As part of obtaining reasonable assurance about whether Tex-La Electric Cooperative of Texas, Inc.'s financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

This report is intended solely for the information and use of the audit committee, management, the Rural Utilities Service, and supplemental lenders, and is not intended to be and should not be used by anyone other than these specified parties. However, this report is a matter of public record and its distribution is not limited.


CERTIFIED PUBLIC ACCOUNTANTS

Lufkin, Texas
April 15, 2011