

CITY OF HILLSBORO, TEXAS

AUDITOR'S REPORT

FINANCIAL STATEMENTS

SEPTEMBER 30, 2010

CITY OF HILLSBORO, TEXAS

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PATTILLO, BROWN & HILL, L.L.P.
CERTIFIED PUBLIC ACCOUNTANTS ■ BUSINESS CONSULTANTS

INDEPENDENT AUDITOR'S REPORT

To the Honorable Mayor and
Members of City Council
City of Hillsboro, Texas

We have audited the accompanying financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of Hillsboro, Texas, as of and for the year ended September 30, 2010, which collectively comprise the City's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the City of Hillsboro, Texas' management. Our responsibility is to express opinions 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 and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the 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 opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of Hillsboro, Texas, as of September 30, 2010, and the respective changes in financial position and cash flows, where applicable, thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have issued a report dated May 2, 2011, on our consideration of the City of Hillsboro, Texas' internal control over financial reporting and on our tests of compliance with certain provisions of laws, regulations, contracts, grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and budgetary comparison information on pages 3 through 9 and 41 through 46 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the City of Hillsboro, Texas's financial statements as a whole. The introductory section and the combining and individual nonmajor fund financial statements, are presented for purposes of additional analysis and are not a required part of the financial statements. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations, and is also not a required part of the financial statements. The combining and individual nonmajor fund financial statements and the schedule of expenditures of federal awards are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole. The introductory section has not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we do not express an opinion or provide any assurance on it.

Pattillo, Brown & Hill, L.L.P.

May 2, 2011

Management's Discussion and Analysis

As management of the City of Hillsboro, we offer readers of the City's financial statements this narrative overview and analysis of the financial activities of the City for the fiscal year ended September 30, 2010. We encourage readers to consider the information presented here in conjunction with the financial statements which can be found in the following section of this report.

FINANCIAL HIGHLIGHTS

- The assets of the City exceed its liabilities as of September 30, 2010, by \$17,934,860 (net assets). Of this amount, \$6,600,130 (unrestricted net assets) may be used to meet the City's ongoing obligations to citizens and creditors in accordance with the City's fund designation and fiscal policies.
- The City's total net assets increased by \$1,777,617.
- As of the close of the current fiscal year, the City's governmental funds reported combined ending fund balances of \$7,000,968. Approximately 92.88% of this total amount, \$6,502,827, is unreserved fund balance available for use within the City's fund designation and fiscal policies.
- As of September 30, 2010, unreserved fund balance for the general fund was \$968,937 or 14.22 percent of total General Fund expenditures.

OVERVIEW OF THE FINANCIAL STATEMENTS

This discussion and analysis is intended to serve as an introduction to the City's basic financial statements. The City's basic financial statements comprise three components: 1) government-wide financial statements, 2) fund financial statements, and 3) notes to the financial statements. This report also contains other supplementary information in addition to the basic financial statements themselves.

Government-wide Financial Statements. The government-wide financial statements, which begin on page 10 of this report, are designed to provide readers with a broad overview of the City's finances, in a manner similar to a private-sector business.

The statement of net assets presents information on all of the City's assets and liabilities, with the difference between the two reported as net assets. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of the City is improving or deteriorating.

The statement of activities presents information showing how the City's net assets changed during the most recent fiscal year. All changes in net assets are reported when the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods (e.g., uncollected taxes and earned but unused compensated absences.)

Both of the government-wide financial statements distinguish functions of the City that are principally supported by taxes and intergovernmental revenues (governmental activities) from functions that are intended to recover all or a significant portion of their cost through user fees and charges (business-type activities). The governmental activities of the City include general government, public safety, streets, library, cemetery, parks and recreation, and community development. The business-type activities of the City include water, wastewater, storm water drainage, solid waste, and airport operations.

The government-wide financial statements can be found on pages 10 – 11 of this report.

Fund Financial Statements. A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The City, like other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. All of the funds of the City can be divided into two categories – governmental funds and proprietary funds.

Governmental Funds. Governmental funds are used to account for essentially the same functions reported as governmental activities in the government-wide financial statements. However, unlike the government-wide financial statements, governmental fund financial statements focus on current sources and uses of spendable resources, as well as on balances of spendable resources available at the end of the fiscal year. Such information may be useful in evaluating a government's near-term financing requirements.

Because the focus of governmental funds is narrower than that of the government-wide financial statements, it is useful to compare the information presented for governmental funds with similar information presented for governmental activities in the government-wide financial statements. By doing so, readers may better understand the long-term impact of the government's near-term financing decisions. Both the governmental fund balance sheet and the governmental fund statement of revenues, expenditures, and changes in fund balances provide a reconciliation to facilitate this comparison between governmental funds and governmental activities.

Beginning on page 12 of this report, information is presented separately in the Governmental Funds Balance Sheet and in the Governmental Funds Statement of Revenues, Expenditures, and Changes in Fund Balances for the General, EDC, Debt Service and Capital Projects Funds, which are considered to be major funds. A budgetary comparison statement has been provided for the General Fund and EDC to demonstrate compliance with the annual appropriated budget in the required supplementary information section. Data for the other governmental funds are combined into a single, aggregated presentation. Individual fund data for each of these nonmajor governmental funds is provided in the form of combining fund statements and schedules elsewhere in this report.

Proprietary Funds. The City maintains one type of proprietary fund. Enterprise funds are used to report the same functions presented as business-type activities in the government-wide financial statements. The City uses the enterprise funds to account for water, wastewater, storm water drainage, solid waste, and airport operations.

Proprietary funds provide the same type of information as the government-wide financial statements, only in more detail.

The basic proprietary fund financial statements can be found on pages 15 – 18 of this report.

Notes to the Financial Statements. The notes provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements. The notes to the financial statements can be found on pages 19 – 40 of this report.

Other Information. In addition to the basic financial statements and accompanying notes, this report also presents combining fund statements and schedules that further support the information in the financial statements. The combining fund statements and schedules for nonmajor funds are presented immediately following the notes to required supplementary information beginning on page 49 of this report.

GOVERNMENT-WIDE FINANCIAL ANALYSIS

As noted earlier, net assets may serve over time as a useful indicator of a government's financial position. In the case of the City, assets exceeded liabilities by \$17,934,860 as of September 30, 2010.

CITY OF HILLSBORO'S NET ASSETS

	Governmental Activities		Business-type Activities		Totals	
	2010	2009	2010	2009	2010	2008
Current assets	\$ 8,157,101	\$ 6,481,072	\$ 2,445,345	\$ 2,165,724	\$ 10,602,446	\$ 8,646,796
Capital assets	<u>13,414,848</u>	<u>12,951,692</u>	<u>11,120,262</u>	<u>10,702,567</u>	<u>24,535,110</u>	<u>23,654,259</u>
Total Assets	<u>21,571,949</u>	<u>19,432,764</u>	<u>13,565,607</u>	<u>12,868,291</u>	<u>35,137,556</u>	<u>32,301,055</u>
Liabilities	726,094	652,165	529,741	400,350	1,255,835	1,052,515
Noncurrent liabilities	<u>10,954,057</u>	<u>10,500,166</u>	<u>4,992,804</u>	<u>4,522,624</u>	<u>15,946,861</u>	<u>15,022,790</u>
Total Liabilities	<u>11,680,151</u>	<u>11,152,331</u>	<u>5,522,545</u>	<u>4,922,974</u>	<u>17,202,696</u>	<u>16,075,305</u>
Net assets:						
Invested in capital assets, net of related debt	4,680,905	4,518,512	6,155,684	6,205,470	10,836,589	10,723,982
Restricted	498,141	629,039	-	-	498,141	629,039
Unrestricted	<u>4,712,752</u>	<u>3,132,882</u>	<u>1,887,378</u>	<u>1,739,847</u>	<u>6,600,130</u>	<u>4,872,729</u>
Total Net Assets	\$ <u>9,891,798</u>	\$ <u>8,280,433</u>	\$ <u>8,043,062</u>	\$ <u>7,945,317</u>	\$ <u>17,934,860</u>	\$ <u>16,225,750</u>

The City uses capital assets to provide services to citizens; consequently, these assets are not available for future spending. Although the City's investment in its capital assets is reported net of related debt, it should be noted that the resources needed to repay this debt must be provided from other sources, since the capital assets themselves cannot be used to liquidate these liabilities. The remaining balance of unrestricted net assets \$6,600,130 may be used to meet the government's ongoing obligations to citizens and creditors.

CITY OF HILLSBORO'S CHANGES IN NET ASSETS

	Governmental Activities		Business-type Activities		Totals	
	2010	2009	2010	2009	2010	2009
REVENUES:						
Program revenues:						
Charges for services	\$ 1,320,690	\$ 1,073,948	\$ 5,226,953	\$ 5,165,776	\$ 6,547,643	\$ 6,239,724
Operating grants	115,288	56,616	429,831	15,187	545,119	71,803
Capital grants and contributions	835,234	304,303	454,408	-	1,289,642	304,303
General revenues:						
Property taxes	3,102,551	3,080,501	-	-	3,102,551	3,080,501
Sales taxes	2,464,389	2,572,730	-	-	2,464,389	2,572,730
Franchise taxes	494,961	521,747	-	-	494,961	521,747
Hotel/motel taxes	306,155	379,311	-	-	306,155	379,311
Other taxes	44,625	83,132	-	-	44,625	83,132
Investment earnings	83,010	125,777	2,002	13,439	85,012	139,216
Miscellaneous	90,436	116,621	54,024	55,861	144,460	172,482
Total Revenues	<u>8,857,339</u>	<u>8,314,686</u>	<u>6,167,218</u>	<u>5,250,263</u>	<u>15,024,557</u>	<u>13,564,949</u>
EXPENSES:						
General government	1,958,587	1,642,858	-	-	1,958,587	1,642,858
Public safety	4,066,292	4,123,236	-	-	4,066,292	4,123,236
Streets	720,652	916,090	-	-	720,652	916,090
Community development	1,245,654	817,064	-	-	1,245,654	817,064
Interest on long-term debt	420,868	500,395	-	-	420,868	500,395
Water and sewer	-	-	3,723,130	3,535,251	3,723,130	3,535,251
Sanitation	-	-	823,552	813,675	823,552	813,675
Airport	-	-	288,205	226,291	288,205	226,291
Total Expenses	<u>8,412,053</u>	<u>7,999,643</u>	<u>4,834,887</u>	<u>4,575,217</u>	<u>13,246,940</u>	<u>12,574,860</u>
INCREASES IN NET ASSETS						
BEFORE TRANSFERS	445,286	315,043	1,332,331	675,046	1,777,617	990,089
TRANSFERS	<u>306,386</u>	<u>907,082</u>	(306,386)	(907,082)	-	-
CHANGE IN NET ASSETS	751,672	1,222,125	1,025,945	(232,036)	1,777,617	990,089
NET ASSETS, BEGINNING	<u>8,280,433</u>	<u>7,141,929</u>	<u>7,945,317</u>	<u>8,177,353</u>	<u>16,225,750</u>	<u>15,319,282</u>
PRIOR PERIOD ADJUSTMENT	<u>859,693</u>	(83,621)	(928,200)	-	(68,507)	(83,621)
NET ASSETS, ENDING	<u>\$ 9,891,798</u>	<u>\$ 8,280,433</u>	<u>\$ 8,043,062</u>	<u>\$ 7,945,317</u>	<u>\$ 17,934,860</u>	<u>\$ 16,225,750</u>

At the end of the current fiscal year, the City is able to report positive balances in all three categories of net assets, both for the business-type activities and the government as a whole.

The government's net assets increased by \$1,777,617 during the current fiscal year. This increase in net assets is due to cost saving tactics used by the City. Additionally, charges for services, operating grants and contributions, capital grants and contributions and property tax revenue increased to cover the decrease in sales tax, franchise, hotel/motel, other taxes, investment earnings and miscellaneous revenues.

Governmental Activities. Governmental activities increased the City's net assets by \$751,672, thereby accounting for 42.29 percent of the total growth in the net assets of the City. Key elements of this increase are as follows:

- Charges for services revenue increased by \$246,742
- Operating grants and contributions revenue increased by 58,672
- Capital grants and contributions revenue increased by 530,931

Business-type Activities. Business-type activities increased the City's net assets by \$1,025,945, accounting for 57.71 percent of the total growth in the net assets of the City. Key elements of this increase are as follows:

- Operating grants and contributions increased by \$414,644.
- Transfers to governmental activities decreased \$600,696
- The Airport Fund had capital grants and contributions of 454,408 which the City did not have in the prior year

FINANCIAL ANALYSIS OF THE GOVERNMENT'S FUNDS

As noted earlier, the City uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements.

Governmental Funds. The focus of the City's governmental funds is to provide information on near term inflows, outflows, and balances of spendable resources. Such information is useful in assessing the City's financing requirements. In particular, unreserved fund balance may serve as a useful measure of a government's net resources available for spending at the end of the fiscal year.

As of the end of the current fiscal year, the City's governmental funds reported combined ending fund balances of \$7,000,968. Approximately 92.88% of this total amount, \$6,502,827 constitutes unreserved fund balance. Refer to page 12 of this report for a more detailed presentation of governmental fund balances.

The General Fund is the chief operating fund of the City. At the end of the current fiscal year, unreserved fund balance of the General Fund was \$968,937, while total fund balance reached \$1,375,745.

The fund balance of the City's General Fund increased by \$2,234 during the current fiscal year. Key factors in this increase are the increases in fines and forfeitures and contributions as well as a decrease in services and capital outlay expenditures.

The Capital Projects Fund has a total fund balance of \$3,396,993. The City is completing street improvement projects, purchasing other equipment and completing park improvements from these funds.

Proprietary Funds. The City's proprietary funds provide the same type of information found in the government-wide financial statements, but in more detail.

Unrestricted net assets of the City's Enterprise Funds at the end of the year amounted to \$1,887,378. The increase in net assets was \$1,025,945. Other factors concerning the finances of these funds have already been addressed in the discussion of the City's business-type activities.

General Fund Budgetary Highlights

No budget amendments were made to the original budget in fiscal year 2010.

Net reimbursement revenues were used to fund the differences in the budgeted expenditures without reducing the budgeted General Fund fund balance.

CAPITAL ASSETS

The City's investment in capital assets for its governmental and business type activities as of September 30, 2010, amounts to \$24,535,110 (net of accumulated depreciation). This investment in capital assets includes land, buildings, improvements, machinery and equipment, park facilities and infrastructure.

Major capital asset events occurring during the current fiscal year included the following:

- Various improvements of \$542,403
- Street improvements of \$310,446
- Acquired equipment for approximately \$226,825

Additional information on the City's capital assets can be found on pages 29 and 30 of this report.

DEBT ADMINISTRATION

At the end of the current fiscal year, the City had total bonded debt of \$15,333,061. All of which represents bonded debt backed by the full faith and credit of the City.

The City's General Obligation, Tax and Certificates of Obligation Bond ratings are listed below.

	<u>Standard and Poor's</u>
General Obligation Bonds	A

Additional information on the City's long term-debt can be found in pages 31 – 35 of this report.

ECONOMIC FACTORS AND BUDGETS AND RATES

The City's elected and appointed officials consider many factors when preparing the City of Hillsboro's budget for the 2011 fiscal year. The property tax rate for the fiscal year 2011 remained at .818331 per \$100 assessed value. A negligible change of .000025 was transferred from maintenance and operations to debt service to maintain the proper debt coverage ratio. Due to the slowing economy, decreases in sales tax revenue (4%), decrease in interest income and decreases in various franchise revenue were considered. Also no step increases for the year and increase of 6% in health care costs.

During the current fiscal year, unreserved fund balance in the General Fund increased to \$968,937. The City uses surplus working capital from the General Fund to supplement capital projects (e.g. street paving, code enforcement demolition, capital replacement) during the year as the needs arise and where favorable unit pricing is received on such projects.

REQUESTS FOR INFORMATION

This financial report is designed to provide a general overview of the City's finances for all those with an interest in the government's finances. Questions concerning any of the information provided in this report or requests for additional information should be addressed to Jack Harper, City Manager, P.O. Box 568, Hillsboro, Texas 76645 or call (254) 582-3271.

CITY OF HILLSBORO, TEXAS

STATEMENT OF NET ASSETS

SEPTEMBER 30, 2010

	Primary Government		
	Governmental Activities	Business-type Activities	Total
ASSETS			
Cash and investments	\$ 6,758,389	\$ 1,543,941	\$ 8,302,330
Receivables (net of allowances for uncollectibles):			
Taxes	647,705	-	647,705
Accounts	67,001	605,777	672,778
Intergovernmental	238,430	117,086	355,516
Other	216,521	-	216,521
Inventories	-	145,472	145,472
Deferred charges	229,055	33,069	262,124
Capital assets:			
Land	764,632	378,391	1,143,023
Buildings and improvements	5,681,221	5,234,001	10,915,222
Machinery and equipment	3,339,946	1,646,271	4,986,217
Infrastructure/water and wastewater distribution	8,243,421	14,175,479	22,418,900
Construction in progress	292,087	1,065,514	1,357,601
Less: accumulated depreciation	(4,906,459)	(11,379,394)	(16,285,853)
Total capital assets	<u>13,414,848</u>	<u>11,120,262</u>	<u>24,535,110</u>
Total assets	<u>21,571,949</u>	<u>13,565,607</u>	<u>35,137,556</u>
LIABILITIES			
Accounts payable	526,616	241,249	767,865
Accrued liabilities	111,721	17,453	129,174
Accrued interest payable	87,757	47,072	134,829
Customer deposits	-	223,967	223,967
Noncurrent liabilities:			
Due within one year	746,165	478,093	1,224,258
Due in more than one year	10,207,892	4,514,711	14,722,603
Total liabilities	<u>11,680,151</u>	<u>5,522,545</u>	<u>17,202,696</u>
NET ASSETS			
Invested in capital assets, net of related debt	4,680,905	6,155,684	10,836,589
Restricted for:			
Court security and technology	183,030	-	183,030
Police seizures	223,778	-	223,778
Debt service	91,333	-	91,333
Unrestricted	<u>4,712,752</u>	<u>1,887,378</u>	<u>6,600,130</u>
Total net assets	<u>\$ 9,891,798</u>	<u>\$ 8,043,062</u>	<u>\$ 17,934,860</u>

The notes to the financial statements are an integral part of this statement.

CITY OF HILLSBORO, TEXAS

STATEMENT OF ACTIVITIES

FOR THE YEAR ENDED SEPTEMBER 30, 2010

	Program Revenues			Net (Expense) Revenue and Changes in Net Assets			
	Expenditures	Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	Governmental Activities	Business-type Activities	Total
Primary Government:							
Governmental activities:							
General government	\$ 1,958,587	\$ 32,053	\$ 52,246	\$ 63,127	\$ (1,811,161)	\$ -	\$ (1,811,161)
Public safety	4,066,292	1,197,677	63,042	177,806	(2,627,767)	-	(2,627,767)
Streets	720,652	-	-	-	(720,652)	-	(720,652)
Community development	1,245,654	90,960	-	594,301	(560,393)	-	(560,393)
Interest on long-term debt	420,868	-	-	-	(420,868)	-	(420,868)
Total governmental activities	<u>8,412,053</u>	<u>1,320,690</u>	<u>115,288</u>	<u>835,234</u>	<u>(6,140,841)</u>	<u>-</u>	<u>(6,140,841)</u>
Business-type activities:							
Water and sewer	3,723,130	3,874,742	364,653	-	-	516,265	516,265
Sanitation	823,552	1,085,177	-	-	-	261,625	261,625
Airport	288,205	267,034	65,178	454,408	-	498,415	498,415
Total business-type activities	<u>4,834,887</u>	<u>5,226,953</u>	<u>429,831</u>	<u>454,408</u>	<u>-</u>	<u>1,276,305</u>	<u>1,276,305</u>
Total	\$ 13,246,940	\$ 6,547,643	\$ 545,119	\$ 1,289,642	\$ (6,140,841)	\$ 1,276,305	\$ (4,864,536)
General revenues:							
Taxes:							
Property - general purposes					1,990,311	-	1,990,311
Property - debt service					1,112,240	-	1,112,240
Sales					2,464,389	-	2,464,389
Franchise					494,961	-	494,961
Hotel/Motel					306,155	-	306,155
Other					44,625	-	44,625
Investment earnings					83,010	2,002	85,012
Miscellaneous					90,436	54,024	144,460
Transfers					306,386	(306,386)	-
Total general revenues					<u>6,892,513</u>	<u>(250,360)</u>	<u>6,642,153</u>
Change in net assets					751,672	1,025,945	1,777,617
Net assets, beginning					8,280,433	7,945,317	16,225,750
Prior period adjustment					859,693	(928,200)	(68,507)
Net assets, ending					<u>\$ 9,891,798</u>	<u>\$ 8,043,062</u>	<u>\$ 17,934,860</u>

The notes to the financial statements are an integral part of this statement.

CITY OF HILLSBORO, TEXAS

BALANCE SHEET

GOVERNMENTAL FUNDS

SEPTEMBER 30, 2010

	<u>General</u>	<u>Economic Development Corporation</u>	<u>Debt Service</u>	<u>Capital Projects</u>	<u>Other Governmental Funds</u>	<u>Total Governmental Funds</u>
ASSETS						
Cash and investments	\$ 1,245,708	\$ 1,911,571	\$ 78,772	\$ 3,412,687	\$ 109,651	\$ 6,758,389
Receivables (net of allowance for uncollectibles)						
Taxes	475,930	34,980	34,311	-	102,484	647,705
Accounts	242,701	-	4,245	-	36,576	283,522
Intergovernmental	-	-	-	-	238,430	238,430
Due from other funds	163,171	-	-	-	518	163,689
Total assets	<u>\$ 2,127,510</u>	<u>\$ 1,946,551</u>	<u>\$ 117,328</u>	<u>\$ 3,412,687</u>	<u>\$ 487,659</u>	<u>\$ 8,091,735</u>
LIABILITIES AND FUND BALANCES						
Liabilities:						
Accounts payable	\$ 377,298	\$ 53,786	\$ -	\$ 15,694	\$ 79,838	\$ 526,616
Accrued liabilities	111,721	-	-	-	-	111,721
Due to other funds	-	-	-	-	163,689	163,689
Deferred revenue	262,746	-	25,995	-	-	288,741
Total liabilities	<u>751,765</u>	<u>53,786</u>	<u>25,995</u>	<u>15,694</u>	<u>243,527</u>	<u>1,090,767</u>
Fund balances:						
Reserved for:						
Court security and technology	183,030	-	-	-	-	183,030
Police seizures	223,778	-	-	-	-	223,778
Debt service	-	-	91,333	-	-	91,333
Unreserved, reported in:						
General fund	968,937	-	-	-	-	968,937
Special revenue funds	-	1,892,765	-	-	216,473	2,109,238
Capital projects funds	-	-	-	3,396,993	27,659	3,424,652
Total fund balances	<u>1,375,745</u>	<u>1,892,765</u>	<u>91,333</u>	<u>3,396,993</u>	<u>244,132</u>	<u>7,000,968</u>
Total liabilities and fund balances	<u>\$ 2,127,510</u>	<u>\$ 1,946,551</u>	<u>\$ 117,328</u>	<u>\$ 3,412,687</u>	<u>\$ 487,659</u>	
Capital assets used in governmental activities are not financial resources and, therefore, are not reported in the funds.						13,414,848
Other long-term assets are not available to pay for current-period expenditures and, therefore, are deferred in the funds.						430,039
Long-term liabilities are not due and payable in the current period and therefore are not reported in the funds.						(10,954,057)
Net assets of governmental activities						<u>\$ 9,891,798</u>

The notes to the financial statements are an integral part of this statement.

CITY OF HILLSBORO, TEXAS

**STATEMENT OF REVENUES, EXPENDITURES AND
CHANGES IN FUND BALANCES**

GOVERNMENTAL FUNDS

FOR THE YEAR ENDED SEPTEMBER 30, 2010

	<u>General</u>	<u>Economic Development Corporation</u>	<u>Debt Service</u>	<u>Capital Projects</u>	<u>Other Governmental Funds</u>	<u>Total Governmental Funds</u>
REVENUES						
Taxes:						
Ad valorem	\$ 1,987,304	\$ -	\$ 1,108,394	\$ -	\$ -	\$ 3,095,698
Sales	2,259,010	205,379	-	-	-	2,464,389
Franchise	494,961	-	-	-	-	494,961
Hotel/motel	-	-	-	-	306,155	306,155
Other	44,625	-	-	-	-	44,625
Services to others	4,548	-	-	-	-	4,548
Licenses and permits	78,310	-	-	-	-	78,310
Fines and forfeitures	971,834	-	-	-	-	971,834
Intergovernmental	24,772	165,928	-	-	675,160	865,860
Interest and penalties	46,038	12,025	21,282	3,281	384	83,010
Rentals	21,635	-	-	-	12,650	34,285
Charges for services	163,157	-	-	-	-	163,157
Cemetery lot sales and fees	26,805	-	-	-	-	26,805
Contributions	63,736	-	-	-	20,926	84,662
Other	78,017	12,257	-	-	162	90,436
Total revenues	<u>6,264,752</u>	<u>395,589</u>	<u>1,129,676</u>	<u>3,281</u>	<u>1,015,437</u>	<u>8,808,735</u>
EXPENDITURES						
Current:						
Personnel	4,919,963	-	-	161,052	20,000	5,101,015
Supplies	462,636	137	-	-	10,365	473,138
Services	921,294	24,806	-	-	562,161	1,508,261
Maintenance	219,767	5,563	-	-	2,510	227,840
Minor equipment	30,188	-	-	-	131,410	161,598
Capital outlay	104,013	322,857	-	210,813	251,245	888,928
Grant expense	8,940	-	-	-	-	8,940
Debt service:						
Principal	134,192	-	2,221,800	-	15,000	2,370,992
Interest	11,183	-	420,652	-	12,907	444,742
Bond issuance costs	-	-	85,670	43,967	-	129,637
Total expenditures	<u>6,812,176</u>	<u>353,363</u>	<u>2,728,122</u>	<u>415,832</u>	<u>1,005,598</u>	<u>11,315,091</u>
EXCESS (DEFICIENCY) OF REVENUES OVER (UNDER) EXPENDITURES	<u>(547,424)</u>	<u>42,226</u>	<u>(1,598,446)</u>	<u>(412,551)</u>	<u>9,839</u>	<u>(2,506,356)</u>
OTHER FINANCING SOURCES (USES)						
Issuance of long-term debt	-	-	1,525,000	2,000,000	-	3,525,000
Premium on long-term debt	-	-	33,631	43,967	-	77,598
Operating transfers in	616,806	-	-	-	51,274	668,080
Operating transfers out	<u>(67,148)</u>	<u>(104,546)</u>	<u>-</u>	<u>-</u>	<u>(190,000)</u>	<u>(361,694)</u>
Total other financing sources (uses)	<u>549,658</u>	<u>(104,546)</u>	<u>1,558,631</u>	<u>2,043,967</u>	<u>(138,726)</u>	<u>3,908,984</u>
NET CHANGE IN FUND BALANCES	2,234	(62,320)	(39,815)	1,631,416	(128,887)	1,402,628
FUND BALANCES, BEGINNING	<u>1,373,511</u>	<u>1,955,085</u>	<u>131,148</u>	<u>1,765,577</u>	<u>373,019</u>	<u>5,598,340</u>
FUND BALANCES, ENDING	<u>\$ 1,375,745</u>	<u>\$ 1,892,765</u>	<u>\$ 91,333</u>	<u>\$ 3,396,993</u>	<u>\$ 244,132</u>	<u>\$ 7,000,968</u>

The notes to the financial statements are an integral part of this statement.

CITY OF HILLSBORO, TEXAS

**RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES
AND CHANGES IN FUND BALANCE OF GOVERNMENTAL FUNDS
TO THE STATEMENT OF ACTIVITIES**

FOR THE YEAR ENDED SEPTEMBER 30, 2010

Amounts reported for governmental activities in the Statement of Activities (page 11) are different because:

Net change in fund balances - total governmental funds (page 13)	\$ 1,402,628
Governmental funds report capital outlays as expenditures. However, in the statement of activities the cost of those assets is allocated over their estimated useful lives and reported as depreciation expense.	463,156
Revenues in the statement of activities that do not provide current financial resources are not reported as revenues in the funds.	48,604
The issuance of long-term debt (e.g., bonds, leases) provides current financial resources to governmental funds, while the repayment of the principal of long-term debt consumes the current financial resources of governmental funds.	(1,314,200)
Some expenses reported in the statement of activities do not require the use of current financial resources and, therefore, are not reported as expenditures in governmental funds.	<u>151,484</u>
Change in net assets of governmental activities (page 11)	<u>\$ 751,672</u>

The notes to the financial statements are an integral part of this statement.

CITY OF HILLSBORO, TEXAS
STATEMENT OF NET ASSETS
PROPRIETARY FUNDS
SEPTEMBER 30, 2010

ASSETS	Business-type Activities-Enterprise Fund			
	Water and Wastewater	Sanitation	Airport	Totals
Cash and investments	\$ 1,228,642	\$ 312,744	\$ 2,555	\$ 1,543,941
Accounts receivable	532,878	48,101	24,798	605,777
Intergovernmental receivable	68,909	-	48,177	117,086
Inventories	122,328	-	23,144	145,472
Other assets	33,069	-	-	33,069
Fixed assets	10,094,139	105,956	920,167	11,120,262
Total assets	\$ 12,079,965	\$ 466,801	\$ 1,018,841	\$ 13,565,607
LIABILITIES				
Current liabilities:				
Accounts payable	\$ 170,776	\$ 65,173	\$ 5,300	\$ 241,249
Customer deposits	223,967	-	-	223,967
Accrued liabilities	16,463	-	990	17,453
Accrued interest payable	47,072	-	-	47,072
Capital lease payable	23,093	-	-	23,093
Bonds payable	455,000	-	-	455,000
Total current liabilities	936,371	65,173	6,290	1,007,834
Long-term liabilities:				
Capital lease payable	48,590	-	-	48,590
Bonds payable	4,437,895	-	-	4,437,895
Vacation payable	26,605	-	1,621	28,226
Total long-term liabilities	4,513,090	-	1,621	4,514,711
Total liabilities	5,449,461	65,173	7,911	5,522,545
NET ASSETS				
Invested in capital assets, net of related debt	5,129,561	105,956	920,167	6,155,684
Unrestricted	1,500,943	295,672	90,763	1,887,378
Total net assets	\$ 6,630,504	\$ 401,628	\$ 1,010,930	\$ 8,043,062

The notes to the financial statements are an integral part of this statement.

CITY OF HILLSBORO, TEXAS

STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN FUND NET ASSETS

PROPRIETARY FUNDS

FOR THE YEAR ENDED SEPTEMBER 30, 2010

	Business-type Activities-Enterprise Fund			
	Water and Wastewater	Sanitation	Airport	Totals
OPERATING REVENUES				
Water and sewer sales	\$ 3,782,990	\$ -	\$ -	\$ 3,782,990
Other service charges	91,752	1,085,177	267,034	1,443,963
Miscellaneous income	<u>54,024</u>	<u>-</u>	<u>-</u>	<u>54,024</u>
Total operating revenues	<u>3,928,766</u>	<u>1,085,177</u>	<u>267,034</u>	<u>5,280,977</u>
OPERATING EXPENSES				
Water purchase	1,474,942	-	-	1,474,942
Personnel	743,208	-	45,935	789,143
Supplies	98,825	-	172,077	270,902
Services	441,627	812,999	27,810	1,282,436
Maintenance	237,627	8,311	9,606	255,544
Depreciation and amortization	<u>480,341</u>	<u>2,242</u>	<u>32,777</u>	<u>515,360</u>
Total operating expenses	<u>3,476,570</u>	<u>823,552</u>	<u>288,205</u>	<u>4,588,327</u>
OPERATING INCOME (LOSS)	<u>452,196</u>	<u>261,625</u>	<u>(21,171)</u>	<u>692,650</u>
NONOPERATING REVENUES (EXPENSES)				
Interest income	2,002	-	-	2,002
Contributions	364,653	-	519,586	884,239
Interest expense	<u>(246,560)</u>	<u>-</u>	<u>-</u>	<u>(246,560)</u>
Total nonoperating revenues (expenses)	<u>120,095</u>	<u>-</u>	<u>519,586</u>	<u>639,681</u>
INCOME (LOSS) BEFORE OPERATING TRANSFERS	572,291	261,625	498,415	1,332,331
OPERATING TRANSFERS FROM (TO) OTHER FUNDS	<u>(6,386)</u>	<u>(320,000)</u>	<u>20,000</u>	<u>(306,386)</u>
CHANGE IN NET ASSETS	565,905	(58,375)	518,415	1,025,945
TOTAL NET ASSETS, BEGINNING	<u>6,992,799</u>	<u>460,003</u>	<u>492,515</u>	<u>7,945,317</u>
PRIOR PERIOD ADJUSTMENT	<u>(928,200)</u>	<u>-</u>	<u>-</u>	<u>(928,200)</u>
TOTAL NET ASSETS, ENDING	<u>\$ 6,630,504</u>	<u>\$ 401,628</u>	<u>\$ 1,010,930</u>	<u>\$ 8,043,062</u>

The notes to the financial statements are an integral part of this statement.

CITY OF HILLSBORO, TEXAS

STATEMENT OF CASH FLOWS

PROPRIETARY FUNDS

FOR THE YEAR ENDED SEPTEMBER 30, 2010

	Business-type Activities - Enterprise Fund			
	Water and Wastewater	Sanitation	Airport	Totals
CASH FLOWS FROM OPERATING ACTIVITIES				
Cash received from customers	\$ 3,883,527	\$ 1,084,774	\$ 248,965	\$ 5,217,266
Cash payments to employees for services	(739,664)	-	(45,668)	(785,332)
Cash payments to suppliers for goods and services	(2,108,526)	(821,428)	(229,043)	(3,158,997)
Cash provided (used) by operating activities	<u>1,035,337</u>	<u>263,346</u>	<u>(25,746)</u>	<u>1,272,937</u>
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES				
Cash paid to other funds	(6,386)	(320,000)	20,000	(306,386)
Cash used for noncapital financing activities	<u>(6,386)</u>	<u>(320,000)</u>	<u>20,000</u>	<u>(306,386)</u>
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES				
Principal repayments on debt	(250,000)	-	-	(250,000)
Capital contributions	295,744	-	17,001	312,745
Proceeds from capital debt	752,895	-	-	752,895
Capital lease payments	(35,414)	-	-	(35,414)
Refunding of bonds	(928,200)	-	-	(928,200)
Interest and fiscal charges on debt	(247,898)	-	-	(247,898)
Acquisition and construction of capital assets	(467,091)	-	(8,800)	(475,891)
Cash provided (used) by capital and related financing activities	<u>(879,964)</u>	<u>-</u>	<u>8,201</u>	<u>(871,763)</u>
CASH FLOWS FROM INVESTING ACTIVITIES				
Interest on investments	<u>2,002</u>	<u>-</u>	<u>-</u>	<u>2,002</u>
Cash provided by investing activities	<u>2,002</u>	<u>-</u>	<u>-</u>	<u>2,002</u>
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	150,989	(56,654)	2,455	96,790
CASH AND CASH EQUIVALENTS, BEGINNING	<u>1,077,653</u>	<u>369,398</u>	<u>100</u>	<u>1,447,151</u>
CASH AND CASH EQUIVALENTS, ENDING	<u>\$ 1,228,642</u>	<u>\$ 312,744</u>	<u>\$ 2,555</u>	<u>\$ 1,543,941</u>

(continued)

CITY OF HILLSBORO, TEXAS
STATEMENT OF CASH FLOWS
PROPRIETARY FUNDS
(Continued)
FOR THE YEAR ENDED SEPTEMBER 30, 2010

	Business-type Activities - Enterprise Fund			
	Water and Wastewater	Sanitation	Airport	Totals
RECONCILIATION OF OPERATING INCOME (LOSS) TO NET CASH PROVIDED BY OPERATING ACTIVITIES				
Operating income (loss)	\$ 452,196	\$ 261,625	\$(21,171)	\$ 692,650
Adjustments to reconcile operating income to net cash provided by operating activities:				
Depreciation and amortization	480,341	2,242	32,777	515,360
Change in assets and liabilities:				
Decrease (increase) in accounts receivable	(47,238)	(403)	(18,069)	(65,710)
Decrease (increase) in other assets	2,097	-	-	2,097
Increase (decrease) in accounts payable	124,142	(118)	3,594	127,618
Increase (decrease) in accrued liabilities	1,011	-	101	1,112
Increase (decrease) in vacation payable	2,533	-	166	2,699
Increase (decrease) in customer deposits	1,999	-	-	1,999
Decrease (increase) in inventory	18,256	-	(23,144)	(4,888)
Total adjustments	<u>583,141</u>	<u>1,721</u>	<u>(4,575)</u>	<u>580,287</u>
Net cash provided by operating activities	<u>\$ 1,035,337</u>	<u>\$ 263,346</u>	<u>\$(25,746)</u>	<u>\$ 1,272,937</u>

The notes to the financial statements are an integral part of this statement.

CITY OF HILLSBORO, TEXAS

NOTES TO THE FINANCIAL STATEMENTS

SEPTEMBER 30, 2010

I. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

General Statement

The City of Hillsboro was incorporated on March 21, 1881. The City operates under a Council-Manager form of government and provides the following services as authorized by its charter: public safety, public works, public health and welfare, recreation and waterworks.

The accounting and reporting policies of the City relating to the funds included in the accompanying basic financial statements conform to generally accepted accounting principles applicable to state and local governments. Generally accepted accounting principles for local governments include those principles prescribed by the *Governmental Accounting Standards Board (GASB)*, the American Institute of Certified Public Accountants in the publication entitled *Audits of State and Local Governmental Units* and by the Financial Accounting Standards Board (when applicable). As allowed in Section P80 of GASB's *Codification of Governmental Accounting and Financial Reporting Standards*, the City has elected not to apply to its proprietary activities Financial Accounting Standards Board Statements and Interpretations, Accounting Principles Board Opinions, and Accounting Research Bulletins of the Committee of Accounting Procedure issued after November 30, 1989. The more significant accounting policies of the City are described below:

Financial Reporting Entity

The accompanying financial statements comply with the provisions of the GASB Statements No. 14 and 39, "The Financial Reporting Entity," in that the financial statements include all organizations, activities, functions and component units for which the City (the "primary government") is financially accountable. Financial accountability is defined as the appointment of a voting majority of a legally separate organization's governing body and either (1) the City's ability to impose its will over the organization, or (2) the potential that the organization will provide a financial benefit to or impose a financial burden on the City. Based on the aforementioned criteria, the City of Hillsboro has a fully blended component unit, the Economic Development Corporation.

Government-wide Fund Financial Statements

The government-wide financial statements (i.e., the statement of net assets and the statement of activities) report information on all of the nonfiduciary activities of the primary government. For the most part, the effect of interfund activity has been removed from these statements. *Governmental activities*, which normally are supported by taxes and intergovernmental revenue, are reported separately from *business-like activities*, which rely to a significant extent on fees and charges for support.

(continued)

I. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Government-wide Fund Financial Statements (Continued)

The statement of activities demonstrates the degree to which the direct expenses of a given function or segment are offset by program revenue. *Direct expenses* are those that are clearly identifiable with a specific function or segment. *Program revenue* includes 1) charges to customers or applicants who purchase, use, or directly benefit from goods, services, or privileges provided by a given function or segment, and 2) grants and contributions that are restricted to meeting the operational or capital requirements of a particular function or segment. Taxes and other items not properly included among program revenue are reported instead as *general revenue*.

Separate financial statements are provided for governmental funds and proprietary funds. Major individual governmental funds and major individual enterprise funds are reported as separate columns in the fund financial statements.

Measurement Focus, Basis of Accounting and Financial Statement Presentation

The government-wide financial statements are reported using the *economic resources measurement focus* and the *accrual basis of accounting*, as are the proprietary fund and fiduciary fund financial statements. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Property taxes are recognized as revenue in the year for which they are levied. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

Governmental fund financial statements are reported using the *current financial resources measurement focus* and the *modified accrual basis of accounting*. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be *available* when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the government considers revenue to be available if collected within 60 days of the end of the current fiscal period. Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However, debt service expenditures, as well as expenditures related to compensated absences and claims and judgments, are recorded only when payment is due.

Property taxes, franchise taxes, sales taxes, and interest associated with the current fiscal period are all considered to be susceptible to accrual and so have been recognized as revenue of the current fiscal period. All other revenue items are considered to be measurable and available only when cash is received by the City.

Governmental Funds are those through which most governmental functions of the City are financed. The acquisition, use, and balances of the City's expendable financial resources and the related liabilities (except those accounted for in the proprietary fund type) are accounted for through governmental funds. The measurement focus is upon determination of changes in financial position, rather than upon net income determination.

(continued)

I. **SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

Measurement Focus, Basis of Accounting and Financial Statement Presentation (Continued)

The City reports the following major governmental funds:

The **General Fund** – is the general operating fund of the City. It is used to account for all financial resources except those required to be accounted for in another fund.

The **Debt Service Fund** – accounts for the resources accumulated and payments made for principal and interest not being financed by Proprietary Funds.

The **Capital Projects Fund** – accounts for financial resources to be used for the acquisition or construction of major capital projects which are not financed by Proprietary Funds.

The **Economic Development Corporation Fund** – accounts for financial resources to be used for the economic growth and development of the City.

Proprietary Funds are used to account for activities that are similar to those often found in the private sector. The measurement focus is upon determination of net income and capital maintenance.

The City reports the following major proprietary funds:

The **Water and Wastewater Fund** – is used to account for the activities necessary for the provisions of water and wastewater services.

The **Sanitation Fund** – is used to account for the activities necessary for the provisions of sanitation services.

The **Airport Fund** – is used to account for the activities necessary for the provisions of airport services and operations.

Additionally, the City reports the following fund types:

Special Revenue Funds – The ***Special Revenue Funds*** are used to account for the proceeds of specific revenue sources (other than assessments, expendable trusts or major capital projects) that are legally restricted to expenditures for specified purposes. These funds include the Hotel/Motel Tax Fund, Library Grants Fund, Search and Rescue Equipment Grant Fund, Main Street Fund, Downtown Streetscape Phase II Fund, Industrial Development Fund, Home Grant Fund, Home Buyers Assistance Grant Fund, Parks and Wildlife Grant Fund, Parks EDI Grant Fund, Energy Grant Fund, Downtown Streetscape Fund and the East Franklin Streetscape Fund.

Capital Projects Funds – ***Capital Projects Funds*** are used to account for financial resources to be used for the acquisition or construction of major capital projects which are not financed by Proprietary Funds. These funds include the Entry Monument Project Fund and the Capital Construction Fund.

(continued)

I. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Measurement Focus, Basis of Accounting and Financial Statement Presentation (Continued)

Enterprise Funds – *Enterprise Funds* are used to account for operations that are financed and operated in a manner similar to private business enterprises where the costs (expenses, including depreciation) of providing water, sewer and sanitation services to the general public on a continuing basis is financed through user charges. The Airport Fund is the only nonmajor Enterprise Fund.

Private-sector standards of accounting and financial reporting issued prior to December 1, 1989, generally are followed in both the government-wide and proprietary fund financial statements to the extent that those standards do not conflict with or contradict guidance of the Governmental Accounting Standards Board. Governments also have the *option* of following subsequent private-sector guidance for their business-type activities and Enterprise Funds, subject to this same limitation. The City has elected not to follow subsequent private-sector guidance.

As a general rule, the effect of interfund activity has been eliminated from the government-wide financial statements. Exceptions to this general rule are charges between the City's water and wastewater function and various other functions of the government. Elimination of these charges would distort the direct costs and program revenue reported for the various functions concerned.

Amounts reported as *program revenues* include: 1) charges to customers or applicants for goods, services, or privileges provided, 2) operating grants and contributions, and 3) capital grants and contributions, including special assessments. Internally dedicated resources are reported as *general revenues* rather than as program revenue. Likewise, general revenue includes all taxes.

Proprietary funds distinguish operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. The principal operating revenues of the City's Enterprise Funds are charges to customers for sales and services. Operating expenses for Enterprise Funds include the cost of sales and services, administrative expenses, and depreciation on capital assets. All revenue and expenses not meeting this definition are reported as nonoperating revenue and expenses.

When both restricted and unrestricted resources are available for use, it is the City's policy to use restricted resources first, then unrestricted resources as they are needed.

(continued)

I. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Assets, Liabilities and Net Assets or Equity

Cash and Cash Equivalents

For purpose of presenting the proprietary fund cash flow statement, cash and cash equivalents include cash demand and time deposits and investments with a maturity date within three months of the date acquired by the City.

Investments

State statutes authorize the City to invest in (1) obligations of the United States or its agencies and instrumentalities; (2) direct obligations of the State of Texas or its agencies; (3) other obligations, the principal of and interest on which are unconditionally guaranteed or insured by the State of Texas or the United States; (4) obligations of states, agencies, counties, cities, and other political subdivisions of any state having been rated as to investment quality by a nationally recognized investment rating firm and having received a rating of not less than "A" or its equivalent; (5) certificates of deposit by state and national banks domiciled in this state that are (a) guaranteed or insured by the Federal Deposit Insurance Corporation, or its successor; or, (b) secured by obligations that are described by (1) – (4); or, (6) fully collateralized direct repurchase agreements having a defined termination date, secured by obligations described by (1) pledged with a third-party selected or approved by the City, and placed through a primary government securities dealer.

Investments maturing within one year of date of purchase are stated at cost or amortized cost, all other investments are stated at fair value, which is based on quoted market prices.

Short-term Interfund Receivables/Payables

During the course of operations, numerous transactions occur between individual funds for goods provided or services rendered. These receivables and payables are classified as "due from other funds" or "due to other funds" on the balance sheet. Any residual balances outstanding between the governmental activities and business-type activities are reported in the government-wide financial statements as "internal balances."

Property Taxes

Property taxes attach as an enforceable lien on property as of January 1. Taxes are levied on October 1 and are due and payable on or before January 31 of the following year. All unpaid taxes become delinquent February 1 of the following year. City property tax revenue is recognized when levied. An allowance is established for delinquent taxes to the extent their collectability is improbable. For the year ended September 30, 2010, the City's property taxes were billed and collected by the Hill County Appraisal District. Receipts are remitted to the City on a monthly basis.

Ad valorem taxes for fiscal year 2010 were levied October 1, 2009, at the rate of \$.818331 per \$100 assessed valuation on a total taxable assessed valuation of \$388,233,073.

(continued)

I. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Assets, Liabilities and Net Assets or Equity (Continued)

Inventories

All inventories are valued at cost (first-in, first-out method). Inventories of governmental funds are recorded as expenditures when consumed rather than when purchased.

Capital Assets

Capital assets, which include property, plant, equipment and infrastructure assets (e.g. roads, bridges, sidewalks and similar items) are reported in the applicable governmental or business-type activities columns in the government-wide financial statements. The City defines capital assets as assets with an initial, individual cost of more than \$1,000 (amount not rounded) and an estimated useful life in excess of one year. Such assets are recorded at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at estimated fair market value at the date of donation.

The costs of normal maintenance and repairs that do not add to the value of the asset or materially extend assets' lives are not capitalized. Major outlays for capital assets and improvements are capitalized as projects are constructed.

Property, plant and equipment is depreciated using the straight-line method over the following estimated useful lives:

Assets	Years
Buildings	20 to 50
Waterworks and sanitation systems	15 to 40
Infrastructure	10 to 40
Machinery and equipment	5 to 10

Retiree Benefits

No post retirement health care benefits are provided by the City for retired employees.

Post-Employment Health Care Benefits

COBRA Benefits

Under the Consolidated Omnibus Budget Reconciliation Act (COBRA), the City provides health care benefits to eligible former employees and eligible dependents. Certain requirements are outlined by the federal government for this coverage. The premium is paid in full by the insured on or before the tenth (10th) day of the month for the actual month covered. This program is offered for a duration of 18 months after the termination date. There is no associated cost to the City under this program, and there were no participants in the program as of September 30, 2010.

(continued)

I. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Assets, Liabilities and Net Assets or Equity (Continued)

Capitalized Interest

The City capitalizes net interest cost and interest earned as part of the cost of constructing various projects when material. During the year ended September 30, 2010, no interest costs were capitalized.

Liability for Compensated Absences

The City allows employees to accumulate unused sick leave to a maximum of 90 days. Sick leave is earned at the rate of 8 hours (10.6 hours for firefighters) per month worked. Unused sick leave is canceled upon termination of employment without compensation to the employee.

Regular fulltime City employees are eligible to accrue paid vacation leave. Employees are encouraged to take regular vacation at least annually. Employees are not credited with vacation leave until the completion of six consecutive months of service with the City. Vacation leave in the amount of 40 hours (60 hours for firefighters) is credited to an employee, upon completion of the initial six-month period. Employees with up to three years of service will be entitled to 120 hours per year of vacation with pay (80 hours for firefighters); with three to nine years of service, 180 hours per year of vacation with pay (120 hours for firefighters); and with 10 years of service and longer, 240 hours per year of vacation with pay (160 hours for firefighters).

The maximum amount of unused vacation leave that an employee can accumulate is 240 hours. Any balance in excess of 240 hours is reduced to the maximum, without compensation to the employee, at the end of each fiscal year. When an employee leaves the services of the City, he or she will be paid for accrued, but unused vacation leave not to exceed 240 hours. The rate of pay will be determined by the salary rate in effect at the time of termination.

Long-term Obligations

In the government-wide financial statements and proprietary fund types in the fund financial statements, long-term debt and other long-term obligations are reported as liabilities in the applicable governmental activities, business-type activities, or proprietary fund type statement of net assets. Bond premiums and discounts, as well as issuance costs, are deferred and amortized over the life of the bonds using the straight-line method, which approximates the effective interest method. Bonds payable are reported net of the applicable bond premium or discount. Bond issuance costs are reported as deferred charges and amortized over the term of the related debt.

(continued)

I. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Assets, Liabilities and Net Assets or Equity (Continued)

Long-term Obligations (Continued)

In the fund financial statements, governmental fund types recognize bond premiums and discounts, as well as issuance costs during the current period. The face amount of debt issued is reported as other financing sources. Premiums received on debt issuances are reported as other financing sources while discounts are reported as other financing uses. Issuance costs, even if withheld from the actual net proceeds received, are reported as expenditures.

Fund Equity

In the fund financial statements, governmental funds report reservations of fund balance for amounts that are not available for appropriation or are legally restricted by outside parties for use for a specific purpose. Designations of fund balance represent tentative management plans that are subject to change.

Net Assets

Net assets represent the difference between assets and liabilities. Net assets invested in capital assets, net of related debt consists of capital assets, net of accumulated depreciation, reduced by the outstanding balances of any borrowing used for the acquisition, construction or improvements of those assets, and adding back unspent proceeds. Net assets are reported as restricted when there are limitations imposed on their use either through the enabling legislations adopted by the City or through external restrictions imposed by creditors, grantors or laws or regulations of other governments.

Estimates

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 and disclosures of contingent liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual amounts could differ from those estimates

(continued)

II. DETAILED NOTES ON ALL FUNDS

Deposits and Investments

The **Public Funds Investment Act** (Government Code Chapter 2256) contains specific provisions in the areas of investment practices, management reports and establishment of appropriate policies. Among other things, it requires the City to adopt, implement, and publicize an investment policy. That policy must address the following areas: (1) safety of principal and liquidity, (2) portfolio diversification, (3) allowable investments, (4) acceptable risk levels, (5) expected rates of return, (6) maximum allowable stated maturity of portfolio investments, (7) maximum average dollar-weighted maturity allowed based on the stated maturity date for the portfolio, (8) investment staff quality and capabilities, and (9) bid solicitation preferences for certificates of deposit. Statutes authorize the City to invest in (1) obligations of the U. S. Treasury, certain U. S. Agencies, and the State of Texas; (2) certificates of deposit, (3) certain municipal securities, (4) money market savings accounts, (5) repurchase agreements, (6) bankers' acceptances, (7) Mutual Funds, (8) Investment pools, (9) guaranteed investment contracts, and (10) common trust funds. The Act also requires the City to have independent auditors perform test procedures related to investment practices as provided by the Act. The City is in substantial compliance with the requirements of the Act and with local policies.

In compliance with the **Public Funds Investment Act**, the City has adopted a deposit and investment policy. That policy does address the following risks:

- a. **Custodial Credit Risk** – Deposits: In the case of deposits, this is the risk that, in the event of a bank failure, the government's deposits may not be returned to it. As of September 30, 2010, the City's deposit balance (cash and certificates of deposit) was \$2,909,487. The City's deposits at September 30, 2010 were not entirely covered by FDIC insurance or by pledged collateral held by the City's agent bank in the City's name.
- b. **Credit Risk:** It is the City's policy to limit investments to investment types with an investment quality rating no lower than AAA or AAA-m or an equivalent rating by at least one nationally recognized rating service or no lower than investment grade by at least one nationally recognized rating service with a weighted average maturity no greater than 90 days. The City's investments were rated AAAM by Standard and Poor's Investors Services.
- c. **Interest Rate Risk:** In accordance with the City's investment policy, the City manages its exposure to declines in fair values by limiting the weighted average maturity of its investment portfolio to 90 days or less, dependent on market conditions.
- d. **Concentration of Credit Risk:** The government's investment policy states the maximum percentage allowed for each different investment instrument that can be used to make up the portfolio.

(continued)

II. DETAILED NOTES ON ALL FUNDS (Continued)

Deposits and Investments (Continued)

At September 30, 2010, the primary government's investments consisted of:

	<u>Fair Value</u>
TexStar	\$ 3,577,994
Texas Term	1,215,394
State Treasurer's Investment Pool (TexPool)	<u>596,747</u>
	<u>\$ 5,390,135</u>

At September 30, 2010 all of the above investments are not categorized by risk. TexStar, TexPool, Texas Term, and government agencies balances are not evidenced by securities that exist in physical or book entry form, and, accordingly, are not categorized by risk. However, the nature of these funds requires that they be used to purchase investments authorized by the Texas Public Funds Investment Act of 1995. The primary objective of these investment pools is to provide a safe environment for the placement of public funds in short-term, fully collateralized investments.

Receivables

Receivables as of year-end for the government's individual major funds and nonmajor funds in the aggregate, including the applicable allowances for uncollectible accounts, are as follows:

	<u>Governmental Funds</u>				<u>Enterprise Funds</u>			<u>Totals</u>
	<u>General</u>	<u>Debt Service</u>	<u>EDC</u>	<u>Nonmajor Funds</u>	<u>Water and Wastewater</u>	<u>Sanitation</u>	<u>Airport</u>	
Receivables:								
Accounts:								
Customers	\$ -	\$ -	\$ -	\$ -	\$ 532,878	\$ 48,101	\$ 24,798	\$ 605,777
Taxes:								
Property	246,890	137,244	-	-	-	-	-	384,134
Sales tax	384,781	-	34,980	-	-	-	-	419,761
Other	29,426	-	-	102,484	-	-	-	131,910
Intergovernmental	-	-	-	238,430	68,909	-	48,177	355,516
Other	<u>1,621,654</u>	<u>4,245</u>	<u>-</u>	<u>36,576</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>1,662,475</u>
Gross receivables	2,282,751	141,489	34,980	377,490	601,787	48,101	72,975	3,559,573
Less: allowance for uncollectibles	(1,564,120)	(102,933)	-	-	-	-	-	(1,667,053)
Net total receivables	<u>\$ 718,631</u>	<u>\$ 38,556</u>	<u>\$ 34,980</u>	<u>\$ 377,490</u>	<u>\$ 601,787</u>	<u>\$ 48,101</u>	<u>\$ 72,975</u>	<u>\$ 1,892,520</u>

Governmental funds report *deferred revenue* in connection with receivables for revenue that is not considered to be available to liquidate liabilities of the current period. Governmental funds also defer revenue recognition in connection with resources that have been received, but not yet earned. At the end of the current fiscal year, the various components of *deferred revenue* and *unearned revenue* reported in the governmental funds were as follows:

	<u>Unavailable</u>
Delinquent property taxes receivable (general fund)	\$ 46,225
Delinquent court fines receivable (general fund)	216,521
Delinquent property taxes receivable (debt service)	<u>25,995</u>
Total Governmental Funds	<u>\$ 288,741</u>

(continued)

II. DETAILED NOTES ON ALL FUNDS (Continued)

Capital Assets

Capital asset activity for the year ended September 30, 2010, was as follows:

	Beginning Balance	Increase	Decrease	Adjustment	Ending Balance
Governmental activities:					
Capital assets, not being depreciated:					
Land	\$ 764,632	\$ -	\$ -	\$ -	\$ 764,632
Construction in progress	1,684,299	852,849	2,245,061	-	292,087
Total assets not being depreciated	<u>2,448,931</u>	<u>852,849</u>	<u>2,245,061</u>	<u>-</u>	<u>1,056,719</u>
Capital assets, being depreciated:					
Buildings and improvements	5,489,579	191,642	-	-	5,681,221
Machinery and equipment	3,113,121	226,825	-	-	3,339,946
Infrastructure	6,190,002	2,053,419	-	-	8,243,421
Total capital assets being depreciated	<u>14,792,702</u>	<u>2,471,886</u>	<u>-</u>	<u>-</u>	<u>17,264,588</u>
Accumulated depreciation:					
Buildings and improvements	2,415,145	156,738	-	-	2,571,883
Machinery and equipment	1,707,703	322,177	-	-	2,029,880
Infrastructure	167,093	137,603	-	-	304,696
Total accumulated depreciation	<u>4,289,941</u>	<u>616,518</u>	<u>-</u>	<u>-</u>	<u>4,906,459</u>
Total capital assets being depreciated, net	<u>10,502,761</u>	<u>1,855,368</u>	<u>-</u>	<u>-</u>	<u>12,358,129</u>
Governmental activities capital assets, net	<u>\$ 12,951,692</u>	<u>\$ 2,708,217</u>	<u>\$ 2,245,061</u>	<u>\$ -</u>	<u>\$ 13,414,848</u>
Business-type activities:					
Capital assets, not being depreciated:					
Land	\$ 378,391	\$ -	\$ -	\$ -	\$ 378,391
Construction in progress - Water/Sewer	52,000	457,951	63,475	-	446,476
Construction in progress - Airport	164,631	454,407	-	-	619,038
Total assets not being depreciated	<u>595,022</u>	<u>912,358</u>	<u>63,475</u>	<u>-</u>	<u>1,443,905</u>
Capital assets, being depreciated:					
Buildings and improvements	5,216,061	17,940	-	-	5,234,001
Machinery and equipment	1,646,271	-	-	-	1,646,271
Infrastructure	14,112,005	63,474	-	-	14,175,479
Total capital assets being depreciated	<u>20,974,337</u>	<u>81,414</u>	<u>-</u>	<u>-</u>	<u>21,055,751</u>
Accumulated depreciation:					
Buildings and improvements	790,298	115,770	-	-	906,068
Machinery and equipment	1,134,717	87,753	-	-	1,222,470
Infrastructure	8,941,774	309,082	-	-	9,250,856
Total accumulated depreciation	<u>10,866,789</u>	<u>512,605</u>	<u>-</u>	<u>-</u>	<u>11,379,394</u>
Total capital assets being depreciated, net	<u>10,107,548</u>	<u>(431,191)</u>	<u>-</u>	<u>-</u>	<u>9,676,357</u>
Business-type activities capital assets, net	<u>\$ 10,702,570</u>	<u>\$ 481,167</u>	<u>\$ 63,475</u>	<u>\$ -</u>	<u>\$ 11,120,262</u>

(continued)

II. DETAILED NOTES ON ALL FUNDS (Continued)

Capital Assets (Continued)

Depreciation expense was charged to functions/programs of the government as follows:

Governmental activities		
General government		\$ 171,556
Public safety		198,564
Public works		74,462
Community development		<u>171,936</u>
Total depreciation expense - governmental activities		<u>\$ 616,518</u>
Business-type activities:		
Water and wastewater		\$ 477,586
Sanitation		2,241
Airport		<u>32,778</u>
Total depreciation expense - business-type activities		<u>\$ 512,605</u>

Interfund Receivables, Payables and Transfers

The composition of interfund balances as of September 30, 2010, is as follows:

<u>Receivable Fund</u>	<u>Payable Fund</u>	<u>Amount</u>
General	Nonmajor	\$ 163,171
Nonmajor	Nonmajor	<u>518</u>
Total		<u>\$ 163,689</u>

Balances resulted from the time lag between the dates that 1) interfund goods and services are provided on reimbursable expenditures occur, and 2) transactions are recorded in the accounting system, and 3) payments between funds are made.

Interfund transfers during the year ended September 30, 2010, are as follows:

<u>Transfers In</u>	<u>Transfers Out</u>	<u>Amount</u>
General	Nonmajor	\$ 190,000
General	EDC	104,546
General	Sanitation	320,000
General	Water and wastewater	2,260
Airport	General	20,000
Nonmajor	General	47,148
Nonmajor	Water and wastewater	<u>4,126</u>
Total		<u>\$ 688,080</u>

(continued)

II. DETAILED NOTES ON ALL FUNDS (Continued)

Long-term Debt

Long-term liability activity from the year ended September 30, 2010, was as follows:

	Debt Outstanding 09/30/09	Additions of New Debt	Retirements and Repayments	Adjustments	Debt Outstanding 09/30/10
<u>Governmental:</u>					
Notes payable	\$ 46,327	\$ -	\$ 46,327	\$ -	\$ -
Certificates of obligation	1,680,000	-	385,000	-	1,295,000
General obligation bonds	8,275,000	3,525,000	1,851,800	(928,200)	9,020,000
Premium	50,211	77,598	2,643	-	125,166
Capital Leases	222,013	-	87,865	-	134,148
Net OPEB obligation	-	85,237	-	68,507	153,744
Vacation payable	226,615	-	616	-	225,999
	<u>10,500,166</u>	<u>3,687,835</u>	<u>2,374,251</u>	<u>(859,693)</u>	<u>10,954,057</u>
<u>Enterprise Fund</u>					
Certificates of obligation	4,390,000	-	250,000	-	4,140,000
General obligation bonds	-	720,000	928,200	928,200	720,000
Premium	-	32,895	-	-	32,895
Capital Leases	107,097	-	35,414	-	71,683
Vacation payable	25,527	2,699	-	-	28,226
	<u>4,522,624</u>	<u>755,594</u>	<u>1,213,614</u>	<u>928,200</u>	<u>4,992,804</u>
Total	<u>\$ 15,022,790</u>	<u>\$ 4,443,429</u>	<u>\$ 3,587,865</u>	<u>\$ 68,507</u>	<u>\$ 15,946,861</u>

The General Fund is generally used to liquidate compensated absences for governmental activities.

L. B. Foster Agreement

During fiscal year 2002, the City entered into an agreement with the Texas Department of Housing and Community Affairs (TDHCA) and L. B. Foster to act as a pass-through agent for the purchase of a building. L. B. Foster will pay the City \$5,833 per month until March 2012, in order to purchase the building. Each month the City then pays this money to TDHCA. Under this agreement, the City is not liable for any debt should L. B. Foster default on the loan. Since the City does not own or use the building and has no liability in regards to the building, no asset or liability has been recorded on the general ledger. Also, no revenue or expense is shown for the debt payments received by the City due to its capacity as a pass-through agent.

(continued)

II. DETAILED NOTES ON ALL FUNDS (Continued)

Long-term Debt

Debt outstanding as of September 30, 2010, consisted of the following:

	Purpose of Issue	Amount Issued	Amount Outstanding	Interest Rate
<u>Governmental</u>				
Note payable	Fire truck	\$ 174,328	\$ -	5.19%
		<u>174,328</u>	<u>-</u>	
Certificates of obligation:				
2005 Series	Street Improvements	600,000	200,000	4.15%
2007 Series	City Hall renovations	315,000	270,000	4.53%
2002 Series	Street improvements and acquisition of equipment	1,725,000	825,000	4.00%-4.80%
		<u>2,640,000</u>	<u>1,295,000</u>	
General obligation bonds:				
1995 Series	Refunding	1,580,000	-	4.50%-5.40%
1998 Series	Refunding	2,943,250	-	4.20%-4.90%
2006 Series	Street Improvements	4,000,000	3,565,000	3.75%-5.125%
2008 Series	Various improvements	2,000,000	1,930,000	4.625%-7.00%
2008 Series Premium		52,854	47,568	
2010 Series	Street Improvements	2,000,000	2,000,000	2.00%-4.05%
2010 Series Premium		43,967	43,967	
2010 Series	Refunding	1,525,000	1,525,000	2.00%-4.05%
2010 Series Premium		33,631	33,631	
		<u>14,178,702</u>	<u>9,145,166</u>	
Total Governmental Long-term		<u>16,993,030</u>	<u>10,440,166</u>	
<u>Enterprise Fund</u>				
Certificates of obligation:				
2002 Series	Improvements to sewer plant	5,870,000	4,140,000	4.00%-4.80%
		<u>5,870,000</u>	<u>4,140,000</u>	
General obligation bonds:				
1998 Series	Refunding	1,881,750	-	4.20%-4.90%
2010 Series	Refunding	720,000	720,000	2.00%-4.25%
2010 Series Premium		32,895	32,895	
		<u>2,634,645</u>	<u>752,895</u>	
Total Enterprise Fund		<u>8,504,645</u>	<u>4,892,895</u>	

(continued)

II. DETAILED NOTES ON ALL FUNDS (Continued)

Long-term Debt (Continued)

Debt service requirements are as follows:

	<u>Year Ended September 30</u>	<u>Principal</u>	<u>Interest</u>	<u>Total Requirements</u>
Certificates of Obligation:				
	2011	65,000	56,943	121,943
	2012	75,000	54,201	129,201
	2013	75,000	51,100	126,100
	2014	80,000	47,899	127,899
	2015	85,000	44,504	129,504
	2016-2020	485,000	163,537	648,537
	2021-2025	430,000	42,031	472,031
	2026-2030	-	-	-
		<u>1,295,000</u>	<u>460,215</u>	<u>1,755,215</u>
General Obligation Bonds:				
	2011	650,000	334,373	984,373
	2012	655,000	335,760	990,760
	2013	560,000	313,754	873,754
	2014	500,000	293,284	793,284
	2015	520,000	275,684	795,684
	2016-2020	2,185,000	1,111,073	3,296,073
	2021-2025	2,515,000	642,341	3,157,341
	2026-2030	1,435,000	145,462	1,580,462
		<u>9,020,000</u>	<u>3,451,731</u>	<u>12,471,731</u>
Total Governmental Debt:				
	2011	715,000	391,316	1,106,316
	2012	730,000	389,961	1,119,961
	2013	635,000	364,854	999,854
	2014	580,000	341,183	921,183
	2015	605,000	320,188	925,188
	2016-2020	2,670,000	1,274,610	3,944,610
	2021-2025	2,945,000	684,372	3,629,372
	2026-2030	1,435,000	145,462	1,580,462
		<u>10,315,000</u>	<u>3,911,946</u>	<u>14,226,946</u>
	Total	<u>\$ 10,315,000</u>	<u>\$ 3,911,946</u>	<u>\$ 14,226,946</u>

(continued)

II. DETAILED NOTES ON ALL FUNDS (Continued)

Long-term Debt (Continued)

Enterprise Fund debt requirements are as follows:

	<u>Year Ended September 30</u>	<u>Principal</u>	<u>Interest</u>	<u>Total Requirements</u>
Certificates of Obligation:	2011	260,000	182,541	\$ 442,541
	2012	275,000	172,203	447,203
	2013	290,000	161,198	451,198
	2014	305,000	149,693	454,693
	2015	315,000	137,217	452,217
	2016-2020	1,835,000	465,318	2,300,318
	2021-2025	860,000	62,417	922,417
	2026-2030	-	-	-
		<u>4,140,000</u>	<u>1,330,587</u>	<u>5,470,587</u>
General Obligation Bonds:	2011	195,000	11,390	206,390
	2012	185,000	10,744	195,744
	2013	210,000	7,044	217,044
	2014	65,000	2,844	67,844
	2015	65,000	1,544	66,544
	2016-2020	-	-	-
	2021-2025	-	-	-
	2026-2030	-	-	-
		<u>720,000</u>	<u>33,566</u>	<u>753,566</u>
Total Enterprise Fund Debt:	2011	455,000	193,931	648,931
	2012	460,000	182,947	642,947
	2013	500,000	168,242	668,242
	2014	370,000	152,537	522,537
	2015	380,000	138,761	518,761
	2016-2020	1,835,000	465,318	2,300,318
	2021-2025	860,000	62,417	922,417
	2026-2030	-	-	-
Total	<u>\$ 4,860,000</u>	<u>\$ 1,364,153</u>	<u>\$ 6,224,153</u>	

(continued)

II. DETAILED NOTES ON ALL FUNDS (Continued)

Long-term Debt (Continued)

Advance Refunding

In 2010, the City issued \$4,245,000 of general obligation bonds, \$2,245,000 of which were to refund previous bond issuances, to provide resources to purchase U.S. Government State and Local Government Series securities that were placed in an irrevocable trust for the purpose of generating resources for all future debt service payments of \$2,205,000 of general obligation bonds. As a result, the refunded bonds are considered to be defeased and the liability has been removed from the governmental activities column of the statements of net assets. The reacquisition price exceeded the net carrying amount of the old debt by \$66,526. This amount is being presented with the new debt and amortized over the life of the new debt, which is shorter than the refunded debt. This advanced refunding was undertaken to reduce total debt service payments over the next 15 years by \$129,861 and resulted in an economic gain of \$118,821.

Capital Leases

The City has acquired certain capital assets for governmental and water and wastewater activities through the use of lease purchase agreements. These lease agreements qualify as capital leases for accounting purposes and, therefore, have been recorded at the present value of their future minimum lease payments as of the inception date.

The assets acquired through capital leases are as follows:

	<u>Asset</u>
Governmental activities	
Assets:	
Roller and Dump Truck Trailer	\$ 151,000
Police Vehicles	69,282
Asphalt Zipper	42,978
Paver	93,890
Total	<u>\$ 357,150</u>
Water and Wastewater activities	
Backhoe	\$ 60,500
Wheel Loader	113,700
Total	<u>\$ 174,200</u>

(continued)

II. DETAILED NOTES ON ALL FUNDS (Continued)

Capital Leases (Continued)

The future minimum lease obligations and the net present value of these minimum lease payments as of September 30, 2010, were as follows:

<u>Year Ending September 30,</u>	<u>Governmental Activities</u>	<u>Water and Wastewater Activities</u>
2011	\$ 37,300	\$ 25,160
2012	37,300	25,160
2013	37,300	25,160
2014	<u>37,300</u>	<u>-</u>
Total minimum lease payments	149,200	75,480
Less: amount representing interest	<u>15,052</u>	<u>3,797</u>
Present value of minimum lease payments	<u>\$ 134,148</u>	<u>\$ 71,683</u>

Fund Equity

Reservations of Fund Equity

Reservations of equity show amounts that are not for expenditures or are legally restricted for specific uses. Generally, the purpose for each is indicated by the account title on the face of the balance sheet. The General Fund reserve for restricted purposes includes police seizure funds and funds collected for municipal court security and technology that can only be used for these purposes.

Designated Fund Equity

Designations of equity are used to show the amounts within unreserved equity which are intended to be used for specific purposes, but are not legally restricted.

Aquilla Water Supply District

The City has entered into a contract with the Aquilla Water Supply District under which the City agrees to purchase water from the District. The terms of the agreement provide that the City will purchase a minimum amount of water each year, determined on a fiscal year ending September 30, at rates determined on an annual basis for each of the District's customers.

The Aquilla Water Supply District is not a joint venture operation. It is governed by its own Board of Directors and is not governed by the entities that are serviced by it. Charges for providing water services under contracts constitute revenue for "operating and maintenance" and "debt service" costs for the facilities utilized.

(continued)

II. DETAILED NOTES ON ALL FUNDS (Continued)

Aquilla Water Supply District (Continued)

The City paid \$1,474,942 for water purchased from the District during the fiscal year ending September 30, 2010.

Retirement Plan

Plan Description

The City provides pension benefits for all of its eligible employees through a non-traditional, joint contributory, hybrid defined benefit plan in the state-wide Texas Municipal Retirement System (TMRS), an agent multiple-employer public employee retirement system. The plan provisions that have been adopted by the city are within the options available in the governing state statutes of TMRS.

TMRS issues a publicly available comprehensive annual financial report that includes financial statements and required supplementary information (RSI) for TMRS; the report also provides detailed explanations of the contributions, benefits and actuarial methods and assumptions used by the System. This report may be obtained by writing to TMRS, P.O. Box 149153, Austin, Texas 78714-9153 or by calling 800-924-8677; in addition the report is available on TMRS' website at www.TMRS.com.

The plan provisions are adopted by the governing body of the City, within the options available in the state statutes governing TMRS. Plan provisions for the City were as follows:

	Plan Year 2009	Plan Year 2010
Employee deposit rate	5.0%	5.0%
Matching ration (city to employee)	2 to 1	2 to 1
Years required for vesting	5	5
Service retirement eligibility (expressed as age/years of service)	60/5,0/20	60/5,0/20
Updated Service Credit	100% Repeating, Transfers	100% Repeating, Transfers
Annuity Increase (to retirees)	70% of CPI Repeating	70% of CPI Repeating

Contributions

Under the state law governing TMRS, the contribution rate for each city is determined annually by the actuary, using the Projected Unit Credit actuarial cost method. This rate consists of the normal cost contribution rate and the prior service cost contribution rate, which is calculated to be a level percent of payroll from year to year. The normal cost contribution rate finances the portion of an active member's projected benefit allocated annually; the prior service contribution rate amortizes the unfunded (overfunded) actuarial liability (asset) over the applicable period for that city. Both the normal cost and prior service contribution rates include recognition of the projected impact of annually repeating benefits, such as Updated Service Credits and Annuity Increases.

(continued)

II. DETAILED NOTES ON ALL FUNDS (Continued)

Retirement Plan (Continued)

Contributions (Continued)

The City contributes to the TMRS Plan at an actuarially determined rate. Both the employees and the City make contributions monthly. Since the City needs to know its contribution rate in advance for budgetary purposes, there is a one-year delay between the actuarial valuation that serves as the basis for the rate and the calendar year when the rate goes into effect. The annual pension cost and net pension obligation/(asset) are as follows:

Actuarial Valuation Date	<u>09/30/10</u>
Annual required contribution (ARC)	\$ 474,108
Interest on Net Pension Obligation	-
Adjustment to the ARC	-
Annual Pension Cost (APC)	<u>474,108</u>
Contributions made	<u>(388,871)</u>
Increase (decrease) in net pension obligation	85,237
Net pension obligation/(Asset), beginning of year	<u>68,507</u>
Net pension obligation/(Asset), end of year	<u>\$ 153,744</u>

Accounting Year Ending	Annual Pension Cost (APC)	Actual Contribution Made	Percentage of APC Contributed	Net Pension Obligation
09/30/08	\$ 344,970	\$ 344,970	100%	\$ -
09/30/09	435,636	367,129	119%	68,507
09/30/10	474,108	388,871	122%	85,237

The required contribution rates for fiscal year 2010 were determined as part of the December 31, 2007 and 2008 actuarial valuations. Additional information as of the latest actuarial valuation, December 31, 2009, also follows:

Valuation Date	12/31/07	12/31/08	12/31/09
Actuarial Cost Method	Projected Unit Credit	Projected Unit Credit	Projected Unit Credit
Amortization Method	Level percent of payroll	Level percent of payroll	Level percent of payroll
GASB 25 Equivalent Single Amortization Period	30 years; closed period	29 years; closed period	28 years; closed period
Amortization Period for new Gains/Losses	30 years	30 years	30 years
Asset Valuation Method	Amortized Cost	Amortized Cost	10-year Smoothed Market
Actuarial Assumptions:			
Investment Rate of Return*	7.0%	7.5%	7.5%
Projected Salary Increases*	Varies by age and service	Varies by age and service	Varies by age and service
*Includes Inflation at Cost-of-Living Adjustments	3.00%	3.00%	3.00%
	2.1%	2.1%	2.1%

(continued)

II. DETAILED NOTES ON ALL FUNDS (Continued)

Retirement Plan (Continued)

Contributions (Continued)

The funded status as of December 31, 2009, the most recent actuarial valuation date, is as follows:

Actuarial Valuation Date	Actuarial Value of Assets	Actuarial Accrued Liability (AAL)	Funded Ratio	Unfunded AAL (UAAL)	Covered Payroll	UAAL as a Percentage of Covered Payroll
12/31/2009	6,151,982	9,796,293	62.8%	3,644,311	4,166,954	87.5%

The schedule of funding progress, presented as Required Supplementary Information following the notes to the financial statements, presents multi-year trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liability of benefits.

Contingencies

The City participates in certain federal and state assisted grant programs. These programs are subject to program compliance audits by the grantors or their representatives. Any liability for reimbursement which may arise as the result of these audits is not believed to be material.

Various claims and lawsuits are pending against the City. In the opinion of City management, after consultation with legal counsel, the potential loss on all claims and lawsuits will not materially affect the City's financial position.

Economic Development Fund

The Economic Development Corporation has been deemed a blended component unit for the City of Hillsboro (see note 1). The Corporation has borrowed money to help attract business to the Hillsboro area. Accounting principles prescribe the Corporation be a Special Revenue Fund.

City of Hillsboro Ordinance No. 02007-12-13 provides for an entity, other than the City, to construct water or sewer infrastructure, dedicate it to the City, and collect a pro rata cost share from intervening property owners for up to the full cost and/or up to 10 years from the date the completed project is dedicated to the City. Under terms of the Utility Developer Agreement approved by City Council in R2008-01-04, the Hillsboro Economic Development Corporation (HEDC) is the developer of the Highway 77 Utilities Project that constructed water and sewer lines and appurtenances to serve a proposed truck stop to be located on Highway 77 in the southeast quadrant of the Hwy 77/I-35 interchange. Any cost recouped from intervening property owners will be receipted into a City trust account dedicated to the project. It will then be dispersed first to the HEDC until its \$500,000 contribution has been met, and second to the City until its \$504,888 contribution has been met. The Project was dedicated during the current fiscal year.

(continued)

II. DETAILED NOTES ON ALL FUNDS (Continued)

Risk Management

The City is a member of the Texas Municipal League's Intergovernmental Risk Pool ("Pool"). The Pool was created for the purpose of providing coverage against risks which are inherent in operating a political subdivision. The City pays annual premiums to the Pool for liability, property and workers' compensation coverage. The City's agreement with the Pool provides that the Pool will be self-sustaining through member premiums and will provide through commercial companies reinsurance contracts. The Pool agrees to handle all liability, property and workers' compensation claims and provide any defense as is necessary. The Pool makes available to the City loss control services to assist the City in following a plan of loss control that may result in reduced losses. The City agrees that it will cooperate in instituting any and all reasonable loss control recommendations made by the Pool. The City also carries commercial insurance on all other risks of loss, including employee health and accident insurance.

The City has experienced no significant reductions in coverage through the Pool over the past year.

There have been no insurance settlements exceeding Pool coverage for any of the past three years.

Prior Period Adjustment

There were two prior period adjustments made to the City's financial statements during the current year. The first adjustment was to properly reflect the portion of the 1998 General Refunding bonds that was to be paid by revenues from the Water and Sewer Fund of \$928,200. This debt was refunded during the current year. The second adjustment of \$68,507 was to record the fiscal year 2009 Net OPEB obligation which was not recorded in the prior year.

CITY OF HILLSBORO, TEXAS

**STATEMENT OF REVENUES, EXPENDITURES AND
CHANGES IN FUND BALANCE - BUDGET AND ACTUAL**

GENERAL FUND

FOR THE YEAR ENDED SEPTEMBER 30, 2010

	Budget		Actual	Variance with
	Original	Final		Final Budget Positive (Negative)
REVENUES				
Taxes:				
Ad valorem	\$ 2,056,935	\$ 2,056,935	\$ 1,987,304	\$(69,631)
Sales, net of rebates	2,321,800	2,321,800	2,259,010	(62,790)
Franchise	550,000	550,000	494,961	(55,039)
Other	27,500	27,500	44,625	17,125
Services to others	5,000	5,000	4,548	(452)
Licenses and permits	79,500	79,500	78,310	(1,190)
Fines and forfeitures	760,100	760,100	971,834	211,734
Intergovernmental	57,600	57,600	24,772	(32,828)
Interest and penalties	60,000	60,000	46,038	(13,962)
Rentals	90,500	90,500	21,635	(68,865)
Charges for services	151,210	151,210	163,157	11,947
Cemetery lot sales and fees	30,000	30,000	26,805	(3,195)
Contributions	44,450	44,450	63,736	19,286
Other	19,700	19,700	78,017	58,317
Total revenues	<u>6,254,295</u>	<u>6,254,295</u>	<u>6,264,752</u>	<u>10,457</u>
EXPENDITURES				
Legislative:				
Personnel	100	100	355	(255)
Supplies	4,300	4,300	2,278	2,022
Services	29,500	29,500	9,065	20,435
	<u>33,900</u>	<u>33,900</u>	<u>11,698</u>	<u>22,202</u>
Administration:				
Personnel	232,347	232,347	232,648	(301)
Supplies	11,100	11,100	5,539	5,561
Services	136,440	136,440	141,646	(5,206)
Maintenance	6,269	6,269	8,283	(2,014)
Capital outlay	1,810	1,810	-	1,810
	<u>387,966</u>	<u>387,966</u>	<u>388,116</u>	<u>(150)</u>

(continued)

CITY OF HILLSBORO, TEXAS

**STATEMENT OF REVENUES, EXPENDITURES AND
CHANGES IN FUND BALANCE - BUDGET AND ACTUAL**

GENERAL FUND

(Continued)

FOR THE YEAR ENDED SEPTEMBER 30, 2010

	Budget		Actual	Variance with Final Budget Positive (Negative)
	Original	Final		
EXPENDITURES (Continued)				
Streets:				
Personnel	235,992	235,992	237,772	(1,780)
Supplies	55,850	55,850	37,472	18,378
Services	161,185	161,185	132,374	28,811
Maintenance	50,450	50,450	38,676	11,774
	503,477	503,477	446,294	57,183
Police:				
Personnel	1,734,728	1,734,728	1,855,881	(121,153)
Supplies	127,450	127,450	169,431	(41,981)
Services	153,700	153,700	138,506	15,194
Maintenance	55,000	55,000	55,046	(46)
Minor equipment	-	-	26,874	(26,874)
Capital outlay	42,000	42,000	54,413	(12,413)
	2,112,878	2,112,878	2,300,151	(187,273)
Library:				
Personnel	268,694	268,694	248,029	20,665
Supplies	11,400	11,400	9,183	2,217
Services	43,590	43,590	37,025	6,565
Maintenance	24,000	24,000	19,376	4,624
Capital outlay	41,000	41,000	34,600	6,400
Grant expense	6,600	6,600	8,940	(2,340)
	395,284	395,284	357,153	38,131
Fire:				
Personnel	1,205,212	1,205,212	1,129,044	76,168
Supplies	109,650	109,650	111,430	(1,780)
Services	105,600	105,600	90,047	15,553
Maintenance	20,700	20,700	16,958	3,742
Minor equipment	-	-	918	(918)
Capital outlay	-	-	15,000	(15,000)
	1,441,162	1,441,162	1,363,397	77,765

(continued)

CITY OF HILLSBORO, TEXAS

**STATEMENT OF REVENUES, EXPENDITURES AND
CHANGES IN FUND BALANCE - BUDGET AND ACTUAL**

GENERAL FUND

(Continued)

FOR THE YEAR ENDED SEPTEMBER 30, 2010

	Budget		Actual	Variance with
	Original	Final		Final Budget
				Positive (Negative)
EXPENDITURES (Continued)				
Municipal court:				
Personnel	142,227	142,227	143,099	(872)
Supplies	5,400	5,400	5,112	288
Services	71,450	71,450	39,242	32,208
Maintenance	<u>2,100</u>	<u>2,100</u>	<u>682</u>	<u>1,418</u>
	<u>221,177</u>	<u>221,177</u>	<u>188,135</u>	<u>33,042</u>
Parks and recreation:				
Personnel	293,181	293,181	276,223	16,958
Supplies	27,750	27,750	30,543	(2,793)
Services	38,000	38,000	36,241	1,759
Maintenance	<u>21,700</u>	<u>21,700</u>	<u>20,944</u>	<u>756</u>
	<u>380,631</u>	<u>380,631</u>	<u>363,951</u>	<u>16,680</u>
Maintenance shop:				
Personnel	88,392	88,392	88,426	(34)
Supplies	68,625	68,625	60,300	8,325
Services	9,707	9,707	4,833	4,874
Maintenance	<u>48,200</u>	<u>48,200</u>	<u>39,159</u>	<u>9,041</u>
	<u>214,924</u>	<u>214,924</u>	<u>192,718</u>	<u>22,206</u>
Cemetery:				
Personnel	15,715	15,715	14,836	879
Supplies	4,700	4,700	1,632	3,068
Services	94,260	94,260	69,600	24,660
Maintenance	<u>2,350</u>	<u>2,350</u>	<u>3,727</u>	<u>(1,377)</u>
	<u>117,025</u>	<u>117,025</u>	<u>89,795</u>	<u>27,230</u>

(continued)

CITY OF HILLSBORO, TEXAS

**STATEMENT OF REVENUES, EXPENDITURES AND
CHANGES IN FUND BALANCE - BUDGET AND ACTUAL**

GENERAL FUND

(Continued)

FOR THE YEAR ENDED SEPTEMBER 30, 2010

	Budget		Actual	Variance with Final Budget Positive (Negative)
	Original	Final		
EXPENDITURES (Continued)				
Community development:				
Personnel	142,483	142,483	128,732	13,751
Supplies	7,000	7,000	3,029	3,971
Services	139,935	139,935	120,230	19,705
Maintenance	12,200	12,200	8,295	3,905
	301,618	301,618	260,286	41,332
Legal:				
Personnel	31,725	31,725	31,676	49
Services	4,500	4,500	4,196	304
	36,225	36,225	35,872	353
Finance:				
Personnel	186,311	186,311	182,226	4,085
Supplies	4,350	4,350	4,546	(196)
Services	46,350	46,350	44,459	1,891
Maintenance	600	600	2,166	(1,566)
	237,611	237,611	233,397	4,214
Information systems:				
Personnel	41,901	41,901	46,207	(4,306)
Supplies	300	300	252	48
Services	9,310	9,310	8,886	424
Maintenance	9,300	9,300	4,342	4,958
	60,811	60,811	59,687	1,124
Marketing/Business development:				
Personnel	191,457	191,457	196,370	(4,913)
Supplies	6,900	6,900	4,027	2,873
Services	53,025	53,025	38,098	14,927
Maintenance	6,000	6,000	1,120	4,880
Minor equipment	-	-	73	(73)
Capital outlay	1,500	1,500	-	1,500
	258,882	258,882	239,688	19,194

(continued)

CITY OF HILLSBORO, TEXAS

**STATEMENT OF REVENUES, EXPENDITURES AND
CHANGES IN FUND BALANCE - BUDGET AND ACTUAL**

GENERAL FUND

(Continued)

FOR THE YEAR ENDED SEPTEMBER 30, 2010

	Budget		Actual	Variance with Final Budget Positive (Negative)
	Original	Final		
EXPENDITURES (Continued)				
Animal control:				
Personnel	50,194	50,194	49,665	529
Supplies	12,850	12,850	11,175	1,675
Services	3,200	3,200	1,360	1,840
Maintenance	4,700	4,700	993	3,707
Minor equipment	-	-	2,323	(2,323)
	<u>70,944</u>	<u>70,944</u>	<u>65,516</u>	<u>5,428</u>
Emergency Management:				
Personnel	-	-	58,774	(58,774)
Supplies	-	-	6,687	(6,687)
Services	-	-	5,486	(5,486)
	<u>-</u>	<u>-</u>	<u>70,947</u>	<u>(70,947)</u>
Debt service:				
Principal	121,139	121,139	134,192	(13,053)
Interest	4,388	4,388	11,183	(6,795)
	<u>125,527</u>	<u>125,527</u>	<u>145,375</u>	<u>(19,848)</u>
Total expenditures	<u>6,900,042</u>	<u>6,900,042</u>	<u>6,812,176</u>	<u>87,866</u>
EXCESS (DEFICIENCY) OF REVENUES OVER (UNDER) EXPENDITURES	<u>(645,747)</u>	<u>(645,747)</u>	<u>(547,424)</u>	<u>98,323</u>
OTHER FINANCING SOURCES (USES)				
Operating transfers in	670,177	670,177	616,806	(53,371)
Operating transfers (out)	(24,430)	(24,430)	(67,148)	(42,718)
Total other financing sources (uses)	<u>645,747</u>	<u>645,747</u>	<u>549,658</u>	<u>(96,089)</u>
CHANGE IN FUND BALANCES	-	-	2,234	2,234
FUND BALANCES, BEGINNING	<u>1,373,511</u>	<u>1,373,511</u>	<u>1,373,511</u>	<u>-</u>
FUND BALANCES, ENDING	<u>\$ 1,373,511</u>	<u>\$ 1,373,511</u>	<u>\$ 1,375,745</u>	<u>\$ 2,234</u>

CITY OF HILLSBORO, TEXAS

ECONOMIC DEVELOPMENT FUND

**STATEMENT OF REVENUES, EXPENDITURES AND
CHANGES IN FUND BALANCE - BUDGET AND ACTUAL**

FOR THE YEAR ENDED SEPTEMBER 30, 2010

	Budget		Actual	Variance with Final Budget Positive (Negative)
	Original	Final		
REVENUES				
Taxes:				
Sales, net of rebates	202,335	202,335	205,379	3,044
Intergovernmental	-	-	165,928	165,928
Interest and penalties	7,000	7,000	12,025	5,025
Other	6,000	6,000	12,257	6,257
Total revenues	<u>215,335</u>	<u>215,335</u>	<u>395,589</u>	<u>180,254</u>
EXPENDITURES				
Community development:				
Supplies	200	200	137	63
Services	118,420	118,420	24,806	93,614
Maintenance	5,000	5,000	5,563	(563)
Capital outlay	<u>1,368,317</u>	<u>1,368,317</u>	<u>322,857</u>	<u>1,045,460</u>
Total expenditures	<u>1,491,937</u>	<u>1,491,937</u>	<u>353,363</u>	<u>1,138,574</u>
EXCESS (DEFICIENCY) OF REVENUES OVER (UNDER) EXPENDITURES	(1,276,602)	(1,276,602)	42,226	1,318,828
OTHER FINANCING SOURCES (USES)				
Operating transfers in	1,381,148	1,381,148	-	(1,381,148)
Operating transfers (out)	(104,546)	(104,546)	(104,546)	-
Total other financing sources (uses)	<u>1,276,602</u>	<u>1,276,602</u>	<u>(104,546)</u>	<u>(1,381,148)</u>
CHANGE IN FUND BALANCES	-	-	(62,320)	(62,320)
FUND BALANCES, BEGINNING	<u>1,955,085</u>	<u>1,955,085</u>	<u>1,955,085</u>	<u>-</u>
FUND BALANCES, ENDING	<u>\$ 1,955,085</u>	<u>\$ 1,955,085</u>	<u>\$ 1,892,765</u>	<u>\$(62,320)</u>

CITY OF HILLSBORO, TEXAS

**TMRS Analysis of Funding Progress
For the Year Ended September 30, 2010
(Unaudited)**

Actuarial Valuation Date	Actuarial Value of Assets	Actuarial Accrued Liability (AAL)	Funded Ratio	Unfunded AAL (UAAL)	Covered Payroll	UAAL as a Percentage of Covered Payroll
12/31/2007	5,296,944	8,433,495	62.8%	3,136,551	3,663,235	85.6%
12/31/2008	5,867,799	9,158,178	64.1%	3,290,379	3,915,677	84.0%
12/31/2009	6,151,982	9,796,293	62.8%	3,644,311	4,166,954	87.5%

CITY OF HILLSBORO, TEXAS

NOTES TO REQUIRED SUPPLEMENTARY INFORMATION SEPTEMBER 30, 2010 (Unaudited)

BUDGETARY INFORMATION

The City follows these procedures annually in establishing the budgetary data reflected in the budgetary comparison schedules:

1. Budgets are adopted on a basis consistent with generally accepted accounting principles. Annual appropriated budgets are adopted for the General Fund, Special Revenue Funds, and the Debt Service Fund. Budgets are adopted for the proprietary funds annually only as a management tool. There are no legally mandated budgetary constraints for the proprietary funds.
2. In May of each year, budget preparation packages are distributed to all City agencies. The agencies of the City submit requests for appropriation to the City Manager before June 15 so that a budget may be prepared. The budget is prepared by department and includes information on the past year, current year estimates and requested appropriations for the next fiscal year. During August, the proposed budget is presented to the City Council for review. The City Council holds public hearings in September and may add to, subtract from, or change appropriations. Any changes in the budget must be within the revenue and reserves estimated as available by the City Manager or the revenue estimates must be changed by an affirmative vote of a majority of the City Council. The final budget must be adopted each year on or before September 27th as required by the City's charter.
3. The appropriated budget is prepared by fund, function and department. The City's management may make transfers of appropriations within a department. Transfers of appropriations between departments require the approval of the City Council. The legal level of budgetary control is the department level. The City Council made several supplementary budget appropriations that were not material during the year.
4. Encumbrances represent commitments related to unperformed contracts for goods and services. Encumbrances are recorded when purchase orders are issued, but are not considered expenditures until liabilities for payments are incurred. Encumbrances are reported as a reservation of fund balance on the balance sheet. Encumbrances do not lapse at the close of the fiscal year, but are carried forward as reserved fund balance until liquidated.
5. Expenditures exceeded appropriations in the General Fund in various departments. These excess expenditures were funded by available fund balance.

CITY OF HILLSBORO, TEXAS
COMBINING BALANCE SHEET
NONMAJOR GOVERNMENTAL FUNDS

SEPTEMBER 30, 2010

	Special Revenue Funds			
	Hotel/Motel Tax	Library Grants	Search and Rescue Equipment Grant	Main Street
ASSETS				
Cash and investments	\$ 76,685	\$ 166	\$ -	\$ 4,833
Intergovernmental receivable	-	-	30,518	-
Accounts receivable	36,576	-	-	-
Taxes receivable	102,484	-	-	-
Due from other funds	-	-	-	-
Total assets	<u>\$ 215,745</u>	<u>\$ 166</u>	<u>\$ 30,518</u>	<u>\$ 4,833</u>
LIABILITIES AND FUND EQUITY				
Liabilities				
Accounts payable	\$ 4,388	\$ 166	\$ 30,518	\$ -
Due to other funds	-	-	-	-
Total liabilities	<u>4,388</u>	<u>166</u>	<u>30,518</u>	<u>-</u>
Fund equity				
Fund balance				
Unreserved				
Designated for specific purposes	211,357	-	-	-
Undesignated	-	-	-	4,833
Total fund equity	<u>211,357</u>	<u>-</u>	<u>-</u>	<u>4,833</u>
Total liabilities and fund equity	<u>\$ 215,745</u>	<u>\$ 166</u>	<u>\$ 30,518</u>	<u>\$ 4,833</u>

Special Revenue Funds

Downtown Streetscape Phase II	Industrial Development	Home Grant	Home Buyers Assistance Grant	Parks and Wildlife Grant	Parks EDI Grant	Energy Grant	Downtown Streetscape
\$ -	\$ 308	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
88,641	-	-	20,000	27,164	24,401	26,780	-
-	-	-	-	-	-	-	-
-	-	-	-	-	-	-	-
-	-	-	-	518	-	-	-
<u>\$ 88,641</u>	<u>\$ 308</u>	<u>\$ -</u>	<u>\$ 20,000</u>	<u>\$ 27,682</u>	<u>\$ 24,401</u>	<u>\$ 26,780</u>	<u>\$ -</u>
\$ 9,275	\$ 25	\$ -	\$ 1,500	\$ 1,036	\$ -	\$ 26,780	\$ -
79,366	-	-	18,500	26,646	24,401	-	-
<u>88,641</u>	<u>25</u>	<u>-</u>	<u>20,000</u>	<u>27,682</u>	<u>24,401</u>	<u>26,780</u>	<u>-</u>
-	283	-	-	-	-	-	-
-	-	-	-	-	-	-	-
-	<u>283</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
<u>\$ 88,641</u>	<u>\$ 308</u>	<u>\$ -</u>	<u>\$ 20,000</u>	<u>\$ 27,682</u>	<u>\$ 24,401</u>	<u>\$ 26,780</u>	<u>\$ -</u>

CITY OF HILLSBORO, TEXAS
COMBINING BALANCE SHEET
NONMAJOR GOVERNMENTAL FUNDS
(continued)
SEPTEMBER 30, 2010

	<u>Special Revenue</u>	<u>Capital Projects</u>		<u>Total Nonmajor Governmental Funds</u>
	<u>East Franklin Streetscape</u>	<u>Entry Monument Project</u>	<u>Capital Construction</u>	
ASSETS				
Cash and investments	\$ -	\$ -	\$ 27,659	\$ 109,651
Intergovernmental receivable	20,926	-	-	238,430
Intergovernmental receivable	-	-	-	36,576
Taxes receivable	-	-	-	102,484
Due from other funds	-	-	-	518
	<u>-</u>	<u>-</u>	<u>-</u>	<u>518</u>
Total assets	<u>\$ 20,926</u>	<u>\$ -</u>	<u>\$ 27,659</u>	<u>\$ 487,659</u>
LIABILITIES AND FUND EQUITY				
Liabilities				
Accounts payable	\$ 6,150	\$ -	\$ -	\$ 79,838
Due to other funds	14,776	-	-	163,689
	<u>20,926</u>	<u>-</u>	<u>-</u>	<u>243,527</u>
Fund equity				
Fund balance				
Unreserved				
Designated for specific purposes	-	-	27,659	239,299
Undesignated	-	-	-	4,833
	<u>-</u>	<u>-</u>	<u>27,659</u>	<u>244,132</u>
Total fund equity	<u>-</u>	<u>-</u>	<u>27,659</u>	<u>244,132</u>
Total liabilities and fund equity	<u>\$ 20,926</u>	<u>\$ -</u>	<u>\$ 27,659</u>	<u>\$ 487,659</u>

CITY OF HILLSBORO, TEXAS

**COMBINING STATEMENT OF REVENUES, EXPENDITURES
AND CHANGES IN FUND BALANCES**

FOR THE YEAR ENDED SEPTEMBER 30, 2010

	Special Revenue Funds			
	Hotel/Motel Tax	Library Grants	Search and Rescue Equipment Grant	Main Street
REVENUES				
Taxes	\$ 306,155	\$ -	\$ -	\$ -
Intergovernmental	-	14,325	177,806	-
Interest	331	-	-	-
Rentals	12,650	-	-	-
Contributions	-	-	-	-
Other	162	-	-	-
Total revenues	319,298	14,325	177,806	-
EXPENDITURES				
Current:				
Personnel	-	-	-	-
Services	173,986	-	33,661	350
Supplies	8,810	-	-	1,555
Maintenance	2,510	-	-	-
Minor equipment	-	14,325	117,085	-
Capital outlay	22,545	-	27,060	-
Debt service:				
Principal	15,000	-	-	-
Interest	12,907	-	-	-
Total expenditures	235,758	14,325	177,806	1,905
EXCESS (DEFICIENCY) OF REVENUES OVER (UNDER) EXPENDITURES	83,540	-	-	(1,905)
OTHER FINANCING SOURCES(USES)				
Operating transfers in	-	-	-	-
Operating transfers out	(190,000)	-	-	-
NET CHANGE IN FUND BALANCES	(106,460)	-	-	(1,905)
FUND BALANCES, BEGINNING	317,817	-	-	6,738
FUND BALANCES, ENDING	\$ 211,357	\$ -	\$ -	\$ 4,833

Special Revenue Funds

Downtown Streetscape Phase II	Industrial Development	Home Grant	Home Buyers Assistance Grant	Parks and Wildlife Grant	Parks EDI Grant	Energy Grant	Downtown Streetscape
\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
84,001	-	303,446	20,000	24,401	24,401	26,780	-
-	-	-	-	-	-	-	-
-	-	-	-	-	-	-	-
-	-	-	-	-	-	-	-
<u>84,001</u>	<u>-</u>	<u>303,446</u>	<u>20,000</u>	<u>24,401</u>	<u>24,401</u>	<u>26,780</u>	<u>-</u>
-	-	-	20,000	-	-	-	-
-	25	327,359	-	-	-	26,780	-
-	-	-	-	-	-	-	-
-	-	-	-	-	-	-	-
84,001	-	-	-	24,401	24,401	-	23,235
-	-	-	-	-	-	-	-
-	-	-	-	-	-	-	-
<u>84,001</u>	<u>25</u>	<u>327,359</u>	<u>20,000</u>	<u>24,401</u>	<u>24,401</u>	<u>26,780</u>	<u>23,235</u>
-	(25)	(23,913)	-	-	-	-	(23,235)
-	-	23,913	-	-	-	-	23,235
-	-	-	-	-	-	-	-
-	(25)	-	-	-	-	-	-
-	308	-	-	-	-	-	-
<u>\$ -</u>	<u>\$ 283</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>

CITY OF HILLSBORO, TEXAS

**COMBINING STATEMENT OF REVENUES, EXPENDITURES
AND CHANGES IN FUND BALANCES
(continued)**

FOR THE YEAR ENDED SEPTEMBER 30, 2010

	<u>Special Revenue</u>	<u>Capital Projects</u>		Total Nonmajor Governmental Funds
	East Franklin Streetscape	Entry Monument Project	Capital Construction	
REVENUES				
Taxes	\$ -	\$ -	\$ -	\$ 306,155
Intergovernmental	-	-	-	675,160
Interest	-	-	53	384
Rentals	-	-	-	12,650
Contributions	20,926	-	-	20,926
Other	-	-	-	162
Total revenues	<u>20,926</u>	<u>-</u>	<u>53</u>	<u>1,015,437</u>
EXPENDITURES				
Current:				
Personnel	-	-	-	20,000
Services	-	-	-	562,161
Supplies	-	-	-	10,365
Maintenance	-	-	-	2,510
Minor equipment	-	-	-	131,410
Capital outlay	20,926	24,676	-	251,245
Debt service:				
Principal	-	-	-	15,000
Interest	-	-	-	12,907
Total expenditures	<u>20,926</u>	<u>24,676</u>	<u>-</u>	<u>1,005,598</u>
EXCESS (DEFICIENCY) OF REVENUES OVER (UNDER) EXPENDITURES	<u>-</u>	<u>(24,676)</u>	<u>53</u>	<u>9,839</u>
OTHER FINANCING SOURCES(USES)				
Operating transfers in	-	4,126	-	51,274
Operating transfers out	-	-	-	(190,000)
NET CHANGE IN FUND BALANCES	<u>-</u>	<u>(20,550)</u>	<u>53</u>	<u>(128,887)</u>
FUND BALANCES, BEGINNING	<u>-</u>	<u>20,550</u>	<u>27,606</u>	<u>373,019</u>
FUND BALANCES, ENDING	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 27,659</u>	<u>\$ 244,132</u>



PATTILLO, BROWN & HILL, L.L.P.
CERTIFIED PUBLIC ACCOUNTANTS ■ BUSINESS CONSULTANTS

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

The Honorable Mayor and City Council
City of Hillsboro, Texas

We have audited the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of Hillsboro, Texas as of and for the year ended September 30, 2010, which collectively comprise the City of Hillsboro, Texas basic financial statements and have issued our report thereon dated May 2, 2011. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

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

A control deficiency 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 misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the City of Hillsboro, Texas ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the City's financial statements that is more than inconsequential will not be prevented or detected by the City's internal control.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the City of Hillsboro, Texas internal control.

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 above.

Compliance and Other Matters

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

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

Pattillo, Brown & Hill, L.L.P.

May 2, 2011

FEDERAL AWARDS SECTION



PATTILLO, BROWN & HILL, L.L.P.
CERTIFIED PUBLIC ACCOUNTANTS ■ BUSINESS CONSULTANTS

**REPORT ON COMPLIANCE WITH REQUIREMENTS
APPLICABLE TO EACH MAJOR PROGRAM AND ON INTERNAL CONTROL
OVER COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133 AND
THE STATE OF TEXAS UNIFORM GRANT MANAGEMENT STANDARDS**

To the Honorable Mayor
And City Council
City of Hillsboro, Texas

Compliance

We have audited the compliance of City of Hillsboro, Texas, (the “City”) with the types of compliance requirements described in the *U. S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement* that are applicable to each of its major federal programs for the year ended September 30, 2010. The City’s major federal programs are identified in the summary of auditors’ results section of the accompanying Schedule of Findings and Questioned Costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to each of its major federal programs is the responsibility of the City’s management. Our responsibility is to express an opinion on the City’s compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; Office of Management and Budget (OMB) Circular A-133, *Audits of States, Local Governments and Nonprofit Organizations*. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above could have a direct and material effect on a major federal program occurred. An audit includes examining on a test basis, evidence about the City’s compliance with those requirements and performing such other procedures, as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on the City’s compliance with those requirements.

In our opinion, the City complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended September 30, 2010.

Internal Control Over Compliance

The management of City of Hillsboro is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts and grants applicable to federal programs. In planning and performing our audit, we considered the City's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the City's internal control over compliance.

A *control deficiency* in an entity's internal control over compliance 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 noncompliance with a type of compliance requirement of a federal program on a timely basis. A *significant deficiency* is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to administer a federal program such that there is more than a remote likelihood that noncompliance with a type of compliance requirement of a federal program that is more than inconsequential will not be prevented or detected by the entity's internal control.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that material noncompliance with a type of compliance requirement of a federal program will not be prevented or detected by the entity's internal control.

Our consideration of internal control over compliance 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 compliance that we consider to be material weaknesses, as defined above.

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

Pattillo, Brown & Hill, L.L.P.

May 2, 2011

CITY OF HILLSBORO, TEXAS
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
YEAR ENDED SEPTEMBER 30, 2010

Federal Grantor/Pass-through Grantor/ Program Title	Federal CFDA Number	Pass-through Grantor's Number	Expenditures
<u>U. S. Department of Housing and Urban Development</u>			
Direct Programs:			
Community Development Block Grant	14.246	B-06-SP-TX-1006	\$ 165,928
Community Development Block Grant	14.246	B-08-SP-TX-0531	84,001
Community Development Block Grant	14.246	B-09-SP-TX-0126	20,926
Home Investment Partnerships Program	14.239	M-08-SG-48-0100	303,446
Home Buyers Assistance Grant	14.239	M-08-SG-48-0100	20,000
Economic Development Initiative-Special Project, Neighborhood Initiative and Miscellaneous Grants	14.251	B-10-SP-TX-0102	24,401
Total U. S. Department of Housing and Urban Development			<u>618,702</u>
<u>U. S. Department of Energy</u>			
Passed through the Office of the Texas State Comptroller			
Energy Efficiency and Conservation Block Grant Program	81.128	DE-EE0000893	26,780
Total U. S. Department of Energy			<u>26,780</u>
<u>U. S. Department of Transportation</u>			
Passed through the Texas Department of Transportation :			
Airport Improvement Program	20.106	08HGHILLS	274,653
Airport Improvement Program	20.106	0809HGHILLS	25,627
Airport Improvement Program	20.106	0909HGHILLS	210,442
Total Passed through the Texas Department of Transportation			<u>510,722</u>
Total U.S. Department of Transportation			<u>510,722</u>
<u>Environmental Protection Agency</u>			
Direct Program:			
Surveys, Studies, Investigations and Special Purpose Grants	66.606	XP-96606601-0	250,760
Total Environmental Protection Agency			<u>250,760</u>
<u>U. S. Department of Homeland Security</u>			
Passed through the Texas Office of the Governor -			
Division of Emergency Management:			
State Homeland Security Program	97.073	2007 SHSP	18,626
State Homeland Security Program	97.073	2008 SHSP	59,893
State Homeland Security Program	97.073	2009 SHSP	99,287
Total Passed through the Texas Office of the Governor - Division of Emergency Management			<u>177,806</u>
Total U. S. Department of Homeland Security			<u>177,806</u>
Total Federal Awards			<u>\$ 1,584,770</u>

CITY OF HILLSBORO, TEXAS

NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

SEPTEMBER 30, 2010

1. GENERAL

The Schedule of Expenditures of Federal Awards presents the activity of all applicable federal awards programs of City of Hillsboro, Texas. The City's reporting entity is defined in Note I of the basic financial statements. Federal awards received directly from federal agencies, as well as federal awards passed through other government agencies, are included on the Schedule of Expenditures of Federal Awards.

2. BASIS OF ACCOUNTING

The Schedule of Expenditures of Federal Awards is presented using the modified accrual basis of accounting. The modified accrual basis of accounting is described in Note I of the basic financial statements.

The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local governments, and Nonprofit Organizations*. Therefore, some of the amounts presented in this schedule may differ from amounts presented in, or used in the preparation of, the financial statements.

CITY OF HILLSBORO, TEXAS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED SEPTEMBER 30, 2010

Summary of Auditors' Results

Type of report on financial statements	Unqualified
Internal control over financial reporting: Material weakness(es) identified?	No
Significant deficiencies identified that are not considered to be material weakness(es)?	None reported
Internal control over major programs: Material weakness(es) identified?	No
Significant deficiencies identified that are not considered to be material weakness(es)?	None reported
Noncompliance which is material to the basic financial statements	None
Type of report on compliance with major programs	Unqualified
Findings and questioned costs for federal and state awards as defined in Section 501(a), OMB Circular A-133 and the State of Texas Uniform Grant Management Standards	None
Dollar threshold considered between Type A and Type B federal and state programs	\$300,000
Low risk auditee statement	The City was not classified as a low-risk auditee in the context of OMB Circular A-133.
Major federal programs	Home Investment Partnership Program, CFDA #14.239 Home Buyers Assistance Grant, CFDA #14.239 Airport Improvement Program, CFDA #20.106

**Findings Relating to the Financial Statements Which are
Required to be Reported in Accordance With Generally
Accepted Auditing Standards**

None

Findings and Questioned Costs for Federal Awards

None

CITY OF HILLSBORO, TEXAS
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
FOR THE YEAR ENDED SEPTEMBER 30, 2010

None