

CITY OF TERRELL, TEXAS

ANNUAL FINANCIAL REPORT

SEPTEMBER 30, 2011

CITY OF TERRELL, TEXAS

TABLE OF CONTENTS

SEPTEMBER 30, 2011

	<u>Page Number</u>
INTRODUCTORY SECTION	
Letter of Transmittal	i – iv
Organization Chart.....	v
Principal Officials	vi
FINANCIAL SECTION	
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, 2011**

	<u>Page Number</u>
FINANCIAL SECTION (Continued)	
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 – 49
Combining Statements	
Nonmajor Governmental Funds	
Combining Balance Sheet.....	50 – 53
Combining Statement of Revenues, Expenditures and Changes in Fund Balances.....	54 – 57
Internal Service Funds	
Combining Statement of Net Assets.....	58
Combining Statement of Revenues, Expenses and Changes in Fund Net Assets	59
Combining Statement of Cash Flows	60

(continued)

CITY OF TERRELL, TEXAS

**TABLE OF CONTENTS
(Continued)
SEPTEMBER 30, 2011**

**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>	61 – 62
Independent Auditors’ Report on Compliance With Requirements Applicable to Each Major Program and Internal Control Over Compliance in Accordance With OMB Circular A-133.....	63 – 64
Schedule of Expenditures of Federal Awards.....	65
Notes to the Schedule of Expenditures of Federal Awards	66
Schedule of Findings and Questioned Costs.....	67 – 69
Summary Schedule of Prior Audit Findings.....	70

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INTRODUCTORY SECTION

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June 15, 2012

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, 2011.

Ricky Jordan
Mayor Pro Tem
District 3

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.

D.J. Ory
Dep. Mayor Pro Tem
District 5

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. 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.

Tommy Spencer
Council Member
District 2

THE REPORT

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 Expenditures and Federal Awards and reports required by the Federal Single Audit Act of 1996.

Charles Whitaker
Council Member
District 4

Torry L. Edwards
City Manager

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.

Mike Sims
Asst. City Manager

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 20.04 square miles, had a 2010 census population of 15,816 which is a 16% increase from the 2000 census population of 13,600.

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. Promotion and development of commercial, industrial, and manufacturing enterprises that create and enhance local job opportunities are provided through a legally separate entity. The Terrell Economic Development Corporation (“TEDC”) which functions, in essence, as a department of the City of Terrell has been included as an integral part of the City of Terrell’s financial statements. Additional information on this legally separate entity can be found in the notes to the financial statements (see Note I.A.).

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, along with airport services. 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, which include Southwestern Christian College and Trinity Valley Community College.

The City actively 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.

Assessed property valuations and sales tax collected for the 10 previous years are as follows:

	ASSESSED PROPERTY VALUATIONS (in millions)	SALES TAX COLLECTIONS (in millions)
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
2008	1,014,913,277	7,123,040
2009	1,005,646,462	6,528,921
2010	1,023,058,460	6,744,263
2011	947,284,405	6,867,379

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 October 31, 2014.

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, 2011, all idle cash totaling \$4,438,329 was invested in certificates of deposit. The overall portfolio provided \$74,481 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 \$50,000 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 2011 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

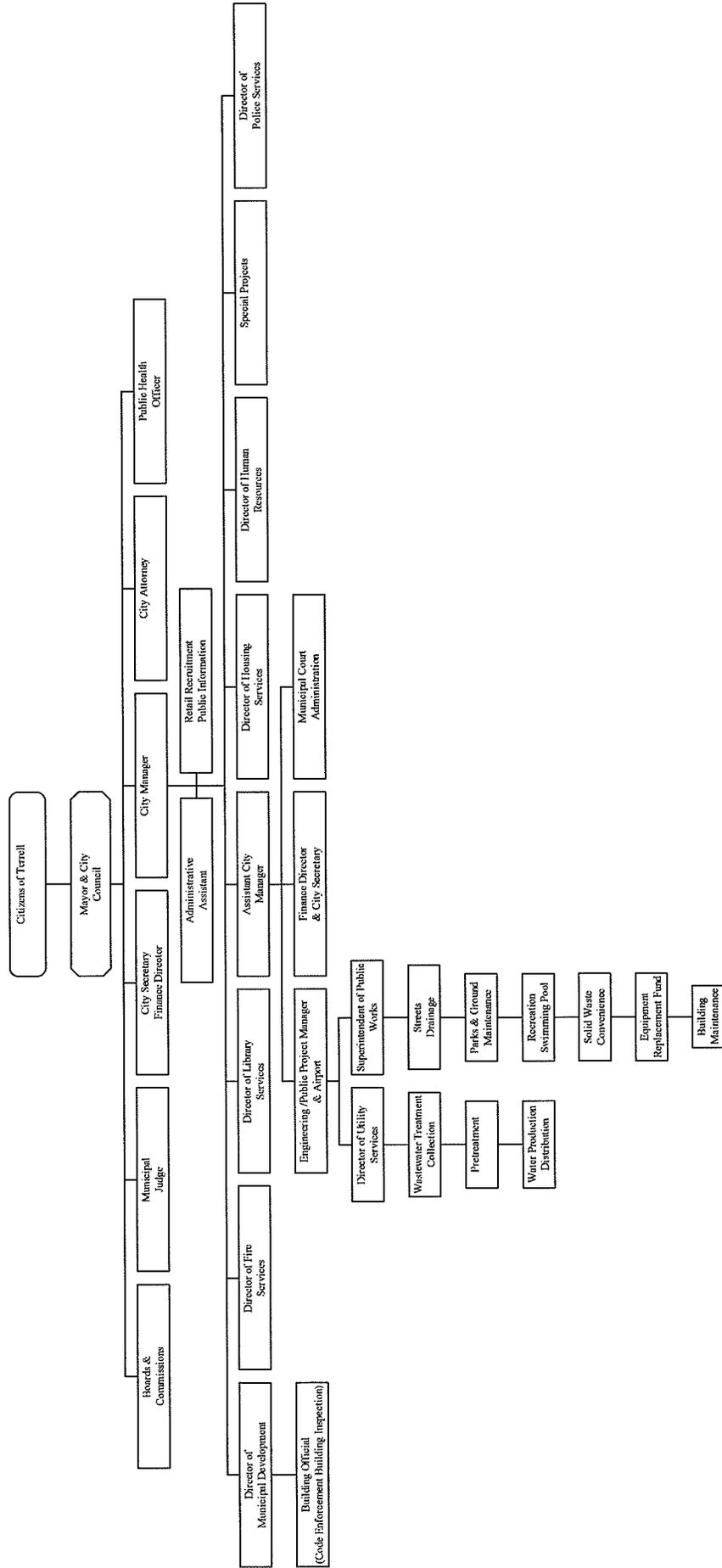
The preparation of this report could not be accomplished without the efficient and dedicated services of the entire staff of all City departments. We would like to express our appreciation to all members of the City's staff who assisted and contributed to its preparation. We would also like to thank 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, 2011

CITY OFFICIALS

Mayor.....Hal Richards
Council Members..... Ricky Jordan, Mayor Pro-Tem
D. J. Ory, Deputy Mayor Pro-Tem
Tommy Spencer
Charles Whitaker
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, 2011, 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, each major fund, and the aggregate remaining fund information of the City of Terrell, Texas, as of September 30, 2011, and the respective changes in financial position, and where applicable, cash flows, thereof and the respective budgetary comparison for the General Fund 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 June 15, 2012, 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 internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards*, and should be considered in assessing the results of our audit.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 3 through 10 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

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

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

June 15, 2012

**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, 2011. 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 \$63,020,745 (net assets). Of this amount, \$11,333,680 (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 \$4,291,505 from operations.
- As of the close of the current fiscal year, the City of Terrell's governmental funds reported combined ending fund balances of \$10,874,108, an increase of \$854,195 in comparison with the prior fiscal year. Approximately 26% of this total amount, \$2,832,081, is available for spending at the City's discretion (unassigned fund balance).
- At the end of the current fiscal year, unassigned fund balance for the General Fund was \$3,097,054 or 23% of the total General Fund expenditures.
- The City's total long-term debt increased by \$4,781,173 during the current fiscal year. The key factor in this increase was the issuance of the 2011A and 2011B Certificates of Obligation.

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 24 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, the 2007A Bond Fund, and the Permanent Street Improvement Fund, each of which are considered to be major funds. Data from the other 18 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 proprietary 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 – 49 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 50 – 60 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 \$63,020,745 as of September 30, 2011.

The largest portion of the City's net assets, 68% (\$43,115,839), 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	
	2011	2010	2011	2010	2011	2010
Current and other assets	\$ 13,428,796	\$ 13,178,104	\$ 12,548,258	\$ 10,868,727	\$ 25,977,054	\$ 24,046,831
Capital assets	<u>22,751,389</u>	<u>23,953,693</u>	<u>48,933,171</u>	<u>40,384,897</u>	<u>71,684,560</u>	<u>64,338,590</u>
Total assets	<u>36,180,185</u>	<u>37,131,797</u>	<u>61,481,429</u>	<u>51,253,624</u>	<u>97,661,614</u>	<u>88,385,421</u>
Long-term liabilities	20,229,512	19,503,908	11,762,548	7,706,979	31,992,060	27,210,887
Other liabilities	<u>987,189</u>	<u>1,236,927</u>	<u>1,661,620</u>	<u>1,208,367</u>	<u>2,648,809</u>	<u>2,445,294</u>
Total liabilities	<u>21,216,701</u>	<u>20,740,835</u>	<u>13,424,168</u>	<u>8,915,346</u>	<u>34,640,869</u>	<u>29,656,181</u>
Net assets:						
Invested in capital assets,						
net of related debt	5,882,668	6,987,265	37,233,171	32,739,897	43,115,839	39,727,162
Restricted	7,951,760	4,938,903	619,466	616,525	8,571,226	5,555,428
Unrestricted	<u>1,129,056</u>	<u>4,464,794</u>	<u>10,204,624</u>	<u>8,981,856</u>	<u>11,333,680</u>	<u>13,446,650</u>
Total net assets	<u>\$ 14,963,484</u>	<u>\$ 16,390,962</u>	<u>\$ 48,057,261</u>	<u>\$ 42,338,278</u>	<u>\$ 63,020,745</u>	<u>\$ 58,729,240</u>

Analysis of the City's Operations

The following table provides a summary of the City's operations for the years ended September 30, 2011 and 2010.

CITY OF TERRELL'S CHANGES IN NET ASSETS

	Governmental Activities		Business-type Activities		Totals	
	2011	2010	2011	2010	2011	2010
Revenues:						
Program revenues:						
Charges for services	\$ 1,226,397	\$ 1,393,877	\$ 10,701,563	\$ 9,952,285	\$ 11,927,960	\$ 11,346,162
Operating grants and contributions	3,797,580	4,325,280	-	-	3,797,580	4,325,280
Capital grants and contributions	-	-	2,494,436	1,221,619	2,494,436	1,221,619
General revenues:						
Property taxes	6,176,372	6,692,572	-	-	6,176,372	6,692,572
Franchise taxes	1,369,396	1,265,384	-	-	1,369,396	1,265,384
Sales taxes	6,856,810	6,745,645	-	-	6,856,810	6,745,645
Other taxes	294,587	300,880	-	-	294,587	300,880
Interest	29,225	89,663	45,260	98,264	74,485	187,927
Miscellaneous	229,193	179,818	1,275	47,516	230,468	227,334
Gain on sale of capital assets	-	3,156	-	-	-	3,156
Contributed Capital	-	-	-	-	-	-
Transfers	(803,005)	(808,986)	803,005	808,986	-	-
Total revenues	<u>19,176,555</u>	<u>20,187,289</u>	<u>14,045,539</u>	<u>12,128,670</u>	<u>33,222,094</u>	<u>32,315,959</u>
Expenses:						
General government	6,725,715	6,121,362	-	-	6,725,715	6,121,362
Public welfare	3,318,781	3,012,076	-	-	3,318,781	3,012,076
Public safety	6,871,948	6,354,682	-	-	6,871,948	6,354,682
Highways and streets	2,021,429	2,636,481	-	-	2,021,429	2,636,481
Sanitation	603,816	565,793	-	-	603,816	565,793
Culture and recreation	651,704	669,093	-	-	651,704	669,093
Interest on long-term debt	721,017	686,893	-	-	721,017	686,893
Water and sewer	-	-	7,874,865	7,411,898	7,874,865	7,411,898
Airport	-	-	451,691	379,011	451,691	379,011
Total expenses	<u>20,914,410</u>	<u>20,046,380</u>	<u>8,326,556</u>	<u>7,790,909</u>	<u>29,240,966</u>	<u>27,837,289</u>
Change in net assets	(1,737,855)	140,909	5,718,983	4,337,761	3,981,128	4,478,670
Net assets, beginning	<u>16,390,962</u>	<u>16,250,053</u>	<u>42,338,278</u>	<u>38,000,517</u>	<u>58,729,240</u>	<u>54,250,570</u>
Prior period adjustment	<u>310,377</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>310,377</u>	<u>-</u>
Net assets, ending	<u>\$ 14,963,484</u>	<u>\$ 16,390,962</u>	<u>\$ 48,057,261</u>	<u>\$ 42,338,278</u>	<u>\$ 63,020,745</u>	<u>\$ 58,729,240</u>

Governmental activities. Of the City's \$4,291,505 overall increase in net assets, governmental activities net assets decreased by \$1,737,855. The most significant governmental expense for the City was general government, which incurred expenses of \$6,725,715. These expenses were funded by revenues collected from a variety of sources, with one of the largest being from sales taxes, which are \$6,856,810 for the fiscal year ended September 30, 2009. Other significant governmental expenses for the City include public safety, which incurred \$6,871,948 in expenses.

Business-type activities. Business-type activities increased the City's net assets by \$5,718,983.

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, unassigned fund balance may serve as a useful measure of a government's net resources available for spending at the end of the fiscal year.

At the end of the current fiscal year, the City of Terrell's governmental funds reported combined ending fund balances of \$10,874,108. Approximately 26% of this total amount (\$2,832,081) constitutes unassigned 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 (\$1,165,154), (2) pay for debt service (\$1,027,012), (3) pay for tourism/economic development (\$4,456,910), (4) pay for grants \$1,105,706, (5) pay for law enforcement \$53,367, (6) pay for park development \$49,604, and (7) pay for development within tax increment reinvestment zones \$165,009.

In the General Fund, the City budgeted for an increase in the fund balance of \$337,755. Actual revenues being less than budgeted, the actual fund balance increased for fiscal year 2011 by \$908,572.

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, \$32,110,074; and the Airport Fund, \$15,947,187. The Water and Sewer Fund's net assets increased in 2011 by \$3,039,498 and the Airport's net assets increased by \$2,679,485.

General Fund Budgetary Highlights

The City made slight 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 \$69,245.

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 more than the budgeted revenue amount by \$415,605.

CAPITAL ASSETS

The City of Terrell's investment in capital assets for its governmental and business-type activities as of September 30, 2011, amounts to \$71,684,560 (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:

- \$9,722,648 was completed on various governmental and business-type construction projects that continue to be in progress; and

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

	Governmental Activities		Business-type Activities		Totals	
	2011	2010	2011	2010	2011	2010
Land	\$ 718,000	\$ 718,000	\$ 1,077,278	\$ 997,340	\$ 1,795,278	\$ 1,715,340
Buildings and improvements	5,192,260	5,456,596	11,517,868	11,872,245	16,710,128	17,328,841
Machinery and equipment	1,482,252	1,580,871	21,686,181	22,467,793	23,168,433	24,048,664
Infrastructure	15,240,553	16,198,226	-	-	15,240,553	16,198,226
Construction in progress	118,324	-	14,651,844	5,047,520	14,770,168	5,047,520
Total capital assets	\$ 22,751,389	\$ 23,953,693	\$ 48,933,171	\$ 40,384,898	\$ 71,684,560	\$ 64,338,591

The largest increase came from airport additions from the TxDOT RAMP grant, Bachelor Creek Improvements, and new storage tank and Phase 1 of utility system improvements. Additional information on the City of Terrell's capital assets can be found in Note 4 on pages 38 – 39 of this report.

DEBT ADMINISTRATION

At the end of the current fiscal year, the City of Terrell had a total bonded debt of \$25,645,000. Of this amount, \$25,445,000 comprises bonded debt backed by the combination of property tax and water/sewer revenues and \$200,000 represents bonds secured solely by water and sewer revenues.

CITY OF TERRELL'S OUTSTANDING DEBT AT YEAR-END

	Governmental Activities		Business-type Activities		Totals	
	2011	2010	2011	2010	2011	2010
General obligation bonds	\$ 1,185,000	\$ 1,575,000	\$ -	\$ -	\$ 1,185,000	\$ 1,575,000
Certificates of obligation	12,760,000	11,985,000	11,500,000	7,345,000	24,260,000	19,330,000
Revenue bonds payable	-	-	200,000	300,000	200,000	300,000
	\$ 13,945,000	\$ 13,560,000	\$ 11,700,000	\$ 7,645,000	\$ 25,645,000	\$ 21,205,000

During the current fiscal year, the City's total bonded debt increased by \$4,440,000 or 21%. This was due to the issuance of the 2011A and B bonds during FY 2011.

The City's bond ratings are listed below:

	<u>Moody's Investors Service</u>	<u>Standard & Poor's</u>
General Obligation Bonds	A1	AA
Revenue Bonds	A1	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 41 – 44 of this report.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGET AND RATES

In the fiscal year 2011 – 2012 budget, General Fund revenues and transfers in are budgeted to decrease by \$2,054,163 from the 2010 – 2011 budget year, with sales taxes making up about 44% of General Fund budgeted revenues and transfers in. Certified assessed valuations decreased over the preceding year. The tax base has increased by a strong annual average of over the past five years. The City's budgets for all funds have decreased from a declining local economy. However, the City's 2011 – 2012 budget reflects slower 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 for fiscal year 2010 – 2011; and it appears to show signs of a marginal increase during the 2011 – 2012 fiscal year. However, this revenue source is the most volatile and sensitive to changes in the local economy.

The budget for 2011 – 2012 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.

**BASIC
FINANCIAL STATEMENTS**

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CITY OF TERRELL, TEXAS
STATEMENT OF NET ASSETS
SEPTEMBER 30, 2011

	Governmental Activities	Business-type Activities	Total
ASSETS			
Cash and investments	\$ 7,597,766	\$ 10,389,304	\$ 17,987,070
Receivables (net, where applicable, of allowances for uncollectibles)	1,784,218	1,493,663	3,277,881
Internal balances	413,712	(413,712)	-
Special assessments	859,063	-	859,063
Investment in land	1,377,312	-	1,377,312
Investment in building	1,216,829	-	1,216,829
Funds in escrow	33,540	-	33,540
Inventory, at cost	19,265	216,603	235,868
Restricted cash and investments	-	619,466	619,466
Deferred charges	127,091	242,934	370,025
Capital assets:			
Land	718,000	1,077,278	1,795,278
Buildings and improvements	6,088,130	57,026,571	63,114,701
Improvements other than buildings	1,823,085	-	1,823,085
Machinery and equipment	4,922,547	137,199	5,059,746
Infrastructure	38,329,128	-	38,329,128
Construction in progress	118,324	14,651,844	14,770,168
Less accumulated depreciation	(29,247,825)	(23,959,721)	(53,207,546)
Total capital assets	22,751,389	48,933,171	71,684,560
Total assets	36,180,185	61,481,429	97,661,614
LIABILITIES			
Accounts payable	566,039	1,124,845	1,690,884
Accrued interest payable	69,681	79,434	149,115
Unearned revenue	14,501	-	14,501
Other accrued liabilities	336,968	69,593	406,561
Customer deposits	-	326,225	326,225
Due to other governments	-	61,523	61,523
Long-term liabilities:			
Due within one year	1,918,156	707,510	2,625,666
Due in more than one year	18,311,356	11,055,038	29,366,394
Total liabilities	21,216,701	13,424,168	34,640,869
NET ASSETS			
Invested in capital assets, net of related debt	5,882,668	37,233,171	43,115,839
Restricted for:			
Tourism/economic development	4,456,910	-	4,456,910
Grants	1,105,706	-	1,105,706
Law enforcement	53,367	-	53,367
Capital projects	2,024,218	-	2,024,218
Park development	49,604	-	49,604
TIRZ	165,009	-	165,009
Debt service	96,946	619,466	716,412
Unrestricted	1,129,056	10,204,624	11,333,680
Total net assets	\$ 14,963,484	\$ 48,057,261	\$ 63,020,745

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

CITY OF TERRELL, TEXAS

STATEMENT OF ACTIVITIES

FOR THE YEAR ENDED SEPTEMBER 30, 2011

Functions/Programs	Expenses	Program Revenue		
		Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions
Primary government				
Governmental activities:				
General government	\$ 6,725,715	\$ 163,358	\$ 347,264	\$ -
Public welfare	3,318,781	11,608	3,437,492	-
Public safety	6,871,948	369,443	12,824	-
Highways and streets	2,021,429	47,404	-	-
Sanitation	603,816	508,217	-	-
Culture and recreation	651,704	126,367	-	-
Interest on long-term debt	721,017	-	-	-
Total governmental activities	<u>20,914,410</u>	<u>1,226,397</u>	<u>3,797,580</u>	<u>-</u>
Business-type activities:				
Water and sewer	7,874,865	10,283,837	-	82,834
Airport	451,691	417,726	-	2,411,602
Total business-type activities	<u>8,326,556</u>	<u>10,701,563</u>	<u>-</u>	<u>2,494,436</u>
Total primary government	<u>\$ 29,240,966</u>	<u>\$ 11,927,960</u>	<u>\$ 3,797,580</u>	<u>\$ 2,494,436</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
\$(6,215,093)	\$ -	\$(6,215,093)
130,319	-	130,319
(6,489,681)	-	(6,489,681)
(1,974,025)	-	(1,974,025)
(95,599)	-	(95,599)
(525,337)	-	(525,337)
(721,017)	-	(721,017)
<u>(15,890,433)</u>	<u>-</u>	<u>(15,890,433)</u>
-	2,491,806	2,491,806
-	2,377,637	2,377,637
<u>-</u>	<u>4,869,443</u>	<u>4,869,443</u>
<u>-</u>	<u>4,869,443</u>	<u>4,869,443</u>
4,402,817	-	4,402,817
1,773,555	-	1,773,555
6,856,810	-	6,856,810
1,369,396	-	1,369,396
294,587	-	294,587
29,225	45,260	74,485
229,193	1,275	230,468
(803,005)	803,005	-
<u>14,152,578</u>	<u>849,540</u>	<u>15,002,118</u>
(1,737,855)	5,718,983	3,981,128
<u>16,390,962</u>	<u>42,338,278</u>	<u>58,729,240</u>
<u>310,377</u>	<u>-</u>	<u>310,377</u>
<u>\$ 14,963,484</u>	<u>\$ 48,057,261</u>	<u>\$ 63,020,745</u>

CITY OF TERRELL, TEXAS

BALANCE SHEET

GOVERNMENTAL FUNDS

SEPTEMBER 30, 2011

	<u>General</u>	<u>Rent Supplement Section 8</u>	<u>Terrell Economic Development Corporation</u>
ASSETS			
Cash and investments	\$ 1,526,239	\$ 968,050	\$ 1,835,404
Taxes receivable, net	1,630,540	-	-
Due from other funds	943,597	-	-
Special assessments	-	-	-
Investment in land	-	-	1,377,312
Investment in building	-	-	1,216,829
Other receivables	31,958	1,582	-
Inventories	<u>19,265</u>	<u>-</u>	<u>-</u>
 Total assets	 <u>\$ 4,151,599</u>	 <u>\$ 969,632</u>	 <u>\$ 4,429,545</u>
LIABILITIES AND FUND BALANCES			
Liabilities:			
Accounts payable	\$ 312,960	\$ 22,667	\$ 8,090
Accrued wages payable	328,899	-	-
Due to other funds	5,078	-	70,786
Deferred revenue	<u>388,343</u>	<u>-</u>	<u>-</u>
Total liabilities	<u>1,035,280</u>	<u>22,667</u>	<u>78,876</u>
Fund balances:			
Non-spendable	19,265	-	-
Restricted:			
Tourism/economic development	-	-	4,350,669
Grants	-	946,965	-
Law enforcement	-	-	-
Capital projects	-	-	-
Park development	-	-	-
TIRZ	-	-	-
Debt service	-	-	-
Unassigned	<u>3,097,054</u>	<u>-</u>	<u>-</u>
Total fund balances	<u>3,116,319</u>	<u>946,965</u>	<u>4,350,669</u>
 Total liabilities and fund balances	 <u>\$ 4,151,599</u>	 <u>\$ 969,632</u>	 <u>\$ 4,429,545</u>

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

Certificates of Obligation Tax and Revenue Series 2004	2007A Bond	Permanent Street Improvement	Other Governmental Funds	Total Governmental Funds
\$ 41,799	\$ 23,063	\$ 366,550	\$ 2,535,824	\$ 7,296,929
-	-	-	153,678	1,784,218
-	-	54,142	5,000	1,002,739
-	-	859,063	-	859,063
-	-	-	-	1,377,312
-	-	-	-	1,216,829
-	-	-	-	33,540
-	-	-	-	19,265
<u>\$ 41,799</u>	<u>\$ 23,063</u>	<u>\$ 1,279,755</u>	<u>\$ 2,694,502</u>	<u>\$ 13,589,895</u>
\$ -	\$ -	\$ -	\$ 53,970	\$ 397,687
-	-	-	-	328,899
58,265	-	10,325	444,573	589,027
-	-	861,564	150,267	1,400,174
<u>58,265</u>	<u>-</u>	<u>871,889</u>	<u>648,810</u>	<u>2,715,787</u>
-	-	-	-	19,265
-	-	-	106,241	4,456,910
-	-	-	158,741	1,105,706
-	-	-	53,367	53,367
-	23,063	407,866	734,225	1,165,154
-	-	-	49,604	49,604
-	-	-	165,009	165,009
-	-	-	1,027,012	1,027,012
(16,466)	-	-	(248,507)	2,832,081
<u>(16,466)</u>	<u>23,063</u>	<u>407,866</u>	<u>2,045,692</u>	<u>10,874,108</u>
<u>\$ 41,799</u>	<u>\$ 23,063</u>	<u>\$ 1,279,755</u>	<u>\$ 2,694,502</u>	<u>\$ 13,589,895</u>

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CITY OF TERRELL, TEXAS

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

SEPTEMBER 30, 2011

Total fund balance, governmental funds	\$ 10,874,108
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.	21,743,972
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.	1,385,673
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.	1,123,123
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.	(20,163,392)
Net assets of governmental activities in the Statement of Net Assets	\$ <u>14,963,484</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, 2011

	General	Rent Supplement Section 8	Terrell Economic Development Corporation
REVENUES			
Taxes and special assessments	\$ 11,090,267	\$ -	\$ 1,672,748
Licenses and permits	111,032	-	-
Hotel/motel occupancy taxes	-	-	-
Fees and fines	352,882	-	-
Intergovernmental	381,557	3,181,102	-
Charges for services	626,309	-	9,661
Investment earnings	9,661	3,796	4,710
Miscellaneous	284,778	1,969	425
Total revenues	12,856,486	3,186,867	1,687,544
EXPENDITURES			
Current:			
General government	4,557,768	275,035	550,609
Public welfare	-	2,811,992	-
Public safety	6,233,680	-	-
Highways and streets	1,160,233	-	-
Sanitation	556,061	-	-
Culture and recreation	509,032	-	-
Principal	98,458	-	411,982
Interest and other charges	4,046	-	130,388
Capital outlay	177,709	-	114,107
Total expenditures	13,296,987	3,087,027	1,207,086
EXCESS (DEFICIENCY) OF REVENUES OVER (UNDER) EXPENDITURES	(440,501)	99,840	480,458
OTHER FINANCING SOURCES (USES)			
Proceeds from long-term debt	-	-	-
Transfers in	1,349,073	-	-
Transfers out	-	-	(179,425)
Total other financing sources and uses	1,349,073	-	(179,425)
NET CHANGE IN FUND BALANCES	908,572	99,840	301,033
FUND BALANCES, BEGINNING	2,207,747	847,125	4,049,636
PRIOR PERIOD ADJUSTMENT	-	-	-
FUND BALANCES, ENDING	\$ 3,116,319	\$ 946,965	\$ 4,350,669

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

Certificates of Obligation Tax and Revenue Series 2004	2007 A Bond	Permanent Street Improvement	Other Governmental Funds	Total Governmental Funds
\$ -	\$ -	\$ -	\$ 1,822,631	\$ 14,585,646
-	-	-	-	111,032
-	-	-	247,669	247,669
-	-	-	-	352,882
-	-	-	279,770	3,842,429
-	-	-	38,759	674,729
1,070	65	1,271	6,291	26,864
-	-	-	-	287,172
<u>1,070</u>	<u>65</u>	<u>1,271</u>	<u>2,395,120</u>	<u>20,128,423</u>
-	-	80,121	267,065	5,730,598
-	-	-	244,311	3,056,303
-	-	-	16,807	6,250,487
-	-	-	-	1,160,233
-	-	-	-	556,061
-	-	-	16,967	525,999
-	-	-	1,177,047	1,687,487
-	-	-	574,431	708,865
-	-	48,842	1	340,659
<u>-</u>	<u>-</u>	<u>128,963</u>	<u>2,296,629</u>	<u>20,016,692</u>
<u>1,070</u>	<u>65</u>	<u>(127,692)</u>	<u>98,491</u>	<u>111,731</u>
-	-	-	1,545,000	1,545,000
-	-	-	1,308,621	2,657,694
(791,058)	-	-	(2,489,747)	(3,460,230)
(791,058)	-	-	363,874	742,464
(789,988)	65	(127,692)	462,365	854,195
773,522	(175,539)	535,558	1,471,487	9,709,536
-	198,537	-	111,840	310,377
<u>\$(16,466)</u>	<u>\$ 23,063</u>	<u>\$ 407,866</u>	<u>\$ 2,045,692</u>	<u>\$ 10,874,108</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, 2011

Net change in fund balances - total governmental funds:	\$	854,195
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.	(1,089,062)
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.	(151,224)
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.		97,707
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.	(790,682)
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.	(<u>658,789</u>)
Change in net assets of governmental activities	\$	<u>(1,737,855)</u>

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

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CITY OF TERRELL, TEXAS

GENERAL FUND

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

FOR THE YEAR ENDED SEPTEMBER 30, 2011

	Budgeted Amounts		Actual Amounts, Budgetary Basis	Variance with Final Budget Positive (Negative)
	Original	Final		
REVENUES				
Property taxes	\$ 4,418,059	\$ 4,418,059	\$ 4,489,891	\$ 71,832
Sales and miscellaneous taxes	6,253,000	6,253,000	6,600,376	347,376
Fees and fines	503,000	503,000	352,882	(150,118)
Licenses and permits	93,950	93,950	111,032	17,082
Intergovernmental	373,217	382,462	381,557	(905)
Charges for services	624,580	624,580	626,309	1,729
Investment earnings	10,000	10,000	9,661	(339)
Miscellaneous	155,830	155,830	284,778	128,948
Total revenues	<u>12,431,636</u>	<u>12,440,881</u>	<u>12,856,486</u>	<u>415,605</u>
EXPENDITURES				
Current:				
General government	4,343,362	4,412,607	4,557,768	(145,161)
Public safety	6,231,584	6,231,584	6,233,680	(2,096)
Highways and street	1,282,808	1,282,808	1,160,233	122,575
Sanitation	564,475	564,475	556,061	8,414
Culture and recreation	513,740	513,740	509,032	4,708
Debt service:				
Principal	213,379	213,379	98,458	114,921
Interest and other charges	16,147	16,147	4,046	12,101
Capital outlay	-	-	177,709	(177,709)
Total expenditures	<u>13,165,495</u>	<u>13,234,740</u>	<u>13,296,987</u>	<u>(62,247)</u>
EXCESS (DEFICIENCY) OF REVENUES OVER (UNDER) EXPENDITURES	<u>(733,859)</u>	<u>(793,859)</u>	<u>(440,501)</u>	<u>353,358</u>
OTHER FINANCING SOURCES (USES)				
Transfers in	1,032,264	1,131,614	1,349,073	217,459
Total other financing sources and uses	<u>1,032,264</u>	<u>1,131,614</u>	<u>1,349,073</u>	<u>217,459</u>
NET CHANGE IN FUND BALANCES	298,405	337,755	908,572	570,817
FUND BALANCES, BEGINNING	<u>2,207,747</u>	<u>2,207,747</u>	<u>2,207,747</u>	<u>-</u>
FUND BALANCES, ENDING	<u>\$ 2,506,152</u>	<u>\$ 2,545,502</u>	<u>\$ 3,116,319</u>	<u>\$ 570,817</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, 2011

	Business-type Activities			Governmental Activities
	Water and Sanitary Sewer	Airport	Total	Internal Service Funds
ASSETS				
Current assets:				
Cash and investments	\$ 8,932,349	\$ 1,456,955	\$ 10,389,304	\$ 300,837
Cash and investments - restricted	619,466	-	619,466	-
Accounts receivable, net	1,493,663	-	1,493,663	-
Deferred charges	226,009	16,925	242,934	-
Due from other funds	108,833	138,546	247,379	-
Inventories at average cost	216,603	-	216,603	-
Total current assets	<u>11,596,923</u>	<u>1,612,426</u>	<u>13,209,349</u>	<u>300,837</u>
Non-current assets:				
Capital assets:				
Land	729,530	347,748	1,077,278	-
Buildings and improvements	41,460,504	15,566,067	57,026,571	-
Construction in progress	10,497,774	4,154,070	14,651,844	-
Machinery and equipment	-	137,199	137,199	3,848,296
Less accumulated depreciation	(19,180,885)	(4,778,836)	(23,959,721)	(2,840,879)
Total capital assets	<u>33,506,923</u>	<u>15,426,248</u>	<u>48,933,171</u>	<u>1,007,417</u>
Total non-current assets	<u>33,506,923</u>	<u>15,426,248</u>	<u>48,933,171</u>	<u>1,007,417</u>
Total assets	<u>45,103,846</u>	<u>17,038,674</u>	<u>62,142,520</u>	<u>1,308,254</u>
LIABILITIES				
Current liabilities:				
Accounts payable	1,118,973	5,872	1,124,845	168,352
Accrued interest payable	73,819	5,615	79,434	-
Due to other funds	661,091	-	661,091	-
Due to other governments	61,523	-	61,523	-
Other accrued expenses	69,593	-	69,593	8,069
Compensated absences	12,510	-	12,510	8,710
Bonds, notes and loans payable	695,000	-	695,000	-
Total current liabilities	<u>2,692,509</u>	<u>11,487</u>	<u>2,703,996</u>	<u>185,131</u>
Non-current liabilities:				
Compensated absences	50,038	-	50,038	-
Customer deposits	326,225	-	326,225	-
Bonds, notes and loans payable	9,925,000	1,080,000	11,005,000	-
Total non-current liabilities	<u>10,301,263</u>	<u>1,080,000</u>	<u>11,381,263</u>	<u>-</u>
Total liabilities	<u>12,993,772</u>	<u>1,091,487</u>	<u>14,085,259</u>	<u>185,131</u>
NET ASSETS				
Invested in capital assets, net of related debt	22,886,923	14,346,248	37,233,171	1,007,417
Restricted for debt service	619,466	-	619,466	-
Unrestricted	8,603,685	1,600,939	10,204,624	115,706
Total net assets	<u>\$ 32,110,074</u>	<u>\$ 15,947,187</u>	<u>\$ 48,057,261</u>	<u>\$ 1,123,123</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, 2011

	Business-type Activities			Governmental Activities
	Water and Sanitary Sewer	Airport	Total	Internal Service Funds
OPERATING REVENUES				
Charges for services	\$ 10,283,837	\$ -	\$ 10,283,837	\$ -
Rental income	-	417,726	417,726	-
Internal service revenues	-	-	-	2,211,007
Miscellaneous	-	1,275	1,275	208,844
Total operating revenues	<u>10,283,837</u>	<u>419,001</u>	<u>10,702,838</u>	<u>2,419,851</u>
OPERATING EXPENSES				
Cost of sales and services	5,792,712	97,032	5,889,744	228,537
Administration	798,647	-	798,647	256,192
Utilities	-	-	-	499,986
Repairs and maintenance	-	-	-	58,778
Other supplies and expenses	-	-	-	325,844
Insurance claims and expenses	-	-	-	1,486,347
Depreciation	831,849	304,139	1,135,988	224,848
Total operating expenses	<u>7,423,208</u>	<u>401,171</u>	<u>7,824,379</u>	<u>3,080,532</u>
OPERATING INCOME (LOSS)	<u>2,860,629</u>	<u>17,830</u>	<u>2,878,459</u>	<u>(660,681)</u>
NON-OPERATING REVENUES (EXPENSES)				
Interest and investment revenues	38,115	7,145	45,260	2,361
Capital grants	82,834	2,411,602	2,494,436	-
Interest and fiscal charges	(451,657)	(50,520)	(502,177)	-
Transfers in	3,069,689	293,428	3,363,117	-
Transfers out	(2,560,112)	-	(2,560,112)	(469)
Total non-operating revenues (expenses)	<u>178,869</u>	<u>2,661,655</u>	<u>2,840,524</u>	<u>1,892</u>
CHANGE IN NET ASSETS	3,039,498	2,679,485	5,718,983	(658,789)
TOTAL NET ASSETS, BEGINNING	<u>29,070,576</u>	<u>13,267,702</u>	<u>42,338,278</u>	<u>1,781,912</u>
TOTAL NET ASSETS, ENDING	<u>\$ 32,110,074</u>	<u>\$ 15,947,187</u>	<u>\$ 48,057,261</u>	<u>\$ 1,123,123</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, 2011

	Business-type Activities			Governmental Activities
	Water and Sanitary Sewer	Airport	Total	Internal Service Funds
CASH FLOWS FROM OPERATING ACTIVITIES				
Cash received from customers and users	\$ 10,164,859	\$ 419,001	\$ 10,583,860	\$ 2,419,851
Cash paid for services and insurance claims	-	-	-	(1,931,933)
Cash paid to suppliers for goods and services	(4,954,297)	(202,336)	(5,156,633)	(629,637)
Cash paid to employees for services	(795,416)	-	(795,416)	(227,864)
Net cash provided (used) by operating activities	<u>4,415,146</u>	<u>216,665</u>	<u>4,631,811</u>	<u>(369,583)</u>
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES				
Transfers in	3,069,689	293,428	3,363,117	-
Transfers out	(2,560,112)	-	(2,560,112)	(469)
Net cash provided for noncapital financing activities	<u>509,577</u>	<u>293,428</u>	<u>803,005</u>	<u>(469)</u>
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES				
Acquisition of capital assets	(6,799,048)	(2,885,214)	(9,684,262)	(111,606)
Principal paid on long-term debt	4,120,000	(65,000)	4,055,000	-
Capital contributions	82,834	2,411,602	2,494,436	-
Interest and fiscal charges paid on debt	(577,658)	(49,003)	(626,661)	-
Net cash used for capital and related financing activities	<u>(3,173,872)</u>	<u>(587,615)</u>	<u>(3,761,487)</u>	<u>(111,606)</u>
CASH FLOWS FROM INVESTING ACTIVITIES				
Investment earnings	<u>38,115</u>	<u>7,145</u>	<u>45,260</u>	<u>2,361</u>
Net cash provided by investing activities	<u>38,115</u>	<u>7,145</u>	<u>45,260</u>	<u>2,361</u>
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	1,788,966	(70,377)	1,718,589	(479,297)
CASH AND CASH EQUIVALENTS, BEGINNING	<u>7,762,849</u>	<u>1,527,332</u>	<u>9,290,181</u>	<u>780,134</u>
CASH AND CASH EQUIVALENTS, ENDING	<u>\$ 9,551,815</u>	<u>\$ 1,456,955</u>	<u>\$ 11,008,770</u>	<u>\$ 300,837</u>

(continued)

CITY OF TERRELL, TEXAS

STATEMENT OF CASH FLOWS

PROPRIETARY FUNDS

(Continued)

FOR THE YEAR ENDED SEPTEMBER 30, 2011

	Business-type			Governmental Activities Internal Service Funds
	Water and Sanitary Sewer	Airport	Total	
RECONCILIATION OF OPERATING INCOME (LOSS) TO NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES:				
Operating income (loss)	\$ 2,860,629	\$ 17,830	\$ 2,878,459	\$(660,681)
Adjustments to reconcile operating income (loss) to net cash provided by operating activities:				
Depreciation	831,849	304,139	1,135,988	224,848
Changes in assets and liabilities:				
Decrease (increase) in assets:				
Customer receivable	(102,267)	-	(102,267)	-
Other receivable	6,221	-	6,221	-
Inventories	(1,225)	-	(1,225)	-
Due from other funds	-	(52,714)	(52,714)	-
Increase (decrease) in liabilities:				
Accounts payable	480,016	4,462	484,478	65,577
Accrued liabilities	2,662	-	2,662	672
Deferred revenue	(23,760)	(57,052)	(80,812)	-
Compensated absences	569	-	569	1
Due to other funds	347,162	-	347,162	-
Due to other governments	6,241	-	6,241	-
Customer deposits	7,049	-	7,049	-
Net cash provided (used) by operating activities	\$ <u>4,415,146</u>	\$ <u>216,665</u>	\$ <u>4,631,811</u>	\$ <u>(369,583)</u>

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

CITY OF TERRELL, TEXAS

NOTES TO FINANCIAL STATEMENTS

SEPTEMBER 30, 2011

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The City of Terrell (the "City") was incorporated on September 6, 1875, under an act of the 14th 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.

(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 **Rent Supplement Section 8 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 **Permanent Street Improvement Fund** is a Capital Projects Fund used to account for various street improvements.

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:

Insurance Fund – to account for the City's 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.

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 \$931,249,501 and the tax rates were \$.4616 per \$100 valuation for maintenance and operations and \$.1845 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 nonspendable fund balance designation.

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, 2011, 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, 2011, the liability for accrued vacation leave and accrued sick leave is \$1,332,854. The amount applicable to the Enterprise Funds (\$62,548) has been recorded in those funds, and the amount applicable to other funds (\$1,270,306) 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 Balance

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

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

When an expenditure is incurred for purposes for which both restricted and unrestricted fund balance is available, the City considers restricted funds to have been spent first. When an expenditure is incurred for which committed, assigned, or unassigned fund balances are available, the City considers amounts to have been spent first out of committed funds, then assigned funds, and finally unassigned funds.

(continued)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

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

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.

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 \$(20,163,392) difference are as follows:

General obligation bonds	\$(1,185,000)
Certificates of obligation	(12,760,000)
Less: deferred charge for issuance costs (to be amortized over life of debt)	127,091
Interest payable	(69,681)
Notes payable	(2,923,721)
Compensated absences	(1,261,595)
TMRS net pension obligation	(774,092)
OPEB liability	(1,316,394)
 Net adjustment to reduce <i>fund balance - total governmental funds</i> to arrive at <i>net assets - governmental activities</i>	 <u>\$(20,163,392)</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

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 \$(1,089,062) difference are as follows:

Capital outlay	\$ 141,564
Depreciation expense	<u>(1,230,626)</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>\$(1,089,062)</u>

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 \$(151,224) difference are as follows:

Deferred property tax revenues	\$(136,150)
Deferred court fines	(23,719)
Deferred special assessments	<u>8,645</u>
Net adjustment to increase <i>fund balance - total governmental funds</i> to arrive at <i>net assets - governmental activities</i>	<u>\$(151,224)</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 \$97,707 difference are as follows:

Principal repayments	\$ 1,642,707
Refunding debt issued	<u>(1,545,000)</u>
Net adjustment to reduce <i>fund balance - total governmental funds</i> to arrive at <i>net assets - governmental activities</i>	<u>\$ 97,707</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.
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 for general government expenditures by \$214,406, public safety expenditures by \$2,096, and capital outlay by \$177,709 in the General Fund.

C. Deficit Fund Balance/Net Assets

The Infrastructure Improvements Fund had a deficit equity balance of \$1,939, the Impact Fees Fund had a deficit equity balance of \$243,818, and the Grant HRA Fund had a deficit equity balance of \$2,750 as of September 30, 2011. 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, 2011, \$500,000 of the City's \$19,138,512 deposit balance was collateralized with securities held by the pledging financial institution. The remaining balance was covered by FDIC insurance.

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	\$ 1,701,153	\$ 180,797	\$ -	\$ 1,881,950
Special assessment	-	1,127,944	-	1,127,944
Accounts	<u>480,496</u>	<u>1,582</u>	<u>1,908,550</u>	<u>2,390,628</u>
Gross receivables	2,181,649	1,310,323	1,908,550	5,400,522
Less: allowance for uncollectibles	<u>(519,151)</u>	<u>(296,000)</u>	<u>(414,887)</u>	<u>(1,230,038)</u>
Net total receivables	<u>\$ 1,662,498</u>	<u>\$ 1,014,323</u>	<u>\$ 1,493,663</u>	<u>\$ 4,170,484</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	\$ 859,064	\$ -
Grants	-	14,501
Adjudicated court fines	27,167	-
Property taxes	499,442	-
Other	<u>-</u>	<u>-</u>
Total	<u>\$ 1,385,673</u>	<u>\$ 14,501</u>

(continued)

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

Capital Assets

Capital asset activity for the year ended September 30, 2011, was as follows:

Primary Government

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Deletions</u>	<u>Adjustments/ Reclassifications</u>	<u>Ending Balance</u>
Governmental activities:					
Capital assets, not being depreciated:					
Land	\$ 718,000	\$ -	\$ -	\$ -	\$ 718,000
Construction in progress	<u>-</u>	<u>118,324</u>	<u>-</u>	<u>-</u>	<u>118,324</u>
Total assets not being depreciated	<u>718,000</u>	<u>118,324</u>	<u>-</u>	<u>-</u>	<u>836,324</u>
Capital assets, being depreciated:					
Buildings	6,146,430	140,237	-	(198,537)	6,088,130
Improvements, other than buildings	1,823,085	-	-	-	1,823,085
Machinery and equipment	4,729,401	193,146	-	-	4,922,547
Infrastructure	<u>38,329,128</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>38,329,128</u>
Total capital assets being depreciated	<u>51,028,044</u>	<u>333,383</u>	<u>-</u>	<u>(198,537)</u>	<u>51,162,890</u>
Less accumulated depreciation:					
Buildings	1,711,396	147,202	-	-	1,858,598
Improvements, other than buildings	801,523	58,834	-	-	860,357
Machinery and equipment	3,148,530	291,765	-	-	3,440,295
Infrastructure	<u>22,130,902</u>	<u>957,673</u>	<u>-</u>	<u>-</u>	<u>23,088,575</u>
Total accumulated depreciation	<u>27,792,351</u>	<u>1,455,474</u>	<u>-</u>	<u>-</u>	<u>29,247,825</u>
Total capital assets being depreciated, net	<u>23,235,693</u>	<u>(1,122,091)</u>	<u>-</u>	<u>(198,537)</u>	<u>21,915,065</u>
Governmental activities capital assets, net	<u>\$ 23,953,693</u>	<u>\$(1,003,767)</u>	<u>\$ -</u>	<u>\$(198,537)</u>	<u>\$ 22,751,389</u>
Business-type Activities					
Capital assets, not being depreciated:					
Land	\$ 997,340	\$ 79,938	\$ -	\$ -	\$ 1,077,278
Construction in progress	<u>5,047,520</u>	<u>9,604,324</u>	<u>-</u>	<u>-</u>	<u>14,651,844</u>
Total assets not being depreciated	<u>6,044,860</u>	<u>9,684,262</u>	<u>-</u>	<u>-</u>	<u>15,729,122</u>
Capital assets, being depreciated:					
Buildings and improvements	20,411,828	-	-	-	20,411,828
Machinery and equipment	<u>36,751,941</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>36,751,941</u>
Total capital assets being depreciated	<u>57,163,769</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>57,163,769</u>
Less accumulated depreciation:					
Buildings and improvements	8,539,583	354,377	-	-	8,893,960
Machinery and equipment	<u>14,284,149</u>	<u>781,611</u>	<u>-</u>	<u>-</u>	<u>15,065,760</u>
Total accumulated depreciation	<u>22,823,732</u>	<u>1,135,988</u>	<u>-</u>	<u>-</u>	<u>23,959,720</u>
Total capital assets being depreciated, net	<u>34,340,037</u>	<u>(1,135,988)</u>	<u>-</u>	<u>-</u>	<u>33,204,049</u>
Business-type activities capital assets, net	<u>\$ 40,384,897</u>	<u>\$ 8,548,274</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 48,933,171</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	\$	303,874
Public safety		84,665
Highways and streets		761,554
Culture and recreation		80,533
Capital assets held by the City's internal service funds are charged to the various functions based on their usage		<u>224,848</u>
Total depreciation expense - governmental activities	\$	<u>1,455,474</u>
Business-type activities:		
Water and sanitary sewer	\$	831,850
Airport		<u>304,138</u>
Total depreciation expense - business-type activities	\$	<u>1,135,988</u>

Construction Commitments

The City has active construction projects as of September 30, 2011. 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, Phase II	\$ 667,459	\$ 561,810	\$ 105,649
State Highway 34 relocation	1,807,273	1,782,354	24,919
2 million gallon storage tank	3,229,520	2,592,409	637,111
Rose Hill Road 20" water line	911,145	715,310	195,835
Utility systems improvements, Phase I	1,553,577	1,217,363	336,214
Utility systems improvements, Phase II	1,083,596	-	1,083,596

(continued)

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

Interfund Receivables and Payables and Transfers

The composition of interfund balances as of September 30, 2011, is as follows:

Due to/from other funds:

<u>Receivable Fund</u>	<u>Payable Fund</u>	<u>Amount</u>
General fund	Nonmajor governmental	\$ 404,408
	Water and sanitary sewer	522,545
	Economic development corporation	16,644
Water and sanitary sewer	Nonmajor governmental	93,430
	Permanent street improvement	10,325
	General fund	5,078
Airport fund	Water and sanitary sewer	138,546
Nonmajor governmental	Nonmajor governmental	5,000
Permanent street improvement	Economic development corporation	<u>54,142</u>
		<u>\$ 1,250,118</u>

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>
Nonmajor governmental	Airport fund	\$ 114,003
	Water and sewer fund	2,278,631
	General fund	97,113
TEDC	Airport fund	179,425
Equipment replacement fund	General fund	469
Certificates of obligation 2004	Water and sewer fund	791,058
Water and sewer fund	General fund	1,251,491
	Nonmajor governmental	<u>1,308,621</u>
		<u>\$ 6,020,811</u>

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

(continued)

4. DETAILED NOTES ON ALL FUNDS (Continued)

Long-term Debt

Bonded Debt

Bonded debt of the City as of September 30, 2011, 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>200,000</u>
					<u>200,000</u>
Certificates of Obligation:					
Series 2002	3.60 - 4.90%	07/23/2002	02/15/2022	4,500,000	2,620,000
Series 2004	3.00 - 4.50%	09/15/2004	02/15/2024	5,500,000	3,920,000
Series 2006	4.00 - 4.375%	08/15/2006	02/15/2026	1,570,000	955,000
Series 2007A	4.29%	04/15/2007	02/15/2027	2,030,000	1,120,000
Series 2009	3.05%	12/17/2009	02/15/2019	3,185,000	2,600,000
Series 2011B	2-5.125%	02/15/2011	02/15/2041	1,545,000	<u>1,545,000</u>
					<u>12,760,000</u>
General Obligation Bonds:					
Series 2004	2.00 - 3.375%	03/01/2005	02/15/2014	3,835,000	<u>1,185,000</u>
					<u>1,185,000</u>
					<u>\$ 14,145,000</u>

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		Certificates of Obligation Revenue Supported	
	Principal	Interest	Principal	Interest	Principal	Interest	Principal	Interest
2012	\$ 835,000	\$ 496,827	\$ 100,000	\$ 6,200	\$ 400,000	\$ 31,194	\$ 595,000	\$ 599,182
2013	860,000	467,729	100,000	2,075	420,000	18,881	630,000	570,579
2014	900,000	436,974	-	-	365,000	6,159	660,000	540,163
2015	930,000	404,132	-	-	-	-	690,000	508,041
2016	970,000	369,339	-	-	-	-	735,000	473,311
2017-2021	4,720,000	1,276,828	-	-	-	-	2,420,000	1,947,629
2022-2026	2,430,000	481,616	-	-	-	-	1,910,000	1,464,884
2027-2031	350,000	229,103	-	-	-	-	1,290,000	1,023,241
2032-2036	335,000	153,815	-	-	-	-	1,070,000	696,600
2037-2041	430,000	57,144	-	-	-	-	1,500,000	266,625
Total	<u>\$ 12,760,000</u>	<u>\$ 4,373,507</u>	<u>\$ 200,000</u>	<u>\$ 8,275</u>	<u>\$ 1,185,000</u>	<u>\$ 56,234</u>	<u>\$ 11,500,000</u>	<u>\$ 8,090,255</u>

(continued)

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

Long-term Debt (Continued)

Notes Payable

As of September 30, 2011, the City's notes payable consisted of the following:

The Terrell Economic Development Corporation (TEDC) entered into a note payable agreement with a local bank on September 18, 2005. As of September 30, 2011, the balance was \$2,159,795. The loan is secured by sales tax revenues of the Corporation and will service monthly over a 15-year period at 4.49% interest.

On May 21, 2010, the TEDC entered into a note payable agreement with a local bank. As of September 30, 2011, the balance was \$763,926. The note has a maturity date of May 21, 2015, and is due in equal monthly installments of \$18,438.

Future maturities and amounts paid under the notes after September 30, 2011, are as follows:

<u>Year Ending September 30,</u>	<u>Principal</u>	<u>Interest</u>
2012	\$ 429,095	\$ 113,983
2013	445,950	96,915
2014	463,572	79,149
2015	407,963	60,956
2016	274,308	47,158
2017-2019	<u>902,833</u>	<u>63,605</u>
Total	<u>\$ 2,923,721</u>	<u>\$ 461,766</u>

(continued)

4. DETAILED NOTES ON ALL FUNDS (Continued)

Long-term Debt (Continued)

Changes in Long-term Liabilities

Long-term liability activity for the year ended September 30, 2011, was as follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Governmental activities					
Compensated absences	\$ 1,134,451	\$ 135,854	\$ -	\$ 1,270,305	\$ 254,061
Notes payable	3,406,428	-	482,707	2,923,721	429,095
Certificates of obligation	11,985,000	1,545,000	770,000	12,760,000	835,000
General obligation bonds	1,575,000	-	390,000	1,185,000	400,000
OPEB liability	879,189	556,471	119,266	1,316,394	-
Net pension obligation	523,840	1,473,721	1,223,469	774,092	-
Governmental activities long-term liabilities	<u>\$ 19,503,908</u>	<u>\$ 3,711,046</u>	<u>\$ 2,985,442</u>	<u>\$ 20,229,512</u>	<u>\$ 1,918,156</u>
Business-type activities					
Compensated absences	\$ 61,979	\$ 569	\$ -	\$ 62,548	\$ 12,510
Certificates of obligation	7,345,000	4,660,000	505,000	11,500,000	595,000
Revenue bonds	300,000	-	100,000	200,000	100,000
Business-type activities long-term liabilities	<u>\$ 7,706,979</u>	<u>\$ 4,660,569</u>	<u>\$ 605,000</u>	<u>\$ 11,762,548</u>	<u>\$ 707,510</u>

Bond Covenants

Bond covenants require the following disclosures:

	Interest and Sinking	Reserve
First Lien Bonds:		
Required ultimate balance	\$ -	\$ 212,240
Required present balance, end of year	62,242	212,240
Actual present balance, end of year	225,100	394,365

Certificates of Obligation

On February 15, 2011, the City issued \$4,660,000 of Certificates of Obligation Bonds Series 2011A. The bonds mature on February 15, 2041, and have stated interest rates of 1.25 – 6.75%. The bonds will be used to fund various projects throughout the City.

On February 15, 2011, the City issued \$1,545,000 of certificates of obligation bonds series 2011B. The bonds mature on February 15, 2041, and have stated interest rates of 2 – 5.125%. The bonds will be used to fund various projects throughout the City.

(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, 2011, 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.

Insurance Plan

The City has established an 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, 2011 and 2010, the estimated value of these liabilities was \$124,112 and \$69,299, respectively.

Employee Retirement Systems and Pension Plans

Plan Description

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

(continued)

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

Employee Retirement Systems and Pension Plans (Continued)

Plan Description (Continued)

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

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

	<u>Plan Year 2010</u>	<u>Plan Year 2011</u>
Employee deposit rate	7.0%	7.0%
Matching ratio (city to employee)	2 to 1	2 to 1
Years required for vesting	5	5
Service retirement eligibility (expressed as age/years of service)	60/5, 0/20	60/5, 0/20
Updated service credit	100% repeating, transfers	100% repeating, transfers
Annuity increase (to retirees)	70% of CPI repeating	70% of CPI repeating

Contributions

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

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

(continued)

4. DETAILED NOTES ON ALL FUNDS (Continued)

Employee Retirement Systems and Pension Plans (Continued)

Contributions (Continued)

Annual Required Contribution (ARC)	\$ 1,466,939
Interest on Net Pension Obligation	39,288
Adjustment to the ARC	(32,506)
Annual Pension Cost	1,473,721
Contributions Made	(1,223,469)
Increase (Decrease) in Net Pension Obligation	250,252
Net Pension Obligation/(Asset), beginning of year	<u>523,840</u>
Net Pension Obligation/(Asset), ending of year	<u>\$ 774,092</u>

Three-Year Trend Information

Accounting Year Ending	Annual Pension Cost (APC)	Actual Contribution Made	Percentage of APC Contributed	Net Pension Obligation
09/30/09	\$ 1,320,381	\$ 1,090,530	82.59%	\$ 229,851
09/30/10	1,460,229	1,166,240	79.87%	523,840
09/30/11	1,473,721	1,223,469	83.02%	774,092

The required contribution rates for fiscal year 2011 were determined as part of the December 31, 2008 and 2009 actuarial valuations. Additional information as of the latest actuarial valuation, December 31, 2010, also follows:

Actuarial Valuation Date	12/31/08	12/31/09	12/31/10 Prior to Restructuring	12/31/10 Restructured
Actuarial cost method	Projected Unit Credit	Projected Unit Credit	Projected Unit Credit	Projected Unit Credit
Amortization method	Level percent of payroll	Level percent of payroll	Level percent of payroll	Level percent of payroll
GASB 25 equivalent single amortization period	29 years - closed	28.1 years - closed	27.3 years - closed	27.2 years - closed
Amortization period for new gains/losses	30 years	30 years	30 years	30 years
Asset valuation method	Amortized cost	10-yr smoothed market	10-yr smoothed market	10-yr smoothed market
Actuarial Assumptions:				
Investment rate of return	7.5%	7.5%	7.5%	7.0%
Projected salary increases	varies by age and service	varies by age and service	varies by age and service	varies by age and service
Inflation	3.0%	3.0%	3.0%	3.0%
Cost-of-living adjustments	2.1%	2.1%	2.1%	2.1%

(continued)

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

Employee Retirement Systems and Pension Plans (Continued)

Contributions (Continued)

Funding Status and Funding Progress

In June 2011, SB 350 was enacted by the Texas Legislature, resulting in a restructure of the TMRS funds. This legislation provided for the actuarial valuation to be completed, as if restructuring had occurred on December 31, 2010. In addition, the actuarial assumptions were updated for the new fund structure, based on an actuarial experience study that was adopted by the TMRS Board at their May 2011 meeting (the review compared actual to expected experience for the four-year period of January 1, 2006 through December 31, 2009). For a complete description of the combined impact of the legislation and new actuarial assumptions, including the effects on TMRS city rates and funding ratios, please see the December 31, 2010 TMRS Comprehensive Annual Financial Report (CAFR).

The funded status as of December 31, 2010, the most recent actuarial valuation date, is as follows:

<u>Actuarial Valuation Date</u>	<u>Actuarial Value of Assets</u>	<u>Actuarial Accrued Liability</u>	<u>Percentage Funded</u>	<u>Unfunded Actuarial Accrued Liability</u>	<u>Annual Covered Payroll</u>	<u>Unfunded Actuarial Accrued Liability as a Percentage of Covered Payroll</u>
12/31/2008	\$ 13,238,540	\$ 22,835,955	58.0%	\$ 9,597,415	\$ 7,583,480	126.6%
12/31/2009	14,765,212	25,349,369	58.2%	10,584,157	8,091,992	130.8%
12/31/2010 (1)	16,282,456	27,156,065	60.0%	10,873,609	8,266,884	131.5%
12/31/2010 (2)	28,512,948	37,400,778	76.2%	8,887,830	8,266,884	107.5%

Annual OPEB Cost and Net OPEB Obligation

The City's annual other postemployment benefit (OPEB) cost (expense) is calculated based on the annual required contribution of the employer (ARC), an amount actuarially determined in accordance with the parameters of GASB Statement 45. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and to amortize any unfunded actuarial liabilities (or funding excess) over a period not to exceed 30 years. The City's annual OPEB cost for the current year and the related information is listed below:

Annual Required Contribution (ARC)	\$ 552,703
Interest on Net Pension Obligation	35,168
Adjustment to the ARC	(31,400)
Annual Pension Cost	556,471
Contributions Made	(119,266)
Increase (Decrease) in Net Pension Obligation	437,205
Net Pension Obligation/(Asset), beginning of year	<u>879,189</u>
Net Pension Obligation/(Asset), ending of year	<u>\$ 1,316,394</u>

(continued)

4. DETAILED NOTES ON ALL FUNDS (Continued)

Employee Retirement Systems and Pension Plans (Continued)

The City's annual OPEB cost, the percentage of annual OPEB cost contributed to the plan, and the net OPEB obligation for the prior three years (4.0% discount rate, and level percent of pay amortization).

<u>Fiscal Year Ended</u>	<u>Annual OPEB Cost</u>	<u>Employer Contribution</u>	<u>Percentage Contributed</u>	<u>Net OPEB Obligation</u>
09/30/09	\$ 552,703	\$ 119,765	21.7%	\$ 432,938
09/30/10	554,559	108,308	19.5%	879,189
09/30/11	556,471	119,266	21.4%	1,316,394

Funding Status and Funding Progress

As of September 30, 2011, the actuarial accrued liability for benefits was \$1,316,394, all of which was unfunded. The covered payroll (annual payroll of active employees covered by the plan) was \$7,065,071 and the ratio of the unfunded actuarial accrued liability to the covered payroll was 77.8%.

The projection of future payments for an ongoing plan involves estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the health care cost trend. Amounts determined regarding the funded status of the plan and the annual required contributions of the employer are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future.

Actuarial Methods and Assumptions

Projection of benefits for financial reporting purposes are based on the substantive plan (the plan as understood by the employer and plan members) and include the types of benefits provided at the time of each valuation and the historical pattern of sharing of benefit costs between the employer and plan members to that point. The actuarial methods and assumptions used include techniques that are designed to reduce short-term volatility in actuarial accrued liabilities and the actuarial value of assets, consistent with the long-term perspective of the calculations.

In the September 30, 2011, actuarial valuation, the entry age normal actuarial cost method was used. The actuarial assumptions included a 4.0 percent investment rate of return and an annual payroll increase of 3.5%. The City's unfunded actuarial accrued liability is being amortized as a level percentage of projected payroll on an open basis. The remaining amortization period at September 30, 2011, was 28 years.

(continued)

4. DETAILED NOTES ON ALL FUNDS (Continued)

Employee Retirement Systems and Pension Plans (Continued)

Supplemental Death Benefits Fund

The City also participates in the cost sharing multiple-employer defined benefit group term life insurance plan operated by the Texas Municipal Retirement System (TMRS) known as the Supplemental Death Benefits Fund (SDBF). The City elected, by ordinance, to provide group-term life insurance coverage to both current and retired employees. The City may terminate coverage under and discontinue participation in the SDBF by adopting an ordinance before November 1 of any year to be effective the following January 1.

The death benefit for active employees provides a lump sum payment approximately equal to the employee's annual salary (calculated based on the employee's actual earnings, for the 12-month period preceding the month of death); retired employees are insured for \$7,500; this coverage is an "other postemployment benefit," or OPEB.

Schedule of Contribution Rates

<u>Accounting Year Ending</u>	<u>Annual Required Contribution (Rate)</u>	<u>Actual Contribution Made (Rate)</u>	<u>Percentage of ARC Contributed</u>	<u>Net Pension Obligation</u>
09/30/09	.22%	.22%	100%	\$ -
09/30/10	.19%	.19%	100%	-
09/30/11	.20%	.20%	100%	-

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.

(continued)

4. DETAILED NOTES ON ALL FUNDS (Continued)

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.

Prior Period Adjustment

The City recorded several prior period adjustments during the year resulting in an overall increase to fund balance of \$310,377. The adjustments were made to remove old payables that had already been paid and to remove deferred revenue and receivables from grants that were closed out.

COMBINING STATEMENTS

NONMAJOR GOVERNMENTAL FUNDS

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.

Red Light Camera Fund – to account for the receipt of traffic fines revenue produced from the photographic traffic signal enforcement system.

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.

Tax Increment Fund – to account for the City's accumulation of funds within the Tax increment zone.

TDHCA Home Buyer Fund – to account for grant funds used with the TDHCA Home Buyer’s Grant.

County TIF #1 Fund – to account for the City’s accumulation of funds within the County Tax increment zone.

Police Grant – to account for grant funds used with the Police Grant.

Housing Grant – to account for grant funds used in housing projects.

Home Grant – to account for grant funds used with the Home Grant.

2010 Police Grant – to account for police grants with the City.

CO 2011B – to account for funds received from the issuance of the Certificates of Obligation 2011B.

Grant HRA – to account for funds received through the HRA Grant.

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, 2011

	<u>Tourism</u>	<u>Grant</u>	<u>Public Improvement District</u>
ASSETS			
Cash and cash equivalents	\$ 135,564	\$ -	\$ -
Taxes receivable, net	-	-	-
Due from other funds	<u>-</u>	<u>-</u>	<u>-</u>
Total assets	<u>\$ 135,564</u>	<u>\$ -</u>	<u>\$ -</u>
LIABILITIES AND FUND BALANCES			
Liabilities:			
Accounts payable	\$ 29,323	\$ -	\$ -
Due to other funds	-	-	-
Deferred revenue	<u>-</u>	<u>-</u>	<u>-</u>
Total liabilities	<u>29,323</u>	<u>-</u>	<u>-</u>
Fund balances:			
Restricted	106,241	-	-
Unassigned	<u>-</u>	<u>-</u>	<u>-</u>
Total fund balances	<u>106,241</u>	<u>-</u>	<u>-</u>
Total liabilities and fund balances	<u>\$ 135,564</u>	<u>\$ -</u>	<u>\$ -</u>

<u>Red Light Cameras</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>Tax Increment Fund</u>	<u>TDHCA Home Buyer Grant</u>
\$ 53,367	\$ -	\$ 711	\$ 99,675	\$ 49,604	\$ 120,774	\$ -
-	-	-	-	-	1	-
-	-	-	-	-	-	-
<u>\$ 53,367</u>	<u>\$ -</u>	<u>\$ 711</u>	<u>\$ 99,675</u>	<u>\$ 49,604</u>	<u>\$ 120,775</u>	<u>\$ -</u>
\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
-	-	2,650	343,493	-	-	-
-	-	-	-	-	-	-
-	-	<u>2,650</u>	<u>343,493</u>	-	-	-
53,367	-	-	-	49,604	120,775	-
-	-	(1,939)	(243,818)	-	-	-
<u>53,367</u>	<u>-</u>	<u>(1,939)</u>	<u>(243,818)</u>	<u>49,604</u>	<u>120,775</u>	<u>-</u>
<u>\$ 53,367</u>	<u>\$ -</u>	<u>\$ 711</u>	<u>\$ 99,675</u>	<u>\$ 49,604</u>	<u>\$ 120,775</u>	<u>\$ -</u>

(continued)

CITY OF TERRELL, TEXAS
COMBINING BALANCE SHEET
NONMAJOR GOVERNMENTAL FUNDS
(Continued)
SEPTEMBER 30, 2011

	<u>County TIF #1</u>	<u>Police Grant</u>	<u>Housing Grant</u>
ASSETS			
Cash and cash equivalents	\$ 44,234	\$ -	\$ -
Taxes receivable, net	-	-	-
Due from other funds	<u>-</u>	<u>-</u>	<u>-</u>
Total assets	<u>\$ 44,234</u>	<u>\$ -</u>	<u>\$ -</u>
LIABILITIES AND FUND BALANCES			
Liabilities:			
Accounts payable	\$ -	\$ -	\$ -
Due to other funds	-	-	-
Deferred revenue	<u>-</u>	<u>-</u>	<u>-</u>
Total liabilities	<u>-</u>	<u>-</u>	<u>-</u>
Fund balances:			
Restricted	44,234	-	-
Unassigned	<u>-</u>	<u>-</u>	<u>-</u>
Total fund balances	<u>44,234</u>	<u>-</u>	<u>-</u>
Total liabilities and fund balances	<u>\$ 44,234</u>	<u>\$ -</u>	<u>\$ -</u>

<u>Home Grant</u>	<u>2010 Police Grant</u>	<u>CO 2011B</u>	<u>Grant HRA</u>	<u>Debt Service</u>	<u>Total Governmental Funds</u>
\$ 167,464	\$ 2,778	\$ 734,225	\$ 2,250	\$ 1,125,178	\$ 2,535,824
-	-	-	-	153,677	153,678
<u>5,000</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>5,000</u>
<u>\$ 172,464</u>	<u>\$ 2,778</u>	<u>\$ 734,225</u>	<u>\$ 2,250</u>	<u>\$ 1,278,855</u>	<u>\$ 2,694,502</u>
\$ 4,500	\$ -	\$ -	\$ -	\$ 20,147	\$ 53,970
-	-	-	5,000	93,430	444,573
<u>9,225</u>	<u>2,776</u>	<u>-</u>	<u>-</u>	<u>138,266</u>	<u>150,267</u>
<u>13,725</u>	<u>2,776</u>	<u>-</u>	<u>5,000</u>	<u>251,843</u>	<u>648,810</u>
158,739	2	734,225	-	1,027,012	2,294,199
-	-	-	(2,750)	-	(248,507)
<u>158,739</u>	<u>2</u>	<u>734,225</u>	<u>(2,750)</u>	<u>1,027,012</u>	<u>2,045,692</u>
<u>\$ 172,464</u>	<u>\$ 2,778</u>	<u>\$ 734,225</u>	<u>\$ 2,250</u>	<u>\$ 1,278,855</u>	<u>\$ 2,694,502</u>

CITY OF TERRELL, TEXAS

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

NONMAJOR GOVERNMENTAL FUNDS

FOR THE YEAR ENDED SEPTEMBER 30, 2011

	<u>Tourism</u>	<u>Grant</u>	<u>Public Improvement District</u>
REVENUES			
Ad valorem taxes	\$ -	\$ -	\$ -
Hotel/motel occupancy taxes	247,669	-	-
Intergovernmental	-	-	-
Charges for services	-	-	-
Interest	<u>616</u>	<u>118</u>	<u>-</u>
Total revenues	<u>248,285</u>	<u>118</u>	<u>-</u>
EXPENDITURES			
Current:			
General government	267,065	-	-
Public welfare	-	-	-
Public safety	-	-	-
Culture and recreation	-	-	-
Capital outlay	-	-	-
Principal	-	-	-
Interest and other charges	<u>-</u>	<u>-</u>	<u>-</u>
Total expenditures	<u>267,065</u>	<u>-</u>	<u>-</u>
EXCESS (DEFICIENCY) OF REVENUES OVER (UNDER) EXPENDITURES	<u>(18,780)</u>	<u>118</u>	<u>-</u>
OTHER FINANCING SOURCES (USES)			
Proceeds from sale of bonds	-	-	-
Transfers in	-	-	-
Transfers out	<u>-</u>	<u>(39,020)</u>	<u>-</u>
Total other financing sources and uses	<u>-</u>	<u>(39,020)</u>	<u>-</u>
NET CHANGE IN FUND BALANCES	<u>(18,780)</u>	<u>(38,902)</u>	<u>-</u>
FUND BALANCES, BEGINNING	<u>125,021</u>	<u>38,902</u>	<u>(9,699)</u>
PRIOR PERIOD ADJUSTMENT	<u>-</u>	<u>-</u>	<u>9,699</u>
FUND BALANCES, ENDING	<u>\$ 106,241</u>	<u>\$ -</u>	<u>\$ -</u>

<u>Red Light Cameras</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>Tax Increment Fund</u>	<u>TDHCA Home Buyer Grant</u>
\$ -	\$ -	\$ -	\$ -	\$ -	\$ 21,529	\$ -
-	-	-	-	-	-	-
-	-	-	-	-	25,385	-
-	-	-	38,759	-	-	-
<u>160</u>	<u>-</u>	<u>2</u>	<u>822</u>	<u>176</u>	<u>145</u>	<u>102</u>
<u>160</u>	<u>-</u>	<u>2</u>	<u>39,581</u>	<u>176</u>	<u>47,059</u>	<u>102</u>
-	-	-	-	-	-	-
-	-	-	-	-	-	-
3,664	-	-	-	-	-	-
-	-	-	-	16,967	-	-
-	-	-	-	-	-	-
-	-	-	-	-	-	-
<u>3,664</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>16,967</u>	<u>-</u>	<u>-</u>
(3,504)	-	2	39,581	(16,791)	47,059	102
-	-	-	-	-	-	-
-	-	-	-	-	-	-
<u>-</u>	<u>-</u>	<u>-</u>	<u>(664,588)</u>	<u>-</u>	<u>-</u>	<u>(58,093)</u>
<u>-</u>	<u>-</u>	<u>-</u>	<u>(664,588)</u>	<u>-</u>	<u>-</u>	<u>(58,093)</u>
(3,504)	-	2	(625,007)	(16,791)	47,059	(57,991)
<u>56,871</u>	<u>(74,214)</u>	<u>42,244</u>	<u>381,189</u>	<u>66,395</u>	<u>73,716</u>	<u>57,991</u>
<u>-</u>	<u>74,214</u>	<u>(44,185)</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
<u>\$ 53,367</u>	<u>\$ -</u>	<u>\$(1,939)</u>	<u>\$(243,818)</u>	<u>\$ 49,604</u>	<u>\$ 120,775</u>	<u>\$ -</u>

(continued)

CITY OF TERRELL, TEXAS

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

**NONMAJOR GOVERNMENTAL FUNDS
(Continued)**

FOR THE YEAR ENDED SEPTEMBER 30, 2011

	<u>County TIF #1</u>	<u>Police Grant</u>	<u>Housing Grant</u>
REVENUES			
Ad valorem taxes	\$ 10,830	\$ -	\$ -
Hotel/motel occupancy taxes	-	-	-
Intergovernmental	-	-	-
Charges for services	-	-	-
Interest	<u>69</u>	<u>1</u>	<u>-</u>
Total revenues	<u>10,899</u>	<u>1</u>	<u>-</u>
EXPENDITURES			
Current:			
General government	-	-	-
Public welfare	-	-	-
Public safety	-	319	-
Culture and recreation	-	-	-
Capital outlay	-	-	-
Principal	-	-	-
Interest and other charges	<u>-</u>	<u>-</u>	<u>-</u>
Total expenditures	<u>-</u>	<u>319</u>	<u>-</u>
EXCESS (DEFICIENCY) OF REVENUES OVER (UNDER) EXPENDITURES	<u>10,899</u>	<u>(318)</u>	<u>-</u>
OTHER FINANCING SOURCES (USES)			
Proceeds from sale of bonds	-	-	-
Transfers in	-	-	-
Transfers out	<u>-</u>	<u>-</u>	<u>-</u>
Total other financing sources and uses	<u>-</u>	<u>-</u>	<u>-</u>
NET CHANGE IN FUND BALANCES	10,899	(318)	-
FUND BALANCES, BEGINNING	<u>33,335</u>	<u>(71,794)</u>	<u>-</u>
PRIOR PERIOD ADJUSTMENT	<u>-</u>	<u>72,112</u>	<u>-</u>
FUND BALANCES, ENDING	<u>\$ 44,234</u>	<u>\$ -</u>	<u>\$ -</u>

<u>Home Grant</u>	<u>2010 Police Grant</u>	<u>CO 2011B</u>	<u>Grant HRA</u>	<u>Debt Service</u>	<u>Total Governmental Funds</u>
\$ -	\$ -	\$ -	\$ -	\$ 1,790,272	\$ 1,822,631
-	-	-	-	-	247,669
241,561	12,824	-	-	-	279,770
-	-	-	-	-	38,759
<u>426</u>	<u>2</u>	<u>913</u>	<u>-</u>	<u>2,739</u>	<u>6,291</u>
<u>241,987</u>	<u>12,826</u>	<u>913</u>	<u>-</u>	<u>1,793,011</u>	<u>2,395,120</u>
-	-	-	-	-	267,065
241,561	-	-	2,750	-	244,311
-	12,824	-	-	-	16,807
-	-	-	-	-	16,967
-	-	1	-	-	1
-	-	-	-	1,177,047	1,177,047
-	-	<u>45,000</u>	<u>-</u>	<u>529,431</u>	<u>574,431</u>
<u>241,561</u>	<u>12,824</u>	<u>45,001</u>	<u>2,750</u>	<u>1,706,478</u>	<u>2,296,629</u>
<u>426</u>	<u>2</u>	<u>(44,088)</u>	<u>(2,750)</u>	<u>86,533</u>	<u>98,491</u>
-	-	1,545,000	-	-	1,545,000
-	-	-	-	1,308,621	1,308,621
<u>-</u>	<u>-</u>	<u>(766,687)</u>	<u>-</u>	<u>(961,359)</u>	<u>(2,489,747)</u>
<u>-</u>	<u>-</u>	<u>778,313</u>	<u>-</u>	<u>347,262</u>	<u>363,874</u>
426	2	734,225	(2,750)	433,795	462,365
<u>158,313</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>593,217</u>	<u>1,471,487</u>
<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>111,840</u>
<u>\$ 158,739</u>	<u>\$ 2</u>	<u>\$ 734,225</u>	<u>\$ (2,750)</u>	<u>\$ 1,027,012</u>	<u>\$ 2,045,692</u>

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INTERNAL SERVICE FUNDS

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
INTERNAL SERVICE FUNDS
COMBINING STATEMENT OF NET ASSETS
SEPTEMBER 30, 2011

	<u>Insurance Fund</u>	<u>Equipment Replacement</u>	<u>Total</u>
ASSETS			
Current assets:			
Cash and cash equivalents	\$ 193,512	\$ 107,325	\$ 300,837
Total current assets	<u>193,512</u>	<u>107,325</u>	<u>300,837</u>
Non-current assets:			
Capital assets:			
Vehicles and equipment	-	3,848,296	3,848,296
Accumulated depreciation	<u>-</u>	<u>(2,840,879)</u>	<u>(2,840,879)</u>
Total non-current assets	<u>-</u>	<u>1,007,417</u>	<u>1,007,417</u>
 Total assets	 <u>193,512</u>	 <u>1,114,742</u>	 <u>1,308,254</u>
LIABILITIES			
Current liabilities:			
Accounts payable	124,112	44,240	168,352
Other accrued expenses	-	8,069	8,069
Compensated absences	<u>-</u>	<u>8,710</u>	<u>8,710</u>
Total current liabilities	<u>124,112</u>	<u>61,019</u>	<u>185,131</u>
 Total liabilities	 <u>124,112</u>	 <u>61,019</u>	 <u>185,131</u>
NET ASSETS			
Invested in capital assets, net of related debt	-	1,007,417	1,007,417
Unrestricted	<u>69,400</u>	<u>46,306</u>	<u>115,706</u>
 Total net assets	 <u>\$ 69,400</u>	 <u>\$ 1,053,723</u>	 <u>\$ 1,123,123</u>

CITY OF TERRELL, TEXAS

INTERNAL SERVICE FUNDS

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

FOR THE YEAR ENDED SEPTEMBER 30, 2011

	<u>Insurance Fund</u>	<u>Equipment Replacement</u>	<u>Total</u>
OPERATING REVENUES			
Maintenance services	\$ -	544,326	\$ 544,326
Insurance premiums	1,666,681	-	1,666,681
Miscellaneous	<u>178,696</u>	<u>30,148</u>	<u>208,844</u>
Total operating revenues	<u>1,845,377</u>	<u>574,474</u>	<u>2,419,851</u>
OPERATING EXPENSES			
Personnel services	-	228,537	228,537
Miscellaneous services	-	256,192	256,192
Administrative fees	499,986	-	499,986
Repairs and maintenance	-	58,778	58,778
Supplies	-	325,844	325,844
Insurance claims and expenses	1,486,347	-	1,486,347
Depreciation	<u>-</u>	<u>224,848</u>	<u>224,848</u>
Total operating expenses	<u>1,986,333</u>	<u>1,094,199</u>	<u>3,080,532</u>
OPERATING INCOME (LOSS)	(140,956)	(519,725)	(660,681)
NON-OPERATING REVENUES (EXPENSES)			
Interest and investment revenue	549	1,812	2,361
Transfers out	<u>-</u>	<u>(469)</u>	<u>(469)</u>
Total non-operating revenue (expenses)	<u>549</u>	<u>1,343</u>	<u>1,892</u>
CHANGE IN NET ASSETS	(140,407)	(518,382)	(658,789)
TOTAL NET ASSETS, BEGINNING	<u>209,807</u>	<u>1,572,105</u>	<u>1,781,912</u>
TOTAL NET ASSETS, ENDING	<u>\$ 69,400</u>	<u>\$ 1,053,723</u>	<u>\$ 1,123,123</u>

CITY OF TERRELL, TEXAS

INTERNAL SERVICE FUNDS

COMBINING STATEMENT OF CASH FLOWS

FOR THE FISCAL YEAR ENDED SEPTEMBER 30, 2011

	<u>Insurance Fund</u>	<u>Equipment Replacement</u>	<u>Total</u>
CASH FLOWS FROM OPERATING ACTIVITIES			
Cash received from customers and users	\$ 1,845,377	\$ 574,474	\$ 2,419,851
Cash paid for services and insurance claims	(1,931,933)	-	(1,931,933)
Cash paid to suppliers for goods and services	-	(629,637)	(629,637)
Cash paid to employees for services	-	(227,864)	(227,864)
Net cash used by operating activities	<u>(86,556)</u>	<u>(283,027)</u>	<u>(369,583)</u>
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES			
Transfers out	-	(469)	(469)
Cash paid to other funds	-	-	-
Net cash used for noncapital financing activities	<u>-</u>	<u>(469)</u>	<u>(469)</u>
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES			
Acquisition of capital assets	-	(111,606)	(111,606)
Net cash used for capital and related financing activities	<u>-</u>	<u>(111,606)</u>	<u>(111,606)</u>
CASH FLOWS FROM INVESTING ACTIVITIES			
Investment earnings	549	1,812	2,361
Net cash provided by investing activities	<u>549</u>	<u>1,812</u>	<u>2,361</u>
DECREASE IN CASH	(86,007)	(393,290)	(479,297)
CASH AND CASH EQUIVALENTS, BEGINNING	<u>279,519</u>	<u>500,615</u>	<u>780,134</u>
CASH AND CASH EQUIVALENTS, ENDING	<u>\$ 193,512</u>	<u>\$ 107,325</u>	<u>\$ 300,837</u>
RECONCILIATION OF OPERATING INCOME (LOSS) TO NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES			
Operating income (loss)	\$(140,956)	\$(519,725)	\$(660,681)
Adjustments to reconcile net income (loss) to net cash provided by operating activities:			
Depreciation	-	224,848	224,848
Increase (decrease) in accounts payable	54,400	11,177	65,577
Increase (decrease) in accrued liabilities	-	672	672
Increase (decrease) in compensated absences	-	1	1
Net cash used by operating activities	<u>\$(86,556)</u>	<u>\$(283,027)</u>	<u>\$(369,583)</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, 2011, which collectively comprise the City of Terrell, Texas' basic financial statements and have issued our report thereon dated June 15, 2012. 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

Management of the City of Terrell, Texas is responsible for establishing and maintaining effective 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 was not designed to identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses and therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. However, as described in the accompanying Schedule of Findings and Questioned Costs, we identified certain deficiencies in internal control over financial reporting that we consider to be significant deficiencies.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. We consider none of the deficiencies described in the accompanying Schedule of Findings and Questioned Costs to be material weaknesses.

A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider the deficiency described in the accompanying Schedule of Findings and Questioned Costs, Finding 2011-1, to be a significant deficiency.

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*.

The City's response to the finding 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, City Council, others within the entity, and federal awarding agencies and pass-through entities, and is not intended to be used and should not be used by anyone other than these specified parties.

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

June 15, 2012



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

To the Honorable City Council
City of Terrell, Texas

Compliance

We have audited the City of Terrell, Texas' compliance with the types of compliance requirements described in the *U. S. Office of Management and Budget (OMB) Circular A-133, Compliance Supplement* that could have a direct and material effect on each of the City of Terrell, Texas' major federal programs for the year ended September 30, 2011. 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 could have a direct and material effect on each of its major federal programs for the year ended September 30, 2011.

Internal Control Over Compliance

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 to determine the auditing procedures for the purpose of expressing our opinion on compliance, and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness the City's internal control over compliance.

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

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

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

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

June 15, 2012

CITY OF TERRELL, TEXAS

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

FOR THE YEAR ENDED SEPTEMBER 30, 2011

<u>Federal Grantor/Pass-through Grantor/ Program Title</u>	<u>Federal CFDA Number</u>	<u>Pass-through Entity Identifying Number</u>	<u>Federal Expenditures</u>
<u>U. S. Department of Housing and Urban Development</u>			
Direct Program:			
Section 8 Housing Choice Vouchers Program	14.871	B-07-MC-48-0042	\$ <u>3,181,102</u>
Total Direct Program			<u>3,181,102</u>
 Total U. S. Department of Housing and Urban Development			 <u>3,181,102</u>
<u>U. S. Department of Justice</u>			
Direct Program:			
Edward Byrne Memorial Justice Assistance Program	16.738 ARRA	2011-H3579-TX-DJ	<u>12,824</u>
Total Direct Program			<u>12,824</u>
 Total U. S. Department of Justice			 <u>12,824</u>
<u>U. S. Department of Transportation</u>			
Passed through Texas Department of Transportation:			
Airport Maintenance Program	20.106	10TBTEREL	<u>1,232,842</u>
Total Passed through Texas Department of Transportation			<u>1,232,842</u>
 Total U. S. Department of Transportation			 <u>1,232,842</u>
 Total Expenditures of Federal Awards			 <u>\$ 4,426,768</u>

CITY OF TERRELL, TEXAS

NOTES TO SCHEDULE OF FEDERAL AWARDS

FOR THE FISCAL YEAR ENDED SEPTEMBER 30, 2011

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, 2011**

Financial Statements:

Type of auditors' report issued Unqualified

Internal control over financial reporting:

Material weakness(es) identified? No

Significant deficiency(ies) identified? 2011-1

Noncompliance material to financial statements
noted? None

Federal Awards:

Internal control over major programs:

Material weakness(es) identified? No

Significant deficiency(ies) identified? None reported

Type of auditors' report issued on compliance
for major programs Unqualified

Any audit findings disclosed that are required
to be reported in accordance with Section
510(a) of OMB Circular A-133? None

Identification of major programs:

CFDA Number(s)

#14.871

#20.106

Name of Federal Program or Cluster:

Section 8 Rental Voucher Program

Airport Maintenance Program

Dollar threshold used to distinguish between type A
and type B programs \$300,000

Auditee qualified as low-risk auditee? No

(continued)

CITY OF TERRELL, TEXAS

**SCHEDULE OF FINDINGS AND QUESTIONED COSTS
(Continued)
FOR THE YEAR ENDED SEPTEMBER 30, 2011**

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

Item 2011-1

- Condition: The City had unauthorized purchases on a City credit card as well as a City fuel card.
- Cause: The City has procedures governing credit cards in their Financial Policy Manual. However, some of the policies were not completely followed and the policy itself needed to be improved to strengthen internal controls over credit card purchases. The Financial Policy Manual lacked a defined set of procedures governing the procedures and policies over fuel cards.
- Cause: The City was unaware that payables had been accrued and recorded the expense in a subsequent period.
- Effect: There were City funds used for unauthorized purchases on a City credit card and fuel card.
- Recommendation: We recommend the City review and make relevant changes to the credit card policy. The City should also have a City training for those administering and using City credit cards. The policy should be laid out for them so all parties involved are aware of the City's policies over cards. A fuel policy should also be created to safeguard fuel purchases. The policies should also be communicated to City personnel as well once completed.
- Management's Response: Upon discovering unauthorized purchases on a City credit card, the City Finance Department reviewed all credit card activity for all employees from October 2008 to January 2012. No similar patterns of abuse of credit card use were detected. Immediately following the review of the credit cards/purchasing cards, department directors and City staff were provided training for the administration and use of City credit cards and the City created an additional review by the finance director and is consulting its auditing firm for the review of purchase logs for the City issued credit cards/purchasing cards to improve accountability and to insure that the policy sets forth the dos and don'ts of the credit card usage and the penalties for violating these restrictions. The City implemented mandatory annual training for all credit card/purchasing card users.

(continued)

CITY OF TERRELL, TEXAS

**SCHEDULE OF FINDINGS AND QUESTIONED COSTS
(Continued)
FOR THE YEAR ENDED SEPTEMBER 30, 2011**

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

Item 2011-1

The City has implemented programs to prohibit unauthorized activity through the use of programming codes to operationally block the City's credit cards/purchasing cards in certain locations (Merchant Category Codes or MCC). Working with our credit card/purchasing card provider, the City has improved its reporting tools that provide spending summaries and additional information allowing the City to receive alerts of unusual spending and catch discrepancies or unusual spending patterns. Consistent Policy enforcement by careful review by all departments and a second review by the finance department as well as the City auditing firm should provide adequate safeguards against unauthorized purchases on a City credit card/purchasing card.

The City developed a City fuel card policy. The policy is currently being reviewed by the City consulting auditors. Once implemented, the training for the fuel card policy will be provided on an annual basis. The fuel card provider has assisted the City with the implementation of reporting tools that provide spending summaries by merchants and card holders allowing the City staff to detect unusual spending and catch discrepancies or unusual spending patterns.

Contact Person Responsible
for Corrective Action:

John Rounsavall, City Secretary/Finance Director

Anticipated Completion Date: August

Findings and Questioned Costs for Federal Awards

None

CITY OF TERRELL, TEXAS
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
FOR THE YEAR ENDED SEPTEMBER 30, 2011

None