

CITY OF ALVARADO, TEXAS
SEPTEMBER 30, 2012

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INDEPENDENT AUDITOR'S REPORT

To the Honorable Mayor and City Council,
City of Alvarado, 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 Alvarado, Texas (the City) as of and for the year then ended September 30, 2012, which collectively comprise the City's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the City's management. Our responsibility is to express an opinions on these financial statements based on our audit.

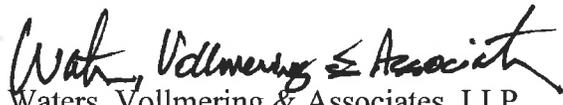
We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and 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, as of September 30, 2012, and the respective changes in financial position and, where applicable, cash flows thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated January 31, 2013, on our consideration of the City of Alvarado, 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 to 16, the budgetary comparison information on pages 48 through 49, and the schedule of funding progress for the retirement plan on page 50 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 assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.


Waters, Vollmering & Associates, LLP
Mansfield, Texas
January 31, 2013

City of Alvarado

104 W. College
Alvarado, Texas 76009

Phone 817-790-3351
FAX 817-783-7925

January 31, 2013

The Honorable Mayor, City Council and the Citizens of the City of Alvarado

The City Council of the City of Alvarado requires that the City's Finance Department prepare a complete set of financial statements presented in conformity with generally accepted accounting principles (GAAP) and audited in accordance with generally accepted auditing standards by a firm of licensed certified public accountants. Accordingly, the Annual Audited Financial Report for the City of Alvarado, Texas for the fiscal year ended September 30, 2012, is hereby issued.

This report consists of management's representations concerning the finances of the City. Consequently, management assumes full responsibility for the completeness and reliability of all information presented in this report. To provide a reasonable basis for making representations, the City has designed a comprehensive internal control framework that is designed both to protect the City's assets from loss, theft, or misuse and to compile sufficient reliable information for the preparation of the City's financial statements in conformity with GAAP. Because the cost of internal controls should not outweigh their benefits, the City's comprehensive framework of internal controls has been designed to provide reasonable, rather than absolute, assurance that the financial statements will be free from material misstatements. As management, we assert, that, to the best of our knowledge and belief, this financial report is complete and reliable in all material respects.

The City's financial statements have been audited by Waters, Vollmering & Associates, Independent Certified Public Accountants. The goal of the independent audit is to provide reasonable assurance that the financial statements for the City for the fiscal year ended September 30, 2012, are free of material misstatements. The independent audit involved examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements; assessing the accounting principles used and significant estimates made by management; and evaluating the overall financial statement presentation. The independent auditor concluded based upon the audit, that there was a reasonable basis for rendering an unqualified opinion that the City's financial statements for the fiscal year ended September 30, 2012, are fairly presented in conformity with GAAP. The independent auditors' report is presented as the first component of the financial section of this report.

GAAP requires the management provide a narrative introduction, overview, and analysis to accompany the basic financial statements in the form of a Management's Discussion and Analysis (MD&A). This letter of transmittal is designed to complement the MD&A and should be read in conjunction with it. The City's MD&A can be found immediately following the report

Profile of the City

The oldest town in Johnson County, Texas, Alvarado was incorporated in 1889 and is located at the intersection of Interstate Highway 35 and U.S. Highway 67, 20 miles south of Fort Worth. The City occupies approximately 4.67 square miles and serves a population of about 4,000. The City is empowered by state statute to levy a tax on both real and business personal property located within its boundaries.

The City operates under a council-manager form of government. Policy-making and legislative authority are vested in a governing Council consisting of the mayor and six (6) Council members. The City is divided into three (3) wards and two (2) Council members represent each ward. While the Council members must live in the ward they serve the Mayor is elected at large. The City Council is responsible for, among other things, passing ordinances, adopting the budget, appointing committees, and hiring the City Manager. The City Manager is responsible for carrying out the policies and ordinances of the City Council, for overseeing the day-to-day operations of the City, and appointing heads of various departments. The Mayor and City Council members serve two-year terms.

The basic financial statements of the City include governmental activities, organizations and functions for which the City is financially accountable as defined by the Government Accounting Standards Board (GASB). Based on these criteria, no other governmental organizations are included in this report.

Services Provided

The City provides a full range of services, including public safety (police, fire, and animal control), maintenance of streets, drainage and infrastructure, sanitation services, maintenance of the treated water distribution system, both sanitary and storm water collection and treatment systems, recreational activities, cultural activities, and general administrative services.

Economic Conditions and Outlook

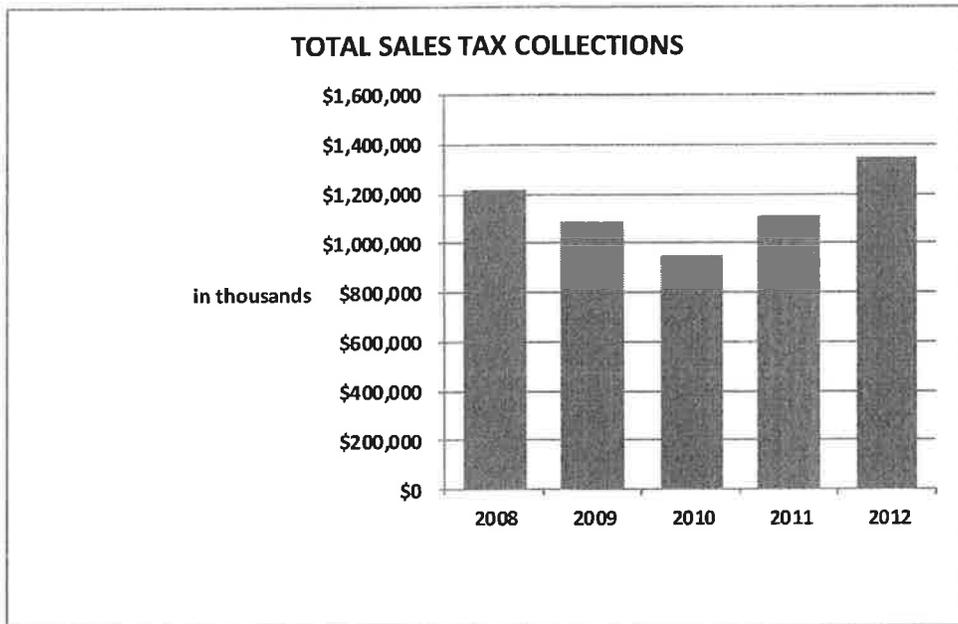
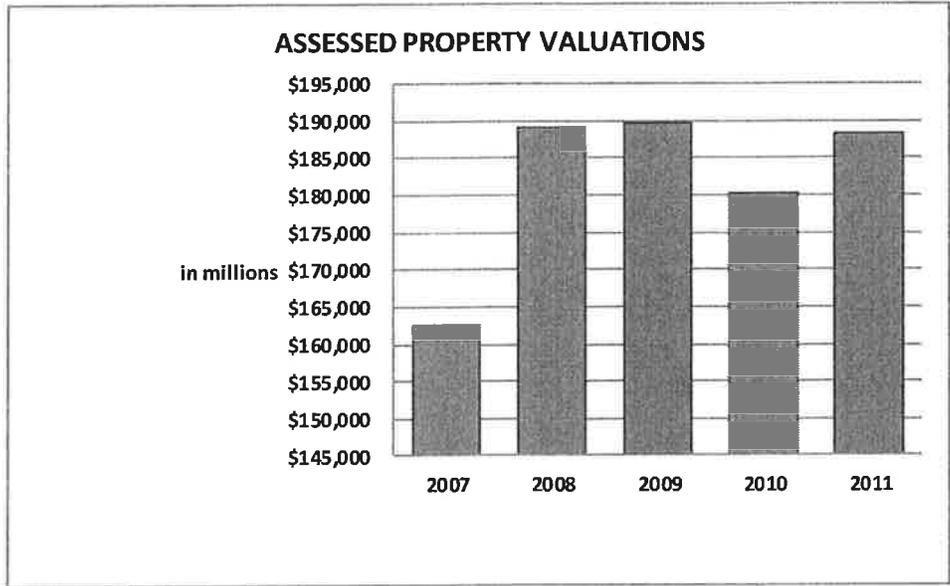
The information presented in the financial statements is perhaps best understood when it is considered from the broader aspect of the specific environment within which the City operates.

Local Economy

2011-2012 proved to be economically challenging much like prior years. However, recent employment opportunities and growth prove encouraging. In addition, there was an increase in commerce as evidenced by a 20.7% rise in sales tax revenue. Sales tax collections increased \$230,949 from \$1,114,510 to \$1,345,459.

Property valuations for 2011 were \$188M, showing an increase of approximately \$8M from the previous year. The property tax rate was increased from \$0.697313 to \$0.722313 for the 2011 valuations. The 2012 valuations show a decrease to \$185M and the property tax rate was also decreased to \$.706872.

The charts below are based upon the 2011-2012 budget year as compared to prior years. Property Valuations noted below for the 2011-2012 budget period are based upon the 2011 assessed property valuations as determined by the Johnson County Appraisal District. Sales Tax collected represents amounts collected during the 2011-2012 budget year.



Accounting System and Budgetary Control

The City's accounting records and general government 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 incurred. Accounting records for the City utilities are maintained on the accrual basis.

The annual budget serves as a foundation of the City's financial planning and control. State law provides that the City Council shall adopt the annual budget prepared by the City Manager. The proposed budget must be submitted to the City Secretary no later than August 1st. The City Manager is authorized to transfer budgeted amounts between line items and departments; 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 departmental level. Financial reports are produced showing budget and actual expenditures by line item, and are distributed monthly to the departmental management and to others by request.

Individual line items are reviewed and analyzed for budgetary compliance. Personnel expenditures are monitored and controlled at a position level and capital expenditures are monitored and controlled item by item. Revenue budgets are reviewed monthly.

Budget-to-actual comparisons are provided in this report for the General Fund on page 48.

Debt Management

The City issues debt only for the purpose of acquiring or constructing capital assets for the general benefit of its citizens, and to allow the fulfillment of its various missions as a City. Debt may be issued for the purposes of purchasing land or right-of-way and/or improvements to land, for construction projects to provide for the general good, or for capital equipment. The City will uphold all related bond covenant agreements associated with bond issues. Bond issues are only conducted after consultation with an outside financial advisor. The City continues to contract with Southwest Securities to provide these services.

Cash Management

The City utilizes its bank depository contract and its investment policy in the management of all cash. Under the Bank depository contract, the City operating account earns the bank's public fund interest rate. The City's investment policy embraces current state regulations on the investment of public funds and authorizes the City to invest in certificates of deposits, direct obligations of the United States Government or the State of Texas, obligations of an agency of the United States Government or the State of Texas, Collateralized mortgage obligations directly issued by a federal agency or instrumentality of the United States, the underlying security for which is guaranteed by an agency or instrumentality of the United States and state government investment pools. The City requires all deposits and investments of City funds other than direct purchases of U.S. Treasuries or Agencies shall be secured by pledged collateral. In order to anticipate market changes and provide a level of security for all funds, the collateralization level will be 102% of market value of principal and accrued interest on the deposits or investments less an amount insured by the FDIC or FSLIC. Evidence of pledged collateral is maintained by the Director of Finance. Repurchase agreements are documented by a specific agreement noting the collateral pledge in each agreement. Collateral is reviewed to assure that the market value of the pledged securities is adequate.

Tax Appraisal/Tax Collection Responsibilities

The appraised value of taxable property in Alvarado is established by the Johnson County Appraisal District. The City of Alvarado and other taxing jurisdictions in Johnson County provide a pro-rata share of the budgeted expenditures incurred by the Appraisal District, based on individual levy. The Johnson County Tax Assessor-Collector provides tax collection services for the City and other taxing jurisdictions with Johnson County.

Risk Management

Risk management within the City is a joint effort of all City departmental heads in coordination with the City's property and casualty provider. Under a contractual arrangement, the City's facilities, procedures, and claims are reviewed by a loss prevention representative with an insurance provider. The representative and department heads address area of needs as identified through both external and internal analysis.

The City purchases liability insurance with limits of \$2M for all exposures. The City also purchases workers' compensation coverage through a public entity insurance pool.

Acknowledgements

The preparation of this report could not be accomplished without efforts of the entire City staff. Staff members are greatly appreciated for their hard work and contributions to this effort. It is through the guidance and leadership of the Mayor and City Council members that these efforts are able to be accomplished. The staff is thankful for the hard work of the Mayor and Council. Most of all the staff is thankful for the citizens of Alvarado and the opportunity to serve such a great community.

Respectfully Submitted,

Clint Davis
City Manager

Kelle Whitfill
Director of Finance and Administration

**CITY OF ALVARADO
PRINCIPAL CITY OFFICIALS
SEPTEMBER 30, 2012**

Mayor

Dewayne Richters

Council Members

Joe Sain

Tom Moore

Shawn Goulding

David Bayless

Jacob Wheat

Arrdeen Vaughan

City Manager

Clint Davis

City Secretary

Debbie Thomas

City Attorney

Bryn D. Meredith

Director of Finance

Kelle Whitfill

Director of Public Works

Terry Hafer

Police Chief

Brad Anderson

Fire Chief

Richard VanWinkle

MANAGEMENT'S DISCUSSION AND ANALYSIS

FISCAL YEAR ENDED SEPTEMBER 30, 2012

As management of the City of Alvarado, we offer readers of the City of Alvarado's financial statements this narrative overview and analysis of the financial activities of the City of Alvarado for the fiscal year ended September 30, 2012. We encourage readers to consider the information presented here in conjunction with additional information that we have furnished in our letter of transmittal. Comparative data is included for comparative analysis of government wide activities.

FINANCIAL HIGHLIGHTS

- The assets of the City of Alvarado exceeded its liabilities at the close of the most recent fiscal year by \$15,480,461 (total net assets). Of this amount, \$3,850,923 (unrestricted net assets) may be used to meet the government's ongoing obligations to citizens and creditors.
- The City's total net assets increased this fiscal year by \$966,281.
- As of the close of the current fiscal year, the City of Alvarado's governmental funds reported combined ending fund balances of \$3,495,066 which is an increase of \$663,207 from the previous year. Approximately 21.98% or \$768,388 is available for spending at the City's discretion (unassigned fund balance).
- At the end of the current fiscal year, the Royalty Fund has a fund balance of \$1,129,891 which can be spent with Council approval (committed fund balance).
- Other Governmental Funds include Alvarado Economic Development Corporation with a fund balance of \$1,181,992, Hotel Fund with a fund balance of \$285,070, and Court Revenue Fund with a fund balance of \$129,725 (restricted fund balances).
- The City's total debt increased by \$4,502,669 during the current fiscal year. The governmental funds debt decreased by \$399,464 as the result of scheduled retirement of debt. The water and sewer proprietary fund debt increased by \$4,902,133 due to the issuance of a new certificate of obligation bond to improve water and sewer projects within the City.

OVERVIEW OF THE FINANCIAL STATEMENTS

The discussion and analysis are intended to serve as an introduction to the City of Alvarado'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 of Alvarado's finances, in a manner similar to private-sector business.

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

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

Both of the government-wide financial statements distinguish functions of the City of Alvarado that are principally supported by taxes and intergovernmental revenues (*governmental activities*) from other functions that are intended to recover all or a significant portion of their costs through user fees and charges (*business-type activities*). The governmental activities of the City of Alvarado include general government, public safety, public works, and culture and recreation. The business-type activity of the City of Alvarado includes a Water and Sewer Fund.

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

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

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

The City of Alvarado maintains 6 individual funds for 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 balance for the general fund, the royalty fund, and the debt service fund, all of which are considered major funds. Data from the other 3 funds (Alvarado Economic Development 4-B, Hotel Tax and Court) are combined into a single, aggregated presentation.

Proprietary funds. The City of Alvarado maintains one type of proprietary fund. *Enterprise funds* are used to report same functions presented as *business-type activities* in the government-wide financial statements. The City of Alvarado uses an enterprise fund to account for its Water and Sewer Fund.

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 Fund, which is considered to be a major fund of the City of Alvarado.

Notes to the financial statement. The notes provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements.

GOVERNMENT-WIDE FINANCIAL ANALYSIS

As noted earlier, net assets may serve over time as a useful indicator of a government's financial position. In the case of the City of Alvarado, assets exceeded liabilities by \$15,480,461 at the close of the most recent fiscal year. This represents an increase of \$966,281 from the previous fiscal year.

The largest portion of the City of Alvarado's net assets is reflected by its investments in capital assets (e.g. land, buildings, equipment, improvements, construction in progress and infrastructure) less any related debt used to acquire those assets that is still outstanding. The City of Alvarado uses these capital assets to provide services to citizens; consequently, these assets are *not* available for future spending. Although the City of Alvarado'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 Alvarado's Net Assets

| | Governmental Activities | | Business-Type Activities | | Total | |
|---|-------------------------|--------------|--------------------------|---------------|---------------|---------------|
| | 2011 | 2012 | 2011 | 2012 | 2011 | 2012 |
| Current Assets | \$ 3,847,768 | \$ 4,123,473 | \$ 2,471,720 | \$ 6,831,562 | \$ 6,319,488 | \$ 10,955,035 |
| Noncurrent Assets | 6,098,675 | 6,300,592 | 12,815,611 | 12,772,738 | 18,914,286 | 19,073,330 |
| Total Assets | 9,946,443 | 10,424,065 | 15,287,331 | 19,604,300 | 25,233,774 | 30,028,365 |
| Current Liabilities | 1,645,339 | 1,282,897 | 689,476 | 432,619 | 2,334,815 | 1,715,516 |
| LongTerm Liabilities | 4,501,834 | 4,077,277 | 3,882,945 | 8,755,111 | 8,384,779 | 12,832,388 |
| Total Liabilities | 6,147,173 | 5,360,174 | 4,572,421 | 9,187,730 | 10,719,594 | 14,547,904 |
| Invested in capital assets, net of related debt | 967,444 | 1,568,825 | 8,695,199 | 3,595,370 | 9,662,643 | 5,164,195 |
| Restricted | 1,180,991 | 1,596,787 | - | 4,868,556 | 1,180,991 | 6,465,343 |
| Unrestricted | 1,650,835 | 1,898,279 | 2,019,711 | 1,952,644 | 3,670,546 | 3,850,923 |
| Total Net Assets | \$ 3,799,270 | \$ 5,063,891 | \$ 10,714,910 | \$ 10,416,570 | \$ 14,514,180 | \$ 15,480,461 |

An additional portion of the City of Alvarado's net assets, \$6,465,343 represents resources that are subject to external restrictions on how they may be used. Unrestricted net assets are \$3,850,923 which may be used to meet the government's ongoing obligations to citizens and creditors.

As of September 30, 2012, the City of Alvarado is able to report positive balances in all three categories of net assets, both for the government as a whole, as well as for its separate governmental and business-type activities.

Governmental Activities. Governmental activities reflected an increase in the City's net assets by \$1,264,621, from \$3,799,270 to \$5,063,891.

Business-type Activities. Net assets from business-type activities decreased by \$298,340 from \$10,714,910 to \$10,416,570.

The following table provides a summary of the City's operations for the year ended September 30, 2012, with the comparative totals for the year ended September 30, 2011.

City of Alvarado's Changes in Net Assets

City of Alvarado's Changes in Net Assets

| | Governmental Activities | | Business Activities | | Total | |
|---------------------------------------|-------------------------|---------------------|----------------------|----------------------|----------------------|----------------------|
| | 2011 | 2012 | 2011 | 2012 | 2011 | 2012 |
| REVENUES: | | | | | | |
| Program Revenues: | | | | | | |
| Charges for Services | \$ 2,343,892 | \$ 1,816,829 | \$ 2,481,582 | \$ 2,468,749 | \$ 4,825,474 | \$ 4,285,578 |
| Operating Grants/Contributions | 58,881 | 52,129 | - | 82,501 | 58,881 | 134,630 |
| Capital Grants/Contributions | 409 | 200 | 1,196,432 | - | 1,196,841 | 200 |
| General Revenues: | | | | | | |
| Property Taxes | 1,295,677 | 1,361,119 | - | - | 1,295,677 | 1,361,119 |
| Sales Tax | 947,341 | 1,158,993 | - | - | 947,341 | 1,158,993 |
| Franchise Tax | 398,965 | 385,146 | - | - | 398,965 | 385,146 |
| Alcoholic beverage taxes | 1,265 | 1,341 | - | - | 1,265 | 1,341 |
| Unrestricted investment earnings | 3,725 | 4,288 | 3,476 | 3,756 | 7,201 | 8,044 |
| Other revenue | 202,536 | 383,137 | (921,200) | - | (718,664) | 383,137 |
| | - | - | - | - | - | - |
| Total Revenue | 5,252,691 | 5,163,182 | 2,760,290 | 2,555,006 | 8,012,981 | 7,718,188 |
| EXPENSES: | | | | | | |
| General government | 672,920 | 675,134 | - | - | 672,920 | 675,134 |
| Public safety | 2,343,298 | 2,357,659 | - | - | 2,343,298 | 2,357,659 |
| Public works | 405,221 | 137,125 | - | - | 405,221 | 137,125 |
| Community development | 229,555 | 197,193 | - | - | 229,555 | 197,193 |
| Cultural & recreational | 253,117 | 275,347 | - | - | 253,117 | 275,347 |
| Social & welfare | 60,768 | 45,420 | - | - | 60,768 | 45,420 |
| Economic development | 32,365 | 44,646 | - | - | 32,365 | 44,646 |
| Interest on long-term debt | 284,481 | 168,346 | 178,219 | 176,542 | 462,700 | 344,888 |
| Water & sewer operations | - | - | 2,621,040 | 2,674,495 | 2,621,040 | 2,674,495 |
| Special item outflow | - | - | - | - | - | - |
| Total Expenses | 4,281,725 | 3,900,870 | 2,799,259 | 2,851,037 | 7,080,984 | 6,751,907 |
| Change in net assets before transfers | 970,966 | 1,262,312 | (38,969) | (296,031) | 931,997 | 966,281 |
| Transfers | 385,138 | 2,309 | (385,138) | (2,309) | - | 0 |
| Change in net assets | 1,356,104 | 1,264,621 | (424,107) | (298,340) | 931,997 | 966,281 |
| Net assets - Beginning | 2,443,166 | 3,799,270 | 11,139,017 | 10,714,910 | 13,582,183 | 14,514,180 |
| Net assets - Ending | \$ 3,799,270 | \$ 5,063,891 | \$ 10,714,910 | \$ 10,416,570 | \$ 14,514,180 | \$ 15,480,461 |

FINANCIAL ANALYSIS OF THE GOVERNMENT'S FUNDS

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

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

As of the end of the current fiscal year, the City's governmental funds reported combined ending fund balances of \$3,495,066, an increase of \$663,207 in comparison with the prior year. Approximately \$768,388 of this total constitutes unassigned fund balance, which is available for spending at the government's discretion with \$1,129,891 as committed fund balance which may be used with Council approval. Refer to page 18 of this report for a more detailed presentation of governmental fund balances.

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

Unrestricted net assets of the City's Proprietary Funds at the end of the year amounted to \$1,952,644, a decrease of \$67,067 from the previous year. There was a decrease in total net assets of \$298,340, impacted by decreased water sales resulting from the drought contingency plan that was implemented and the impact that the dry summer had on water well repairs.

General Fund Budgetary Highlights

The City's actual revenue for 2012 increased by \$384,554 or 12% when compared to the original budget. The budget was revised and increased slightly at mid-year. The upward trend for sales tax revenue provided an increase of \$181,935 or a 22% increase over the revised budgeted amount.

Total general fund revenues increased when compared to the prior year by \$496,947 or 16%.

Total general fund year-end expenditures totaled \$298,490 less than the previous year and \$205,932 less than the revised budget total. This was the result of each department practicing a conservative approach to spending.

CAPITAL ASSETS

The City of Alvarado's investment in capital assets for its governmental and business-type activities as of September 30, 2012, amounts to \$18,682,630 (net of accumulated depreciation.). This investment in capital assets includes land, buildings and improvements, machinery, equipment, infrastructure and construction in progress.

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

- An EMS vehicle for the Fire Department was purchased for \$42,316;
- 10 Airpacks were purchased for the Fire Department at \$56,740;
- The Police Department purchased 2 Tahoes for \$72,735;
- Purchased Digital Interceptors for the new Police vehicles for \$5,990;
- 8 laptops were purchased for Police vehicles for \$9,816;
- 15 Radios were purchased for the Police Department for \$86,208;
- 2 Radar Guns were purchased for the Police Department for \$5,222;
- Continuation of the street improvement program at the cost of \$401,657;
- Major repairs were necessary at Well #4 for \$66,232;
- Pump & Motor Replacement at Well #1 for \$15,741;
- Motor & Pipe Replacement at Well #9 for \$12,393;
- 2 pumps were purchased for the Davis Lift Station for \$29,583;
- Purchased a new Sewer Machine and trailer for \$49,304;
- Purchased 3 new trucks for the Public Works Department for \$62,265;
- The City completed an EPA Grant in the amount of \$320,565 for sewer system upgrades;
- The Wastewater Treatment Plant received a new blower & alignment for \$8,890;
- Repaired the Annex Building parking lot for \$8,355;
- Roof replacement at the Senior Citizen/Community Center for \$14,700.

The following table provides a summary of the City's capital assets for the year ended September 30, 2012 as compared to the summary of capital assets for the year ended September 30, 2011:

CAPITAL ASSETS AT YEAR-END

| | Governmental Activities | | Business-Type Activities | | Totals | |
|--------------------------|-------------------------|------------------|--------------------------|-------------------|-------------------|-------------------|
| | 2011 | 2012 | 2011 | 2012 | 2011 | 2012 |
| Land | 462,548 | 462,548 | 602,949 | 1,045,959 | 1,065,497 | 1,508,507 |
| Buildings & Improvements | 1,857,398 | 1,832,095 | 17,550 | 15,750 | 1,874,948 | 1,847,845 |
| Infrastructure | 2,927,109 | 3,205,267 | | | 2,927,109 | 3,205,267 |
| Vehicles | 269,427 | 232,149 | 7,033 | 48,927 | 276,460 | 281,076 |
| Parks Improvements | 127,588 | 73,204 | | | 127,588 | 73,204 |
| Water System | | | 3,811,350 | 3,635,887 | 3,811,350 | 3,635,887 |
| Sewer System | | | 8,059,134 | 7,656,180 | 8,059,134 | 7,656,180 |
| Other Equipment | 257,473 | 310,965 | 74,193 | 138,333 | 331,666 | 449,298 |
| Construction in Progress | 25,367 | 25,367 | 170,611 | - | 195,978 | 25,367 |
| Total | <u>5,926,910</u> | <u>6,141,595</u> | <u>12,742,820</u> | <u>12,541,036</u> | <u>18,669,730</u> | <u>18,682,631</u> |

DEBT ADMINISTRATION

Total Debt. The City of Alvarado's total debt outstanding at the end of the current fiscal year is \$13,697,473. This amount is an increase from the previous fiscal year.

Long-term Debt. At the end of the current fiscal year, the City of Alvarado had total long-term debt outstanding of \$12,832,388. Of this amount, \$12,564,206 is comprised of combination tax and revenue certificate of obligations debt to be paid from property tax revenue, as well as water and sewer revenues from the City and a tax anticipation note to be paid from property tax revenue. The remainder of the debt, \$268,182, is comprised of various notes for vehicles, equipment and buildings. This debt includes a new \$4,810,000 combination tax revenue certificate of obligation issued at the end of this budget year to fund improvements in water, sewer and wastewater treatment plant.

Current Debt. At the end of the current fiscal year, the City of Alvarado had total current debt of \$865,085 including current bonds payable, current notes payable and compensated absences.

The following table provides a summary of the City's outstanding debt for the year ended September 30, 2012 as compared to the summary of capital assets for the year ended September 30, 2011:

OUTSTANDING DEBT AT YEAR-END

| | Governmental Activities | | Business-Type Activities | | Totals | |
|----------------------------|-------------------------|---------------------|--------------------------|---------------------|---------------------|----------------------|
| | 2011 | 2012 | 2011 | 2012 | 2011 | 2012 |
| Certificates of Obligation | \$ 4,155,680 | \$ 3,831,046 | \$ 4,037,815 | \$ 8,850,160 | \$ 8,193,495 | \$ 12,681,206 |
| Tax Anticipation Notes | 695,000 | 535,000 | - | - | 695,000 | 535,000 |
| Capital Leases | 97,356 | 113,818 | 9,806 | 95,505 | 107,162 | 209,323 |
| Notes Payable | 90,672 | 157,189 | - | - | 90,672 | 157,189 |
| Compensated Absences | 92,523 | 94,714 | 15,952 | 20,041 | 108,475 | 114,755 |
| Total | <u>\$ 5,131,231</u> | <u>\$ 4,731,767</u> | <u>\$ 4,063,573</u> | <u>\$ 8,965,706</u> | <u>\$ 9,194,804</u> | <u>\$ 13,697,473</u> |

ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES

The following factors were considered in preparing the City of Alvarado's budget for the 2013 fiscal year:

- The City benefits from its strategic location, which is approximately 20 miles from Fort Worth and 35 miles from Dallas.
- Local inflation factors remain low while the median income continues to rise.
- The City decreased the adopted tax rate from \$.740505 to \$.706872 per \$100 of valuation, keeping the tax rate equal to the effective rate.
- The City currently receives royalties from 15 gas wells.
- 7 single family homes requested permits with an average value of \$125,700 per structure.
- 4 new commercial buildings applied for permits.
- Miscellaneous repair permits continue to be issued as homeowners work on remodeling and adding accessory buildings.
- Continuation of the street improvement program for the City of Alvarado.
- Several properties have requested annexation into the City.
- Development of property on Hwy 67 on the west side of Interstate 35 is moving forward with the anticipated construction to begin in April 2013 of a Quick Trip spearheading the expansion.
- New businesses that have opened within the past year include Go Loco, Taco Bell, Alvarado Medical Clinic, a dentist office and a new bakery, How Sweet It Is.
- The City's sales tax has benefited from the November 2011 election that allowed for the sale of all alcoholic beverages. Several stores are selling beer and wine and two liquor stores have opened and are operating within our City limits.

All of these factors were considered in preparing the City of Alvarado's budget for the 2013 fiscal year. The City estimated that its General Fund Operating Budget for both revenues and expenditures for fiscal year 2013 will decrease by about 1% or \$104,647 from the fiscal year 2012 final budget. The decrease in the property tax revenue is estimated to be \$205,820 as the result of the ad valorem rate being lowered from \$.740505 per \$100 of taxable value in 2012 to \$.706872 in 2013. Sales tax revenue is budgeted to increase by \$222,500 or 27% over the previous budget.

Requests for Information

This financial report is designed to provide a general overview of the City of Alvarado's finances for all those with an interest in the city's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the City of Alvarado, Office of the Finance Director, 104 West College, Alvarado, Texas 76009.

BASIC FINANCIAL STATEMENTS

CITY OF ALVARADO, TEXAS
STATEMENT OF NET ASSETS
September 30, 2012

| | Governmental Activities | Business-type Activities | Total |
|---|----------------------------|-----------------------------|---------------------|
| ASSETS | | | |
| Current assets: | | | |
| Cash | \$630,561 | \$240,049 | \$870,610 |
| Investments | 2,700,757 | 1,216,820 | 3,917,577 |
| Receivables (net) | | | |
| Taxes receivable | 258,622 | - | 258,622 |
| Accounts receivable | 81,840 | 334,183 | 416,023 |
| Inventory | - | 46,967 | 46,967 |
| Restricted assets | | | |
| Cash | - | 4,800,808 | 4,800,808 |
| Deposits | 25 | 119,346 | 119,371 |
| Investments | 451,668 | 73,389 | 525,057 |
| Total current assets | <u>4,123,473</u> | <u>6,831,562</u> | <u>10,955,035</u> |
| Noncurrent assets: | | | |
| Capital assets, net | 6,141,595 | 12,541,035 | 18,682,630 |
| Deferred bond issuance costs | 158,997 | 231,703 | 390,700 |
| Total noncurrent assets | <u>6,300,592</u> | <u>12,772,738</u> | <u>19,073,330</u> |
| Total assets | <u>10,424,065</u> | <u>19,604,300</u> | <u>30,028,365</u> |
| LIABILITIES | | | |
| Current liabilities: | | | |
| Accounts payable | 423,696 | 80,306 | 504,002 |
| Accrued liabilities | 191,324 | 15,122 | 206,446 |
| Due to other governments | 13,387 | - | 13,387 |
| Deferred tax revenue | - | - | - |
| Deposits | - | 126,596 | 126,596 |
| Current portion | | | |
| Revenue bonds payable | 485,000 | 167,000 | 652,000 |
| Notes payable | 30,236 | - | 30,236 |
| Capital leases | 44,540 | 23,554 | 68,094 |
| Compensated absences | 94,714 | 20,041 | 114,755 |
| Total current liabilities | <u>1,282,897</u> | <u>432,619</u> | <u>1,715,516</u> |
| Noncurrent liabilities: | | | |
| Revenue bonds payable | 3,881,046 | 8,683,160 | 12,564,206 |
| Notes payable | 126,953 | - | 126,953 |
| Capital leases | 69,278 | 71,951 | 141,229 |
| Total noncurrent liabilities | <u>4,077,277</u> | <u>8,755,111</u> | <u>12,832,388</u> |
| Total liabilities | <u>5,360,174</u> | <u>9,187,730</u> | <u>14,547,904</u> |
| NET ASSETS | | | |
| Invested in capital assets, net of related debt | 1,568,825 | 3,595,370 | 5,164,195 |
| Restricted | | | |
| Public Safety | 1,596,787 | - | 1,596,787 |
| Capital improvements | - | 4,868,556 | 4,868,556 |
| Unrestricted | 1,898,279 | 1,952,644 | 3,850,923 |
| Total net assets | <u>\$5,063,891</u> | <u>\$10,416,570</u> | <u>\$15,480,461</u> |

See accompanying notes and independent auditor's report

CITY OF ALVARADO, TEXAS
STATEMENT OF ACTIVITIES
For the Fiscal Year Ended September 30, 2012

| Functions/Programs | Program Revenues | | | Net (Expense) Revenue and Change in Net Assets | | | |
|-------------------------------------|------------------|----------------------|------------------------------------|--|-------------------------|--------------------------|---------------|
| | Expenses | Charges for Services | Operating Grants and Contributions | Capital Grants and Contributions | Governmental Activities | Business-Type Activities | Total |
| Governmental activities: | | | | | | | |
| General government: | | | | | | | |
| General government | \$675,134 | \$576,558 | \$52,129 | - | (\$46,447) | - | (\$46,447) |
| Public safety | 2,357,658 | 587,681 | - | \$200 | (1,769,777) | - | (1,769,777) |
| Public works | 137,125 | - | - | - | (137,125) | - | (137,125) |
| Cultural and recreational | 275,347 | 7,293 | - | - | (268,054) | - | (268,054) |
| Economic development | 44,646 | 336,365 | - | - | 291,719 | - | 291,719 |
| Community development | 197,194 | 269,637 | - | - | 72,443 | - | 72,443 |
| Social and welfare | 45,420 | 39,295 | - | - | (6,125) | - | (6,125) |
| Interest on long-term debt | 168,346 | - | - | - | (168,346) | - | (168,346) |
| Total governmental activities | \$3,900,870 | \$1,816,829 | 52,129 | \$200 | (\$2,031,712) | - | (\$2,031,712) |
| Business-type activities: | | | | | | | |
| Water and sewer | \$2,851,037 | \$2,468,749 | \$82,501 | - | - | (\$299,787) | (\$299,787) |
| General revenues: | | | | | | | |
| Taxes: | | | | | | | |
| General property taxes | | | | | 1,361,119 | - | 1,361,119 |
| Sales tax | | | | | 1,160,334 | - | 1,160,334 |
| Franchise tax | | | | | 385,146 | - | 385,146 |
| Interest income | | | | | 4,288 | 3,756 | 8,044 |
| Administrative fee | | | | | 167,108 | - | 167,108 |
| Miscellaneous | | | | | 216,029 | - | 216,029 |
| Transfers | | | | | 2,309 | (2,309) | - |
| Total general revenues and proceeds | | | | | 3,296,333 | 1,447 | 3,297,780 |
| Change in net assets | | | | | 1,264,621 | (298,340) | 966,281 |
| Net assets-beginning | | | | | 3,799,270 | 10,714,910 | 14,514,180 |
| Net assets-ending | | | | | \$5,063,891 | \$10,416,570 | \$15,480,461 |

CITY OF ALVARADO, TEXAS
BALANCE SHEET
GOVERNMENTAL FUNDS
September 30, 2012

| | General Fund | Debt Service Fund | Royalty Fund | Other Governmental Funds | Total Governmental Funds |
|-------------------------------------|--------------------|-------------------|--------------------|--------------------------|--------------------------|
| ASSETS | | | | | |
| Cash | \$355,661 | - | \$2,237 | \$272,663 | \$630,561 |
| Investments | 437,047 | - | 1,129,550 | 1,134,160 | 2,700,757 |
| Receivables, net | | | | | |
| Accounts | 81,840 | | | - | 81,840 |
| Property taxes | 71,714 | \$57,098 | | - | 128,812 |
| Sales taxes | 177,642 | | | 74,825 | 252,467 |
| Fines receivable | 185,693 | | | - | 185,693 |
| Restricted | | | | | |
| Intergovernmental Receivable | 25 | | | - | 25 |
| Investments | | 336,529 | | 115,139 | 451,668 |
| Total assets | <u>\$1,309,622</u> | <u>\$393,627</u> | <u>\$1,131,787</u> | <u>\$1,596,787</u> | <u>\$4,431,823</u> |
| LIABILITIES | | | | | |
| Accounts payable | \$38,023 | \$383,777 | \$1,896 | - | \$423,696 |
| Accrued liabilities | 191,324 | | | - | 191,324 |
| Due to other governments | 13,387 | | | - | 13,387 |
| Deferred tax revenue | 253,897 | 54,453 | | | 308,350 |
| Total liabilities | <u>496,631</u> | <u>438,230</u> | <u>1,896</u> | <u>-</u> | <u>936,757</u> |
| FUND BALANCES | | | | | |
| Fund balances: | | | | | |
| Nonspendable | | | | | |
| Restricted | 44,603 | (44,603) | | 1,596,787 | 1,596,787 |
| Committed | | | 1,129,891 | | 1,129,891 |
| Assigned | | | | | |
| Unassigned | 768,388 | | | | 768,388 |
| Total fund balances | <u>812,991</u> | <u>(44,603)</u> | <u>1,129,891</u> | <u>1,596,787</u> | <u>\$3,495,066</u> |
| Total liabilities and fund balances | <u>\$1,309,622</u> | <u>\$393,627</u> | <u>\$1,131,787</u> | <u>\$1,596,787</u> | |

Amounts reported for governmental activities in the statement of net assets are different because:

Capital assets used in governmental activities are not financial resources and, therefore, are not reported in the funds
 Long-term liabilities, including bond payable, are not due and payable in the current period and therefore are not reported in the funds (Note B)
 Compensated absences are not due and payable in the current period and therefore are not reported in the funds

Net assets of governmental activities

6,141,595
 (4,478,056)
 (94,714)
\$ 5,063,891

CITY OF ALVARADO, TEXAS
STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCE
GOVERNMENTAL FUNDS

For the Fiscal Year Ended September 30, 2012

| | General Fund | Debt Service Fund | Royalty Fund | Other Governmental Funds | Total Governmental Funds |
|--|------------------|-------------------|--------------------|--------------------------|--------------------------|
| REVENUE: | | | | | |
| General property taxes, interest and penalties | \$757,783 | \$603,336 | - | - | \$1,361,119 |
| Sales tax | 1,009,094 | - | - | \$336,365 | 1,345,459 |
| Hotel tax | - | - | - | 149,899 | 149,899 |
| Fines and forfeitures | 587,681 | - | - | - | 587,681 |
| Franchise tax | 385,146 | - | - | - | 385,146 |
| Mixed beverage tax | 1,341 | - | - | - | 1,341 |
| Rental fees | 39,295 | - | - | - | 39,295 |
| Intergovernmental | 321,766 | - | - | - | 321,766 |
| Licenses, fees and permits | 105,215 | - | - | 37,635 | 142,850 |
| Interest | 1,712 | - | \$1,309 | 1,267 | 4,288 |
| Contributions and donations | 200 | - | - | - | 200 |
| Water/Sewer administrative fee | 174,401 | - | - | - | 174,401 |
| Oil and gas royalties | - | - | 430,865 | - | 430,865 |
| Miscellaneous | 215,417 | - | - | 612 | 216,029 |
| Total Revenue | 3,599,051 | 603,336 | 432,174 | 525,778 | 5,160,339 |
| EXPENDITURES: | | | | | |
| Current operating | | | | | |
| General government | 389,255 | - | 89,528 | 13,200 | 491,983 |
| Public safety | 2,113,560 | - | - | 15,283 | 2,128,843 |
| Community development | 186,017 | - | - | 11,177 | 197,194 |
| Public works | 104,701 | - | - | - | 104,701 |
| Cultural and recreational | 231,185 | - | - | - | 231,185 |
| Social and welfare | 44,882 | - | - | - | 44,882 |
| Economic development | - | - | - | 44,646 | 44,646 |
| Capital Outlay | 14,700 | - | 540,869 | 5,222 | 560,791 |
| Debt Service | - | - | - | - | - |
| Principal | - | 534,969 | - | - | 534,969 |
| Interest | - | 159,312 | - | - | 159,312 |
| Paying agent | - | 900 | - | - | 900 |
| Total Expenditures | 3,084,300 | 695,181 | 630,397 | 89,528 | 4,499,406 |
| Excess (Deficiency) of Revenues Over (Under) Expenditures | 514,751 | (91,845) | (198,223) | 436,250 | 660,933 |
| OTHER FINANCING SOURCES: | | | | | |
| Transfers in | - | 63,329 | - | - | 63,329 |
| Transfers out | (40,566) | - | - | (20,454) | (61,020) |
| NET CHANGE IN FUND BALANCES | 474,185 | (28,516) | (198,223) | 415,796 | 663,242 |
| FUND BALANCE - October 1, 2011 | 338,806 | (16,087) | 1,328,114 | 1,180,991 | 2,831,824 |
| FUND BALANCE - September 30, 2012 | \$812,991 | (\$44,603) | \$1,129,891 | \$1,596,787 | \$3,495,066 |

CITY OF ALVARADO, TEXAS
RECONCILIATION OF THE STATEMENTS OF REVENUES, EXPENDITURES, AND CHANGES
IN FUND BALANCE OF GOVERNMENTAL FUNDS TO THE STATEMENT OF ACTIVITIES
For the Year Ended September 30, 2012

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

| | |
|---|---------------------------|
| Net change in fund balances - total governmental funds | \$663,242 |
| 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. This is the amount of assets acquired during the year. | 703,740 |
| 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. This is the amount for depreciation in the current period. | (489,055) |
| The net effect of various miscellaneous transactions involving capital assets (i.e., sales, trade-ins, and interfund transfers) is to decrease net assets. | 79,751 |
| Governmental funds report principle reductions as expenditures. However, in the statement of activities the payment of the debt principal reduces the outstanding liability. This is the amount of principal payments during the current period. | 543,902 |
| The issuance of long-term debt (e.g. bonds, leases, compensated absences) provides current financial resources to government funds. Issuance of long-term debt does not effect net assets. This is the amount of debt issued in the current period. | (142,247) |
| Governmental funds do not report compensated absences as expenditures. However, in the statement of activities the accrual of compensated absences increases the expenditure accounts. This is the amount of compensated absences expenditures for the current period. | <u>(94,712)</u> |
| Changes in net assets of governmental activities | <u><u>\$1,264,621</u></u> |

CITY OF ALVARADO, TEXAS
STATEMENT OF NET ASSETS
WATER AND SEWER PROPRIETARY FUND
September 30, 2012

ASSETS

| | |
|--|------------|
| Current assets: | |
| Cash | \$240,049 |
| Investments | 1,216,820 |
| Accounts receivable (net of allowance for uncollectible amounts) | 334,183 |
| Inventory | 46,967 |
| Restricted assets | |
| Cash | 4,800,808 |
| Deposits | 119,346 |
| Investments | 73,389 |
| Total current assets | 6,831,562 |
| Noncurrent assets: | |
| Capital assets, net | 12,541,035 |
| Deferred bond issuance costs | 231,703 |
| Total noncurrent assets | 12,772,738 |
| Total assets | 19,604,300 |

LIABILITIES

| | |
|------------------------------|-----------|
| Current liabilities: | |
| Accounts payable | 80,306 |
| Accrued liabilities | 15,122 |
| Deposits | 126,596 |
| Current portion | |
| Revenue bonds payable | 167,000 |
| Capital leases | 23,554 |
| Compensated absences | 20,041 |
| Total current liabilities | 432,619 |
| Noncurrent liabilities: | |
| Revenue bonds payable | 8,683,160 |
| Capital lease payable | 71,951 |
| Total noncurrent liabilities | 8,755,111 |
| Total liabilities | 9,187,730 |

NET ASSETS

| | |
|---|--------------|
| Invested in capital assets, net of related debt | 3,595,370 |
| Restricted for: | |
| Capital Improvements | 4,868,556 |
| Unrestricted | 1,952,644 |
| Total net assets | \$10,416,570 |

See accompanying notes and independent auditor's report

CITY OF ALVARADO, TEXAS
STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN FUND NET ASSETS
WATER AND SEWER PROPRIETARY FUND
For the Fiscal Year Ended September 30, 2012

| | |
|--|--------------|
| OPERATING REVENUES: | |
| Water service | \$1,158,116 |
| Sewer service | 781,332 |
| Garbage service | 450,288 |
| Late charges | 59,938 |
| Miscellaneous income | 19,075 |
| Total operating revenues | 2,468,749 |
| | |
| OPERATING EXPENSES: | |
| Personnel services | 510,112 |
| Contractual services | 870,446 |
| Supplies and maintenance | 431,356 |
| Administrative fees | 256,951 |
| Depreciation and amortization | 605,630 |
| Total operating expenses | 2,674,495 |
| Operating income (loss) | (205,746) |
| | |
| NON-OPERATING REVENUES (EXPENSES) | |
| Grant revenue | 82,501 |
| Interest income | 3,756 |
| Interest expense | (176,542) |
| Net non-operating revenues (expenses) | (90,285) |
| INCOME (LOSS) BEFORE CONTRIBUTIONS AND TRANSFERS | (296,031) |
| | |
| Operating transfers in | 5,356,144 |
| Operating transfers out | (5,358,453) |
| Net transfers | (2,309) |
| CHANGE IN NET ASSETS | (298,340) |
| | |
| NET ASSETS, October 1, 2011 | 10,714,910 |
| NET ASSETS, September 30, 2012 | \$10,416,570 |

See accompanying notes and independent auditor's report

CITY OF ALVARADO, TEXAS
STATEMENT OF CASH FLOWS
WATER AND SEWER PROPRIETARY FUND
For the Fiscal Year Ended September 30, 2012

CASH FLOWS FORM OPERATING ACTIVITIES:

| | |
|---|-------------|
| Cash received from: | |
| Customers | \$2,640,241 |
| Interfund payments | 256,951 |
| Cash paid to/for: | |
| Employees | (502,092) |
| Suppliers | (2,110,597) |
| Net cash flows provided by operating activities | 284,503 |

CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES

| | | |
|--|---------------|---------|
| Operating transfers out | (\$5,358,453) | |
| Operating transfers in | 5,356,144 | |
| Net cash flows used by noncapital financing activities | | (2,309) |

CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES:

| | | |
|---|-----------|-----------|
| Acquistion and construction of capital assets | (397,857) | |
| Principal paid on bonds, notes and lease obligations | (178,905) | |
| Intergovernmental grants | 82,501 | |
| Interest paid on bonds, notes and lease obligations | (176,542) | |
| Net cash flows used in capital and related financing activities | | (670,803) |

CASH FLOWS FROM INVESTING ACTIVITIES:

| | | |
|---|-----------|-----------|
| Proceeds received from certificate of obligations | 4,810,000 | |
| Amount received from interest income | 3,756 | |
| Proceeds received from capital leases | 103,369 | |
| Net cash flows provided by investing activities | | 4,917,125 |

| | |
|---|-----------|
| Net decrease in cash and cash equivalents | 4,528,516 |
|---|-----------|

| | |
|---|-------------|
| Cash and cash equivalents, October 1, 2011 | 1,921,896 |
| Cash and cash equivalents, September 30, 2012 | \$6,450,412 |

RECONCILIATION OF OPERATING INCOME TO NET CASH FLOWS FROM OPERATING ACTIVITIES

| | | |
|---|-----------|-------------|
| Operating income (loss) | | (\$205,746) |
| Adjustments for transactions not requiring cash | | |
| Depreciation and amortization | \$605,630 | |
| Miscellaneous (income) expense | (1,320) | |
| Change in current assets and current liabilities | | |
| (Increase) decrease in accounts receivable | 166,012 | |
| (Increase) decrease in inventory | 2,662 | |
| Increase (decrease) in accounts payable | (296,235) | |
| Increase (decrease) in accrued liabilities | 3,931 | |
| Increase (decrease) in customer deposits | 5,480 | |
| Increase (decrease) in compensated absences payable | 4,089 | |
| Total adjustments and changes | | 490,249 |
| Net cash provided by operating activities | | \$284,503 |

See accompanying notes and independent auditor's report

CITY OF ALVARADO, TEXAS
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2012

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The financial statements of the City of Alvarado, Texas (the “City”), have been prepared in conformity with accounting principles generally accepted in the United States of America (“GAAP”). The Governmental Accounting Standards Board (“GASB”) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. Governments are also required to follow the pronouncements of the Financial Accounting Standards Board (FASB) issued through November 30, 1989 (when applicable) that do not conflict with or contradict GASB pronouncements. Although the City has the option to apply FASB pronouncements issued after that date to its business-type activities and enterprise funds, the City has chosen not to do so. The more significant accounting policies established in GAAP and used by the City are discussed below.

1. Reporting Entity

The City is a municipal corporation formed in 1889 by charter as a general law city. The City is governed by an elected mayor and six-member Council. Two council members are elected for each of three wards while the mayor is elected at large. As required by generally accepted accounting principles, these financial statements present the City and its component units, for which the City is considered to be financially accountable. Blended component units, although legally separate entities, are in substance, part of the City’s operations, and data from these units are combined with data from the primary government. Information regarding blended component units can be obtained at City Hall.

Blended Component Units

Alvarado Economic Development Corporation (“AEDC”) – This entity was created in May of 2001. It began collecting sales and use tax in October of 2001. The entity’s board of directors is appointed by the City Council and the City Management maintains significant continuing management oversight with respect to policies. Additionally, the City is ultimately responsible for all fiscal matters. The AEDC was formed for the purpose of benefiting and accomplishing public purposes for the promotion and development of industrial and manufacturing enterprises and to promote and encourage employment and public welfare of the City by issuing bonds on behalf of the City for financing as stated in the Development Corporation Act of 1979. The AEDC provides these services exclusively to the City and does not issue separate financial statements. Results of operations are combined with data from the primary government in the Other Governmental Funds.

2. Government-wide and Fund Financial Statements

The basic financial statements include both government-wide (based on the City as a whole) and fund financial statements. The government-wide financial statements (i.e., the statement of net assets and the statement of activities) report information on all of the non-fiduciary activities of the primary government and its component units. For the most part, the effect of the 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. Likewise, the primary government is reported separately from certain legally separate component units for which the primary government is financially accountable.

In the government-wide Statement of Net Assets, both the governmental and business-type activities columns (a) are presented on a consolidated basis by column, (b) and are reported on a full accrual, economic resource basis, which recognizes all long-term assets and receivables as well as long-term debt and obligations. The City's net assets are reported in three parts – invested in capital assets, net of related debt; restricted assets; and unrestricted net assets. The City first utilizes restricted resources to finance qualifying activities.

The government-wide Statement of Activities demonstrates the degree to which the direct expenses of a functional category (Police, Public Works, etc.) or segment are offset by program revenues. Direct expenses are those that are clearly identifiable with specific function or segment. 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 or segment, 2) grants and contributions that are restricted to meeting the operational requirements of a particular function or segment, and 3) grants and contributions that are restricted to meeting capital requirements of a particular function or segment. Taxes and other items not properly included among program revenues are reported instead as general revenues. The City does not allocate indirect costs. An administrative service fee is charges by the General Fund to the proprietary fund to recover the direct costs of General Fund services provided (finance, personnel, purchasing, legal, technology management, etc.)

The net cost (by function or business-type activity) is normally covered by general revenue (property, sales, franchise taxes, intergovernmental revenues, interest income, etc.). Separate fund based financial statements are provided for governmental funds, proprietary funds, and fiduciary funds, even though the latter are excluded from the government-wide financial statements. Major individual governmental funds and major individual enterprise funds are reported as separate columns in the fund financial statements. The major governmental funds are the general fund, debt service fund, and royalty fund. The major enterprise fund is the water and sewer fund. GASB Statement No. 34 sets forth minimum criteria (percentage of assets, liabilities, revenues or expenditures/expenses of either fund category for the governmental and enterprise combined) for the determination of major category funds. The City has four non-major funds, which are the capital projects fund, hotel and occupancy tax fund, grant fund and the AEDC special revenue fund. The non-major funds are combined in a separate column in the fund financial statements.

The government-wide focus is more on the sustainability of the City as an entity and the change in aggregate financial position resulting from the activities of the fiscal period. The focus of the fund financial statements is on the major individual funds of the governmental and business-type categories, as well as the fiduciary funds, (by category) and the component units. Each presentation provides valuable information that can be analyzed and compared to enhance the usefulness of the information.

3. Measurement Focus and Basis of Accounting

The government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting, as are the proprietary fund and fiduciary fund 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 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 when they are susceptible to accrual, as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the government considers revenues (except grant revenues) to be available if they are collected within 30 days of the end of the current fiscal period. The City considers the availability period for grants to be one year. 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 judgment, are recorded only when the obligation has matured and will be paid shortly after year end (not to exceed one month).

Ad valorem, franchise and sales tax revenues recorded in the General Fund and ad valorem tax revenues recorded in the Debt Service Fund are recognized under the susceptible to accrual concept. Licenses and permits, charges for services, fines and forfeitures, contributions, and miscellaneous revenues are recorded as revenues when received in cash, as the resulting receivable is immaterial. Investment earnings are recorded as earned since they are measurable and available. In applying the susceptible to accrual concept to intergovernmental revenues, the legal and contractual requirements of the numerous individual programs are used as guidance. There are, however, essentially two types of these revenues. In one, as soon as all eligibility requirements have been met, including monies must be expended for the specific purpose or project before any amounts will be paid to the City; therefore, revenues are recognized based upon the expenditures recorded. In other, monies are virtually unrestricted as to purpose of expenditure and are usually revocable only for failure to comply with prescribed compliance requirements. These resources are reflected as revenues at the time of receipt or earlier if all eligibility requirements are met.

Business type activities and all proprietary funds are accounted for on a flow of economic resources measurement focus. With this measurement focus, all assets and all liabilities associated with the operation of these funds are included on the balance sheet. Proprietary fund-

type operating statements present increases (e.g. revenues) and decreases (e.g. expenses) in net total assets. 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 water and sewer are charges to customers for sales and services. Operating expenses for the enterprise funds include the cost of sales and services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

The government reports the following major governmental funds:

The General Fund is the operating fund of the City. All general tax revenues and other receipts that are not restricted by law or contractual agreements to some other fund are accounted for in this fund. General operating expenditures, the fixed charges, and the capital improvement costs that are not paid through other funds are paid from the General Fund.

The Debt Service Fund is used to account for the accumulation of resources for, and the payment of principal, interest and related costs on general long-term debt. The primary source of revenue is ad valorem taxes, which are levied by the City.

The Royalty Fund is used to account for the accumulation of royalties from oil and gas leases on land held by the city. The primary source of revenue is royalty income. Expenses are decided by the City.

The Other Governmental Funds column is a summarization of all the non-major governmental fund types. These are as follows:

The Capital Projects Fund is used to account for financial resources to be used for the acquisition or construction of major capital facilities.

Alvarado Economic Development Corporation Fund (AEDC) – is used to account for the revenues collected for economic development and related expenditures.

The Grant Fund – is used to account for the proceeds of grants that are restricted to expenditures for specified purposes.

The Hotel Occupancy Tax Fund is used to account for the revenues collected for hotel and occupancy tax and related expenditures.

The government reports the following major proprietary fund:

The Water and Sewer Fund accounts for the operation of the City's water and sewer utility. Activities of the Fund include administration, operation and maintenance of the water and sewer system and billing and collection activities. The Fund also accounts for the accumulation of resources for, and the payment of, long-term debt principal and interest for

general obligation and revenue bonds. All costs are financed through charges made to utility customers with rates reviewed regularly and adjusted if necessary to ensure integrity of the Fund.

4. Assets, Liabilities, and Net Assets or Equity

Cash and Cash Equivalents

The City's cash and cash equivalents are considered to be cash on hand, demand deposits, and investments with original maturities of three months or less from the end of the fiscal year.

For fiscal year 2012, the City invested in the external government investment pool administered by the State of Texas, which is entitled the TexPool Fund, as authorized by the City's investment policy. The City records interest revenue earned from investment activities in each respective fund and recognizes its investments on a fair value basis.

Inventory

Inventory consists primarily of water and sewer plant parts and supplies, valued at estimated FIFO. Inventory is expensed when purchased and adjusted to actual at year-end. Inventory as of September 30, 2012 was \$46,967.

Prepaid Expenditures/Expenses

Payments made to vendors for services that will benefit periods beyond are recorded as prepaid items. The nonspendable portion of the fund balance is provided equal to the amount of prepaid items, as the amount is not available for expenditure. These payments are recognized under the consumption method.

Capital Assets

Capital assets, which include property, plant, equipment, and infrastructure assets (e.g., roads, bridges, sidewalks, and similar items), are recorded in the applicable governmental or business-type activities columns in the government-wide financial statements and in the fund financial statements for proprietary funds. The government defines capital assets as assets with an initial, individual cost of more than \$5,000 (amount not rounded) and an estimated useful life in excess of two years. Such assets are recorded at cost where historical records are available and at an estimated historical cost where no historical records exist. Donated fixed assets are valued at their estimated fair value on the date of donation.

The costs of normal maintenance and repairs that do not add to the value of the asset or materially extend asset lives are not capitalized, while improvements and betterments are capitalized.

Depreciation has been calculated on each class of depreciable property using the straight-line method. Estimated useful lives are as follows:

| | |
|-----------------------------------|-------------|
| Building and Improvements | 20-30 years |
| Water Systems | 10-33 years |
| Sewer Systems | 50 years |
| Vehicles, Machinery and Equipment | 3-5 years |
| Infrastructure | 30 years |

Interest is capitalized on capital assets acquired with tax-exempt debt. The amount of interest to be capitalized is calculated by offsetting interest expense incurred from the date of the borrowing until completion of the project with the interest earned on invested proceeds over the same period. The City did not capitalize any interest during the fiscal year 2012.

Property Tax

Property taxes attach as an enforceable lien on property as of January 1st. Taxes are levied on October 1 and are due and payable on or before January 31st of the following year. All unpaid taxes become delinquent on February 1 of the following year. The Johnson County Central Appraisal District bills and collects property taxes on behalf of the City. Property tax revenues are recognized when they are both measurable and available. Revenues are considered both measurable and available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the government considers revenues to be available if they are collected within 30 days of the end of the current fiscal period.

Compensated Absences

Vested or accumulated vacation leave is accrued in the government-wide and proprietary fund financial statements when incurred. No liability is recorded for nonvesting, accumulating rights to receive sick pay benefits. Vacation is earned in varying amounts up to a maximum of twenty (20) days for city employees with twelve (12) or more years of service and up to a maximum of approximately twenty-eight (28) days for fire suppression personnel with twelve (12) or more years of service. Employee vacation policy allows for the accrual and carryover of 240 hours. In addition, the City allows for the accrual of compensatory time for non-department heads. Compensatory and vacation time can either be paid or used. As of September 30, 2012, the liability for accrued vacation and compensatory time, calculated in accordance with GASB Statements 16, "Accounting for Compensated Absences," was \$94,714 in the general fund. The amount applicable to the Proprietary Fund was \$20,041 and has been recorded in that fund.

Deferred Bond Issuance Costs

In Government Fund types, bond issuance costs are amortized equally over the term of the bond. Bond issuance costs for Proprietary Fund types are deferred and amortized over the term of the bonds using the bonds-outstanding method, which approximates the effective interest method. In the proprietary fund, amortization expense is presented on the Statement of Revenue, Expense and Change in Fund Net Assets – Water and Sewer Proprietary Fund.

Fair Value of Financial Instruments

The following disclosure of the estimated fair value of financial instruments is made in accordance with the requirements of AU Section 312, "Disclosures about Fair Value of Financial Instruments." The City, using available market information and appropriate valuation methodologies, has determined the estimated fair value amounts. However, considerable judgment is required in interpreting market data to develop the estimates of fair value. Accordingly, the estimates presented herein are not necessarily indicative of the amounts that the companies could realize in a current market exchange. The use of different market assumptions and/or estimation methodologies may have a material effect on the estimated fair value amounts.

Cash and Cash Equivalents, Investments, Accounts Receivable, Accounts Payable and Accrued Expenses – The carrying amounts of these items are a reasonable estimate of their value.

Long-term Debt – Interest rates that are currently available to the City for issuance of debt with similar terms and remaining maturities are used to estimate fair value for debt issues for which no market quotes are available. The carrying amount of this item is a reasonable estimate of fair value.

The fair value estimates presented herein are based on pertinent information available to management as of September 30, 2012. Although management is not aware of any factors that would significantly affect the estimated fair value amounts, such amounts have not been comprehensively revalued for purposes of these financial statements since that date, and current estimates of fair value may differ significantly from the amounts presented herein.

Interfund Transfers and Charges

Short-term advances between funds are accounted for in the appropriate interfund receivable and payable on the Balance Sheet – Governmental Funds and the Statement of Fund Net Assets – Proprietary Fund. All legally authorized transfers are appropriately treated as operating transfers and are included in the results of operations on the Statement of Revenues, Expenditures and Changes in Fund Balance – Governmental Funds and Statement of Revenues, Expenses and Changes in Fund Net Assets – Proprietary Fund. The City allocates to the Water and Sewer Fund a portion of the salaries and wages and related costs of personnel who perform administrative services for the fund but are paid through the General Fund. During the year ended September 30, 2012, the City chose to allocate a portion of the administrative services to the Water and Sewer Fund which totaled \$174,401.

Restricted Assets

Certain proceeds of Enterprise Fund Revenue Bonds, as well as certain resources set aside for their repayment are classified as Restricted Assets on the balance sheet because their use is limited by applicable bond covenants.

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 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 amounts 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, are reported as debt service expenditures.

Use of 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, disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting periods. Final settlement amounts could differ from those estimates.

Fund Balance Classification

The preparation of financial statements in conformity with government accounting standards requires management to classify the fund balances. For *committed* fund balance classification, the City Council must take formal action to establish, modify or rescind a fund balance commitment. For *assigned* fund balance classification, the City Manager with a concurrence of the Finance Director is authorized to assign amounts for a specific purpose. The *restricted* fund balance classification includes amounts that have constraints that are externally imposed (creditors, grantors, etc) or imposed by enabling legislation. The *nonspendable* classification includes amounts that are not in spendable form or required to be maintained intact. The *unassigned* fund balance classification represents fund balance that has not been classified to another category. The City considers an amount spent when an expenditure is incurred for purposes for which both *restricted* or *unrestricted* fund balance is available. In addition, the City considers an amount spent when an expenditure is incurred for purposes for which an amount in the *committed*, *assigned*, or *unassigned* amounts could be used.

Budget Control

The City operates as a Type A General Law Municipality under the Texas Local Government Code. The City Council adopts an annual budget prepared in accordance with generally accepted accounting principles in the United States of America. The City Council may transfer part or all of any unencumbered appropriation balance among programs within a specific fund, and, any revisions that alter the total expenditures must be approved by the City Council. The City Council may require their approval of these transfers above a limit they wish to establish. The current City Council has not established a limit that they wish to approve on transfers. Council approval is needed only if the expenditures exceed the certain thresholds set by the Council.

The City, for management purposes, adopts budgets for all funds. Legal budgets are adopted for all funds. Capital Projects are funded through the issuance of general obligation debt authorized for a specific purpose.

5. Implementation of New Accounting Principles

The GASB has issued the following Statements which will become effective in future years as shown below:

Statement No. 61, *“The Financial Reporting Entity: Omnibus an amendment of GASB No. 14 and 34”* The objective of this Statement is to improve financial reporting for a government financial reporting entity. This Statement will become effective for the City in fiscal year 2013. Management has not yet determined the effect of this statement on financial statements.

Statement No. 62, *“Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements”* The objective of this Statement is to incorporate into the GASB’s authoritative literature certain accounting and financial reporting guidance that is included in the following pronouncements issued on or before November 30, 1989, which does not conflict or contradict GASB pronouncements: Financial Accounting Standard Board (FASB) Statements and Interpretations, Accounting Principles Board Opinions, Accounting Research Bulletins of the American Institute of Certified Public Accountants (AICPA) Committee on Accounting Procedure. This Statement will become effective for the City in fiscal year 2013. Management has not yet determined the effect of this statement on financial statements.

Statement No. 63 *“Financial Reporting of Deferred Outflows of Resources, Deferred Inflow of Resources, and Net Position”* This Statement provides financial reporting guidance for deferred outflow of resources and deferred inflow of resources. This Statement will become effective for the City in fiscal year 2013. Management has not yet determined the effect of this statement on financial statements.

Statement No. 65, *“Items Previously Reported as Assets and Liabilities”* This statement establishes accounting and financial reporting standards that reclassify, as deferred outflows of resources or deferred inflows of resources, certain items that were previously reported as assets and liabilities and recognizes, as outflows of resources or inflows of resources, certain items that were previously reported as assets and liabilities. This Statement will become effective for the City in fiscal year 2014. Management has not yet determined the effect of this statement on financial statements.

Statement No. 66, *“Technical Corrections – 2012 an amendment of GASB Statements No. 10 and 62”* The objective of this Statement is to improve accounting and financial reporting for a governmental financial reporting entity by resolving conflicting guidance that resulted from the issuance of two pronouncements, Statement No 54 *“Fund Balance Reporting and Governmental Fund Type Definitions,”* and No. 62 *“Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASBA and AICPA Pronouncements.”* This

Statement will become effective for the City in fiscal year 2014. Management has not yet determined the effect of this statement on financial statements.

Statement No. 67, “*Financial Reporting for Pension Plans – and amendment of GASB Statement No. 25*” The objective of this Statement is to improve financial reporting by state and local government pension plans. This Statement will become effective for the City in fiscal year 2014. Management has not yet determined the effect of this statement on financial statements.

Statement No. 68, “*Accounting and Financial Reporting for Pensions – an amendment of GASB Statement No. 27*” The objective of this Statement is to improve accounting and financial reporting by state and local governments for pensions. This Statement will become effective for the City in fiscal year 2015. Management has not yet determined the effect of this statement on financial statements.

NOTE B – RECONCILIATION OF GOVERNMENT-WIDE AND FUND FINANCIAL STATEMENTS

Explanation of certain differences between the governmental fund balance sheet and the government-wide statement of net assets:

The government fund balance sheet includes a reconciliation between fund balance – total governmental funds and net assets – governmental activities as reported in the governmental-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 \$4,478,056 difference are as follows:

| | |
|--|------------------------|
| Bonds payable | \$4,180,000 |
| Issuance costs (to be amortized over life of debt) | (158,997) |
| Premium on issuance of bonds | 186,046 |
| Capital lease payable | 113,818 |
| Notes payable | <u>157,189</u> |
| Net adjustment to reduce fund balance – total governmental funds to arrive at net assets – governmental activities | <u>\$4,478,056</u> |

NOTE C – CASH AND INVESTMENTS

The City maintains a cash pool that is available for use by all funds. Each funds portion of this pool is reflected on the balance sheet or statement of net assets as “Cash” under each fund’s caption. Except for bond-related and other restricted transactions, the City conducts all its banking and investment transactions with the depository bank, First Financial Bank, Alvarado.

The City maintains separate investment accounts. Each fund type's portion is reflected on the combined balance sheet as "Investments" under each fund's caption.

Deposits

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 market value of not less than the principal amount of the deposits. The City's deposits, including certificates of deposit, were fully insured or collateralized as required by the state statutes at September 30, 2012. At year-end, the carrying amount of the City's deposits was \$487,234, with respective bank balances of \$512,889. Included in the bank balances are Certificates of Deposit totaling \$119,346.

Investments

State statutes, city bond ordinances and city resolutions authorize the City's investments. The City is authorized to invest idle funds with the external government investment pool administered by the State of Texas, which is entitled the TexPool Fund. TexPool operates in a manner consistent with the SEC Rule 2a7 of the Investment Company Act of 1940. TexPool uses amortized cost rather than market value to report net assets to compute share prices. Accordingly, the fair value of the position in TexPool is the same as the value of TexPool shares. The City's investment policy does not contain any specific provisions intended to limit the City's exposure to interest rate risk or credit risk.

The City's investments carried at fair value as of September 30, 2012 are:

| <u>Investments:</u> | <u>Fair Value</u> | <u>Effective Duration</u> | <u>Credit Risk</u> |
|---------------------|-------------------|---------------------------|--------------------|
| Government Pools | | | |
| Unrestricted | \$3,917,577 | N/A | AAAM |
| Restricted | 525,051 | N/A | AAAM |

TexPool is an external investment pool operated by the Texas Comptroller of Public Accounts and is not SEC registered. The Texas Interlocal Cooperation Act and the Texas Public Funds Investments Act provide for creation of public funds investment pools and permit eligible governmental entities to jointly invest their funds in authorized investments. The State Comptroller has established an advisory board composed both of participants in TexPool and of other persons who do not have a business relationship with TexPool. The Advisory Board members review the investment policy and management fee structure.

Interest Rate Risk – The City minimizes its interest rate risk by only investing in government investment pools.

Credit Risk – The City minimizes its credit risk by only investing in government investment pools. As noted in the above table, TexPool is rated AAAM by Standard & Poors. As a requirement to maintain the rating, weekly portfolio information must be submitted to Standard & Poors, as well as the office of the Comptroller of Public Accounts for review.

NOTE D – RECEIVABLES

Receivables at September 30, 2012, consisted of the following:

| | Governmental Funds | | | | Proprietary Fund |
|--------------------------------------|--------------------|-----------------|-----------------|------------------|--------------------------|
| | General | Debt Service | Other | Total | Water & Sewer Enterprise |
| Taxes Receivable | | | | | |
| Ad valorem taxes | \$85,998 | \$68,468 | - | \$154,466 | - |
| Allowance for uncollectible accounts | (14,284) | (11,370) | - | (25,654) | - |
| Sales taxes | 177,642 | | \$74,825 | 252,467 | - |
| Total Taxes Receivable | 249,356 | 57,098 | 74,825 | 381,249 | |
| Services Receivable | | | | | |
| Service accounts | 81,840 | - | - | 81,840 | \$340,086 |
| Allowance for uncollectible accounts | - | - | - | - | (5,903) |
| Total Services Receivable | 81,840 | - | - | 81,840 | 334,183 |
| Other Receivables | | | | | |
| Court fees & other | 452,478 | - | - | 452,478 | |
| Allowance for uncollectible accounts | (266,785) | | | (266,785) | |
| | 185,693 | - | | 185,693 | |
| Total Receivables | \$516,889 | \$57,098 | \$74,825 | \$648,812 | \$334,183 |

NOTE E – CHANGES IN CAPITAL ASSETS**Primary Government**

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

| | Balance 9/30/11 | Additions | Retirements | Transfers | Balance 9/30/12 |
|--|--------------------|-----------|-------------|-----------|--------------------|
| Land | \$462,548 | \$-0- | \$(-0-) | \$(-0-) | \$462,548 |
| Construction in progress | 25,367 | -0- | (-0-) | (-0-) | 25,367 |
| Building & improvements | 2,209,421 | 23,055 | (-0-) | (-0-) | 2,232,476 |
| Infrastructure | 3,580,323 | 401,657 | (-0-) | (-0-) | 3,981,980 |
| Vehicles | 1,324,210 | 115,051 | (15,986) | (-0-) | 1,423,275 |
| Parks improvements | 337,525 | -0- | (-0-) | (-0-) | 337,525 |
| Equipment | 1,068,395 | 163,977 | (-0-) | (-0-) | 1,232,372 |
| Total capital assets | 9,007,789 | 703,740 | (15,986) | -0- | 9,695,543 |
| Less accumulated depreciation: | | | | | |
| Building & improvements | 352,023 | 48,358 | (-0-) | (-0-) | 400,381 |
| Infrastructure | 653,214 | 123,499 | (-0-) | (-0-) | 776,713 |
| Vehicles | 1,054,783 | 152,329 | (15,986) | (-0-) | 1,191,126 |
| Parks improvements | 209,937 | 54,384 | (-0-) | (-0-) | 264,321 |
| Equipment | 810,922 | 110,485 | (-0-) | (-0-) | 921,407 |
| Total accumulated depreciation | 3,080,879 | 489,055 | (15,986) | (-0-) | 3,553,948 |
| Governmental activities capital assets, net | \$5,926,910 | \$214,685 | \$(-0-) | \$(-0-) | \$6,141,595 |

Business-Type Activities

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

| | Balance 9/30/11 | Additions | Retirements | Transfers | Balance 9/30/12 |
|--|---------------------|--------------------|-----------------|----------------|---------------------|
| Land | \$602,949 | \$-0- | \$(-0-) | \$443,010 | \$1,045,959 |
| Construction in Progress | 170,611 | -0- | (-0-) | (170,611) | -0- |
| Building & Improvements | 36,000 | -0- | (-0-) | -0- | 36,000 |
| Water System | 7,059,676 | 94,365 | (-0-) | -0- | 7,154,041 |
| Sewer System | 9,155,572 | 149,953 | (-0-) | (272,398) | 9,033,127 |
| Equipment | 272,764 | 100,434 | (-0-) | -0- | 373,198 |
| Vehicles | 111,232 | 53,106 | (30,199) | -0- | 134,139 |
| Total capital assets | <u>17,408,804</u> | <u>397,857</u> | <u>(30,199)</u> | <u>-0-</u> | <u>17,776,463</u> |
| Less accumulated depreciation: | | | | | |
| Building & Improvements | 18,450 | 1,800 | (-0-) | -0- | 20,250 |
| Water System | 3,248,326 | 269,828 | (-0-) | -0- | 3,518,154 |
| Sewer System | 1,096,438 | 280,509 | (-0-) | -0- | 1,376,947 |
| Equipment | 198,571 | 36,294 | (-0-) | -0- | 234,865 |
| Vehicles | 104,199 | 11,212 | (30,199) | -0- | 85,212 |
| Total accumulated depreciation | <u>4,665,984</u> | <u>599,643</u> | <u>(30,199)</u> | <u>-0-</u> | <u>5,235,428</u> |
| Business-type activities capital assets, net | <u>\$12,742,820</u> | <u>\$(201,786)</u> | <u>\$(-0-)</u> | <u>\$(-0-)</u> | <u>\$12,541,035</u> |

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

| | |
|--|------------------|
| Governmental activities: | |
| General government | \$183,151 |
| Public safety | 228,780 |
| Public works | 32,424 |
| Cultural and recreational | 44,162 |
| Social and welfare | 538 |
| Total depreciation expense – governmental activities | <u>\$489,055</u> |
| Business-type activities: | |
| Water and sewer | <u>\$599,643</u> |

NOTE F – STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY

For the year ended September 30, 2012, revenues exceeded expenditures in the General Fund by \$514,751.

NOTE G – INTERFUND BALANCES AND TRANSFERS – GOVERNMENT WIDE

The composition of interfund operating transfers for the year ended September 30, 2012, is as follows:

| Fund | Transfer to Other Funds | Transfer from Other Funds |
|-----------------------------|----------------------------|------------------------------|
| General Fund | \$40,566 | \$ -0- |
| Debt Service Fund | -0- | 63,329 |
| Nonmajor Governmental Funds | 20,454 | -0- |
| Water and Sewer Fund | 5,290,974 | 5,288,665 |
| | <u>\$5,351,994</u> | <u>\$5,351,994</u> |

The purpose of interfund operating transfers is to appropriately classify capital assets expenditures and debt expenditures in the correct fund. During the fiscal year 2012, a new bond was issued and the proceeds of approximately \$4,973,580, were reclassified from the capital project fund to the water sewer fund (Note H).

NOTE H - LONG TERM DEBT

1. Governmental activities –

Combination Tax and Revenue Certificate of Obligation:

Combination tax and revenue certificate of obligation are serial debt collateralized by the full faith and credit of the City and are payable from property tax and sales tax revenue. The debt matures annually in varying amounts through 2026, and interest is payable semi-annually. Certificates of obligation proceeds are recorded in the appropriate fund for which the debt was issued and approved by the City. The ordinances authorizing the issuance of the bonds created an interest and sinking fund (Debt Service Fund).

Certificates of obligation debt outstanding and Tax anticipation note at September 30, 2012, is comprised of the following:

| <u>Description of Debt</u> | <u>Amount</u> |
|--|---------------|
| \$3,960,000 General Obligation Refunding Bonds, Series 2011, to refinance the City's debt. Principal payments begin in 2012 and are due in annual installments \$210,000 to \$320,000 through August of 2026; interest payments of \$6,400 to \$60,525 from February 2012 through August 2026 with an interest rate of 2% to 4%. | \$3,645,000 |
| Add: Premium on General Obligation Refunding Bonds, Series 2011 | 186,046 |
| Subtotal Certificate of Obligation | 3,831,046 |
| \$1,000,000 2008 Tax Anticipation Note for city improvements, due in annual installments ranging from \$150,000 to \$185,000 beginning August 2010 through August 2015, interest payments ranging from \$4,172 to \$22,550 from February 2009 through August 2015 with interest rate of 4.51% | 535,000 |
| Total Certificate of obligation and tax anticipation | \$4,366,046 |

Annual debt service requirements to maturity for certificates of obligation debt, before netting of bond discounts and premiums are as follows:

| Year Ending September 30 | Principal | Premium | Interest | Total |
|-----------------------------|-------------|-----------|-------------|-------------|
| 2013 | \$ 485,000 | \$8,108 | \$ 138,878 | \$ 631,986 |
| 2014 | 390,000 | 6,953 | 124,912 | 521,865 |
| 2015 | 400,000 | 7,826 | 112,594 | 520,420 |
| 2016 | 220,000 | 6,574 | 99,950 | 326,524 |
| 2017 | 230,000 | 6,574 | 95,550 | 332,124 |
| 2018 – 2022 | 1,255,000 | 68,586 | 317,270 | 1,640,856 |
| 2023 – 2027 | 1,200,000 | 81,425 | 122,600 | 1,404,025 |
| Total | \$4,180,000 | \$186,046 | \$1,011,754 | \$5,377,800 |

Notes Payable:

Note payable debt outstanding at September 30, 2012, is comprised of the following:

| <u>Description of Debt</u> | <u>Amount</u> |
|---|---------------|
| Note payable to a financial institution secured by equipment costing \$86,208 maturing March 2017, requiring annual installments of \$18,754 including interest at 4.39%. | \$ 86,208 |
| Note payable to a financial institution secured by land costing \$116,000 maturing April 2018, requiring monthly installments of \$1,235 including interest at 5% | 70,981 |
| Total | \$157,189 |

Annual debt service requirements to maturity for notes payable debt are as follows:

| Year Ending September 30 | Principal | Interest | Total |
|-----------------------------|------------------|------------------|------------------|
| 2013 | \$ 30,236 | \$ 3,333 | \$ 33,569 |
| 2014 | 27,871 | 5,005 | 32,876 |
| 2015 | 29,191 | 4,379 | 33,570 |
| 2016 | 30,622 | 1,544 | 32,166 |
| 2017 | 32,062 | 789 | 32,851 |
| 2018 - 2022 | 7,207 | 722 | 7,929 |
| Total | <u>\$157,189</u> | <u>\$ 15,722</u> | <u>\$172,961</u> |

Capital Lease:

Capital lease debt outstanding at September 30, 2012, is comprised of the following:

| <u>Description of Debt</u> | <u>Amount</u> |
|--|------------------|
| Capital lease obligation secured by equipment costing \$89,129 maturing July 2014, requiring monthly installments of \$20,016 including interest accruing at 3.99% with a purchase option of \$1 at conclusion of the lease. | \$37,758 |
| Capital lease obligation secured by equipment costing \$160,109 maturing November 2016, requiring monthly installments of \$2,926 including interest accruing at 3.69% | 48,931 |
| Capital lease obligation secured by software costing \$86,968 maturing June 2014, requiring monthly installments of \$1,652 including interest accruing at 4.00% with a purchase option of \$1 at conclusion of the lease | 27,129 |
| Total | <u>\$113,818</u> |

Annual debt service requirements to maturity for capital lease debt are as follows:

| Year Ending September 30 | Principal | Interest | Total |
|-----------------------------|------------------|-----------------|------------------|
| 2013 | \$44,540 | \$6,136 | \$50,676 |
| 2014 | 42,249 | 3,241 | 45,490 |
| 2015 | 11,558 | 733 | 12,291 |
| 2016 | 11,982 | 309 | 12,291 |
| 2017 | 3,489 | 26 | 3,515 |
| Total | <u>\$113,818</u> | <u>\$10,445</u> | <u>\$124,263</u> |

Changes in long-term liabilities:

Long-term debt activity for the year ended September 30, 2012, was as follows:

| | Amounts payable at beginning of year | Amounts added during year 2012 | Amounts retired during fiscal year 2012 | Amounts payable at end of year | Amounts due within one year |
|----------------------------|--------------------------------------|--------------------------------|---|--------------------------------|-----------------------------|
| Certificates of obligation | \$4,155,680 | \$ -0- | \$(324,634) | \$3,831,046 | \$315,000 |
| Tax anticipation notes | 695,000 | -0- | (160,000) | 535,000 | 170,000 |
| Notes payable | 90,672 | 86,209 | (19,692) | 157,189 | 30,236 |
| Capital lease obligation | 97,356 | 56,038 | (39,576) | 113,818 | 44,540 |
| Compensated Absences | 92,523 | 2,191 | (-0-) | 94,714 | 94,714 |
| Total | \$5,131,231 | \$144,438 | \$(543,902) | \$4,731,767 | \$654,490 |

2. Business-type activities -

Combination Tax and Revenue Certificate of Obligation:

Combination tax and revenue certificate of obligation are serial debt collateralized by the full faith and credit of the City and are payable from the gross revenues of the water and sewer system. Gross revenues are to be used first to pay operating and maintenance expenses of the system, and second, to maintain revenue bond funds in accordance with the bond covenants. Remaining revenues may then be used for any lawful purpose. The debt matures annually in varying amounts through 2045, and interest is payable semi-annually. Certificates of obligation proceeds are recorded in the appropriate fund for which the debt was issued and approved by the City. The ordinances authorizing the issuance of the bonds created an interest and sinking fund.

Certificates of obligation debt outstanding at September 30, 2012, is comprised of the following:

| <u>Description of Debt</u> | <u>Amount</u> |
|---|---------------|
| \$2,200,000 Combination Tax Revenue Certificate of Obligation Series 2008B for construction of the waste water treatment plant due in annual installments ranging from \$35,000 to \$195,000, beginning September 2008 through 2022, interest payments ranging from \$7,605 to \$28,123 from September 2008 through 2022 with interest rate at 3.9% | \$1,655,000 |
| \$2,346,000 Combination Tax Revenue Certificate of Obligation Series 2008A for construction of the waste water treatment plant due in annual installments ranging from \$12,000 to \$122,000 beginning September 2008 through 2047, interest payments ranging from \$5,490 to \$105,030 from September 2008 through 2022 with interest rate at 4.5% | 2,236,000 |
| \$4,810,000 Combination Tax Revenue Certificate of Obligation Series 2012 for improvements to the waste water treatment plant, sewer, and water improvements due in annual installments ranging from \$135,000 to \$330,000 beginning August 2014 through 2037, interest payments ranging from \$6,600 to \$76,482 from February 2013 through 2037 with interest rate ranging from 2% to 4% | 4,810,000 |
| Subtotal | \$8,701,000 |
| Add: Net premiums and discounts on certificates of obligations | 149,160 |
| Total | \$8,850,160 |

Annual debt service requirements to maturity for certificates of obligation debt, before netting of bond discounts and premiums, are as follows:

| Year Ending September 30 | Principal | Premiums (Discounts) | Interest | Total |
|-----------------------------|-------------|-------------------------|-------------|--------------|
| 2013 | \$ 167,000 | \$ 4,840 | \$ 318,129 | \$ 489,969 |
| 2014 | 309,000 | 4,840 | 311,455 | 625,295 |
| 2015 | 320,000 | 4,840 | 301,793 | 626,633 |
| 2016 | 316,000 | 4,840 | 291,793 | 612,633 |
| 2017 | 318,000 | 4,840 | 281,755 | 604,595 |
| 2018 – 2022 | 1,747,000 | 24,200 | 1,247,329 | 3,018,529 |
| 2023 – 2027 | 1,040,000 | 24,200 | 1,007,028 | 2,071,228 |
| 2028 – 2032 | 1,581,000 | 19,140 | 732,863 | 2,333,003 |
| 2033 – 2037 | 1,892,000 | 19,140 | 461,457 | 2,372,597 |
| 2038 – 2042 | 450,000 | 19,140 | 188,780 | 657,920 |
| 2043 – 2047 | 561,000 | 19,140 | 77,898 | 658,038 |
| Total | \$8,701,000 | 149,160 | \$5,220,280 | \$14,070,440 |

Changes in long-term liabilities:

Long-term debt activity for the year ended September 30, 2012, was as follows:

| | Amounts payable at beginning of year | Amounts added during year 2012 | Amounts retired during fiscal year 2012 | Amounts payable at end of year | Amounts due within one year |
|----------------------------|--------------------------------------|--------------------------------|---|--------------------------------|-----------------------------|
| Certificates of Obligation | \$4,037,815 | \$4,973,580 | \$(161,235) | \$8,850,160 | \$167,000 |
| Capital Lease | 9,806 | 103,369 | (17,670) | 95,505 | 23,554 |
| Compensated Absences | 15,952 | 4,089 | (-0-) | 20,041 | 20,041 |
| Total | \$4,063,573 | \$5,081,038 | \$(178,905) | \$8,965,706 | \$210,595 |

NOTE I – RESTRICTED ASSETS

Restricted assets balance at September 30, 2012, was as follows:

| Fund | Cash & Deposits | Investments | Intergovernmental Receivable |
|-------------------------------|--------------------|------------------|------------------------------|
| Government Activities: | | | |
| Court | \$-0- | \$115,139 | \$-0- |
| Animal Shelter | -0- | -0- | 25 |
| Debt Service Fund | -0- | 336,529 | -0- |
| Water and Sewer Fund | 4,920,154 | 73,389 | -0- |
| | \$4,920,154 | \$525,057 | \$25 |

NOTE J - RETIREMENT PLAN

The City participates in the Texas Municipal Retirement System.

Plan Description

The City provides pension benefits for all of its eligible employees through a non-traditional, joint contributory, hybrid defined benefit plan in the state-wide Texas Municipal Retirement System (TMRS), one of the 827 administered by the 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.

Benefits depend upon the sum of the employee's contributions to the plan, with interest, and the City-financed monetary credits, with interest. At the date the plan began, the City granted monetary credits for service rendered before the plan began of a theoretical amount equal to two times what would have been contributed by the employee, with interest, prior to establishment of

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

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 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 the 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 and with the actuarial constraints also in the statutes. Plan provisions for the City were as follows (as of 5/17/2012):

| | |
|--|---------|
| Deposit Rate: | 6% |
| Matching Ratio (city to Employee) | 2 to 1 |
| A member is vested after | 5 years |
| Members can retire at certain ages, based on the years of service with the City. The Service Retirement Eligibilities for the City are: 5yrs/age 60, 20 yrs/any age. | |

Contributions

Under the state law governing TMRS, the contribution rate for the 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, both of which are 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. currently accruing monetary credits due to the City matching percent, which are the obligation of the City as of an employee's retirement date, not at the time the employee's contributions are made. The normal cost contribution rate is the actuarially determined percent of payroll necessary to satisfy the obligation of the City to each employee at the time his/her retirement becomes effective. The prior service contribution rate amortizes the unfunded (overfunded) actuarial liability (asset) over the remainder of the plan's 25-year amortization period. The Projected Unit Credit actuarial cost method is used for determining the City contribution rate. Both the employees and the City make contributions monthly. Since the

City needs to know its contribution rate in advance 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 (i.e. December 31, 2011 valuation is effective for rates beginning January 2012).

| | | | |
|---|-----------------|-----------------|-----------------|
| Actuarial Valuation Date | <u>12/31/11</u> | <u>12/31/10</u> | <u>12/31/09</u> |
| Actuarial Value of Assets | \$1,450,132 | \$1,225,240 | \$915,288 |
| Actuarial Accrued Liability | \$1,649,968 | \$1,486,668 | \$1,232,819 |
| Percentage Funded | 87.9% | 82.4% | 74.2% |
| Unfunded Actuarial Accrued Liability (UAAL) | \$199,836 | \$261,428 | \$317,531 |
| Annual Covered Payroll | \$2,165,476 | \$2,133,755 | \$2,121,347 |
| UAAL as a Percentage of Covered Payroll | 9.2% | 12.3% | 15.0% |
| Net Pension Obligation (NPO) at the Beginning of the Period | -0- | -0- | -0- |
| Annual Pension Cost: | | | |
| Annual required contribution (ARC) | \$103,726 | \$100,287 | \$102,036 |
| Contributions Made | (103,726) | (100,287) | (102,036) |
| NPO at the end of the period | <u>\$0</u> | <u>\$0</u> | <u>\$0</u> |

Actuarial Assumptions

| | | | |
|--|---------------------------|---------------------------|---------------------------|
| Valuation Date | 12/31/2011 | 12/31/2010 | 12/31/2009 |
| Actuarial Cost Method | Projected Unit Credit | Projected Unit Credit | Projected Unit Credit |
| Amortization Method | Level Percent of Payroll | Level Percent of Payroll | Level Percent of Payroll |
| GASB 25 Equivalent Single Amortization Period | 20.6 years; closed period | 21.9 years; closed period | 23.1 years; closed period |
| Amortization Period for new Gains/Losses | 25 years | 25 years | 25 years |
| Asset Valuation Method | 10-year Smoothed Market | 10-year Smoothed Market | 10-year Smoothed Market |
| Investment Rate of Return | 7.0% | 7.0% | 7.5% |
| Projected Salary Increased | Varies by Age and Service | Varies by Age and Service | Varies by Age and Service |
| Includes Inflation At Cost-of-Living Adjustments | 3.0% | 3.0% | 3.0% |
| Payroll Growth Assumption | None | None | None |
| Withdrawal rates for Male/Female | 3.0% | 3.0% | 3.0% |
| | Mid/Mid-Low | Mid/Mid-Low | Mid/Mid-Low |

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

NOTE K - COMMITMENTS AND CONTINGENCIES

Audits of Grant Activities

The City receives Federal and State grants for specific purposes that are subject to review and audit by Federal and State agencies. Such audits could result in a request for reimbursement by the Federal and State grantor agencies for expenditures disallowed under the terms and conditions of the appropriate agency. In the opinion of the City management, such disallowances, if any, will not be significant.

The City contracts with various engineering and construction companies to oversee significant construction projects. At September 30, 2012 the City was contracted with Dannebaum Engineering to oversee the EPA grant project that was still ongoing at year-end.

NOTE L – RISK MANAGEMENT

The City manages its risk through the purchasing of insurance policies through the Texas Municipal League. Significant losses are covered by commercial insurance for all major programs. For such insured programs, there have been no significant reductions in insurance coverage, and settlement amounts have not exceeded insurance coverage for the current year or three prior years.

NOTE O – SUBSEQUENT EVENTS

The City evaluated subsequent events through January 31, 2013, which is the same date that the financial statements were issued and no events were determined to be reported.

REQUIRED SUPPLEMENTAL INFORMATION

CITY OF ALVARADO, TEXAS
SCHEDULE OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES - BUDGET AND ACTUAL
GENERAL FUND
For the Fiscal Year Ended September 30, 2012

| | Budgeted Amounts | | | Actual Amounts | Variance with Final Budget - Positive (Negative) |
|---|------------------|-----------|-----------|----------------|---|
| | Original | Amended | Final | | |
| REVENUE: | | | | | |
| General Property Taxes, Interest and Penalties | \$765,176 | \$765,176 | \$765,176 | \$757,783 | (\$7,393) |
| Sales tax | 818,500 | 828,500 | 828,500 | 1,010,435 | 181,935 |
| Fines and forfeitures | 650,000 | 650,000 | 650,000 | 587,681 | (62,319) |
| Franchise fees & rental fees | 378,150 | 384,678 | 384,678 | 385,146 | 468 |
| Rental fees | 32,600 | 32,600 | 32,600 | 39,295 | 6,695 |
| Licenses, fees and permits | 73,400 | 104,800 | 104,800 | 105,215 | 415 |
| Interest | 2,000 | 2,000 | 2,000 | 1,712 | (288) |
| Intergovernmental | 287,120 | 287,327 | 287,327 | 321,766 | 34,439 |
| Donations | 500 | 500 | 500 | 200 | (300) |
| Water/Sewer administrative fee | 174,401 | 174,401 | 174,401 | 174,401 | - |
| Miscellaneous | 32,650 | 60,250 | 60,250 | 215,417 | 155,167 |
| Total Revenue | 3,214,497 | 3,290,232 | 3,290,232 | 3,599,051 | 308,819 |
| EXPENDITURES: | | | | | |
| Current operating | | | | | |
| General government | 389,821 | 413,490 | 413,490 | 389,255 | 24,235 |
| Public safety | 2,203,667 | 2,241,139 | 2,241,139 | 2,113,560 | 127,579 |
| Public works | 116,084 | 126,540 | 126,540 | 104,701 | 21,839 |
| Cultural and recreational | 247,695 | 247,880 | 247,880 | 231,185 | 16,695 |
| Community development | 195,003 | 199,076 | 199,076 | 186,017 | 13,059 |
| Social and welfare | 62,227 | 62,107 | 62,107 | 44,882 | 17,225 |
| Other | - | - | - | - | - |
| Capital Outlay | - | - | - | 14,700 | (14,700) |
| Total Expenditures | 3,214,497 | 3,290,232 | 3,290,232 | 3,084,300 | 205,932 |
| Excess (Deficiency) of Revenues Over (Under) Expenditures | - | - | - | 514,751 | 514,751 |
| OTHER FINANCING SOURCES: | | | | | |
| Loan proceeds | - | - | - | - | - |
| Transfers | - | - | - | (40,566) | (40,566) |
| NET CHANGE IN FUND BALANCES | - | - | - | 474,185 | 474,185 |
| FUND BALANCE - October 1, 2011 | 338,806 | 338,806 | 338,806 | 338,806 | - |
| FUND BALANCE - September 30, 2012 | \$338,806 | \$338,806 | \$338,806 | \$812,991 | \$474,185 |

CITY OF ALVARADO, TEXAS
NOTES TO REQUIRED SUPPLEMENTARY INFORMATION
SEPTEMBER 30, 2012

NOTE A – STEWARDSHIP, COMPLIANCE, AND ACCOUNTABILITY

1. Budgetary Information

The City Council adopts an annual budget prepared in accordance with GAAP. The City Manager may transfer part or all of any unencumbered appropriation balance among programs within a specific fund; however, any revisions that alter the total expenditures of the fund must be approved by the City Council. The City, for management purposes, adopts budgets for all funds. Legal budgets are also adopted for all funds and the legal level of control is the fund level.

Capital Projects are funded through the issuance of general obligation debt authorized for a specific purpose.

All unused appropriations, except appropriations for capital expenditures, lapse at the close of the fiscal year to the extent they have not been expended or encumbered. An appropriation for capital expenditures shall continue in force until the purpose for which it was made has been accomplished or abandoned if three (3) years pass without any disbursement from or encumbrance of the appropriation. No supplemental budgetary appropriations occurred in the debt service funds or in the general fund. The revised budgets are used for budget versus actual comparisons. Revenues in the general fund were more than budget by \$308,819 and expenditures were less than budget by \$205,932.

2. Reconciliation of Budgetary Information to GAAP Information

Because the City budgets debt expenditures in the Debt Service Fund they are not included in the general fund budget versus actual schedule. Such debt service payments amounted to \$695,181.

The City generally budgets capital outlays in the department with which they are associated, whereas for actual financial statement purposes they are all grouped on a separate line. Amounts budgeted for the general fund amounted to \$0. The total actual capital outlays for the year in the general fund amounted to \$14,700.

NOTE B – RETIREMENT PLAN

**Texas Municipal Retirement System
Schedule of Funding Progress**

| | (1) | (2) | (3) | (4) | (5) | (6) |
|---|---------------------------------|--|---------------------------------|----------------------------|------------------------------|---|
| Actuarial Valuation Date December 31, | Actuarial Value of Assets | Actuarial Accrued Liability (AAL) | Percentage Funded (1)/(2) | Unfunded AAL (2)-(1) | Annual Covered Payroll | Unfunded AAL as a Percentage of Covered Payroll (4)/(5) |
| 2005 | \$245,772 | \$439,312 | 55.9% | \$193,540 | \$1,381,916 | 14.0% |
| 2006 | 371,088 | 571,329 | 65.0% | 200,241 | 1,519,196 | 13.2% |
| 2007 | 508,434 | 738,497 | 68.8% | 230,063 | 1,715,098 | 13.4% |
| 2008 | 733,422 | 1,017,621 | 72.1% | 284,199 | 1,928,937 | 14.7% |
| 2009 | 915,288 | 1,232,819 | 74.2% | 317,531 | 2,121,347 | 15.0% |
| 2010 | 1,225,240 | 1,486,668 | 82.4% | 261,428 | 2,133,755 | 12.3% |
| 2011 | 1,450,132 | 1,649,968 | 87.9% | 199,836 | 2,165,476 | 9.2% |

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 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 the TMRS website at www.tmr.com

**Texas Municipal Retirement System
Schedule of Employer Contributions**

| Fiscal Year Ended | TMRS – Annual Required Contribution | Percentage of TMRS Contributed |
|-------------------|--|-----------------------------------|
| 9/30/2011 | \$103,726 | 100% |
| 9/30/2010 | 100,287 | 100% |
| 9/30/2009 | 102,036 | 100% |
| 9/30/2008 | 107,183 | 100% |
| 9/30/2007 | 57,001 | 100% |
| 9/30/2006 | 51,459 | 100% |
| 9/30/2005 | 48,579 | 100% |

SUPPLEMENTAL REPORT



**INDEPENDENT AUDITOR'S 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 Mayor, and City Council
City of Alvarado, Texas

We have audited the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of City of Alvarado, Texas as of and for the year ended September 30, 2012, which collectively comprise the City of Alvarado, Texas' basic financial statements and have issued our report thereon dated January 31, 2013. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to the financial audit contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

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

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

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in the internal control over financial reporting that might be deficiencies, significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above. However, as described below, we identified certain deficiencies in internal control over financial reporting that we consider to be significant deficiencies. A significant deficiency is a deficiency, or 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.

Closing procedures

A good system of internal control provides for a timely and accurate closing of financial statements during for interim and year-end periods. The City's finance department has only one employee who is responsible for not only the daily financial activities, but also to perform the closing procedures. Closings should include recording fixed assets and long-term debt transactions that occur during the period. These transactions are currently not being recorded in a timely manner.

Certified Public Accountants

By adopting closing procedures, the City's internal controls over financial reporting will improve and reduce the possibility of irregularities not being prevented or detected in a timely manner. We recommend that management review the current process for closing the financial statements and prepare a set of formal closing procedures that includes fixed assets and debt transactions incurred during the period.

Between the end of the fiscal year, September 30, 2012 and the issuance of the audit report, we determined that the city has taken steps to improve their closing procedures. The City Finance Director continues to take a proactive approach in improving her skills and knowledge as to the closing procedures for long-term debt and fixed assets. We have reviewed our audit adjustments related to fixed assets and debt transactions with the Finance Director and she is prepared to make the entries going forward.

Compliance and Other Matters

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

This report is intended solely for the information and use of the City Council, management, others within the organization, 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.



Waters, Vollmering & Associates, LLP
Mansfield, Texas
January 31, 2013