



Hillsboro TEXAS

CITY OF HILLSBORO
ANNUAL FINANCIAL REPORT

FOR THE YEAR ENDED
SEPTEMBER 30, 2012



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

CITY OF HILLSBORO, TEXAS

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INDEPENDENT AUDITOR'S REPORT

To the Honorable Mayor and
Members of the 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 (the "City"), as of and for the year ended September 30, 2012, 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 the 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, 2012, 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 also issued our report dated March 27, 2013, on our consideration of the City of Hillsboro, Texas' internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, grants and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with Government Auditing Standards and should be considered in assessing the results of our audit.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis, the analysis of funding progress and budgetary comparison information on pages 3 through 9 and 44 through 49 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' financial statements as a whole. The combining and individual nonmajor fund financials 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.

Pattillo, Brown + Hill, L.L.P.

March 27, 2013

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, 2012. 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, 2012, by \$22,232,420 (net assets). Of this amount, \$3,243,431 (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 \$2,487,286.
- As of the close of the current fiscal year, the City's governmental funds reported combined ending fund balances of \$7,625,808. Approximately 11.96% of this total amount, \$911,837, is unassigned fund balance available for use within the City's fund designation and fiscal policies.
- As of September 30, 2012, unassigned fund balance for the general fund was \$911,837 or 13.62 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, CDBG Grant, Parks EDI Grant, 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 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 17 – 20 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 21 – 43 of this report.

Other Information. In addition to the basic financial statements and accompanying notes, this report also presents combining fund statements that further support the information in the financial statements. The combining fund statements for nonmajor funds are presented immediately following the notes to required supplementary information beginning on page 52 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 \$22,232,420 as of September 30, 2012.

CITY OF HILLSBORO'S NET ASSETS

	Governmental Activities		Business-type Activities		Totals	
	2012	2011	2012	2011	2012	2011
Current assets	\$ 8,982,253	\$ 8,598,360	\$ 2,870,677	\$ 2,669,607	\$ 11,852,930	\$ 11,267,967
Capital assets	17,427,613	14,221,422	10,240,659	10,737,219	27,668,272	24,958,641
Total Assets	26,409,866	22,819,782	13,111,336	13,406,826	39,521,202	36,226,608
Liabilities	782,975	780,598	434,773	445,133	1,217,748	1,225,731
Noncurrent liabilities	11,913,341	10,734,420	4,157,693	4,510,596	16,071,034	15,245,016
Total Liabilities	12,696,316	11,515,018	4,592,466	4,955,729	17,288,782	16,470,747
Net assets:						
Invested in capital assets, net of related debt	6,211,165	4,877,676	6,116,678	6,257,312	12,327,843	11,134,988
Restricted	6,661,146	5,596,079	-	-	6,661,146	5,596,079
Unrestricted	841,239	831,009	2,402,192	2,193,785	3,243,431	3,024,794
Total Net Assets	\$ 13,713,550	\$ 11,304,764	\$ 8,518,870	\$ 8,451,097	\$ 22,232,420	\$ 19,755,861

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 \$3,243,431 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	
	2012	2011	2012	2011	2012	2011
REVENUES:						
Program revenues:						
Charges for services	\$ 1,477,999	\$ 1,936,572	\$ 5,404,605	\$ 5,536,844	\$ 6,882,604	\$ 7,473,416
Operating grants	106,148	239,346	3,600	266,935	109,748	506,281
Capital grants and contributions	1,492,656	170,788	-	-	1,492,656	170,788
General revenues:						
Property taxes	2,998,682	3,004,134	-	-	2,998,682	3,004,134
Sales taxes	2,592,259	2,581,795	-	-	2,592,259	2,581,795
Franchise taxes	503,178	528,480	-	-	503,178	528,480
Hotel/motel taxes	320,022	281,211	-	-	320,022	281,211
Other taxes	43,711	40,231	-	-	43,711	40,231
Investment earnings	94,109	97,368	2,073	1,853	96,182	99,221
Miscellaneous	133,926	184,134	103,751	84,493	237,677	268,627
Total Revenues	<u>9,762,690</u>	<u>9,064,059</u>	<u>5,514,029</u>	<u>5,890,125</u>	<u>15,276,719</u>	<u>14,954,184</u>
EXPENSES:						
General government	2,170,068	1,925,592	-	-	2,170,068	1,925,592
Public safety	4,249,685	4,199,834	-	-	4,249,685	4,199,834
Streets	700,527	928,316	-	-	700,527	928,316
Community development	557,139	767,870	-	-	557,139	767,870
Interest on long-term debt	431,558	422,096	-	-	431,558	422,096
Water and sewer	-	-	3,457,654	3,747,075	3,457,654	3,747,075
Sanitation	-	-	814,478	863,115	814,478	863,115
Airport	-	-	408,324	279,285	408,324	279,285
Total Expenses	<u>8,108,977</u>	<u>8,243,708</u>	<u>4,680,456</u>	<u>4,889,475</u>	<u>12,789,433</u>	<u>13,133,183</u>
INCREASES IN NET ASSETS						
BEFORE TRANSFERS	1,653,713	820,351	833,573	1,000,650	2,487,286	1,821,001
TRANSFERS	<u>765,800</u>	<u>592,615</u>	<u>(765,800)</u>	<u>(592,615)</u>	<u>-</u>	<u>-</u>
CHANGE IN NET ASSETS	2,419,513	1,412,966	67,773	408,035	2,487,286	1,821,001
NET ASSETS, BEGINNING	<u>11,304,764</u>	<u>9,891,798</u>	<u>8,451,097</u>	<u>8,043,062</u>	<u>19,755,861</u>	<u>17,934,860</u>
PRIOR PERIOD ADJUSTMENT	<u>(10,727)</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>(10,727)</u>	<u>-</u>
NET ASSETS, ENDING	<u>\$ 13,713,550</u>	<u>\$ 11,304,764</u>	<u>\$ 8,518,870</u>	<u>\$ 8,451,097</u>	<u>\$ 22,232,420</u>	<u>\$ 19,755,861</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 governmental and business-type activities and the government as a whole.

The government's net assets increased by \$2,487,286 during the current fiscal year. This increase in net assets is mainly due to the \$1,321,868 increase in capital grants and contributions offset by a \$590,812 decrease in charges for services. Additionally, there was a \$343,750 decrease in total expenses.

Governmental Activities. Governmental activities increased the City's net assets by \$2,419,513, thereby accounting for 97.28 percent of the total growth in the net assets of the City. Key elements of this increase are as follows:

- Capital grants and contributions revenue increased by \$1,321,868
- Street expenses decreased by 227,789
- Community development expenses decreased by 210,731

Business-type Activities. Business-type activities increased the City's net assets by \$67,773, accounting for 2.72 percent of the total growth in the net assets of the City. Key elements of this increase are as follows:

- Miscellaneous revenue increased by \$19,258.
- Water and sewer expenses decreased by \$289,421

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, unassigned 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 \$7,625,808. Approximately 11.96% of this total amount, \$911,837 constitutes unassigned fund balance. Refer to pages 12 – 13 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, unassigned fund balance of the General Fund was \$911,837, while total fund balance reached \$1,147,692.

The fund balance of the City's General Fund increased by \$1,193 during the current fiscal year. Key factors in this slight increase are the increases in sales tax, licenses and permits and charges for services revenues as well as a decrease in capital outlay expenditures offset by a decrease in intergovernmental revenue.

The Capital Projects Fund had an ending fund balance of \$2,854,897. 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 \$2,402,192. The increase in net assets was \$67,773. 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 2012.

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, 2012, amounts to \$27,668,272 (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:

- Completion of various street projects in the amount of \$3,193,330
- Acquired equipment for approximately \$254,303
- Transfer of capital assets between departments of \$106,454

Additional information on the City's capital assets can be found on pages 32 and 33 of this report.

DEBT ADMINISTRATION

At the end of the current fiscal year, the City had total bonded debt of \$15,066,880. 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 35 – 39 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 2013 fiscal year. The property tax rate for the fiscal year 2013 remained at .818331 per \$100 assessed value. A slight decrease in sales tax revenue (1%) and decreases in various franchise revenues were considered. Also, a one- time 2% of salary payment in lieu of raises for employees for the year and a 12% increase in health care costs.

During the current fiscal year, unassigned fund balance in the General Fund was \$911,837. 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.

**BASIC
FINANCIAL STATEMENTS**

CITY OF HILLSBORO, TEXAS

STATEMENT OF NET ASSETS

SEPTEMBER 30, 2012

	Primary Government		
	Governmental Activities	Business-type Activities	Total
ASSETS			
Cash and investments	\$ 6,800,524	\$ 1,726,377	\$ 8,526,901
Receivables (net of allowances for uncollectibles):			
Taxes	683,670	-	683,670
Accounts	95,952	646,177	742,129
Intergovernmental	961,711	-	961,711
Other	273,662	-	273,662
Internal balances	(167,823)	167,823	-
Inventories	52,825	170,223	223,048
Deferred charges	281,732	160,077	441,809
Capital assets:			
Land	803,426	378,391	1,181,817
Buildings and improvements	6,819,458	5,865,462	12,684,920
Machinery and equipment	4,239,374	1,680,437	5,919,811
Infrastructure/water and wastewater distribution	10,969,372	14,410,108	25,379,480
Construction in progress	753,638	5,667	759,305
Less: accumulated depreciation	(6,157,655)	(12,099,406)	(18,257,061)
Total capital assets	<u>17,427,613</u>	<u>10,240,659</u>	<u>27,668,272</u>
Total assets	<u>26,409,866</u>	<u>13,111,336</u>	<u>39,521,202</u>
LIABILITIES			
Accounts payable	535,979	169,307	705,286
Accrued liabilities	139,286	20,696	159,982
Accrued interest payable	107,710	19,167	126,877
Customer deposits	-	225,603	225,603
Noncurrent liabilities:			
Due within one year	762,209	564,705	1,326,914
Due in more than one year	11,151,132	3,592,988	14,744,120
Total liabilities	<u>12,696,316</u>	<u>4,592,466</u>	<u>17,288,782</u>
NET ASSETS			
Invested in capital assets, net of related debt	6,211,165	6,116,678	12,327,843
Restricted for specific purposes	6,661,146	-	6,661,146
Unrestricted	841,239	2,402,192	3,243,431
Total net assets	\$ <u>13,713,550</u>	\$ <u>8,518,870</u>	\$ <u>22,232,420</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, 2012

Functions/Programs	Expenses	Program Revenues			Net (Expense) Revenue and Changes in Net Assets		
		Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	Governmental Activities	Business-type Activities	Total
Primary Government:							
Governmental activities:							
General government	\$ 2,170,068	\$ 38,906	\$ 15,545	\$ 764,750	\$(1,350,867)	\$ -	\$(1,350,867)
Public safety	4,249,685	1,279,348	90,203	72,923	(2,807,211)	-	(2,807,211)
Streets	700,527	80,000	-	-	(620,527)	-	(620,527)
Community development	557,139	79,745	400	654,983	177,989	-	177,989
Interest on long-term debt	431,558	-	-	-	(431,558)	-	(431,558)
Total governmental activities	8,108,977	1,477,999	106,148	1,492,656	(5,032,174)	-	(5,032,174)
Business-type activities:							
Water and sewer	3,457,654	3,969,143	3,600	-	-	515,089	515,089
Sanitation	814,478	1,070,216	-	-	-	255,738	255,738
Airport	408,324	365,246	-	-	-	(43,078)	(43,078)
Total business-type activities	4,680,456	5,404,605	3,600	-	-	727,749	727,749
Total	\$ 12,789,433	\$ 6,882,604	\$ 109,748	\$ 1,492,656	\$(5,032,174)	\$ 727,749	\$(4,304,425)
General revenues:							
Taxes:							
Property - general purposes					1,920,855		1,920,855
Property - debt service					1,077,827		1,077,827
Sales					2,592,259		2,592,259
Franchise					503,178		503,178
Hotel/Motel					320,022		320,022
Other					43,711		43,711
Investment earnings					94,109	2,073	96,182
Miscellaneous					133,926	103,751	237,677
Transfers					765,800	(765,800)	-
Total general revenues					7,451,687	(659,976)	6,791,711
Change in net assets					2,419,513	67,773	2,487,286
Net assets, beginning					11,304,764	8,451,097	19,755,861
Prior period adjustment					(10,727)	-	(10,727)
Net assets, ending					\$ 13,713,550	\$ 8,518,870	\$ 22,232,420

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

CITY OF HILLSBORO, TEXAS

BALANCE SHEET

GOVERNMENTAL FUNDS

SEPTEMBER 30, 2012

	<u>General</u>	<u>Economic Development Corporation</u>	<u>CDBG Grant Fund</u>	<u>Parks EDI Grant</u>
ASSETS				
Cash and investments	\$ 437,940	\$ 2,179,940	\$ 12,775	\$ -
Receivables (net of allowance for uncollectibles)				
Taxes	538,712	38,584	-	-
Accounts	368,962	-	-	-
Intergovernmental	-	-	224,654	400,000
Inventory	52,825	-	-	-
Due from other funds	607,200	93,324	-	-
Total assets	<u>\$ 2,005,639</u>	<u>\$ 2,311,848</u>	<u>\$ 237,429</u>	<u>\$ 400,000</u>
LIABILITIES				
Accounts payable	\$ 274,735	\$ -	\$ 79,576	\$ -
Accrued liabilities	135,395	-	-	-
Due to other funds	93,324	-	157,853	400,000
Deferred revenue	354,493	-	-	-
Total liabilities	<u>857,947</u>	<u>-</u>	<u>237,429</u>	<u>400,000</u>
FUND BALANCE				
Nonspendable:				
Inventory	52,825	-	-	-
Restricted for:				
Court security and technology	183,030	-	-	-
Debt service	-	-	-	-
Economic development	-	2,311,848	-	-
Capital projects	-	-	-	-
Capital improvements	-	-	-	-
Industrial development	-	-	-	-
Library operations	-	-	-	-
Public Safety	-	-	-	-
Tourism	-	-	-	-
Unassigned	911,837	-	-	-
Total fund balances	<u>1,147,692</u>	<u>2,311,848</u>	<u>-</u>	<u>-</u>
Total liabilities and fund balances	<u>\$ 2,005,639</u>	<u>\$ 2,311,848</u>	<u>\$ 237,429</u>	<u>\$ 400,000</u>

Capital assets used in governmental activities are not financial resources and, therefore, are not reported in the funds.

Other long-term assets are not available to pay for current-period expenditures and, therefore, are deferred in the funds.

Long-term liabilities are not due and payable in the current period and therefore are not reported in the funds.

Net assets of governmental activities

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

Debt Service	Capital Projects	Other Governmental Funds	Total Governmental Funds
\$ 110,499	\$ 2,914,006	\$ 1,145,364	\$ 6,800,524
48,474	-	57,900	683,670
652	-	-	369,614
-	-	337,057	961,711
-	-	-	52,825
<u>2,535</u>	<u>-</u>	<u>-</u>	<u>703,059</u>
\$ <u>162,160</u>	\$ <u>2,914,006</u>	\$ <u>1,540,321</u>	\$ <u>9,571,403</u>
\$ -	\$ 46,604	\$ 135,064	\$ 535,979
2,535	-	1,356	139,286
-	12,505	207,200	870,882
<u>44,955</u>	<u>-</u>	<u>-</u>	<u>399,448</u>
<u>47,490</u>	<u>59,109</u>	<u>343,620</u>	<u>1,945,595</u>
-	-	-	52,825
-	-	-	183,030
114,670	-	-	114,670
-	-	-	2,311,848
-	2,854,897	-	2,854,897
-	-	13,789	13,789
-	-	21	21
-	-	32,361	32,361
-	-	829,926	829,926
-	-	320,604	320,604
-	-	-	911,837
<u>114,670</u>	<u>2,854,897</u>	<u>1,196,701</u>	<u>7,625,808</u>
\$ <u>162,160</u>	\$ <u>2,914,006</u>	\$ <u>1,540,321</u>	
			17,427,613
			573,470
			(11,913,341)
			\$ <u>13,713,550</u>

CITY OF HILLSBORO, TEXAS

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

GOVERNMENTAL FUNDS

FOR THE YEAR ENDED SEPTEMBER 30, 2012

	<u>General</u>	<u>Economic Development Corporation</u>	<u>CDBG Grant Fund</u>	<u>Parks EDI Grant</u>
REVENUES				
Taxes:				
Ad valorem	\$ 1,899,255	\$ -	\$ -	\$ -
Sales	2,376,238	216,021	-	-
Franchise	503,178	-	-	-
Hotel/motel	-	-	-	-
Other	43,711	-	-	-
Services to others	6,676	-	-	-
Licenses and permits	70,603	-	-	-
Fines and forfeitures	828,613	-	-	-
Intergovernmental	47,185	-	274,979	373,899
Interest and penalties	49,527	12,185	-	-
Rentals	85,975	-	-	-
Charges for services	172,244	-	-	-
Cemetery lot sales and fees	26,255	-	-	-
Contributions	52,719	-	-	-
Other	67,727	65,223	-	-
Total revenues	<u>6,229,906</u>	<u>293,429</u>	<u>274,979</u>	<u>373,899</u>
EXPENDITURES				
Current:				
Personnel	4,750,191	17,349	-	-
Supplies	510,941	-	-	-
Services	907,293	11,956	20,000	-
Maintenance	238,061	6,316	-	-
Minor equipment	45,548	-	-	-
Capital outlay	153,244	-	306,979	373,899
Debt service:				
Principal	82,833	-	-	-
Interest	8,919	-	-	-
Bond issuance costs	-	-	-	-
Total expenditures	<u>6,697,030</u>	<u>35,621</u>	<u>326,979</u>	<u>373,899</u>
EXCESS (DEFICIENCY) OF REVENUES OVER (UNDER) EXPENDITURES	<u>(467,124)</u>	<u>257,808</u>	<u>(52,000)</u>	<u>-</u>
OTHER FINANCING SOURCES (USES)				
Issuance of long-term debt	-	-	-	-
Premium on long-term debt	-	-	-	-
Payment to escrow agent	-	-	-	-
Operating transfers in	750,329	-	52,000	-
Operating transfers out	(282,012)	(12,000)	-	-
Total other financing sources (uses)	<u>468,317</u>	<u>(12,000)</u>	<u>52,000</u>	<u>-</u>
NET CHANGE IN FUND BALANCES	1,193	245,808	-	-
FUND BALANCES, BEGINNING	<u>1,157,226</u>	<u>2,066,040</u>	<u>-</u>	<u>-</u>
PRIOR PERIOD ADJUSTMENT	<u>(10,727)</u>	<u>-</u>	<u>-</u>	<u>-</u>
FUND BALANCES, ENDING	<u>\$ 1,147,692</u>	<u>\$ 2,311,848</u>	<u>\$ -</u>	<u>\$ -</u>

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

<u>Debt Service</u>	<u>Capital Projects</u>	<u>Other Governmental Funds</u>	<u>Total Governmental Funds</u>
\$ 1,066,109	\$ -	\$ -	\$ 2,965,364
-	-	-	2,592,259
-	-	-	503,178
-	-	320,022	320,022
-	-	-	43,711
-	-	-	6,676
-	-	-	70,603
-	-	248,014	1,076,627
-	-	846,318	1,542,381
24,409	1,841	6,147	94,109
-	-	9,142	95,117
-	-	-	172,244
-	-	-	26,255
-	-	3,704	56,423
-	-	976	133,926
<u>1,090,518</u>	<u>1,841</u>	<u>1,434,323</u>	<u>9,698,895</u>
-	163,351	55,169	4,986,060
-	-	11,353	522,294
1,600	-	204,428	1,145,277
-	-	17,133	261,510
-	-	18,886	64,434
-	1,028,653	1,193,804	3,056,579
710,000	-	52,919	845,752
390,077	-	21,547	420,543
23,952	54,044	-	77,996
<u>1,125,629</u>	<u>1,246,048</u>	<u>1,575,239</u>	<u>11,380,445</u>
(35,111)	(1,244,207)	(140,916)	(1,681,550)
895,000	1,870,000	-	2,765,000
56,441	87,406	-	143,847
(926,837)	-	-	(926,837)
11,667	-	270,345	1,084,341
-	-	(24,529)	(318,541)
<u>36,271</u>	<u>1,957,406</u>	<u>245,816</u>	<u>2,747,810</u>
1,160	713,199	104,900	1,066,260
<u>113,510</u>	<u>2,141,698</u>	<u>1,091,801</u>	<u>6,570,275</u>
-	-	-	(10,727)
<u>\$ 114,670</u>	<u>\$ 2,854,897</u>	<u>\$ 1,196,701</u>	<u>\$ 7,625,808</u>

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, 2012

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

Net change in fund balances - total governmental funds (page 15)	\$ 1,066,260
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.	2,402,765
Revenues in the statement of activities that do not provide current financial resources are not reported as revenues in the funds.	63,795
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.	(1,171,573)
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>58,266</u>
Change in net assets of governmental activities (page 11)	\$ <u>2,419,513</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, 2012

	Business-type Activities-Enterprise Fund			
	Water and Wastewater	Sanitation	Airport	Totals
ASSETS				
Cash and investments	\$ 1,494,467	\$ 231,794	\$ 116	\$ 1,726,377
Accounts receivable	543,852	50,456	51,869	646,177
Inventories	121,091	-	49,132	170,223
Due from other funds	167,823	-	-	167,823
Other assets	160,077	-	-	160,077
Fixed assets	<u>9,248,964</u>	<u>101,756</u>	<u>889,939</u>	<u>10,240,659</u>
 Total assets	 <u>\$ 11,736,274</u>	 <u>\$ 384,006</u>	 <u>\$ 991,056</u>	 <u>\$ 13,111,336</u>
LIABILITIES				
Current liabilities:				
Accounts payable	\$ 102,606	\$ 64,145	\$ 2,556	\$ 169,307
Customer deposits	225,603	-	-	225,603
Accrued liabilities	19,056	-	1,640	20,696
Accrued interest payable	19,167	-	-	19,167
Capital lease payable	24,705	-	-	24,705
Bonds payable	<u>540,000</u>	<u>-</u>	<u>-</u>	<u>540,000</u>
Total current liabilities	<u>931,137</u>	<u>64,145</u>	<u>4,196</u>	<u>999,478</u>
Long-term liabilities:				
Bonds payable	3,559,276	-	-	3,559,276
Vacation payable	<u>31,598</u>	<u>-</u>	<u>2,114</u>	<u>33,712</u>
Total long-term liabilities	<u>3,590,874</u>	<u>-</u>	<u>2,114</u>	<u>3,592,988</u>
Total liabilities	<u>4,522,011</u>	<u>64,145</u>	<u>6,310</u>	<u>4,592,466</u>
NET ASSETS				
Invested in capital assets, net of related debt	5,124,983	101,756	889,939	6,116,678
Unrestricted	<u>2,089,280</u>	<u>218,105</u>	<u>94,807</u>	<u>2,402,192</u>
Total net assets	<u>\$ 7,214,263</u>	<u>\$ 319,861</u>	<u>\$ 984,746</u>	<u>\$ 8,518,870</u>

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, 2012

	Business-type Activities-Enterprise Fund			
	Water and Wastewater	Sanitation	Airport	Totals
OPERATING REVENUES				
Water and sewer sales	\$ 3,868,934	\$ -	\$ -	\$ 3,868,934
Other service charges	100,209	1,070,216	365,246	1,535,671
Miscellaneous income	103,751	-	-	103,751
Total operating revenues	<u>4,072,894</u>	<u>1,070,216</u>	<u>365,246</u>	<u>5,508,356</u>
OPERATING EXPENSES				
Water purchase	1,356,974	-	-	1,356,974
Personnel	710,642	-	46,349	756,991
Supplies	105,299	-	291,982	397,281
Services	428,976	804,590	39,039	1,272,605
Maintenance	239,084	7,788	1,694	248,566
Depreciation and amortization	478,086	2,100	29,260	509,446
Total operating expenses	<u>3,319,061</u>	<u>814,478</u>	<u>408,324</u>	<u>4,541,863</u>
OPERATING INCOME (LOSS)	<u>753,833</u>	<u>255,738</u>	<u>(43,078)</u>	<u>966,493</u>
NONOPERATING REVENUES (EXPENSES)				
Interest income	2,073	-	-	2,073
Contributions	3,600	-	-	3,600
Interest expense	(138,593)	-	-	(138,593)
Total nonoperating revenues (expenses)	<u>(132,920)</u>	<u>-</u>	<u>-</u>	<u>(132,920)</u>
Income (loss) before operating transfers	620,913	255,738	(43,078)	833,573
Transfer in	-	-	33,000	33,000
Transfer out	(452,000)	(346,800)	-	(798,800)
CHANGE IN NET ASSETS	168,913	(91,062)	(10,078)	67,773
TOTAL NET ASSETS, BEGINNING	<u>7,045,350</u>	<u>410,923</u>	<u>994,824</u>	<u>8,451,097</u>
TOTAL NET ASSETS, ENDING	<u>\$ 7,214,263</u>	<u>\$ 319,861</u>	<u>\$ 984,746</u>	<u>\$ 8,518,870</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, 2012

	Business-type Activities - Enterprise Fund			
	Water and Wastewater	Sanitation	Airport	Totals
CASH FLOWS FROM OPERATING ACTIVITIES				
Cash received from customers	\$ 4,115,527	\$ 1,068,707	\$ 338,184	\$ 5,522,418
Cash payments to employees for services	(709,243)	-	(45,232)	(754,475)
Cash payments to suppliers for goods and services	(2,291,651)	(811,446)	(326,827)	(3,429,924)
Cash provided (used) by operating activities	<u>1,114,633</u>	<u>257,261</u>	<u>(33,875)</u>	<u>1,338,019</u>
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES				
Advances from other funds	(167,823)	-	-	(167,823)
Cash paid to other funds	(452,000)	(346,800)	33,000	(765,800)
Cash used for noncapital financing activities	<u>(619,823)</u>	<u>(346,800)</u>	<u>33,000</u>	<u>(933,623)</u>
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES				
Principal repayments on debt	(469,021)	-	-	(469,021)
Capital contributions	3,600	-	-	3,600
Proceeds from capital debt	3,741,981	-	-	3,741,981
Capital lease payments	(23,886)	-	-	(23,886)
Refunding of bonds	(3,605,000)	-	-	(3,605,000)
Interest and fiscal charges on debt	(165,231)	-	-	(165,231)
Acquisition and construction of capital assets	(5,668)	-	-	(5,668)
Cash provided (used) by capital and related financing activities	<u>(523,225)</u>	<u>-</u>	<u>-</u>	<u>(523,225)</u>
CASH FLOWS FROM INVESTING ACTIVITIES				
Interest on investments	2,073	-	-	2,073
Cash provided by investing activities	<u>2,073</u>	<u>-</u>	<u>-</u>	<u>2,073</u>
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(26,342)	(89,539)	(875)	(116,756)
CASH AND CASH EQUIVALENTS, BEGINNING	<u>1,520,809</u>	<u>321,333</u>	<u>991</u>	<u>1,843,133</u>
CASH AND CASH EQUIVALENTS, ENDING	<u>\$ 1,494,467</u>	<u>\$ 231,794</u>	<u>\$ 116</u>	<u>\$ 1,726,377</u>

(continued)

CITY OF HILLSBORO, TEXAS
STATEMENT OF CASH FLOWS
PROPRIETARY FUNDS
(Continued)
FOR THE YEAR ENDED SEPTEMBER 30, 2012

	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)	\$ 753,833	\$ 255,738	\$(43,078)	\$ 966,493
Adjustments to reconcile operating income to net cash provided by operating activities:				
Depreciation and amortization	478,086	2,100	29,261	509,447
Change in assets and liabilities:				
Decrease (increase) in accounts receivable	40,565	(1,509)	(27,063)	11,993
Decrease (increase) in other assets	(136,982)	-	-	(136,982)
Increase (decrease) in accounts payable	12,638	932	1,147	14,717
Increase (decrease) in accrued liabilities	(1,054)	-	547	(507)
Increase (decrease) in vacation payable	2,453	-	570	3,023
Increase (decrease) in customer deposits	2,068	-	-	2,068
Decrease (increase) in inventory	(36,974)	-	4,741	(32,233)
Total adjustments	<u>360,800</u>	<u>1,523</u>	<u>9,203</u>	<u>371,526</u>
Net cash provided by operating activities	<u>\$ 1,114,633</u>	<u>\$ 257,261</u>	<u>\$(33,875)</u>	<u>\$ 1,338,019</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, 2012

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

The **CDBG Grant Fund** – accounts for financial resources of the Community Development Block grant received by the City.

The **Parks EDI Grant Fund** – accounts for financial resources of the Housing and Urban Development economic incentives grant received by the City.

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.

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.

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, Search and Rescue Equipment Grant Fund, Downtown Streetscape Phase II Fund, Industrial Development Fund, Library Special Fund, Home Buyers Assistance Grant Fund, Parks and Wildlife Grant Fund, Police Local Forfeiture, Federal Forfeiture and Special Funds, Energy Grant Fund, Safe Route to Schools Fund and the East Franklin Streetscape Fund.

(continued)

I. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

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

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 Capital Construction Fund.

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.

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

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.

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.

(continued)

I. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Assets, Liabilities and Net Assets or Equity (Continued)

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, 2012, 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 2012 were levied October 1, 2011, at the rate of \$.818331 per \$100 assessed valuation on a total taxable assessed valuation of \$381,475,943.

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.

(continued)

I. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Assets, Liabilities and Net Assets or Equity (Continued)

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:

<u>Assets</u>	<u>Years</u>
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, 2012.

(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, 2012, 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 and Net Assets

The governmental fund financial statements present fund balances based on classifications that comprise a hierarchy that is based primarily on the extent to which the City is bound to honor constraints on the specific purposes for which amounts in the respective governmental funds can be spent. The classifications used in the governmental fund financial statements are as follows:

- **Nonspendable:** This classification includes amounts that cannot be spent because they are either (a) not in spendable form or (b) are legally or contractually required to be maintained intact. Nonspendable items are not expected to be converted to cash or are not expected to be converted to cash within the next year.
- **Restricted:** This classification includes amounts for which constraints have been placed on the use of the resources either (a) externally imposed by creditors, grantors, contributors, or laws or regulations of other governments, or (b) imposed by law through constitutional provisions or enabling legislation.
- **Committed:** This classification includes amounts that can be used only for specific purposes pursuant to constraints imposed by board resolution of the City council, the City's highest level of decision making authority. These amounts cannot be used for any other purpose unless the City council removes or changes the specified use by taking the same type of action that was employed when the funds were initially committed. This classification also includes contractual obligations to the extent that existing resources have been specifically committed for use in satisfying those contractual requirements.
- **Assigned:** This classification includes amounts that are constrained by the City's intent to be used for a specific purpose but are neither restricted nor committed. This intent can be expressed by the City council.
- **Unassigned:** This classification includes the residual fund balance for the General Fund. The unassigned classification also includes negative residual fund balance of any other governmental fund that cannot be eliminated by offsetting of assigned fund balance amounts.

(continued)

I. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Assets, Liabilities and Net Assets or Equity (Continued)

Fund Equity and Net Assets (Continued)

In the government-wide financial statements, 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.

In the government-wide financial statements, the City's restrictions on net assets are for amounts that are not available for appropriation. The City's restricted net assets are as follows:

Restricted for Court Security & Technology	\$	183,030
Restricted for Debt Service		114,670
Restricted for Economic Development		2,311,848
Restricted for Capital Projects		2,854,897
Restricted for Capital Improvements		13,789
Restricted for Industrial Development		21
Restricted for Library Operations		32,361
Restricted for Public Safety		829,926
Restricted for Tourism		<u>320,604</u>
Total	\$	<u>6,661,146</u>

The government-wide and fund level financial statements report restricted fund balances for amounts not available for appropriation or legally restricted for specific uses. When an expenditure is incurred for purposes for which both restricted and unrestricted fund balance is available, it is the City's policy to use restricted resources first, then unrestricted resources as needed. When an expenditure is incurred for which committed, assigned, or unassigned fund balances are available, the City considers amounts to have been spent first out of committed funds, then assigned funds, and finally unassigned funds.

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, 2012, the City's deposit balance (cash and certificates of deposit) was \$3,597,293. The City's deposits at September 30, 2012 were 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, 2012, the primary government's investments consisted of:

	<u>Fair Value</u>
TexStar	\$ 1,042,223
Texas Term	1,545,731
State Treasurer's Investment Pool (TexPool)	<u>555,281</u>
	<u>\$ 3,143,235</u>

At September 30, 2012 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:

	Governmental Funds					Enterprise Funds			Totals	
	General	EDC	CDBG Grant Fund	Parks EDI	Debt Service	Nonmajor Funds	Water and Wastewater	Sanitation		Airport
Receivables:										
Accounts:										
Customers	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 543,852	\$ 50,456	\$ 51,869	\$ 646,177
Taxes:										
Property	348,753	-	-	-	193,895	-	-	-	-	542,648
Sales tax	424,613	38,584	-	-	-	-	-	-	-	463,197
Other	26,911	-	-	-	-	57,900	-	-	-	84,811
Intergovernmental	-	-	224,654	400,000	-	337,057	-	-	-	961,711
Other	<u>2,457,199</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>652</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>2,457,851</u>
Gross receivables	3,257,476	38,584	224,654	400,000	194,547	394,957	543,852	50,456	51,869	5,156,395
Less: allowance for uncollectibles	<u>(2,349,802)</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>(145,421)</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>(2,495,223)</u>
Net total receivables	<u>\$ 907,674</u>	<u>\$ 38,584</u>	<u>\$ 224,654</u>	<u>\$ 400,000</u>	<u>\$ 49,126</u>	<u>\$ 394,957</u>	<u>\$ 543,852</u>	<u>\$ 50,456</u>	<u>\$ 51,869</u>	<u>\$ 2,661,172</u>

(continued)

II. DETAILED NOTES ON ALL FUNDS (Continued)

Receivables (Continued)

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)	\$ 80,831
Delinquent court fines receivable (general fund)	273,662
Delinquent property taxes receivable (debt service)	<u>44,955</u>
Total Governmental Funds	<u>\$ 399,448</u>

Capital Assets

Capital asset activity for the year ended September 30, 2012, was as follows:

	<u>Beginning Balance</u>	<u>Increase</u>	<u>Decrease</u>	<u>Adjustment</u>	<u>Ending Balance</u>
Governmental activities:					
Capital assets, not being depreciated:					
Land	\$ 803,426	\$ -	\$ -	\$ -	\$ 803,426
Construction in progress	<u>1,004,958</u>	<u>2,941,610</u>	<u>3,193,330</u>	400	<u>753,638</u>
Total assets not being depreciated	<u>1,808,384</u>	<u>2,941,610</u>	<u>3,193,330</u>	400	<u>1,557,064</u>
Capital assets, being depreciated:					
Buildings and improvements	5,692,446	1,147,001	19,989	-	6,819,458
Machinery and equipment	4,198,639	254,303	202,668	(10,900)	4,239,374
Infrastructure	<u>8,902,330</u>	<u>2,067,042</u>	<u>-</u>	<u>-</u>	<u>10,969,372</u>
Total capital assets being depreciated	<u>18,793,415</u>	<u>3,468,346</u>	<u>222,657</u>	(10,900)	<u>22,028,204</u>
Accumulated depreciation:					
Buildings and improvements	2,727,664	158,228	17,499	-	2,868,393
Machinery and equipment	2,366,545	383,140	151,653	(10,900)	2,587,132
Infrastructure	<u>482,742</u>	<u>219,388</u>	<u>-</u>	<u>-</u>	<u>702,130</u>
Total accumulated depreciation	<u>5,576,951</u>	<u>760,756</u>	<u>169,152</u>	(10,900)	<u>6,157,655</u>
Total capital assets being depreciated, net	<u>13,216,464</u>	<u>2,707,590</u>	<u>53,505</u>	-	<u>15,870,549</u>
Governmental activities capital assets, net	<u>\$ 15,024,848</u>	<u>\$ 5,649,200</u>	<u>\$ 3,246,835</u>	<u>\$ 400</u>	<u>\$ 17,427,613</u>

(continued)

II. DETAILED NOTES ON ALL FUNDS (Continued)

Capital Assets (Continued)

	Beginning Balance	Increase	Decrease	Adjustment	Ending Balance
Business-type activities:					
Capital assets, not being depreciated:					
Land	\$ 378,391	\$ -	\$ -	\$ -	\$ 378,391
Construction in progress - Water/Sewer	-	5,667	-	-	5,667
Total assets not being depreciated	<u>378,391</u>	<u>5,667</u>	<u>-</u>	<u>-</u>	<u>384,058</u>
Capital assets, being depreciated:					
Buildings and improvements	5,865,462	-	-	-	5,865,462
Machinery and equipment	1,669,537	-	-	10,900	1,680,437
Infrastructure	14,700,102	-	289,994	-	14,410,108
Total capital assets being depreciated	<u>22,235,101</u>	<u>-</u>	<u>289,994</u>	<u>10,900</u>	<u>21,956,007</u>
Accumulated depreciation:					
Buildings and improvements	1,015,896	111,933	-	-	1,127,829
Machinery and equipment	1,304,469	75,864	-	10,900	1,391,233
Infrastructure	9,555,908	314,430	289,994	-	9,580,344
Total accumulated depreciation	<u>11,876,273</u>	<u>502,227</u>	<u>289,994</u>	<u>10,900</u>	<u>12,099,406</u>
Total capital assets being depreciated, net	<u>10,358,828</u>	<u>(502,227)</u>	<u>-</u>	<u>-</u>	<u>9,856,601</u>
Business-type activities capital assets, net	<u>\$ 10,737,219</u>	<u>\$ (496,560)</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 10,240,659</u>

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

Governmental activities	
General government	\$ 156,476
Public safety	286,967
Public works	239,769
Community development	<u>77,544</u>
Total depreciation expense - governmental activities	<u>\$ 760,756</u>
Business-type activities:	
Water and wastewater	\$ 470,867
Sanitation	2,100
Airport	<u>29,260</u>
Total depreciation expense - business-type activities	<u>\$ 502,227</u>

(continued)

II. DETAILED NOTES ON ALL FUNDS (Continued)

Interfund Receivables, Payables and Transfers

The composition of interfund balances as of September 30, 2012, is as follows:

<u>Receivable Fund</u>	<u>Payable Fund</u>	<u>Amount</u>
EDC	General	\$ 93,324
General	Nonmajor	207,200
Water & Wastewater	CDBG Grant	157,853
Water & Wastewater	Capital Projects	9,970
General	Parks EDI Grant	400,000
Debt Service	Capital Projects	<u>2,535</u>
Total		<u>\$ 870,882</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, 2012, are as follows:

<u>Transfers In</u>	<u>Transfers Out</u>	<u>Amount</u>
General	EDC	\$ 12,000
General	Nonmajor	24,529
General	Sanitation	150,000
Airport	Sanitation	33,000
Nonmajor	General	270,345
General	Water & Wastewater	400,000
CDBG	Water & Wastewater	52,000
Debt Service	General	11,667
General	Sanitation	<u>163,800</u>
Total		<u>\$ 1,117,341</u>

(continued)

II. DETAILED NOTES ON ALL FUNDS (Continued)

Long-term Debt

Long-term liability activity from the year ended September 30, 2012, was as follows:

	Debt Outstanding 09/30/11	Additions of New Debt	Retirements and Repayments	Debt Outstanding 09/30/12
<u>Governmental:</u>				
Certificates of obligation	\$ 1,230,000	\$ -	\$ 995,000	\$ 235,000
General obligation bonds	8,370,000	2,765,000	655,000	10,480,000
Premium	116,961	143,847	8,204	252,604
Capital Leases	538,618	-	115,752	422,866
Net OPEB obligation	227,141	36,682	-	263,823
Vacation payable	251,700	7,348	-	259,048
	<u>10,734,420</u>	<u>2,952,877</u>	<u>1,773,956</u>	<u>11,913,341</u>
<u>Enterprise Fund</u>				
Certificates of obligation	3,880,000	-	3,880,000	-
General obligation bonds	525,000	3,520,000	185,000	3,860,000
Premium	26,316	221,981	9,021	239,276
Capital Leases	48,590	-	23,885	24,705
Vacation payable	30,690	3,022	-	33,712
	<u>4,510,596</u>	<u>3,745,003</u>	<u>4,097,906</u>	<u>4,157,693</u>
Total	<u>\$ 15,245,016</u>	<u>\$ 6,697,880</u>	<u>\$ 5,871,862</u>	<u>\$ 16,071,034</u>

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

(continued)

II. DETAILED NOTES ON ALL FUNDS (Continued)

Long-term Debt (Continued)

Debt outstanding as of September 30, 2012, consisted of the following:

	<u>Purpose of Issue</u>	<u>Amount Issued</u>	<u>Amount Outstanding</u>	<u>Interest Rate</u>
<u>Governmental</u>				
Certificates of obligation:				
2007 Series	City Hall renovations	315,000	235,000	4.53%
		<u>315,000</u>	<u>235,000</u>	
General obligation bonds:				
2006 Series	Street Improvements	4,000,000	3,240,000	3.75%-5.125%
2008 Series	Various improvements	2,000,000	1,785,000	4.625%-7.00%
2008 Series Premium		52,854	42,282	
2010 Series	Street Improvements	2,000,000	1,930,000	2.00%-4.05%
2010 Series Premium		43,967	39,570	
2010 Series	Refunding	1,525,000	760,000	2.00%-4.05%
2010 Series Premium		33,631	26,905	
2012 Series	Street Improvements	1,870,000	1,870,000	2.00%-3.00%
2012 Series	Refunding	895,000	895,000	2.00%-3.00%
2012 Series Premium		87,406	87,406	
2012 Series Premium	Refunding	56,441	56,441	
		<u>12,564,299</u>	<u>10,732,604</u>	
Total Governmental Long-term		<u>12,879,299</u>	<u>10,967,604</u>	
<u>Enterprise Fund</u>				
General obligation bonds:				
2010 Series	Refunding	720,000	340,000	2.00%-4.25%
2010 Series Premium		32,895	19,737	
2012 Series	Refunding	3,520,000	3,520,000	2.00%-3.00%
2012 Series Premium		221,981	219,539	
		<u>4,494,876</u>	<u>4,099,276</u>	
Total Enterprise Fund		<u>4,494,876</u>	<u>4,099,276</u>	
		<u>\$ 17,374,175</u>	<u>\$ 15,066,881</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:	2013	20,000	10,646	30,646
	2014	20,000	9,740	29,740
	2015	20,000	8,833	28,833
	2016	20,000	7,927	27,927
	2017	25,000	7,022	32,022
	2018-2022	<u>130,000</u>	<u>18,120</u>	<u>148,120</u>
		<u>235,000</u>	<u>62,288</u>	<u>297,288</u>
General Obligation Bonds:	2013	625,000	380,992	1,005,992
	2014	635,000	368,584	1,003,584
	2015	655,000	348,284	1,003,284
	2016	550,000	326,690	876,690
	2017	575,000	307,778	882,778
	2018-2022	3,210,000	1,201,545	4,411,545
	2023-2027	3,040,000	569,226	3,609,226
	2028-2032	<u>1,190,000</u>	<u>100,187</u>	<u>1,290,187</u>
		<u>10,480,000</u>	<u>3,603,286</u>	<u>14,083,286</u>
Total Governmental Debt:	2013	645,000	391,638	1,036,638
	2014	655,000	378,324	1,033,324
	2015	675,000	357,117	1,032,117
	2016	570,000	334,617	904,617
	2017	600,000	314,800	914,800
	2018-2022	3,340,000	1,219,665	4,559,665
	2023-2027	3,040,000	569,226	3,609,226
	2028-2032	<u>1,190,000</u>	<u>100,187</u>	<u>1,290,187</u>
	Total	<u>\$ 10,715,000</u>	<u>\$ 3,665,574</u>	<u>\$ 14,380,574</u>

Enterprise Fund debt requirements are as follows:

	<u>Year Ended September 30</u>	<u>Principal</u>	<u>Interest</u>	<u>Total Requirements</u>
General Obligation Bonds:	2013	540,000	85,210	625,210
	2014	385,000	85,294	470,294
	2015	390,000	77,594	467,594
	2016	335,000	69,550	404,550
	2017	345,000	62,850	407,850
	2018-2022	<u>1,865,000</u>	<u>171,150</u>	<u>2,036,150</u>
		<u>3,860,000</u>	<u>551,648</u>	<u>4,411,648</u>

(continued)

II. DETAILED NOTES ON ALL FUNDS (Continued)

Long-term Debt (Continued)

Advance Refunding

The government issued \$6,285,000 in general obligation bonds with interest rates ranging from 2.0% to 3.0%. The proceeds were used to advance refund \$4,525,000 of outstanding 2002 and 2005 certificates of obligation which had interest rates ranging from 4.00% to 4.80%. The net proceeds of \$4,572,052 (including a \$365,829 premium and after payment of \$175,415 in underwriting fees and other issuance costs, new debt of \$1,900,000 and \$3,362 deposited to I&S) were deposited in an irrevocable trust with an escrow agent to provide funds for the future debt service payment on the refunded bonds. As a result, this portion of the 2002 and 2005 certificates of obligation are considered defeased and the liability for those bonds has been removed from the statement of net position.

The reacquisition price exceeded the net carrying amount of the old debt by \$47,052. Of this amount, \$40,215 is being netted against the new debt and amortized over the life of the refunding debt in the business-type activities. The government advance refunded this portion of the 2002 and 2005 certificate of obligation to reduce its total debt service payments over 13 years by \$664,834 and to obtain an economic gain (difference between the present values of the debt service payments on the old and new debt) of \$585,375.

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	185,635
EMS Vehicle/Equipment	250,000
Paver	93,890
Total	<u>\$ 680,525</u>
Water and Wastewater activities	
Wheel Loader	\$ 113,700
Total	<u>\$ 113,700</u>

(continued)

II. DETAILED NOTES ON ALL FUNDS (Continued)

The future minimum lease obligations and the net present value of these minimum lease payments as of September 30, 2012, were as follows:

Year Ending September 30,	Governmental Activities	Water and Wastewater Activities
2013	\$ 134,668	\$ 25,160
2014	134,668	-
2015	97,369	-
2016	97,370	-
Total minimum lease payments	464,075	25,160
Less: amount representing interest	41,209	455
Present value of minimum lease payments	\$ 422,866	\$ 24,705

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.

The City paid \$1,356,974 for water purchased from the District during the fiscal year ending September 30, 2012.

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.

(continued)

II. DETAILED NOTES ON ALL FUNDS (Continued)

Retirement Plan (Continued)

Plan Description (Continued)

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 2011	Plan Year 2012
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.

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>09/30/12</u>
Annual required contribution (ARC)	\$ 497,902
Interest on Net Pension Obligation	-
Adjustment to the ARC	-
Annual Pension Cost (APC)	<u>497,902</u>
Contributions made	<u>(461,220)</u>
Increase (decrease) in net pension obligation	36,682
Net pension obligation/(Asset), beginning of year	<u>227,141</u>
Net pension obligation/(Asset), end of year	<u><u>\$ 263,823</u></u>

(continued)

I. DETAILED NOTES ON ALL FUNDS (Continued)

Retirement Plan (Continued)

Contributions (Continued)

Accounting Year Ending	Annual Pension Cost (APC)	Actual Contribution Made	Percentage of APC Contributed	Net Pension Obligation
09/30/10	474,108	388,871	122%	85,237
09/30/11	516,613	443,216	117%	73,397
09/30/12	497,902	461,220	108%	36,682

The required contribution rates for fiscal year 2012 were determined as part of the December 31, 2010 and 2011 actuarial valuations. Additional information as of the latest actuarial valuation, December 31, 2011, also follows:

Valuation Date	12/31/09	12/31/10	12/31/11
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	28.2 years; closed period	27.2 years; closed period	26.2 years; closed period
Amortization Period for new Gains/Losses	30 years	30 years	30 years
Asset Valuation Method	10-year Smoothed Market	10-year Smoothed Market	10-year Smoothed Market
Actuarial Assumptions:			
Investment Rate of Return*	7.5%	7.0%	7.0%
Projected Salary Increases*	Varies by age and service	Varies by age and service	Varies by age and service
*Includes Inflation at	3.00%	3.00%	3.00%
Cost-of-Living Adjustments	2.1%	2.1%	2.1%

Funded Status and Funding Progress – The funded status as of December 31, 2011, under the two separate actuarial valuations, is presented 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
12/31/2011	10,103,860	13,027,440	77.6%	2,923,580	4,069,166	71.8%

Actuarial valuations involve estimates of the value of reported amounts and assumptions about the probability of events far into the future. Actuarially determined amounts are subject to continual revision as actual results are compared to past expectations and new estimates are made about the future.

(continued)

II. DETAILED NOTES ON ALL FUNDS (Continued)

Retirement Plan (Continued)

Contributions (Continued)

Actuarial calculations are based on the benefits provided under the terms of the substantive plan in effect at the time of each valuation, and reflect a long-term perspective. Consistent with that perspective, actuarial methods and assumptions used include techniques that are designed to reduce short-term volatility in actuarial accrued liabilities and the actuarial value of assets. The schedule of funding progress, presented as Required Supplementary Information following the notes to the financial statements, present 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 completed during fiscal year 2011.

(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 four years.

Prior Period Adjustment

A prior period adjustment in the amount of \$10,727 was made in order to reflect prior expenditures of an Energy grant that were disallowed due to parts contained in units installed not meeting the allowable requirements for the grant.

**REQUIRED
SUPPLEMENTARY INFORMATION**

CITY OF HILLSBORO, TEXAS

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

GENERAL FUND

FOR THE YEAR ENDED SEPTEMBER 30, 2012

	Budget		Actual	Variance with Final Budget Positive (Negative)
	Original	Final		
REVENUES				
Taxes:				
Ad valorem	\$ 1,904,000	\$ 1,904,000	\$ 1,899,255	\$(4,745)
Sales, net of rebates	2,295,800	2,295,800	2,376,238	80,438
Franchise	490,000	490,000	503,178	13,178
Other	25,000	25,000	43,711	18,711
Services to others	4,500	4,500	6,676	2,176
Licenses and permits	52,150	52,150	70,603	18,453
Fines and forfeitures	825,200	825,200	828,613	3,413
Intergovernmental	63,000	63,000	47,185	(15,815)
Interest and penalties	45,000	45,000	49,527	4,527
Rentals	80,500	80,500	85,975	5,475
Charges for services	285,810	285,810	172,244	(113,566)
Cemetery lot sales and fees	25,300	25,300	26,255	955
Contributions	47,800	47,800	52,719	4,919
Other	51,500	51,500	67,727	16,227
Total revenues	6,195,560	6,195,560	6,229,906	34,346
EXPENDITURES				
Legislative:				
Personnel	345	345	280	65
Supplies	1,550	1,550	106	1,444
Services	21,050	21,050	30,308	(9,258)
	22,945	22,945	30,694	(7,749)
Administration:				
Personnel	233,350	233,350	241,304	(7,954)
Supplies	21,450	21,450	19,282	2,168
Services	120,800	120,800	128,576	(7,776)
Maintenance	4,500	4,500	6,317	(1,817)
Minor equipment	-	-	14,197	(14,197)
	380,100	380,100	409,676	(29,576)

(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, 2012

	Budget		Actual	Variance with Final Budget Positive (Negative)
	Original	Final		
EXPENDITURES (Continued)				
Streets:				
Personnel	230,275	230,275	228,817	1,458
Supplies	59,850	59,850	44,408	15,442
Services	118,815	118,815	135,689	(16,874)
Maintenance	30,950	30,950	49,830	(18,880)
	439,890	439,890	458,744	(18,854)
Police:				
Personnel	1,852,695	1,852,695	1,760,275	92,420
Supplies	139,950	139,950	196,086	(56,136)
Services	131,600	131,600	150,723	(19,123)
Maintenance	61,150	61,150	51,436	9,714
Minor equipment	-	-	14,653	(14,653)
Capital outlay	73,000	73,000	86,545	(13,545)
	2,258,395	2,258,395	2,259,718	(1,323)
Library:				
Personnel	272,840	272,840	258,288	14,552
Supplies	9,685	9,685	7,147	2,538
Services	34,760	34,760	44,185	(9,425)
Maintenance	16,000	16,000	11,437	4,563
Capital outlay	32,500	32,500	24,224	8,276
	365,785	365,785	345,281	20,504
Fire:				
Personnel	1,218,160	1,218,160	1,196,166	21,994
Supplies	115,450	115,450	88,821	26,629
Services	88,050	88,050	113,432	(25,382)
Maintenance	19,200	19,200	24,246	(5,046)
Minor equipment	1,500	1,500	9,904	(8,404)
Capital outlay	-	-	12,285	(12,285)
	1,442,360	1,442,360	1,444,854	(2,494)

(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, 2012

	Budget		Actual	Variance with Final Budget Positive (Negative)
	Original	Final		
EXPENDITURES (Continued)				
Municipal court:				
Personnel	145,010	145,010	156,772	(11,762)
Supplies	5,500	5,500	3,421	2,079
Services	49,950	49,950	43,741	6,209
Maintenance	2,500	2,500	3,361	(861)
Capital outlay	-	-	8,428	(8,428)
	202,960	202,960	215,723	(12,763)
 Parks and recreation:				
Personnel	284,545	284,545	267,903	16,642
Supplies	26,650	26,650	29,488	(2,838)
Services	25,000	25,000	31,359	(6,359)
Maintenance	16,100	16,100	18,497	(2,397)
Minor equipment	1,500	1,500	2,095	(595)
	353,795	353,795	349,342	4,453
 Maintenance shop:				
Personnel	102,890	102,890	108,657	(5,767)
Supplies	63,475	63,475	92,302	(28,827)
Services	9,305	9,305	8,706	599
Maintenance	48,000	48,000	45,490	2,510
	223,670	223,670	255,155	(31,485)
 Cemetery:				
Personnel	15,745	15,745	15,102	643
Supplies	3,200	3,200	732	2,468
Services	83,825	83,825	58,977	24,848
Maintenance	2,350	2,350	516	1,834
	105,120	105,120	75,327	29,793

(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, 2012

	Budget		Actual	Variance with
	Original	Final		Final Budget Positive (Negative)
EXPENDITURES (Continued)				
Community development:				
Personnel	128,360	128,360	128,515	(155)
Supplies	3,850	3,850	3,171	679
Services	111,085	111,085	95,281	15,804
Maintenance	7,500	7,500	8,014	(514)
Minor equipment	-	-	341	(341)
	250,795	250,795	235,322	15,473
Legal:				
Personnel	31,615	31,615	31,611	4
Services	2,000	2,000	1,873	127
	33,615	33,615	33,484	131
Finance:				
Personnel	187,775	187,775	188,854	(1,079)
Supplies	3,400	3,400	4,137	(737)
Services	41,150	41,150	40,086	1,064
Maintenance	750	750	-	750
Minor equipment	1,500	1,500	1,049	451
	234,575	234,575	234,126	449
Information systems:				
Personnel	50,910	50,910	51,412	(502)
Supplies	100	100	836	(736)
Services	3,215	3,215	3,970	(755)
Maintenance	7,500	7,500	8,126	(626)
Minor equipment	-	-	431	(431)
Capital outlay	-	-	21,762	(21,762)
	61,725	61,725	86,537	(24,812)

(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, 2012

	Budget		Actual	Variance with Final Budget Positive (Negative)
	Original	Final		
EXPENDITURES (Continued)				
Animal control:				
Personnel	50,400	50,400	50,938	(538)
Supplies	13,950	13,950	9,072	4,878
Services	3,900	3,900	3,463	437
Maintenance	9,900	9,900	10,540	(640)
Minor equipment	-	-	2,878	(2,878)
	<u>78,150</u>	<u>78,150</u>	<u>76,891</u>	<u>1,259</u>
Emergency Management:				
Personnel	87,780	87,780	65,297	22,483
Supplies	20,200	20,200	11,932	8,268
Services	32,500	32,500	16,924	15,576
Maintenance	2,300	2,300	251	2,049
Minor equipment	500	500	-	500
	<u>143,280</u>	<u>143,280</u>	<u>94,404</u>	<u>48,876</u>
Debt service:				
Principal	82,800	82,800	82,833	(33)
Interest	9,000	9,000	8,919	81
	<u>91,800</u>	<u>91,800</u>	<u>91,752</u>	<u>48</u>
Total expenditures	<u>6,688,960</u>	<u>6,688,960</u>	<u>6,697,030</u>	<u>(8,070)</u>
EXCESS (DEFICIENCY) OF REVENUES OVER (UNDER) EXPENDITURES	<u>(493,400)</u>	<u>(493,400)</u>	<u>(467,124)</u>	<u>26,276</u>
OTHER FINANCING SOURCES (USES)				
Operating transfers in	501,400	501,400	750,329	248,929
Operating transfers (out)	(8,000)	(8,000)	(282,012)	(274,012)
Total other financing sources (uses)	<u>493,400</u>	<u>493,400</u>	<u>468,317</u>	<u>(25,083)</u>
CHANGE IN FUND BALANCES	-	-	1,193	1,193
FUND BALANCES, BEGINNING	<u>1,157,226</u>	<u>1,157,226</u>	<u>1,157,226</u>	<u>-</u>
PRIOR PERIOD ADJUSTMENT	<u>-</u>	<u>-</u>	<u>(10,727)</u>	<u>(10,727)</u>
FUND BALANCES, ENDING	<u>\$ 1,157,226</u>	<u>\$ 1,157,226</u>	<u>\$ 1,147,692</u>	<u>\$ 1,193</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, 2012

	Budget		Actual	Variance with Final Budget Positive (Negative)
	Original	Final		
REVENUES				
Taxes:				
Sales, net of rebates	200,100	200,100	216,021	15,921
Interest and penalties	7,000	7,000	12,185	5,185
Other	<u>46,200</u>	<u>46,200</u>	<u>65,223</u>	<u>19,023</u>
Total revenues	<u>253,300</u>	<u>253,300</u>	<u>293,429</u>	<u>40,129</u>
EXPENDITURES				
Community development:				
Personnel	94,510	94,510	17,349	77,161
Supplies	200	200	-	200
Services	1,304,390	1,304,390	11,956	1,292,434
Maintenance	<u>12,500</u>	<u>12,500</u>	<u>6,316</u>	<u>6,184</u>
Total expenditures	<u>1,411,600</u>	<u>1,411,600</u>	<u>35,621</u>	<u>1,375,979</u>
EXCESS (DEFICIENCY) OF REVENUES OVER (UNDER) EXPENDITURES	(1,158,300)	(1,158,300)	257,808	1,416,108
OTHER FINANCING SOURCES (USES)				
Operating transfers (out)	(12,000)	(12,000)	(12,000)	-
Total other financing sources (uses)	<u>(12,000)</u>	<u>(12,000)</u>	<u>(12,000)</u>	<u>-</u>
CHANGE IN FUND BALANCES	(1,170,300)	(1,170,300)	245,808	1,416,108
FUND BALANCES, BEGINNING	<u>2,066,040</u>	<u>2,066,040</u>	<u>2,066,040</u>	<u>-</u>
FUND BALANCES, ENDING	<u>\$ 895,740</u>	<u>\$ 895,740</u>	<u>\$ 2,311,848</u>	<u>\$ 1,416,108</u>

CITY OF HILLSBORO, TEXAS

**TMRS Analysis of Funding Progress
For the Year Ended September 30, 2012
(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
12/31/2009	6,151,982	9,796,293	62.8%	3,644,311	4,166,954	87.5%
12/31/2010	9,225,141	12,297,814	75.0%	3,072,673	3,994,428	76.9%
12/31/2011	10,103,860	13,027,440	77.6%	2,923,580	4,069,166	71.8%

CITY OF HILLSBORO, TEXAS

NOTES TO REQUIRED SUPPLEMENTARY INFORMATION

SEPTEMBER 30, 2012

(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 nonspendable fund balance on the balance sheet. Encumbrances do not lapse at the close of the fiscal year, but are carried forward until liquidated.
5. Expenditures exceeded appropriations in the General Fund in various departments. These excess expenditures were funded by available fund balance.

COMBINING SCHEDULES

CITY OF HILLSBORO, TEXAS
COMBINING BALANCE SHEET
NONMAJOR GOVERNMENTAL FUNDS

SEPTEMBER 30, 2012

	Special Revenue Funds			
	Hotel/Motel Tax	Search and Rescue Equipment Grant	Downtown Streetscape Phase II	Industrial Development
ASSETS				
Cash and investments	\$ 266,961	\$ -	\$ -	\$ 21
Intergovernmental receivable	-	-	3,234	-
Taxes receivable	57,900	-	-	-
Due from other funds	-	-	-	-
Total assets	<u>\$ 324,861</u>	<u>\$ -</u>	<u>\$ 3,234</u>	<u>\$ 21</u>
LIABILITIES				
Accounts payable	\$ 4,257	\$ -	\$ -	\$ -
Accrued liabilities	-	-	-	-
Due to other funds	-	-	3,234	-
Total liabilities	<u>4,257</u>	<u>-</u>	<u>3,234</u>	<u>-</u>
FUND BALANCE				
Restricted for:				
Capital improvements	-	-	-	-
Industrial development	-	-	-	21
Library operations	-	-	-	-
Public Safety	-	-	-	-
Tourism	320,604	-	-	-
Total fund balances	<u>320,604</u>	<u>-</u>	<u>-</u>	<u>21</u>
Total liabilities and fund equity	<u>\$ 324,861</u>	<u>\$ -</u>	<u>\$ 3,234</u>	<u>\$ 21</u>

Special Revenue Funds

Library Special Fund	Home Buyers Assistance Grant	Parks and Wildlife Grant	Police Local Forfeiture	Police Federal Forfeiture	Police Special	Energy Grant
\$ 32,361	\$ -	\$ -	\$ 800,981	\$ 27,643	\$ 3,608	\$ -
-	-	-	-	-	-	12,683
-	-	-	-	-	-	-
<u>\$ 32,361</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 800,981</u>	<u>\$ 27,643</u>	<u>\$ 3,608</u>	<u>\$ 12,683</u>
\$ -	\$ -	\$ -	\$ -	\$ 950	\$ -	\$ -
-	-	-	1,356	-	-	-
-	-	-	-	-	-	12,683
-	-	-	1,356	950	-	12,683
-	-	-	-	-	-	-
-	-	-	-	-	-	-
32,361	-	-	799,625	26,693	3,608	-
-	-	-	-	-	-	-
<u>32,361</u>	<u>-</u>	<u>-</u>	<u>799,625</u>	<u>26,693</u>	<u>3,608</u>	<u>-</u>
<u>\$ 32,361</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 800,981</u>	<u>\$ 27,643</u>	<u>\$ 3,608</u>	<u>\$ 12,683</u>

CITY OF HILLSBORO, TEXAS
COMBINING BALANCE SHEET
NONMAJOR GOVERNMENTAL FUNDS
(continued)
SEPTEMBER 30, 2012

	Special Revenue		Capital Projects	
	Safe Route To Schools	East Franklin Streetscape	Capital Construction	Total Nonmajor Governmental Funds
ASSETS				
Cash and investments	\$ -	\$ -	\$ 13,789	\$ 1,145,364
Intergovernmental receivable	131,140	190,000	-	337,057
Taxes receivable	-	-	-	57,900
Due from other funds	-	-	-	-
	<u>\$ 131,140</u>	<u>\$ 190,000</u>	<u>\$ 13,789</u>	<u>\$ 1,540,321</u>
LIABILITIES				
Accounts payable	\$ 129,857	\$ -	\$ -	\$ 135,064
Accrued liabilities	-	-	-	1,356
Due to other funds	1,283	190,000	-	207,200
Total liabilities	<u>131,140</u>	<u>190,000</u>	<u>-</u>	<u>343,620</u>
FUND BALANCE				
Restricted for:				
Capital improvements	-	-	13,789	13,789
Industrial development	-	-	-	21
Library operations	-	-	-	32,361
Public Safety	-	-	-	829,926
Tourism	-	-	-	320,604
Total fund balances	<u>-</u>	<u>-</u>	<u>13,789</u>	<u>1,196,701</u>
Total liabilities and fund equity	<u>\$ 131,140</u>	<u>\$ 190,000</u>	<u>\$ 13,789</u>	<u>\$ 1,540,321</u>

CITY OF HILLSBORO, TEXAS

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

FOR THE YEAR ENDED SEPTEMBER 30, 2012

	Special Revenue Funds			
	Hotel/Motel Tax	Search and Rescue Equipment Grant	Downtown Streetscape Phase II	Industrial Development
REVENUES				
Taxes	\$ 320,022	\$ -	\$ -	\$ -
Intergovernmental	-	75,063	3,212	-
Fines and forfeitures	-	-	-	-
Interest	153	-	-	-
Rentals	9,142	-	-	-
Contributions	-	-	-	-
Other	125	-	-	-
Total revenues	329,442	75,063	3,212	-
EXPENDITURES				
Current:				
Personnel	4,763	-	-	-
Services	197,771	-	-	-
Supplies	454	-	-	-
Maintenance	1,463	-	-	-
Minor equipment	-	1,453	-	-
Capital outlay	-	72,923	3,212	-
Debt service:				
Principal	20,000	-	-	-
Interest	11,550	-	-	-
Total expenditures	236,001	74,376	3,212	-
EXCESS (DEFICIENCY) OF REVENUES OVER (UNDER) EXPENDITURES	93,441	687	-	-
OTHER FINANCING SOURCES(USES)				
Operating transfers in	-	1,923	-	-
Operating transfers out	(21,000)	(2,610)	-	-
NET CHANGE IN FUND BALANCES	72,441	-	-	-
FUND BALANCES, BEGINNING	248,163	-	-	21
FUND BALANCES, ENDING	\$ 320,604	\$ -	\$ -	\$ 21

Special Revenue Funds

Library Special Fund	Home Buyers Assistance Grant	Parks and Wildlife Grant	Police Local Forfeiture	Police Federal Forfeiture	Police Special	Energy Grant
\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
-	400	390,851	-	-	-	-
-	-	-	248,014	-	-	-
-	-	-	5,937	32	-	-
-	-	-	-	-	-	-
2,500	-	-	-	-	1,204	-
-	-	851	-	-	-	-
<u>2,500</u>	<u>400</u>	<u>391,702</u>	<u>253,951</u>	<u>32</u>	<u>1,204</u>	<u>-</u>
-	-	-	50,406	-	-	-
-	400	-	6,032	-	225	-
-	-	-	10,000	-	899	-
-	-	-	12,109	3,561	-	-
-	-	-	8,365	8,568	500	-
-	-	652,771	59,694	13,378	-	-
-	-	-	32,919	-	-	-
-	-	-	9,997	-	-	-
<u>-</u>	<u>400</u>	<u>652,771</u>	<u>189,522</u>	<u>25,507</u>	<u>1,624</u>	<u>-</u>
<u>2,500</u>	<u>-</u>	<u>(261,069)</u>	<u>64,429</u>	<u>(25,475)</u>	<u>(420)</u>	<u>-</u>
-	-	261,069	-	-	-	-
<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
2,500	-	-	64,429	(25,475)	(420)	-
<u>29,861</u>	<u>-</u>	<u>-</u>	<u>735,196</u>	<u>52,168</u>	<u>4,028</u>	<u>-</u>
<u>\$ 32,361</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 799,625</u>	<u>\$ 26,693</u>	<u>\$ 3,608</u>	<u>\$ -</u>

CITY OF HILLSBORO, TEXAS
COMBINING STATEMENT OF REVENUES, EXPENDITURES
AND CHANGES IN FUND BALANCES
(continued)
FOR THE YEAR ENDED SEPTEMBER 30, 2012

	Special Revenue		Capital Projects	Total Nonmajor Governmental Funds
	Safe Route To Schools	East Franklin Streetscape	Capital Construction	
REVENUES				
Taxes	\$ -	\$ -	\$ -	\$ 320,022
Intergovernmental	218,329	158,463	-	846,318
Fines and forfeitures	-	-	-	248,014
Interest	-	-	25	6,147
Rentals	-	-	-	9,142
Contributions	-	-	-	3,704
Other	-	-	-	976
Total revenues	218,329	158,463	25	1,434,323
EXPENDITURES				
Current:				
Personnel	-	-	-	55,169
Services	-	-	-	204,428
Supplies	-	-	-	11,353
Maintenance	-	-	-	17,133
Minor equipment	-	-	-	18,886
Capital outlay	217,410	165,816	8,600	1,193,804
Debt service:				
Principal	-	-	-	52,919
Interest	-	-	-	21,547
Total expenditures	217,410	165,816	8,600	1,575,239
EXCESS (DEFICIENCY) OF REVENUES OVER (UNDER) EXPENDITURES	919	(7,353)	(8,575)	(140,916)
OTHER FINANCING SOURCES(USES)				
Operating transfers in	-	7,353	-	270,345
Operating transfers out	(919)	-	-	(24,529)
NET CHANGE IN FUND BALANCES	-	-	(8,575)	104,900
FUND BALANCES, BEGINNING	-	-	22,364	1,091,801
FUND BALANCES, ENDING	\$ -	\$ -	\$ 13,789	\$ 1,196,701

COMPLIANCE SECTION



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, 2012, which collectively comprise the City of Hillsboro, Texas basic financial statements and have issued our report thereon dated March 27, 2013. 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 *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented or detected and corrected on a timely basis.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, 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, the City Council, federal and state awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Patillo, Brown & Hill, L.L.P.

March 27, 2013

FEDERAL AWARDS SECTION



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

**INDEPENDENT AUDITORS' REPORT ON COMPLIANCE WITH REQUIREMENTS
THAT COULD HAVE A DIRECT AND MATERIAL EFFECT ON EACH MAJOR PROGRAM
AND ON INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH OMB
CIRCULAR A-133**

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

Compliance

We have audited the City of Hillsboro, Texas's (the "City's") compliance with the types of compliance requirements described in the *OMB Circular A-133, Compliance Supplement* that could have a direct and material effect on each of the City's major federal programs for the year ended September 30, 2012. 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 the financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments and Nonprofit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that 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 of the City's compliance with those requirements.

In our opinion, the City of Hillsboro, Texas complied, in all material respects, with the compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended September 30, 2012.

Internal Control Over Compliance

Management of the City of Hillsboro, Texas is responsible for establishing and maintaining effective internal control over compliance with the 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 the 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 and to test and report on internal control over compliance in accordance with OMB Circular A-133, 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 the City's internal control over compliance.

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. *A material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be deficiencies, 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.

The purpose of this report is solely to describe the scope of our testing of compliance with the types of compliance requirements applicable to each of the City's major programs and our testing of internal control over compliance and the results of our testing, and to provide an opinion on the City's compliance but not to provide an opinion on the effectiveness of the City's internal control over compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the City's compliance with requirements applicable to each major program and its internal control over compliance. Accordingly, this report is not suitable for any other purpose.

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

March 27, 2013

CITY OF HILLSBORO, TEXAS
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
YEAR ENDED SEPTEMBER 30, 2012

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-08-SP-TX-0531	\$ 3,212
Community Development Block Grant	14.246	B-09-SP-TX-0126	158,463
Community Development Block Grant	14.228	711259	274,979
Home Buyers Assistance Grant	14.239	M-08-SG-48-0100	400
Economic Development Initiative-Special Project, Neighborhood Initiative and Miscellaneous Grants	14.251	B-10-SP-TX-0102	<u>373,899</u>
Total U. S. Department of Housing and Urban Development			<u>810,953</u>
<u>U. S. Department of Justice</u>			
Direct Programs:			
American Recovery and Reinvestment Act Justice Assistance Grant	16.804	2009-SB-B9-2841	<u>14,000</u>
Total U. S. Department of Justice			<u>14,000</u>
<u>U. S. Department of Transportation</u>			
Passed through the Texas Department of Transportation :			
Federal-Aid Highway Program	20.205	CSJ#0909-37-051	<u>218,329</u>
Total U.S. Department of Transportation			<u>218,329</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	2009 SHSP	<u>75,063</u>
Total Passed through the Texas Office of the Governor -			<u>75,063</u>
Division of Emergency Management:			
Passed through the Texas Department of Public Safety -			
Division of Emergency Management:			
Disaster Grants - Public Assistance (FEMA - Fire Disaster)	97.036	DR-4029	<u>8,418</u>
Total Passed through the Texas Department of Public Safety -			<u>8,418</u>
Division of Emergency Management:			
Total U. S. Department of Homeland Security			<u>83,481</u>
Total Federal Awards			<u>\$ 1,126,763</u>

CITY OF HILLSBORO, TEXAS

NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

SEPTEMBER 30, 2012

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, 2012

Summary of Auditor's Results

Financial Statements:

Type of auditors' report issued Unqualified

Internal control over financial reporting:

Material weakness(es) identified? No

Significant deficiency(ies) identified? None reported

Noncompliance material to the financial statements noted?

None

Federal Awards:

Internal control over major programs:

Material weakness(es) identified? No

Significant deficiency(ies) identified? None reported

Type of auditors' report issued on compliance for major programs

Unqualified

Any audit findings disclosed that are required to be reported in accordance with Section 510(a) of OMB Circular A-133?

None

Indentification of major programs:

CFDA Number(s)

14.228

14.251

Name of Federal Program or Cluster:

Community Development Block Grant

Economic Development Initiative-Special Project, Neighborhood Initiative

Dollar threshold used to distinguish between Type A and Type B programs

\$300,000

Auditee qualified as a low-risk auditee?

The City was not classified as a low-risk auditee in the context of OMB Circular A-133.

Findings Relating to the Financial Statements Which are Required to be Reported in Accordance With Generally Accepted Government 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, 2012

None