

# **CITY OF TERRELL, TEXAS**

**ANNUAL FINANCIAL REPORT**

**SEPTEMBER 30, 2007**



**CITY OF TERRELL, TEXAS**

**TABLE OF CONTENTS**

**SEPTEMBER 30, 2007**

	<b><u>Page Number</u></b>
<b>INTRODUCTORY SECTION</b>	
Letter of Transmittal .....	i – iv
Organization Chart.....	v
Principal Officials .....	vi
<b>FINANCIAL SECTION</b>	
Independent Auditors’ Report.....	1 – 2
Management’s Discussion and Analysis .....	3 – 10
Basic Financial Statements	
Government-wide Financial Statements	
Statement of Net Assets .....	11
Statement of Activities.....	12 – 13
Fund Financial Statements	
Balance Sheet – Governmental Funds .....	14 – 15
Reconciliation of the Governmental Funds Balance Sheet to the Statement of Net Assets .....	16
Statement of Revenues, Expenditures and Changes in Fund Balances – Governmental Funds .....	17 – 18
Reconciliation of the Statement of Revenues, Expenditures and Changes in Fund Balances of Governmental Funds to the Statement of Activities.....	19

**(continued)**

**CITY OF TERRELL, TEXAS**

**TABLE OF CONTENTS  
(Continued)  
SEPTEMBER 30, 2007**

	<b><u>Page Number</u></b>
<b>FINANCIAL SECTION (Continued)</b>	
Fund Financial Statements (Continued)	
Statement of Revenues, Expenditures and Changes in Fund Balance – Budget and Actual – General Fund.....	20
Statement of Net Assets – Proprietary Funds .....	21
Statement of Revenues, Expenses and Changes in Fund Net Assets – Proprietary Funds .....	22
Statement of Cash Flows – Proprietary Funds.....	23 – 24
Notes to Financial Statements.....	25 – 45
Combining Statements	
Nonmajor Governmental Funds	
Combining Balance Sheet.....	46 – 47
Combining Statement of Revenues, Expenditures and Changes in Fund Balances .....	48 – 49
Internal Service Funds	
Combining Statement of Net Assets .....	50
Combining Statement of Revenues, Expenses and Changes in Fund Net Assets .....	51
Combining Statement of Cash Flows .....	52

**(continued)**

**CITY OF TERRELL, TEXAS**

**TABLE OF CONTENTS  
(Continued)  
SEPTEMBER 30, 2007**

**Page  
Number**

**SINGLE AUDIT SECTION**

Report on Compliance and on Internal Control Over Financial Reporting Based on an Audit of Financial Statements Performed in Accordance With <i>Government Auditing Standards</i> .....	53 –54
Report on Compliance With Requirements Applicable to Each Major Program and Internal Control Over Compliance in Accordance With OMB Circular A-133.....	55 – 56
Schedule of Expenditures of Federal Awards.....	57
Notes to the Schedule of Expenditures of Federal Awards .....	58
Schedule of Findings and Questioned Costs.....	59 – 63
Summary Schedule of Prior Audit Findings.....	64

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# **INTRODUCTORY SECTION**

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April 7, 2008

The Honorable Mayor and Members of the City Council  
City of Terrell  
Terrell, Texas

Hal Richards  
Mayor

The Finance Department and the City Manager's office are pleased to submit the basic financial statements for the City of Terrell, Texas (the "City") for the fiscal year ended September 30, 2007.

Ricky Jordan  
Mayor Pro tem

Jack Jones  
Deputy Mayor Pro tem

This report is published to provide the City Council, City staff, our citizens, our bondholders, and other interested parties with detailed information concerning the financial condition and activities of the City government. Responsibility for both the accuracy of the presented data and the completeness and fairness of the presentation, including all disclosures, rests with the City.

Jack Jones  
Deputy Mayor Pro tem

Tommy Spencer  
Council Member

To the best of our knowledge and belief, the enclosed data is accurate in all material respects and is organized in a manner designed to fairly present the financial position and results of the City as measured by the financial activity of its various funds and account groups. We also believe that all disclosures necessary to enable the reader to gain the maximum understanding of the City's financial affairs have been included.

Don Thurman  
Council Member

### **THE REPORT**

Torry L. Edwards  
City Manager

Michael Sims  
Assistant City Manager

This report is presented in three sections: Introductory, Financial and Single Audit. The introductory section includes this transmittal letter, a listing of the City officials, and an organizational chart of the City. The financial section includes Management's Discussion and Analysis (MD&A), basic financial statements and combining and individual fund statements and schedules, as well as the independent auditors' report on the basic financial statements. The MD&A is a narrative introduction, overview, and analysis to accompany the basic financial statements. This letter of transmittal is designed to complement the MD&A and should be read in conjunction with it. The City of Terrell's MD&A can be found immediately following the report of the independent auditors. The Single Audit section contains a schedule of federal expenditures and reports required by the Federal Single Audit Act of 1996.

The financial section described above is prepared in accordance with generally accepted accounting principles for governments as prescribed by the Governmental Accounting Standards Board (GASB) and other professional associations, as applicable.

P.O. BOX 310 • 201 E. Nash Street • Terrell, Texas 75160 • (972) 551-6600

The mission of the City Council of the City of Terrell, Texas, is to create pride by serving the community in a proactive manner and to enhance the quality of life through providing the highest level of services in the most efficient manner.

## **CITY PROFILE**

### **Location**

The City of Terrell, Texas is located on U. S. Highway 80 just north of Interstate 20, and approximately 32 miles east of Dallas, Texas. The City, encompassing approximately 18.6 square miles, had a 2000 census population of 13,600 which is a 9% increase from the 1990 census population of 12,490.

The City operates under the Council-Manager form of government. The City Council is comprised of the Mayor and four Council members, who enact local laws, determine policies and adopt the annual budget. The City Manager is appointed by the City Council and is responsible for the daily management of the City. The basic financial statements of the City include all government activities, organizations and functions for which the City is financially accountable as defined by the GASB. Based on these criteria, no other governmental organizations are included in this report.

### **Services Provided**

The City provides to its citizens those services that have proven to be necessary and meaningful and which the City at the least cost can provide. Major services provided under general government and enterprise functions are: police and fire protection, water and sewer services, sanitation services, park and recreational facilities, library services, street improvements and general administrative services. The City also offers an airport. Internal services of the City accounted for on a cost reimbursement basis, are the fleet services operations and employee health coverage.

### **Accounting System and Budgetary Control**

The City's accounting records for general governmental operations are maintained on a modified accrual basis, with the revenues being recorded when available and measurable and expenditures being recorded when the services or goods are received and the liabilities are incurred. Accounting records of the City's utilities and other proprietary activities are maintained on the accrual basis.

In developing and maintaining the City's accounting system, consideration is given to the adequacy of the internal control structure. Internal accounting controls are designed to provide reasonable, but not absolute, assurance regarding: (1) the safeguarding of assets against loss from unauthorized use or disposition; and (2) the reliability of financial records for preparing financial statements and maintaining accountability for assets. The concept of reasonable assurance recognizes that: (1) the cost of a control should not exceed the benefits likely to be derived; and (2) the evaluation of costs and benefits requires estimates and judgments by management.

All internal control evaluations occur within the above framework. We believe that the City's internal accounting controls adequately safeguard assets and provide reasonable assurance of proper recording of financial transactions.

The City charter provides that the City Council shall adopt the annual budget prepared by City Management. This budget is reviewed by the City Council and is formally adopted by the passage of a budget ordinance. The City Manager is authorized to transfer budgeted amounts between line items and departments within any fund; however, any revisions that alter the total expenditures of any fund must be approved by the City Council.

Budgetary control has been established at the individual fund level. Financial reports are produced showing budget and actual expenditures by line item, and are distributed monthly to City departmental and divisional management and to others upon request.

Individual line items are reviewed and analyzed for budgetary compliance. Personnel expenditures are monitored and controlled at a position level and capital expenditures (items over \$5,000 and having a useful life of three or more years) are monitored and controlled item by item. Revenue budgets are reviewed monthly.

## ECONOMIC OUTLOOK AND FINANCIAL CONDITION

The information presented in the financial statements is perhaps best understood when it is considered from the broader perspective of the specific environment within which the City operates.

Terrell has a diversified industrial base consisting of manufacturers, distributors, and processors.

Two institutions of higher education are located here. They are Southwestern Christian College and Trinity Valley Community College.

The City activity works with the Terrell Economic Development Corporation and local industries to encourage expansions and relations to our community. Land is available for development and the area has an abundant water supply. Incentives are also available to facilitate business expansions or relocations.

The outlook is encouraging with industrial, commercial, and residential development expected to continue. The potential for sustained development is present, and many people are working to promote positive economic growth.

Economic signs...

	ASSESSED PROPERTY VALUATIONS (in millions)	SALES TAX COLLECTIONS (in millions)
2000	\$ 506,373,987	\$ 5,468,815
2001	586,621,575	5,662,562
2002	603,618,789	5,756,021
2003	665,698,525	6,008,287
2004	727,025,258	6,595,836
2005	834,587,541	6,683,382
2006	894,542,447	7,002,351
2007	931,051,598	6,976,566

### Cash Management

The City awards its depository contract through official bidding procedures for a three-year period, with an option to extend the contract for an additional two years. The current depository contract with American National Bank expires September 30, 2010.

The City has a services-only contract, where a minimum amount of cash is held in interest bearing checking accounts to meet the City's operational needs. The remaining idle cash is invested by City officials in securities as allowed by Texas Statutes and by the City's investment policy.

At September 30, 2007, all idle cash totaling \$4,077,409 was invested in certificates of deposit. The overall portfolio provided \$594,522 in interest income during the year.

It is the City's policy that all demand deposits and time deposits are secured by pledged collateral with a market value equal to no less than 100% of the deposits less an amount insured by the FDIC. The Finance Department and a third party financial institution maintains evidence of the pledged collateral. Collateral is reviewed monthly to assure the market value of the securities pledged equals or exceeds the related bank balances.

All safekeeping arrangements are in accordance with a safekeeping agreement approved by the City Manager that clearly defines the procedural steps for gaining access to pledge collateral on deposits should the City of Terrell determine that the City's funds are in jeopardy. The safekeeping institution, or Custodian, is the Federal Home Loan Bank or an institution not affiliated with the firm pledging the collateral. The safekeeping agreement is a three-party contract between the City, the depository bank and the Federal Home Loan Bank as Custodian. The security is held in the name of the depository bank on behalf of the City. The original copy of all safekeeping statements is delivered to the City.

All collateral is subject to inspection and audit by the City Secretary and the City's independent auditors.

## **Risk Management**

### Property and Liability Plans

The City is exposed to various risks of loss related to torts; damage to, and destruction of assets; errors and omissions and natural disasters. A comprehensive insurance plan for property and casualty and general liability coverage has been established with the Texas Municipal League.

### Workers' Compensation Plan

The City is exposed to risk of loss due to injuries by employees while performing work-related duties. The City provides workers' compensation insurance coverage with the Texas Municipal League, which provides statutory coverage against potential losses.

### Health Plan

The City has established a self-insurance plan for health care benefits that pays 100% of employee claims limited to \$15,000 per employee and \$650,000 in aggregate. The City has insured claims in excess of plan limits.

## **INDEPENDENT AUDIT**

The City Charter requires an annual audit by independent certified public accountants. The accounting firm of Pattillo, Brown, & Hill, L.L.P. was selected by the City Council to perform the fiscal 2007 audit. In addition to meeting City Charter requirements, the audit also was designed to meet the requirements of the Federal Single Audit Act of 1996 and related OMB Circular A-133. The auditors' report on the basic financial statements is in the financial section.

## **ACKNOWLEDGEMENTS**

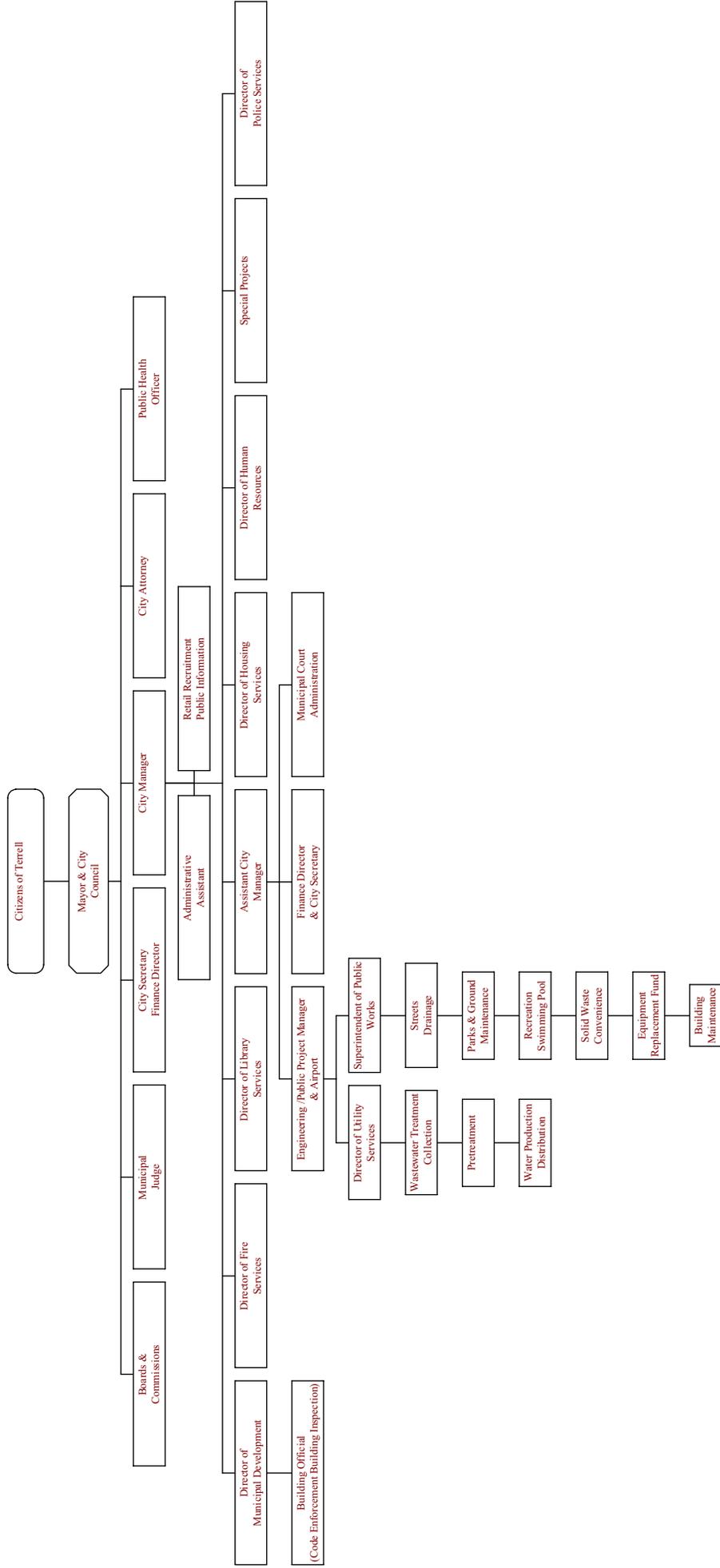
The preparation of this report could not be accomplished without the efficient and dedicated services of the entire staff of all City departments. We would like to express our appreciation to all members of the City's staff who assisted and contributed to its preparation. We would also like to thank the Mayor and City Council members for their interest and support in planning and conducting the financial operations of the City in a responsible and progressive manner.

Respectfully submitted,



John Rounsavall  
City Secretary

# City of Terrell Organizational Chart



**CITY OF TERRELL, TEXAS**

**PRINCIPAL OFFICIALS**

**SEPTEMBER 30, 2007**

**CITY OFFICIALS**

Mayor.....Hal Richards

Council Members..... Ricky Jordan, Mayor Pro-Tem

Jack Jones, Deputy Mayor Pro-Tem

Tommy Spencer

Don Thurman

City Manager ..... Torry Edwards

City Secretary..... John Rounsavall

City Attorney ..... Mary Gayle Ramsey

# **FINANCIAL SECTION**

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## INDEPENDENT AUDITORS' REPORT

To the Honorable City Council  
City of Terrell, 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 Terrell, Texas, as of and for the year ended September 30, 2007, 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 Terrell, Texas' management. Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the City of Terrell, Texas, as of September 30, 2007, and the respective changes in financial position, and, where applicable, cash flows 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 April 7, 2008, on our consideration of the City of Terrell, Texas' internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing and not to provide an opinion on 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.

The Management's Discussion and Analysis on pages 3 through 10 is not a required part of the basic financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the City of Terrell, Texas' basic financial statements. The introductory section, combining and individual nonmajor fund financial statements, and statistical section are presented for purposes of additional analysis and are not a required part of the basic 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 Nonprofit Organizations*, and is also not a required part of the basic financial statements of the City of Terrell, Texas. The combining and individual nonmajor fund financial statements and the Schedule of Expenditures of Federal Awards have been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, are fairly stated in all material respects in relation to the basic financial statements taken as a whole. The introductory and statistical sections have not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we express no opinion on them.

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

April 7, 2008

**MANAGEMENT'S  
DISCUSSION AND ANALYSIS**

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## **Management's Discussion and Analysis**

As management of the City of Terrell, we offer readers of the City's financial statements this narrative overview and analysis of the financial activities for the fiscal year ended September 30, 2007. This discussion and analysis is designed to (a) assist the reader in focusing on significant financial issues, (b) provide an overview of the City's financial activity, (c) identify changes in the City's financial position (its ability to address the next and subsequent years' challenges), (d) identify any material deviations from the financial plan (the approved budget); and (e) identify individual fund issues or concerns. We encourage readers to consider the information presented here in conjunction with additional information that we have furnished in our letter of transmittal, which can be found on pages i – iv of this report.

### **FINANCIAL HIGHLIGHTS**

- The assets of the City of Terrell exceeded its liabilities at the close of the most recent fiscal year by \$47,549,286 (net assets). Of this amount, \$10,801,075 (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 \$3,807,091 from operations. However, governmental capital assets decreased by \$1,277,337 as a result of a capital asset inventory. The net effect was an overall increase in net assets of \$2,529,754.
- As of the close of the current fiscal year, the City of Terrell's governmental funds reported combined ending fund balances of \$11,852,561, a decrease of \$3,482,382 in comparison with the prior fiscal year, due to adding an IT Department and Special Projects Department to the General Fund. Approximately 43% of this total amount, \$4,996,954, is available for spending at the City's discretion (unreserved fund balance).
- At the end of the current fiscal year, unreserved fund balance for the General Fund was \$3,166,156 or 21% of the total General Fund expenditures.
- The City's total long-term debt increased by \$1,253,159 during the current fiscal year. The key factor in this increase was the issuance of the 2007A and B Certificates of Obligation issued for both governmental and business-type activities.

### **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 are comprised of 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 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 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 the future fiscal periods (e.g., uncollected taxes earned but unused and 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 costs through user fees (business-type activities).

- Governmental activities include general government and administration, public safety, library, and parks and recreation.
- Business-type activities include the City's water and sewer system and airport operations. Charges for services covers all or most of the cost for these services.

The government-wide financial statements can be found on pages 11– 13 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. Fund accounting is used by state and local governments to control and manage money for particular purposes and to ensure finance-related legal requirements. The City uses two fund types – governmental and proprietary.

- **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 funds balance sheet and the governmental funds statements of revenues, expenditures, and changes in fund balances provide a reconciliation to facilitate this comparison between governmental funds and governmental activities.

The City maintains 15 governmental funds. Information is presented separately in the governmental fund balance sheet and in the governmental fund statement of revenues, expenditures and changes in fund balances for the General Fund, Section 8 Rent Supplement Fund, Terrell Economic Development Corporation Fund, the C. O. Tax and Revenue Series 2004 Fund, and the 2007A Bond Fund, each of which are considered to be major funds. Data from the other 10 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 statements elsewhere in this report.

The basic governmental funds financial statements can be found on pages 14 – 20 of this report.

- **Proprietary funds** – The City maintains two types of proprietary funds. Enterprise Funds are used to report the same functions presented as business-type activities in the government-wide financial statements. The City uses Enterprise Funds to account for its water and sewer utility and airport services. Internal Service Funds are an accounting device used to accumulate and allocate costs internally among the City’s various functions. The City uses its Internal Service Funds to account for its fleet services and self-insurance self funded health insurance. Because these services predominantly benefit governmental rather than business-type functions, it is included within governmental activities in the government-wide financial statements.

Proprietary funds provide the same type of information as the government-wide financial statements, only in more detail. The proprietary fund financial statements provide separate information for the Water and Sewer Utility, and Airport Funds since they are considered to be major funds of the City. All Internal Service Funds are combined into a single aggregated presentation in the proprietary fund financial statements. Individual fund data for the Internal Service Funds is provided in the form of combining statements elsewhere in this report.

The fund financial statements can be found on pages 21 – 24 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 25 – 45 of this report.

### **Other Information**

The combining statements referred to earlier in connection with nonmajor governmental funds and Internal Service Funds are presented following the notes to the financial statements. Combining and individual statements and schedules can be found on pages 46 – 52 of this report.

## GOVERNMENT-WIDE FINANCIAL ANALYSIS

As noted earlier, net assets may serve over time as a useful indicator of the City's financial position. In the case of the City of Terrell, assets exceeded liabilities by \$47,549,286 as of September 30, 2007.

The largest portion of the City's net assets, 65% (\$31,022,516), reflects its investments in capital assets (e.g., land, building, equipment, improvements, construction in progress and infrastructure), less any debt used to acquire those assets that are still outstanding. The City uses these capital assets to provide service 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.

### CITY OF TERRELL'S NET ASSETS

	Governmental Activities		Business-type Activities		Totals	
	2007	2006	2007	2006	2007	2006
Current and other assets	\$ 15,581,449	\$ 18,063,802	\$ 7,987,014	\$ 4,838,546	\$ 23,568,463	\$ 22,902,348
Capital assets	23,352,440	20,617,483	29,948,303	29,220,174	53,300,743	49,837,657
Total assets	<u>38,933,889</u>	<u>38,681,285</u>	<u>37,935,317</u>	<u>34,058,720</u>	<u>76,869,206</u>	<u>72,740,005</u>
Long-term liabilities	22,667,363	23,301,947	4,016,720	2,128,977	26,684,083	25,430,924
Other liabilities	1,857,030	1,277,225	778,807	1,012,324	2,635,837	2,289,549
Total liabilities	<u>24,524,393</u>	<u>24,579,172</u>	<u>4,795,527</u>	<u>3,141,301</u>	<u>29,319,920</u>	<u>27,720,473</u>
Net assets:						
Invested in capital assets, net of related debt	4,983,572	( 1,647,319)	26,038,944	27,150,174	31,022,516	25,502,855
Restricted	5,144,276	9,647,430	581,419	216,747	5,725,695	9,864,177
Unrestricted	<u>4,281,648</u>	<u>6,102,002</u>	<u>6,519,427</u>	<u>3,550,498</u>	<u>10,801,075</u>	<u>9,652,500</u>
Total net assets	<u>\$ 14,409,496</u>	<u>\$ 14,102,113</u>	<u>\$ 33,139,790</u>	<u>\$ 30,917,419</u>	<u>\$ 47,549,286</u>	<u>\$ 45,019,532</u>

## Analysis of the City's Operations

The following table provides a summary of the City's operations for the years ended September 30, 2007 and 2006.

### CITY OF TERRELL'S CHANGES IN NET ASSETS

	Governmental Activities		Business-type Activities		Totals	
	2007	2006	2007	2006	2007	2006
Revenues:						
Program revenues:						
Charges for services	\$ 1,825,401	\$ 2,232,819	\$ 8,086,274	\$ 7,739,591	\$ 9,911,675	\$ 9,972,410
Operating grants and contributions	3,600,975	4,663,465	-	-	3,600,975	4,663,465
Capital grants and contributions	-	-	245,000	-	245,000	-
General revenues:						
Property taxes	5,859,100	5,493,214	-	-	5,859,100	5,493,214
Franchise taxes	1,531,938	1,726,828	-	-	1,531,938	1,726,828
Sales taxes	6,976,566	7,002,351	-	-	6,976,566	7,002,351
Other taxes	228,328	235,195	-	-	228,328	235,195
Interest	457,236	278,335	156,029	66,492	613,265	344,827
Miscellaneous	214,368	284,098	878,893	379,325	1,093,261	663,423
Transfers	945,546	-	(945,546)	-	-	-
Total revenues	<u>21,639,458</u>	<u>21,916,305</u>	<u>8,420,650</u>	<u>8,185,408</u>	<u>30,060,108</u>	<u>30,101,713</u>
Expenses:						
General government	6,790,406	5,896,460	-	-	6,790,406	5,896,460
Public safety	5,878,397	6,103,070	-	-	5,878,397	6,103,070
Streets	2,583,474	2,671,672	-	-	2,583,474	2,671,672
Sanitation	502,139	502,107	-	-	502,139	502,107
Culture and recreation	613,304	709,433	-	-	613,304	709,433
Public welfare	2,782,861	3,733,149	-	-	2,782,861	3,733,149
Interest on long-term debt	904,157	920,357	5,810,696	-	6,714,853	920,357
Water and sewer	-	-	-	6,669,564	-	6,669,564
Airport	-	-	387,583	380,248	387,583	380,248
Total expenses	<u>20,054,738</u>	<u>20,536,248</u>	<u>6,198,279</u>	<u>7,049,812</u>	<u>26,253,017</u>	<u>27,586,060</u>
Change in net assets	1,584,720	1,380,057	2,222,371	1,135,596	3,807,091	2,515,653
Net assets, beginning	14,102,113	12,722,056	30,917,419	29,781,823	45,019,532	42,503,879
Prior period adjustment	(1,277,337)	-	-	-	(1,277,337)	-
Net assets, ending	<u>\$ 14,409,496</u>	<u>\$ 14,102,113</u>	<u>\$ 33,139,790</u>	<u>\$ 30,917,419</u>	<u>\$ 47,549,286</u>	<u>\$ 45,019,532</u>

**Governmental activities.** Of the City's \$2,529,754 overall increase in net assets, governmental activities net assets increased by \$307,383. The most significant governmental expense for the City was general government, which incurred expenses of \$6,790,406. These expenses were funded by revenues collected from a variety of sources, with the largest being from sales taxes, which are \$6,976,566 for the fiscal year ended September 30, 2007. Other significant governmental expenses for the City include public safety, which incurred \$5,878,397 in expenses.

**Business-type activities.** Business-type activities increased the City's net assets by \$2,222,371.

## **FINANCIAL ANALYSIS OF THE GOVERNMENT'S FUNDS**

### **Governmental Funds**

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

At the end of the current fiscal year, the City of Terrell's governmental funds reported combined ending fund balances of \$11,852,561. Approximately 42% of this total amount (\$4,996,954) constitutes unreserved fund balance. The remainder of the fund balance is reserved to indicate that it is not available for new spending because it has already been committed to (1) pay for capital projects (\$4,759,991), (2) pay for debt service (\$413,319), (3) pay for investments held for resale (\$1,391,667), and (4) other miscellaneous reservations (\$290,632).

In the General Fund, the City budgeted for a decrease in the fund balance of \$3,103,183. Actual expenditures being less than budgeted, the actual fund balance decreased for fiscal year 2007 by \$1,817,778.

### **Proprietary Funds**

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

Net assets of the respective proprietary funds are the Water and Sewer Fund, \$24,847,767; and the Airport Fund, \$8,292,023. The Water and Sewer Fund's net assets increased in 2007 by \$2,256,842 and the Airport's net assets decreased by \$34,471.

### **General Fund Budgetary Highlights**

The City made revisions to the original appropriations approved by the City Council. Overall, these changes resulted in an increase of budgeted General Fund expenditures from the original budget of \$1,145,482.

The City had budgeted for little or no increase in most revenue categories from the prior year collections based on economic conditions. However, actual revenues were greater than the budgeted revenue amount by \$431,058.

## **CAPITAL ASSETS**

The City of Terrell's investment in capital assets for its governmental and business-type activities as of September 30, 2007, amounts to \$53,300,743 (net of accumulated depreciation). This investment in capital assets includes land, building, equipment, improvements, infrastructure and construction in progress.

More capital asset events during the current fiscal year included the following:

- \$257,478 was spent on land to be used for governmental purposes;
- \$4,614,529 was completed on various governmental and business-type construction projects that continue to be in progress; and
- \$958,972 was spent on the completed NTMWD transmission line and pump station.

**CITY OF TERRELL'S CAPITAL ASSETS AT YEAR-END  
Net of Accumulated Depreciation**

	Governmental Activities		Business-type Activities		Totals	
	2007	2006	2007	2006	2007	2006
Land	\$ 718,000	\$ 665,035	\$ 885,019	\$ 885,019	\$ 1,603,019	\$ 1,550,054
Buildings and improvements	2,350,502	2,450,152	5,333,304	7,551,053	7,683,806	10,001,205
Machinery and equipment	1,946,151	2,381,161	21,366,248	16,775,096	23,312,399	19,156,257
Infrastructure	12,402,780	13,198,741	-	-	12,402,780	13,198,741
Construction in progress	5,935,007	1,922,394	2,363,732	4,009,006	8,298,739	5,931,400
Total capital assets	\$ 23,352,440	\$ 20,617,483	\$ 29,948,303	\$ 29,220,174	\$ 53,300,743	\$ 49,837,657

The City had a capital asset inventory completed during the 2007 fiscal year. This caused the City to make a prior period adjustment to reduce capital assets by \$1,063,949. Additional information on the City of Terrell's capital assets can be found in Note 4 on pages 37 – 38 of this report.

**DEBT ADMINISTRATION**

At the end of the current fiscal year, the City of Terrell had a total bonded debt of \$21,400,000. Of this amount, \$20,800,000 comprises bonded debt backed by the combination of property tax and water/sewer revenues and \$600,000 represents bonds secured solely by water and sewer revenues.

**CITY OF TERRELL'S OUTSTANDING DEBT AT YEAR-END**

	Governmental Activities		Business-type Activities		Totals	
	2007	2006	2007	2006	2007	2006
General obligation bonds	\$ 2,710,000	\$ 3,095,000	\$ -	\$ -	\$ 2,710,000	\$ 3,095,000
Certificates of obligation	14,730,000	13,685,000	3,360,000	1,385,000	18,090,000	15,070,000
Revenue bonds payable	-	-	600,000	685,000	600,000	685,000
	\$ 17,440,000	\$ 16,780,000	\$ 3,960,000	\$ 2,070,000	\$ 21,400,000	\$ 18,850,000

During the current fiscal year, the City's total bonded debt increased by \$2,550,000 or 14%. The main reason for the increase was the 2007A and 2007B in the amount of \$4,060,000.

The City's bond ratings are listed below:

	<u>Moody's Investors Service</u>	<u>Standard &amp; Poor's</u>
General Obligation Bonds	Aaa	AA
Revenue Bonds	Aaa	AA

Several of the City's bonds are insured, thus holding a Triple A credit rating from both Moody's and Standard & Poor's. Additional information on the City of Terrell's long-term debt can be found in Note 4 on pages 40 – 42 of this report.

### **ECONOMIC FACTORS AND NEXT YEAR'S BUDGET AND RATES**

In the fiscal year 2007-08 budget, General Fund revenues and transfers in are budgeted to decrease by 5% from the 2006-07 budget year, with sales taxes making up about 45% of General Fund budgeted revenues and transfers in. Certified assessed valuations increased 5% over the preceding year. The tax base has increased by a strong annual average of 5% over the past five years. The City's budgets for all funds have benefited from an expanding local economy. However, the City's 2007-08 budget reflects a slower recovery in economic growth. The City of Terrell's favorable location continues to attract distribution firms and residential development. The City has imposed an impact fee for single-family housing developments. Sales tax receipts increased less than 1% for fiscal year 2006-07 and appears to continue to show signs of a marginal increase during the 2007-08 fiscal year. However, this revenue source is the most volatile and sensitive to changes in the local economy.

The budget for 2007-08 reflects the allocation of resources necessary to continue projects and operations at approximately the same level as last year.

### **REQUESTS FOR INFORMATION**

The financial report is designed to provide our citizens, customers, investors and creditors with a general overview of the City's finances. If you have questions about this report or need any additional information, contact the Office of the City Secretary/Finance Director John Rounsavall at (972) 551-6600 or email [jrounsavall@cityofterrell.org](mailto:jrounsavall@cityofterrell.org).

**BASIC  
FINANCIAL STATEMENTS**

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# CITY OF TERRELL, TEXAS

## STATEMENT OF NET ASSETS

SEPTEMBER 30, 2007

	Governmental Activities	Business-type Activities	Total
<b>ASSETS</b>			
Cash and investments	\$ 11,650,697	\$ 5,686,349	\$ 17,337,046
Receivables (net, where applicable, of allowances for uncollectibles)	1,641,303	1,465,328	3,106,631
Internal balances	34,857	( 34,857)	-
Due from other governments	14,089	105,075	119,164
Special assessments	739,137	-	739,137
Investment in land	1,391,667	-	1,391,667
Inventory, at cost	12,890	107,262	120,152
Restricted cash and investments	27,000	581,419	608,419
Deferred charges	69,809	76,438	146,247
Capital assets:			
Land	718,000	885,019	1,603,019
Buildings and improvements	3,414,764	16,722,695	20,137,459
Improvements other than buildings	1,091,550	-	1,091,550
Machinery and equipment	4,517,226	29,685,421	34,202,647
Infrastructure	31,838,431	-	31,838,431
Construction in progress	5,935,007	2,363,732	8,298,739
Less accumulated depreciation	( 24,162,538)	( 19,708,564)	( 43,871,102)
Total capital assets	<u>23,352,440</u>	<u>29,948,303</u>	<u>53,300,743</u>
Total assets	<u>38,933,889</u>	<u>37,935,317</u>	<u>76,869,206</u>
<b>LIABILITIES</b>			
Accounts payable	1,298,522	399,565	1,698,087
Accrued interest payable	106,992	12,780	119,772
Other accrued liabilities	197,062	39,516	236,578
Customer deposits	-	301,336	301,336
Due to other governments	254,454	25,610	280,064
Long-term liabilities:			
Due within one year	2,272,139	301,344	2,573,483
Due in more than one year	20,395,224	3,715,376	24,110,600
Total liabilities	<u>24,524,393</u>	<u>4,795,527</u>	<u>29,319,920</u>
<b>NET ASSETS</b>			
Invested in capital assets, net of related debt	4,983,572	26,038,944	31,022,516
Restricted for:			
Economic development	2,787,054	-	2,787,054
Debt service	414,409	581,419	995,828
Capital projects	1,652,183	-	1,652,183
Other purposes	290,630	-	290,630
Unrestricted	<u>4,281,648</u>	<u>6,519,427</u>	<u>10,801,075</u>
Total net assets	<u>\$ 14,409,496</u>	<u>\$ 33,139,790</u>	<u>\$ 47,549,286</u>

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

**CITY OF TERRELL, TEXAS**  
**STATEMENT OF ACTIVITIES**  
**FOR THE YEAR ENDED SEPTEMBER 30, 2007**

Functions/Programs	Expenses	Program Revenue		
		Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions
<b>Primary government</b>				
Governmental activities:				
General government	\$ 6,790,406	\$ 202,494	\$ 391,416	\$ -
Public welfare	2,782,861	-	3,203,644	-
Public safety	5,878,397	785,552	5,915	-
Highways and streets	2,583,474	171,674	-	-
Sanitation	502,139	533,430	-	-
Culture and recreation	613,304	132,251	-	-
Interest on long-term debt	904,157	-	-	-
Total governmental activities	<u>20,054,738</u>	<u>1,825,401</u>	<u>3,600,975</u>	<u>-</u>
Business-type activities:				
Water and sewer	5,810,696	7,769,569	-	245,000
Airport	387,583	316,705	-	-
Total business-type activities	<u>6,198,279</u>	<u>8,086,274</u>	<u>-</u>	<u>245,000</u>
Total primary government	<u>\$ 26,253,017</u>	<u>\$ 9,911,675</u>	<u>\$ 3,600,975</u>	<u>\$ 245,000</u>

**General revenues:**

Taxes:  
Property taxes, levied for general purposes  
Property taxes, levied for debt service  
Sales taxes  
Franchise taxes  
Other taxes  
Unrestricted investment earnings  
Miscellaneous  
Transfers  
Total general revenues and transfers  
Change in net assets  
Net assets - beginning  
Prior period adjustment  
Net assets - ending

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

Net (Expense) Revenue and Changes in Net Assets		
Primary Government		
Governmental Activities	Business-type Activities	Total
\$( 6,196,496)	\$ -	\$( 6,196,496)
420,783	-	420,783
( 5,086,930)	-	( 5,086,930)
( 2,411,800)	-	( 2,411,800)
31,291	-	31,291
( 481,053)	-	( 481,053)
( 904,157)	-	( 904,157)
<u>( 14,628,362)</u>	<u>-</u>	<u>( 14,628,362)</u>
-	2,203,873	2,203,873
<u>-</u>	<u>( 70,878)</u>	<u>( 70,878)</u>
<u>-</u>	<u>2,132,995</u>	<u>2,132,995</u>
<u>-</u>	<u>2,132,995</u>	<u>2,132,995</u>
4,226,831	-	4,226,831
1,632,269	-	1,632,269
6,976,566	-	6,976,566
1,531,938	-	1,531,938
228,328	-	228,328
457,236	156,029	613,265
214,368	878,893	1,093,261
945,546	<u>( 945,546)</u>	<u>-</u>
<u>16,213,082</u>	<u>89,376</u>	<u>16,302,458</u>
1,584,720	2,222,371	3,807,091
14,102,113	30,917,419	45,019,532
<u>( 1,277,337)</u>	<u>-</u>	<u>( 1,277,337)</u>
<u>\$ 14,409,496</u>	<u>\$ 33,139,790</u>	<u>\$ 47,549,286</u>

**CITY OF TERRELL, TEXAS**

**BALANCE SHEET**

**GOVERNMENTAL FUNDS**

**SEPTEMBER 30, 2007**

	<u>General</u>	<u>Rent Supplement Section 8</u>	<u>Terrell Economic Development Corporation</u>
<b>ASSETS</b>			
Cash and investments	\$ 2,688,559	\$ 580,482	\$ 1,450,215
Taxes receivable, net	1,528,905	-	-
Due from other funds	212,850	-	37,688
Receivable from other governments	-	-	-
Special assessments	-	-	-
Investment in land	-	-	1,391,667
Inventories	<u>12,890</u>	<u>-</u>	<u>-</u>
 Total assets	 <u>\$ 4,443,204</u>	 <u>\$ 580,482</u>	 <u>\$ 2,879,570</u>
<b>LIABILITIES AND FUND BALANCES</b>			
Liabilities:			
Accounts payable	\$ 489,108	\$ 3,053	\$ 38,374
Accrued wages payable	193,483	-	-
Due to other funds	48,090	23,826	54,142
Due to other governments	254,454	-	-
Deferred revenue	<u>291,913</u>	<u>-</u>	<u>-</u>
Total liabilities	<u>1,277,048</u>	<u>26,879</u>	<u>92,516</u>
Fund balances:			
Reserved for:			
Debt service	-	-	-
Grants/donations	-	-	-
Capital projects	-	-	1,391,667
Housing assistance	-	290,632	-
Unreserved	<u>3,166,156</u>	<u>262,971</u>	<u>1,395,387</u>
Total fund balances	<u>3,166,156</u>	<u>553,603</u>	<u>2,787,054</u>
 Total liabilities and fund balances	 <u>\$ 4,443,204</u>	 <u>\$ 580,482</u>	 <u>\$ 2,879,570</u>

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

Certificates of Obligation Tax and Revenue Series 2004	2007A Bond	Other Governmental Funds	Total Governmental Funds
\$ 1,797,571	\$ 1,894,111	\$ 2,400,995	\$ 10,811,933
-	-	112,398	1,641,303
-	-	54,143	304,681
-	-	14,089	14,089
-	-	739,137	739,137
-	-	-	1,391,667
-	-	-	12,890
<u>\$ 1,797,571</u>	<u>\$ 1,894,111</u>	<u>\$ 3,320,762</u>	<u>\$ 14,915,700</u>
\$ 555,635	\$ 28,239	\$ 91,837	\$ 1,206,246
-	-	-	193,483
-	-	143,766	269,824
-	-	-	254,454
-	-	847,219	1,139,132
<u>555,635</u>	<u>28,239</u>	<u>1,082,822</u>	<u>3,063,139</u>
-	-	413,319	413,319
-	-	( 2)	( 2)
1,241,936	1,865,872	1,652,183	6,151,658
-	-	-	290,632
-	-	172,440	4,996,954
<u>1,241,936</u>	<u>1,865,872</u>	<u>2,237,940</u>	<u>11,852,561</u>
<u>\$ 1,797,571</u>	<u>\$ 1,894,111</u>	<u>\$ 3,320,762</u>	<u>\$ 14,915,700</u>

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## CITY OF TERRELL, TEXAS

### RECONCILIATION OF THE GOVERNMENTAL FUNDS BALANCE SHEET TO THE STATEMENT OF NET ASSETS

SEPTEMBER 30, 2007

Total fund balance, governmental funds	\$ 11,852,561
Amounts reported for governmental activities in the Statement of Net Assets are different because:	
Capital assets used in governmental activities are not current financial resources and therefore are not reported in this fund financial statement, but are reported in the governmental activities of the Statement of Net Assets.	21,685,137
Certain other long-term assets are not available to pay current period expenditures and therefore are not reported in this fund financial statement, but are reported in the governmental activities of the Statement of Net Assets.	1,139,132
The assets and liabilities of certain Internal Service Funds are not included in the fund financial statement, but are included in the governmental activities of the Statement of Net Assets.	2,429,535
Some liabilities, (such as notes payable, long-term compensated absences, and bonds payable), are not due and payable in the current period and are not included in the fund financial statement, but are included in the governmental activities of the Statement of Net Assets.	<u>( 22,696,869)</u>
Net assets of governmental activities in the Statement of Net Assets	\$ <u>14,409,496</u>

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

**CITY OF TERRELL, TEXAS**

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

**GOVERNMENTAL FUNDS**

**FOR THE YEAR ENDED SEPTEMBER 30, 2007**

	<u>General</u>	<u>Rent Supplement Section 8</u>	<u>Terrell Economic Development Corporation</u>
<b>REVENUES</b>			
Taxes and special assessments	\$ 12,732,345	\$ -	\$ -
Licenses and permits	139,341	-	-
Hotel/motel occupancy taxes	-	-	-
Fees and fines	342,762	-	-
Intergovernmental	362,516	3,106,083	-
Charges for services	610,579	-	14,200
Investment earnings	137,261	17,720	45,045
Street assessments	-	-	-
Miscellaneous	<u>241,009</u>	<u>12,776</u>	<u>-</u>
Total revenues	<u>14,565,813</u>	<u>3,136,579</u>	<u>59,245</u>
<b>EXPENDITURES</b>			
Current:			
General government	5,156,245	287,018	409,417
Public welfare	-	2,728,629	-
Public safety	5,815,122	-	-
Highways and streets	1,872,346	-	-
Sanitation	502,139	-	-
Culture and recreation	568,295	-	-
Principal	339,316	-	731,121
Interest and other charges	36,522	-	150,833
Capital outlay	<u>847,295</u>	<u>-</u>	<u>50,874</u>
Total expenditures	<u>15,137,280</u>	<u>3,015,647</u>	<u>1,342,245</u>
<b>EXCESS (DEFICIENCY) OF REVENUES OVER EXPENDITURES</b>	<u>( 571,467)</u>	<u>120,932</u>	<u>( 1,283,000)</u>
<b>OTHER FINANCING SOURCES (USES)</b>			
Proceeds from long-term debt	-	-	-
Gain on sale of capital assets	69	-	86,382
Transfers in	500,000	-	1,770,754
Transfers out	<u>( 1,746,380)</u>	<u>-</u>	<u>-</u>
Total other financing sources and uses	<u>( 1,246,311)</u>	<u>-</u>	<u>1,857,136</u>
<b>NET CHANGE IN FUND BALANCES</b>	<u>( 1,817,778)</u>	<u>120,932</u>	<u>574,136</u>
<b>FUND BALANCES, BEGINNING</b>	5,197,322	432,671	2,212,918
<b>PRIOR PERIOD ADJUSTMENT</b>	<u>( 213,388)</u>	<u>-</u>	<u>-</u>
<b>FUND BALANCES, ENDING</b>	<u>\$ 3,166,156</u>	<u>\$ 553,603</u>	<u>\$ 2,787,054</u>

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

Certificates of Obligation Tax and Revenue Series 2004	2007 A Bond	Other Governmental Funds	Total Governmental Funds
\$ -	\$ -	\$ 1,627,388	\$ 14,359,733
-	-	-	139,341
-	-	216,608	216,608
-	-	-	342,762
-	-	198,529	3,667,128
-	-	165,549	790,328
111,837	27,835	98,795	438,493
-	-	26,125	26,125
-	-	-	253,785
<u>111,837</u>	<u>27,835</u>	<u>2,332,994</u>	<u>20,234,303</u>
-	164,963	269,526	6,287,169
-	-	54,232	2,782,861
-	-	-	5,815,122
-	-	-	1,872,346
-	-	-	502,139
-	-	-	568,295
-	-	1,370,000	2,440,437
-	27,000	650,950	865,305
<u>4,533,451</u>	<u>-</u>	<u>-</u>	<u>5,431,620</u>
<u>4,533,451</u>	<u>191,963</u>	<u>2,344,708</u>	<u>26,565,294</u>
( 4,421,614)	( 164,128)	( 11,714)	( 6,330,991)
-	2,030,000	-	2,030,000
-	-	-	86,451
-	-	461,730	2,732,484
<u>-</u>	<u>-</u>	<u>( 40,558)</u>	<u>( 1,786,938)</u>
<u>-</u>	<u>2,030,000</u>	<u>421,172</u>	<u>3,061,997</u>
( 4,421,614)	1,865,872	409,458	( 3,268,994)
5,663,550	-	1,828,482	15,334,943
<u>-</u>	<u>-</u>	<u>-</u>	<u>( 213,388)</u>
<u>\$ 1,241,936</u>	<u>\$ 1,865,872</u>	<u>\$ 2,237,940</u>	<u>\$ 11,852,561</u>

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## CITY OF TERRELL, TEXAS

### RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES OF GOVERNMENTAL FUNDS TO THE STATEMENT OF ACTIVITIES

FOR THE YEAR ENDED SEPTEMBER 30, 2007

Net change in fund balances - total governmental funds: \$( 3,268,994)

Amounts reported for governmental activities in the Statement of Activities are different because:

Governmental funds report outlays for capital assets as expenditures because such outlays use current financial resources. In contrast, the Statement of Activities reports only a portion of the outlay as expense. The outlay is allocated over the assets' estimated useful lives as depreciation expense for the period. This is the amount by which capital outlays exceeded depreciation in the current period. 4,108,386

Governmental funds do not present revenues that are not available to pay current obligations. In contrast, such revenues are reported in the Statement of Activities when earned. 105,299

Governmental funds report bond proceeds as current financial resources. In contrast, the Statement of Activities treats such issuance of debt as a liability. Governmental funds report repayment of bond principal as an expenditure, In contrast, the Statement of Activities treats such repayments as a reduction in long-term liabilities. This is the amount by which proceeds exceeded repayments. 410,437

Some expenses reported in the Statement of Activities do not require the use of current financial resources and these are not reported as expenditures in governmental funds ( 204,979)

Internal Service Funds are used by management to charge the costs of certain activities, such as equipment maintenance and self-insurance, to individual funds. The net revenue (expense) of certain Internal Service Funds is reported with governmental activities. 434,571

Change in net assets of governmental activities \$ 1,584,720

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

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**CITY OF TERRELL, TEXAS**

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

**GENERAL FUND**

**FOR THE YEAR ENDED SEPTEMBER 30, 2007**

	<u>Budgeted Amounts</u>		<u>Actual Amounts, Budgetary Basis</u>	<u>Variance with Final Budget Positive (Negative)</u>
	<u>Original</u>	<u>Final</u>		
<b>REVENUES</b>				
Property taxes	\$ 4,239,354	\$ 4,239,354	\$ 4,212,121	\$( 27,233)
Sales and miscellaneous taxes	8,199,000	8,199,000	8,520,224	321,224
Fees and fines	389,000	389,000	342,762	( 46,238)
Licenses and permits	206,700	206,700	139,341	( 67,359)
Intergovernmental	403,515	410,911	362,516	( 48,395)
Charges for services	493,160	493,160	610,579	117,419
Investment earnings	55,000	55,000	137,261	82,261
Miscellaneous	<u>243,130</u>	<u>141,630</u>	<u>241,009</u>	<u>99,379</u>
Total revenues	<u>14,228,859</u>	<u>14,134,755</u>	<u>14,565,813</u>	<u>431,058</u>
<b>EXPENDITURES</b>				
Current:				
General government	5,341,053	5,687,085	5,156,245	530,840
Public safety	5,803,301	6,311,686	5,815,122	496,564
Highways and street	1,867,682	1,991,589	1,872,346	119,243
Sanitation	498,549	498,549	502,139	( 3,590)
Culture and recreation	598,858	766,016	568,295	197,721
Debt service:				
Principal	133,350	133,350	339,316	( 205,966)
Interest and other charges	-	-	36,522	( 36,522)
Capital outlay	<u>673,164</u>	<u>673,164</u>	<u>847,295</u>	<u>( 174,131)</u>
Total expenditures	<u>14,915,957</u>	<u>16,061,439</u>	<u>15,137,280</u>	<u>924,159</u>
<b>EXCESS (DEFICIENCY) OF REVENUES OVER EXPENDITURES</b>	<u>( 687,098)</u>	<u>( 1,926,684)</u>	<u>( 571,467)</u>	<u>1,355,217</u>
<b>OTHER FINANCING SOURCES (USES)</b>				
Gain on sale of capital assets	-	-	69	69
Transfers in	500,000	500,000	500,000	-
Transfers out	<u>( 1,676,500)</u>	<u>( 1,676,500)</u>	<u>( 1,746,380)</u>	<u>( 69,880)</u>
Total other financing sources and uses	<u>( 1,176,500)</u>	<u>( 1,176,500)</u>	<u>( 1,246,311)</u>	<u>( 69,811)</u>
<b>NET CHANGE IN FUND BALANCES</b>	<u>( 1,863,598)</u>	<u>( 3,103,184)</u>	<u>( 1,817,778)</u>	<u>1,285,406</u>
<b>FUND BALANCES, BEGINNING</b>	5,197,322	5,197,322	5,197,322	-
<b>PRIOR PERIOD ADJUSTMENT</b>	<u>( 213,388)</u>	<u>( 213,388)</u>	<u>( 213,388)</u>	<u>-</u>
<b>FUND BALANCES, ENDING</b>	<u>\$ 3,120,336</u>	<u>\$ 1,880,750</u>	<u>\$ 3,166,156</u>	<u>\$ 1,285,406</u>

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

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**CITY OF TERRELL, TEXAS**  
**STATEMENT OF NET ASSETS**  
**PROPRIETARY FUNDS**  
**SEPTEMBER 30, 2007**

	Business-type Activities			Governmental
	Water and Sanitary Sewer	Airport	Total	Activities Internal Service Funds
<b>ASSETS</b>				
Current assets:				
Cash and investments	\$ 4,852,045	\$ 834,304	\$ 5,686,349	\$ 865,764
Cash and investments - restricted	581,419	-	581,419	-
Accounts receivable, net	1,465,328	-	1,465,328	-
Deferred charges	50,641	25,797	76,438	-
Due from other funds	108,833	85,808	194,641	-
Due from other governments	105,075	-	105,075	-
Inventories at average cost	107,262	-	107,262	-
Total current assets	<u>7,270,603</u>	<u>945,909</u>	<u>8,216,512</u>	<u>865,764</u>
Non-current assets				
Capital assets:				
Land	537,271	347,748	885,019	-
Buildings and improvements	4,846,314	11,876,381	16,722,695	-
Construction in progress	2,309,188	54,544	2,363,732	-
Machinery and equipment	29,548,222	137,199	29,685,421	3,874,987
Less accumulated depreciation	<u>( 15,985,012)</u>	<u>( 3,723,552)</u>	<u>( 19,708,564)</u>	<u>( 2,207,684)</u>
Total capital assets	<u>21,255,983</u>	<u>8,692,320</u>	<u>29,948,303</u>	<u>1,667,303</u>
Total non-current assets	<u>21,255,983</u>	<u>8,692,320</u>	<u>29,948,303</u>	<u>1,667,303</u>
Total assets	<u>28,526,586</u>	<u>9,638,229</u>	<u>38,164,815</u>	<u>2,533,067</u>
<b>LIABILITIES</b>				
Current liabilities:				
Accounts payable	390,590	8,975	399,565	92,276
Accrued interest payable	5,549	7,231	12,780	-
Due to other funds	229,498	-	229,498	-
Due to other governments	25,610	-	25,610	-
Other accrued expenses	39,516	-	39,516	3,579
Compensated absences	11,344	-	11,344	7,677
Bonds, notes and loans payable	<u>230,000</u>	<u>60,000</u>	<u>290,000</u>	<u>-</u>
Total current liabilities	<u>932,107</u>	<u>76,206</u>	<u>1,008,313</u>	<u>103,532</u>
Non-current liabilities				
Compensated absences	45,376	-	45,376	-
Customer deposits	301,336	-	301,336	-
Bonds, notes and loans payable	<u>2,400,000</u>	<u>1,270,000</u>	<u>3,670,000</u>	<u>-</u>
Total non-current liabilities	<u>2,746,712</u>	<u>1,270,000</u>	<u>4,016,712</u>	<u>-</u>
Total liabilities	<u>3,678,819</u>	<u>1,346,206</u>	<u>5,025,025</u>	<u>103,532</u>
<b>NET ASSETS</b>				
Invested in capital assets, net of related debt	18,676,624	7,362,320	26,038,944	1,667,303
Restricted for debt service	581,419	-	581,419	-
Unrestricted	<u>5,589,724</u>	<u>929,703</u>	<u>6,519,427</u>	<u>762,232</u>
Total net assets	<u>\$ 24,847,767</u>	<u>\$ 8,292,023</u>	<u>\$ 33,139,790</u>	<u>\$ 2,429,535</u>

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

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**CITY OF TERRELL, TEXAS**

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

**PROPRIETARY FUNDS**

**FOR THE YEAR ENDED SEPTEMBER 30, 2007**

	Business-type Activities			Governmental Activities
	Water and Sanitary Sewer	Airport	Total	Internal Service Funds
<b>OPERATING REVENUES</b>				
Charges for services	\$ 7,769,569	\$ -	\$ 7,769,569	\$ -
Rental income	-	316,705	316,705	-
Internal service revenues	-	-	-	2,576,479
Miscellaneous	<u>873,854</u>	<u>5,039</u>	<u>878,893</u>	<u>16,656</u>
Total operating revenues	<u>8,643,423</u>	<u>321,744</u>	<u>8,965,167</u>	<u>2,593,135</u>
<b>OPERATING EXPENSES</b>				
Cost of sales and services	5,052,490	85,893	5,138,383	175,302
Administration	97,945	-	97,945	168,953
Utilities	-	-	-	521,766
Repairs and maintenance	-	-	-	62,104
Other supplies and expenses	-	-	-	249,252
Insurance claims and expenses	-	-	-	687,959
Depreciation	<u>631,781</u>	<u>239,777</u>	<u>871,558</u>	<u>306,524</u>
Total operating expenses	<u>5,782,216</u>	<u>325,670</u>	<u>6,107,886</u>	<u>2,171,860</u>
<b>OPERATING INCOME (LOSS)</b>	<u>2,861,207</u>	<u>( 3,926)</u>	<u>2,857,281</u>	<u>421,275</u>
<b>NON-OPERATING REVENUES (EXPENSES)</b>				
Capital contributions	245,000	-	245,000	-
Interest and investment revenues	124,661	31,368	156,029	18,743
Interest and fiscal charges	( 28,480)	( 61,913)	( 90,393)	( 5,447)
Transfers out	<u>( 945,546)</u>	<u>-</u>	<u>( 945,546)</u>	<u>-</u>
Total non-operating revenues (expenses)	<u>( 604,365)</u>	<u>( 30,545)</u>	<u>( 634,910)</u>	<u>13,296</u>
<b>CHANGE IN NET ASSETS</b>	2,256,842	( 34,471)	2,222,371	434,571
<b>TOTAL NET ASSETS, BEGINNING</b>	<u>22,590,925</u>	<u>8,326,494</u>	<u>30,917,419</u>	<u>1,994,964</u>
<b>TOTAL NET ASSETS, ENDING</b>	\$ <u>24,847,767</u>	\$ <u>8,292,023</u>	\$ <u>33,139,790</u>	\$ <u>2,429,535</u>

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

**CITY OF TERRELL, TEXAS**

**STATEMENT OF CASH FLOWS**

**PROPRIETARY FUNDS**

**FOR THE YEAR ENDED SEPTEMBER 30, 2007**

	Business-type Activities			Governmental Activities Internal Service Funds
	Water and Sanitary Sewer	Airport	Total	
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>				
Cash received from customers and users	\$ 8,501,140	\$ 321,744	\$ 8,822,884	\$ 2,593,135
Cash paid for services and insurance claims	-	-	-	( 1,246,234)
Cash paid to suppliers for goods and services	( 5,093,381)	( 264,211)	( 5,357,592)	( 473,756)
Cash paid to employees for services	( 56,172)	-	( 56,172)	( 180,604)
Net cash provided by operating activities	<u>3,351,587</u>	<u>57,533</u>	<u>3,409,120</u>	<u>692,541</u>
<b>CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES</b>				
Transfers out	( 945,546)	-	( 945,546)	-
Cash received from other funds	-	-	-	( 376)
Net cash used for noncapital financing activities	<u>( 945,546)</u>	<u>-</u>	<u>( 945,546)</u>	<u>( 376)</u>
<b>CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES</b>				
Acquisition of capital assets	( 1,556,129)	( 43,558)	( 1,599,687)	( 199,254)
Principal paid on long-term debt	( 85,000)	( 55,000)	( 140,000)	( 192,121)
Proceeds from debt issuance	2,030,000	-	2,030,000	-
Capital contributions	245,000	-	245,000	-
Interest and fiscal charges paid on debt	( 53,314)	( 59,591)	( 112,905)	( 5,447)
Net cash used for capital and related financing activities	<u>580,557</u>	<u>( 158,149)</u>	<u>422,408</u>	<u>( 396,822)</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>				
Investment earnings	<u>124,661</u>	<u>31,368</u>	<u>156,029</u>	<u>18,743</u>
Net cash provided by investing activities	<u>124,661</u>	<u>31,368</u>	<u>156,029</u>	<u>18,743</u>
<b>NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS</b>	3,111,259	( 69,248)	3,042,011	314,086
<b>CASH AND CASH EQUIVALENTS, BEGINNING</b>	<u>2,322,205</u>	<u>903,552</u>	<u>3,225,757</u>	<u>551,678</u>
<b>CASH AND CASH EQUIVALENTS, ENDING</b>	<u>\$ 5,433,464</u>	<u>\$ 834,304</u>	<u>\$ 6,267,768</u>	<u>\$ 865,764</u>

(continued)

**CITY OF TERRELL, TEXAS**  
**STATEMENT OF CASH FLOWS**  
**PROPRIETARY FUNDS**  
**(Continued)**  
**FOR THE YEAR ENDED SEPTEMBER 30, 2007**

	Business-type			Governmental Activities Internal Service Funds
	Water and Sanitary Sewer	Airport	Total	
Reconciliation of operating income (loss) to net cash provided by operating activities:				
Operating income (loss)	\$ 2,861,207	\$( 3,926)	\$ 2,857,281	\$ 421,275
Adjustments to reconcile operating income (loss) to net cash provided by operating activities:				
Depreciation	631,781	239,777	871,558	306,524
Changes in assets and liabilities:				
Decrease (increase) in assets:				
Customer receivable	( 146,288)	-	( 146,288)	-
Other receivable	( 105,075)	-	( 105,075)	-
Inventories	33,509	-	33,509	-
Due from other funds	34,594	( 75,539)	( 40,945)	-
Increase (decrease) in liabilities:				
Accounts payable	( 198,864)	( 102,779)	( 301,643)	( 29,956)
Accrued liabilities	39,516	-	39,516	( 3,912)
Compensated absences	( 2,257)	-	( 2,257)	( 1,390)
Due to other funds	173,849	-	173,849	-
Due to other governments	25,610	-	25,610	-
Customer deposits	4,005	-	4,005	-
Net cash provided by operating activities	<u>\$ 3,351,587</u>	<u>\$ 57,533</u>	<u>\$ 3,409,120</u>	<u>\$ 692,541</u>

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

# CITY OF TERRELL, TEXAS

## NOTES TO FINANCIAL STATEMENTS

SEPTEMBER 30, 2007

### 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The City of Terrell (the "City") was incorporated on September 6, 1875, under an act of the 14<sup>th</sup> Legislature of the State of Texas. The City operates under a Council-Manager form of government and provides the following services: public safety (police and fire); highways and streets; sanitation; culture-recreation; public improvements; planning and zoning; and general administrative services.

The accounting policies of the City of Terrell conform to generally accepted accounting principles as applicable to local governments. The following is a summary of the more significant accounting policies.

#### A. Reporting Entity

As required by generally accepted accounting principles, these financial statements have been prepared based on considerations regarding the potential for inclusion of other entities, organizations, or functions as part of the City's financial reporting entity. Based on these considerations, the Terrell Economic Development Corporation has been included in the City's reporting entity as blended component unit; although legally separate entity is in substance a part of the City's operations.

The Terrell Economic Development Corporation ("TEDC") was incorporated in 1990 under the provisions of the Development Corporation Act of 1979, as amended. TEDC operates under a five-member Board of Directors appointed by the City Council. The purpose of TEDC is to promote and develop commercial, industrial, and manufacturing enterprises to create and enhance local job opportunities. The City Council maintains organizational control over TEDC in addition to significant managerial control over the assets and operations. TEDC has been incorporated into these financial statements as a major governmental fund. Essential disclosures are included in separately issued financial statements of the TEDC. These statements may be obtained at the City's administrative office.

The Terrell Development Corporation (the "Corporation") was created in 1979 for the special purpose of promoting and developing commercial, industrial and manufacturing enterprise and encouraging employment in the City. The members of the Board of the Corporation are appointed by the City Council. The Corporation is authorized to issue industrial development revenue bonds after approval of the City Council. During 1997, the Corporation issued \$7,600,000 of development revenue bonds. The bonds do not constitute indebtedness of the City and are secured solely by the revenues received from the commercial organization on whose behalf they were issued. The City assumes no responsibility for the operating expenses of the Corporation as they are financed by fees charged to the commercial organization. The Corporation has been excluded from the City's financial statements.

(continued)

## 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### **B. Government-wide and Fund Financial Statements**

The government-wide financial statements (i.e., the statement of net assets and the statement of changes in net assets) report information 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 revenues, are reported separately from business-type activities which rely to a significant extent on fees and charges for support.

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

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.

### **C. 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 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 revenues 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 City considers revenues to be available if they are 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, licenses, and interest associated with the current fiscal period are all considered to be susceptible to accrual and so have been recognized as revenues of the current fiscal period. All other revenue items are considered to be measurable and available only when cash is received by the City.

(continued)

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

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

The City reports the following major governmental funds:

The **General Fund** is the City's primary operating fund. It accounts for all financial resources of the general government, except those required to be accounted for in another fund.

The **Section 8 Rent Supplement Fund** is a Special Revenue Fund used to account for federal funds received under contract from the Department of Housing and Urban Development for housing rental assistance.

The **Terrell Economic Development Fund** is a component unit of the City and accounts for ½ cent sales tax revenues used to promote and develop commercial, industrial and manufacturing enterprises to create and enhance job opportunities.

The **C. O. Tax and Revenue Series 2004 Fund** is a Capital Projects Fund used to account for construction projects funded by the Series 2004 Bond issuance.

The **2007A Bond Fund** is a Capital Projects Fund used to account for construction projects funded by the Series 2007 Bond issuance.

The City reports the following major proprietary funds:

The **Water and Sanitary Sewer Fund** is used to account for sale of water and wastewater treatment by the City to businesses and residential customers and to surrounding communities.

The **Airport Fund** is used to account for operations of the Terrell Municipal Airport.

Additionally, the City reports the following fund types:

**Internal Service Funds** are used to account for the financing of goods or services provided by one department or agency to other departments or agencies of the City on a cost-reimbursement basis. The City reports the following Internal Service Funds:

**Self-insurance Fund** – to account for the City's self-insurance programs.

**Equipment Replacement Fund** – to track fleet maintenance, repair and replacement.

(continued)

## 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

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

Private-sector standards of accounting and financial reporting issued prior to December 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 Government 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 the general rule are charges between the City's water utilities function and various other functions. Elimination of these charges would distort the direct costs and program revenues 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 revenues. Likewise, general revenues include 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 and of the Internal Service Funds are charges to customers for sales and services. The City also recognizes as operating revenue the portion of tap fees intended to recover the cost of connecting new customers to the system. Operating expenses for Enterprise Funds and Internal Service Funds include the cost of sales and services, administrative expense, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

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

### D. Assets, Liabilities, and Net Assets or Equity

#### **Equity in Pooled Cash and Investments**

The City reclassifies certain of its cash and investments into equity in pooled cash and investments. Each fund participates on a daily transaction basis and income for all assets included in pooled cash and investments is allocated to individual funds based on their respective balance in equity in pooled cash and investments.

(continued)

## 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### D. Assets, Liabilities, and Net Assets or Equity (Continued)

#### **Equity in Pooled Cash and Investments** (Continued)

Additionally, deposits and investments continue to be held separately by several of the City's funds. Income on these assets is recorded in the respective fund holding the deposits and investments.

All assets in equity in pooled cash and investments and demand deposits on hand have been considered as cash equivalents for purposes of the statement of cash flows.

#### **Investments**

State statutes authorize the City to invest in obligations of the U. S. Treasury, commercial paper, corporate bonds, and repurchase agreements. Investments are stated at fair value.

#### **Investment in Land**

The Terrell Economic Development Corporation invests in land to sell to prospective businesses to enhance economic development. Investment in land is stated at cost.

#### **Receivables and Payables**

Activity between funds that are representative of lending/borrowing arrangements outstanding at the end of the fiscal year are referred to as either "due to/from other funds" (i.e., the current portion of interfund loans) or "advances to/from other funds" (i.e., the noncurrent portion of interfund loans). All other outstanding balances between funds are reported as "due to/from other funds." Any residual balances outstanding between the governmental activities and business-type activities are reported in the government-wide financial statements as "internal balances."

Advances between funds, as reported in the fund financial statements, are offset by a fund balance reserve account in applicable governmental funds to indicate that they are not available for appropriation and are not expendable available financial resources.

All receivables are shown net of an allowance for uncollectible. The City provides an allowance for doubtful accounts based upon the anticipated collectibility of each specific account as determined by experience.

Property taxes are levied October 1 on the assessed value of property at January 1 and are due by January 31 of the following year. The total assessed value of property was \$1,096,004,506 and the tax rates were \$.4685 per \$100 valuation for maintenance and operations and \$.1815 per \$100 valuation for debt service. Unpaid taxes attach as an enforceable lien on property as of January 31. Revenue from taxes assessed is recorded as deferred revenue on October 1. The deferred revenue from taxes is then recognized as revenue during the year as the taxes are actually received.

(continued)

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

D. **Assets, Liabilities, and Net Assets or Equity** (Continued)

**Inventories and Prepaid Items**

Inventories of materials and supplies are accounted for using the consumption method. Under the consumption method, inventories are recorded as expenditures when they are used with significant amounts on hand reported on the balance sheet at average cost. In governmental funds, reported inventories do not represent available spendable resources and are, therefore, equally offset by a fund balance reservation.

**Restricted Assets**

Certain proceeds of the City's Enterprise Fund revenue bonds, as well as certain resources set aside for their repayment, are classified as restricted assets on the balance sheet because they are maintained in separate bank accounts and their use is limited by applicable bond covenants. The Water and Sanitary Sewer Fund Debt Service Fund account is used to segregate resources accumulated for debt service payments over the life of the bonds.

**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. Capital assets are defined by the government as assets with an initial, individual cost of more than \$5,000 (amount not rounded) and an estimated life in excess of three years. 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 are not capitalized.

Property, plant and equipment of the primary government, as well as the component units, is depreciated using the straight-line method over the following estimated useful lives:

<u>Assets</u>	<u>Years</u>
Buildings	45
Building improvements	10 - 20
Improvements other than buildings	20 - 45
Public domain infrastructure	20 - 40
Vehicles	12
Heavy equipment	10 - 15
Office equipment	7
Computer equipment	5 - 7

(continued)

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

**D. Assets, Liabilities, and Net Assets or Equity (Continued)**

**Construction in Progress**

Expenditures on incomplete capital projects have been capitalized as construction in progress. The assets resulting from these projects will be transferred from the construction in progress accounts to the appropriate asset account as the projects are completed. Interest incurred, when material, during the construction phase of business-type activities is included as a part of the capitalized value of the constructed asset. During the fiscal year ended September 30, 2007, there was no interest capitalized.

**Compensated Absences**

The City's vacation pay policy provides that vacation pay accrues at various rates based on length of service up to the maximum of 21 days per year. Generally, sick leave is not paid upon termination except for firemen and policemen. Firemen and policemen accumulate unused sick leave up to a maximum of 90 days. All other employees are paid only upon illness while in the employ of the City.

As of September 30, 2007, the liability for accrued vacation leave and accrued sick leave is \$1,177,598. The amount applicable to the Enterprise Funds (\$56,720) has been recorded in those funds, and the amount applicable to other funds (\$1,120,878) has been recorded in the Statement of Net Assets for governmental activities.

**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.

In the fund financial statements, governmental fund types recognize bond premiums and discounts, as well as bond 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 on debt issuances are reported as other financing uses. Issuance costs, whether or not withheld from the actual debt proceeds received, are reported as debt service expenditures.

**(continued)**

## 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### D. Assets, Liabilities, and Net Assets or Equity (Continued)

#### **Fund Equity**

Reserves of fund balance or retained earnings are used to indicate that a portion of fund equity is not available for expenditure or is legally segregated for a specific future use. Designated fund balances represent tentative plans for future use of financial resources.

#### **Net Assets**

Net assets represents the difference between assets and liabilities. Net assets invested in capital assets, net of related debt, consists of the City's capital assets, net of accumulated depreciation, reduced by any outstanding debt used for the acquisition or construction of those assets. Net assets reported as restricted are those amounts which have limitations imposed on their use either through legislation adopted by the City or through external restrictions imposed by creditors, grantors or other laws and regulations.

#### **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 at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

#### **Encumbrances**

Encumbrance accounting, under which purchase orders, contracts, and other commitments for the expenditure of monies are recorded in order to reserve that portion of the applicable appropriation, is employed in governmental funds. Encumbrances outstanding at year-end are reported as reservations of fund balances since they do not constitute expenditures or liabilities. There were no encumbrances outstanding at September 30, 2007.

In accordance with the budgetary policies of the City, encumbrance accounting is also employed by proprietary fund types for management control purposes. Encumbrances outstanding at year-end are not reported as reservations of retained earnings nor have they been included as expenses or liabilities of proprietary fund types.

## 2. RECONCILIATION OF GOVERNMENT-WIDE AND FUND FINANCIAL STATEMENTS

### A. Explanation of Certain Differences Between the Governmental Fund Balance Sheet and the Government-wide Statement of Net Assets

The governmental fund balance sheet includes a reconciliation between *fund balance – total governmental funds* and *net assets – governmental activities* as reported in the government-wide statement of net assets. One element of that reconciliation explains, “Long-term liabilities, including bonds payable, are not due and payable in the current period and therefore are not reported in the funds.” The details of this \$(22,696,869) difference are as follows:

General obligation bonds	\$( 2,710,000)
Certificates of obligation	( 14,730,000)
Less: deferred charge for issuance costs (to be amortized over life of debt)	69,809
Interest payable	( 106,992)
Notes payable	( 4,106,485)
Compensated absences	<u>( 1,113,201)</u>
 Net adjustment to reduce <i>fund balance - total governmental funds</i> to arrive at <i>net assets - governmental activities</i>	 <u>\$( 22,696,869)</u>

### B. Explanation of Certain Differences Between the Governmental Fund Statement of Revenue, Expenditures and Changes in Fund Balances and the Government-wide Statement of Activities

The governmental fund statement of revenue, expenditures and changes in fund balances includes a reconciliation between *net changes in fund balances – total governmental fund* and *changes in net assets of governmental activities* as reported in the government-wide statement of activities. One element of that reconciliation explains, “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.” The details of this \$4,108,386 difference are as follows:

Capital outlay	\$ 5,067,805
Depreciation expense	<u>( 959,419)</u>
 Net adjustment to increase <i>net changes in fund balances - total governmental funds</i> to arrive at <i>changes in net assets of governmental activities</i>	 <u>\$ 4,108,386</u>

(continued)

**2. RECONCILIATION OF GOVERNMENT-WIDE AND FUND FINANCIAL STATEMENTS**  
(Continued)

**B. Explanation of Certain Differences Between the Governmental Fund Statement of Revenue, Expenditures and Changes in Fund Balances and the Government-wide Statement of Activities** (Continued)

Another element of that reconciliation states, “Certain receivables will be collected next year but are not available soon enough to pay for the current period’s expenditures and, therefore, are reported as deferred revenues in the funds.” The details of this \$105,299 difference are as follows:

Deferred property tax revenues	\$ 19,591
Deferred special assessments	<u>85,708</u>
Net adjustment to increase <i>fund balance - total governmental funds</i> to arrive at <i>net assets - governmental activities</i>	<u>\$ 105,299</u>

Another element of that reconciliation states, “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. Neither transaction, however, has any effect on net assets. Also, governmental funds report the effect of issuance costs, and similar items when debt is first issued, whereas these amounts are deferred and amortized in the statement of activities.” The details of this \$410,437 difference are as follows:

Issuance of certificates of obligation	\$( 2,030,000)
Principal repayments	<u>2,440,437</u>
Net adjustment to reduce <i>fund balance - total governmental funds</i> to arrive at <i>net assets - governmental activities</i>	<u>\$ 410,437</u>

**3. STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY**

**A. Budgetary Information**

The City follows these procedures in establishing the budgetary data reflected in the financial statements:

1. Prior to August 1, the City Manager submits to the City Council a proposed operating budget for the fiscal year commencing the following October 1. The operating budget includes proposed expenditures and the means of financing them.
2. Prior to October 1, the budget is legally enacted through passage of an ordinance.

(continued)

### 3. STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY (Continued)

#### A. Budgetary Information (Continued)

3. The City Council approves, by ordinance, budget appropriations on a departmental basis. The City Manager is authorized to transfer budget amounts within any department; however, any revisions that alter the total departmental appropriation must be approved by the City Council. Therefore, the level of budgetary responsibility is by total appropriations for each department.
4. A formal budget is adopted for the General Fund on a basis consistent with generally accepted accounting principles.
5. Several budget amendments were made during the year.
6. Appropriations lapse at year-end.

#### B. Expenditures Over Appropriations

Expenditures exceeded appropriations in the Sanitation function by \$3,590, the Debt Service Principal function by \$205,966, the interest and other charges function by \$36,522, and the capital outlay function by \$174,131 in the General Fund.

#### C. Deficit Fund Balance/Net Assets

The Self-Insurance Internal Service Fund had a deficit equity balance of \$64,297, the Housing Rehabilitation and Ownership Assistance Fund had a deficit equity balance of \$2, and the Certificates of Obligation Tax and Revenue Series 2002 Fund had a deficit equity balance of \$74,214 as of September 30, 2007. The deficit equity balances will be covered by future transfers from the General Fund.

### 4. DETAILED NOTES ON ALL FUNDS

#### Deposits and Investments

*Custodial Credit Risk.* In the case of deposits, this is the risk that in the event of a bank failure, the City's deposits may not be returned to it. State statutes require that all deposits in financial institutions be fully collateralized by U. S. Government obligations or its agencies and instrumentalities or direct obligations of Texas or its agencies and instrumentalities that have a fair value of not less than the principal amount of deposits. As of September 30, 2007, \$17,647,112 of the City's \$17,847,112 deposit balance was collateralized with securities held by the pledging financial institution. The remaining balance, \$200,000 was covered by FDIC insurance.

(continued)

4. **DETAILED NOTES ON ALL FUNDS** (Continued)

**Deposits and Investments** (Continued)

The City Council has adopted a written investment policy regarding the investments of its funds as defined by the Public Funds Investment Act of 1995 (Chapter 2256, Texas Government Code). The investments of the City are in compliance with the Council's investment policies. All significant legal and contractual provisions for investments were complied with during the year.

**Receivables**

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

	<u>General</u>	<u>Nonmajor and Other</u>	<u>Water Utilities</u>	<u>Total</u>
Receivables:				
Taxes	\$ 2,086,035	\$ 132,233	\$ -	\$ 2,218,268
Special assessment	-	1,103,921	-	1,103,921
Accounts	<u>-</u>	<u>-</u>	<u>1,561,105</u>	<u>1,561,105</u>
Gross receivables	2,086,035	1,236,154	1,561,105	4,883,294
Less: allowance for uncollectibles	<u>( 557,130)</u>	<u>( 384,619)</u>	<u>( 95,777)</u>	<u>( 1,037,526)</u>
Net total receivables	<u>\$ 1,528,905</u>	<u>\$ 851,535</u>	<u>\$ 1,465,328</u>	<u>\$ 3,845,768</u>

Governmental funds report *deferred revenue* in connection with receivables for revenues that are 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>	<u>Unearned</u>
Street improvement assessments	\$ 739,137	\$ -
Property taxes	399,995	-
Grants	<u>-</u>	<u>-</u>
Total	<u>\$ 1,139,132</u>	<u>\$ -</u>

(continued)

#### 4. DETAILED NOTES ON ALL FUNDS (Continued)

##### Capital Assets

Capital asset activity for the year ended September 30, 2007, was as follows:

##### **Primary Government**

	Beginning Balance	Increases	Reclassification/ Decreases	Ending Balance
<b>Governmental activities:</b>				
Capital assets, not being depreciated:				
Land	\$ 665,035	\$ 257,478	\$ 204,513	\$ 718,000
Construction in progress	1,922,394	4,614,529	601,916	5,935,007
Total assets not being depreciated	<u>2,587,429</u>	<u>4,872,007</u>	<u>806,429</u>	<u>6,653,007</u>
Capital assets, being depreciated:				
Buildings	3,733,462	-	318,698	3,414,764
Improvements, other than buildings	1,166,689	75,035	150,174	1,091,550
Machinery and equipment	4,704,739	320,017	507,530	4,517,226
Infrastructure	31,838,431	-	-	31,838,431
Total capital assets being depreciated	<u>41,443,321</u>	<u>395,052</u>	<u>976,402</u>	<u>40,861,971</u>
Less accumulated depreciation:				
Buildings	1,746,958	86,089	387,592	1,445,455
Improvements, other than buildings	703,041	27,289	19,973	710,357
Machinery and equipment	2,323,578	356,604	109,107	2,571,075
Infrastructure	18,639,690	795,961	-	19,435,651
Total accumulated depreciation	<u>23,413,267</u>	<u>1,265,943</u>	<u>516,672</u>	<u>24,162,538</u>
Total capital assets being depreciated, net	<u>18,030,054</u>	<u>( 870,891)</u>	<u>459,730</u>	<u>16,699,433</u>
Governmental activities capital assets, net	<u>\$ 20,617,483</u>	<u>\$ 4,001,116</u>	<u>\$ 1,266,159</u>	<u>\$ 23,352,440</u>
<b>Business-type Activities</b>				
Capital assets, not being depreciated:				
Land	\$ 885,019	\$ -	\$ -	\$ 885,019
Construction in progress	4,009,006	958,972	2,604,246	2,363,732
Total assets not being depreciated	<u>4,894,025</u>	<u>958,972</u>	<u>2,604,246</u>	<u>3,248,751</u>
Capital assets, being depreciated:				
Buildings and improvements	16,722,695	-	-	16,722,695
Machinery and equipment	26,440,459	3,244,962	-	29,685,421
Total capital assets being depreciated	<u>43,163,154</u>	<u>3,244,962</u>	<u>-</u>	<u>46,408,116</u>
Less accumulated depreciation:				
Buildings and improvements	9,171,642	331,833	( 1,885,916)	11,389,391
Machinery and equipment	9,665,363	539,726	1,885,916	8,319,173
Total accumulated depreciation	<u>18,837,005</u>	<u>871,559</u>	<u>-</u>	<u>19,708,564</u>
Total capital assets being depreciated, net	<u>24,326,149</u>	<u>2,373,403</u>	<u>-</u>	<u>26,699,552</u>
Business-type activities capital assets, net	<u>\$ 29,220,174</u>	<u>\$ 3,332,375</u>	<u>\$ 2,604,246</u>	<u>\$ 29,948,303</u>

(continued)

**4. DETAILED NOTES ON ALL FUNDS (Continued)**

**Capital Assets** (Continued)

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

Governmental activities:		
General government		\$ 54,299
Public safety		63,275
Highways and streets		796,836
Culture and recreation		45,009
Capital assets held by the City's internal service funds are charged to the various functions based on their usage		<u>306,524</u>
Total depreciation expense - governmental activities		<u>\$ 1,265,943</u>
Business-type activities:		
Water and sanitary sewer		\$ 631,781
Airport		<u>239,778</u>
Total depreciation expense - business-type activities		<u>\$ 871,559</u>

**Construction Commitments**

The City has active construction projects as of September 30, 2007. The projects include street construction and expansion. At year-end, the City's commitments with contractors are as follows:

<u>Project</u>	<u>Contract Amounts</u>	<u>Spent to Date</u>	<u>Estimated Remaining Commitment</u>
Bachelor Creek Interceptor	\$ 3,500,000	\$ -	\$ 3,500,000
State Highway 34 relocation	900,000	-	900,000
2 million gallon storage tank	4,735,000	50,000	4,685,000
Airport auto parking and entrance road	1,500,000	-	1,500,000

**Interfund Receivables and Payables and Transfers**

The composition of interfund balances as of September 30, 2007, is as follows:

**Due to/from other funds:**

<u>Receivable Fund</u>	<u>Payable Fund</u>	<u>Amount</u>
General fund	Rent Supplement Section 8	\$ 23,826
	Water and sanitary sewer	143,690
	Nonmajor governmental	45,334
Economic development corporation	Nonmajor governmental	37,688
Water and sanitary sewer	Nonmajor governmental	108,833
Nonmajor governmental	Economic development corporation	54,143
Airport	Water and sanitary sewer	<u>85,808</u>
		<u>\$ 499,322</u>

(continued)

4. **DETAILED NOTES ON ALL FUNDS** (Continued)

**Interfund Receivables and Payables and Transfers** (Continued)

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

**Interfund transfers:**

<u>Transfers out</u>	<u>Transfers in</u>	<u>Amount</u>
General	TEDC	\$ 1,746,225
	Nonmajor governmental	155
Water and sanitary sewer	General	500,000
	Nonmajor governmental	445,546
Nonmajor governmental	TEDC	24,529
	Nonmajor governmental	<u>16,029</u>
		<u>\$ 2,732,484</u>

Transfers are used to move revenues from the fund required by statute or budget to collect them to the fund expending them.

**Long-term Debt**

**Bonded Debt**

Bonded debt of the City as of September 30, 2007, is comprised of the following individual issues:

	<u>Interest Rates</u>	<u>Date Issued</u>	<u>Maturity Date</u>	<u>Amount of Original Issue</u>	<u>Amount Outstanding</u>
Water and Sewer Revenue Bonds:					
Series 1973	4.10 - 4.15%	01/10/1973	01/10/2013	\$ 1,000,000	\$ <u>600,000</u>
					<u>600,000</u>
Certificates of Obligation:					
Series 1999	3.75 - 4.75%	03/02/1999	02/15/2016	4,500,000	3,555,000
Series 2002	3.60 - 4.90%	07/23/2002	02/15/2022	4,500,000	3,270,000
Series 2003	4.00 - 4.70%	03/21/2003	02/15/2023	1,500,000	1,330,000
Series 2004	3.00 - 4.50%	09/15/2004	02/15/2024	5,500,000	4,750,000
Series 2006	4.00 - 4.375%	08/15/2006	02/15/2026	1,570,000	1,125,000
Series 2007A	4.29%	04/15/2007	02/15/2027	2,030,000	2,030,000
Series 2007B	5.99%	04/15/2007	02/15/2027	2,030,000	<u>2,030,000</u>
					<u>18,090,000</u>
General Obligation Bonds:					
Series 2004	2.00 - 3.375%	03/01/2005	02/15/2014	3,835,000	<u>2,710,000</u>
					<u>2,710,000</u>
					<u>\$ 21,400,000</u>

(continued)

**4. DETAILED NOTES ON ALL FUNDS (Continued)**

**Long-term Debt (Continued)**

**Bonded Debt (Continued)**

Annual debt service requirements to maturity for bonded debt are as follows:

Year Ending September 30,	Certificates of Obligation Tax Supported		Revenue Bonds		General Obligation Bonds	
	Principal	Interest	Principal	Interest	Principal	Interest
2008	\$ 1,160,000	\$ 827,656	\$ 100,000	\$ 22,600	\$ 385,000	\$ 69,344
2009	1,320,000	725,024	100,000	18,500	370,000	61,331
2010	955,000	674,721	100,000	14,400	380,000	52,419
2011	1,000,000	632,034	100,000	10,300	380,000	42,306
2012	1,050,000	587,851	100,000	6,200	400,000	31,194
2013-2017	6,065,000	2,169,673	100,000	2,075	795,000	25,040
2018-2022	4,915,000	875,114	-	-	-	-
2023-2027	<u>1,625,000</u>	<u>119,534</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
Total	<u>\$ 18,090,000</u>	<u>\$ 6,611,607</u>	<u>\$ 600,000</u>	<u>\$ 74,075</u>	<u>\$ 2,710,000</u>	<u>\$ 281,634</u>

**Notes Payable**

As of September 30, 2007, the City's notes payable consisted of the following:

The Terrell Economic Development Corporation, a component unit of the City of Terrell, had an outstanding balance of \$46,600 of its \$2,559,797 construction note from a local bank for funding of capital improvements to Airport Road. The note is secured by sales tax revenues of the Corporation and will service monthly over a five-year period at 3.65% interest.

The Terrell Economic Development Corporation (TEDC) entered into a note payable agreement with a local bank on September 18, 2005. As of September 30, 2007, the balance was \$2,978,945. The loan is secured by sales tax revenues of the Corporation and will service monthly over a 15-year period at 4.49% interest.

\$610,000 lease purchase agreement with Wells Fargo for the purchase of a records management system for police department. The agreement calls for five annual payments of \$133,349, including interest at 3.48%, with the final payment of the unpaid balance due October 14, 2009.

\$345,979 equipment note to a bank for the purchase of a fire pumper. The note is due in five annual payments of \$75,225, including interest at 4.0%, with the final payment of unpaid balance due October 15, 2010. The note is secured by the fire pumper.

\$700,000 real estate note to a bank for the purchase of property at 1220 Brin. The note is due in five annual payments of \$159,855, including interest at 4.59%, with the final payment of unpaid balance due October 15, 2010. The note is secured by the real estate.

(continued)

4. **DETAILED NOTES ON ALL FUNDS (Continued)**

**Long-term Debt (Continued)**

**Notes Payable (Continued)**

Future maturities and amounts paid under the notes after September 30, 2007, are as follows:

<u>Year Ending September 30,</u>	<u>Principal</u>	<u>Interest</u>
2008	\$ 562,963	\$ 167,542
2009	540,911	145,147
2010	554,239	121,933
2011	289,976	105,054
2012	229,290	92,176
2013-2017	1,314,066	293,265
2018-2022	<u>615,040</u>	<u>29,020</u>
Total	<u>\$ 4,106,485</u>	<u>\$ 954,137</u>

**Changes in Long-term Liabilities**

Long-term liability activity for the year ended September 30, 2007, was as follows:

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Adjustments</u>	<u>Ending Balance</u>	<u>Due Within One Year</u>
<b>Governmental activities</b>						
Compensated absences	\$ 1,037,145	\$ 83,733	\$ -	\$ -	\$ 1,120,878	\$ 224,176
Notes payable	5,484,802	-	1,262,558	115,759	4,106,485	562,963
Certificates of obligation	13,685,000	2,030,000	985,000	-	14,730,000	1,100,000
General obligation bonds	<u>3,095,000</u>	<u>-</u>	<u>385,000</u>	<u>-</u>	<u>2,710,000</u>	<u>385,000</u>
Governmental activities long-term liabilities	<u>\$ 23,301,947</u>	<u>\$ 2,113,733</u>	<u>\$ 2,632,558</u>	<u>\$ 115,759</u>	<u>\$ 22,667,363</u>	<u>\$ 2,272,139</u>
<b>Business-type activities</b>						
Compensated absences	\$ 58,977	\$ -	\$ 2,257	\$ -	\$ 56,720	\$ 11,344
Certificates of obligation	1,385,000	2,030,000	55,000	-	3,360,000	190,000
Revenue bonds	<u>685,000</u>	<u>-</u>	<u>85,000</u>	<u>-</u>	<u>600,000</u>	<u>100,000</u>
Business-type activities long-term liabilities	<u>\$ 2,128,977</u>	<u>\$ 2,030,000</u>	<u>\$ 142,257</u>	<u>\$ -</u>	<u>\$ 4,016,720</u>	<u>\$ 301,344</u>

**Bond Covenants**

Bond covenants require the following disclosures:

	<u>Interest and Sinking</u>	<u>Reserve</u>
First Lien Bonds:		
Required ultimate balance	\$ -	\$ 212,240
Required present balance, end of year	30,650	212,240
Actual present balance, end of year	209,546	371,873

(continued)

#### **4. DETAILED NOTES ON ALL FUNDS (Continued)**

##### **Contingent Liabilities**

The City is defendant in various lawsuits. Although the outcome of the lawsuits is not presently determinable, in the opinion of the City Attorney, the resolution of these matters will not have a material adverse effect on the financial condition of the City.

The City participates in a number of federal and state assisted grant programs. These programs are subject to program compliance audits by the grantors or their representatives. The audits of these programs for the year ended September 30, 2007, have not yet been conducted. Accordingly, the City's compliance with applicable grant requirements will be established at some future date. The amount, if any, of expenditures which may be disallowed by the granting agencies cannot be determined at this time although the City expects such amounts, if any, to be immaterial.

On November 28, 1997, the City was issued an Administrative Order from Region VI of the U. S. Environmental Protection Agency ("EPA") for apparent violations of the City's National Pollution Discharge Elimination System Permit ("NPDES" Permit) for exceeding the allowable amount of silver, which could be discharged from the City's wastewater treatment plant. Failure of the City to comply with the Order could result in substantial penalties being assessed against the City.

##### **Self-insurance Plan**

The City has established a self-insurance plan for health care benefits that pays 100% of employee claims limited to \$20,000 per employee and \$650,000 in aggregate. The City has insured claims in excess of plan limits. Accrued claims payable include provisions for claims reported and claims incurred but not reported. The provision for reported claims is determined by estimating the amount which will ultimately be paid each claimant. The provision for claims incurred but not yet reported is estimated based on the City's experience. Claims liabilities are reevaluated periodically to take into consideration settlement of claims, new claims, and other factors. As of September 30, 2007 and 2006, the estimated value of these liabilities was \$80,475 and \$116,984, respectively.

##### **Retirement Commitments**

The City provides pension benefits for all of its fulltime employees through a nontraditional, joint contributory, hybrid defined benefit plan in the statewide Texas Municipal Retirement System (TMRS), one of over 821 administered by TMRS, an agent multiple-employer public employee retirement system.

Benefits depend upon the sum of the employee's contributions to the plan, with interest, and the City-financed monetary credits, with interest. At the date the plan began, the City granted monetary credits for service rendered before the plan began of a theoretical amount equal to two times what would have been contributed by the employee, with interest, prior to establishment of the plan. Monetary credits for service since the plan began, are a percent (100%, 150%, or 200%) of the employee's accumulated contributions. In addition, the City can grant, as often as annually, another type of monetary credit referred to as an updated service credit which is a theoretical amount which, when added to the employee's accumulated contributions and the monetary credits for service since the plan began, would be the total monetary credits and employee contributions accumulated with interest if the current employee contribution rate and City matching percent had always been in existence and if the employee's salary had always been the average of his salary in the last three years that are one year before the effective date. At retirement, the benefit is calculated as if the sum of the employee's accumulated contributions with interest and the employer-financed monetary credits with interest were used to purchase an annuity.

**(continued)**

**4. DETAILED NOTES ON ALL FUNDS (Continued)**

**Retirement Commitments** (Continued)

Members can retire at ages 60 and above with 5 or more years of service or with 20 years of service regardless of age. The plan provisions are adopted by the governing body of the City, within the options available in the state statutes governing TMRS and within the actuarial constraints also in the statutes.

The contribution rate for the employees is 7% and the City matching percent is currently 2 to 1, both as adopted by the governing body of the City. Under the state law governing TMRS, the actuary annually determines the City contribution rate. This rate consists of the normal cost contribution rate and the prior service cost contribution rate, both of which are calculated to be a level percent of payroll from year to year. The normal cost contribution rate finances the currently accruing monetary credits due to the City matching percent, which are the obligation of the City as of an employee's retirement date, not at the time the employee's contributions are made. The normal cost contribution rate is the actuarially determined percent of payroll necessary to satisfy the obligation of the City to each employee at the time his/her retirement becomes effective. The prior service contribution rate amortizes the unfunded (overfunded) actuarial liability (asset) over the remainder of the plan's 25-year amortization period. When the City periodically adopts updated service credits and increases in annuities in effect, the increased unfunded actuarial liability is to be amortized over a new 25-year period. The unit credit actuarial cost method is used for determining the City contribution rate. Both the employees and the City make contributions monthly. Since the City needs to know its contribution rate in advance to budget for it, there is a one-year delay between the actuarial valuation that is the basis for the rate and the calendar year when the rate goes into effect, (i.e., December 31, 2006, valuation is effective for rates beginning January 2008).

**Schedule of Actuarial Liabilities and Funding Progress**

Actual Valuation Date	12/031/04	12/031/05	12/031/06
Actuarial value of assets	\$ 11,777,623	\$ 12,338,896	\$ 12,435,490
Actuarial accrued liability	15,956,385	16,906,445	17,730,583
Percent funded	73.8%	73.0%	70.1%
Unfunded (overfunded) actuarial accrued liability (UAAL)	4,178,762	4,567,549	5,295,093
Annual covered payroll	6,240,183	6,964,691	7,132,587
UAAL as a percentage of covered payroll	67.0%	65.6%	74.2%
Net pension obligation (NPO at the beginning of period)	-	-	-
Annual Pension Cost:			
Annual required contribution (ARC)	874,475	926,156	894,657
Interest on NPO	-	-	-
Adjustment to the ARC	874,475	926,156	894,657
Contributions made	874,475	926,156	894,657
Increase in NPO	<u>-</u>	<u>-</u>	<u>-</u>
NPO at the end of the period	\$ <u>-</u>	\$ <u>-</u>	\$ <u>-</u>

(continued)

#### 4. DETAILED NOTES ON ALL FUNDS (Continued)

##### Retirement Commitments (Continued)

The City of Terrell is one of 821 municipalities having the benefit plan administered by TMRS. Each of the 821 municipalities has an annual, individual actuarial valuation performed. All assumptions for the December 31, 2006, valuations are contained in the 2006 TMRS Comprehensive Annual Financial Report, a copy of which may be obtained by writing to P. O. Box 149153, Austin, Texas 78714-9153.

##### **Actuarial Assumptions**

Actuarial Cost Method	-	Unit Credit
Amortization Method	-	Level Percent of Payroll
Remaining Amortization Period	-	25 Years - Open Period
Asset Valuation Method	-	Amortized Cost (to accurately reflect the requirements of GASB Statement No. 25, paragraphs 36e and 138)
Amortization Period	-	Open
Investment Rate of Return	-	7%
Projected Salary Increases	-	None
Includes Inflation at	-	3.5%
Cost-of-living Adjustments	-	None

##### Risk Management

The City is exposed to risk of loss due to injuries incurred by employees while performing work-related duties. The City provides workers' compensation insurance coverage with the Texas Municipal League, which provides statutory coverage against potential losses.

The City is exposed to various risks of loss related to torts, damage to, and destruction of assets; errors and omissions and natural disasters. A comprehensive insurance plan for property and casualty and general liability coverage has been established with the Texas Municipal League.

##### Commitments

During the fiscal year ended September 30, 2005, the City entered into an agreement with North Texas Municipal Water District (the "District"). Under the agreement, the District has agreed to acquire property and construct a transmission line in order to sell water to the City. As part of the agreement, the project will be financed by a bond issue in the amount of \$12,470,000 issued in the name of the District. The District is responsible for the cost of the project only to the extent of the bond issue and any additional construction costs are the responsibility of the City. During the construction phase, the City is responsible for the monthly transfer of funds to the District in order to pay the debt service obligation of the bonds and to fund any necessary reserve funds established by the bond ordinance. Upon completion of the project, the rights, title and interest in the project will rest irrevocably with the City. This transaction shall result in the automatic sale and delivery of the project to the City in consideration of the agreement of the City to perform its obligations under the agreement.

(continued)

**4. DETAILED NOTES ON ALL FUNDS (Continued)**

**Prior Period Adjustment**

The City had a capital asset inventory completed on the City's governmental activities capital assets. Upon completion, the inventory stated an amount that was significantly different from amounts the City had calculated on their depreciation schedules and reported in their government-wide financial statements in prior financial reports. The difference between the schedules and the actual capital asset inventory caused a decrease in beginning net assets of \$1,063,949.

The City had an advance of grant funds in a receivable in FY 2006. Upon further analysis, these funds were to be sent back to FEMA as they are not going to be spent. These funds should have been recorded as a deferred revenue. This caused a decrease in the beginning fund balance of the General Fund and net assets of governmental activities of \$213,388.

# **COMBINING STATEMENTS**

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## **NONMAJOR GOVERNMENTAL FUNDS**

***Housing Rehabilitation and Ownership Assistance Fund*** – to account for federal block grants awarded by the Texas Department of Community Affairs for housing rehabilitation and first time home buyer assistance of privately owned dwellings by primarily low income citizens.

***Tourism Fund*** – to account for expenditures designated for the promotion of local tourism. Resources are provided from the collection of hotel/motel occupancy tax revenues.

***Grant Fund*** – to account for receipt and disbursement of grant funds used to construct a new road to a new business.

***Public Improvement District*** – to account for costs of street improvements to Airport Road. Financing is provided from \$3,500,000 note proceeds from a local bank through the Terrell Economic Development Corporation and \$1,000,000 in assessments of property owners for a portion of the cost.

***Permanent Street Improvement Fund*** – to account for the cost of street improvements within the City. Financing is provided by the sale of general obligation bonds and assessments of property owners for a portion of the cost.

***C.O. Tax and Revenue Series 2002 Fund*** – to account for construction projects funded by the Series 2002 bond issuance.

***Infrastructure Improvements*** – to account for street and utility service construction for Pioneer Terraces multifamily housing subdivision.

***Impact Fees Fund*** – to account for fees charged on developments in order to improve current existing infrastructure.

***Park Land/Park Dedication Fees Fund*** – to account for fees charged on new residential construction for future parks development.

***Debt Service Fund*** – to account for the accumulation of resources for payment of interest and principal on general obligation long-term bonded debt. A portion of the annual ad valorem tax levy is designated for debt service.

**CITY OF TERRELL, TEXAS**  
**COMBINING BALANCE SHEET**  
**NONMAJOR GOVERNMENTAL FUNDS**  
**SEPTEMBER 30, 2007**

	Housing Rehabilitation and Ownership Assistance	Tourism	Grant	Public Improvement District
	<u>Assistance</u>	<u>Tourism</u>	<u>Grant</u>	<u>District</u>
<b>ASSETS</b>				
Cash and cash equivalents	\$ -	\$ 97,653	\$ 63,842	\$ 38,292
Taxes receivable, net	-	-	-	-
Due from other funds	-	-	-	-
Receivable from other governments	-	-	14,089	-
Special assessments	<u>-</u>	<u>-</u>	<u>-</u>	<u>46,364</u>
Total assets	<u>\$ -</u>	<u>\$ 97,653</u>	<u>\$ 77,931</u>	<u>\$ 84,656</u>
<b>LIABILITIES AND FUND BALANCES</b>				
Liabilities:				
Accounts payable	\$ -	\$ -	\$ 1,427	\$ -
Due to other funds	2	-	2,322	37,687
Deferred revenue	<u>-</u>	<u>-</u>	<u>-</u>	<u>46,364</u>
Total liabilities	<u>2</u>	<u>-</u>	<u>3,749</u>	<u>84,051</u>
Fund balances:				
Reserved for:				
Debt service	-	-	-	-
Grants/donations	( 2)	-	-	-
Capital projects	-	-	-	-
Unreserved	<u>-</u>	<u>97,653</u>	<u>74,182</u>	<u>605</u>
Total fund balances	<u>( 2)</u>	<u>97,653</u>	<u>74,182</u>	<u>605</u>
Total liabilities and fund balances	<u>\$ -</u>	<u>\$ 97,653</u>	<u>\$ 77,931</u>	<u>\$ 84,656</u>

<u>Permanent Street Improvement</u>	<u>Certificates Obligation Tax and Revenue Series 2002</u>	<u>Infrastructure Improvements</u>	<u>Impact Fees</u>	<u>Park Land/Park Dedication Fees</u>	<u>Debt Service</u>	<u>Total Governmental Funds</u>
\$ 562,835	\$ -	\$ -	\$ 1,032,731	\$ 102,881	\$ 502,761	\$ 2,400,995
-	-	-	-	-	112,398	112,398
54,143	-	-	-	-	-	54,143
-	-	-	-	-	-	14,089
<u>692,773</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>739,137</u>
<u>\$ 1,309,751</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 1,032,731</u>	<u>\$ 102,881</u>	<u>\$ 615,159</u>	<u>\$ 3,320,762</u>
\$ 7,319	\$ 74,214	\$ -	\$ 8,549	\$ -	\$ 328	\$ 91,837
10,325	-	-	-	-	93,430	143,766
692,773	-	-	-	-	108,082	847,219
<u>710,417</u>	<u>74,214</u>	<u>-</u>	<u>8,549</u>	<u>-</u>	<u>201,840</u>	<u>1,082,822</u>
-	-	-	-	-	413,319	413,319
-	-	-	-	-	-	( 2)
599,334	( 74,214)	-	1,024,182	102,881	-	1,652,183
-	-	-	-	-	-	172,440
<u>599,334</u>	<u>( 74,214)</u>	<u>-</u>	<u>1,024,182</u>	<u>102,881</u>	<u>413,319</u>	<u>2,237,940</u>
<u>\$ 1,309,751</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 1,032,731</u>	<u>\$ 102,881</u>	<u>\$ 615,159</u>	<u>\$ 3,320,762</u>

**CITY OF TERRELL, TEXAS**

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

**NONMAJOR GOVERNMENTAL FUNDS**

**FOR THE YEAR ENDED SEPTEMBER 30, 2007**

	Housing Rehabilitation and Ownership Assistance	Tourism	Grant	Public Improvement District
	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>
<b>REVENUES</b>				
Ad valorem taxes	\$ -	\$ -	\$ -	\$ -
Hotel/motel occupancy taxes	-	216,608	-	-
Intergovernmental	-	-	98,529	-
Charges for services	-	-	-	-
Interest	-	2,452	17,357	605
Street assessments	-	-	-	24,529
Total revenues	<u>-</u>	<u>219,060</u>	<u>115,886</u>	<u>25,134</u>
<b>EXPENDITURES</b>				
Current:				
General government	-	173,581	-	-
Public welfare	-	-	54,232	-
Principal	-	-	-	-
Interest and other charges	-	-	-	-
Total expenditures	<u>-</u>	<u>173,581</u>	<u>54,232</u>	<u>-</u>
<b>EXCESS (DEFICIENCY) OF REVENUES OVER EXPENDITURES</b>	<u>-</u>	<u>45,479</u>	<u>61,654</u>	<u>25,134</u>
<b>OTHER FINANCING SOURCES (USES)</b>				
Transfers in	-	-	184	-
Transfers out	<u>( 29)</u>	<u>-</u>	<u>-</u>	<u>( 24,529)</u>
Total other financing sources and uses	<u>( 29)</u>	<u>-</u>	<u>184</u>	<u>( 24,529)</u>
<b>NET CHANGE IN FUND BALANCES</b>	<u>( 29)</u>	<u>45,479</u>	<u>61,838</u>	<u>605</u>
<b>FUND BALANCES, BEGINNING</b>	<u>27</u>	<u>52,174</u>	<u>12,344</u>	<u>-</u>
<b>FUND BALANCES, ENDING</b>	<u><u>\$ ( 2)</u></u>	<u><u>\$ 97,653</u></u>	<u><u>\$ 74,182</u></u>	<u><u>\$ 605</u></u>

<u>Permanent Street Improvement</u>	<u>Certificates Obligation Tax and Revenue Series 2002</u>	<u>Infrastructure Improvements</u>	<u>Impact Fees</u>	<u>Park Land/Park Dedication Fees</u>	<u>Debt Service</u>	<u>Total Governmental Funds</u>
\$ -	\$ -	\$ -	\$ -	\$ -	\$ 1,627,388	\$ 1,627,388
-	-	-	-	-	-	216,608
100,000	-	-	-	-	-	198,529
-	-	-	145,549	20,000	-	165,549
16,238	-	-	36,941	1,880	23,322	98,795
1,596	-	-	-	-	-	26,125
<u>117,834</u>	<u>-</u>	<u>-</u>	<u>182,490</u>	<u>21,880</u>	<u>1,650,710</u>	<u>2,332,994</u>
81,387	-	10	14,548	-	-	269,526
-	-	-	-	-	-	54,232
-	-	-	-	-	1,370,000	1,370,000
-	-	-	-	-	650,950	650,950
<u>81,387</u>	<u>-</u>	<u>10</u>	<u>14,548</u>	<u>-</u>	<u>2,020,950</u>	<u>2,344,708</u>
<u>36,447</u>	<u>-</u>	<u>( 10)</u>	<u>167,942</u>	<u>21,880</u>	<u>( 370,240)</u>	<u>( 11,714)</u>
-	-	-	16,000	-	445,546	461,730
-	-	-	-	( 16,000)	-	( 40,558)
-	-	-	16,000	( 16,000)	445,546	421,172
36,447	-	( 10)	183,942	5,880	75,306	409,458
<u>562,887</u>	<u>( 74,214)</u>	<u>10</u>	<u>840,240</u>	<u>97,001</u>	<u>338,013</u>	<u>1,828,482</u>
<u>\$ 599,334</u>	<u>\$ ( 74,214)</u>	<u>\$ -</u>	<u>\$ 1,024,182</u>	<u>\$ 102,881</u>	<u>\$ 413,319</u>	<u>\$ 2,237,940</u>

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## **INTERNAL SERVICE FUNDS**

*Self-insurance Fund* – to account for the receipt and disbursement of medical insurance expenditures and related transfers from other funds.

*Equipment Replacement Fund* – to account for the acquisition, maintenance and other operation expenses of the City's fleet assets. Revenues are generated from the rental of equipment to various departments within the City.

**CITY OF TERRELL, TEXAS**  
**COMBINING STATEMENT OF NET ASSETS**  
**INTERNAL SERVICE FUNDS**  
**SEPTEMBER 30, 2007**

	<u>Self- insurance</u>	<u>Equipment Replacement</u>	<u>Total</u>
<b>ASSETS</b>			
Current assets:			
Cash and cash equivalents	\$ 16,178	\$ 849,586	\$ 865,764
Total current assets	<u>16,178</u>	<u>849,586</u>	<u>865,764</u>
Non-current assets:			
Capital assets:			
Vehicles and equipment	-	3,874,987	3,874,987
Accumulated depreciation	<u>-</u>	<u>( 2,207,684)</u>	<u>( 2,207,684)</u>
Total non-current assets	<u>-</u>	<u>1,667,303</u>	<u>1,667,303</u>
 Total assets	 <u>16,178</u>	 <u>2,516,889</u>	 <u>2,533,067</u>
<b>LIABILITIES</b>			
Current liabilities:			
Accounts payable	80,475	11,801	92,276
Other accrued expenses	-	3,579	3,579
Compensated absences	<u>-</u>	<u>7,677</u>	<u>7,677</u>
Total current liabilities	<u>80,475</u>	<u>23,057</u>	<u>103,532</u>
 Total liabilities	 <u>80,475</u>	 <u>23,057</u>	 <u>103,532</u>
<b>NET ASSETS</b>			
Invested in capital assets, net of related debt	-	1,667,303	1,667,303
Unrestricted	<u>( 64,297)</u>	<u>826,529</u>	<u>762,232</u>
 Total net assets	 <u><u>\$( 64,297)</u></u>	 <u><u>\$ 2,493,832</u></u>	 <u><u>\$ 2,429,535</u></u>

**CITY OF TERRELL, TEXAS**

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

**INTERNAL SERVICE FUNDS**

**FOR THE YEAR ENDED SEPTEMBER 30, 2007**

	<u>Self- insurance</u>	<u>Equipment Replacement</u>	<u>Total</u>
<b>OPERATING REVENUES</b>			
Maintenance services	\$ -	\$ 1,320,200	\$ 1,320,200
Insurance premiums	1,256,279	-	1,256,279
Miscellaneous	<u>2,645</u>	<u>14,011</u>	<u>16,656</u>
Total operating revenues	<u>1,258,924</u>	<u>1,334,211</u>	<u>2,593,135</u>
<b>OPERATING EXPENSES</b>			
Personnel services	-	175,302	175,302
Miscellaneous services	-	168,953	168,953
Administrative fees	521,766	-	521,766
Repairs and maintenance	-	62,104	62,104
Supplies	-	249,252	249,252
Insurance claims and expenses	687,959	-	687,959
Depreciation	<u>-</u>	<u>306,524</u>	<u>306,524</u>
Total operating expenses	<u>1,209,725</u>	<u>962,135</u>	<u>2,171,860</u>
<b>OPERATING INCOME</b>	49,199	372,076	421,275
<b>NON-OPERATING REVENUES (EXPENSES)</b>			
Interest and investment revenue	3,864	14,879	18,743
Interest expense	<u>-</u>	<u>( 5,447)</u>	<u>( 5,447)</u>
Total non-operating revenue (expenses)	<u>3,864</u>	<u>9,432</u>	<u>13,296</u>
<b>CHANGE IN NET ASSETS</b>	53,063	381,508	434,571
<b>TOTAL NET ASSETS, BEGINNING</b>	<u>( 117,360)</u>	<u>2,112,324</u>	<u>1,994,964</u>
<b>TOTAL NET ASSETS, ENDING</b>	<u><u>\$ ( 64,297)</u></u>	<u><u>\$ 2,493,832</u></u>	<u><u>\$ 2,429,535</u></u>

**CITY OF TERRELL, TEXAS**

**COMBINING STATEMENT OF CASH FLOWS**

**INTERNAL SERVICE FUNDS**

**FOR THE FISCAL YEAR ENDED SEPTEMBER 30, 2007**

	<u>Self-insurance</u>	<u>Equipment Replacement</u>	<u>Total</u>
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>			
Cash received from customers and users	\$ 1,258,924	\$ 1,334,211	\$ 2,593,135
Cash paid for services and insurance claims	( 1,246,234)	-	( 1,246,234)
Cash paid to suppliers for goods and services	-	( 473,756)	( 473,756)
Cash paid to employees for services	-	( 180,604)	( 180,604)
Net cash provided by operating activities	<u>12,690</u>	<u>679,851</u>	<u>692,541</u>
<b>CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES</b>			
Cash received from other funds	( 376)	-	( 376)
Net cash used for noncapital financing activities	<u>( 376)</u>	<u>-</u>	<u>( 376)</u>
<b>CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES</b>			
Acquisition of capital assets	-	( 199,254)	( 199,254)
Principal paid on long-term debt	-	( 192,121)	( 192,121)
Interest and fiscal charges paid on debt	-	( 5,447)	( 5,447)
Net cash used for capital and related financing activities	<u>-</u>	<u>( 396,822)</u>	<u>( 396,822)</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>			
Investment earnings	<u>3,864</u>	<u>14,879</u>	<u>18,743</u>
Net cash provided by investing activities	<u>3,864</u>	<u>14,879</u>	<u>18,743</u>
<b>INCREASE IN CASH</b>	16,178	297,908	314,086
<b>CASH AND CASH EQUIVALENTS, BEGINNING</b>	<u>-</u>	<u>551,678</u>	<u>551,678</u>
<b>CASH AND CASH EQUIVALENTS, ENDING</b>	<u>\$ 16,178</u>	<u>\$ 849,586</u>	<u>\$ 865,764</u>
<b>RECONCILIATION OF OPERATING INCOME (LOSS) TO NET CASH PROVIDED BY OPERATING ACTIVITIES</b>			
Operating income	\$ 49,199	\$ 372,076	\$ 421,275
Adjustments to reconcile net income (loss) to net cash provided by operating activities:			
Depreciation	-	306,524	306,524
Increase (decrease) in accounts payable	( 36,509)	6,553	( 29,956)
Increase (decrease) in accrued liabilities	-	( 3,912)	( 3,912)
Increase (decrease) in compensated absences	-	( 1,390)	( 1,390)
Net cash provided by operating activities	<u>\$ 12,690</u>	<u>\$ 679,851</u>	<u>\$ 692,541</u>

# **SINGLE AUDIT SECTION**

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**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**

To the Honorable City Council  
City of Terrell, Texas

We have audited the financial statements of the governmental activities, business-type activities, each major fund and the aggregate remaining fund information of the City of Terrell, Texas, as of and for the year ended September 30, 2007, which collectively comprise the City of Terrell, Texas' basic financial statements and have issued our report thereon dated April 7, 2008. 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's 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.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed below, we identified certain deficiencies in internal control over financial reporting that we consider to be significant deficiencies.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the City's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the City's financial statements that is more than inconsequential will not be prevented or detected by the City's internal control. We consider the deficiencies described in the accompanying Schedule of Findings and Questioned Costs to be significant deficiencies in internal control over financial reporting, Items 2007-01 through 2007-04.

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

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, of the significant deficiencies described above, we consider Items 2007-01 through 2007-04 to be a material weakness.

### **Compliance and Other Matters**

As part of obtaining reasonable assurance about whether the City's 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.

We noted certain matters that we reported to management of the City in a separate letter dated April 7, 2008.

The City's response to the findings identified in our audit is described in the accompanying Schedule of Findings and Questioned Costs. We did not audit the City's response and, accordingly, we express no opinion on it.

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

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

April 7, 2008



**REPORT ON COMPLIANCE WITH REQUIREMENTS APPLICABLE TO EACH  
MAJOR PROGRAM AND INTERNAL CONTROL OVER COMPLIANCE  
IN ACCORDANCE WITH OMB CIRCULAR A-133**

To the Honorable City Council  
City of Terrell, Texas

**Compliance**

We have audited the compliance of the City of Terrell, Texas, with the types of compliance requirements described in the *U. S. Office of Management and Budget (OMB) Circular A-133, Compliance Supplement* that are applicable to each of its major federal programs for the year ended September 30, 2007. The City of Terrell, Texas' 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 of Terrell, Texas' management. Our responsibility is to express an opinion on the City of Terrell, Texas' compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; 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 of Terrell, Texas' compliance with those requirements and performing such other procedures, as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on the City of Terrell, Texas' compliance with those requirements.

In our opinion, the City of Terrell, Texas, complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended September 30, 2007.

## Internal Control Over Compliance

The management of the City of Terrell, 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, 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 *control deficiency* in an entity's internal control over compliance exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect noncompliance with a type of compliance requirement of a federal program on a timely basis. A *significant deficiency* is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to administer a federal program such that there is more than a remote likelihood that noncompliance with a type of compliance requirement of a federal program that is more than inconsequential will not be prevented or detected by the entity's internal control.

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

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

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

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

April 7, 2008

**CITY OF TERRELL, TEXAS**

**SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS**

**FOR THE YEAR ENDED SEPTEMBER 30, 2007**

Federal Grantor/Pass-through Grantor/ Program Title	Federal CFDA Number	Pass-through Entity Identifying Number	Federal Expenditures
<b><u>U. S. Department of Housing and Urban Development</u></b>			
Passed through Office of Rural Community Affairs:			
Community Development Block Grant's State Program	14.228	724012	\$ <u>233,500</u>
Total Passed through Office of Rural Community Affairs			<u>233,500</u>
Direct Programs:			
HOME Investment Partnerships Program	14.239	N/A	<u>83,472</u>
Total Direct Programs			<u>83,472</u>
Passed through Department of Housing and Community Affairs:			
Section 8 Housing Choice Vouchers Program	14.871	TX493	<u>2,982,429</u>
Total Passed through Department of Housing and Community Affairs			<u>2,982,429</u>
Total U. S. Department of Housing and Urban Development			<u>3,299,401</u>
Total Expenditures of Federal Awards			\$ <u><u>3,299,401</u></u>

**CITY OF TERRELL, TEXAS**

**NOTES TO SCHEDULE OF FEDERAL AWARDS**

**FOR THE FISCAL YEAR ENDED SEPTEMBER 30, 2007**

**BASIS OF PRESENTATION**

The accompanying Schedule of Expenditures of Federal Awards includes the federal grant activity of the City of Terrell presented on the accrual basis of accounting. 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 amounts presented in this schedule may differ from amounts presented in, or used in the preparation of, the basic financial statements.

**CITY OF TERRELL, TEXAS**  
**SCHEDULE OF FINDINGS AND QUESTIONED COSTS**  
**FOR THE YEAR ENDED SEPTEMBER 30, 2007**

**Summary of Auditors' Results**

Type of report on financial statement	Unqualified
Internal control over financial reporting Material weakness(es) identified	Yes
Significant deficiencies identified that are not considered to be material weakness(es)	No
Internal control over major programs Material weakness(es) identified	No
Significant deficiencies identified that are not considered to be material weakness(es)	None reported
Noncompliance which is material to the basic financial statement	None
Type of report on compliance with major programs	Unqualified
Findings and questioned costs for federal awards as defined in Section 501(a), OMB Circular A-133 disclosed	None
Dollar threshold considered between Type A and Type B federal programs	\$300,000
Low risk auditee statement	The City was classified as a low-risk auditee in the context of OMB Circular A-133
Major federal program	Section 8 Rental Voucher Program, CFDA #14.871

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

None

(continued)

**CITY OF TERRELL, TEXAS**

**SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
(Continued)  
FOR THE YEAR ENDED SEPTEMBER 30, 2007**

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

**Item 2007-1**

Condition: The City Secretary/Finance Director has a wide range of duties, which include supervising all financial departments, making most journal entries, being in charge of all bank activity and utility operations. There is currently little oversight and segregation of duties for this function.

Effect: Currently, the City is relying heavily on one person to perform a wide range of tasks, many of which are significant to the financial statements. Over reliance on one individual makes the City more vulnerable to mistakes and increases the risk of a material misstatement to the financial statements.

Cause: The City Secretary/Finance Director's job description requires him to be in charge of most of the Finance Department as well as review the work performed in that area.

Recommendation: It is recommended the City amend the job descriptions and functions of the finance office to distribute duties among the staff and to allow for better review procedures to limit the amount of reliance on one person.

Management's Response: Staff concurs with the audit finding. Separate individuals should be responsible for custody, authorization, and recordkeeping within the finance department.

Over the past several years staff implemented several mitigating controls to address the separation of duties. This included the distribution of receipting and deposit recording by a municipal court clerk. Payroll functions are distributed between the department's Administrative Secretary and Accounts Payable Technician. Deposit reconciliation and bank deposits are completed by the Utility Billing Clerk. Clearing Fund and Payroll Reconciliation are outsourced. Reconciliation of other funds and all other financial functions are performed by the City Secretary/Finance Director.

Changes in internal operations during the past two years (i.e. Information Technology, Elections, etc.) required the City Secretary/Finance Director to assume additional duties that require significant time making the City more vulnerable to mistakes and increasing the risk of material misstatements.

**(continued)**

**CITY OF TERRELL, TEXAS**

**SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
(Continued)  
FOR THE YEAR ENDED SEPTEMBER 30, 2007**

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

**Item 2007-1** (Continued)

Management's Response: (Continued)

In the upcoming months staff will develop a plan with emphasis on the following action items:

- Review and develop detailed job descriptions and functions of the finance office.
- Review and develop appropriate staffing requirements for all functions associated to the City Secretary/Finance office.
- Develop appropriate review procedures and limit reliance on the City Secretary/Finance Director.

**Item 2007-2**

Condition: A prior period adjustment was required to record unspent Hurricane Katrina grant funds due to FEMA as a liability that had been recorded as revenue in a prior period.

Effect: Because the Katrina funds were recorded as revenue when received, liabilities as of September 30, 2006, were understated. Unspent grant proceeds should be recorded as deferred revenue, which is a liability, until they are spent.

Cause: Grant funds should only be recorded as revenues when they are spent on allowable expenditures. Since the funds from FEMA did not get spent, they should have been kept on the general ledger as a liability.

Recommendation: Grants are good sources of revenue that governments are able to use in certain situations. However, accounting for grants and adhering to their requirements can be difficult. The City should check with the granting agency as well as become familiar with the grant contract to verify the treatment of transactions involving grants. This will insure that all balances involving grant related transactions will be properly stated in the general ledger.

Management's Response: Staff acknowledges audit comment and concurs with the finding. During the next fiscal year, Staff will work closely with the Granting agency and the City's outside consulting auditor to ensure that balances involving grant related transactions will be properly stated in the general ledger.

(continued)

**CITY OF TERRELL, TEXAS**

**SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
(Continued)  
FOR THE YEAR ENDED SEPTEMBER 30, 2007**

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

**Item 2007-3**

Condition: The City had an inventory of capital assets performed during the 2008 fiscal year. Upon completion, the City had to make a prior period adjustment to governmental capital asset balances to get them to agree to the detailed listing of capital assets.

Effect: The City overstated governmental capital asset balances and net assets in prior periods.

Cause: The City has been keeping a detailed listing of capital assets and the related depreciation of these assets. However, the City has not compared the list to an actual physical inventory in several years. This caused actual assets to deviate from those on the capital assets schedules by material amounts.

Recommendation: The City should periodically complete physical inventories over capital assets. This will aid in keeping the detailed list of capital assets in agreement with actual capital assets. By comparing the actual to the list, the City can evaluate differences and verify that assets are properly disposed of.

Management's Response: Staff acknowledges audit comment and concurs with the finding. In the 2007 fiscal year, the City retained the services of American Appraisal Associates to update the capital assets inventory. Additional dedicated resources are required to develop, set and sustain procedures and systems that will assure the timely identification, tracking, recording, and periodic physical inspection of the City's capital assets. Staff goals include:

- Reviewing the status and propriety of Capital Asset accounting ledgers.
- Extending the Capital Asset General Ledger reconciliation to the current year.
- Updating the fiscal year 2008 asset values on a timely basis.
- Perform controlled interim and year-end physical inventory at all warehouse locations.
- Implement formal test count procedures
- Document control and operational procedures.

**(continued)**

**CITY OF TERRELL, TEXAS**

**SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
(Continued)  
FOR THE YEAR ENDED SEPTEMBER 30, 2007**

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

**Item 2007-4**

- Condition: During the audit entries were required to record A/P at the end of the year for the self-insurance fund and for Terrell Economic Development Corporation. In each case, the entry required was considered material to that opinion unit.
- Effect: The City's liabilities were materially understated in two separate funds.
- Cause: The City did not review the payable balances in both areas and record these amounts to the general ledger. This will allow the City to properly state payable balances at the end of the fiscal year.
- Recommendation: We recommend the City review invoices that come in after year-end and accrue proper amounts and liability balances. The City should also look at the "lag" report over insurance claims to verify that liability amounts are stated at proper amounts.
- Management's Response: Staff acknowledges audit comments and concurs with the findings. The City will monitor the insurance "lag" report on a regular basis to ensure outstanding insurance claims are properly reflected in the liabilities of the self-insurance fund. The City reviews invoices that come in after year-end and if needed, accrues the amounts into liabilities. On occasion, a vendor or contractor will not submit invoices in a timely manner which causes the invoice to be overlooked during the review process. In the future, the City will extend the time-range of the review to ensure that late arriving invoices are properly accounted for.

**Findings and Questioned Costs for Federal Awards**

None

**CITY OF TERRELL, TEXAS**  
**SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS**  
**YEAR ENDED SEPTEMBER 30, 2007**

None