

CITY OF ELKHART, TEXAS
AUDITED FINANCIAL STATEMENTS
SEPTEMBER 30, 2012

CITY OF ELKHART, TEXAS

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**CITY OF ELKHART, TEXAS
PRINCIPAL CITY OFFICIALS
SEPTEMBER 30, 2012**

Honorable Raymond DunlapMayor
Randy McCoyMayor Pro Tem
Karen Bridges Councilmember
Lucia Butler Councilmember
Doug Smith Councilmember
Erroll Tatum..... Councilmember
Donna Surber City Secretary

Todd, Hamaker & Johnson, LLP

CERTIFIED PUBLIC ACCOUNTANTS

420 S 1st Street • PO Box 468 • Lufkin, TX 75902-0468 • (936) 632-8181
301 N 6th Street • PO Box 1249 • Crockett, TX 75835-1249 • (936) 544-2143

Melvin R. Todd, CPA
Daren Hamaker, CPA
Kim Johnson, CPA
Rachel Kennerly, CPA

INDEPENDENT AUDITORS' REPORT

Honorable Mayor and City Council
City of Elkhart, Texas

We have audited the accompanying financial statements of the governmental activities, the business-type activities and each major fund of the City of Elkhart, Texas, (the City) as of and for the year ended September 30, 2012, which collectively comprise the City's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the City's management. Our responsibility is to express an opinion on these basic 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 opinion.

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 and each major fund of the City of Elkhart, Texas as of September 30, 2012, and the respective changes in financial position and cash flows, where applicable, thereof for the year ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated March 29, 2013, on our consideration of the City's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis, budgetary comparison information, and schedule of funding progress – pension plan on pages 5 through 10 and pages 36 through 37, respectively, 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 operations, 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

INDEPENDENT AUDITORS' REPORT – CONTINUED

of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Todd, Hamaker & Johnson, LLP

Todd, Hamaker & Johnson, LLP
Lufkin, Texas

March 29, 2013

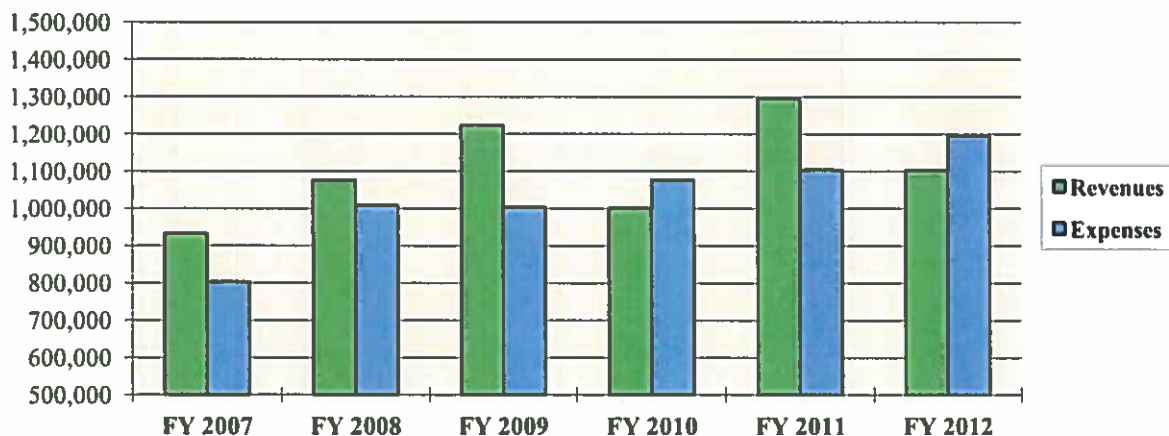
**CITY OF ELKHART, TEXAS
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED SEPTEMBER 30, 2012
(UNAUDITED)**

As management of City of Elkhart, Texas (the City), we offer readers of the City's financial statements this narrative overview and analysis of the financial activities of the City for the fiscal year ended September 30, 2012. We encourage readers to consider information presented here as well as the City's financial statements, which follow this section.

FINANCIAL HIGHLIGHTS

- The overall assets of the City decreased by \$135,662 during the fiscal year. Cash and other current assets decreased by \$80,426; capital assets decreased by \$55,236.
- The City's total long-term debt obligations decreased by \$35,514 during the current fiscal year. Total debt outstanding at year end was \$900,516; \$840,000 in bond obligations and \$60,516 in capital lease obligations. In April, 2012 the City entered into a five-year capital lease agreement in the amount of \$65,667 for the purchase of a backhoe.
- The City's overall assets exceeded its total liabilities by \$1,553,419 (*net assets*) at September 30, 2012. Of this amount, \$299,562 (*unrestricted net assets*) may be used to meet the on-going obligations to citizens and creditors.
- Excluding grant revenues received, overall revenues increased by \$41,469 from the prior year. Increases in utility revenue accounted for the bulk of this increase.
- Overall expenses increased by \$92,191 from the prior year. Personnel and related expenses, as well as increases in street repairs and maintenance, were the two largest contributors to this increase.
- Overall expenses exceeded revenues (or a decrease in net assets) by \$92,833. Net assets increased by \$17,230 in the governmental fund and decreased by \$110,063 in the proprietary fund.

**Total Revenues and Expenses
Governmental and Business-Type Activities**



**CITY OF ELKHART, TEXAS
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED SEPTEMBER 30, 2012
(UNAUDITED)**

OVERVIEW OF THE FINANCIAL STATEMENTS

This discussion and analysis is intended to serve as an introduction to the City's basic financial statements. The City's basic financial statements are comprised of three components: (1) government-wide financial statements, (2) fund financial statements, and (3) notes to the financial statements.

Government-wide Financial Statements. The *government-wide financial statements*, which begin on page 12 of this report, are designed to provide readers with a broad overview of the City's finances, in a manner similar to a private-sector business.

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

The *statement of activities* presents information showing how the City's net assets changed during the fiscal year. Revenues are recorded when earned and expenses are recorded when the liability is incurred, regardless of the timing of related cash flows.

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

Governmental Funds 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 *balances of spendable resources* available at the end of the fiscal year. Revenues are recognized when they are both measurable and available. Expenditures are recorded when the related fund liability is incurred, except for general obligation bond principal and interest, which are reported as expenditures in the year due.

Proprietary Funds are used to report the same functions presented as *business-type* activities in the government-wide financial statements. The City uses a proprietary fund to account for the operations of the water, sewer and garbage collections systems that are financed and operated in a manner similar to private business enterprises -- where the intent of the governing body is that the cost (expenses, including depreciation) of providing goods and services to the general public on a continuing basis are to be financed or recovered primarily through user charges. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows.

The basic governmental and proprietary fund financial statements can be found on pages 15 - 20 of this report.

Notes to the Financial Statements. The notes provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements. The notes to the financial statements can be found on pages 22 - 34 of this report.

THE CITY'S NET ASSETS

Over time, net assets may serve as a useful indicator of a government's financial position. At September 30, 2012, the City's assets exceeded its liabilities by \$1,553,419.

**CITY OF ELKHART, TEXAS
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED SEPTEMBER 30, 2012
(UNAUDITED)**

The City has a large investment in capital assets (e.g., land, buildings, equipment, and construction in progress) and related debt used to acquire those assets that remains outstanding. The City uses these capital assets to provide service to citizens; consequently, these assets are not available for future spending. Although the City's investment in its capital assets is reported net of related debt, it should be noted that the resources needed to repay this debt must be provided from other sources, since the capital assets themselves cannot be used to liquidate these liabilities. Net assets invested in capital assets, net of related debt, totaled \$1,128,912 at September 30, 2012.

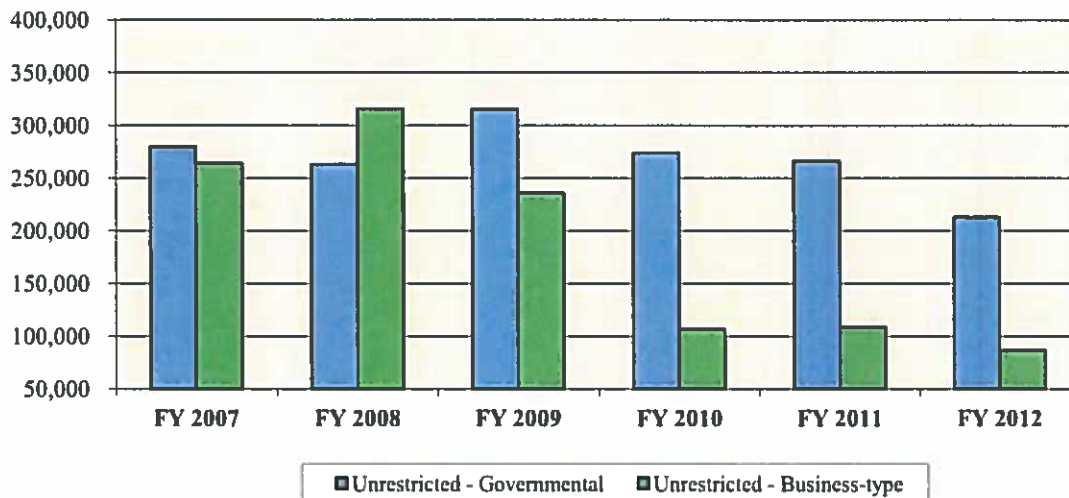
An additional portion of the City's net assets, \$124,945, represents resources that are subject to external restriction on how they may be used. The remaining balance is \$299,562 and unrestricted in nature.

During the year, expenses exceeded revenues (or a decrease in net assets) by \$92,833.

The City's Net Assets

	Governmental Activities		Business-type Activities		Total	
	2012	2011	2012	2011	2012	2011
Current and other assets	\$ 349,152	\$ 401,388	\$ 213,620	\$ 241,810	\$ 562,772	\$ 643,198
Capital assets	97,608	74,317	1,931,820	2,010,347	2,029,428	2,084,664
Total assets	446,760	475,705	2,145,440	2,252,157	2,592,200	2,727,862
Long-term liabilities	740,000	784,510	160,516	151,520	900,516	936,030
Other liabilities	11,215	12,880	127,050	132,700	138,265	145,580
Total liabilities	751,215	797,390	287,566	284,220	1,038,781	1,081,610
Net assets						
Invested in capital assets, net of related debt	(642,392)	(710,193)	1,771,304	1,858,827	1,128,912	1,148,634
Restricted	124,945	122,035	-	-	124,945	122,035
Unrestricted	212,992	266,473	86,570	109,110	299,562	375,583
Total net assets	\$ (304,455)	\$ (321,685)	\$ 1,857,874	\$ 1,967,937	\$ 1,553,419	\$ 1,646,252

**Unrestricted Net Assets
Governmental and Business-Type Activities**

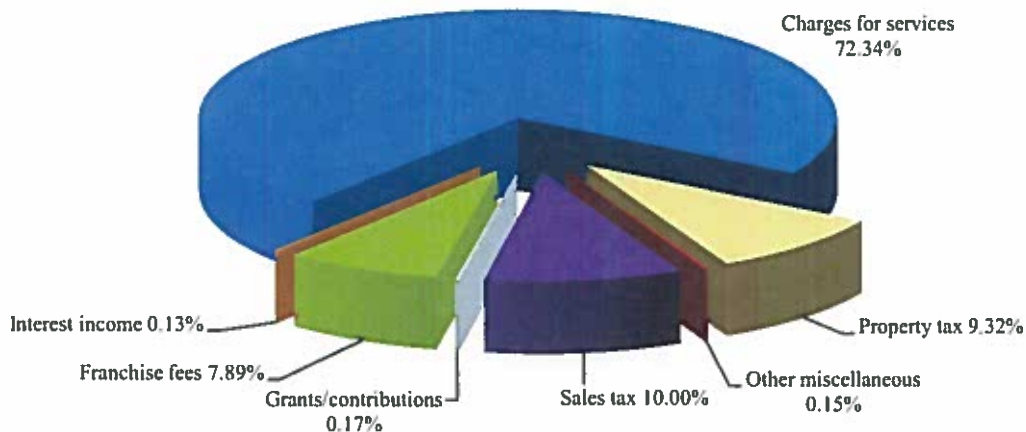


**CITY OF ELKHART, TEXAS
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED SEPTEMBER 30, 2012
(UNAUDITED)**

Change in Net Assets

	<u>Governmental Activities</u>		<u>Business-type Activities</u>		<u>Total</u>	
	<u>2012</u>	<u>2011</u>	<u>2012</u>	<u>2011</u>	<u>2012</u>	<u>2011</u>
Revenues						
Charges for services	\$ -	\$ -	\$ 798,580	\$ 764,075	\$ 798,580	\$ 764,075
Property taxes	102,877	85,426	-	-	102,877	85,426
Sales taxes	110,339	103,856	-	-	110,339	103,856
Franchise fees	87,058	81,762	-	-	87,058	81,762
Interest income	1,371	2,782	40	287	1,411	3,069
Grants and contributions	1,920	-	-	234,894	1,920	234,894
Other miscellaneous	1,690	18,492	-	3,806	1,690	22,298
Total revenues	305,255	292,318	798,620	1,003,062	1,103,875	1,295,380
Expenses						
General government	207,672	218,865	-	-	207,672	218,865
Streets and drainage	108,297	76,266	-	-	108,297	76,266
Fire protection	9,233	-	-	-	9,233	-
Municipal court	2,329	-	-	-	2,329	-
Water, sewer, sanitation	-	-	649,136	606,769	649,136	606,769
Depreciation	7,191	3,532	170,817	152,691	178,008	156,223
Interest on long-term debt	33,990	36,164	8,043	10,230	42,033	46,394
Total expenses	368,712	334,827	827,996	769,690	1,196,708	1,104,517
Transfers						
In (out)	80,687	74,281	(80,687)	(74,281)	-	-
Total transfers	80,687	74,281	(80,687)	(74,281)	-	-
Increase (decrease) in net assets	17,230	31,772	(110,063)	159,091	(92,833)	190,863
Net assets at beginning of year	(321,685)	(353,457)	1,967,937	1,808,846	1,646,252	1,455,389
Net assets at end of year	<u>\$ (304,455)</u>	<u>\$ (321,685)</u>	<u>\$ 1,857,874</u>	<u>\$ 1,967,937</u>	<u>\$ 1,553,419</u>	<u>\$ 1,646,252</u>

**Revenue by Major Category
Governmental and Business-Type Activities
For the Fiscal Year Ended September 30, 2012**



**CITY OF ELKHART, TEXAS
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED SEPTEMBER 30, 2012
(UNAUDITED)**

FINANCIAL ANALYSIS OF THE GOVERNMENT'S FUNDS

As noted earlier, the City uses fund accounting to ensure and demonstrate compliance with finance related 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 balances may serve as a useful measure of a government's net resources available for spending at the end of the fiscal year.

As of September 30, 2012, the City's governmental funds reported a total fund balance of \$341,987. This fund balance is comprised of \$124,945 that is restricted for payment of debt service and \$1,624 that is assigned for street repair/construction. The remaining balance, \$215,418, is unassigned. During the year, the fund balance in the City's governmental funds decreased by \$50,945.

General Fund Budget. A comparison of the general fund budget and actual results is presented as required supplementary information on page 36. Actual revenues were higher than budgeted amounts by \$2,066. Actual expenses exceeded budgeted amounts by \$62,299. The General fund balance decreased by \$53,855 during the fiscal year; an increase of \$25,530 in fund balance was budgeted.

CAPITAL ASSETS

The City's investment in capital assets as of September 30, 2012, totaled \$2,029,428 (net of accumulated depreciation). This investment includes land, buildings and improvements, streets and drainage, equipment, and construction work in progress.

Capital assets of \$128,010 were purchased during the year. Significant purchases included:

- Backhoe
- Heat pump for the VFD
- 2012 Dodge truck
- Fencing around various wells
- Construction of a pavilion at the park (in progress at year end)

Capital Assets (Net of Depreciation)

	Governmental Activities		Business-type Activities		Total	
	2012	2011	2012	2011	2012	2011
Land	\$ 2,350	\$ 2,350	\$ 61,203	\$ 61,203	\$ 63,553	\$ 63,553
Buildings and improvements	48,008	44,691	-	-	48,008	44,691
Plant and equipment	-	-	1,520,852	1,636,578	1,520,852	1,636,578
Machinery and equipment	12,251	13,799	322,361	284,542	334,612	298,341
Transportation equipment	-	-	22,411	21,222	22,411	21,222
Office equipment & furniture	17,340	13,477	4,992	6,801	22,332	20,278
Streets and drainage	-	-	-	-	-	-
Construction in progress	17,660	-	-	-	17,660	-
Total net assets	<u>\$ 97,609</u>	<u>\$ 74,317</u>	<u>\$ 1,931,819</u>	<u>\$ 2,010,346</u>	<u>\$ 2,029,428</u>	<u>\$ 2,084,663</u>

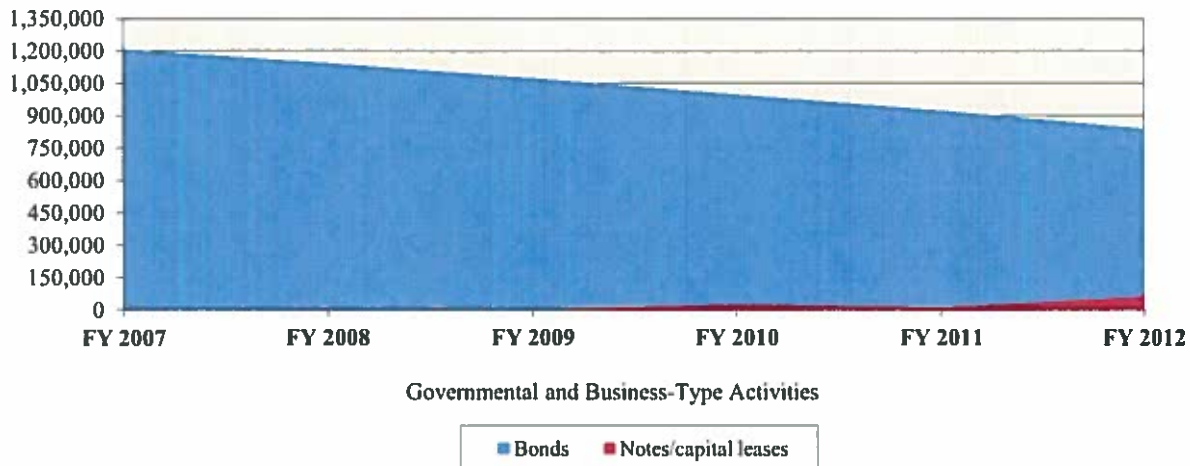
**CITY OF ELKHART, TEXAS
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED SEPTEMBER 30, 2012
(UNAUDITED)**

DEBT ADMINISTRATION

At the end of the current fiscal year, the City had total debt outstanding of \$900,516.

Debt Outstanding

	<u>Governmental Activities</u>		<u>Business-type Activities</u>		<u>Total</u>	
	2012	2011	2012	2011	2012	2011
Notes payable	\$ -	\$ 4,510	\$ -	\$ 6,520	\$ -	\$ 11,030
Capital lease obligations	60,516	-	-	-	60,516	-
Bonds payable	740,000	780,000	100,000	145,000	840,000	925,000
Total	\$ 800,516	\$ 784,510	\$ 100,000	\$ 151,520	\$ 900,516	\$ 936,030



ECONOMIC FACTORS AND NEXT YEAR'S BUDGET AND RATES

In August, 2012, the Council approved the 2012/2013 budget. The City adopted a property tax rate of .302123 per \$100, a reduction from the prior year. No increases in utility rates were projected. With slight variances, the overall revenues and expenses of the City were budgeted to remain at prior year levels.

REQUESTS FOR INFORMATION

This financial report is designed to provide our citizens, taxpayers, customers, investors and creditors with a general overview of the City's finances and to show the City's accountability for the money it receives. If you have any questions about this report or need additional information, contact the City office at 110 W. Parker, Elkhart, Texas.

GOVERNMENT-WIDE FINANCIAL STATEMENTS

CITY OF ELKHART, TEXAS
STATEMENT OF NET ASSETS
SEPTEMBER 30, 2012

	Primary Government		
	Governmental Activities	Business-type Activities	Total
ASSETS			
Cash and cash equivalents	\$ 212,418	\$ 80,489	\$ 292,907
Receivables, net of allowance for uncollectibles			
Customers	-	93,755	93,755
Property taxes	-	-	-
Sales taxes	8,121	-	8,121
Due from other governments	-	-	-
Inventory	-	40,424	40,424
Internal balances	3,668	(3,668)	-
Restricted assets			
Cash and cash equivalents	124,945	-	124,945
Capital assets			
Land	20,010	61,203	81,213
Capital assets, being depreciated	247,469	4,284,134	4,531,603
Accumulated depreciation	(169,871)	(2,413,517)	(2,583,388)
Bond issue costs, net of accumulated amortization	-	2,620	2,620
TOTAL ASSETS	446,760	2,145,440	2,592,200
LIABILITIES			
Accounts payable	7,165	24,825	31,990
Accrued interest	4,050	625	4,675
Customer deposits payable	-	89,469	89,469
Deferred revenue	-	12,131	12,131
Noncurrent liabilities			
Due within one year	40,000	62,602	102,602
Due in more than one year	700,000	97,914	797,914
TOTAL LIABILITIES	751,215	287,566	1,038,781
NET ASSETS			
Invested in capital assets, net of related debt	(642,392)	1,771,304	1,128,912
Restricted for debt service	124,945	-	124,945
Unrestricted	212,992	86,570	299,562
TOTAL NET ASSETS	\$ (304,455)	\$ 1,857,874	\$ 1,553,419

See accompanying notes to financial statements.

CITY OF ELKHART, TEXAS
STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED SEPTEMBER 30, 2012

Functions/Programs	Program Revenues			Net (Expenses) Revenues and Changes in Net Assets			
	Expenses	Fees, Fines, Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	Changes in Net Assets		
					Governmental Activities	Primary Government Business-type Activities	Total
Primary government							
Governmental activities							
General government	\$ 214,863	\$ -	\$ 1,920	\$ -	\$ (212,943)	\$ -	\$ (212,943)
Streets and drainage	108,297	-	-	-	(108,297)	-	(108,297)
Fire protection	9,233	-	-	-	(9,233)	-	(9,233)
Municipal court	2,329	-	-	-	(2,329)	-	(2,329)
Interest on long-term debt	33,990	-	-	-	(33,990)	-	(33,990)
Total governmental activities	368,712	-	1,920	-	(366,792)	-	(366,792)
Business-type activities							
Water, sewer, garbage	819,953	798,580	-	-	-	(21,373)	(21,373)
Interest on long-term debt	8,043	-	-	-	-	(8,043)	(8,043)
Total business-type activities	827,996	798,580	-	-	-	(29,416)	(29,416)
Total primary government	\$ 1,196,708	\$ 798,580	\$ 1,920	\$ -	(366,792)	(29,416)	(396,208)
General revenues							
Property taxes					102,877	-	102,877
Sales taxes					110,339	-	110,339
Franchise taxes					87,058	-	87,058
Investment income					1,371	40	1,411
Miscellaneous income					1,690	-	1,690
Transfers					80,687	(80,687)	-
Total general revenues and transfers					384,022	(80,647)	303,375
Change in net assets					17,230	(110,063)	(92,833)
Net assets - beginning					(321,685)	1,967,937	1,646,252
Net assets - ending					\$ (304,455)	\$ 1,857,874	\$ 1,553,419

See accompanying notes to financial statements.

FUND FINANCIAL STATEMENTS

**CITY OF ELKHART, TEXAS
BALANCE SHEET
GOVERNMENTAL FUNDS
SEPTEMBER 30, 2012**

	<u>General</u>	<u>Debt Service</u>	<u>Special Revenue</u>	<u>Total</u>
ASSETS				
Cash and cash equivalents	\$ 212,418	\$ -	\$ -	\$ 212,418
Receivables, net of allowance for uncollectibles				
Property taxes	-	-	-	-
Sales taxes	6,497	-	1,624	8,121
Due from other funds	3,668	-	-	3,668
Restricted assets				
Cash and cash equivalents	-	124,945	-	124,945
TOTAL ASSETS	<u>\$ 222,583</u>	<u>\$ 124,945</u>	<u>\$ 1,624</u>	<u>\$ 349,152</u>
LIABILITIES				
Accounts payable	\$ 7,165	\$ -	\$ -	\$ 7,165
Accrued expenses	-	-	-	-
Deferred revenue	-	-	-	-
Total liabilities	<u>7,165</u>	<u>-</u>	<u>-</u>	<u>7,165</u>
FUND BALANCE				
Restricted	-	124,945	-	124,945
Assigned	-	-	1,624	1,624
Unassigned	215,418	-	-	215,418
Total fund balance	<u>215,418</u>	<u>124,945</u>	<u>1,624</u>	<u>341,987</u>
TOTAL LIABILITIES AND FUND BALANCES	<u>\$ 222,583</u>	<u>\$ 124,945</u>	<u>\$ 1,624</u>	

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

Capital assets used in governmental activities are not financial resources and therefore, are not reported in the fund	97,608
Other assets are not available to pay for current period expenditures and therefore, are deferred in the funds	-
Long-term liabilities are not due and payable in the current period and therefore, are not reported in the fund	(740,000)
Interest payable on long-term debt does not require current financial resources and therefore, are not reported in the fund	<u>(4,050)</u>
Net assets of governmental activities	<u>\$ (304,455)</u>

CITY OF ELKHART, TEXAS
STATEMENT OF REVENUES, EXPENDITURES
AND CHANGES IN FUND BALANCE - GOVERNMENTAL FUNDS
FOR THE YEAR ENDED SEPTEMBER 30, 2012

	General	Debt Service	Special Revenue	Total
REVENUES				
Property taxes, penalty and interest	\$ 102,877	\$ -	\$ -	\$ 102,877
Sales taxes	88,271	-	22,068	110,339
Franchise taxes	87,058	-	-	87,058
Intergovernmental	1,920	-	-	1,920
Interest income	-	1,371	-	1,371
Other revenues	1,690	-	-	1,690
Total revenues	<u>281,816</u>	<u>1,371</u>	<u>22,068</u>	<u>305,255</u>
EXPENDITURES				
General government	207,372	-	-	207,372
Streets	86,229	-	22,068	108,297
Fire	9,233	-	-	9,233
Municipal court	2,329	300	-	2,629
Capital outlay	30,483	-	-	30,483
Debt service				
Principal retired	10,210	40,000	-	50,210
Interest	163	34,200	-	34,363
Total expenditures	<u>346,019</u>	<u>74,500</u>	<u>22,068</u>	<u>442,587</u>
EXCESS (DEFICIENCY) OF REVENUES OVER EXPENDITURES	<u>(64,203)</u>	<u>(73,129)</u>	<u>-</u>	<u>(137,332)</u>
OTHER FINANCING SOURCES (USES)				
Loan proceeds	5,700	-	-	5,700
Transfers in (out)	4,648	76,039	-	80,687
Net other financing sources (uses)	<u>10,348</u>	<u>76,039</u>	<u>-</u>	<u>86,387</u>
EXCESS (DEFICIENCY) OF REVENUES OVER EXPENDITURES AND OTHER USES	<u>(53,855)</u>	<u>2,910</u>	<u>-</u>	<u>(50,945)</u>
FUND BALANCE - BEGINNING OF YEAR	<u>269,273</u>	<u>122,035</u>	<u>1,624</u>	<u>392,932</u>
FUND BALANCE - END OF YEAR	<u>\$ 215,418</u>	<u>\$ 124,945</u>	<u>\$ 1,624</u>	<u>\$ 341,987</u>

See accompanying notes to financial statements.

**CITY OF ELKHART, TEXAS
RECONCILIATION OF THE STATEMENT OF REVENUES,
EXPENDITURES, AND CHANGES IN FUND BALANCE -
GOVERNMENTAL FUNDS TO THE STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED SEPTEMBER 30, 2012**

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

Net change in fund balance - governmental funds	\$	(50,945)
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Governmental funds report capital outlay as expenditures. 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 by which capital outlays exceeded depreciation in the current period.		23,292
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The issuance of long-term debt (e.g. bonds, leases) provides current financial resources to governmental funds, while the repayment of the principal of long-term debt consumes the current financial resources of governmental funds. This amount is the net effect of these differences in the treatment of long-term debt and related items.		44,510
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Accrued interest expense on long-term debt is reported in the government-wide statement of activities and changes in net assets, but does not require the use of current financial resources; therefore, accrued interest expense is not reported as expenditures in governmental funds. This amount is the change in accrued interest.		373
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Change in net assets of governmental activities	\$	<u>17,230</u>
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**CITY OF ELKHART, TEXAS
STATEMENT OF NET ASSETS
PROPRIETARY FUND
SEPTEMBER 30, 2012**

	<u>Utility</u>
ASSETS	
Current assets	
Cash and cash equivalents	\$ 80,489
Receivables, net of allowance for uncollectibles	68,488
Unbilled receivables	25,267
Inventory	40,424
Total current assets	<u>214,668</u>
Noncurrent assets	
Capital assets	
Land	61,203
Capital assets, being depreciated	4,284,134
Accumulated depreciation	<u>(2,413,517)</u>
Total capital assets, net	<u>1,931,820</u>
Other assets	
Bond issue costs, net of accumulated amortization	<u>2,620</u>
Total other assets	<u>2,620</u>
Total noncurrent assets	<u>1,934,440</u>
TOTAL ASSETS	<u>2,149,108</u>
LIABILITIES	
Current liabilities	
Accounts payable	24,825
Accrued interest	625
Customer deposits payable	89,469
Due to other funds	3,668
Deferred revenue	12,131
Capital leases - current maturities	12,602
Bonds payable - current maturities	<u>50,000</u>
Total current liabilities	<u>193,320</u>
Noncurrent liabilities	
Capital leases	47,914
Bonds payable	<u>50,000</u>
Total noncurrent liabilities	<u>97,914</u>
TOTAL LIABILITIES	<u>291,234</u>
NET ASSETS	
Invested in capital assets, net of related debt	1,771,304
Unrestricted	<u>86,570</u>
TOTAL NET ASSETS	<u>\$ 1,857,874</u>

See accompanying notes to financial statements.

CITY OF ELKHART, TEXAS
STATEMENT OF REVENUES, EXPENSES
AND CHANGES IN FUND NET ASSETS - PROPRIETARY FUND
FOR THE YEAR ENDED SEPTEMBER 30, 2012

	<u>Utility</u>
OPERATING REVENUES	
Water sales	\$ 413,882
Sewer income	206,336
Garbage income	142,513
Late charges and other income	<u>35,849</u>
Total operating revenues	<u>798,580</u>
OPERATING EXPENSES	
Personnel and related costs	202,961
Supplies and materials	102,632
Repairs and maintenance	48,467
Garbage expense	132,824
Professional fees	69,795
Insurance	6,331
Utilities	66,629
Office expense	9,431
Other expense	8,756
Depreciation	170,817
Amortization	<u>1,310</u>
Total operating expenses	<u>819,953</u>
INCOME (LOSS) FROM OPERATIONS	(21,373)
NONOPERATING REVENUES (EXPENSES)	
Interest income	40
Interest expense	(8,043)
Transfers in (out)	<u>(80,687)</u>
Total nonoperating revenues (expenses)	<u>(88,690)</u>
CHANGE IN NET ASSETS	(110,063)
NET ASSETS - BEGINNING OF YEAR	<u>1,967,937</u>
NET ASSETS - END OF YEAR	<u>\$ 1,857,874</u>

See accompanying notes to financial statements.

**CITY OF ELKHART, TEXAS
STATEMENT OF CASH FLOWS
PROPRIETARY FUND
FOR THE YEAR ENDED SEPTEMBER 30, 2012**

CASH FLOWS FROM OPERATING ACTIVITIES

Cash received from customers and users	\$ 800,553
Cash payments to suppliers	(433,489)
Cash payments to employees	<u>(204,083)</u>
Net cash provided by operating activities	<u>162,981</u>

CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES

Operating transfers out	<u>(80,687)</u>
Net cash used by noncapital financing activities	<u>(80,687)</u>

CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES

Acquisition of capital assets	(92,291)
Principal payments on long-term debt	8,996
Interest payments on long-term debt	<u>(8,043)</u>
Net cash used by capital and related financing activities	<u>(91,338)</u>

CASH FLOWS FROM INVESTING ACTIVITIES

Interest received	<u>40</u>
Net cash provided by investing activities	<u>40</u>

NET DECREASE IN CASH AND CASH EQUIVALENTS (9,004)

CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR 89,493

CASH AND CASH EQUIVALENTS AT END OF YEAR \$ 80,489

**RECONCILIATION OF OPERATING INCOME (LOSS) TO NET CASH
PROVIDED (USED) BY OPERATING ACTIVITIES**

Operating loss before nonoperating revenues	\$ (21,373)
Adjustments to reconcile operating loss to net cash provided by operating activities:	
Depreciation and amortization	172,127
Changes in assets and liabilities	
(Increase) decrease in accounts receivable	4,372
(Increase) decrease in inventory	9,837
Increase (decrease) in accounts payable	(2,129)
Increase (decrease) in accrued interest	(1,122)
(Increase) decrease in due to other funds	3,668
Increase (decrease) in customer deposits payable	<u>(2,399)</u>
Total adjustments	<u>184,354</u>

NET CASH PROVIDED BY OPERATING ACTIVITIES \$ 162,981

During the year, the City purchased a backhoe and a truck that were partially financed by a capital lease and a note payable for \$65,667 and \$11,400, respectively.

NOTES TO FINANCIAL STATEMENTS

**CITY OF ELKHART, TEXAS
NOTES TO FINANCIAL STATEMENTS
SEPTEMBER 30, 2012**

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Introduction

The financial statements of the City of Elkhart, Texas (the "City") have been prepared in accordance with generally accepted accounting principles (GAAP). The Governmental Accounting Standards Board (GASB) is responsible for establishing GAAP for state and local governments through its pronouncements (Statements and Interpretations). The more significant accounting and reporting policies used by the City are discussed below.

Reporting entity

The City of Elkhart is a political subdivision and municipal corporation of the State of Texas. The City operates under a Mayor-Council form of government. The City's major operations include: street repair and maintenance; general administrative services; and water, sewer, and sanitation utilities.

For financial reporting purposes, based on standards established by GASB Statement No. 14, "The Financial Reporting Entity", these financial statements should present the City (the primary government) and its component units. Component units generally are legally separate entities for which the primary government is financially accountable. The City does not have any blended or discretely presented component units.

Government-wide and fund financial statements

The government-wide financial statements include the statement of net assets and the statement of activities. These statements report information on all of the activities of the City as a whole. *Governmental activities*, which normally are supported by taxes and intergovernmental revenues, are reported separately from *business-type activities*, which rely to a significant extent on fees and charges for support.

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

As a general rule, the effect of interfund activity has been eliminated from the government-wide financial statements.

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

Measurement focus, basis of accounting, and financial statement presentation

The government-wide statements and the proprietary fund financial statements are reported using the *economic resources measurement focus* and the *accrual basis of accounting*. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Property tax revenues are recognized in the year for which they are levied. Grants and donations are recognized as revenue in the fiscal year in which grantor eligibility requirements are met.

CITY OF ELKHART, TEXAS
NOTES TO FINANCIAL STATEMENTS
SEPTEMBER 30, 2012

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 both measurable and available. Available means collectible within the current period or soon enough thereafter to pay current liabilities. The City considers revenues to be available if they are collected within 60 days of the end of the fiscal year. Expenditures are recorded when the related liability is incurred, as under accrual accounting. Debt service expenditures, both principal and interest, are recorded only when payment is due.

Major governmental fund revenue sources susceptible to accrual include: sales and use taxes, property taxes, franchise taxes and investment income. In general, all other revenue items are considered to be measurable and available only when cash is received.

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

The government has three governmental funds:

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

The *debt service fund* is used to account for the accumulation of restricted monies for the payment of general obligation debt.

The *special revenue fund* is used to account for the proceeds of specific revenues that are restricted to expenditures for special purposes. The City has one special purpose fund -- the Street Maintenance and Repair Fund.

The government has one proprietary fund:

The *utility fund* is used to account for operations of the water, sewer and sanitation systems that are financed and operated in a manner similar to private business enterprises -- where the intent of the governing body is that the cost (expenses, including depreciation) of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges.

When an expenditure is incurred for purposes for which both restricted and unrestricted (committed, assigned, or unassigned) amounts are available, it is the City's policy to generally consider restricted amounts to have been reduced first. When an expenditure is incurred for purposes for which amounts in any of the unrestricted fund balance classifications could be used, it is the policy of the City that committed amounts would be reduced first, followed by assigned amounts, and then unassigned amounts. In both instances, when a proposed expenditure is made with specific balances identified as the source of the funding, that specific fund balance will be used.

All expenses incurred by the City are properly segregated and accounted for in the fund to which they apply. Certain general and administrative expenses are allocated to the proprietary fund and to the

**CITY OF ELKHART, TEXAS
NOTES TO FINANCIAL STATEMENTS
SEPTEMBER 30, 2012**

governmental fund based on the level of services rendered through each fund as estimated by management.

The financial statements of the City are prepared in accordance with generally accepted accounting principles (GAAP). The City's reporting entity applies all relevant Governmental Accounting Standards Board (GASB) pronouncements and applicable Financial Accounting Standards Board (FASB) pronouncements and Accounting Principles Board (APB) opinions issued on or before November 30, 1989, unless they conflict with GASB pronouncements. The City's reporting entity does not apply FASB pronouncements or APB opinions issued after November 30, 1989.

Assets, liabilities, and net assets or fund balance

Deposits and investments

The City's cash and cash equivalents are considered to be cash on hand, demand deposits, money market accounts, and certificates of deposit or short-term, highly liquid investments that are readily convertible to known amounts of cash and so near maturity that they present insignificant risk of changes in value because of changes in interest rates. Cash equivalents include investments with original maturities of three months or less and are stated at fair value.

Time deposits consist of certificates of deposit with maturities greater than three months. Certificates of deposit are recorded at cost, which approximates market value. The City did not own any certificates of deposit at year end or at any time during the current fiscal year.

The City is authorized to invest in the following instruments, as authorized by the Public Funds Investment Act: U.S. Treasury securities which have a liquid market; direct obligations of the State of Texas, and other obligations that are guaranteed by the State of Texas or United States of America; obligations of states, agencies, counties, and other political subdivisions of any state having been rated as investment quality by a nationally recognized investment rating firm and having received a rating of not less than "A" or its equivalent; fully insured or collateralized certificates of deposit at commercial banks; repurchase agreements collateralized by U.S. Treasury or U.S. Government Agency securities in accordance with a master repurchase agreement; joint pools of political subdivisions in the State of Texas which invest in instruments and follow practices allowed by current law (investment in such pools shall be limited to 15% of the City's entire portfolio and the pool must be continuously rated no lower than "AAA" or "AAA-M" by at least one nationally recognized rating service).

The City did not have any investments at year end or at any time during the current fiscal year.

Fair value of financial instruments

The City evaluates the fair value of its non-investment financial instruments based on the current interest rate environment and current pricing of debt instruments with comparable terms. The carrying value of all non-investment financial instruments, including debt, is considered to approximate fair value.

Receivables

All customer and property tax receivables are shown net of an allowance for uncollectibles. These allowances are reviewed annually by City management.

Inventories

Inventories are valued at cost. Inventory consists of expendable supplies and repair parts held for consumption and are valued at cost using the first-in/first out method.

CITY OF ELKHART, TEXAS
NOTES TO FINANCIAL STATEMENTS
SEPTEMBER 30, 2012

Restricted assets

Certain assets are classified as restricted because they are maintained in separate accounts and their use is limited by applicable bond covenants and/or other contractual agreements.

Capital assets and depreciation

Capital assets, which include land, buildings and improvements, furniture and equipment, and infrastructure assets are reported in the applicable governmental or business-type activities column in the government-wide financial statements. Capital assets are defined by the City as assets with an initial, individual cost of more than \$500 and an estimated useful life in excess of one year. Such assets are recorded at historical cost or estimated historical cost if purchased or constructed. Contributed capital assets are recorded at estimated fair market value at the date received. The City, a Phase 3 government as described by GASB Statement No. 34, has elected not to report major general infrastructure assets retroactively.

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

Capital assets are depreciated using the straight-line method. When capital assets are disposed, the cost and applicable accumulated depreciation are removed from the respective accounts, and the resulting gain or loss is recorded in operations.

The estimated useful lives are as follows:

Buildings and improvements	20 to 50 years
Utility plant and equipment	7 to 40 years
Machinery and equipment	5 to 20 years
Transportation equipment	5 years
Office furniture and equipment	5 to 10 years
Streets and drainage	10 years

Compensated absences

Employees of the City are entitled to paid vacation and sick days, depending on length of service.

The City's policy is for employees to take their vacation within the City's fiscal year. If not used within the time frame allotted, the vacation time is forfeited. Under certain Council-approved circumstances, employees are allowed to carry over vacation time balances. No accrual is made to record year-end vacation time carried over in this financial statement because the amount is immaterial.

Employee sick leave time may be carried over from one year to the next, but no cash payment for accumulated sick leave is made when an employee separates from the City, whatever the reason. The City's policy is to pay for, and expense, sick leave as it is taken.

Long-term obligations

In the government-wide and proprietary 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. 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.

**CITY OF ELKHART, TEXAS
NOTES TO FINANCIAL STATEMENTS
SEPTEMBER 30, 2012**

The governmental fund financial statements recognize bond premiums and discounts, as well as bond issuance costs, during the current period. Premiums received on debt issuance are reported as other financing sources while discounts on debt issuances are reported as other financing uses. Issuance costs, whether or not withheld from the actual debt proceeds received, are reported as debt service expenditures.

Net assets and fund balances

In the government-wide financial statements, the difference between the City's total assets and total liabilities represents net assets. Net assets are displayed in three components – invested in capital assets, net of related debt; restricted; and unrestricted. At September 30, 2012, restricted net assets represent monies that are legally restricted for payment of debt service. Unrestricted net assets represent the net assets available for future operations.

In the governmental fund financial statements, fund balances are classified as follows:

Non-spendable – amounts that cannot be spent either because they are in non-spendable form (such as inventories and prepaid amounts) or because they are legally or contractually required to be maintained intact.

Restricted – amounts that can be spent only for specific purposes due to constraints imposed on resources either (a) externally by creditors (such as through debt covenants), grantors, contributors, or laws or regulations of other governments; or (b) imposed by law through constitutional provisions or enabling legislation.

Committed – amounts that can only be used for specific purposes pursuant to constraints imposed by formal resolutions or ordinances of the Council – the government's highest level of decision making authority. Commitments may be established, modified, or rescinded only through ordinances or resolutions approved by the Council.

Assigned – amounts that do not meet the criteria to be classified as restricted or committed but that are intended to be used for specific purposes.

Unassigned – all other spendable amounts.

Proprietary fund net assets are classified the same as in government-wide statements.

Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

CITY OF ELKHART, TEXAS
NOTES TO FINANCIAL STATEMENTS
SEPTEMBER 30, 2012

STEWARDSHIP, COMPLIANCE, AND ACCOUNTABILITY

Budgetary information

In accordance with the City's legal requirements, the City adopts an annual budget for the general fund. Budgeted expenditures for the current year, as adopted in the original budget, may be amended to take into account special authorizations of the City Council during the year. All appropriations lapse at the end of each fiscal year. No amendments were made to the City's original budget during the current fiscal year.

During the current year, the general fund overspent by \$79,385.

Restricted balances

Bond covenants and other contractual provisions require that the City establish separate bank accounts, with minimum balance requirements, for certain bond debt service and grant related capital expenditures. The City maintained the minimum balance requirements in these accounts at all times during the year and all debt service expenditures were made timely.

DETAILED NOTES ON ALL FUNDS

ASSETS

Deposits

The City maintains its cash deposits at financial institutions whose deposits are insured by the FDIC. It is the policy of the City to require that deposits in excess of the applicable coverage be collateralized with securities held by the pledging financial institutions. All cash and investments are reported at fair value. All deposits were fully secured by FDIC coverage and/or securities pledged by the depository banks.

Elkhart Volunteer Fire Department (EVFD) donations

The City receives donations for the EVFD, generally through utility collections. These donations are transacted through a separate cash account and remitted to the EVFD on a periodic basis. Both the cash and offsetting liability are excluded from these financial statements. At September 30, 2012, the balance of collections to be remitted to the EVFD totaled \$3,738.

Receivables

The City's receivables at year end, including the related allowances for uncollectible accounts, are as follows:

	<u>Governmental Activities</u>	<u>Business-type Activities</u>	<u>Total</u>
Customer accounts	\$ -	\$ 80,135	\$ 80,135
Unbilled services	-	25,267	25,267
Property taxes	19,575	-	19,575
Sales taxes	8,121	-	8,121
Less allowance for uncollectibles	<u>(19,575)</u>	<u>(11,647)</u>	<u>(31,222)</u>
Net	<u>\$ 8,121</u>	<u>\$ 93,755</u>	<u>\$ 101,876</u>

CITY OF ELKHART, TEXAS
NOTES TO FINANCIAL STATEMENTS
SEPTEMBER 30, 2012

Property taxes

Property taxes are levied on October 1 on the assessed value listed as of the prior January 1 for all real and business personal property located in the City. Taxes are due upon receipt of the tax bill and are delinquent if not paid before February 1 of the year following the year in which imposed. On January 31 of each year, a tax lien attaches to property to secure the payment of all taxes, penalties, and interest ultimately imposed. Property taxes are considered available when paid.

The property tax rate to finance general governmental services for the year ended September 30, 2012, was \$.30424 per \$100 of assessed valuation. The total taxable value and total tax levy assessed for the year was \$32,476,909 and \$98,808, respectively. The City has contracted with the Anderson County Central Appraisal District for the collection of property taxes.

Capital assets

A summary of changes in capital assets for the year ended September 30, 2012, is as follows:

Governmental activities

	Balance 09/30/2011	Additions	Deletions	Balance 09/30/2012
Capital assets, not being depreciated:				
Land	\$ 2,350	\$ -	\$ -	\$ 2,350
Construction in progress	-	17,660	-	17,660
Total capital assets, not being depreciated	2,350	17,660	-	20,010
Capital assets, being depreciated:				
Buildings & improvements	62,298	5,046	-	67,344
Machinery & equipment	15,456	6,684	-	22,140
Office equipment & furniture	23,269	1,093	(7,033)	17,329
Streets	140,656	-	-	140,656
Total capital assets being depreciated	241,679	12,823	(7,033)	247,469
Less accumulated depreciation	(169,713)	(7,191)	7,033	(169,871)
Total capital assets being depreciated, net	71,966	5,632	-	77,598
Total capital assets – governmental activities, net of depreciation	\$ 74,316	\$ 23,292	\$ -	\$ 97,608

Depreciation expense was charged to the following functions/programs of governmental activities as follows:

General government	<u>\$ 7,191</u>
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CITY OF ELKHART, TEXAS
NOTES TO FINANCIAL STATEMENTS
SEPTEMBER 30, 2012

Business-type activities

	Balance 09/30/2011	Additions	Deletions	Balance 09/30/2012
Capital assets, not being depreciated:				
Land	\$ 61,203	\$ -	\$ -	\$ 61,203
Total capital assets not being depreciated	<u>61,203</u>	<u>-</u>	<u>-</u>	<u>61,203</u>
Capital assets, being depreciated:				
Plant & equipment	3,758,948	13,029	(1,369)	3,770,608
Transportation equipment	65,796	10,737	-	76,534
Machinery & equipment	378,888	73,761	(23,242)	429,406
Office equipment	<u>42,600</u>	<u>-</u>	<u>(35,014)</u>	<u>7,586</u>
Total capital assets being depreciated	<u>4,246,232</u>	<u>97,527</u>	<u>(59,625)</u>	<u>4,284,134</u>
Less accumulated depreciation	<u>(2,297,089)</u>	<u>(170,817)</u>	<u>54,389</u>	<u>(2,413,517)</u>
Total capital assets being depreciated, net	<u>1,949,143</u>	<u>(73,290)</u>	<u>(5,236)</u>	<u>1,870,617</u>
Total capital assets – business-type activities, net of depreciation	<u>\$ 2,010,346</u>	<u>\$ (73,290)</u>	<u>\$ (5,236)</u>	<u>\$ 1,931,820</u>

Depreciation expense of \$170,817 was charged to the proprietary fund.

LIABILITIES

Capital leases

The City has entered into a lease agreement as lessee for financing the acquisition of machinery and equipment. This lease agreement qualifies as a capital lease for accounting purposes, and therefore, has been recorded at the present value of its future minimum lease payments as of the inception date.

The asset acquired through a capital lease is as follows:

	General Fund	Utility Fund
Asset:		
Machinery and equipment	\$ -	\$ 70,703
Less accumulated depreciation	<u>-</u>	<u>(1,963)</u>
Total	<u>\$ -</u>	<u>\$ 68,740</u>

CITY OF ELKHART, TEXAS
NOTES TO FINANCIAL STATEMENTS
SEPTEMBER 30, 2012

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

<u>Year ending September 30,</u>	<u>General Fund</u>	<u>Utility Fund</u>
2013	\$ -	\$ 14,175
2014	-	14,175
2015	-	14,175
2016	-	14,175
2017	-	8,268
Total minimum lease payments	\$ -	\$ 64,967
Less amount representing interest	-	(4,395)
Present value of minimum lease payments	<u>\$ -</u>	<u>\$ 60,572</u>

Long-Term Debt

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

Governmental activities

	<u>Balance 09/30/11</u>	<u>Additions</u>	<u>Reductions</u>	<u>Balance 09/30/12</u>	<u>Due Within One Year</u>
Bonds and notes payable					
Series 2005 bonds	\$ 780,000	\$ -	\$ (40,000)	\$ 740,000	\$ 40,000
Notes payable –					
Elkhart State Bank	<u>4,510</u>	<u>5,700</u>	<u>(10,210)</u>	<u>-</u>	<u>-</u>
Total long-term liabilities – governmental activities	<u>\$ 784,510</u>	<u>\$ 5,700</u>	<u>\$ (50,210)</u>	<u>\$ 740,000</u>	<u>\$ 40,000</u>

Business-type activities

	<u>Balance 09/30/11</u>	<u>Additions</u>	<u>Reductions</u>	<u>Balance 09/30/12</u>	<u>Due Within One Year</u>
Bonds payable					
Series 1999 bonds	\$ 145,000	\$ -	\$ (45,000)	\$ 100,000	\$ 50,000
Notes payable –					
Elkhart State Bank	<u>6,520</u>	<u>11,400</u>	<u>(17,920)</u>	<u>-</u>	<u>-</u>
Total long-term liabilities – business-type activities	<u>\$ 151,520</u>	<u>\$ 11,400</u>	<u>\$ (62,920)</u>	<u>\$ 100,000</u>	<u>\$ 50,000</u>

The annual debt service requirements to maturity for all long-term debt are as follows:

<u>Year Ending September 30,</u>	<u>Governmental Activities</u>		<u>Business-Type Activities</u>	
	<u>Principal</u>	<u>Interest</u>	<u>Principal</u>	<u>Interest</u>
2013	\$ 40,000	\$ 32,400	\$ 50,000	\$ 5,000
2014	40,000	30,600	50,000	2,500
2015	100,000	27,450	-	-
2016	100,000	22,950	-	-
2017	105,000	18,338	-	-
2018-2022	<u>355,000</u>	<u>24,637</u>	<u>-</u>	<u>-</u>
Total	<u>\$ 740,000</u>	<u>\$ 156,375</u>	<u>\$ 100,000</u>	<u>\$ 7,500</u>

CITY OF ELKHART, TEXAS
NOTES TO FINANCIAL STATEMENTS
SEPTEMBER 30, 2012

Additional information regarding the City's long-term debt obligations follows:

General Obligation Refunding Bonds, Series 2005.

During the fiscal year ended September 30, 2006, the City issued General Obligation Refunding Bonds, Series 2005, in the amount of \$960,000. The bonds were issued in order to retire the Waterworks and Sewer System Bonds Series 1989 and 1989-A and take advantage of lower interest rates. The 2005 bonds were dated November 8, 2005, bear interest at 4.50%, and mature in years through 2020. Bonds in increments of \$5,000 may be called on February 15, 2015, or on any date thereafter at the redemption price of par. The bond indenture allows the City to pay the bonds from the proceeds of an additional ad valorem tax that may be levied by the City, and the City has pledged any such proceeds to secure the payment. However, the City Council has elected to repay the bonds from the City's proprietary fund revenues.

Tax and Waterworks and Sewer System Surplus Revenue Certificates of Obligation, Series 1999.

During the fiscal year ended September 30, 2000, the City issued Tax and Waterworks and Sewer System Surplus Revenue Certificates of Obligation, Series 1999, in the amount of \$550,000. The bonds were dated March 15, 1999, bear interest at 5.00% to 5.35%, and mature in years through 2014. Bonds in increments of \$5,000 may be called on August 15, 2009, or any date thereafter at the redemption price of par. The bonds were issued for the purpose of water and sewer system improvements. The bonds are repaid from and secured by a pledge of surplus net revenues of the City's proprietary fund.

Notes payable to Elkhart State Bank.

In November of 2010, the City financed the purchase of a 2010 Dodge truck for \$22,755. The note was payable at a rate of 5.00% and matured in December of 2011. The note was fully paid off as of September 30, 2012.

In December of 2011, the City financed the purchase of a 2012 Dodge truck for \$17,100. The note was payable at a rate of 5.00% and a maturity date of January 1, 2013. The note was fully paid off as of September 30, 2012.

Bond compliance requirements.

The bond ordinances require that during the period in which the bonds are outstanding, the City must create and maintain certain accounts or funds to receive the proceeds from the sale of the bonds and to account for the revenues (as defined) and/or taxes, which are pledged for payment of the bonds. The assets can be used only in accordance with the terms of the bond ordinance and for the specific purpose(s) designated therein.

The City is generally required to make a monthly transfer to debt service funds equal to one-sixth of the next interest payment and one-twelfth of the next principal payment. Certain bond ordinances have additional requirements for the establishment of rates and the accumulation of principal and interest repayment amounts from surplus operating funds. Generally, the bonds may be redeemed prior to their maturities in accordance with the bond ordinances and at various premiums equal to or less than 2%.

At September 30, 2012, the City had \$124,995 available in the debt service fund to service the bond indebtedness.

Interfund Receivables, Payables and Transfers

During the course of routine operations, transactions occur between individual funds. Receivables and payables created by these transactions are classified as "internal balances" on the government-wide statement of net assets.

CITY OF ELKHART, TEXAS
NOTES TO FINANCIAL STATEMENTS
SEPTEMBER 30, 2012

At September 30, 2012, internal balances consisted of the following:

<u>Receivable fund</u>	<u>Payable fund</u>	<u>Amount</u>
General fund	Utility fund	\$ 3,668

Interfund transfers during the year consisted of the following:

<u>Transfer from</u>	<u>Transfer to</u>	<u>Amount</u>
Utility fund	General fund	\$ 4,648
Utility fund	Debt service fund	76,039
	Total	<u>\$ 80,687</u>

OTHER INFORMATION

Pension plan

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

TMRS issues a publicly available comprehensive annual financial report that includes financial statements and required supplementary information (RSI) for TMRS; the report also provides detailed explanations of the contributions, benefits and actuarial methods and assumptions used by the System. The report may be obtained from TMRS' website at [www. TMRS.com](http://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. The plan provisions for the City were as follows:

	<u>Plan Year 2011</u>	<u>Plan Year 2012</u>
Employee deposit rate	5%	5%
Matching ratio (city to employee)	1 to 1	1 to 1
Years required for vesting	5	5
Service retirement eligibility (expressed as age/years of service)	60/5, 0/25	60/5, 0/25
Updated Service Credit	100% Repeating, Transfers	100% Repeating, Transfers
Annuity Increase (to retirees)	70% of CPI Repeating	70% of CPI Repeating

Contributions and actuarial information. Under the state law governing TMRS, the contribution rate for each City is determined annually by the actuary, using the Projected Unit Credit actuarial cost method. The rate was 8.59% for the months in calendar year 2011 and 6.33% for the months in calendar year 2012. This rate consists of the normal cost contribution rate and the prior service cost contribution rate, which is calculated to be a level percent of payroll from year to year. The normal cost contribution rate finances the portion of an active member's projected benefit allocated annually; the prior service contribution rate amortizes the unfunded (overfunded) actuarial liability (asset) over the applicable period

CITY OF ELKHART, TEXAS
NOTES TO FINANCIAL STATEMENTS
SEPTEMBER 30, 2012

for that city. Both the normal cost and prior service contribution rates include recognition of the projected impact of annually repeating benefits, such as Updated Service Credits and Annuity Increases.

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

The City's Annual Pension Cost for the year equaled their actual contributions, which totaled \$17,966.

Three-Year Trend Information

<u>Accounting Year Ending</u>	<u>Annual Pension Cost ("APC")</u>	<u>Percentage of APC Contributed</u>	<u>Net Pension Obligation</u>
9/30/10	\$21,907	100%	-
9/30/11	\$20,962	100%	-
9/30/12	\$17,966	100%	-

The required contribution rates for fiscal year 2012 were determined as part of the December 31, 2009 and 2010 actuarial valuations. Additional information as of the latest actuarial valuation, December 31, 2011, also follows:

Contribution information

	<u>12/31/2009</u>	<u>12/31/2010</u>	<u>12/31/2011</u>
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	27.7 years; Closed Period	27.0 years; Closed Period	26.1 years; Closed Period
Amortization Period for new Gains/Losses	30 years	18 years	17 years
Asset Valuation Method	10-year Smoothed Market	10-year Smoothed Market	10-year Smoothed Market

Actuarial assumptions

	<u>12/31/2009</u>	<u>12/31/2010</u>	<u>12/31/2011</u>
Investment Rate of Return *	7.5%	7.0%	7.0%
Projected Salary Increases *	Varies by age and service	Varies by age and service	Varies by age and service
* Includes Inflation at:	3.00%	3.00%	3.00%
Cost-of-Living Adjustments	2.1%	2.1%	2.1%

CITY OF ELKHART, TEXAS
NOTES TO FINANCIAL STATEMENTS
SEPTEMBER 30, 2012

Funded Status and Funding Progress. The funded status as of December 31, 2011, the most recent actuarial valuation date, is presented as follows:

Actuarial Valuation Date	Actuarial Value of Assets	Actuarial Accrued Liability (AAL)	Funded Ratio	Unfunded AAL (UAAL)	Covered Payroll	UAAL UAAL as a Percentage of Covered Payroll
	(1)	(2)	(3)	(4)	(5)	(6)
			(1) / (2)	(2) - (1)		(4) / (5)
12/31/11	\$438,601	\$531,054	82.6%	\$92,453	\$232,916	39.7%

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

Actuarial calculations are based on the benefits provided under the terms of the substantive plan in effect at the time of each valuation, and reflect a long-term perspective. Consistent with that perspective, actuarial methods and assumptions used include techniques that are designed to reduce short-term volatility in actuarial accrued liabilities and the actuarial value of assets. The schedule of funding progress, presented as Required Supplementary Information following the notes to the financial statements, presents multi-year trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liability of benefits.

Risk management

The City is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions, injuries to employees; and natural disasters. The City provides insurance coverage for each of those risks of loss by participation in the Texas Municipal League Intergovernmental Risk Pool. Management believes such coverage is sufficient to preclude any significant uninsured losses to the City. The City did not have any significant claims during the current year.

Contingent liabilities

Amounts received or receivable from grant agencies are subject to audit and adjustment by grantor agencies. Any disallowed claims, including amounts already collected, may constitute a liability of the applicable funds. The amount, if any, of expenditures that may be disallowed by the grantor cannot be determined at this time, although the City expects such amounts, if any, to be immaterial.

Subsequent events

Management has evaluated subsequent events through March 29, 2013, the date when the financial statements were available to be issued.

REQUIRED SUPPLEMENTARY INFORMATION

CITY OF ELKHART, TEXAS
SCHEDULE OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCE
BUDGET AND ACTUAL
GENERAL FUND
FOR THE YEAR ENDED SEPTEMBER 30, 2012

	Original and Final Budget	Actual	Variance Favorable (Unfavorable)
REVENUES			
Property taxes	\$ 93,000	\$ 99,473	\$ 6,473
Penalties and interest	2,000	3,404	1,404
Sales taxes	103,000	88,271	(14,729)
Franchise taxes	75,000	87,058	12,058
Grant income	-	1,920	1,920
Miscellaneous	6,750	1,690	(5,060)
Total revenues	<u>279,750</u>	<u>281,816</u>	<u>2,066</u>
EXPENDITURES			
Personnel and related costs	126,470	158,016	(31,546)
Repair and maintenance, including streets	71,750	52,598	19,152
Professional fees	22,900	23,448	(548)
Insurance	14,500	13,414	1,086
Utilities	39,700	43,420	(3,720)
Office expense	8,200	11,610	(3,410)
Other expense	200	2,657	(2,457)
Capital outlay	-	30,483	(30,483)
Debt service	-	10,373	(10,373)
Total expenditures	<u>283,720</u>	<u>346,019</u>	<u>(62,299)</u>
EXCESS (DEFICIENCY) OF REVENUES OVER EXPENDITURES	<u>(3,970)</u>	<u>(64,203)</u>	<u>(60,233)</u>
OTHER FINANCING SOURCES (USES)			
Loan proceeds	-	5,700	5,700
Transfers in (out)	29,500	4,648	(24,852)
Net other financing sources	<u>29,500</u>	<u>10,348</u>	<u>(19,152)</u>
NET CHANGE IN FUND BALANCE	25,530	(53,855)	(79,385)
FUND BALANCE - BEGINNING OF YEAR	<u>269,273</u>	<u>269,273</u>	<u>-</u>
FUND BALANCE - END OF YEAR	<u>\$ 294,803</u>	<u>\$ 215,418</u>	<u>\$ (79,385)</u>

See Independent Auditors' Report.

CITY OF ELKHART, TEXAS
SCHEDULE OF FUNDING PROGRESS OF PENSION PLAN -
TEXAS MUNICIPAL RETIREMENT SYSTEM
FOR THE YEAR ENDED SEPTEMBER 30, 2012

The following schedule presents multi-year information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial liability for benefits.

Actuarial Valuation Date	Actuarial Value of Assets	Actuarial Accrued Liability (AAL)	Funded Ratio	Unfunded AAL (UAAL)	Covered Payroll	UAAL as a Percentage of Covered Payroll
	(1)	(2)	(3)	(4)	(5)	(6)
			(1) / (2)	(2) - (1)		(4) / (5)
12/31/2004	\$ 204,552	\$ 293,000	69.8%	\$ 88,488	\$ 136,966	64.6%
12/31/2005	\$ 234,238	\$ 321,273	72.9%	\$ 87,035	\$ 166,553	52.2%
12/31/2006	\$ 263,795	\$ 369,664	71.4%	\$ 105,869	\$ 170,091	62.2%
12/31/2007	\$ 295,505	\$ 447,407	66.0%	\$ 151,902	\$ 227,957	66.6%
12/31/2008	\$ 331,711	\$ 473,805	70.0%	\$ 142,094	\$ 206,043	69.0%
12/31/2009	\$ 382,117	\$ 506,778	75.4%	\$ 124,661	\$ 233,976	53.3%
12/31/2010	\$ 429,537	\$ 549,823	78.1%	\$ 120,286	\$ 227,371	52.9%
12/31/2011	\$ 438,601	\$ 531,054	82.6%	\$ 92,453	\$ 232,916	39.7%

INTERNAL CONTROL AND COMPLIANCE

Todd, Hamaker & Johnson, LLP

CERTIFIED PUBLIC ACCOUNTANTS

420 S 1st Street • PO Box 468 • Lufkin, TX 75902-0468 • (936) 632-8181
301 N 6th Street • PO Box 1249 • Crockett, TX 75835-1249 • (936) 544-2143

Melvin R. Todd, CPA
Daren Hamaker, CPA
Kim Johnson, CPA
Rachel Kennerly, CPA

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 Elkhart, Texas

We have audited the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of Elkhart, Texas (the City) as of and for the year ended September 30, 2012, which collectively comprise the City's basic financial statements and have issued our report thereon dated March 29, 2013. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

INTERNAL CONTROL OVER FINANCIAL REPORTING

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

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

Our consideration of internal control was for the limited purpose described in the first paragraph and was not designed to identify all deficiencies in internal control that might be significant deficiencies or material weaknesses and therefore there can be no assurance that all such deficiencies have been identified. We did not identify any deficiencies in internal control that we consider to be material weaknesses, as defined above.

COMPLIANCE AND OTHER MATTERS

As part of obtaining reasonable assurance about whether the City's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The

**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 – CONTINUED**

results of our tests disclosed no instances of noncompliance and other matters that are required to be reported under *Government Auditing Standards*.

We noted certain matters that we reported to management of the City in a separate letter dated March 29, 2013.

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

Todd, Hamaker & Johnson, LLP

Todd, Hamaker & Johnson, LLP
Lufkin, Texas

March 29, 2013